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# THE EC AND THE USA THE FUTURE OF FARM TRADE

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In recent years, the competition in agricultural commodities between the USA and the EC for agricultural commodities has become so intense as to verge on a trade war. In *Span* 29, 3, 1986, Dr T. L. Oyloe, of the Agriculture Council of America, discussed the matter from the standpoint of the USA. In this article Mr Avery responds; he is a policy adviser at the European Community in Brussels and has recently spent a year as a Fellow of the Center for International Affairs at Harvard University.

In the field of nuclear arms, it is the USA and the USSR who are acknowledged to be the 'superpowers'. Although they are not the only states with these weapons of destruction, they have an overwhelming superiority in stockpiles and in the capacity to deliver them.

The result is an uneasy peace, in which the statigists on both sides elaborate plans for defence and counter-attack, assuming (as they must) that the 'worst case' may happen. Meanwhile their political leaders struggle to find a solution which will reduce the risk of conflict, increase mutual confidence, and contain public expenditure. Other countries watch, wait, and hope for the best.

It is not so different in the field of agricultural trade, but here the 'superpowers' are the European Community (EC) and the USA. These are the green giants, whose agricultural output and export potential have grown so much in the last 20 years. Other countries have the same or even greater resources of land and labour available for farming - this is certainly the case for the USSR and many of the poorer countries of the world. But they have not yet succeeded in creating the economic, social and political conditions in which their agriculture can exploit the extraordinary potential of modern technology in the way that has been done in Europe and North America.

So it is on the EC and the USA that attention is focused in farm trade matters, and in recent years with growing apprehension. Each side tends to view the other's intentions as aggressive, and indeed, on the US side, recent developments have been of an overtly aggressive nature. The Administration, under pressure from Congress, and in response to a financial crisis in the farm-belt, has brought in farm export subsidies which American spokesmen for many years denounced as 'dirty weapons'. At the end of 1986 it threatened to impose heavy taxes on food imports from the EC, in retaliation for the adoption by Spain and Portugal of Europe's agricultural policy. Fortunately, last-minute diplomacy prevented this leading to an all-out trade war.

Why has this confrontation come about, particularly between two groupings who have so much in common? The 12-member

European Community has many shared values with the Americans. These values include the tradition of parliamentary democracy, and the system of the market economy. Moreover, most EC members are also NATO members, and all EC members share with North America fundamental interests of defence and security in Western Europe - and sectoral trade issues such as agriculture do have an effect on wider economic and political relations between states.

### Linking farm trade and policy

It must be high time that international leaders took the matter in hand and tried to find a solution through cooperation rather than confrontation. Fortunately, they are trying to do so. At their summit meeting in Tokyo in 1986, the Heads of Government of the seven major industrialised nations (Canada, France, Germany, Great Britain, Italy, Japan, USA), together with the EC Commission's President, declared:

'We note with concern that a situation of global structural surplus now exists for some important agricultural products, arising partly from technological improvements, partly from changes in the world market situation, and partly from long-standing policies of domestic subsidy and protection of agriculture in all our countries. This is a problem which we all share and can be dealt with only in cooperation with each other. We all recognise the importance of agriculture to the well-being of rural communities, but we are agreed that, where there are surpluses, action is needed to redirect policies and adjust the structure of agricultural production.'

This kind of declaration is certainly not a solution to the problem: it is no more than a description of it, with an exhortation. But what was significant in this case was that the Prime Ministers and Presidents placed the farm trade question fairly and squarely in the context of surplus production resulting from the combination of domestic price support with rapid technological change.

They realised that the simple approach of reducing trade barriers is not enough to deal with farm trade difficulties, which have their origin in domestic programmes. These

programmes must be brought under control, in order to stop generating the surpluses, and thus stop the 'arms race' of subsidies on exports and barriers to imports.

In other words, we have a situation where there is an interplay between domestic and external policies. This is true, of course, not only for agriculture but also for other sectors where international trade and payments take place. No country conducts its trade policy as if it had nothing to do with domestic economic policies concerning incomes and employment.

What distinguishes agriculture from other sectors is the degree of state involvement in the markets, and this is true both for the EC and the USA. Indeed, it is true not only for the industrialised countries, but also for the poorer countries of the world. It is no exaggeration to say that among the first actions of those aspiring to govern a state are to organise its territorial defence and the regulation of its agriculture and food supplies.

### Farm policies worldwide

But analysts are becoming more and more aware of the distortions to which agricultural policies can give rise. In its World Development Report for 1986, the World Bank made a magisterial survey of the problem. Dealing first with the developing countries, it said:

'Paradoxically, many countries which have been stressing the importance of agricultural development have established a complex set of policies that is strongly biased against agriculture. Thus, some developing countries impose taxes on agricultural exports while lamenting the adverse impact of declining commodity prices on the farm sector. Some pay their producers half the world price for grains (or even less) and then spend scarce foreign exchange to import food.'

The World Bank is no less severe with the policies of the industrial countries, including the USA, Canada, the European Community, and Japan. It finds that in these countries:

'The main justification for agricultural protection is to improve the incomes of farm families, especially those under financial stress. But the benefits of protection go primarily to better-off

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### About this journal

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farmers, while the burden of higher food prices is borne disproportionately by poorer consumers. Moreover, most of the benefits of the programmes become capitalised into the price of the land at the time the programmes are inaugurated.

After analysing the costs and benefits of such policies in industrial countries, the Bank's report concludes that the net costs are more than \$40 billion a year. It adds that:

'Industrial countries' agricultural policies may be aimed at solving domestic problems, but their effects spill over onto the rest of the world. By expanding output and depressing domestic demand, their policies reduce world prices and distort the relative prices of agricultural and manufactured goods. By granting special trading privileges to remedy some of the harm, industrial countries can make matters worse. And by destabilising international markets, their farm policies can amplify rather than dampen commodity price fluctuation.'

Policy makers in Europe and the USA would agree with many of these strictures. What are they doing to put their respective houses in order?

### Response of Europe

The EC is going through a period of important reforms in its Common Agricultural Policy. After the European Commission spelt out the options rather starkly in its Green paper of 1985, the Council of Ministers has had to address some of the problems; and this is putting a real strain on the EC's decision-making.

While the decisions should normally be taken by the 12 Ministers of Agriculture in their specialised Council, it is also natural for the 12 Budget Ministers (not to mention the Foreign Ministers and the Trade Ministers) to want to exert their influence. This creates tension and conflicts which it is difficult to resolve, taking into account also the positions of the European Parliament.

Nevertheless, as the Commissioner for Agriculture, Frans Andriessen has said, there is near-consensus on some of the basic aims:

- (i) although drastic cuts in price support are not practicable, because of the unacceptable consequences for farmers' incomes, the EC has to pursue a tough price policy;
- (ii) priority has to be given to better control of production, rather than to encouraging it;
- (iii) budget limits have to be taken seriously;
- (iv) a rigorous line on price and markets policy has to be balanced with social and structural measures to help farmers find alternative sources of income;
- (v) because the EC is so involved in world markets, as both an exporter and an importer, it has to accept its responsibilities to other countries.

What are the prospects for putting these aims into effect? In 1985 the Commission insisted on a cut in grain support prices – and in the face of the Council's indecision, it used its executive powers to make that reduction stick. In 1986 there were indirect price cuts for grain, through the adjustment of quality standards, plus a levy of 3% on grain produced and marketed in Europe.

Meanwhile for milk, the quota system introduced in 1984 has reduced Europe's production, and the Commission has proposed further cutbacks. The EC is also exploring ideas of taking land out of production (like 'set-aside' in the US) and reducing the intensity of production by means of subsidies for 'environment-friendly' farming.

### US measures

On the other side of the Atlantic, the main development has been the new Farm Bill, signed into law by President Reagan at the end of 1985. It represented a real effort to move towards a more market-oriented farm policy. Agriculture Secretary John Block said, 'we cannot have price-support programs that lead to surplus production', and 'we can no longer afford open-ended budget expenditures'. These were honourable aims, but it is by no means clear that they are being achieved.

US loan rates for grain have indeed been cut, but farmers are insulated from the effect of this by generous deficiency payments, financed by the taxpayer. Federal price support to agriculture for the fiscal year 1986 is estimated to cost \$25 billion. This is even more than the EC's price support bill of \$20 billion, and while the EC's support is for 11 million farmers, the US payments go to only 2.5 million farmers.

The cut in loan rates had its main impact on world market prices. They went down, and stayed down. Moreover, the export subsidies paid by the US ('Export Enhancement Program') have pushed them down even further. The disastrous experience with these subsidies – which have mobilised other agricultural exporters against the US, but have not increased the US share of world grain markets – has made many people in Washington wonder whether they are not a political liability. Not even the fall in value of the dollar, which should make US exports more competitive, appears to have had a significant effect on the US farm trade balance. For several months in 1986 this was actually in deficit rather than surplus.

At the same time, the cash crisis in the farm states continues, as farmers struggle to service debts, which they contracted in better days, for investments which have proved unwise – including the purchase of land at high prices. These regional pressures increase the risk that Congress may oblige the Administration to take protectionist or other measures that will further destabilise world agricultural markets.

This feature of US decision-making is an ever-present problem for its trade partners, since in the field of trade the authority of the Administration is frequently circumscribed, and subject to approval by Congress. This means that it is sometimes impossible to be sure with exactly whom one is negotiating, while the negotiations themselves call for patience and can lead to disappointing surprises.

One must hope, therefore, that good sense and good faith will continue to inspire EC/US farm trade relations, and that bilateral disputes will not get out of hand. The EC remains, after all, the biggest

customer of the US for farm exports, and American farmers would have much to lose in a conflict. What the EC and the USA have in common is a mutual interest in cooperation to find solutions. Otherwise, as competitors, they will continue to rely on solutions which lead to increased financial costs, without corresponding benefits even for their farmers.

### Multilateral disarmament

What are the prospects for solving these problems and reducing the risks of conflict? Europe and the USA are the green superpowers, and much depends on their capacity for mutual understanding. But an agreed framework of rules and disciplines for farm trade cannot simply be a bilateral matter between two states.

The forum in which it must be defined is the General Agreement on Tariffs and Trade (GATT) which is now entering a new phase of negotiations, known as the 'Uruguay Round' because it opened at Punta del Este in Uruguay in September 1986. This new round, which is supposed to be concluded in four years, will cover many fields of trade policy, including tariff and non-tariff barriers, subsidies and countervailing measures, dispute settlement procedures, agricultural and industrial goods, services and so on.

Agriculture will be an important, even crucial, element in this round. It is thus especially interesting to note what the parties to the negotiations, including the EC and the USA, declared to be their intentions. They agreed at Punta del Este that 'there is an urgent need to bring some more discipline and predictability to world agricultural trade by correcting and preventing restrictions and distortions, including those related to structural surpluses, so as to reduce the uncertainty, imbalances and instability in world agricultural markets'.

The aim of the negotiations, therefore, is to reduce the barriers to farm trade and bring both import and export policies under more effective rules and disciplines. The Punta del Este declaration identifies three ways of pursuing this aim:

- (i) by improving market access through, among other things, the reduction of import barriers;
- (ii) by improving the competitive environment by increasing discipline in the use of all direct and indirect subsidies and other measures affecting agricultural trade directly or indirectly, including the phased reduction of their negative effects and dealing with their causes;
- (iii) by minimising the adverse effects that veterinary and plant health regulations and barriers can have on trade in agriculture, taking into account the relevant international agreements.'

This is an ambitious programme, which embraces not only a wide range of measures affecting farm trade, but also the idea that the causes of farm problems are often to be found in domestic support policies. Governments throughout the world, including Europe and the USA, will need courage and foresight to carry it out.