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TRENDS IN DOMESTIC SUPPORT – MARKET PRICE SUPPORT

COMMUNICATION FROM THE UNITED STATES OF AMERICA

1 OVERVIEW

1.1. WTO Members have agreed to the long-term objective of fair and market-oriented trading system for agricultural products. Developments in domestic support policies bear consideration because of changes in policies in a number of Members and their effects on the operation of global agricultural markets. One area of particular importance for review is the change in types of domestic support, in particular with respect to both exempt and non-exempt trade-distorting domestic support. This paper focuses on one of the most trade-distorting forms of support: market price support (MPS). While there has been progressive reduction in the application of MPS policies among the Members with the highest levels of support for agriculture in the 1980s, current trends show an increasing use of MPS policies by other Members.

1.2. Trends in the most trade-distorting forms of amber box domestic support is an area for consideration by the Committee on Agriculture because of the impact of such support on production (i.e., increased production) and trade (i.e., reduced imports and/or increased exports). Further, economic studies have shown that the most trade-distorting measures typically are the least efficient at transferring income benefits to farmers.[1]

2 WTO CATEGORIZATION OF TRADE DISTORTING SUPPORT

2.1. Under the Agreement on Agriculture, WTO Members report both exempt and non-exempt domestic support. As part of the Uruguay Round negotiations, countries submitted data on domestic support for the years 1986 – 1988. The sum of non-exempt trade-distorting support became the basis for establishing the Base Total Aggregate Measurement of Support (AMS), which is the basis for certain commitments made in the Uruguay Round. This data was reported through the Agricultural Supporting Tables (AGST) and can be reviewed through the WTO home page.[2]

2.2. Through the AGST, Members reported the scope of: 1) non-trade distorting measures exempt from reduction commitments (i.e., green box measures, Annex 2); 2) exempt product-specific and non-product specific trade-distorting support (i.e., Article 6.2 and blue box); and 3) non-exempt product-specific and non-product-specific trade-distorting support (i.e., amber box). In reporting trade-distorting support, Members detailed the amount of support through MPS, non-exempt direct payments, and other production or trade-distorting support. These types of support were aggregated without distinguishing more-distorting from less-distorting support. However, research suggests some of these forms of support are more distorting than others. Since the drafting of the Agreement on Agriculture, some Members have continued to make reforms to their agricultural policies moving towards less trade- and production-distorting measures, whether to the green box (e.g., fully decoupling), blue box (e.g., production limiting) or still in the amber box (e.g., partially decoupling). As a result, what was once only a minor distinction amongst amber box policies is now much more significant.

[1] Joe Dewbre, Jesús Antón and Wyatt Thompson. "The Transfer Efficiency and Trade Effects of Direct Payments", *American Journal of Agricultural Economics.* Vol. 83, Now. 5. (Dec. 2001), pp. 1204-1214.

[2] See http://www.wto.org/english/tratop_e/agric_e/supporting_tables_e.htm for copies of the AGST and http://www.wto.org/english/tratop_e/agric_e/dataset_ds_e.xls for a database in spreadsheet form.

3 THE EFFECTS OF MARKET PRICE SUPPORT

3.1. MPS policies are typically implemented with the objectives of increasing production of select commodities that are in short supply domestically and/or raising the income of producers of that commodity. Production objectives are typically cited by proponents of MPS policies as a protection against food security disruptions from potentially unreliable import sources. Proponents also commonly cite MPS policies as a way to increase producer incomes through higher and more stable prices.

3.2. Production incentives arise from guaranteeing higher prices for certain commodities over other commodities. Thus, MPS distorts production of targeted commodities by influencing production decisions, which may affect availability of other commodities not supported. By ensuring a minimum price, usually backed up by a government offer to operate as the buyer of last resort in the event of a fall in domestic prices, governments attempt to shield producers from the potential effects of falling demand or excess supply. Moreover, by raising the market price for a select commodity, proponents also state that they are able to provide the benefits of income support to the poorest and most rural producers without requiring a direct transfer of money.

3.3. According to OECD research, MPS is estimated to have one of the largest trade-distortive-effects and one of the lowest intended income effects for producers out of the major types of agricultural production support (i.e., market price support and four types of budgetary payments based on: output, variable input use, area planted in the current period, and area planted in an historical period).[3]

3.4. In practice, MPS affects and distorts the global agricultural economy in several important ways including changes in agricultural prices, resource allocations, food security, production/stock levels, and competitiveness.

3.1 Increased prices

3.5. The most direct and clear impact of the government setting minimum prices is an increase in domestic market prices for both producers and consumers.[4] The effect is most direct when a government sets a minimum price and places no limit on the quantity it is willing to purchase at the set price. However, the effect of the MPS can still be felt across the whole economy even when the government only purchases a limited quantity due to farmer's perceived reduced risk in prices falling below the set price. Higher prices increase the cost of the basic commodity and any processed product that incorporates that basic product.

3.6. Moreover, to sustain higher prices, imports must be closely regulated to guard against more competitively priced products from undermining the MPS scheme. Since MPS works by ensuring a high market price is available to producers, whether or not the government actually purchases at the administrative price, often Members that operate such systems maintain high tariffs, tariff rate quotas, or non-tariff measures. This deprives consumers in the subsidizing country and producers in exporting countries of the gains from trade.

3.2 Resource allocation

3.7. In contrast to direct payments (even when fully coupled to production decisions), MPS sets a minimum price for the market, which ensures that not only the producer of the basic commodity is

[3] OECD (2002). "Agricultural Policies in OECD Countries: A Positive Reform Agenda," p.32. https://encrypted.google.com/books?id=r2b9UC6vd7YC&printsec=frontcover&source=gbs_ViewAPI#v=onepage&q&f=false (https://encrypted.google.com/books?id=r2b9UC6vd7YC&printsec=frontcover&source=gbs_ViewAPI%23v=onepage&q&f=false) ; OECD (2001). "Market Effects of Crop Support Measures," pp. 22-25. http://www.keepeek.com/Digital-Asset-Management/oecd/agriculture-and-food/market-effects-of-crop-support-measures_9789264195011-en#page1 (http://www.keepeek.com/Digital-Asset-Management/oecd/agriculture-and-food/market-effects-of-crop-support-measures_9789264195011-en%23page1) .

[4] OECD (2001). "Market Effects of Crop Support Measures," 13-14. http://www.keepeek.com/Digital-Asset-Management/oecd/agriculture-and-food/market-effects-of-crop-support-measures_9789264195011-en#page1 (http://www.keepeek.com/Digital-Asset-Management/oecd/agriculture-and-food/market-effects-of-crop-support-measures_9789264195011-en%23page1) .

affected by the policy, but every other economic actor that has a relationship to the product is also affected. For example, the supported commodity represents a higher input cost for processors, which leads to adjustments in resource allocations and competitiveness throughout the food sector. Similarly, substitute products must also be regulated to guard against any price competition.

3.3 Impaired food security

3.8. Unlike other types of support, MPS policies increase food prices for both producers and consumers. As a result, MPS can contribute to food insecurity, particularly for already food insecure populations, which cannot afford higher food prices. Further, small self-sufficient producers who consume an important share of their production will not benefit from higher market prices for the portion of crops they consume, and they may pay higher prices for other supported crops they need to purchase.[5]

3.9. To address higher prices for consumers, governments must reduce the sales price through food subsidies, whether targeted to a low-income population that is unable to afford higher prices or the general population. This simultaneous lowering of consumer food prices and raising of producer prices can result in an expensive and complex market intervention scheme that only further disrupts market signals.

3.4 Over-production/stock buildups

3.10. Higher domestic prices, due to MPS, may directly induce over-production of a supported commodity, which can result in displacement of imports in the domestic market and the development of surplus stocks, often a result of government purchases. These stock build-ups can impact production and purchasing decisions in both domestic and international markets distorting prices further. In some cases, governments must resort to production quotas to address burgeoning government purchase and commodity surpluses.

3.5 Uncompetitive exports

3.11. High domestic prices make exports uncompetitive in world markets, and may encourage countries to use export subsidy policies to reduce the cost of maintaining domestic stocks. Since domestic market prices are artificially high due to MPS policies and private sector export sales are uncompetitive, export subsidies and the associated government intervention are required to move supported commodities into international markets. This adds further to the distorting effects of the original policy objective.

4 TRENDS IN MARKET PRICE SUPPORT

4.1. The European Union, the United States of America, Japan and Canada, the four Members with highest AMS levels in the 1986 – 1988 period, each reported substantial amounts of support through MPS policies. The situation of these Members is summarized below, along with those of India and China, two Members that reported MPS programs and have increased such support substantially for certain crops benefitting from this support.

4.1 European Union

4.2. In the AGST, the European Union reported MPS for beef, sheep meat, butter, skimmed milk powder, barley, wheat (common and durum), maize, rice, rye, sorghum, and sugar.[6] These sectors were covered by a variable levy system, which made it difficult for imports to compete on a price basis with the European Union product. The MPS was also backed up by European Union guarantees to farmers that all domestic production could be purchased by governments through

[5] Jonathan Brooks and Erik Jonasson, "Modeling the Welfare Implications of Agricultural Policies in Developing Countries," May 2012, pp. 19. http://www.gu.se/digitalAssets/1373/1373650_jonasson.pdf

[6] G/AG/AGST/EEC

intervention buying.[7] As a result of these policies, the European Union imports of these products were extremely limited, and the European Union producers responded to high prices with substantial surplus production that was removed from the domestic market with the aid of export subsidies.[8]

4.3. However, the European Union reform of domestic support measures began even during the long Uruguay Round negotiation.[9] Through a series of reforms to the Common Agricultural Policy, intervention prices are set at relatively low levels, limiting instances of government purchases. At the same time, the European Union has instituted a system of partially decoupled and fully decoupled payments to support producer income. As a consequence of these reforms the most recent European Union domestic support notification (2010) only reports MPS for butter, skimmed milk powders, and wheat.[10] Reported MPS has fallen nearly 85% in value terms. At the same time, the European Union use of export subsidies has also declined: in its last notification the European Union reported export subsidies only for beef, pork, poultry, eggs, and processed products.[11] Export subsidy activity reported for 2011/2012 is only a fraction of the level bound in the Uruguay Round, 130 million Euro compared to a sum of bound commitments of over 7.6 billion ECU. While the European Union tariffs continue to be applied at the high rates to protect the MPS system, the reforms have created scope for the European Union to negotiate tariff reductions without resulting in uncontained cost obligations in the event domestic prices fall due to increased competition from imports.

4.2 United States of America

4.4. In the AGST, the United States of America reported MPS for four products: beef, dairy, peanuts and sugar. After the reforms of successive Farm Bills, MPS only remains for sugar. The MPS system for beef was relatively small (US$158 million in reported support). There is currently no AMS support for beef. The U.S. tariff binding for beef is 26.4%.

4.5. The peanut program, prior to reform in the 2002 Farm Bill, was a rigid system where production quotas were distributed to growers eligible for the high domestic price support. Farmers interested in growing peanuts, but who lacked quota, could grow the crop, but were only permitted to sell the so-called "additional" peanuts on world markets. Because of the production controls, high priced peanuts were not taken into U.S. stocks or disposed of with export subsidies. The U.S. WTO bound tariff for peanuts is 163%, reflecting the level of protection needed to maintain high domestic prices. However, since 2002, peanuts have been covered by the same mixed system of direct government payments as other program commodities, including the partially decoupled direct payments under the 2014 Farm Bill.

4.6. The U.S. dairy program has also transitioned over time. Support measured in the AGST came from a system where all milk was covered by MPS, amounting to over US$5 billion per year. After a partial reform that limited MPS to certain dairy products (cheese, butter, and non-fat dry milk), MPS was ended in the 2014 Farm Bill. Dairy will now only be supported through a margin protection program, which makes direct payments to producers when production margins fall below US$4/cwt. As with other direct payment programs that replaced historical MPS schemes going back to before the Uruguay Round, payments under this program are partially decoupled: they apply when prices fall but are based on historical, not current, individual production decisions. Export subsidies had been available for dairy, but rarely used in recent years. Export subsidy authority for dairy was terminated with the reforms in the 2014 Farm Bill. U.S. dairy tariffs range from 5% to 140%.

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[7] *Ad valorem* equivalents of the tariff equivalents established for these products cover the following ranges (calculations based on AVE exercise in Doha): Beef (0201 and 0202): 77% - 146%; Sheep meat (0204): 27% - 104%; Butter (0405): 69% - 135%; Skimmed milk powder (0402): 19% - 183%; Barley (1003): 70%; Wheat (1001): 59% - 82%; Maize (1005): 73%; Rice (1006): 7% - 94%; Rye (1002): 64%; Sorghum (1007): 87%; Sugar (1701): 80% - 132%.

[8] The European Union established export subsidy bases for wheat, coarse grains, rice, rapeseed, olive oil, sugar, butter, skim milk powder, cheese, other milk products, beef, pork, poultry, eggs, wine, fruit and vegetables (fresh and processed), tobacco, alcohol and processed products.

[9] European Commission Agriculture and Rural Development, "The CAP in perspective: from market intervention to policy innovation," Brief No. 1 rev. January 2011. http://ec.europa.eu/agriculture/policy-perspectives/policy-briefs/01_en.pdf

[10] G/AG/N/EU/17 Supporting Table DS 5

[11] G/AG/N/EU/18

4.7. The U.S. sugar program is largely unchanged since the Uruguay Round. Sugar has a relatively high tariff (140% - 186% on an ad valorem equivalent basis) which limits imports outside of significant WTO tariff-rate quotas and commitments under free trade agreements. In the most recent U.S. notification, the notified AMS for sugar was US$1.4 billion.[12] Domestic production is limited by a system of marketing allotments, and the government stands by as a buyer of last resort if prices fall below administered price levels. The United States of America does not export sugar.

4.3 Japan

4.8. In the AGST, Japan reported MPS for beef, pork, milk, barley, rice, wheat, starch, sugar, and silk worm cocoons. Each of these sectors had high tariffs, and in the case of rice a complete import ban, prior to the Uruguay Round. Due to Japan's import needs, complex regimes were established for each product (including tariff-rate quotas, gate price systems, and use of state trading enterprises) that allowed imports but protected high domestic prices. Japan's domestic supply and demand situation also dictated that all production was destined for internal use, with limited exports and no use of export subsidies.

4.9. Currently Japan only reports MPS for beef and pork. The total amount of MPS is substantially below Uruguay Round base period levels: around 10% according to Japan's 2012 notification.[13] A significant change was the transition of rice from MPS to a system of exempt direct payments under production-limiting programs and various decoupled support systems.[14] As a result of this transition, MPS of 2.9 trillion yen from the 1986-1988 base period has been replaced by a little over 300 billion yen in direct payments. Japan continues to maintain high tariffs for rice, in excess of 700%, limiting imports and protecting domestic prices.

4.4 Canada

4.10. In the AGST, Canada reported MPS for wheat and milk. Wheat is no longer receiving MPS and instead benefits from the suite of insurance and income protection programs provided in Canada. However, dairy continues to be a highly protected sector where high domestic prices are enforced through production quotas, high tariffs (many over 300%) and other market access barriers, and export subsidies.

4.5 China

4.11. China's AGST covers the 1996 – 1998 period and includes MPS for wheat, rice, corn and cotton. For all of these commodities, except for corn, the MPS is negative, reflecting administered prices below world reference prices for that period. Market prices are protected against imports by high tariffs for these commodities: 65% for the grains and 40% for cotton. Complex tariff-rate quota administration schemes and application of sanitary and phytosanitary measures also reduce price pressure from trade.

4.12. In its latest notification (2008), China reported MPS only for wheat and rice, and reported support continued to be negative.[15] MPS has been supplemented with other programs, in particular seed and transportation subsidies and, for cotton, the cost of maintaining large and growing government held stocks.

4.6 India

4.13. India's AGST records MPS for a large number of commodities, almost all negative because administered prices were below external reference prices.[16] In India's latest notification (2003), it reports MPS for rice, wheat, pulses, cotton and jute.[17] These are all reported as negative levels, with applied administered prices below the fixed external reference price, even with the conversion

[12] G/AG/N/USA/93 Supporting Table DS 5
[13] G/AG/N/JPN/191 Supporting Table DS 5
[14] G/AG/N/JPN/192
[15] G/AG/N/CHN/21 Supporting Table DS 5
[16] Gram, Moong, Tur, Urad, Bajra, Barley, Jawar, Maize, Rice, Wheat, Groundnut, Rapeseed, Soyabean, Sugar cane, Tobacco, Cotton, and Tea.
[17] G/AG/N/IND/7 Supporting Table DS 5

of the reference price from rupee to dollars. Market prices are protected against imports by high tariffs: India's bound tariffs for pulses, wheat and cotton are 100%, 70 - 80% for rice, and 40% for jute. At times, applied rates are lower.

4.7 Relative Support Levels

4.14. The relative administered prices/price support levels are summarized in the table below. Administered prices vary considerably across countries. The United States of America marketing loan rate, which is a fully coupled output payment and most analogous to MPS policies in other countries, is provided for comparison purposes only. Importantly, however, the loan rate does not have the broader economic distortions associated with administered prices. Compared to the Fixed External Reference Price (FERP) established in Members' AGST documents, administered prices have increased substantially.

MPS: Administered and Fixed External Reference Prices

		2013 Administered Price	FERP
Rice			
	India	US$335/MT	US$262.51/MT
	China	US$426/MT	US$320.58/MT
	Thailand	US$468/MT	Not Notified
	Brazil	US$159-183/MT	US$174.13/MT
	*U.S.A.***	*US$143.30/MT*	*Not Notified*
Wheat			
	India	US$238/MT	US$264.00/MT
	China	US$361/MT	US$204.72/MT
	Brazil	US$246/MT	US$130.93/MT
	*U.S.A.***	*US$108/MT*	*Not Notified*
Sugar			
	India	US$35.84/MT	US$11.64/MT
	Thailand	US$618.37/MT	Not Notified
	*U.S.A.***	*US$413.36/MT*	*US$230.824/MT*
Cotton			
	India	US$631.42/MT	US$1,292.64/MT
	China	US$3,290/MT	US$1,758/MT
	Brazil	US$1,379/MT	US$1,255/MT
	*U.S.A.***	*US$1,146/MT*	*Not Notified*
Corn			
	India	US$223.56/MT	US$238.57/MT
	China	US$358-365/MT	US$144.53/MT
	Brazil	US$135-160/MT	US$131.35/MT
	*U.S.A.***	*US$76.77/MT*	*Not Notified*

** U.S.A. price is the loan rate for the marketing assistance loan program, which is not a price support program, but rather a coupled output program with fixed reference prices. It is included here for comparison purposes only.

Sources: India: Ministry of Agriculture.
China: China National Development and Reform Commission.
Thailand: Ministry of Commerce.
Brazil: Ministry of Agriculture, Livestock, and Supply
WTO Notifications.
Calculations by USDA.

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