## "Free exchange: Signs of Life?",

*Economist*, 15 Nov 2014, p. 68

**Evidence that globalisation is on the march again**

There are many definitions of globalisation, but the DHL Global Connectedness Index (Nov 2014) provides a useful means of assessing the degree to which the world is inter-connected, and the progress toward integration and less bothersome borders. The index uses one that is fairly all-embracing, encompassing four main types of cross-border flow: trade (in both goods and services), information, people (including tourists, students and migrants) and capital. It tracks not just the depth of international connections (how much activity crosses borders), but also their breadth (how many different borders are being crossed) and their direction (how do outward and inward flows compare).

Two economists, Pankaj Ghemawat of New York University's Stern School and Steven Altman of IESE Business School compiled it using data from 140 countries, which account for 99% of the world's GDP and 95% of its population. The authors found that the depth of global integration, perhaps the most straightforward definition of globalisation, fell sharply after 2008, by nearly one-tenth. Yet since then it has recovered strongly. By 2013 it was well above its pre-crash peak.

By contrast, the breadth measure continued to slide in 2013 and is nearly 5% below its peak. That is, there are more cross-border connections being made, but with fewer places. This may reflect the growing popularity of bilateral trade deals in the absence of big multilateral liberalisations. Another factor may be Western firms' slow response to the growing weight of emerging economies. In 2013 emerging economies generated only 17% of the profits of 100 of the biggest firms based in rich countries, even though they accounted for 36% of the world's GDP. The ten countries that globalised most in 2013 were emerging markets, most in Latin America and the Caribbean.

As the chart shows, the globalisation of information, measured by such things as the number of cross-border phone calls and Skype usage, slowed after the crash but did not fall, and accelerated again in 2013. Capital flows remain below pre-crisis levels, however. Trade in goods and services plunged in the aftermath of the crash, rebounded a bit, and then started sliding again, when measured by value (volumes are rising, albeit sluggishly).

**Trading paces**

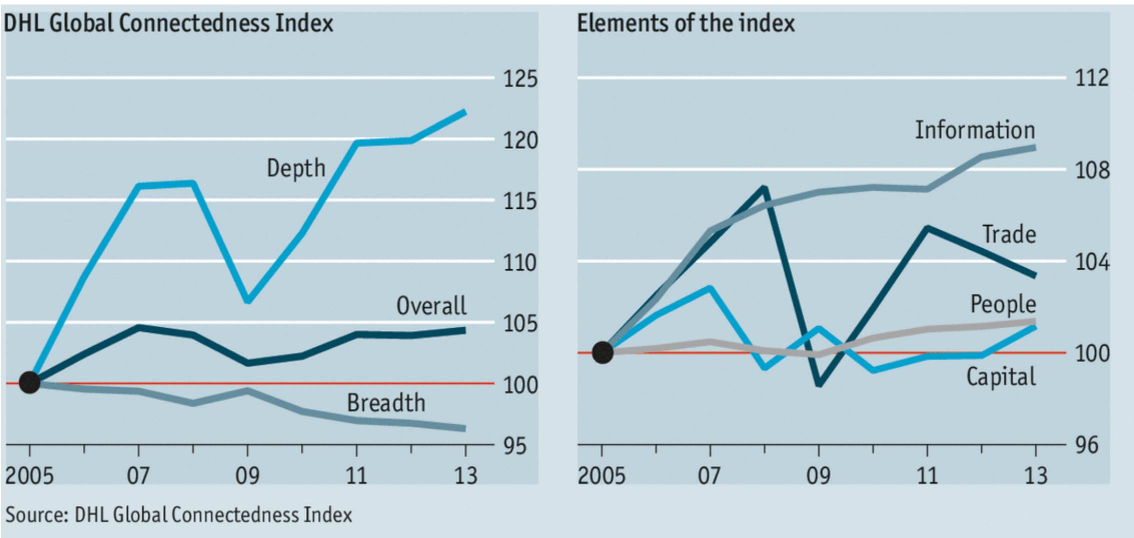
How worrying is the decline in trade? The economists calculate that the lower share of traded goods and services in total output is largely a function of sluggish global demand, and predict that as the world economy strengthens trade will too. There is evidence that protectionism is growing. Global Trade Alert, a watchdog, says that since 2008, over 70% of the changes to trade rules around the world have curbed trade, rather than spurring it. The World Trade Organisation (WTO), which is supposed to resist and reverse such measures, has struggled to do so.

Past episodes of deglobalisation suggest that political pressure to retreat from the world builds slowly but is also slow to dissipate. That seems to be the case this time too, in many European countries at least, where populist parties are still growing in strength, even though the local economy has stabilised and, in most instances, started growing again. The fact that globalisation is advancing again after such a calamitous crisis is encouraging, but further reversals are perfectly possible.

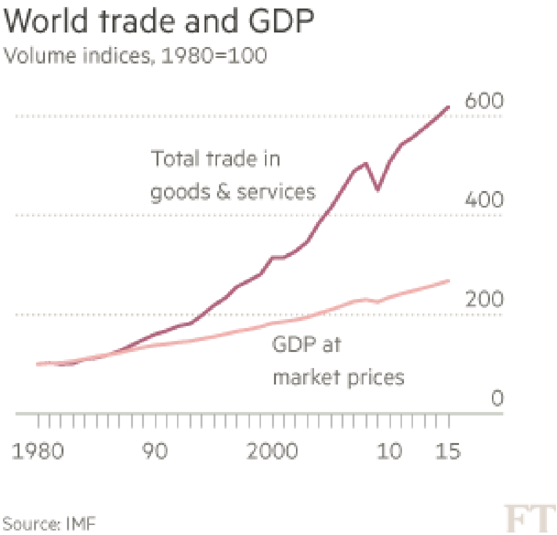
## "The WTO in Brief: Part 1. The multilateral trading system – past, present and future", World Trade Organization website, www.wto.org > About the WTO > Introductory brochures, accessed 2015

The World Trade Organization came into being in 1995 to administer the agreements which have been signed by the governments of its member states. One of the youngest of the international organizations, the WTO is the successor to the General Agreement on Tariffs and Trade (GATT) established in the wake of the Second World War. So, while the WTO is still young, the multilateral trading system that was originally set up under GATT is well over 50 years old. The WTO is the only international organization dealing with the global rules of trade between nations. Its main function is to ensure that trade flows as smoothly, predictably and freely as possible.

The past 50 years have seen an exceptional growth in world trade. Merchandise exports grew on average by 6% annually. Total trade in 2000 was 22-times the level of 1950. GATT and the WTO have helped to create a strong and prosperous trading system contributing to unprecedented growth.



The system was developed through a series of multilateral trade negotiations [i.e., many-sided participating member states whose numbers have increased over time], or rounds, held under GATT. Since GATT's creation in 1947-48 there have been eight rounds of multilateral trade negotiations. The first rounds dealt mainly with tariff reductions but later negotiations included other areas such as anti-dumping and non-tariff measures. A ninth round, under the Doha Development Agenda, is now underway. At first these focused on lowering tariffs (customs duties) on imported industrial goods. As a result of the negotiations, by the mid-1990s industrial countries' tariff rates on industrial goods had fallen steadily to less than 4%. But by the 1980s, the negotiations had expanded to cover non-tariff barriers on goods, and to the new areas such as services and intellectual property.



Source: *Financial Times*, "Embattled future of global trade policy", by Martin Wolf, 13 May 2015, p. 9

Opening markets can be beneficial, but it also requires adjustment. The WTO agreements allow countries to introduce changes gradually, through "progressive liberalization". Developing countries are usually given longer to fulfil their obligations.The last round — the 1986-94 Uruguay Round — led to the WTO's creation.

The negotiations did not end there. Some continued after the end of the Uruguay Round. In February 1997 agreement was reached on telecommunications services, with 69 governments agreeing to wide-ranging liberalization measures that went beyond those agreed in the Uruguay Round.

In the same year 40 governments successfully concluded negotiations for tariff-free trade in information technology products, and 70 members concluded a financial services deal covering more than 95% of trade in banking, insurance, securities and financial information.

In 2000, new talks started on agriculture and services. These have now been incorporated into a broader agenda launched at the fourth WTO Ministerial Conference in Doha, Qatar, in November 2001.

The work programme, the Doha Development Agenda (DDA), adds negotiations and other work on non-agricultural tariffs, trade and environment, WTO rules such as anti-dumping and subsidies, investment, competition policy, trade facilitation, transparency in government procurement, intellectual property, and a range of issues raised by developing countries as difficulties they face in implementing the present WTO agreements.

## "Understanding the WTO: The Agreements", WTO, www.wto.org (click on 'trade topics')

**Overview: a navigational guide**

The World Trade Organization is the international organization whose primary purpose is to open trade for the benefit of all. The WTO provides a forum for negotiating agreements aimed at reducing obstacles to international trade and ensuring a level playing field for all, thus contributing to economic growth and development. The WTO also provides a legal and institutional framework for the implementation and monitoring of these agreements, as well as for settling disputes arising from their interpretation and application. The current body of trade agreements comprising the WTO consists of 16 different multilateral agreements (to which all WTO members are parties) and two different plurilateral agreements (to which only some WTO members are parties).

Over the past 60 years, the WTO, which was established in 1995, and its predecessor organization the GATT have helped to create a strong and prosperous international trading system, thereby contributing to unprecedented global economic growth. The WTO currently has 161 members, of which 117 are developing countries or separate customs territories. WTO activities are supported by a Secretariat based in Geneva, Switzerland, comprised of some 700 staff, led by the WTO Director-General.

Decisions in the WTO are generally taken by consensus of the entire membership. The highest institutional body is the Ministerial Conference, which meets roughly every two years. A General Council conducts the organization's business in the intervals between Ministerial Conferences. Both of these bodies comprise all members. Specialised subsidiary bodies (Councils, Committees, Sub-committees), also comprising all members, administer and monitor the implementation by members of the various WTO agreements.

More specifically, the WTO's main activities are:

- negotiating the reduction or elimination of obstacles to trade (import tariffs, other barriers to trade) and agreeing on rules governing the conduct of international trade (e.g. antidumping, subsidies, product standards, etc.);
- administering and monitoring the application of the WTO's agreed rules for trade in goods, trade in services, and trade-related intellectual property rights;
- monitoring and reviewing the trade policies of our members, as well as ensuring transparency of regional and bilateral trade agreements;
- settling disputes among our members regarding the interpretation and application of the agreements;
- building capacity of developing country government officials in international trade matters;
- assisting the process of accession of some 30 countries who are not yet members of the organization;
- conducting economic research and collecting and disseminating trade data in support of the WTO's other main activities;
- explaining to and educating the public about the WTO, its mission and its activities.

The WTO's founding and guiding principles remain the pursuit of open borders, the guarantee of most-favoured-nation principle and non-discriminatory treatment by and among members, and a commitment to transparency in the conduct of its activities. The opening of national markets to international trade, with justifiable exceptions or with adequate flexibilities, will encourage and contribute to sustainable development, raise people's welfare, reduce poverty, and foster peace and stability. At the same time, such market opening must be accompanied by sound domestic and international policies that contribute to economic growth and development according to each member's needs and aspirations.

The WTO agreements cover goods, services and intellectual property. They spell out the principles of liberalization, and the permitted exceptions. They include individual countries' commitments to lower customs tariffs and other trade barriers, and to open and keep open services markets. They set procedures for settling disputes. They prescribe special treatment for developing countries. They require governments to make their trade policies transparent by notifying the WTO about laws in force and measures adopted, and through regular reports by the secretariat on countries' trade policies. These agreements are often called the WTO's trade rules, and the WTO is often described as "rules-based", a system based on rules. But it's important to remember that the rules are actually agreements that governments negotiated.

**What we do**

The WTO is run by its member governments. All major decisions are made by the membership as a whole, either by ministers (who usually meet at least once every two years) or by their ambassadors or delegates (who meet regularly in Geneva).

While the WTO is driven by its member states, it could not function without its Secretariat to coordinate the activities. The Secretariat employs over 600 staff, and its experts — lawyers, economists, statisticians and communications experts — assist WTO members on a daily basis to ensure, among other things, that negotiations progress smoothly, and that the rules of international trade are correctly applied and enforced.

**Trade negotiations**

The WTO agreements cover goods, services and intellectual property. They spell out the principles of liberalization, and the permitted exceptions. They include individual countries' commitments to lower customs tariffs and other trade barriers, and to open and keep open services markets. They set procedures for settling disputes. These agreements are not static; they are renegotiated from time to time and new agreements can be added to the package. Many are now being negotiated under the Doha Development Agenda, launched by WTO trade ministers in Doha, Qatar, in November 2001.

**Implementation and monitoring**

WTO agreements require governments to make their trade policies transparent by notifying the WTO about laws in force and measures adopted. Various WTO councils and committees seek to ensure that these requirements are being followed and that WTO agreements are being properly implemented. All WTO members must undergo periodic scrutiny of their trade policies and practices, each review containing reports by the country concerned and the WTO Secretariat.

**Dispute settlement**

The WTO's procedure for resolving trade quarrels under the Dispute Settlement Understanding is vital for enforcing the rules and therefore for ensuring that trade flows smoothly. Countries bring disputes to the WTO if they think their rights under the agreements are being infringed. Judgements by specially appointed independent experts are based on interpretations of the agreements and individual countries' commitments.

## Market Access: Trade in Goods

Uruguay Round: There was no legally binding agreement that set out the targets for tariff reductions (e.g. by what percentage tariffs were to be cut as part of the final deal). Instead, individual countries listed their commitments in schedules annexed to Marrakesh Protocol to the General Agreement on Tariffs and Trade 1994. This was the legally binding agreement for the reduced tariff rates. Since then, additional commitments were made under the 1997 Information Technology Agreement.

### Tariffs: more bindings and closer to zero

The bulkiest results of Uruguay Round are the 22,500 pages listing individual countries' commitments on specific categories of goods and services. These include commitments to cut and "bind" their customs duty rates on imports of goods. In some cases, tariffs were cut to zero. There was a significant increase in the number of "bound" tariffs — duty rates that are committed in the WTO to having ceilings and are difficult to raise.

**'Binding' tariffs**

The market access schedules are not simply announcements of tariff rates. They represent commitments not to increase tariffs above the listed rates — the rates are "bound". For developed countries, the bound rates are generally the rates actually charged. Most developing countries have bound the rates somewhat higher than the actual rates charged, so the bound rates serve as ceilings.

Countries can break a commitment (i.e. raise a tariff above the bound rate), but only with difficulty. To do so they have to negotiate with the countries most concerned and that could result in compensation for trading partners' loss of trade.

Tariff cuts

Developed countries' tariff cuts were for the most part phased in over five years from 1 January 1995. The result is a 40% cut in their tariffs on industrial products, from an average of 6.3% to 3.8%. The value of imported industrial products that receive duty-free treatment in developed countries will jump from 20% to 44%.

There will also be fewer products charged high duty rates. The proportion of imports into developed countries from all sources facing tariffs rates of more than 15% will decline from 7% to 5%. The proportion of developing country exports facing tariffs above 15% in industrial countries will fall from 9% to 5%.

The Uruguay Round package has been improved. On 26 March 1997, 40 countries accounting for more than 92% of world trade in information technology products, agreed to eliminate import duties and other charges on these products by 2000 (by 2005 in a handful of cases). As with other tariff commitments, each participating country is applying its commitments equally to exports from all WTO members (i.e. on a most-favoured-nation basis), even from members that did not make commitments.

**More bindings**

Developed countries increased the number of imports whose tariff rates are "bound" (committed and difficult to increase) from 78% of product lines to 99%. For developing countries, the increase was considerable: from 21% to 73%. Economies in transition from central planning increased their bindings from 73% to 98%. This all means a substantially higher degree of market security for traders and investors.

**And agriculture ...**
Tariffs on all agricultural products are now bound. Almost all import restrictions that did not take the form of tariffs, such as quotas, have been converted to tariffs — a process known as "tariffication". This has made markets substantially more predictable for agriculture. Previously more than 30% of agricultural produce had faced quotas or import restrictions. The first step in "tariffication" was to replace these restrictions with tariffs that represented about the same level of protection. Then, over six years from 1995-2000, these tariffs were gradually reduced (the reduction period for developing countries ends in 2005). The market access commitments on agriculture also eliminate previous import bans on certain products.

In addition, the lists include countries' commitments to reduce domestic support and export subsidies for agricultural products. (S*ee section on* *market access:agriculture*.)

**Market Access: Agriculture**

Under the reform programme, members have converted their non-tariff measures to equivalent bound tariffs. Some additional market access was provided through tariff rate quotas, and the tariffs were reduced. Contingency protection is provided through special safeguards, and transparency works through notifications and reporting on compliance.

**The conceptual framework**
On the market access side, the Uruguay Round resulted in a key systemic change: the switch from a situation where a myriad of non-tariff measures impeded agricultural trade flows to a regime of bound tariff-only protection plus reduction commitments. The key aspects of this fundamental change have been to stimulate investment, production and trade in agriculture by (i) making agricultural market access conditions more transparent, predictable and competitive, (ii) establishing or strengthening the link between national and international agricultural markets, and thus (iii) relying more prominently on the market for guiding scarce resources into their most productive uses both within the agricultural sector and economy-wide.

In many cases, tariffs were the only form of protection for agricultural products before the Uruguay Round — the Round led to the "binding" in the WTO of a maximum level for these tariffs. For many other products, however, market access restrictions involved non-tariff barriers. This was frequently, though not only, the case for major temperate zone agricultural products. The Uruguay Round negotiations aimed to remove such barriers. For this purpose, a "tariffication" package was agreed which, amongst other things, provided for the replacement of agriculture-specific non-tariff measures with a tariff which afforded an equivalent level of protection. The tariffs resulting from the tariffication process account, on average of the developed country Members, for around one fifth of the total number of agricultural tariff lines. For the developing country Members, this share is considerably smaller. Following the entry into force of the Agreement on Agriculture, there is now a prohibition on agriculture-specific non-tariff measures, and the tariffs on virtually all agricultural products traded internationally are bound in the WTO.

**Schedule of tariff concessions**
Each WTO Member has a "schedule" of tariff concessions covering all agricultural products. These concessions are an integral part of the results of the Uruguay Round, are formally annexed to the Marrakesh Protocol [cross-reference] and have become an integral part of the GATT 1994 [cross-reference]. The schedule sets out for each individual agricultural product, or, in some cases agricultural products defined more generally, the maximum tariff that can be applied on imports into the territory of the Member concerned. The tariffs in the schedules include those that resulted from the tariffication process, which, in many cases, are considerably higher than industrial tariffs, reflecting the incidence of agriculture-specific non-tariff measures prior to the WTO. Many developing countries have bound their previously unbound tariffs at "ceiling" levels, i.e. at levels higher than the applied rates prior to the WTO.

Developed country Members have agreed to reduce, over a six-year period beginning in 1995, their tariffs by 36 per cent on average of all agricultural products, with a minimum cut of 15 per cent for any product. For developing countries, the cuts are 24 and 10 per cent, respectively, to be implemented over ten years. Those developing country Members which bound tariffs at ceiling levels did not, in many cases, undertake reduction commitments. Least-developed country Members were required to bind all agricultural tariffs, but not to undertake tariff reductions.

**... and tariff quota commitments**
As part of the tariffication package, WTO Members were required to maintain, for tariffied products, current import access opportunities at levels corresponding to those existing during the 1986-88 base period. Where such "current" access had been less than 5 per cent of domestic consumption of the product in question in the base period, an (additional) minimum access opportunity had to be opened on a most-favoured-nation basis. This was to ensure that in 1995, current and minimum access opportunities combined represented at least 3 per cent of base-period consumption and are progressively expanded to reach 5 per cent of that consumption in the year 2000 (developed country Members) or 2004 (developing country Members), respectively.

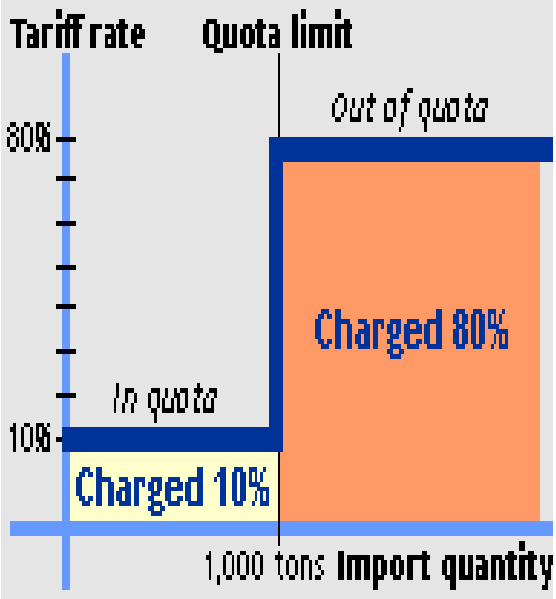
The current and minimum access opportunities are generally implemented in the form of tariff quotas. In case of minimum access, the applicable duty was required to be low or minimal, low that is either in absolute terms or, at least, in relation to the "normal" ordinary customs duty that applies to any imports outside the tariff quota. These tariff quotas, including the applicable tariff rates and any other conditions related to the tariff quotas, are specified in the schedules of the WTO Members concerned.

While the vast majority of tariff quotas in agriculture have their origin in the Uruguay Round negotiations, a number of such commitments were the result of accessions to the WTO. Currently (July 1999), 37 Members have tariff quotas specified in their schedules. In total, there are 1374 individual tariff quotas. These tariff quotas constitute binding commitments as opposed to autonomous tariff quotas which Members may establish at any time, for example, in order to stabilize the domestic price after a poor harvest.

**The prohibition of non-tariff border measures**
Article 4.2 of the Agreement on Agriculture prohibits the use of agriculture-specific non-tariff measures. Such measures include quantitative import restrictions, variable import levies, minimum import prices, discretionary import licensing procedures, voluntary export restraint agreements and non-tariff measures maintained through state-trading enterprises. All similar border measures other than "normal customs duties" are also no longer permitted. Although Article XI:2(c) of the GATT [cross-reference] continues to permit non-tariff import restrictions on fisheries products, it is now inoperative as

regards agricultural products because it is superseded by the Agreement on Agriculture.

**A tariff-quota**
This is what a tariff-quota might look like.




Imports entering under the tariff-quota (up to 1,000 tons) are generally charged 10%. Imports entering outside the tariff-quota are charged 80%. Under the Uruguay Round agreement, the 1,000 tons would be based on actual imports in the base period or an agreed "minimum access" formula. Tariff quotas are also called "tariff-rate quotas".

However, Article 4.2 of the Agreement on Agriculture does not prevent the use of non-tariff import restrictions consistent with the provisions of the GATT or other WTO agreements which are applicable to traded goods generally (industrial or agricultural). Such measures include those maintained under balance-of-payments provisions (Articles XII and XVIII of GATT), general safeguard provisions (Article XIX of GATT and the related WTO agreement), general exceptions (Article XX of GATT), the Agreement on the Application of Sanitary and Phytosanitary Measures, the Agreement on Technical Barriers to Trade or other general, non -agriculture-specific WTO provisions.

**Special treatment**
The Agreement on Agriculture contains a "special treatment" clause (Annex 5), under which four countries were permitted, subject to strictly circumscribed conditions, to maintain non-tariff border measures on certain products during the period of tariff reductions (with the possibility of extending the special treatment, subject to further negotiations). As one of the conditions, market access in the form of progressively increasing import quotas has to be provided for the products concerned. The products and countries concerned are: rice in the case of Japan, Korea and the Philippines; and cheese and sheepmeat in the case of Israel. As of 1 April 1999, Japan has ceased to apply special treatment.

**The special safeguard provisions**
As a third element of the tariffication package, Members have the right to invoke for tariffied products the special safeguard provisions of the Agreement on Agriculture (Article 5), provided that a reservation to this effect ("SSG") appears beside the products concerned in the relevant Member's schedule. The right to make use of the special safeguard provisions has been reserved by 38 Members, and for a limited number of products in each case.

The special safeguard provisions allow the imposition of an additional tariff where certain criteria are met. The criteria involve either a specified surge in imports (volume trigger), or, on a shipment by shipment basis, a fall of the import price below a specified reference price (price trigger). In case of the volume trigger, the higher duties only apply until the end of the year in question. In case of the price trigger, any additional duty can only be imposed on the shipment concerned. The additional duties cannot be applied to imports taking place within tariff quotas.

**Notification obligations**
The bound agricultural tariffs and the tariff quota commitments are contained in Members' schedules. There is no requirement for Members to notify their tariffs to the Committee on Agriculture. Applied tariffs are, however, to be submitted to other bodies of the WTO, including the Committee on Market Access and in the context of the Trade Policy Review mechanism.

Members with tariff quotas and the right to use the special safeguard provisions are required to make both ad hoc and annual notifications to the Committee on Agriculture. At the beginning of the implementation period, an "up-front" notification was due, setting out how each tariff quota is to be administered. Such notifications disclose, for example, if imports are permitted on a "first-come-first-served" basis or if import licences are used — and in the latter case, an indication of who is able to obtain a licence and how they are allocated. An ad hoc notification is required if the method of allocation under any tariff quota changes. At the end of each year, a notification of the quantity of imports entering under each tariff quota is required (tariff quota fill).

Members with the right to use the special safeguard provisions must notify its first use in order to allow its trading partners to establish the parameters of the special safeguard action, such as the volume or price used to trigger the special safeguard action. In the case of the price trigger, an upfront notification of the relevant reference prices has also been possible. In addition, an annual summary notification of the use of the special safeguard is required.

## Agricultural Negotiations

Market access: tariffs and tariff quotas
Nowadays, among WTO members, agricultural products are protected only by tariffs. All non-tariff barriers had to be eliminated or converted to tariffs as a result of the Uruguay Round (the conversion was known as "tariffication"). In some cases, the calculated equivalent tariffs — like the original measures that were tariffied — were too high to allow any real opportunity for imports. So a system of tariff-rate quotas was created to maintain existing import access levels, and to provide minimum access opportunities. This means lower tariffs within the quotas, and higher rates for quantities outside the quotas.

The discussion since the Uruguay Round has focused broadly on two issues: the high levels of tariffs outside the quotas (with some countries pressing for larger cuts on the higher tariffs), and the quotas themselves — their size, the way they have been administered, and the tariffs charged on imports within the quotas.

By the time of the 2002-2003 preparations for "modalities", the discussions cover six headings: **tariffs; tariff quotas; tariff quota administration; special safeguards; importing state trading enterprises**, and

**other issues.** Within each heading, is a list of subheadings such as: general comments; scope/definitions/product coverage; stages/timetables; transparency and notification; and so on. Special and differential treatment for developing countries and non-trade concerns are discussed under all of them, and again members differ as to whether the Doha declaration treats these as equals or whether non-trade concerns have a lesser priority.

During the discussion, new members and transition economies repeatedly argue for special and differential treatment for countries in their position, because of the state of their economies and because the new members are still implementing market-access commitments under their membership agreements.

Tariffs: Phase 1
The discussion of tariffs covers both tariffs on quantities within quotas and those outside. Traditionally, the tariff reductions that resulted from trade negotiations came from bilateral product-by-product bargaining, or they were based on formulas that applied over a broad range of products, or combinations of the two. How the reductions will be handled in the present negotiations is hotly debated. Some countries — such as Canada and the US — are advocating that in addition, "sectoral liberalization" should be negotiated. In some sectors in past negotiations, this has sometimes meant "zero-for-zero" deals. It would include negotiating the complete elimination of tariffs (and possibly other measures such as export subsidies or subsidized export credits) by at least the key WTO members in specific sectors such as oilseeds, and barley and malt. Some countries — for example Japan — have said they do not support this.

One country, the US, has gone so far as to argue that because so many agricultural tariffs are high, the negotiations to reduce tariffs should start with "applied rates" (the tariffs governments actually charge on agricultural imports) and not the generally higher "bound rates" (the legally binding ceilings committed in the WTO as a result of previous negotiations). This has proved quite controversial because it would break a tradition of basing negotiations on bound rates. A number of countries have also countered that they should be given credit for unilaterally applying tariffs that are more liberal than the negotiated bound rates, instead of being forced to make even deeper cuts than countries that kept to their higher bound rates. Some countries that recently joined the WTO also feel that they accepted low tariffs in order to become members and therefore should not have to reduce them much further.

A number of developing countries also complain that they face difficulty if they try to increase their incomes by processing the agricultural raw materials that they produce. This is because the countries they see as potential export markets impose higher duties on processed imports than on the raw materials — known as tariff escalation — in order to protect their own processing industries.

Some countries see tariffs and other import barriers as necessary in order to protect domestic production and maintain food security. For this reason, some countries are linking lower import barriers with disciplines on other countries' export restraints and export taxes — if producing countries do not restrict their exports, then importing countries can feel more secure about being able to obtaining food from them. Some developing countries say they need flexibility in deciding the level of import duties they charge to protect their farmers against competition from imports whose prices are low because of export subsidies.

**Tariffs: Phase 2**
Two proposals have emerged for tariff reductions in general. One would copy the formula of the 1986-94 Uruguay Round negotiations which used an average reduction over all products, allowing some variation for individual products provided a minimum reduction was met. This would be "simpler" to implement, advocates say. Another, known as a "cocktail" approach envisages a flat rate percentage reduction for all products (the percentage so far unspecified), with additional "non-linear" reductions on higher tariffs, expanding quotas, and special treatment for developing countries. Advocates have described this as "fairer".

**Developed countries:** three bands of tariff rates, cut over 5 years

| **Tariff rate** | **Average cut** | **Minimum cut for any product** |
|---|---|---|
| 90%+ | 60% | 45% |
| 15-90% | 50% | 35% |
| 0-15% | 40% | 25% |

**Developing countries:** four bands of tariff rates plus a "special products" category, cut over 10 years

| Tariff rate | Average cut | Minimum cut for any product |
|---|---|---|
| 120%+ | 40% | 30% |
| 60-120% | 35% | 25% |
| 20-60% | 30% | 20% |
| 0-20% | 25% | 15% |
| Special products | 10% | 5% |

**Tariff quotas: Phase 1**
Quota administration is a technical subject, but it has a real impact on trade — on whether a product exported from one country can gain access to the market of another country at the lower, within-quota tariff.

Methods used for giving exporters access to quotas include first-come, first-served allocations, import licensing according to historical shares and other criteria, administering through state trading enterprise, bilateral agreements, and auctioning. The terms can also specify time periods for using the quotas, for example periods of time for applying for licences, or for delivering the products to the importing countries. Exporters are sometimes concerned that their ability to take advantage of tariff quotas can be handicapped because of the way the quotas are administered. Sometimes they also complain that the licensing timetables put them at a disadvantage when production is seasonal and the products have to be transported over long distances.

Each method has advantages and disadvantages, and many WTO members acknowledge that it can be difficult to say conclusively whether one method is better than another. Several countries want the negotiations to deal with tariff quotas: to replace them with low tariffs, to increase their size, to sort out what they consider to be restricting and non-transparent allocation methods, or to clarify which methods are legal or illegal under WTO rules in order to provide legal certainty.

Tariff quota administration: Phase 2
Participants in the negotiations generally accept that there is no single "best" method of administering quotas. Some want the negotiations to sort out which allocation methods should be allowed and which should not. Others are looking for broad principles such as transparency and

access for all-comers (at least for part of the quota allocation).

Some countries say that if part of a quota is unused ("underfill"), this is often a problem caused by the administration method. They propose various solutions to reduce underfill, including carrying unused portions over to subsequent periods, preventing imports at out-of-quota tariff rates until the quotas are filled, and closer monitoring. Others say underfill is often caused by supply and demand conditions, and should not be considered a problem.

Auctioning quotas is one method that has aroused a lot of discussion. One view is that the money governments raise from auctioning is equivalent to an additional tax and could violate tariff commitments ("bindings"). Another is that auctioning simply makes the additional value created by a quota ("quota rent") more transparent, and shifts it to the government instead of to private companies. Supporters add that it meets the objectives of transparency and simplicity, while giving all importing companies the chance to participate.

A number of other methods are also examined and their pros and cons debated. These included first-come-first-served, historical allocation, etc. ♦

## Agreement on Subsidies and Countervailing Measures (SCM),

WTO, www.wto.org (click on 'trade topics' > subsidies)

### Subsidies and countervailing measures: overview

The Agreement on Subsidies and Countervailing Measures ("SCM Agreement") addresses two separate but closely related topics: multilateral disciplines regulating the provision of subsidies, and the use of countervailing measures to offset injury caused by subsidized imports (module 4).

Multilateral disciplines are the rules regarding whether or not a subsidy may be provided by a Member. They are enforced through invocation of the WTO dispute settlement mechanism. Countervailing duties are a unilateral instrument, which may be applied by a Member after an investigation by that Member and a determination that the criteria set forth in the SCM Agreement are satisfied.

**Definition of subsidy** Unlike the Tokyo Round Subsidies Code, the WTO SCM Agreement contains a definition of the term "subsidy". The definition contains three basic elements: (i) a financial contribution (ii) by a government or any public body within the territory of a Member (iii) which confers a benefit. All three of these elements must be satisfied in order for a subsidy to exist.

The concept of "financial contribution" was included in the SCM Agreement only after a protracted negotiation. Some Members (EC) argued that there could be no subsidy unless there was a charge on the public account. Other Members (US) considered that forms of government intervention that did not involve an expense to the government nevertheless distorted competition and should thus be considered to be subsidies. The SCM Agreement basically adopted the former approach. The Agreement requires a financial contribution and contains a list of the types of measures that represent a financial contribution, e.g., grants, loans, equity infusions, loan guarantees, fiscal incentives, the provision of goods or services, the purchase of goods.

A financial contribution to be a subsidy must be made by or at the direction of a government or any public body within the territory of a Member. Thus, the SCM Agreement applies not only to measures of national governments, but also to measures of sub-national governments and of such public bodies as state-owned companies.

A financial contribution by a government is not a subsidy unless it confers a "benefit." In many cases, as in the case of a cash grant, the existence of a benefit and its valuation will be clear. In some cases, however, the issue of benefit will be more complex. For example, when does a loan, an equity infusion or the purchase by a government of a good confer a benefit? Although the SCM Agreement does not provide complete guidance on these issues, the Appellate Body has ruled (Canada – Aircraft) that the existence of a benefit is to be determined by comparison with the market-place (i.e., on the basis of what the recipient could have received in the market). In the context of countervailing duties, Article 14 of the SCM Agreement provides some guidance with respect to determining whether certain types of measures confer a benefit. In the context of multilateral disciplines, however, the issue of the meaning of "benefit" is not fully resolved.

**Specificity.** Assuming that a measure is a subsidy within the meaning of the SCM Agreement, it nevertheless is not subject to the SCM Agreement unless it has been specifically provided to an enterprise or industry or group of enterprises or industries. The basic principle is that a subsidy that distorts the allocation of resources within an economy should be subject to discipline. Where a subsidy is widely available within an economy, such a distortion in the allocation of resources is presumed not to occur. Thus, only "specific" subsidies are subject to the SCM Agreement disciplines. There are four types of "specificity" within the meaning of the SCM Agreement:

- **Enterprise-specificity**. A government targets a particular company or companies for subsidization;
- **Industry-specificity.** A government targets a particular sector or sectors for subsidization.
- **Regional specificity.** A government targets producers in specified parts of its territory for subsidization.
- **Prohibited subsidies.** A government targets export goods or goods using domestic inputs for subsidization.

**Categories of Subsidies**
The SCM Agreement creates two basic categories of subsidies: those that are prohibited, those that are actionable (i.e., subject to challenge in the WTO or to countervailing measures). All specific subsidies fall into one of these categories.

**Prohibited subsidies** Two categories of subsidies are prohibited by Article 3 of the SCM Agreement. The first category consists of subsidies contingent, in law or in fact, whether wholly or as one of several conditions, on export performance ("export subsidies"). A detailed list of export subsidies is annexed to the SCM Agreement. The second category consists of subsidies contingent, whether solely or as one of several other conditions, upon the use of domestic over imported goods ("local content subsidies"). These two categories of subsidies are prohibited because they are designed to directly affect trade and thus are most likely to have adverse effects on the interests of other Members.

The scope of these prohibitions is relatively narrow. Developed countries had already accepted the prohibition on export subsidies under the Tokyo Round SCM Agreement, and local content subsidies of the type prohibited by the SCM Agreement were already inconsistent with Article III of the GATT 1947. What is most significant about the new Agreement in this area is the extension of the obligations to developing country Members subject to specified transition rules (see section below on special and differential treatment), as well as the creation in Article 4 of the SCM Agreement of a rapid (three-month) dispute settlement mechanism for complaints regarding prohibited subsidies.

**Actionable subsidies** Most subsidies, such as production subsidies, fall in the "actionable" category. Actionable subsidies are not prohibited. However, they are subject to challenge, either through multilateral dispute settlement or through countervailing action, in the event that they cause adverse effects to the interests of another Member. There are three types of adverse effects. First, there is **injury** to a domestic industry caused by subsidized imports in the territory of the complaining Member. This is the sole basis for countervailing action. Second, there is **serious prejudice**. Serious prejudice usually arises as a result of adverse effects (e.g., export displacement) in the market of the subsidizing Member or in a third country market. Thus, unlike injury, it can serve as the basis for a complaint related to harm to a Member's export interests. Finally, there is **nullification or impairment** of benefits accruing under the GATT 1994. Nullification or impairment arises most typically where the improved market access presumed to flow from a bound tariff reduction is undercut by subsidization.

**Agricultural subsidies** Article 13 of the Agreement on Agriculture establishes, during the implementation period specified in that Agreement (until 1 January 2003), special rules regarding subsidies for agricultural products. Export subsidies which are in full conformity with the Agriculture Agreement are not prohibited by the SCM Agreement, although they remain countervailable. Domestic supports which are in full conformity with the Agriculture Agreement are not actionable multilaterally, although they also may be subject to countervailing duties. Finally, domestic supports within the "green box" of the Agriculture Agreement are not actionable multilaterally nor are they subject to countervailing measures. After the implementation period, the SCM Agreement shall apply to subsidies for agricultural products subject to the provisions of the Agreement on Agriculture, as set forth in its Article 21.

### Transition Rules and Special and Differential Treatment

Developed countries
Members not otherwise eligible for special and differential treatment are allowed three years from the date on which for them the SCM Agreement enters into force to phase out prohibited subsidies. Such subsidies must be notified within 90 days of the entry into force of the WTO Agreement for the notifying Member.

Developing countries
The SCM Agreement recognizes three categories of developing country Members: least-developed Members ("LDCs"), Members with a GNP per capita of less than $1000 per year which are listed in Annex VII to the SCM Agreement, and other developing countries. The lower a Member's level of development, the more favourable the treatment it receives with respect to subsidies disciplines. Thus, for example, LDCs and Members with a GNP per capita of less than $1000 per year listed in Annex VII are exempted from the prohibition on export subsidies. Other developing country Members have an eight-year period to phase out their export subsidies (they cannot increase the level of their export subsidies during this period). With respect to import-substitution subsidies, LDCs have eight years and other developing country Members five years, to phase out such subsidies. There is also more favourable treatment with respect to actionable subsidies. For example, certain subsidies related to developing country Members' privatization programmes are not actionable multilaterally.. With respect to countervailing measures, developing country Members' exporters are entitled to more favourable treatment with respect to the termination of investigations where the level of subsidization or volume of imports is small.

Members in transformation to a market economy
Members in transformation to a market economy are given a seven-year period to phase out prohibited subsidies. These subsidies must, however, have been notified within two years of the date of entry into force of the WTO Agreement (i.e., by 31 December 1996) in order to benefit from the special treatment. Members in transformation also receive preferential treatment with respect to actionable subsidies.

**Notifications**

Subsidies Article 25 of the SCM Agreement requires that Members notify all specific subsidies (at all levels of government and covering all goods sectors, including agriculture) to the SCM Committee. New and full notifications are due every three years with update notifications in intervening years. The notifications are the subject of extensive review and discussion by the SCM Committee.

Countervailing legislation and measures All Members are required to notify their countervailing duty laws and regulations to the SCM Committee pursuant to Article 32.6 of the SCM Agreement. Members are also required to notify all countervailing actions taken on a semi-annual basis, and preliminary and final countervailing actions at the time they are taken. Members also are required to notify which of their authorities are competent to initiate and conduct countervailing investigations.

**Dispute Settlement**
The SCM Agreement generally relies on the dispute settlement rules of the DSU. However the Agreement contains extensive special or additional dispute settlement rules and procedures providing, inter alia, for expedited procedures, particularly in the case of prohibited subsidy allegations. It also provides special mechanisms for the gathering of information necessary to assess the existence of serious prejudice in actionable subsidy cases.

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## Understanding the WTO: The Agreements,
WTO, www.wto.org (click on 'trade topics')

The Agriculture Agreement: new rules and commitments

The objective of the Agriculture Agreement is to reform trade in the sector and to make policies more market-oriented. This would improve predictability and security for importing and exporting countries alike.

The new rules and commitments apply to:

- **market access** — various trade restrictions confronting imports
- **domestic support** — subsidies and other programmes, including those that raise or guarantee farmgate prices and farmers' incomes
- **export subsidies** and other methods used to make exports artificially competitive.

The agreement does allow governments to support their rural economies, but preferably through policies that cause less distortion to trade. It also allows some flexibility in the way commitments are implemented. Developing countries do not have to cut their subsidies or lower their tariffs as much as developed countries, and they are given extra time to complete their obligations. Least-developed countries don't have to do this at all. Special provisions deal with the interests of countries that rely on imports for their food supplies, and the concerns of least-developed economies.

"Peace" provisions within the agreement aim to reduce the likelihood of disputes or challenges on agricultural subsidies over a period of nine years, until the end of 2003.

Domestic support: some you can, some you can't
The main complaint about policies which support domestic prices, or subsidize production some other way, is that they encourage over-production. This squeezes out imports or leads to export subsidies and low-priced dumping on world markets. The Agriculture Agreement distinguishes between support programmes that stimulate production directly, and those that are considered to have no direct effect.

Domestic policies that do have a direct effect on production and trade have to be cut back. WTO members calculated how much support of this kind they were providing per year for the agricultural sector (using calculations known as "total aggregate measurement of support" or "Total AMS") in the base years of 1986-88. Developed countries agreed to reduce these figures by 20% over six years starting in 1995. Developing countries agreed to make 13% cuts over 10 years. Least-developed countries do not need to make any cuts. (This category of domestic support is sometimes called the "amber box", a reference to the amber colour of traffic lights, which means "slow down".)

Measures with minimal impact on trade can be used freely — they are in a "green box" ("green" as in traffic lights). They include government services such as research, disease control, infrastructure and food security. They also include payments made directly to farmers that do not stimulate production, such as certain forms of direct income support, assistance to help farmers restructure agriculture, and direct payments under environmental and regional assistance programmes.

Also permitted, are certain direct payments to farmers where the farmers are required to limit production (sometimes called "blue box" measures), certain government assistance programmes to encourage agricultural and rural development in developing countries, and other support on a small scale ("de minimis") when compared with the total value of the product or products supported (5% or less in the case of developed countries and 10% or less for developing countries).

Export subsidies: limits on spending and quantities
The Agriculture Agreement prohibits export subsidies on agricultural products unless the subsidies are specified in a member's lists of commitments. Where they are listed, the agreement requires WTO members to cut both the amount of money they spend on export subsidies and the quantities of exports that receive subsidies. Taking averages for 1986-90 as the base level, developed countries agreed to cut the value of export subsidies by 36% over the six years starting in 1995 (24% over 10 years for developing countries). Developed countries also agreed to reduce the quantities of subsidized exports by 21% over the six years (14% over 10 years for developing countries). Least-developed countries do not need to make any cuts.

During the six-year implementation period, developing countries are allowed, under certain conditions, subsidies to reduce the costs of marketing and transporting exports.

The least-developed and those depending on food imports
Under the Agriculture Agreement, WTO members have to reduce their subsidized exports. But some importing countries depend on supplies of cheap, subsidized food from the major industrialized nations. They include some of the poorest countries, and although their farming sectors might receive a boost from higher prices caused by reduced export subsidies, they might need temporary assistance to make the necessary adjustments to deal with higher priced imports, and eventually to export. A special ministerial decision sets out objectives, and certain measures, for the provision of food aid and aid for agricultural development. It also refers to the possibility of assistance from the International Monetary Fund and the World Bank to finance commercial food imports.

**What is a 'distortion'?**
This is a key issue. Trade is distorted if prices are higher or lower than normal, and if quantities produced, bought, and sold are also higher or lower than normal — i.e. than the levels that would usually exist in a competitive market.

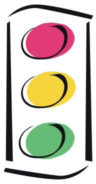
For example, import barriers and domestic subsidies can make crops more expensive on a country's internal market. The higher prices can encourage over-production. If the surplus is to be sold on world markets, where prices are lower, then export subsidies are needed. As a result, the subsidizing countries can be producing and exporting considerably more than they normally would.
Governments usually give three reasons for supporting and protecting their farmers, even if this distorts agricultural trade:

- to make sure that enough food is produced to meet the country's needs
- to shield farmers from the effects of the weather and swings in world prices
- to preserve rural society.

But the policies have often been expensive, and they have created gluts leading to export subsidy wars. Countries with less money for subsidies have suffered. The debate in the negotiations is whether these objectives can be met without distorting trade.

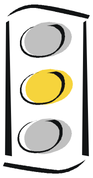
## "Domestic Support in Agriculture",

*www.wto.org*



**The Boxes**
In WTO terminology, subsidies in general are identified by "boxes" which are given the colours of traffic lights: green (permitted), amber (slow down — i.e. be reduced), red (forbidden). In agriculture, things are, as usual, more complicated. The Agriculture Agreement has no red box, although domestic support exceeding the reduction commitment levels in the amber box is prohibited; and there is a blue box for subsidies that are tied to programmes that limit production. There are also exemptions for developing countries (sometimes called an "S&D box", including provisions in Article 6.2 of the agreement).

**AMBER BOX**

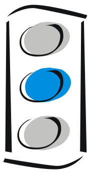


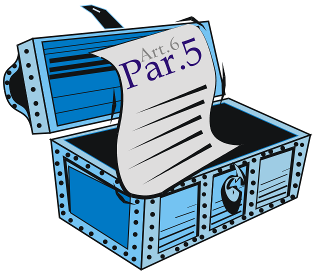

All domestic support measures considered to distort production and trade (with some exceptions) fall into the amber box, which is defined in Article 6 of the Agriculture Agreement as all domestic supports except those in the blue and green boxes. These include measures to support prices, or subsidies directly related to production quantities.

These supports are subject to limits: "de minimis" minimal supports are allowed (5% of agricultural production for developed countries, 10% for developing countries); the 30 WTO members that had larger subsidies than the de minimis levels at the beginning of the post-Uruguay Round reform period are committed to reduce these subsidies.

The reduction commitments are expressed in terms of a "Total Aggregate Measurement of Support" (Total AMS) which includes all supports for specified products together with supports that are not for specific products, in one single figure. In the current negotiations, various proposals deal with how much further these subsidies should be reduced, and whether limits should be set for specific products rather than continuing with the single overall "aggregate" limits. In the Agriculture Agreement, AMS is defined in Article 1 and Annexes 3 and 4.

**BLUE BOX**

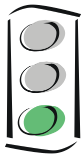





This is the "amber box with conditions" — conditions designed to reduce distortion. Any support that would normally be in the amber box, is placed in the blue box if the support also requires farmers to limit production (details set out in Paragraph 5 of Article 6 of the Agriculture Agreement).

At present there are no limits on spending on blue box subsidies. In the current negotiations, some countries want to keep the blue box as it is because they see it as a crucial means of moving away from distorting amber box subsidies without causing too much hardship. Others wanted to set limits or reduction commitments, some advocating moving these supports into the amber box.

**GREEN BOX**




The green box is defined in Annex 2 of the Agriculture Agreement.

In order to qualify, green box subsidies must not distort trade, or at most cause minimal distortion (paragraph 1). They have to be government-funded (not by charging consumers higher prices) and must not involve price support.

They tend to be programmes that are not targeted at particular products, and include direct income supports for farmers that are not related to (are "decoupled" from) current production levels or prices. They also include environmental protection and regional development programmes. "Green box" subsidies are therefore allowed without limits, provided they comply with the policy-specific criteria set out in Annex 2.

In the current negotiations, some countries argue that some of the subsidies listed in Annex 2 might not meet the criteria of the annex's first paragraph — because of the large amounts paid, or because of the nature of these subsidies, the trade distortion they cause might be more than minimal. Among the subsidies under discussion here are: direct payments to producers (paragraph 5), including decoupled income support (paragraph 6), and government financial support for income insurance and income safety-net programmes (paragraph 7), and other paragraphs. Some other countries take the opposite view — that the current criteria are adequate, and might even need to be made more flexible to take better account of non-trade concerns such as environmental protection and animal welfare.

**More**:
http://www.wto.org/english/tratop_e/agric_e/agric_e.htm
and
http://www.wto.org/english/tratop_e/agric_e/negoti_e.htm

***OECD's Producer Support Estimate and Related Indicators of Agricultural Support (The PSE Manual)***, OECD: Paris, 2010. http://www.oecd.org/tad/agricultural-policies/psemanual.htm

## Ch 2. OVERVIEW OF THE OECD INDICATORS OF AGRICULTURAL SUPPORT

2.1. Why measure agricultural support?

The OECD indicators were developed to monitor and evaluate developments in agricultural policy, to establish a common base for policy dialogue among countries, and to provide economic data to assess the effectiveness and efficiency of policies. The indicators were mandated by OECD Ministers in 1987, and have since been calculated for OECD and an increasing number of non-OECD countries, and are widely referred to in the public domain.

The objectives and priorities of agricultural policies in OECD countries encompassed over time a wide range of issues – from overcoming food shortages or surpluses in the post-war period to securing food safety, environmental quality and preservation of rural livelihoods at present. Policy instruments have been equally varied, reflecting changes in domestic political and economic settings and, progressively, developments in the international economic arena. Despite this diversity, policy measures applied in a country within a certain period of time can be brought together and expressed in one or several simple numbers – called support indicators – which are comparable across time and between countries. The utility of doing this is three-fold.

First, support indicators can be used to ***monitor and evaluate developments of agricultural policies***.[1] This includes the extent of policy reform achieved by countries, both over time and through specific reform efforts (*e.g.* the US Farm Bills and various CAP reforms), as well as progress towards achieving the commitment agreed to at the 1982 OECD Ministerial Council of reforming agricultural policies. This commitment stated that "agricultural trade should be more fully integrated within the open and multilateral trading system", and it called for OECD countries to pursue "a gradual reduction in protection and a liberalisation of trade, in which a balance should be maintained as between countries and commodities." Ministers also requested the OECD to develop a method to measure the level of protection to monitor and evaluate progress.

Closely related to this, the indicators establish a ***common base for policy dialogue*** by using a consistent and comparable method to evaluate the nature and incidence of agricultural policies. While the indicators were calculated initially for OECD countries, the analysis currently includes 43 countries (27 EU members treated as a single entity), with estimates covering the period from 1986 to the present. The international comparability of the indicators and wide country coverage makes the indicators a useful tool for policy dialogue not only amongst OECD countries, but also with non-OECD countries, inter-governmental organisations (WTO, World Bank, IMF and FAO), farming and non-government organisations, as well as research institutions.

Finally, the indicator database is used in further research on policy impacts. The data serve as an ***input into modelling*** to assess the effectiveness and efficiency of policies in delivering the outcomes for which they were designed and to understand their effects on production, trade, income, the environment, etc. While the indicators cannot by themselves quantify these impacts, the economic information upon which they are based is an important building block for further analysis.

2.2. Overview of support indicators: key terms, definitions and distinctions

- "Support" is understood as gross transfers to agriculture from consumers and taxpayers, arising from governments' policies that support agriculture.
- In addition to budgetary expenditures, support includes other estimated transfers, which do not require actual monetary disbursements (e.g., credit concessions).
- The indicators reflect the provision of support, or the level of effort made by governments, as implied by their agricultural policies. As such, they are not intended to and do not measure policy impacts on production, farm incomes, consumption, trade or environment.
- The indicators represent different ways to analyse agricultural policy transfers and measure their levels in relation to various key economic variables. Together they provide a comprehensive picture of agricultural support.
- The indicators can be distinguished according to the recipient of the transfer, the unit of measurement in which they are expressed, and the type of aggregation.

Agricultural policies may provide direct payments to farmers. They may maintain domestic agricultural prices above those at the country's border, or grant tax and credit concessions to farmers. Support is not only comprised of budgetary payments that appear in government accounts, but also includes support of market prices, as well as other concessions that do not necessarily imply actual budgetary expenditure, such as tax concessions. The common element to all these policies is that they generate transfers to agriculture.

The concept of "transfer" presumes both a source of the transfer and the existence of a recipient. In the present methodology, agriculture is generally regarded as a supported sector and the main recipient of policy transfers. Consumers of agricultural commodities and taxpayers represent the two sources of transfers, *i.e.* the economic groups bearing the cost of agricultural support. The term "agriculture" designates primary agricultural producers as an economic group. Agricultural producers are viewed from two perspectives – as individual entrepreneurs, and collectively. These distinctions underlie the key dimensions in which agricultural support is measured and the basic structure of the indicators.

The terms "support" and "policy transfers" are broadly synonymous, but may be used in different contexts. The term "support" is predominantly used to mean a "policy measure" (that generates a policy transfer) and usually appears when identifying, scoping and classifying the relevant policies. The term "policy transfer" is used mainly with respect to calculations, *i.e.* the process of obtaining numerical expressions of policies.

[1] The term "policy evaluation" is understood to be the analysis of levels and composition of agricultural support with respect to the implementation of the policy reform agenda. The term is not used as the evaluation of the effectiveness or efficiency of policies, except in the cases where the foucs is specifically on that issue.

More fundamental for understanding of the indicators, however, is the distinction between the notions of "provision of support" and the "impact of support" (*i.e.* impacts of policy transfers). The indicators are the various measures of gross policy transfers. As such, they reflect the *provision* of support, or the level of effort made by governments, as implied by their agricultural policies. The indicators do not account for the losses of that effort within the economic system, as experienced by the recipients of support. In fact, a proportion of the transfers will not end up as extra producer net income because support induces higher prices for agricultural inputs and factors, as well as generating deadweight loss of economic welfare.

Moreover, the actual impact of policies on its recipients will depend on, among other things, the basis upon which support is provided (*e.g.* whether it is provided per tonne of output, per land unit, per farm, etc.), the level of support, and the responsiveness of farmers to changes in support. The indicators, therefore, are not intended to and do not measure *the impact* of policy effort on farm production, farm incomes, trade or environment. This explanation of the indicators as representing measures of policy effort is crucial for understanding them properly.

The support indicators, which are introduced below, are different ways to analyse agricultural policy transfers and measure their levels in relation to various key economic variables. The names, abbreviations and definitions of the indicators are listed in the box below. No single indicator can capture all aspects of agricultural support. Each serves a purpose, highlighting a dimension of the support framework. The indicators are interlinked and mutually reinforcing. When analysed together, they provide a comprehensive picture of the level and composition of support.

Three distinctions can be made between the indicators. The first relates to the *intended recipient* of the transfer – producers individually, producers collectively, or consumers, although agriculture is always understood to be the economic sector supported by the policies.

A second distinction can be made in relation to the *unit of measurement*. An indicators is expressed in *monetary* terms, as *percentages* or as or *ratios*. An advantage of monetary indicators is that they can be used to analyse the composition of support, *e.g.* to calculate the shares of PSE or GSSE by policy category, or the shares of TSE according to whether the transfers come from consumers or taxpayers. However, the monetary indicators are influenced by the size and structure of the country's agricultural sector, as well as the country's rate of inflation. Consequently, there are difficulties in using them to compare support levels between countries, to evaluate changes over time, or to assess the level of support provided within a country to different commodities. In contrast, percentage indicators and ratios, which relate policy transfers to some other monetary base, *e.g.* the value of agricultural production, allow such comparisons to be made.

Finally, the indicators can be distinguished according to the *type of aggregation* at which they can be derived — across commodities or geographically. While all the indicators can be calculated at the national and multi-country level, some can also be calculated for individual commodities or for groups of commodities.

Names and definitions of the OECD indicators of agricultural support

1. Indicators of support to producers

*Producer Support Estimate (PSE):* the annual monetary value of gross transfers from consumers and taxpayers to agricultural producers, measured at the farm-gate level, arising from policy measures that support agriculture, regardless of their nature, objectives or impacts on farm production or income. The PSE in percentage terms (%PSE) is the PSE as a share of gross farm receipts (inclusive of support). The PSE is the most widely reported support measure. (Other support measures are not provided in this summary.)

2. Indicators of support for general services in agriculture

General Services Support Estimate: the annual monetary value of gross transfers to general services provided to agricultural producers collectively (such as research, development, training, inspection, marketing and promotion), arising from policy measures that support agriculture regardless of their nature, objectives and impacts on farm production, income, or consumption. The GSSE does not include any transfers to individual producers. It is also measured as a share of GDP.

3. Indicators of support to consumers

*Consumer Support Estimate (CSE):* the annual monetary value of gross transfers from (to) consumers of agricultural commodities, measured at the farm gate level, arising from policy measures that support agriculture, regardless of their nature, objectives or impacts on consumption of farm products. It is also measured as a share of consumption expenditure (measured at farm gate) net of taxpayer transfers to consumers. (There are other measures of support to consumers that are not provided in this summary.)

4. Indicators of total support to agriculture

*Total Support Estimate (TSE):* the annual monetary value of all gross transfers from taxpayers and consumers arising from policy measures that support agriculture, net of associated budgetary receipts, regardless of their objectives and impacts on farm production and income, or consumption of farm products. TSE is also measured as a share of GDP.

## 2.3. Basic principles of measuring support

Several key principles determine the scope and policy measures to be considered in the estimation of agricultural support and the method for measuring support, such as:

- A policy measure is included if it generates transfers to agricultural producers, regardless of the nature, objectives or impacts of the policy measure;
- Transfers are measured in gross terms, taking no account of adjustments which producers may make to receive the support, e.g., to meet compliance conditions;
- Transfers to individual producers are measured at the farm gate level.

A number of principles, or general rules, guide the measurement of agricultural support. Principles 1 to 3 determine the scope of policy measures to be considered in estimating agricultural support and provide criteria for identifying agricultural policies in a complex mix of government actions. Principles 4 and 6 help to define the method for measuring support and are important for interpreting the indicators.

*Principle 1: generation of transfers to agricultural producers as a key criterion for inclusion of policy in the measurement of support*. Policy measures generate explicit or implicit transfers to supported individuals or groups. A policy measure is considered for measurement if agricultural producers, individually or collectively, are the only, or the principal, intended recipients of economic transfers generated by it. This is sufficient criterion for inclusion of a policy measure in the estimation of agricultural support.

*Principle 2: there is no consideration of the nature, objectives or economic impacts of a policy measure* beyond an ―accounting‖ for transfers. This principle complements principle 1, in that the stated objectives, or perceived economic impacts of a policy measure, are not used as alternative or additional criteria to determine the inclusion or exclusion of a policy measure in the estimation of agricultural support.

*Principle 3: general policy measures available throughout the entire economy are not considered in the estimation of agricultural support*, even if such measures create policy transfers to/from the agriculture [i.e., only partial equilibrium analysis is considered]. Thus, a situation of zero support to agriculture would occur when there are only general economy-wide policies in place with no policies specifically altering the economic conditions for agriculture.

*Principle 4: transfers generated by agricultural policies are measured in gross terms.* Policy transfers can be defined in gross or net terms, *i.e.* as revenue (gross receipts) or income (revenue less costs) generated by a policy measure. The phrase *gross transfers* in the definitions emphasises that no adjustment is made in the indicators for costs incurred by producers in order to receive the support, *e.g.* costs to meet compliance conditions attached to certain payments, or tax clawbacks.

*Principle 5: policy transfers to individual producers are measured at the farm gate level*, which follows from the objective to measure support only to primary producers of agricultural commodities. Consequently, the word "*consumer"* in the definitions and methodology is understood as a first-stage buyer of agricultural commodities.

*Principle 6: policy measures supporting individual producers are classified according to implementation criteria*, such as: (i) the basis upon which support is provided (a unit of output, an animal head, a land unit, etc.); (ii) whether support is based on current or non-current production parameters; and (iii) whether production is required to receive support or not; and other criteria. These policy characteristics affect producer behaviour, and distinguishing policies according to implementation criteria enables further analysis of policy impacts on, for example, production, trade, income, and the environment.

Annex 2.1. A Short History of the Indicators

The widespread policy goal from the late 1940s to produce more food led to increasing concern about the effects of agricultural policies on trade relations and on the cost of policies. Combined with rapid technical progress and structural changes, trade barriers and domestic production support measures led to surpluses of farm goods, which were stocked or exported with additional subsidies. World prices for temperate-zone commodities were driven down. The costs of stock-holding and export subsidies placed heavy burdens on government budgets, consumers in countries with protected markets faced higher food bills, and competitive producers in other countries were penalised by restrictions on access to those markets. By the beginning of the 1980s, a number of OECD countries realised that action was urgently needed.

At the 1982 OECD Ministerial Council (consisting of Ministers of Economics, Trade and Foreign Affairs, plus a few Agriculture Ministers), it was agreed "that agricultural trade should be more fully integrated within the open and multilateral trading system… (and) that the desirable adjustments in domestic policies can best take place if such moves are planned and co-ordinated within a concerted multilateral approach aimed at achieving a gradual reduction in protection and a liberalisation of trade, in which a balance should be maintained as between countries and commodities." Ministers also decided that the Secretariat should "study the various possible ways in which the above aims could be achieved as a contribution to progress in strengthening co-operation on agricultural trade issues and as a contribution to the development of practical multilateral and other solutions."

An integral part of this investigation was to develop an appropriate basis for measuring agricultural subsidies. After considering the options available, the Secretariat decided to use the Producer Subsidy Equivalent (PSE), initially defined as *the payment that would be required to compensate farmers for the loss of income resulting from the removal of a given policy measure* (OECD, 1987).[2] While the PSE was at first used for modelling the effects on world commodity prices of a small reduction in agricultural subsidies, it was also recognised as a very useful tool in its own right to establish a consistent and comparative method to evaluate agricultural policies between countries.

The notion of a "subsidy equivalent" derives from the economic theory of protection developed in the 1960s to evaluate the effects of tariffs (Corden, 1971). According to this theory, the *producer subsidy equivalent of a policy measure*, whether an import tariff, export subsidy, payment per tonne or per hectare, etc., is the payment per unit of output that a government would have to pay producers to generate the same impact on production as that policy measure. (Likewise, the consumer tax equivalent is the per unit tax that a government would have to impose to generate the same impact on consumption as that policy measure.) In the early 1970s, Tim Josling had applied this concept to the empirical measurement of agricultural subsidies in work for the FAO, introducing the term PSE (Josling, 1973 and Josling, 1975).

In 1987, a major OECD study entitled *National Policies and Agricultural Trade* offered an in-depth analysis of the agricultural policies of individual OECD countries based largely on the PSE and related indicators. This study recognised the linkages between domestic and trade policies and concluded that in order to improve the

[2] The consumer subsidy equivalent (CSE) was defined as the "implicit tax on consumption resulting from a given policy measure (market price support element of the PSE) and any subsidies on consumption."

trading environment actions were necessary on both trade barriers and domestic policies.

It was clear from the start that the "income compensation" definition did not match what was actually being measured by the OECD PSE. While policy measures providing the same amount of *monetary* transfers to producers have the same *revenue* subsidy equivalent, they may have different production and income subsidy equivalents which depend on the way the measures are implemented (per unit of output or per hectare of land producing the same output, for example). One of the first critiques in this regard noted, *inter alia*, that the PSE was a measurement of revenue transfer (Peters, 1988).

As a result, the PSE was redefined in 1990 as *the annual monetary value of gross transfers from consumers and taxpayers to agricultural producers, measured at the farm-gate level, arising from policy measures that support agriculture, regardless of their nature, objectives or impact on farm production or income*.

Four major refinements were made in 1999:

- The PSE acronym was changed from meaning "Producer Subsidy Equivalent" to "Producer Support Estimate". It was recognised that: (a) transfers associated with a wide range of diverse policies have different "subsidy equivalents; and (b) that some of the transfers were given for the provision of services and positive externalities rather than to subsidise the production of agricultural commodities. The more neutral term "support" acknowledges that a monetary transfer is involved whatever the policy objective.
- Changes were made to the classification of policies within the PSE (Table below). This was required because of the growing scope of support policies introduced since the mid-1980s. Previously, there were five PSE categories with policies classified according to the *type* of support measure. The 1999 refinements introduced seven types of support measures with policies classified according to how they were *implemented*.
- A closely related change involved the establishment of a separate indicator to measure support provided to producers collectively, the General Services Support Estimate (GSSE). Support for "General Services" had been previously included in the PSE. This was separated from the calculation of the PSE, which now measures only support received by producers individually.

Consequently, the indicator and method for measuring the total cost to consumers and taxpayers of agricultural policies also changed, from the Total Transfers to Total Support Estimate (TSE).

- Finally, a new method for calculating the national (aggregate) PSE was introduced. Previously, this had been calculated by "extrapolating" the average %PSE for a common set of commodities to all agricultural production. A new method was introduced whereby only the average ratio of MPS to gross farm receipts for a set of commodities is extrapolated across to the rest of agricultural production (section 6.1.1), with all transfers from non-MPS policies included specifically within the PSE through classification in the appropriate categories.

Further changes were introduced in 2007 to enable the indicators to better capture recent policy developments, *e.g.* the move to ―decouple‖ the provision of support from specific commodity production and ―re-couple‖ the provision of support to other criteria. Three major changes were made:

- Although still based on implementation criteria, the PSE categories were substantially redefined.
- Labels were introduced, with the result that each policy, in addition to being classified into a PSE category, could also have up to six different labels attached to it so as to provide additional detail on implementation criteria; labels serve as shorthand for categories not included in the main presentation. For example, labels give additional information on whether a payment is with or without limit, or whether a payment implies any constraints on input use by the recipient, etc.
- PSEs for individual commodities are no longer calculated. Instead, a country total PSE is divided into Single Commodity Transfers, Group Commodity Transfers, All Commodity Transfers; and Other Transfers to Producers. This change reflects the fact that as a result of policy reform, support in many OECD countries is less tied to an individual commodity. Support is being increasingly provided to groups of commodities or all commodities in general, or without obliging a recipient to engage in commodity production at all. In this situation the link between some support transfers and individual commodities becomes less apparent. This necessitated an alternative presentation of support transfers with respect to their commodity specificity.

| Initial 1987 categories | 1999 Revision |
|---|---|
| A. Market price support<br>B. Direct payments<br>C. Reduction in input costs<br>D. General services<br>E. Other | A. Market price support<br>B. Payments based on output<br>C. Payments based on area planted/animal numbers<br>D. Payments based on historical entitlements<br>E. Payments based on input use<br>F. Payments based on input constraints<br>G. Miscellaneous |
| 2007 Revision | |
| A. Support based on commodity output<br>A1. Market price support<br>A2. Payments based on output<br>B. Payments based on input use<br>C. Payments based on current area, animal numbers, receipts or income, where production is required<br>D. Payments based on non-current area, animal numbers, receipts or income, where production is required<br>E. Payments based on non-current area, animal numbers, receipts or income, where production is not required<br>F. Payments based on non-commodity criteria<br>G. Miscellaneous | |