

# Export Competition Issues in the Doha Round

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### **Introduction**

Export competition emerged as one of the three pillars upon which agricultural trade liberalization was built in the Uruguay Round Agreement on Agriculture (URAA). This pillar not only addresses direct export subsidies, believed to be one of the most distortionary policy instruments applied to agricultural trade, but also institutional relationships under which implicit export subsidies may arise. Food aid, officially supported export credit, and exporting state trading enterprises are key institutions examined in this area. Export taxes, export promotion activities, and certain domestic policy arrangements which may be equivalent to export subsidies are also addressed in World Trade Organization (WTO) Doha Round negotiations, in a variety of venues.

### ***Unfinished Business from the URAA***

The URAA limited the use of explicit export subsidies by putting maximums on both expenditures and on the volume of agricultural exports subsidized. Expenditures were to be reduced by 36 percent from 1986–90 base year levels, and quantities subsidized were to be reduced by 21 percent, over a six-year implementation period ending in 2001. Developing countries were given 10 years to meet their reduction commitments, and all countries agreed not to introduce any new export subsidies. It is noteworthy, however, that the URAA reduced but did not eliminate direct export subsidies. Some countries have caused controversy by rolling over unused export subsidies to future periods, and occasionally commitments have been violated—usually only for one year. By and large these commitments have been met, however, and now only the European Union (EU) utilizes direct export subsidies heavily, accounting for nearly 90 percent of their use post URAA.

The agreement also recognized that officially supported export credit programs can provide a subsidy element, so WTO members were instructed to work toward disciplines in the Organization for Economic Cooperation and Development (OECD). The OECD has a long history of dealing with export credits outside agriculture, and as most members employing this institution were OECD members, this seemed a logical venue for negotiations, although some developing countries have objected to being excluded from those negotiations. The OECD negotiations failed to resolve this issue, and so export credits are now on the agenda of the Doha Round agricultural negotiations on export competition.

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The issue of state trading enterprises (STEs) was remanded to a working committee that addressed issues of reporting and definition. Reporting requirements, though comprehensive, were slow to be established, and compliance has been poor. At least one dispute involving an STE, the Canadian Dairy Board case, arose as an export subsidy issue. Issues concerning future disciplines of exporting state trading agencies are on the agenda of the Doha Round, and importing agencies are now being treated separately from exporting agencies.

URAA provisions also established that food aid may not be used as a disguised export subsidy. Concerns with potential impacts on developing countries were most evident in the Marrakesh Ministerial Decision on Measures Concerning the Possible Negative Effects of the Reform Programme on Least-Developed and Net Food-Importing Developing Countries (subsequently referred to as the Marrakesh Decision) (WTO 1999). While the food aid provisions largely confirmed the need to adhere to principles established in other venues (e.g., United Nations Food and Agriculture Organization and the Food Aid Convention of the International Grains Council), the subsequent outcome has left many donors, as well as food-insecure developing countries, dissatisfied for a variety of reasons. Food security is a concern developing countries hope to see addressed in current negotiations, and some of their implementation issues relate to developments in food aid following the URAA.

The concern with export taxes arose largely as a reaction to EU export taxes following the price run-ups of the mid 1990s, and the evident desire of the EU to export its instability in times of high as well as low world prices. Export taxes are therefore also a part of current negotiations, but were not disciplined in the URAA.

Implicit subsidies as a consequence of both domestic policy and trade facilitation are issues mostly addressed elsewhere in the URAA, as well as in Doha Round negotiations. But issues do arise when these lead to implicit export subsidies. Expiration of the peace clause could bring challenges to policies permitted under domestic support provisions of the URAA as export subsidies, most likely under the General Agreement on Tariffs and Trade (GATT) subsidies code, not the Agreement on Agriculture. Disputes based on institutions violating rules in the GATT subsidies code and/or URAA agreements raise concerns as to the adequacy of the URAA and Doha negotiating approach, and specifically as to the adequacy of export subsidy definitions.

### ***Framework for Liberalization***

The approach taken in the Uruguay Round, and subsequently adopted for the Doha Round negotiations, is to set commitments leading to reductions in (and in the Doha Round eventual elimination of) direct export subsidies. Rules are established to discipline institutions which could give rise to implicit subsidies, but those institutions are permitted to continue to exist. The challenge has been, and continues to be, writing rules that effectively prevent export subsidization and trade distortions without crippling the beneficial aspects of these institutions. This is most obvious in the case of food aid,

where rules need to insure food aid is not an indirect subsidy, and yet allows the humanitarian value of food aid to persist.

One of the lessons from the URAA has been that as institutions are disciplined, institutional innovations emerge to achieve the same or similar underlying policy objectives. Also, rules may be interpreted differently by dispute resolution panels than was the original intention of negotiators (Tarullo 2003). This can make writing rules to discipline implicit forms of subsidies difficult, as those institutional innovations and re-interpretations may have not been, and cannot be fully, anticipated by rule writers.

### ***Subsequent Use of Export Subsidies***

Following implementation of URAA commitments, and given ongoing reforms of agricultural policies in some countries, the main export competition issues are now each a one-country/region issue. In the case of direct exports subsidies, only the EU continues to use this instrument heavily. The export credit debate focuses on U.S. programs, the only ones where the subsidy component appears significant and where term lengths of loans exceed one year. State trading on the export side appears to focus mostly on the U.S. disputes with the Canadian wheat and dairy boards—concern with Australian STEs, with China’s grain exporting STE (COFCO), and with several much smaller developing country exporting boards appear less evident. Food aid debate focuses on programs run by the U.S. Department of Agriculture Foreign Agricultural Service with a market development objective, on food aid given as loans instead of grants, and on the surplus disposal motive which still seems to drive the U.S. donation levels. The export tax issue seems mostly a reaction to EU stabilization efforts of the mid 1990s.

### ***Doha Round Agricultural Negotiations***

There have been two major events relative to Doha Round negotiations on agricultural export competition—the Doha mandate issued in Qatar in November 2001 and the failed March 31, 2003 deadline to establish modalities from which countries would elaborate their offers in the agricultural negotiations. Export subsidies were a contentious issue in the Doha Ministerial debate, which some have argued almost led to failure over a few words in the Ministerial declaration. The EU objected to language explicitly calling for elimination of export subsidies, insisting on qualifying language. The reader is left to judge for himself how strongly the final brief wording, “reductions of, with a view to phasing out, all forms of export subsidies” calls for elimination of subsidies, and so who prevailed at Doha. The Doha Ministerial declaration also called for “Modalities for the further commitments, including provisions for special and differential treatment, shall be established no later than 31 March 2003. Participants shall submit their comprehensive draft Schedules based on these modalities no later than the date of the Fifth Session of the Ministerial Conference” (WTO 2001a). That Ministerial conference is scheduled for Cancun this September, and now has a busy agenda since issues left unresolved in the attempt to draft a modalities document have been pushed back onto that forum.

In an effort to meet the March 2003 deadline, a draft of a modalities agreement by Stuart Harbison, chairman of the WTO agricultural negotiating committee, was issued in March 2003 (this will be subsequently referred to as the Harbison text)(WTO 2003). That paper is clearer on points related to export competition, particularly the elimination of direct subsidies, than are position papers or the Doha declaration, providing a formula for gradual elimination of direct export subsidies over nine years. The Harbison text also offers extensive appendices on export credits, exporting state trading enterprises, and food aid, and even includes a section on banning export taxes by developed countries. While that document includes bracketed text indicating options to be decided on later by negotiation among WTO members, it does take positions on issues, such as calling for elimination, not just reduction, of direct export subsidies. It also follows the URAA approach of writing rules to discipline but not eliminate institutions which may give rise to implicit export subsidies. Harbison noted the difficulty in drafting the modalities document, and even greater difficulty in coming to agreement, due to lack of political will on the part of negotiating countries to compromise on key agricultural issues, including the export competition concerns.

### ***Doha Development Agenda***

The Doha Ministerial Declaration and subsequent negotiations are billed by the WTO as the Doha Development Agenda (WTO 2001a), highlighting the importance of developing countries in this round. Developing country concerns permeate debate, particularly in agriculture. The most evident effect is the inclusion of special and differential treatment for developing countries in each of the three pillars of agricultural negotiations, in addition to specific negotiations on special and differential treatment more generally by the WTO in a specially designated negotiating committee. Other issues, particularly related to treatment of food aid, arise from the previously cited Marrakesh Decision, and perceived broken promises leading to some of the implementation issues (e.g., commitments on guaranteed levels of food aid donations), for which there is another special negotiating committee. The Harbison text on export competition issues includes provisions for special and differential treatment of developing countries in each of the key problem areas, some of which seem not to be in the self interest of developing countries. Position papers of developing countries focus on broader food security concerns, and cut across the three pillars. These issues may not be well addressed as a consequence of following the URAA framework for liberalization, especially where concerns overlap negotiating committee jurisdictions.

### ***Surprises in Negotiating Positions***

Since the tabling of positions by 2001 (since the Doha Ministerial) debate has been more informal among WTO delegates. Relatively few new position papers have been published and available on the WTO website, and with relatively little movement or specificity in the few position papers released leading up to the March 31 deadline on a modalities document for the agricultural negotiations. There are a few mild surprises in recent positions, however, which bear analysis relative to the reasons why export subsidies persist in spite of their cost and distortionary effects. First, the EU in its most

recent position paper (European Commission 2003), offered elimination of export subsidies on some commodities where they have been heavily used, including wheat, oilseeds, olive oil, and tobacco, but not on some evidently politically more sensitive commodities, such as dairy and sugar. Second, developing countries are in principle beneficiaries of direct export subsidies, but consistently support their elimination, seemingly in contradiction of their self-interest. Third, the United States continues in its strong trade liberalization stance while making permanent domestic policy instruments (namely, marketing loans) which may implicitly violate export competition commitments, and are at least inconsistent in direction from the United States stated WTO position—calling for reduced payments to agriculture while legislation is increasing those payments in a manner which risks being in violation of existing commitments.

### ***Moving Forward***

Even though the March 31 deadline on modalities was missed, the draft Harbison text is the most explicit statement of where the WTO negotiations on export competition stand at this point. U.S. negotiators stated that this document now takes on greater importance than individual countries positions, and will serve as the basis for future negotiations as countries seek to resolve the deadlock in Cancun in September. Hence, that document will serve as the starting point for our analysis, even though negotiations centered around filling in the brackets of the Harbison text may fail, and even if that text leaves broader issues on the approach to agricultural trade reform unaddressed.

This paper proceeds first with a more detailed and comprehensive review of country positions on the several export competition issues. Since we reviewed in detail export competition issues for the IATRC in May 2001 (Young, Abbott, and Leetma 2001), our goal here is to not repeat that work in either our review of positions or our analysis of issues, but rather to complement that work by focusing on what has happened since then. We then tackle the four key export competition issues one at a time—direct export subsidies, officially supported export credit, export state trading enterprises and food aid—examining in detail the issues and existing analysis of each concern. We both critique the Harbison text positions and make recommendations based on our analysis, paying particular attention to developing country concerns in these areas.

### **Summary of Positions**

Positions taken by the major players in the Doha Round negotiations on agricultural export competition reflect usage of specific programs, hence explicit or implicit subsidies, by a country and responses by its competitors. With the expansion of membership and greater involvement of developing countries, new views beyond those of the United States, EU and Cairns group are also influencing the debate. Therefore, our review of positions on export competition will take a broader view, attempting to go beyond U.S.-EU conflict and incorporate the perspectives brought to the table by developing countries, mostly focusing on broader food security concerns.

Positions submitted by WTO members indicate a desire to discipline export subsidies in all of their forms. Norway encapsulates this general sentiment in their statement, “It should be ensured that the subsidy element of all forms of export competition measures, such as direct export subsidies, export credits, state trading export enterprises and food aid, are treated equally in the continuation of the reform process, without restricting the availability of genuine food aid in fully grant form and taking into account possible negative effects of the reform process on net-food importing developing countries.” (WTO 2001b). Other submissions reflecting this sentiment include those by the EU, Korea, India, Poland, Namibia, Egypt, Jordan, and the Cairns Group, demonstrating wide-spread support among a diverse group of members.

There is a high level of support for the reduction and eventual elimination of direct export subsidies, with differences between members on the pace and extent of reductions. The EU, the largest user of export subsidies by far, proposes a 45 percent reduction in budgetary expenditures on export subsidies (their position does not say over what period), with some flexibility to members in the pace of reductions for particular commodities. In addition, the EU agrees to eliminate the use of export subsidies on wheat, oilseeds, olive oil, and tobacco, as long as other members are not allowed to use indirect export subsidies for these products. In particular, the EU is concerned about the implicit subsidization of exports by the United States through the use of export credit guarantees and food aid.

While a few WTO members (Poland and Japan) propose to reduce but not eliminate export subsidies, far more advocate for their complete elimination (including the United States, India, and the Cairns Group). It is notable that many developing countries support the complete elimination of export subsidies and are adamant on this point. Members of the West African Monetary Union state, “It is often argued that the beneficiaries of export subsidies, which are granted mainly by developed countries, are urban consumers in developing countries, who thus have access to low-cost food products. This generally proves to be no more than a short-term benefit, for it is often eroded by balance-of-payments difficulties, so that the real beneficiaries are the producers in the developed countries, whose income levels are maintained through subsidies.” (WTO 2002a). Many developing countries (Namibia, Morocco, India, and Mali) note that they cannot afford to subsidize and thus cannot compete with developed country exports, with a detrimental impact on their agricultural exports. Mali, for example, requests the abolition of export subsidies for rice, an important agricultural export for developing countries (WTO 2001c). The WTO African group links willingness to further reduce their tariffs to “substantial progressive reduction of domestic support and export subsidies in developed countries” (WTO 2001d).

While there is wide-spread support for disciplining officially supported export credits, proposals vary in term of the timing, severity, and details of proposed disciplines. The EU desires strict disciplines on export credits in return for reductions in its use of direct export subsidies, and has proposed that officially supported export credits be bound and reduced over time at the same percentages established for direct export subsidies. The EU proposal is by far the most comprehensive submission on export credits and

details proposed terms and conditions. The United States, the dominant user of export credits, lists the programs and terms to be disciplined, but does not offer specific proposals to do so. A group of members including MERCOSUR, Bolivia, Chile, Costa Rica, Guatemala, India, and Malaysia argue that the WTO is the appropriate forum for the negotiation of export credits. Their concern is likely prompted by the URAA, which remanded the negotiations to the OECD, thus excluding many WTO members who have a stake in rules on export credits. Their proposal also requests development of a definition of officially supported export credits and criteria for identification of relevant programs, and provides a long list of credit terms to be disciplined. This proposal details the need for a minimum interest rate that would address the needs of developing countries, and special and differential treatment for developing country members. Turkey notes that use of officially supported export credits by developed countries brings about effects similar to that of direct export subsidies. Those market consequences have motivated developing country support for disciplines on export credit (including the African Group). Notably absent from developing country proposals is recognition of the role that export credit can play in promoting the food security of NFIDCs by removing liquidity constraints that might restrict their ability to import.

Members propose wide-ranging approaches to disciplining export state trading enterprises. The EU wants disciplines to eliminate potential STE behaviors including cross subsidization, price pooling, and a prohibition of exporting at less than the price paid for the product. However, the only action proposed is increased notification requirements for acquisition costs and export pricing. Increased notification requirements are also sought by the United States, Korea and Japan, with the United States seeking reporting of transactions level data. In addition, the United States proposes eliminating STEs monopoly right to export. Both Japan and the United States seek to eliminate any special financing privileges possessed by STEs. Japan proposes that exporting STEs be required to hold stocks to stabilize the international market. Mexico, and a joint submission by MERCOSUR countries, Chile and Columbia support disciplines on sole STE exporters but do not provide details. Positions favoring STEs include submissions by Mali and Mauritius, who favor maintenance of the right of LDCs to use STEs for exports. Notably absent from the discussion of STEs is the CAIRNS group, as several of its members, including Australia, Canada, and New Zealand maintain monopoly STE exporters. China also maintains an important export STE but acceded to the WTO after the submission of position papers.

Food security, rather than food aid, is a dominant theme in both developing and developed country proposals. However, views vary widely on the role of the WTO in providing assistance to food insecure developing countries over the next few years and on how to increase the food security of developing countries over the long run. The EU seeks disciplines to ensure that food aid is provided to “well-defined vulnerable groups and in response to well-recognized emergencies” to achieve the goal of preventing the use of food aid as an implicit export subsidy, particularly by the United States. In addition the EU advocates for food aid only in grant form, a position mentioned by several developing country submissions. The United States has contributed little on food aid and left it entirely out of its latest submission (USDA 2002).

Developing-country proposals show a high level of dissatisfaction over lack of commitment to address their food security needs and inadequate WTO action to date to implement the Marrakesh Decision. In fact, the African Group proposed to make the implementation of this decision a binding WTO commitment. Most developing country proposals recognize that increasing their food security requires a comprehensive approach to increasing their agricultural production and capacity to export, and so did not focus on food aid specifically. Developing country proposals that did mention food aid indicated that both the reliability and level of food aid has not been adequate to meet their food security needs, and in response, Nigeria proposed increased commitments for food aid by developed countries. Reflecting general dissatisfaction with food aid, Egypt proposed a food financing facility that would assist developing countries that are constrained in their ability to import food requirements. These countries would receive a rebate from a revolving fund after purchasing their requirements on the world market. This proposal gained support from 16 developing nations.<sup>2</sup>

Overall, proposals reflect increased participation of developing countries in the WTO, as 54 developing countries have become WTO members since 1995, and presently two-thirds of WTO members are developing countries. Proposals also reflect the fact that developing countries are concerned with the impact of export subsidies on their access to world markets as two-fifths (63 of 148) developing country members are net agricultural exporters (Valdés and McCalla 1999).

Proposals overall, including the attempt to move negotiations forward in the Harbison text, still focus to a large extent on trade-offs between the United States and the European Union. EU willingness to agree to severe reductions in direct export subsidies hinges on U.S. acceptance of disciplines on export credits and food aid. While the concessions by the EU are certainly more substantial in terms of the changes involved in EU domestic policy and its impact on world markets than those it desires of the United States, the trade-off appears to be of some political importance to the EU.

### **Direct Export Subsidies**

The URAA imposed reduction commitments in both value and volume terms on the use of export subsidies as one of its three pillars. Thus, policy instruments which led to domestic prices above world prices on exported commodities were disciplined by those provisions. Some policy instruments do this directly, in a transparent way, such as the EU export restitutions and payments under the U.S. Export Enhancement Program (EEP) and Dairy Export Incentive Program (DEIP). In such cases, public expenditures are required to maintain the wedge between domestic and world prices, and quantities subsidized may also be determined in a transparent manner. In other situations, such as the export credit, state trading and food aid cases, more complex, indirect, and less transparent policies give rise to implicit export subsidies, to be recognized by the relationship between domestic and world prices maintained by that institutional arrangement. When more

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<sup>2</sup> Côte d'Ivoire, Cuba, Dominican Republic, Egypt, Honduras, Jamaica, Kenya, Mauritius, Morocco, Pakistan, Senegal, Sri Lanka, St. Lucia, Trinidad and Tobago, Tunisia, and Venezuela.

complex policies evolve, the burden of the cost arising from the price wedge can be partially or fully borne by other economic actors—producers or consumers (Schluep and de Gorter 2000).

One of the tasks of the URAA was also to define export subsidies so that the more indirect institutions could be disciplined when appropriate. That definition identifies various means by which government may offer subsidies in cash, in-kind or as favorable terms, and includes them as export subsidies when they are “in law or in fact, whether wholly or as one of several other conditions, contingent upon export performance.” (WTO 1998) A debate has ensued over whether that definition is adequate to identify implicit export subsidies.

### *Use of Export Subsidies*

Currently countries notify the WTO of their use of direct, transparent export subsidies, for which there are reportable public expenditures, and for which there are reduction commitments. Implicit subsidies through other institutions, such as the estimated subsidy component of export credit or food aid, being not recognized as export subsidies by the lender/donor country, are not in those notifications.<sup>3</sup> Table 1 reports the use of direct export subsidies, based on those country notifications to the WTO, which as of the 2002 Secretariat report (WTO 2002b, WTO 2002c) included complete notifications only through 1999. In total, countries have been spending between \$6 and 7.5 billion in total per year, amounting to nearly \$33 billion between 1995 and 1999. Of that total \$29.3 billion, or 91.6 percent of export subsidies by value, are from the EU. Switzerland and Norway account for another \$1.8 billion, and the United States has only used \$487 million in direct agricultural export subsidies since 1995. Another 23 countries engage in quite small expenditures on export subsidies totaling less than \$1.5 billion over these five years. These include several developing countries, six of which (India, Korea, Morocco, Pakistan, Thailand, and Tunisia) did not establish that they were using export subsidies, and so did not make reduction commitments in the URAA. Thus, they may have violated their commitments not to initiate new export subsidies.

Table 2 documents the extent to which national commitments have been met, or violated, looking at both the value and volume commitments. The EU uses between 60 and 80 percent of its budgetary commitment and from 65 to 107 percent of its volume commitment—being beyond its volume commitment in one year, and never in total above its value commitment. Columbia is often near its volume commitment, but is spending only 15–20 percent of its budgetary commitment. In 1999 the United States exceed both its value and volume commitments, as did Norway. Other violations of aggregate export subsidy commitments are extremely rare according to country notifications. Where there have been violations, technicalities such as claiming credit for unused earlier subsidies have been invoked, and subsequently violations seldom persist.

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<sup>3</sup> There are separate notification requirements for state trading enterprises, and proposals for notifications of food aid and export credit activities.

Thus, by and large countries have honored at least the letter of this law, and to a large extent its spirit, as well.

TABLE 1. Export Subsidy Use (US\$ million)

	1995	1996	1997	1998	1999	2000	Total
<i>Members with export subsidy reduction commitments</i>							
Australia	0	0	0	1	2	0	3
Canada	38	4	0	0	-	-	42
Colombia	18	22	25	23	0	0	88
Costa Rica	0	0	105	123	20	-	248
Cyprus	3	3	2	4	0	-	12
Czech Republic	40	42	40	42	35	24	223
EC	6,292	6,684	4,915	5,835	5,588	-	29,314
Hungary	41	18	10	12	13	-	94
Iceland	6	1	0	0	0	-	7
Israel	19	13	6	1	1	0	40
Mexico	0	0	36	4	-	-	40
Norway	83	78	102	77	128	-	468
Poland	0	16	9	14	55	36	130
Romania	0	0	0	2	7	-	9
Slovak Republic	8	8	13	12	12	12	65
South Africa	40	42	18	3	5	3	111
Switzerland-Liecht.	447	369	295	292	-	-	1,403
Turkey	30	17	39	29	28	27	170
United States	26	122	112	147	80	-	487
Venezuela	3	20	2	5	-	-	30
Total	7,094	7,459	5,729	6,626	5,974	102	32,984
<i>Members without export subsidy reduction commitments</i>							
India	-	2	4	2	2	1	11
Korea	2	3	3	3	12	-	23
Morocco	1	-	1	1	0.4	-	3.4
Pakistan	0	2	2	3	0.4	-	7.4
Thailand	15	6	5	0	0	0	26
Tunisia	0	2	5	6	6	6	25
Total	18	13	16	13	18.8	6	84.8

Source: WTO, TN/AG/S/1, 2002c

Table 3 presents use of export subsidies by commodity for all countries, the EU and the United States. Grains dominate in volume exported, whereas dairy accounts for a large fraction of the value of export subsidy expenditures. Policy reforms and political sensitivities explain this commodity pattern of subsidy use.

The need for countries to use export subsidies has been influenced by both economic and political factors. Agricultural policy reforms in the United States and EU have both led to lower export subsidy expenditures, by decoupling some policy instruments in the United States as a result of the 1996 farm bill, and by lowering intervention prices in the EU due to Agenda 2000 reforms. Decisions taken in December to accommodate accession of Eastern European countries also have implications for future (lower) export subsidy costs as EU domestic agricultural policies have been altered. High world prices in the mid 1990s led to much lower usage of subsidies then, and even export taxes to stabilize EU domestic grain prices in 1995–96. In addition, the strengthening of the dollar relative to the (weak) Euro has lessened the need for EU subsidies after 1999.

TABLE 2. Percent Use of Value and Volume Commitments, 1995–2000<sup>1</sup>

Member	1995		1996		1997		1998		1999		2000	
	% of budget comm.	% of volume comm.	% of budget comm.	% of volume comm.	% of budget comm.	% of volume comm.	% of budget comm.	% of volume comm.	% of budget comm.	% of volume comm.	% of budget comm.	% of volume comm.
Australia	0	0	0	0	0	0	6	3	12	4	0	0
Brazil	0	0	0	0	0	0	0	0				
Bulgaria	n.r.	n.r.	n.r.	n.r.	0	0	0	0	0	0		
Canada	59	58	8	5	0	0	0	0	0	101		
Colombia	15	59	20	76	17	125	22	152	0	0	0	0
Cyprus	164	86	50	44	46	129	75	98				
Czech Republic	28	51	32	34	38	34	38	33	53	47	31	50
European Communities	54	65	61	85	51	82	69	91	82	107	50	74
Hungary	58	23	31	22	20	18	73	21	114	37		
Iceland	26	61	4	10	1	1	0	0	0	0		
Indonesia	0	0	0	0	0	0	0	0	0	0	0	0
Israel	44	69	31	63	13	20	9	15	13	33	0	0
Mexico	0	0	0	0	3	17	14	60				
New Zealand	0.01	n.r.	0	n.r.	0	n.r.	0	n.r.	0	n.r.		
Norway	68	69	44	45	83	94	65	78	184	170		
Panama	n.r.	n.r.	n.r.	n.r.		n.r.		n.r.		n.r.		
Poland	0.2	1	36	116	21	149	21	63	95	103	42	66
Romania	0	0	0	0	0	0	4	48	6	32		
Slovak Republic	12	32	23	28	32	56	29	56	46	71	54	62
South Africa	15	15	51	52	35	45	28	3	48	4	39	2
Switzerland-Liechten.	70	81	73	81	45	34	65	55				
Turkey	47	71	92	89	71	72	66	70	61	71	70	72
Uruguay	0	0	0	0	0	0	0	0	0	0		
United States	22	35	56	50	50	70	74	73	185	199		
Venezuela	19	37	49	29	11	25	33	47				

<sup>1</sup>Simple average use of export subsidy commitment levels across all relevant product groups in percent (excluding zero-use notifications).

Source: WTO, TN/AG/S/8, 2002b

TABLE 3. Export Subsidy Notifications by Commodity

Product	All WTO Members				European Community								United States				
	1999		2000		1999				2000				1999		2000		
	Volume	% comm.	Volume	% comm.	Volume	% comm.	Value	% comm.	Volume	% comm.	Value	% comm.	Volume	% comm.	Value	% comm.	Volume
Wheat and wheat flour	15,606	44%	10,204	62%	15,606	100%	509	34%	10,204	71%	108	8%	0	0	0	0	0
Coarse grains	19,226	96%	737	6%	18,379	161%	730	63%	7,080	65%	192	18%	0	0	0	0	0
Rice	140	25%	132	31%	140	101%	26	65%	132	99%	32	88%	0	0	0	0	0
Oilseeds	0		27	6%	0		0		0		0		0	0	0	0	0
Vegetable oils	50	5%	10	3%	0		0		0		0		0	0	0	0	0
Oilcakes	0		0														
Sugar	1,107	42%	1,001	43%	971	73%	470	86%	882	69%	373	75%					
Butter and butter oil	206	40%	197	45%	194	46%	333	32%	197	49%	338	36%	5.3	21%	7.3	22%	0
Skim milk powder	644	105%	205	44%	417	146%	338	112%	128	47%	26	9%	101.4	133%	45.3	50%	0
Cheese	349	78%	305	82%	305	89%	236	60%	305	95%	238	70%	3.9	121%	5.6	140%	0
Other milk products	1,263	101%	920	83%	1,104	110%	905	119%	873	91%	410	59%	17.9	711%	20.3	702%	0
Bovine meat	775	63%	495	51%	766	87%	726	52%	475	58%	383	31%	0		0.0		0
Pigmeat	715	122%	130	28%	694	150%	243	115%	129	29%	34	18%	0		0.0		0
Poultry meat	336	50%	263	78%	318	101%	75	75%	261	91%	57	63%	2.5	9%	1.6	0.1%	0
Sheepmeat	0	1%	0														
Live animals	9	6%											0		0		0
Eggs	102	94%	84	83%	101	97%	14	30%	84	85%	8	19%	0		0		0
Wine	1	0%	0		2	99%	26	61%	2	99%	24	60%					
Fruit and vegetables	1,103	18%	1,145	21%	981	105%	43	64%	815	91%	31	51%					
Tobacco	0		0		0		0		0		0						
Cotton	0		0														
Acohol					1,998	167%	219	208%	891	78%	96	99%					
Incorporated products							720	151%			414	100%					

Notes: Volumes are notified subsidized export volume in thousand metric tons.  
 Values are budgetary outlays (subsidy value) in million Euros for the European Community and \$ millions for the United States.  
 Percent of commitment is reported after both volume and value measures.  
 Zeros are shown only where there was a commitment for that commodity.

Source: WTO, TN/AG/S/8, 2002b

### *Why Export Subsidies Persist*

Export subsidies generally arise to support domestic agricultural policy regimes resulting in high (sometimes stable) domestic prices. They are typically an unwanted consequence of that domestic policy regime, and do not reflect a desire to transfer resources to foreigners. This helps to explain why export subsidies persist, particularly in their implicit forms, in spite of the criticism that they have received over the years from both academics and policymakers. One of the threads in our literature due to Anania, Bohman, and Carter (1992), is that export subsidies may be rational in the sense that they make existing domestic policy institutions less costly in meeting overall farm program objectives. While this reasoning relies on assumptions concerning inertia in domestic institutions (a very reasonable view from our perspective), it helps to explain the persistence and reluctance to eliminate this institution, unless there is radical policy reform. The evolution of the EU's Common Agricultural Policy from a revenue generating import protection scheme to one requiring export subsidies to dispose of surpluses is consistent with this view. The fact that the United States has not used EEP since 1995 is also consistent, once one recognizes that the 1996 farm bill radically reformed legislation in manner such that export subsidies were no longer required to contain program costs for most commodities (with the exception of dairy).

An understanding of the use and persistence of export subsidies is also aided by recognizing the tradeoffs between the exercise of market power in international trade (which calls for export taxes, not subsidies) and the fundamental goals of agricultural policy to redistribute income toward producers. Thus, export subsidies must be examined in a second best framework, where other distortions interacting with trade matter. Institutions may evolve to resolve this tradeoff, and so achieve a broader range of policy goals than explicit, general export subsidies could address. And limitations on the policy choice set (e.g., the United States constitutional prohibition on export taxes), as well as historical experience may dictate institutional mechanisms chosen. Targeting of direct subsidies to specific importers is an example that permits price discrimination and so implicit taxation (Abbott, Paarlberg, and Sharples 1987). This is one solution practiced explicitly by the EU, by the United States (formerly under EEP, currently with DEIP) and implicitly by state traders. State trading should be viewed as another institutional form seeking to resolve in the favor of producers the conflict between the exercise of market power and other agricultural policy goals. Even in a single country, these institutions leading to export subsidies may vary across commodities, as observed in the continued use of DEIP for dairy and marketing loans for soybeans in the United States.

Our literature has also debated the strategic value of export subsidies, albeit in a static context and has generally found it difficult to build a case for strategic interaction. However, the value of export subsidies is generally realized in a dynamic framework, as the goal of an export subsidy may be to incur cost today in order to improve market conditions in the future. Predatory pricing to exploit persistence in market share would be one example. Lags in supply response may also condition the dynamic costs and benefits of subsidies. Recent efforts to build export capacity in developing countries is another example, arising from examining the successful use of export subsidies outside

agriculture by the Asian Miracle countries. The fact that export subsidies may reduce stocks, particularly those held by government, is another argument for dynamic analysis of subsidies. In fact, it may often be the case that countries consider stockholding, not lower producer prices, as the alternative to export subsidies.

### ***Country Positions Revisited***

As noted earlier, country positions on direct export subsidies are straightforward and follow from practice in their use since 1995. We believe that both those positions, and persistent use of export subsidies, reflect countries' desires to achieve broad agricultural policy goals in a dynamic and uncertain market, and with political inertia in institutional reform. Thus, the United States, the Cairns group, and developing countries have advocated elimination of direct export subsidies, while the EU, who continues to use such instruments heavily, seeks reduction but not necessarily elimination.

We also noted earlier that there are two mild curiosities evident in the stated positions related to direct export subsidies. First, the EU has indicated a willingness to eliminate, and reduce earlier, subsidies on wheat, oilseeds, olive oil, and tobacco, while reducing slowly (but not eliminating) more politically sensitive subsidies for meat, dairy, and sugar. We hypothesize that the EU has already done the hard work of reforming policy institutions for the commodities where subsidies are to be given up, since these are the commodities for which budgetary costs would have become prohibitive when the EU expands to include Eastern Europe. Where Eastern European accession brought less pressure for reform, institutions have not been as dramatically altered, and so institutional inertia to maintain existing policy instruments persists.

The second curiosity is that food importing developing countries, which are in principle beneficiaries of export subsidies, support their elimination in apparent conflict with their own self interest. But export subsidies make domestic agricultural programs in developing countries more expensive. Developing countries are concerned because they perceive benefits from cheaper imports are small, and because many of them are significant agricultural exporters as well as importers, and so are concerned about the consequences of low and variable world prices. Moreover, import subsidies are received only when world prices are low—not when they are really needed to lower import costs at times of high world prices. EU use of export subsidies transfers the EU's domestic market instability to world markets, and puts a greater burden on developing countries to adjust to unstable world market conditions, at a time when commitments under the WTO, bilateral trade agreements, and structural adjustment programs have stripped them of policies to cope with world market instability.

### ***Incidence of Subsidy Costs and Benefits***

A two-panel diagram can help to explain the incidence of export subsidy costs and benefits. It illustrates the tradeoff between achieving farm policy objectives versus exercising market power in trade, and shows how the extent of benefit accruing to importers depends on the extent of that market power, which both the EU and developing

countries may see as small. Figure 1 presents two such two-panel diagrams—the first is the normal case, demonstrating the potentially high cost of export subsidies to a large country exporter, while the second illustrates some extreme assumptions about elasticities. Interpretation of the second diagram suggests why the cost of export subsidies is perceived as low by the EU, given their domestic policy objectives. It also illustrates why developing countries perceive the benefits they realize from such subsidies as being low as well.

The upper two-panel diagram of Figure 1 presents a typical export subsidy incidence calculation for a large exporting country. The change in world price from free trade depends on the magnitude of the subsidy, and also the slope of the exporting country's net export supply function relative to the slope of the net import demand function that country faces. With similar slopes, the increase in price to the exporter about equals the fall in price to the importers (which is the subsidy accruing to foreigners), whereas in the lower diagram the very elastic world market means virtually all of the subsidy goes to domestic agents in the exporting country. The Harberger triangles represent inefficiency losses from misallocated resources as a consequence of the subsidy to domestic agents, and are typically small relative to the redistributions the subsidy brings about. Export subsidies are typically very costly for large exporters, where a substantial fraction of the benefit goes to foreigners. This effect is much greater than the inefficiency effects. All these costs are incurred to achieve increased producer benefits, which the lower panel shows will be larger relative to subsidy costs when the exporter is nearly self-sufficient in the commodity subsidized.

In the case of EU subsidies, policy makers there are likely to argue that the lower diagram is more typical of situations they face, with very low short run elasticities in the domestic market, and facing elastic net import demand. The world market elasticity, it should be remembered, is the net of both importer price responsiveness and the responses to price of competing exporters, so depends on the U.S. response to forces or strategies which might otherwise lower world prices. Dynamic effects complicate assessment of long-run costs and benefits, and do not simply mean larger long-run elasticities mean larger Harberger triangles, especially if world prices are expected to rise in future years. Evidence consistent with this is that subsidies are only used when world prices are low, and have become taxes when world prices are high.

### ***Developing Countries, Subsidies, and Export Taxes***

In the case of typical developing country exporters, market power is small, and where it is not, export taxes are more prevalent. Thus, for them the tradeoffs between producer benefit under domestic policies is weighed against the small inefficiencies captured in the Harberger triangles (and the small portion of the subsidy accruing to foreigners). But where policy instruments do not yet exist, better alternatives than export subsidization probably can be found to implement domestic agricultural policy in developing countries.

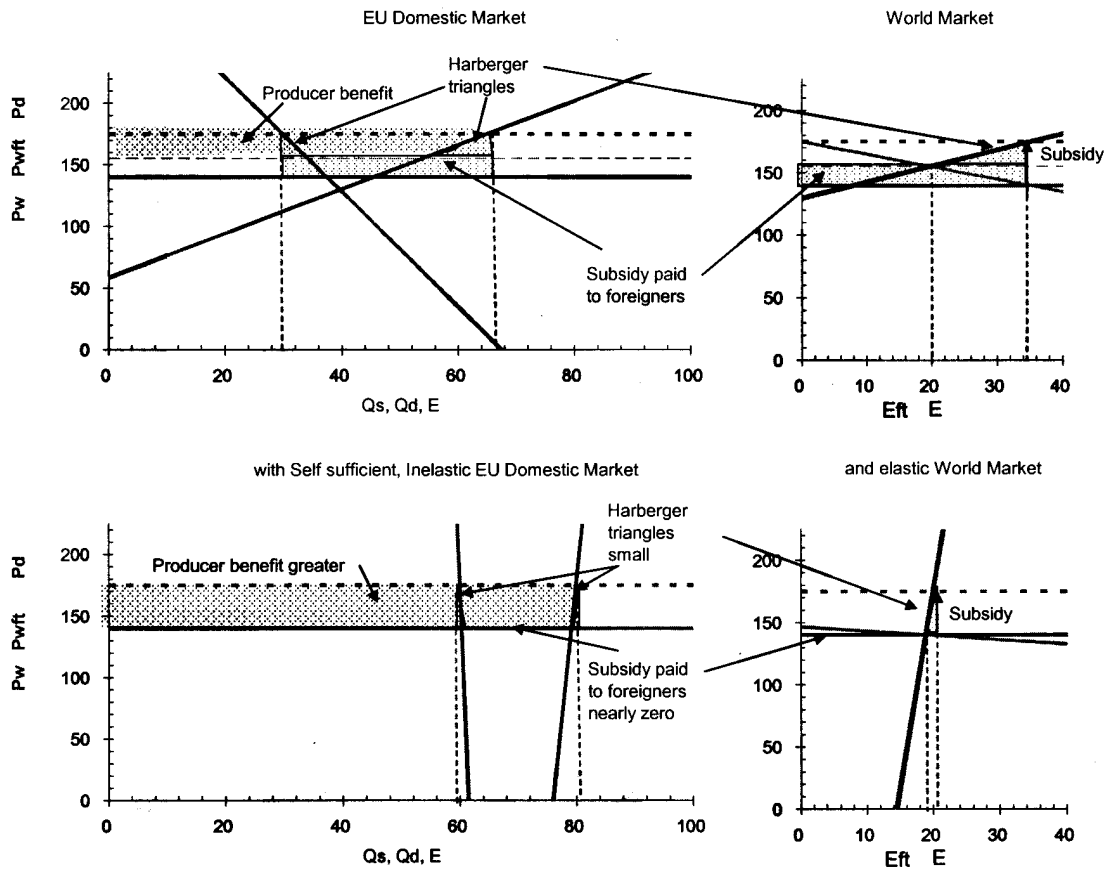


FIGURE 1. EU Export Subsidy Incidence

The Harbinson text does not address well the broad food security concerns of developing countries. The URAA and structural adjustment have stripped developing countries of agricultural policy instruments to establish safety nets for their agricultural producers, a concern which remains evident also in developed countries. WTO initiatives on permitted agricultural policy instruments need to take a more dynamic perspective on market adjustments, addressing concerns of instability and agricultural policies to cope with market variability

The export tax issue highlights the concern with instability—both the extent to which export policy can be used by a country to export its instability onto world markets, and the concern that policies include export subsidies, at least implicitly because wedges are desired between domestic prices and unstable world prices. In light of this analysis, the most surprising country position is the EU's apparent willingness to give up some of its export subsidies. It is less surprising that developing countries are seeking special and differential treatment to continue to use these instruments for as long as possible.

### ***Harbison Modalities Proposal***

The Harbison text is clear on the future of export subsidies—they are to be eliminated over nine years. Several formulae are proposed for gradual reduction, with a significant down payment in the form of immediate subsidy reductions (bracketed at 30 percent). That proposal also calls for faster elimination of some subsidies—5 years for 50 percent of products subsidized. Special and differential treatment is offered to developing countries in the form of slower elimination, over 11 to 13 years, and with exemptions for marketing costs and transport subsidies that had been granted in the URAA. It does not, however, lift the prohibition on new export subsidies—a provision which in a few instances developing countries have violated. All specifics are in bracketed text, to be negotiated, but the important element of this proposal is that it calls for eventual subsidy elimination, not just reduction.

The Harbison text does not deal with several of the technical issues that arose in implementation of URAA commitments. It does not address rollover of unused subsidy commitments, specific levels of commodity aggregation, or the practice of using subsidies for products where the allowed subsidy commitment is for an intermediate input. Each of these has been used to justify temporary potential violations of commitments. These are examples of the difficulty in writing rules and allowing countries to follow the letter but not spirit of their commitments. Disputes, generally informal, have arisen in each case about whether past commitments are being honored. But in the end, these are just details on how fast reform occurs or what is the true extent of a commitment. They become much less important if subsidies are ultimately to become zero.

The Harbison text also does not directly address the issue of reduction commitments being expressed in both quantity and value terms. Proposed reduction schedules apply equally to existing quantity and value commitments. The quantity commitment can limit subsidies in times of high as well as low world prices, but is more binding on certain instruments, making general subsidies difficult to implement when export volumes would be large. Thus, in principle they could lead to faster reform of certain subsidy instruments. But the common practice of targeting subsidies to specific importers can mitigate the constraint quantity limits impose on export subsidization.

### ***New Export Subsidy Mechanisms in Domestic Agricultural Programs***

New policy mechanisms may give rise to instruments that could be subject to the reduction commitments on export subsidies, but now are addressed only in the domestic support pillar. For example, a recent complaint pressed by Brazil against the U.S. programs that subsidize upland cotton illustrates the difficulty in separating domestic and export subsidies (Bureau of National Affairs 2003). Brazil states that the combination of U.S. programs, including marketing loans, export credits and commodity certificates, have spurred U.S. cotton production and exports. The Brazilian complaint states that U.S. subsidized exports have increased to the extent that world prices have been depressed and the Brazilian industry has suffered injury. The legitimacy of this complaint due to

limitations imposed by the Peace Clause is unclear (U.S. Mission Geneva 2003), but is immaterial to our point, which is that there is a strong link between domestic programs and export subsidization. Such issues may be missed by following the three pillars approach, and targeting unfinished business from the URAA.

### ***Recommendations***

Recommendations on direct export subsidies are simpler than will be the case for the implicit subsidy institutions. We applaud both the notion that direct export subsidies should be eliminated, as embodied in the Harbison proposal, and that countries are given sufficient time to evolve to new institutional mechanisms which achieve domestic policy objectives without exporting a country's instability onto world markets. While a slower pace may be called for in developing countries, better institutional mechanisms than export subsidies should be encouraged under special and differential treatment to achieve food security goals. The failure of the Harbison text, evident here and more evident for implicit subsidy institutions, is that it focuses on disciplining problem areas of developed country trade, and does not come to grips with the broader food security concerns of developing countries. In the cases of indirect subsidies, where we turn next, the problems with meeting broad food security concerns of developing countries become more acute.

### **Officially Supported Export Credit**

Export credit is addressed in the WTO agricultural negotiations on export competition because various government programs can influence or improve the terms on loans between private banks or governments of agricultural exporting countries and the importers, and are tied to agricultural export transactions. These programs include direct interest rate subsidies, insurance, credit guarantees, and involvement of government agencies in credit transactions—including state trading, food aid and government-to-government loans, and various other mechanisms such as foreign exchange hedging and refinancing. These programs are addressed in the category now labeled by the WTO as officially supported export credit. Credit guarantees on private transactions are the most prevalent form of officially supported export credit for agricultural commodities, but the other mechanisms are occasionally used.

### ***Measuring Implicit Subsidies***

Officially supported export credit results in implicit export subsidization when the terms of loans are better than would occur under private market transactions, and result in lower interest rates than would be charged to appropriately reflect the risks of those loans. The OECD (2000) has estimated the subsidy component of existing official export credit programs utilizing a methodology developed by Raynaud and Scully, and applied to agricultural trade by Hyberg et al. (1995) earlier. That methodology is based on the difference between actual interest rates charged under these programs and estimates of risk corrected market based interest rates, utilizing Moody's ratings for countries (governments) receiving the loans or the OECD Commercial Interest Reference Rates

(CIRRs). Estimating these risk premiums is problematic, since comparable short-term loans are not common (Yang and Wilson 1996) and country rates may be underestimates of the risks from these transactions, especially if importing country governments are not involved. The extent of subsidization also depends on other terms of these loans, including down payments, grace periods, term lengths, and program fees. For example, the longer the term, the greater is the subsidy component of a loan for a given effective interest rate differential or subsidy.

While this methodology gives a good first approximation of the extent of subsidization from these programs, it may not capture the very reason many of these programs exist. In some instances, importers may be unable to obtain credit at any interest rate, and so are facing “liquidity constraints.” While the subsidy component of a program could be much greater when liquidity constraints bind, establishing an equivalent risk premium in such a case is certainly not practical, and is conceptually problematic as well. But evidence suggest they may often relieve such constraints and enable credit transactions and so trade flows which would not otherwise occur. That raises another issue complicating evaluation of officially export credit programs as subsidies—the additionality of exports they may bring about, so that these subsidies may expand imports of a commodity, benefiting all exporters.

Additionality is a reason not to analyze the market effects of these programs by treating the subsidy component as equivalent to an equal value direct export subsidy (as established by Baron 1983). More importantly, if these act like income subsidies rather than as price subsidies, world demand for the commodity is expanded, and additional imports arise, so that costs to other exporters may not occur. Tying trade flows to these credit transactions does capture market share, so that costs to exporters depends on how differentiated or competitive one sees the determination of market share. In any case the potential trade distortions accruing to other exporters from these subsidies are likely to be small.

### ***Use of Officially Supported Export Credit***

The best evidence on practice and subsidization under these programs is from the OECD study cited above. According to that study, \$6–8 billion dollars per year of agricultural exports benefit from official credit programs. Almost half of that is from agricultural exports from the United States, with the EU, Canada, and Australia accounting for about equal shares of nearly all of the rest (see Table 4). The OECD report (and Table 4) also show that virtually all (generally greater than 96 percent) of officially supported export credit transactions of a term length longer than one year come from the United States. The extent of use of these programs varies somewhat with market conditions, and the Asian financial crisis stimulating much greater use in 1997–98. A surprisingly small fraction of these transactions involve developing country importers, and particularly least developed countries (LDCs) or Net Food Importing Developing Countries (NFIDCs). The fraction of U.S. exports benefiting from officially supported credit programs that are going to LDCs and NFIDCs is typically 20 percent, the highest

share among exporters. The EU fraction increased to 13 percent during the Asian financial crisis.

TABLE 4. Officially Supported Export Credits in Agriculture

	----- 1995 -----		----- 1996 -----		----- 1997 -----		----- 1998 -----	
<i>Value of exports benefiting from official credit – \$ millions, % of total exports</i>								
United States	2,843	4.7%	3,188	4.9%	2,845	4.6%	3,929	6.8%
EU	985	1.7%	989	1.7%	1,151	1.9%	1,254	2.2%
Canada	570	3.8%	697	4.2%	1,239	6.8%	1,108	6.3%
Australia	1,106	10.5%	2,014	17.8%	2,130	16.9%	1,553	14.9%
Rest of World	0	0.0%	71	0.7%	58	0.7%	66	0.7%
Total	5,504	3.6%	6,959	4.3%	7,423	4.6%	7,910	5.2%
<i>Exports benefiting from long-term credit (one-year term or more) – \$ millions, % of exports under credit</i>								
United States	2,487	87.5%	3,066	96.2%	2,758	96.9%	3,785	96.3%
EU	40	4.1%	15	1.5%	118	10.3%	113	9.0%
Canada	23	4.0%	0	0.0%	39	3.1%	37	3.3%
Australia	0	0.0%	0	0.0%	0	0.0%	0	0.0%
Rest of World	0	0.0%	0	0.0%	4	6.9%	9	13.6%
<i>Exports to LLDCs and NFIDCs – \$ millions, % of exports benefiting from credit</i>								
United States	633.1	22.3%	666.0	20.9%	560.7	19.7%	361.1	9.2%
EU	48.4	4.9%	39.8	4.0%	150.2	13.0%	174.2	13.9%
Canada	26.1	4.6%	1.3	0.2%	39.7	3.2%	37.5	3.4%
Australia	31.1	2.8%	46.5	2.3%	60.3	2.8%	52.9	3.4%
Rest of World	0		0		0		0	
<i>Subsidy element estimates – \$ millions, % of export value</i>								
United States							258.0	6.6%
EU							23.6	1.9%
Canada							13.6	1.2%
Australia							5.1	0.3%
Rest of World							0.2	0.3%

Source: OECD, 2000

The most surprising result of the OECD study is the small subsidy component from these transactions. The longer-term U.S. programs resulted in a subsidy component of 6.6 percent in 1998, with even lower subsidy components for loans from the EU (at 1.9 percent), Canada (at 1.2 percent), and Australia (at 0.3 percent). We suggest as a hypothesis that these programs exist but offer no apparent subsidy because they are effectively breaking liquidity constraints. Otherwise these programs would not be so popular, and there would be little reason for government involvement in private transactions. That their use expanded with the Asian financial crisis and enabled then both credit and trade flows that would not otherwise have occurred is also consistent with the liquidity constraint hypothesis, and is supported in popular press reports. The U.S. General Accounting Office (1992) used a very different methodology to assess agricultural credit guarantee programs, and found a subsidy component based on expenditures to cover losses from defaults at 9 percent. That at least suggests that interest rate premiums determined by the OECD methodology are underestimates of underlying risk, and we believe is further indirect evidence of these programs relieving liquidity constraints. Hence, it is not surprising that subsidy components seem low, but the agricultural trade and especially financial interests are strong proponents of these programs.

The OECD study also argues that the justification for these programs as tools to benefit developing countries is weak, based on the small fraction of transactions involving LDCs and NFDCs. But elimination of these programs could put at risk over \$500 million in imports by those countries, especially if liquidity constraints matter. And exports during the Asian financial crisis very likely would not have occurred, consistent with the notion of additionality due to export credit programs. Should these programs be eliminated, finding vehicles for expanded credit at times of such crises would be difficult.

### ***URAA Outcome and Afterwards***

The approach taken in the URAA recognized the potential for officially supported export credits to act as implicit export subsidies, but did not eliminate them. The issue of appropriate disciplines was remanded to negotiations under OECD auspices, who has a history of successfully dealing with non-agricultural export credit programs. It appeared that the OECD negotiations would focus on limiting term lengths of these programs to one year or less, thus limiting but not eliminating the subsidy component of these programs. Negotiations broke down at the end of 2000 over the treatment of credit transactions by state traders. Some interests, particularly in developing countries, also felt that these negotiations were better placed in the WTO where there would be broader participation.

The export credit issue was also raised in the Marrakesh Decision, asking that appropriate provisions be included for special and differential treatment in favor of LDCs and NFDCs. Export credit issues are among the implementation concerns of developing countries, and in particular those countries have proposed a WTO sanctioned Food Financing Facility to cope with developing country credit concerns.

With the failure of the OECD negotiations, and from the implementation concerns of developing countries, export credits have become one of the elements of Doha Round agricultural negotiations under export competition. The EU is most explicit in its position, calling for comprehensive treatment of export subsidies, including export credit. The export credit issue is largely seen as a U.S. problem, where the bulk of existing subsidies arise, but the extent of that subsidization measured in value terms is much less than the extent of direct export subsidies, certainly by the EU and possibly even in the United States.

### ***The Harbison Proposal on Export Credit***

The Harbison proposal on modalities included a rather long appendix on rules for disciplining export credit programs consistent with the URAA approach of disciplining, but not eliminating or even reducing the use of these programs (unless they do not conform to the rules ultimately negotiated). It follows the Scully/Hyberg/OECD methodology in seeking to reduce or eliminate the subsidy component of these programs. Interest rates would need to conform to CIRRs or other measures of market based interest rates. The draft also stipulates that interest rates and fees must fully cover the costs of these programs, including default risk guaranteed, so that the additional subsidization

found in the GAO methodology would also not arise, and so governments could not explicitly put money into these programs. Moreover, each of the elements leading to the extent of subsidization in the OECD formula—down payments, term length, payment frequency, etc.—was subjected to specific disciplines. While term lengths are brackets rather than explicit in many cases, the final general category does suggest six months rather than one year as an appropriate maximum.

The Harbison text on exporting state trading enterprises also touches on this issue, by proposing that those entities be prohibited from offering export credit programs. That proposal is strongly rejected by Canada and Australia, where the impact of that proposal would be most severe.

Special and differential treatment of developing countries comes in several forms. Longer terms for loans to developing countries are suggested as a possibility, but specifics are not spelled out. Exemptions are to be permitted in emergency situations, presumably a response to concern over the importance of these instruments during the Asian financial crisis, and their potential as a food security tool when individual country crises occur. The text also hints at slightly less restrictive rules and longer implementation periods for developing countries that might wish to use this instrument.

### ***Disciplines Via Rules – The Right Approach?***

It seems no surprise that export credit programs are to be disciplined but not eliminated under the Harbison proposal, given their strong industry support and potential benefit to developing country importers. Credit is crucial to international transactions. Especially when there may be credit market imperfections, a very likely possibility with developing country trade, these programs need to continue. But the disciplines included in the Harbison proposal cause us to question the approach to export competition negotiations—disciplining these institutions via detailed rules, especially in this case.

The rules in the Harbison proposal will likely apply to terms negotiated between two private sector agents, the exporting country banks and private traders in the importing countries. Trade liberalization and privatization have been about getting government out of private transactions, yet this would result in an increased role for a super government, the WTO. The extensive rules in the Harbison text look somewhat like fair-trade rules propping up prices before privatization initiatives of the 1980s. One might prefer that the WTO outcome require that government may not impose detailed conditions on loans between private parties. If governments should not be setting those terms, neither should the WTO. The intent seems now to force reform of specific existing programs than to find an optimal policy regime. Given institutional innovations following the URAA, getting rules right to insure a liberal market outcome seems fraught with difficulty, and the vagueness of interpretation of proposed rules is likely to lead to much future institutional innovation.

The specifics of the rules are also troubling in terms of the distribution of benefits they may bring about. Continuing officially supported export credit programs, but

insuring that interest rates charged reflect full risk premiums means that the private banks and not the importing countries will derive the benefits of these programs. Special and differential treatment is clearly needed for the NFIDCS and LDCs on minimum interest rates if humanitarian benefits to these programs are to be realized. If liquidity constraints are most likely to arise in these cases, the requirement that default losses be covered by interest rates and fees is also likely to make these programs prohibitive for that group of countries. Longer repayment terms are probably less useful special and differential provisions, since these are consumption loans and will not generate assets from which earnings will be generated to repay the loans.

### ***Recommendations***

Our recommendation is that officially export credit programs be allowed to continue. Subsidies from this program are low, trade distortions are small, and the possibility of additionality and of relieving liquidity constraints makes these attractive to both exporters and importers. But we worry very much about the attempt to write detailed rules to discipline these programs. Rules on transactions between private actors seem an illiberal non-market approach, so constraints but not specifications should be set. Moreover, institutional innovations could frustrate the intent of quite specific rules, which none-the-less can be interpreted differently by different parties. New rules might sometimes force out beneficial aspects of programs while the problem programs continue under minor revision. The OECD effort to limit term lengths, but not other provisions, was probably more in the right direction. Since these are consumption (or more appropriately international transactions) loans, the limited term should not be restrictive. The proposed rules do not help to insure additionality, but mostly insure that the importer pay the full market cost of the loan, minimizing prospects for additionality. Special and differential treatment should insure that minimum interest rates do not apply to developing countries, and might also permit direct public expenditure support when humanitarian benefits are evident. For developed country transactions, we believe that reduction commitments on public expenditures supporting export credit programs are the most effective mechanism for establishing necessary disciplines.

### **State Trading Enterprises**

State trading enterprises exist to implement a country's agricultural policy. To do so, these agencies must address multiple goals that may include producer support, consumer subsidization, price stability, marketing system efficiency, and the exercise of market power in both domestic and international markets. In the WTO there is concern that the activities of state traders are not transparent and so STE exporters may be able to subsidize exports in a disguised manner, and possibly violate a member's export subsidy commitments.

The United States has strongly supported further disciplines for STEs and has advocated for the elimination of the monopoly rights of STEs (USDA 2002). U.S. concern over STEs is largely directed at the Canadian Wheat Board (CWB), who is both

a competitor with U.S. multinational firms in world wheat markets and an exporter to the U.S. market. The United States has made numerous complaints and investigations of the CWB over the last ten years, and is using the WTO negotiations as a way to seek disciplines to change the operation of the CWB. This approach means that exporting STEs are more broadly targeted for discipline in ongoing WTO negotiations, however, including in the Harbison text.

Over the last twenty years, many governments have reformed or eliminated their state trading enterprises, due largely to pressure from structural adjustment reforms, and not due to WTO commitments or a will to reform. Table 5 details the agricultural export state trading enterprises that have been notified to the WTO. Comparison to the study by Ackerman and Dixit (USDA 1999) indicates that reform and elimination of STEs has continued over the past few years, leaving relatively few exporting STEs that may have significant market power in world markets. STEs from both Turkey and South Africa were included in the Ackerman and Dixit compilation as large exporters. Both countries have notified the WTO that they no longer maintain STEs in keeping with the WTO definition, eliminating STEs in wheat (Turkey), and maize, fruit, and citrus (South Africa). New Zealand has removed the monopoly export rights previously held by the state trading agencies for apples, kiwis, and pears and has changed the institutional structure of these exporters. The New Zealand Dairy Board and the Australian Wheat Board have been transformed into grower cooperatives that do not receive any financial support from the government. Sixty countries notified the WTO that they do not currently maintain any agricultural STEs.

### ***Concerns over State Trading Exporters***

One avenue for subsidization of an export STEs is direct treasury support of its operations. As these subsidies can be made transparent, and can be notified and limited, this type of subsidization is relatively easy for the WTO to discipline. More problematic is the fact that export STEs can use some combination price pooling, price discrimination, market segmentation, and protection of the domestic market that enable an outcome similar to export subsidies.

Price discrimination is the practice of selling goods at different prices in different markets according to their respective elasticities of demand. For price discrimination to be effective, market power must be present. Price discrimination is not prohibited by the WTO and is commonly used by private firms. A common concern about the CWB is that pooling may enhance its ability to price discriminate.

Price pooling is the practice of purchasing commodities from producers with an initial payment, but an unspecified final price, and returning net revenue at a later time from a pool of receipts. The pool may consist of sales over time, across markets, or across commodities. Because pooling enables market power through entry barriers and segmentation, pooling and price discrimination become interrelated. One possible consequence of pooling in conjunction with price discrimination is that producers realize a higher, more stable price and so increase production.

TABLE 5. Agricultural Export STEs as Notified to the WTO

Country	Agency/Commodity	Item	Year	Domestic Production	Export Volume	Export by State Trading	Sole Exporter
<b><u>Developed</u></b>							
<b>Australia</b>	Australian Dairy Corporation	Butter, butter oil, blends	1997-98	164,000	95,000	NA <sup>a</sup>	No
		Cheese	1997-98	310,000	153,000	47,000 <sup>b</sup>	No
		Skim milk powder	1997-98	215,000	178,000	9,000 <sup>b</sup>	No
		Whole milk powder	1997-98	128,000	95,000	NA <sup>a</sup>	No
	Australian Wheat Board	Wheat	1997-98	19,417,000	15,679,000	15,679,000	Yes
	Queensland Sugar Corporation	Raw cane sugar	1997-98	5,901,000 (raw)	4,758,000	4,516,000	Yes
	Grainco	Barley	1997-98	6,482,000	3,463,000	NA	Yes
	New South Wales Grains Board	Sorghum	1997-98	1,081,000	251,000	NA	Yes
		Oilseeds	1997-98	2,056,000	908,000	NA	Yes
	Grain Pool WA	Lupins	1997-98	1,380,000	972,000	846,000	Yes
		Rapeseed	1997-98	860,000	590,000	195,000	Yes
	NSW Rice Marketing Board	Rice	1997-98	1,331,000	680,000	680,000	Yes
	NSW Grains Board	Oats	1997-98	1,634,000	155,000	NA	Yes
	Australian Barley Board	Oats	1997-98	As above	As above	NA	Yes
	<b>Canada</b>	Canadian Dairy Commission	Butter and other fats and oils derived from milk	1996-97	90	11	6
Canadian Wheat Board		Wheat	1996-97	29,801,400	19,366,000 <sup>c</sup>	21,383,337	Yes
		Barley	1996-97	15,562,000	4,005,400 <sup>c</sup>	4,474,133	Yes
Ontario Bean Producers Marketing Board	White pea beans	1997-98	43,500 (Ontario)	31,438 (Ontario)	24,947	No	
<b>Israel</b>	Israel Groundnuts Production and Marketing Board	Groundnuts	1994-95	19,500	10,184	10,184	Yes
	Fruit Board of Israel	Non-citrus fruit	1994	385,491	52,499	52,499	Yes
	The Vegetable Production and Marketing Board of Israel	Vegetables	1994-95	1,720,000	99,900	90,938	Yes
Canadian Freshwater Fish Corporation	Freshwater fish	1997	38,798	22,984	8,344	No	
<b>New Zealand</b>	New Zealand Dairy Board (elimination has occurred but has not been reported)	Butter and butter oil	2000	344,000	336,000	336,000	Yes
		Skim milk powder	2000	187,000	172,000	172,000	Yes
		Cheese	2000	297,000	249,000	249,000	Yes
		Other milk products	2000	480,000	584,000	584,000	Yes
		Casein and caseinates	2000	97,000	106,000	106,000	Yes
	State Trading: Enza Limited	Apples	2000	590,155	335,505	317,718	No
		Pears	2000	NA	8,939	8,457	No
	Zespri Group	Kiwifruit	2000	217,000	196,448	186,500	No
New Zealand Hop Marketing Board	Hops	2000	831	614	614	Yes	
<b><u>Developing</u></b>							
<b>Barbados</b>	Barbados Dairy Industries Limited	Unclear	NA	NA	NA	NA	Yes
	Barbados Agricultural Development Corporation	Sugar (raw)	1994		30,863	NA	Yes
<b>China</b>	China National Cereals, Oil and Foodstuff Import and Export Co. (Group)	Rice	2001	187,910,000	1,860,000	1,670,000	Yes
		Corn	2001	106,000,000	6,000,000	5,710,000	Yes
	China National Textiles Import and Export Co.	Cotton	2001	5,320,000	60,000	50,000	Yes

(continued)

Country	Agency/Commodity	Item	Year	Domestic Production	Export Volume	Export by State Trading	Sole Exporter	
Cyprus	Cyprus Potato Marketing Board	Potatos	1993-94	137,000	108,000	108,000	Yes	
	Cyprus Carrot and Beetroot Marketing Board	Carrots	1994	400	19	19	Yes	
		Beetroot	1994	2,000	1,436	1,436	Yes	
	Vine Products Commission <sup>d</sup>	Raw grape alcohol			NA	0	0	Yes
		Raisins			NA	0	0	Yes
		Cyprus Olive Products Marketing Board <sup>e</sup>	Olives	1994	5,000	0	0	Yes
	Olive oil		1994	2,500	0	0	Yes	
Dominica	Dominica Banana and Marketing Corporation	Bananas	NA	NA	NA	NA	Yes <sup>f</sup>	
Fiji	Fiji Sugar Marketing Company	Sugar	1997	347,389	303,339	303,339	Yes	
India	Various State Level Cooperatives	Gum karaya	2000-01	NA	1,000	1,000	Yes	
	Various State Level Cooperatives	Niger seeds		NA	29,000	29,000	Yes	
	Various State Level Cooperatives	Onions		NA	519,000	519,000	Yes	
Indonesia	Badan Urusan Logistik (Bulog)	Rice	2001	28,206,900	0	0	No <sup>g</sup>	
Jamaica	The Cocoa Industry Board	Cocoa	NA	NA	NA	NA	Unclear	
	The Coconut Industry Board	Coconuts	NA	NA	NA	NA	Unclear	
	The Coffee Industry Board	Coffee	NA	NA	NA	NA	Unclear	
	The Banana Board	Bananas	NA	NA	NA	NA	Unclear	
	The Sugar Industry Authority	Sugar	NA	NA	NA	NA	Unclear	
Korea	Korea Ginseng Cooperative Federation	Ginseng	1997	11,259	347	19	No	
Mauritius	Agricultural Marketing Board	Tea	1997	1,787	436	0	No	
Namibia	Meatco <sup>h</sup>	Meat and meat products from cattle, sheep and goats					No	
Philippines	National Food Authority <sup>i</sup>	Rice	2001	12,954,870	0	0	Unclear	
Taiwan	Council of Agriculture, Executive Yuan	Brown rice	2000	1,540,000	119,000	0	Unclear	
	State Trading: Taiwan Provincial Fruit Marketing Cooperative	Banana	2000	198,455	42,603	42,603	Yes	
	State Trading: Taiwan Salt Industrial Corporation	Salt	2000	69,525	336	100	Yes	
	Taiwan Sugar Company	Sugar <sup>j</sup>	2000	259,000	14,705	14,705	Yes	
Trinidad and Tabago	Cocoa and Coffee Industry Board of Trinidad and Tabago	Cocoa beans	1997	1,736	1,378	990	Yes	
		Coffee beans	1997	NA	NA	1,082		
	Caroni	Sugar	1997	113,568 (raw)	69,577 (raw) 8,026 (refined)	69,577 (raw) 8,026 (refined)	Yes	
	National Flour Mill Limited	Soya oil	1997	35,126	NA	1,256,322 (litres)	Unclear	
	Soya meal	1997	51,869	NA	30,274,500	Unclear		
Tunisia	National Edible Oils Board	Olive oil	1998-99	180,000	NA	76,971	No	

<sup>a</sup>Australia Dairy Corporation trades internationally on a competitive basis with private Australian traders in these products.

<sup>b</sup>Australia Dairy Corporation has exclusive rights to specified markets.

<sup>c</sup>Total quantity exported may differ from quantity exported by STE due to different reporting periods used by Statistics Canada and the CWB.

<sup>d</sup>Insufficient production for exports.

<sup>e</sup>No exports due to high domestic prices.

<sup>f</sup>Sole exporter to countries outside of the Caribbean.

<sup>g</sup>Bulog maintains the right to intervene in the market when necessary.

<sup>h</sup>Meatco exists to export to the EU.

<sup>i</sup>National Food Authority did not engage in the export of rice and corn in 2001 due to domestic shortages.

<sup>j</sup>Taiwan Sugar Company only exports sugar to the United States according to quota allocation.

Source: Compiled by authors from country notifications to the WTO in the document series G/STR/N on the WTO website <http://www.wto.org>.

Some STEs have monopoly control over the domestic market (only). If they have effective barriers to imports, they can charge domestic consumers a higher price than their sales on the world market. This outcome can occur when STEs or similar institutions segment domestic and world markets. This combination of instruments used by STEs may lead to an outcome of consumer-financed subsidies (Schluep and de Gorter 2000). For example, the Canadian Dairy Board sets a high price for milk in their domestic market and uses a combination of import barriers and supply management to restrict milk supply. In 2002 a WTO panel found that the market segmentation resulting from Canadian Dairy Board policies resulted in an export subsidy, as processors could buy milk from producers at a price lower than the government determined domestic price (WTO 2002d).

The WTO panel ruled that the average total cost of production is an appropriate benchmark for export sales as one factor in determining if export subsidies were given, treating such actions in a manner parallel to dumping.

Another concern presented in position statements is that STE exporters may have market power in international markets. Examination of Table 5 indicates that relatively few agricultural exporting STEs are likely to have enough market share to significantly alter world prices. The CWB and the Australian Wheat Board accounted for an average of 15 and 13 percent of world wheat and wheat flour trade between 1997–2001.<sup>4</sup> China's COFCO both imports and exports grains in order to stabilize domestic supplies. Due to large swings in its net position, COFCO may be able to exert market power in some years. In 1993 COFCO accounted for about 8 percent of world corn exports, changing to net corn importer in 1995, and accounting for about 15 percent of the world corn imports in that year. The Queensland Sugar Corporation exported almost 12 percent of world sugar in 1997–98, and COFCO accounted for about 6 percent of world rice exports in 2001. The New Zealand Dairy Commission, which accounted for 30 percent of the world dairy market, has recently been replaced by an export cooperative named Fonterra. However, New Zealand has not notified this change to the WTO and insufficient information has made it difficult to assess if Fonterra has an effective export monopoly.<sup>5</sup>

In a recent evaluation, Carter and Smith (2001) conclude that the balance of evidence indicates that grains markets are most likely competitive, due to the number of players in the market and freedom of entry. Earlier studies have disputed this claim, and have cited evidence of imperfect competition in grain and other agricultural markets. We believe that the CWB and the AWB may have some market power in some circumstances, and have additional concern over the possibility of market power in the thin and highly distorted world dairy market.

Relatively low market shares in most cases may lead to the conclusion that concern over market power by most exporting STEs is misplaced. However, this

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<sup>4</sup> These calculations use export volumes reported by countries in their STE notifications and world trade volumes from FAOSTAT (2003).

<sup>5</sup> Rae (2003) indicates that Fonterra does not have a legal export monopoly, however, this information was not available through New Zealand's WTO notification.

conclusion must be tempered by the caveat that if products are differentiated, or markets are highly segmented, that the market power of these entities may be greater than indicated by their market share.

If WTO reforms were to eliminate STEs or contribute to their demise, they may be replaced by imperfectly competitive private actors, a common outcome following structural adjustment reforms. In addition, to the extent that market power exists, if STEs are eliminated, then the rents will be captured by private oligopolistic firms instead of being funneled to producers through public entities.

In Canada there has been an intense domestic debate about whether or not Canadian producers are well served by the CWB. Producers who desire to market their grain, and interests who feel that the current system is inefficient, have been vocal proponents for change. We feel that these questions are best resolved at the national level.

### *URAA and State Trading*

State trading has been permitted by the WTO and previously by the GATT. Members using export state traders are obligated to ensure that their activities are consistent with non-discriminatory treatment, that sales are made in accordance with commercial practices, and that notifications are made in accordance with WTO procedures.

One mechanism the WTO implemented in order to deal with potential market distortions due to STE activities is to increase transparency through notification requirements. These notification requirements were revised after the URAA by the Working Group on State Trading Enterprises (WTO 2001e). Members are to submit a full notification every third year and to notify the WTO of changes in intervening years. Full notification requirements include a description of the enterprise, its legal authority, how import and export volumes and prices are determined, and statistical information. Young, Abbott, and Leetma (2001) advocated for notification as a means to detect inappropriate activity on the part of STEs in our last analysis of potential disciplines for this round. Experience with post URAA notification raises concern with that recommendation.

Examination of notifications reveals that many members have never notified the WTO about whether or not they maintain STEs (approximately 46 countries, some of whom may still have STEs) and that many notifications are delayed, inadequate, or present out-of-date statistical information. For example, New Zealand notified the WTO regarding its STEs in July of 2001, but no subsequent notifications have indicated to the WTO the change in status of the NZ Dairy Marketing Commission (WTO 2001f). Canada's latest notification, dated November 2002, reports 1996–97 data for the Canadian Wheat Board (WTO 2002e).

Given the controversial nature of STEs, and in particular the CWB, we believe that timely reporting is in their self-interest in order to demonstrate the effectiveness of notification in lieu of other disciplines. Problems with the timeliness and completeness of

notification are also evident for export subsidies and export credit guarantees, and are potentially problematic for food aid.

### ***Harbinson Proposal on State Trading***

The Harbinson text allows the continuation of agricultural exporting STEs, while proposing strict disciplines to ensure that they cannot provide implicit export subsidies. The proposal states that members are to ensure that state trading agencies do not circumvent national commitments under their export subsidy commitments and that state traders do not enjoy special rights that would impair conditions of competition in world markets. Several specific disciplines are proposed to achieve those goals.

***No Export Subsidies.*** A provision applying to both developing and developed WTO members states that exports of a product cannot take place at a price less than the price paid by the enterprise to the domestic producers of the product. One interpretation of this is that the average export price over a marketing year cannot be less than the price paid to producers. An alternative interpretation is that the STE cannot engage in any export transactions in which the price received is less than the initial price paid to producers. Under this interpretation, if world prices decline over the marketing year to a price lower than anticipated, and lower than the initial price, an STE would not be able to sell their remaining supplies. Any private actor holding stocks could not operate under such a rule.

***Elimination of Monopoly Rights.*** The Harbinson text proposes that national governments in developed countries must allow private enterprises the right to purchase agricultural goods for export and to engage in exporting. This provision removes the monopoly status of exporting STEs and directs them to coexist with the private sector, with an implementation plan to be included in each member's schedule.

Examination of WTO notifications indicates that in a few cases STEs coexist with the private sector. Examples of this mostly occur when export STEs are responsible for fulfilling export quotas. An example is Taiwan for sugar. In the case of Poland, coexistence for their wheat STE was a first step in a reform process that ultimately resulted in the elimination of the STE and this may have been the intent when the monopoly rights were removed (USDA 1998). There are several instances under structural adjustment reforms where rules such as this, requiring coexistence, have been ineffective, so that private firms either do not try to compete (e.g., cocoa in Ghana) or fail (in Egypt). We are unaware of cases of co-existence in which both an exporting STE and private traders maintain viable market shares over a substantial period of time.

If these reforms are pressed on countries that have chosen to implement their agricultural policy goals through STEs, the governments may resist the reforms. For example, governments may enact legislation that places the private sector at a disadvantage in the market, or may not enact enabling legislation allowing the private sector to function effectively. This might explain why the NZ cooperatives for kiwi, apples, and pears maintain 95 percent of their export market, despite the elimination of

their monopoly rights to export, or why Cocobod in Ghana still exports 100 percent of that country's cocoa exports. And in Nigeria and Cameroon, in spite of elimination of cocoa parastatals, legislation to enable a fully functional private sector was still not in place a decade later.

In cases where governments do enact real coexistence in keeping with the proposal, it may be difficult for the STE to fulfill its mission through the realization of economies of scale in marketing and by funneling any rents from market power to producers, since the intent of coexistence is precisely to eliminate that market power. In particular, removal of the monopoly export rights of the CWB is likely to result in the demise of the CWB in its current form. The CWB uses accredited export agents who are branches of large multinational companies with extensive experience in the market and investments in infrastructure. A WTO rule eliminating the CWB's monopoly right to export is likely to result in the entry of these companies into the market and an uncertain future for the CWB. This may be an exceptional case, since in most instances prior to reform viable exporting agents to replace the parastatal are not present.

When STEs are monopoly exporters who use high domestic prices as a means of subsidizing exports to the world market, this results in a decrease in world market prices, making it more difficult for low cost exporters to compete. The mechanism to correct this outcome is to ensure that real access exists to the domestic "sanctuary" markets of the STEs, so that artificially high domestic prices do not subsidize exports.

***No Special Financing Privileges.*** It is proposed that developed country governments cannot grant special financing privileges to STEs that export a significant share of the member's total exports of an agricultural product. This proposal prohibits members from subsidizing the operation of an STE. This prohibition is more severe than current or potential disciplines on direct export subsidies. If the Harbinson proposal is successful, direct export subsidies will be eliminated over two rounds of negotiations and a time period of fifteen years. A policy more consistent with other WTO disciplines would be to allow governments to subsidize the operation of export STEs, and to require that expenditures are reported, bound, and reduced over time. This approach would put expenditures on STEs on par with government expenditures on domestic support or export subsidies, and not penalize members that have chosen a different instrument for the implementation of their agricultural policy.

This provision also appears to prohibit STEs from offering officially supported export credits, a restriction beyond the disciplines proposed by the Harbinson text on Officially Supported Export Credits. Under this interpretation, the CWB or the Australian Wheat Board, for example, cannot offer export credits, but the U.S. Commodity Credit Corporation can through its GSM program. It is reasonable that export STEs be bound by the disciplines on Officially Supported Export Credits. However, to apply a prohibition on their use to STEs alone is not supported by research nor is it comparable to other WTO disciplines. In response to such a prohibition, a member might innovate by creating a new institution, legally separate from the STE that would provide WTO legal export

credits. This speaks to the challenge that the WTO faces in attempting write rules that discipline behavior effectively.

***Notification Requirements.*** This provision would require members maintaining an STE to notify the WTO of relevant information as requested by the COA. Details are not specified. While USTR has cited this as a call for greater transparency, it is not clear how this goes beyond current URAA notification requirements—which have not been strictly adhered to.

### ***Conclusions on STEs***

Proposals on exporting STEs in the Harbison text closely mirror the U.S. position and reflect U.S. concerns with the Canadian Wheat Board. Positions of other WTO members indicated a desire to discipline STEs, but did not advance these specific disciplines, and did not advocate for the elimination of STEs monopoly right to export. WTO members need to assess if these disciplines reflect the balance of their concerns.

It is difficult to write rules that will eliminate any possible distortion caused by STEs while preserving their ability to achieve their mandate. Rules in the Harbison text are punitive in their treatment of state trading enterprises, and not consistent with the approach taken in other agricultural disciplines.

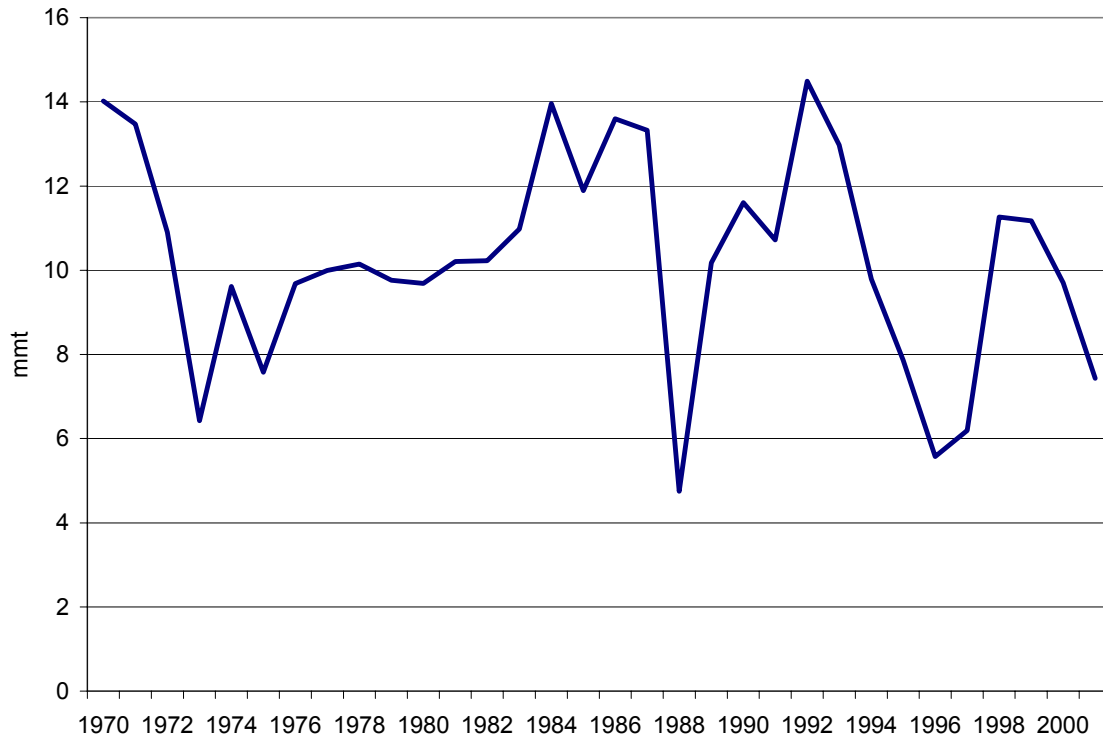
Coexistence of STEs with private firms is intended to insure competitive market outcomes. But if this rule or other WTO requirements lead to elimination of STEs, the likely replacement may be oligopolistic private firms. It is not apparent that replacing a monopolistic public entity with a social mandate by an imperfectly competitive private sector leads to preferable outcomes.

In our view, STEs are a legitimate instrument for the implementation of agricultural policy goals. They may result in some limited distortions to world markets due to somewhat greater ability to price discriminate, due to pooling and due to limited market power in a few cases. In making a decision on disciplines, WTO negotiators need to carefully assess the cost of eliminating the policy instrument of choice for some countries, with gains from eliminating the likely small distortions caused by STE exporters.

## **Food Aid**

### ***Players and Perspectives***

Historically, exporters/donors and recipients share a concern about the impact of food aid on markets. Agricultural exporters are concerned that food aid can be used as a mechanism for donor nations to potentially circumvent their export subsidy commitments and to reduce surplus stocks at times when world prices are low. Recipients are concerned that relatively large quantities of food aid may be sold over a short period of



**FIGURE 2. Global Food Aid**

Source: FAOSTAT – Agriculture Data, 2003.

time on local markets with impacts on the level and variability of local commodity prices. Recipients are also concerned with the reliability of food aid, as it is well known that food aid donations tend to increase in times of surplus, and decrease in times of shortage and high prices when most needed by recipients. Figure 2 illustrates this variability. Finally, recipients take issue with donor criteria for some food aid programs.

Food aid is a difficult issue to negotiate in the Doha Round, as it is not easy to write rules that eliminate the potential abuse of food aid as an implicit export subsidy while ensuring that genuine needs are met, and that producers in developing countries are not harmed. Negotiations on food aid in the Doha Round have been centered on concerns expressed by the EU about U.S. food aid programs. The EU is concerned that U.S. programs include food aid on a loan basis rather than grants, and have a market development objective. Concern also continues over U.S. use of food aid programs as a mechanism to dispose of surplus stocks. The EU has made an effort to ensure that its food aid programs are not linked to the existence of EU agricultural surpluses (European Commission 2000), an effort not matched by the United States.

The United States is the largest food aid donor, giving 63 percent of global food aid in 2002, and accounting for an average of 55 percent of food aid over the 1990s. Donations by the European Commission are variable, and accounted for a low of eight and a high of 29 percent of global food aid donations during the 1990s. While food aid has been dominated by these two donors, non-traditional donors are entering, as indicated

in Table 6. Other non-traditional donors in 2001 included Algeria, Jordan, Libya, Nigeria, Oman, Sri Lanka, Thailand, and Vietnam.

TABLE 6. Food Aid Donors, 2001

Donor	mmt	percent
United States	6.80	62.0
EU Commission and Members	1.90	17.0
Japan	0.90	8.0
China	0.44	4.0
Canada	0.28	2.5
Republic of Korea	0.20	2.0
Australia	0.16	1.5

Source: WFP, 2002

The World Food Program (WFP) of the United Nations delivered 42 percent of global food aid in 2001, including nearly 70 percent of emergency aid and 27 percent of project aid. WFP donations originate from bilateral donors, such as the United States or EU, and are intended to reduce the political motivations behind food aid distribution.

Non-governmental organizations (NGOs) and private voluntary organizations (PVOs) play an important role in delivering food aid from both bilateral donors and the WFP. In this capacity, they are described as the “channels” for food aid. In the 1990s, NGOs and PVOs delivered between 60–70 percent of global food aid. These agencies finance their activities by selling food aid they control on recipient country domestic markets, a practice called “monetization.” In some cases the funds from monetized food aid are used to cover overhead costs of distributing food aid, and in other cases the funds are used by NGOs to finance a variety of food security and broader development projects.

### ***Food Aid in the URAA***

Food aid was included in Article 10.4 of the URAA (GATT Secretariat 1994), and drew on protocols and commitments that previously were implemented in other agreements. This sparse article is titled “Prevention of Circumvention of Export Subsidy Commitments.” It states that food aid shall not be tied directly or indirectly to commercial exports of agricultural products to recipient countries; that food aid must be carried out in accordance with the UN Food and Agriculture Organization’s “Principles of Surplus Disposal and Consultative Obligations;” and that food aid be provided to the extent possible in fully grant form or on terms no less concessional than in Article 4 of the 1986 Food Aid Convention. This article provided little new discipline on food aid transactions.

Developing countries anticipated that the implementation of the URAA would increase world market prices and volatility, making it more difficult for them to import their food requirements. In response to these concerns, the URAA included the Marrakesh Decision mentioned earlier in this paper. In terms of food aid, the decision committed the WTO to review the level of food aid under the Food Aid Convention of

1986 and initiate negotiations to ensure that the legitimate needs of developing countries were met during the implementation of the URAA. The Marrakesh Decision also directed the WTO to ensure that an increasing percentage of basic food stuffs would be provided in grant form and/or on concessional terms.

### ***Additionality and Monetization***

Additionality and monetization are closely related concepts concerned with the potential market impacts of food aid. Food aid is considered additional if it is given to people who would not have consumed it otherwise, and under this stringent condition it should have no impact on commercial markets. The degree to which food aid is additional depends on how well it is targeted to recipients and how much is sold. Food aid that is sold, or “monetized,” on local markets either competes against domestic production or reduces the demand for commercial imports.

Historically food aid has been divided into three types. Emergency food aid is given to victims of natural disasters and political strife. While emergency food aid is most likely to meet additionality criteria, all three major donors allow some portion of emergency aid to be monetized to cover transportation and overhead costs. Project food aid is distributed to target beneficiary groups to support poverty alleviation objectives and may include projects such as food for work, mother and child nutrition projects, or a broad range of other development projects less directly related to food security. It may be additional or monetized to varying degrees. Programme food aid is a resource transfer in which food aid is sold by the recipient government and the money is used for balance of payments or budgetary objectives, and hence is mostly monetized. Programme food aid is given solely through bilateral programs as the WFP does not give programme food aid.<sup>6</sup>

Emergency food aid accounted for 5.5 mmts, or half of total food aid in 2001, and has accounted for an increased proportion of total food aid over the last decade. The WFP delivered nearly 70 percent of emergency food aid. Twenty-two percent of global 2001 emergency food aid was accomplished through triangular transactions and local procurement which are likely to be helpful to developing country markets.

Project food aid accounted for 25–30 percent of the total in 2001 and 2002. The United States is currently providing more project food aid (and less programme food aid) and in 2002 provided 77 percent of global project food aid. The United States allowed NGOs to monetized 35 percent of this food aid on developing country markets, and is the only donor that allows project food aid to be monetized (Simon 2003). In 2002, U.S. monetized project food aid accounted for 43 percent of total project food aid. While project food aid may meet worthwhile goals, the high level of monetization now practiced indicates that much of it is not additional. It may be sold in quantities that are large for local markets, and over a short period of time. Project food is more widely

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<sup>6</sup> Clay and Stokke (2000) provide an excellent discussion of the inadequacy of this historical classification of food aid given the level of diversity that currently exists in the goals and methods of projects concerned with increasing the food security of developing countries.

dispersed than emergency or programme food aid. Thirteen recipients received 62 percent of 2001 project aid, and the balance of 38 percent is spread among 69 countries.

The United States gave 81 percent of global programme food aid in 2002. All programme food aid is sold on local markets. Although such sales may lower local prices and enable purchases of food by poor consumers, it is unlikely that much programme food aid is additional. In the United States, programme food aid is delivered through the U.S. P.L. 480 Title I program, which is also contentious due to its market development objective and the fact that this food aid program is provided as loans instead of grants. Programme food aid is also provided through U.S. P.L. 480 Title III, Section 416(b) and the Food for Progress programs. Programme food aid is highly unstable, as indicated by its growth from 1.8 mmt in 1997 to 8 mmt in 1999, then decreasing to 2.7 mmt in 2001. This pattern suggests this form of aid was one vehicle to respond to the Asian financial crisis, and so may have been somewhat additional in the sense that foreign exchange would not have otherwise been available to import food.

### ***Food Aid Variability and Conditionality***

Developing countries have voiced dissatisfaction with the implementation of the Marrakesh Decision in terms of WTO commitments to meeting their food security concerns. In the 1999 Food Aid Convention (FAC), donors decreased their pledged amount to 4.8 mmt, the lowest level since the initiation of the FAC 33 years earlier. However, food aid donations have exceeded the minimum commitments by a substantial amount. Discussions within the WTO indicate a desire by developing countries for higher food aid commitments that would be part of legally enforceable country schedules.

Conditionality is the granting of food aid on the basis of recipients meeting specified criteria, and is most evident in project and programme food aid. U.S. donations under the “Food for Progress” program require that countries have “made commitments to free enterprise in their agricultural economies.” In the U.S. P.L. 480 Title I program, qualifying countries must demonstrate the potential to become commercial markets for U.S. agricultural commodities. The EC laid down strict criteria for the granting of aid, so that recipients must be politically stable and have an operational food security plan. The EC states that they will give food aid to countries that do not meet their criteria through donations to the UN WFP. Conditionality can impose costs on recipient countries and may force them in political or economic directions they would not choose on their own. These “strings” reduce the perceived value of food aid by recipients.

Both the variability and conditionality evident in food aid programs may have motivated substantial developing country support for a food financing facility—an option they see as better addressing their food security concerns. A proposal led by Egypt prompted the Committee on Agriculture to request an evaluation of this idea by a committee consisting of representatives of relevant multilateral institutions and UN agencies. The panel’s mandate was to evaluate means of implementing access by LDCs and NFDCs to multilateral programs and facilities to assist with short-term difficulties in financing normal levels of commercial imports of food and to evaluate the feasibility of a

revolving fund. The panel's investigation indicated that in many cases difficulty in importing was due to liquidity constraints faced by private importers, and that there were many difficulties in designing a revolving financing fund that would overcome this constraint. For a variety of reasons the panel concluded that creation of a revolving fund was infeasible and small modifications to current IMF programs were recommended (WTO 2002f).

### ***The Harbinson Proposal on Food Aid***

The Harbinson proposal on food aid reflects the tension inherent in food aid disciplines, a tension between encouraging a generous response to need without allowing food aid to provide a mechanism for exporters to dispose of agricultural surpluses.

***Food Aid Not Tied to an Obligation to Import.*** The proposal includes language similar to that currently existing in the URAA Article 10.4 (a) that states that food aid cannot be tied to an obligation on the part of the recipient to import goods from the donors. However, the language is now stronger and more detailed. No complaints have been brought to the WTO dispute resolution understanding on food aid and it is difficult to assess if stronger language will have a measurable impact. The language does meet a need expressed in some position statements to ensure that food aid is freely given without obligation on the part of the recipient to engage in commercial transactions with the donor.

***Emergency Food Aid.*** The Harbinson proposal details the conditions and situations under which emergency food aid is valid, and the agencies, organizations, and donors who are legitimate donors and intermediaries. While meeting the need expressed by the EU and several developing country members for criteria for food aid, the language on emergency food aid does not appear to restrict the ability of the international community to respond to crises with food aid.

***Legitimate Channels for Project and Programme Food Aid.*** Section 4 (b) (ii) of the proposal does not comprehensively illustrate or define legitimate project and programme food aid. Its approach is to list various ways that grant and in-kind food aid can be provided and mentions specialized UN agencies, non-governmental humanitarian agencies, and charitable bodies in agreement with donor governments as channels. This list does not include government-to-government transactions and implies that they would not be allowed. Several countries gave food aid in 2000 on a government-to-government basis, in all categories of food aid, totaling just over 3 mmts as illustrated in Table 7. About 68 percent is accounted for by U.S. programme food aid. The exclusion of government-to-government food aid is a blunt tool to use in disciplining U.S. programme food aid, and could affect food aid programs that are widely regarded as legitimate. This seems to promote channeling food aid through NGOs and minimizes the role of developing country governments in implementing their own development strategies. These authors have not seen research that investigates the effectiveness of different channels for bilateral food aid, and feel that the motivation and reasoning behind this discipline needs to be further demonstrated.

TABLE 7. Government-to-Government Food Aid, 2000

	Emergency	Project	Programme	Total
	----- metric tonnes, grain equivalent -----			
Australia		49,500		49,500
Canada	10,000		51,577	61,577
EU	33,000			33,000
France		57,805	79,905	137,710
Italy	6,328	13,507	10,969	30,804
Japan		37,109	112,346	149,455
United States	149,686	350,512	2,103,231	2,603,429
Total	199,014	508,433	2,358,028	3,065,475

Source: WFP data grain equivalent calculated by the authors, 2003

***Project and Programme Food Aid: Allowed with Notification.*** Program and project food aid are allowed to continue with increased notification to the WTO Committee on Agriculture. Potential problems caused by duplication of existing notification requirements to the UN Food and Agriculture Subcommittee on Surplus Disposal are not addressed. While increased transparency through notification is a useful goal, recent WTO experience indicates that notification requirements enacted in the URAA have not been diligently met.

***Grant Form Only.*** It is proposed that all food aid be provided in grant form, so that concessional loan programs would be considered an export subsidy. The United States is the only donor that provides food aid on loan terms, and food aid in the form of loans accounted for 12 percent of total U.S. donations in 2001, varying between 7 and 17 percent in the 1990s (WTO 2000). The Foreign Agricultural Service of the U.S. Department of Agriculture reports that the amount of Title I food aid declined from 1.25 mmts in 2000 to a half a million metric tones in 2002. In addition, some “Food for Progress” donations are listed as funded by Title I and the amounts are small. Title I programs have been criticized both because they provide loans, not grants, and due to their market development objectives. Since is possible that a loan program with food security objectives could prove useful to recipients and would no longer be allowed, this is another blunt instrument to target a specific problem program.

***Assessment of Violations.*** Food aid that neither complies with the provisions of the proposed disciplines (i.e., not provided in grant form) and cannot be accommodated within the member’s export subsidy commitments will be assessed as non-commercial transactions that circumvent the member’s export subsidy commitments. Details on how the subsidy component of the food aid would be measured have not been specified. It is likely, nevertheless, that the U.S. Title I grains sales could be accommodated within U.S. commitments for export subsidies. Donations of dairy might have difficulty as the United States was in excess of its dairy export subsidy commitments in 1999, and later data is not yet available.

### ***Conclusions on Food Aid***

Food aid presents a three-pronged dilemma for the WTO and other concerned entities. It achieves humanitarian objectives, both by feeding hungry people and by enabling greater financing for development projects through monetization. But if food aid is not additional, it may either lower prices to domestic producers or reduce commercial imports. Trade liberalization makes the latter more likely while forcing developing countries to face the vagaries of unstable world markets, so proposed WTO rules focus on trade impacts. The WTO is an appropriate forum for addressing the disciplines to minimize the impact of food aid on commercial markets, which fits within the WTO's primary mandate. Due to this mandate, it is not clear that the WTO will adequately address concerns over the sufficiency and reliability of food aid, or meet developing country requests for an alternative mechanism to assist them in importing their food requirements when faced with private or public liquidity constraints. It also seems to put a lower priority on market impacts within recipient countries.

Exporter concerns over the use of food aid as an explicit export subsidy are partially addressed in the Harbison proposal by eliminating the use of food aid that is not in grant form. It specifically targets the U.S. P.L. 480 Title I market development program. In addition, it also attempts to provide a definition of legitimate food aid, donors and intermediaries, and requires notification of specified transactions. These are necessary first steps for a WTO member to make a complaint about questionable food aid and to take the complaint through the dispute settlement process. However, the Harbison proposal appears to resist excessive disciplines on food aid that might limit donor motivation to provide food aid. We feel that the WTO needs to err on the side of allowing food aid in the hope of meeting legitimate need, even at the risk of adverse impacts on commercial markets that may be felt by agricultural exporters. In previous work we have judged that this impact is likely to be small (Young, Abbott, and Leetma 2001).

### **Conclusions on the Export Competition Negotiations**

Both The Doha Ministerial mandate and the Harbison proposal on modalities for a new WTO agreement on agriculture utilize the framework for trade liberalization established in the URAA. That approach is to set rules governing institutions involved in trade and domestic agricultural policy implementation, and to make reduction commitments for distortionary policy instruments, including export subsidies. Issues are again divided into the three pillars—market access, domestic support, and export competition. In the area of export competition, the Harbison proposal calls for gradual elimination of export subsidies (over nine years for developed countries) and sets disciplines for officially supported export credit, food aid, and exporting state traders.

Both country proposals to the WTO and the Harbison text address unfinished business from the URAA. Following that agreement, each of the substantive areas addressed has become largely a one-country issue. The EU utilizes over 90 percent of the remaining direct export subsidies. Nearly all of the measured subsidy component of the

many officially supported export credit programs arise from the long-term U.S. GSM programs. Food aid issues focus on U.S. P.L. 480 Title I programs that are given as loans rather than grants, and for which one objective is market development. State trading focuses on U.S. disputes with the Canadian Wheat and Dairy Boards.

The Harbison proposal is not a country position nor a negotiated outcome, but is likely the document from which negotiations must move forward. Country positions have been mostly stagnant since the Doha Ministerial, so this document was an attempt by the Chairman of the agriculture negotiating committee to move negotiations forward and meet the (missed) March 31 deadline for a modalities document. While much is incorporated as bracketed text to be resolved in negotiation, some clear positions emerge on export competition. It calls for elimination, albeit gradually, not simply reduction of this highly distortionary trade policy instrument. But institutions which can give rise to implicit export subsidies—export credit, state trading, and food aid—are subjected to disciplines via rules rather than being outlawed.

Setting disciplines faces difficult tradeoffs since beneficial aspects of each institution potentially implicitly subsidizing exports are recognized. Food aid can help the hungry poor or finance development projects. Export credit can break liquidity constraints and lead to additional imports. State trading remains a popular alternative mechanism to implement domestic agricultural policy. Hence, the Harbison text rules seek to prevent subsidization while permitting these institutions to continue.

While issues may center on single country programs, the WTO must write rules that are applicable to all members. Writing such rules has in the past evidenced some weakness in this approach. Strict rules may eliminate some beneficial institutions or practices, while the problem program may innovate slightly and continue to pursue its prior farm policy objectives. Institutional innovation under strict interpretation of URAA Articles means to some extent the hoped for liberalization from the URAA has been more limited than was expected. Rules are subject to interpretation, and so have not always succeeded in preventing offending practices, while in other instances negotiators have objected that dispute panels may go well beyond their original intentions. In the case of export credits, those rules may impose conditions on transactions between private actors that would not normally apply in liberalized markets, such as minimum prices that stifle competition. And those rules may direct benefits away from desirable social outcomes. In the case of food aid, rules may inhibit achieving its humanitarian benefits, and in the case of export credit it may direct benefits to banks and intermediaries rather than the poor in developing countries.

Following the URAA approach may also leave new issues badly addressed. New subsidy mechanisms may not be as well targeted in the Harbison text, especially when they overlap more than one of the three pillars. For example, U.S. marketing loan programs are likely to lead to implicit export subsidies, but are addressed only as domestic support measures. Of more central concern is developing country focus on broad food security objectives in their position papers. Repeatedly we found that issues of concern to developing countries remain unaddressed in the Harbison text. Developing-

country concerns are now typically addressed by provisions granting special and differential treatment, which simply involve longer implementation periods to adopt disciplines or reduction commitments targeting developed country practices. If the WTO philosophy is correct, these provisions, and so delayed reform, may not always be in the self-interest of developing countries. More importantly, they do not address the true concerns of developing countries—how to establish measures to protect the food security of their vulnerable populations.

No attempt has been made to create a mechanism that would assist developing countries in financing import requirements and do so in a manner that gives them some independence from the conditionality inherent in bilateral food aid programs and in the assistance offered by multilateral institutions, such as the IMF food financing facility. In the rounds of trade negotiations that occurred under the GATT, countries traded off concessions in their tariff schedules. In the new WTO, developing country members have little to trade in term of concessions, and certainly they have little to trade in terms of reductions in export subsidies. They have expressed desire for higher commitments of food aid and a food financing facility. Part of their difficulty in securing these in the current round may be that other institutions have been concerned with these issues in the past. Another difficulty may be that these issues are mostly being addressed outside of the negotiations, again making trade-offs difficult.

It was interesting to observe the extent to which developing countries oppose an institution that can potentially offer benefits to them—since they may be the recipients of export subsidies. But they were more concerned with the potential impacts on their own markets, and on the costs of running their own agricultural programs. This was especially evident in the food aid debate. Benefits from subsidies may be small, unreliable, arising when world prices are low not high, and subject to onerous conditions. The emphasis of the WTO on minimizing impacts on commercial markets rather than on hungry people or developing country domestic markets is why the WTO may be the wrong forum to resolve some of these issues.

One of the concerns evident in the debate on export competition, and particularly on state trading, is the dilemma of how broad a range of agricultural policy institutions to permit. The URAA endorses the decoupled approach to subsidizing agricultural producers only. State trading is another approach to implementation of agricultural policy that countries, particularly developing countries, are reluctant to give up. The WTO focus on a static assessment of market distortions, rather than a dynamic assessment incorporating desires by countries for stability and for safety net for their farmers, is evident in the URAA outcome, yet has not served well concerns in agricultural sectors, including interest groups in the United States and EU. We believe that these issues will need to be addressed, particularly with sensitivity to the circumstances of developing countries, if the goals of a Doha Development Agenda are truly to be realized. While it is unlikely that export subsidies, which allow countries to export their instability to the rest of the world, would be in the optimal mix of policies, they are likely to persist until permissible, better alternatives emerge.

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