TOWARDS FREE TRADE IN AGRICULTURE

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Towards Free Trade in Agriculture

by

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Preface

Agriculture seems to be a difficult sector to manage for most governments. Developing countries face tough dilemmas in deciding on appropriate price policies to stimulate food production and maintain stable, preferably low, prices for poor consumers. Governments in developed countries face similar difficult decisions. They are called upon to give income guarantees to farmers whose incomes are unstable and relatively low when compared to those in the nonagricultural sector. These guarantees often lead to ever-increasing budgetary outlays and unwanted agricultural surpluses.

High prices make new investments and the application of new technologies more attractive than world prices warrant, and a process is set in motion where technological innovation attains a momentum of its own, in turn requiring price policies that maintain their rates of return.

Surpluses are disposed of with subsidies in domestic markets or in the international market. Price competition reduces the market share of other exporters, who may be efficient producers, unless they are willing to engage in subsidy competition. This lowers export earnings and farm incomes or depletes the public resources of developing countries that export competing products. Retaliatory measures have led to frictions and further distortions of world prices.

Every so often the major agricultural exporters – the USA, the EC, Australia, or Canada – accuse one another of unfair intervention. Though they have agreed to discuss agricultural trade liberalization under GATT negotiations, if anything, the expenditure on farm support has continued to increase in both the EC and the USA.

Some developing countries do benefit from the subsidized disposal of surplus cereals on the world market. This, however, might be only a short-term gain. Low prices are a disincentive to their own producers and lead, in the long run, to an unsustainable dependence on imports, as appears to be the case in many parts of Africa. Also, these benefits of cheap cereals may not offset the loss of markets, such as the sugar market, which is important to a large number of developing countries.

Against that background and in the light of the fact that many countries have agreed to discuss agricultural trade liberalization under GATT, it is important to assess the consequences of agricultural trade liberalization. It should increase efficiency at the global level as countries adjust their production more in line with their comparative advantages. However, in the absence of

compensating transfers, some countries may lose under liberalization. An assessment of efficiency gains at the global level and gains and losses of countries can provide some insight into the degree to which their own production and trade have become distorted and how large the adjustment costs may be. Several questions are relevant here: what if the developed market economies remove border protection? But also: what consequences can be expected from the removal of border protection by developing countries only? (This is an issue that can be usefully analyzed as it belongs to the regular package of adjustment policies recommended by the World Bank and the IMF.) What would be the impact of simultaneous liberalization by all market economies? Who would gain and who would lose?

This book reports on a study that explored these questions using a system of empirically estimated national agricultural policy models linked together through trade and capital transfers. A general equilibrium approach is followed for both the national models and the international linkage. Thus, behavioral responses of consumers and producers, as well as the responses of government policies to changes in world market conditions, are accounted for.

We call this system of models the Basic Linked System (BLS). It consists of 18 national models, two models of regions – namely, the EC and the Council for Mutual Economic Assistance (CMEA) – and 14 somewhat simpler models of groups of countries. Together these cover all the nations of the world. We believe that the BLS is particularly suited – at least, better than any other existing analytic tool – for the analysis of issues related to agricultural trade liberalization and self-sufficiency.

The present study differs from other available studies on trade liberalization in combining all the following features: a general equilibrium approach is applied to both the national and international levels; most of the parameters are empirically estimated; a number of agricultural commodities are distinguished; nations are distinguished; and a rich variety of policy instruments for national governments is permitted, including tariffs, trade, quotas, taxes, transfers, and stock operations. The existence of these features can significantly alter policy conclusions derived from the analysis.

The development of BLS, without the use of which this study could not have been made, has involved many people in the Food and Agriculture Program (FAP) at the International Institute for Applied Systems Analysis (IIASA) and its network of collaborating institutions. As with any large project that takes many years, it is virtually impossible to give individual credit to all those who have contributed; yet one must try. The program core of FAP consisted of the following:

Kirit Parikh (Program Leader 1980–1986)
Ferenc Rabar (Program Leader 1976–1980)
Günther Fischer
Klaus Frohberg
Michiel Keyzer

The members of the program core have been responsible for all aspects of model development and analysis. Conception of the system and development of the algorithms was done mainly by Michiel Keyzer.

Other program participants who have contributed to development of various aspects of the BLS are: Michael Abkin, Csaba Csaki, Tom Christensen, Odd Gulbrandsen, Janos Hrabovszky, Gerhard Krömer, Bozena Lopuch, Douglas Maxwell, Donald Mitchell, Jan Morovic, Nanduri Narayana, Martha Neunteufel, Karl Ortner, Gerald Robertson, Mahendra Shah, Ulrike Sichra, Ralph Seeley, T.N. Srinivasan, Eric Wailes, David Watt, Chris Wolf, and Laszlo Zeold.

A large number of others were involved in the program, particularly for the development of detailed national policy analysis models for specific countries. Though several of these models have been used in a number of countries, not all of them are currently available as a part of the BLS. Naturally the study has benefited from the country-specific knowledge and evaluations made by many of these researchers.

Other researchers have also commented constructively on various aspects of the system methodology and behavior. Among them are, in alphabetical order, the following: Reinaldo Adams, Harold Carter, Hartwig de Haen, U. Färber, Bruce Gardner, Erik Geyskens, John Graham, John Guise†, Werner Güth, Bruce Huff, Vladimir Iakimets, Raul Jorge, Werner Kiene, F. Desmond McCarthy, Constantine Meghir, Haruo Onishi, Brian Parmenter, Pierpaolo Pierani, Leon Podkaminer, Todor Popov, Alberto Portugal, Allan N. Rae, Bruno Raguét, Sudhaker Rao, E. George Rossmiller, Kozo Sasaki, Stephen Schmidt, Peter Michael Schmitz, Jörg-Volker Schrader, Taisto Sonnensson, Valter Jose Stülp, Stefan Tangermann, Robert Thompson, Anton Timman, Wouter Tims, Paul J.J. Veenendaal, Anton Visser, Matthias von Oppen, Jean Waelbroeck, Anton Wagemeyer, and Cheryl Williamson.

In designing our approach to the study of trade liberalization we have benefited from the suggestions and comments of Bruce Gardner, Bruce Huff, Michiel Keyzer, T.N. Srinivasan, and Robert Thompson.

We have also benefited from the constructive comments of T. N. Srinivasan and Wouter Tims, who read the various drafts of this report.

It is my privilege to gratefully acknowledge the many contributions of all my colleagues at IIASA and the various program participants in the many collaborating institutions. A great deal of credit goes to them; but the authors of this report bear all the responsibility.

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