

The Uruguay Round Agreement on Agriculture: *A Forward-Looking Assessment*

Tim Josling*

I. Introduction

It is generally agreed that the completion in 1993 of the Uruguay Round of trade negotiations marked an historic turning point in the reform of the agricultural trade system. The Uruguay Round Agreement on Agriculture (URAA) put in place a set of rules which has already gone some way toward improving the conditions under which agricultural goods are traded. Bound tariffs have replaced non-tariff import measures, export subsidies have been curbed and domestic programs have been codified on the basis of their potential to distort trade.¹

The Agreement did little, however, to liberalize trade in agricultural products and improve market access. Tariffs on agricultural goods are on average about three times as high as on manufactured goods and continue to distort trade.² The process of “tariffication” has produced a number of tariffs bound at such high levels that it is difficult to see any profitable trade developing in their shadow. Where tariff rate quotas were negotiated to prize open these markets a little, the prospect of quota rents has led governments to agree to a network of bilateral deals which guarantee continued state involvement in trade for years to come. This has in turn exacerbated the problem of competition between state trading enterprises and the private trade. Export subsidies

* Professor and Senior Fellow, Institute for International Studies, Stanford University. This paper was prepared for a seminar at the Organisation for Economic Cooperation and Development (OECD), Paris, October 26-27, 1998.

¹ See IATRC (1998) for a more complete discussion of the Uruguay Round results and Josling (1998) for the need for further reform of the agricultural trade rules.

² The gap for industrial countries is even greater, where the ratio of agricultural to industrial tariffs is closer to ten-to-one.

still exist, and are in effect legitimized to the extent of their incorporation in country schedules. The domestic farm policies of the major industrial countries have been required to make only relatively minor changes to bring them into conformity with the Agreement. Thus the time is ripe for initiating another set of multilateral talks to complete the job started by the Uruguay Round. This paper attempts to assess the significance of the Uruguay Round Agreement on Agriculture (URAA), give a brief indication as to what needs to be done in the next stage of reform, and look forward to the agenda for the next round of agricultural talks which will start in a little over a years time. The organization of the paper makes use of the distinction between three sets of issues which were identified in the Uruguay Round discussions and embedded in the Agreement: “market access”; “export competition”; and “domestic support”.³ In each section there is brief comment on the importance of the URAA to the trade system, the distance still to be traveled in terms of trade liberalisation, and the likely agenda of the next round of talks on agriculture. Some comments are included on the need for further analytical work as a background to the talks themselves. A final section of the paper emphasizes the different starting point of these talks relative to the Uruguay Round and argues for sights to be set high.

Issues which are sometimes thought of as “new” fall conveniently within this now familiar framework. The question of the allocation of TRQs is clearly one of market access, and can be addressed under that agenda item. Countries have indicated a wish to confront the issue of state trading in agriculture, but that topic can usefully be separated into the components of market access (state trading importers) and export competition (state trading exporters). The use of export restraints may also be challenged in the next round, in part as a reaction to the concern over food security in importing countries. But this also can be subsumed under the heading of export competition. Thus by expanding somewhat the definition of the three major agenda items one can incorporate the “new” as well as the “old” issues.

³ The issue of the Sanitary and Phytosanitary Agreement and its possible amendment is not discussed in this paper as this topic is treated elsewhere in the agenda for the OECD meeting.

II. Market Access

Improving the conditions for **market access** remains the keystone of any trade negotiation. Such negotiations will be more straightforward for agricultural goods than in the past. This will be the first set of agricultural negotiations where the level of agricultural protection (at the border) is visible and quantified. Tariffication, as was intended, has made the conditions of market access in agricultural trade significantly more transparent. What is now visible is the high level of protection for long hidden by non-tariff barriers. This level of protection in agricultural markets is exposed as very high relative to the trade barriers in manufactures.

The major market access question for the next round is what process can one initiate that would lead to a removal of this discrepancy in a reasonable time period. How does one get from tariffs of 100-200 or even 300 per cent to the levels of 5 - 15 per cent found in most other areas of trade, or to zero if tariff-free trade is agreed for manufactured goods? This looks to be a tall order: it implies a continued period of significant tariff cuts extending well into the next millennium. But the next Round of talks will not be a success unless a substantial step is taken to reduce these high levels of agricultural tariffs.

A. The URAA and Market Access

The major accomplishment of the Uruguay Round in the field of agricultural trade was undoubtedly the conversion of non-tariff barriers to tariffs for agricultural goods. Bound tariffs are the most transparent trade barrier and the one that is easiest to remove, whether in regional or multilateral negotiations. Agriculture has in this major respect been brought into the mainstream of trade diplomacy. But this progress was achieved at a high price. First, the levels of tariffs agreed were undoubtedly higher than the true tariff equivalent of the non-tariff measures that they replaced.⁴ Second, many developing countries chose to bind “ceiling” tariffs without going through the process of calculating the tariff equivalent for individual commodities. Thirdly, many countries bound tariffs at levels above those that they were applying in their commercial

relations, thus giving themselves some room to increase tariffs without violating their bindings. Fourthly, as most WTO members are also members of free trade areas or customs unions, the tariffs bound in the WTO are usually way above the level at which preferential trade is admitted. The Uruguay Round Agreement instituted tariff rate quotas (TRQs) in those situations where tariffs had replaced non-tariff barriers. For specified access quantities the tariff charged is some fraction of that agreed as the bound tariff in the schedules. The quantity is set to increase over time, generally from three percent to five percent of consumption.⁵ The notion was to provide at least a modicum of market opening where previously the door had been shut. But, however laudable the aim, the existence of a TRQ still does not guarantee that level of imports. As a consequence, additional disciplines may be necessary to ensure access as agreed by the Schedules. Moreover, the TRQ system runs the risk of becoming embedded in the trade rules: it was designed as a temporary palliative, and consideration should be given to its eventual replacement. The act of tariffication has exposed the difference between state trading importers and others. Many countries still channel imports of basic agricultural products through a parastatal import agency (see Josling, 1996a). Under these circumstances the benefits of a tariff-only system are considerably diluted. If the agency decides to keep strict control of imports to support domestic producer prices then the introduction of a tariff in place of a quota will not change the behavior of the agency. Whether or not the tariff is paid, the decision as to how much to import will still be ruled by the amount that can be sold on the domestic market at the desired price. In other words the act of tariffication exposed the issue of state trading as a possible way to circumvent the impact of tariffication. This issue needs to be addressed directly in the next Round.

⁴ This is often referred to as “dirty tariffication”.

⁵ The TRQs are in fact a combination of three elements: the quantity of “current” access (so that tariffication did not actually reduce trade flows); the quantity of trade flowing under pre-existing bilaterals, such as preferential schemes and voluntary export restraints; and the minimum access determined with respect to consumption. In many cases these different elements were consolidated in the schedules.

B. Market Access in the Post Uruguay Round Era

The high tariff levels that were bound in the Uruguay Round for agricultural goods stand out as a major distorting feature of the trade landscape. As a result of the succession of GATT Rounds, manufacturing tariffs are now at modest levels in most of the industrial countries of the world and an increasing number of middle- and low-income nations. Many of these tariffs are of the order of 5-10 percent, and several countries have average manufactured product tariffs of considerably less than 10 percent. Agricultural tariffs by contrast average above 40 percent, with tariff peaks (“mega-tariffs”) of over 300 percent. Table 1 shows the broad picture by commodity, the *ad valorem* tariff for a number of agricultural goods averaged over 20 major trading countries in North America, Asia, Europe and Latin America.⁶ But the averages hide the tariff peaks which effectively block trade. A well known example of such mega-tariffs is that of Canadian dairy imports: the tariff on butter is 351 percent and on cheese is a formidable 289 percent. Even by the year 2000 these will still be at the levels of 299 percent and 246 percent respectively (IATRC, 1994). Poultry tariffs are also above two-hundred percent in Canada.⁷ The US has mega-tariffs for sugar and dairy products, as does Japan for grains, sugar and dairy products. Not to be outdone, the EU has tariff levels of more than one hundred percent for several products, including sugar (297 percent in 1995 declining to 279 percent by the year 2000), dairy (289

⁶ The table shows the unweighted average *ad valorem* tariff of the numerous individual tariff lines relating to the product groups identified. Two cautions should be noted. First, the unweighted average tariff does not distinguish between the importance of the individual items either in the current trade basket or in any potential pattern of trade; and secondly the average omits specific tariffs which cannot be averaged without assumptions about the level of world prices. An ambitious attempt to convert the specific tariffs often found in agricultural trade into *ad valorem* equivalents has been proceeding at the World Bank (Ingco and Hathaway, 1996). This indicates that specific tariffs are often higher than the *ad valorem* tariffs, though this is not always the case. More importantly the Japanese and Korean protection on rice imports is not yet in the form of a tariff, and is not included in the table. Nor is the EU protection on grains, as this is limited to a level below the bound tariff. The bound tariffs can overstate the level of protection actually applied: several Latin American countries apply tariffs which are well below their bound levels.

⁷ Canada has, of course, lower tariffs on most other agricultural import items. An example of a country with consistently high tariffs is India, with an unweighted average bound tariff for unprocessed agricultural goods of 97 percent and for processed agricultural goods of 139 percent. Hong Kong, at the other end of the scale, has bound a zero tariff for agricultural goods, as one might expect in a country with no agricultural production.

percent in 1995 falling to 205 percent by 2000) and beef (125 percent in 1995 though this will decline to 80 percent by the year 2000).⁸

There is little doubt that agricultural protection as evidenced by these high tariff levels remains one of the major distortions in the world economy today. As a result, domestic prices are pushed far above those on the international market. In such instances the allocation of resources among sectors is grossly distorted, and consumers of foodstuffs bear a heavy burden to support the high cost local production. The importing countries themselves have a strong interest in reducing the cost of foodstuffs to consumers and improving the efficiency of their own resource use.

Table 1: Average Unweighted Ad-valorem Bound Tariff Rates Post-Uruguay Round for Agricultural Goods, Twenty Countries

Product	percent	Product	Percent
Grains	46.7	Dairy Products	47.1
Oilseeds	41.7	Sugar	48.7
Fats and Oils	41.6	Fresh Fruits and Vegetables	35.5
Meats	39.3	Processed Fruit & Vegetables	35.3
Milk	40.7	Other Agriculture	24.4

Source: WTO

The TRQ system is also a major concern for the health of the agricultural trade system. A total of 1366 tariff rate quotas were notified to the WTO Secretariat under the reporting requirements of the Uruguay Round. Such arrangements are particularly common in the markets for fruits and

⁸ Many of the EU tariffs are specific rather than ad valorem. These ad valorem equivalents are reported in Ingco and Hathaway (1996).

vegetables (350), meat products (249), cereals (215), dairy products (183) and oilseed products (124). Thirty-six countries undertook such commitments in their Uruguay Round schedules. Among those administering the greatest number of such quotas are Norway (232), Poland (109), Iceland (90) and the European Union (85). One worrying feature of the TRQ system is the degree of “underfill” of the quotas. The simple average quota “fill” for the years 1995 and 1996 was 64 percent and 63 percent, respectively, suggesting that the allocation mechanism is not yet adequate, that parastatals are effectively keeping imports out or that within-quota tariffs are too high to allow imports to compete. Though one can still argue that the TRQs are in most cases an improvement on the non-tariff barriers that were in place before the Round, they pose a potential threat to the further liberalization of trade.⁹

C. Improving Market Access

Several techniques can be used for implementing the improvement in market access that should be at the cornerstone of the new Round. Bold initiatives are probably better than modest proposals, though they have to have some underlying rationale to be credible. The longer term objective should be to minimize the gap which now exists between average agricultural tariffs and those in other sectors. The following modalities could be considered as ways of meeting this objective.

One approach to the issue of improving market access is to use the same base which was established in the Uruguay Round for the next set of tariff cuts (Tangermann, 1997). A further 36 percent cut in the average level of tariffs from the same base would imply a 72 percent cut over the two “reform” periods, a rather significant reduction over a dozen years. This approach would have the advantage of stressing the continuity of the process of reform. It might be simpler to extend an existing agreement than to devise a new market-opening formula. Another advantage of this approach is that the effect on trade would accelerate over time: the same percentage cut would have greater impact the higher the base tariff used. The use of the same base simplifies

⁹ Data from WTO Secretariat based on the first two years notification to the Committee on Agriculture.

negotiations, as a reopening of the issue of the base would itself cause controversy. But perhaps the strongest reason for supporting such an approach is that it simplifies and clarifies the question of “credit” for unilateral moves taken during negotiations. Countries would no longer need to delay unilateral reductions in border protection for fear of “paying twice”: the unilateral policy change would automatically count towards the reduction as it will have always occurred after the base period.

The continuation of the same schedule of cuts, however, poses some problems. First, should the cuts in tariff include a provision, as in the Uruguay Round, which would allow countries to lower tariffs of some line items by only 15 percent while cutting less sensitive (and often less significant) commodity tariffs by more than 36 percent to maintain the (un-weighted) average. Perhaps constraints should be placed on this averaging, by (a) agreeing to a line-item minimum for the whole reform period of (say) 50 percent, which would imply larger reductions for those products that escaped last time; or (b) insisting on a balance in the trade volume between those with higher and lower than average cuts (i.e. trade weighted tariff reductions).

As an alternative to a further round of differentiated tariff reductions, subject to an average, countries could agree on a rule of “no exceptions” to the agreed cut. This then becomes an “across-the-board” tariff reduction. One could perhaps aim at a 50 per cent cut in all tariffs over a five year period. This has the advantage of simplicity and transparency. It could be combined with the technique of using the same base period, or it could apply to the bound tariffs as of an agreed date, say the year 2000. In the past, such across the board cuts have often been riddled with exceptions. This would need to be kept under control. An across the board cut would, however, still leave some tariffs at a very high level.

As an alternative to such uniform cuts, agricultural tariffs could be reduced on a formula basis, with higher tariffs being reduced at a greater rate. The ‘Swiss Formula’ that was used for tariff reductions in industrial goods in the Tokyo Round would be an appropriate technique to use. This could be a faster and fairer way to get liberalization than the across the board cuts. Much of the ‘water’ would be squeezed out of the high tariffs (and the element of ‘dirty tariffication’

removed) by such an approach.¹⁰ The main advantage of using a formula approach is that it would reduce the distribution of tariff levels among products. The process of tariff reduction in the Round may indeed have increased the variance of tariff levels.¹¹ But formula reductions appear to put more of a burden on those countries with dispersed tariff rates, and they might be expected to argue for more uniform cuts.

A somewhat different approach to the issue of tariff reduction has had some success in other areas of trade, such as information technology. This approach is to negotiate “zero-for-zero” agreements that would eliminate tariffs completely on particular goods.¹² Clearly there are advantages as well as disadvantages in such an approach. Political sensitivities restraining liberalization in some products such as dairy and sugar would not hold up a move to competitive markets in others such as oilseeds and pigmeat. Trade would therefore be expanded in the latter markets as protection was reduced. However, the benefit of this trade from the point of view of both the importing country and the world as a whole would be offset by the costs of trade diverted as zero-tariff items replaced the lower-cost but higher-priced goods still subject to tariffs.¹³ The zero-for-zero approach rests in part on the notion that the isolation of the markets that are presently highly protected will force them eventually to come into line. Unfortunately, it is equally likely that one might “let off the hook” the sensitive commodities unless the sector-by-sector reductions were in a framework that ensured no long-term exclusions.

¹⁰ The ‘water’ in a tariff is the unused protection when no imports can sell at the tariff inclusive price. The ‘dirty’ element in the agricultural tariffs refers to the use of price gaps between domestic and world markets which overstated the existing protection at the time of tariffication, leading to larger than necessary tariffs. Tariff bindings were also often set well above the actual tariff in operation, giving an element of discretion to governments. Thus a reduction in the high rates of tariff removes the water, cleans up the tariff and removes the discretionary element of ceiling bindings.

¹¹ This was the case, for example, in the EU, Japan and the USA. See Tangermann (1995). As an alternative approach to the problem of tariff dispersion, a maximum level of tariff could be agreed to which all higher tariffs would have to be reduced over an agreed period. This could be combined with an across the board cut to give both a general reduction as well as a consolidation of rates.

¹² This approach is discussed more fully in Miner *et al* (1996).

¹³ The EU knows well the problem of “unbalanced” protection as a result of easy access to oilseeds negotiated in the Dillon Round.

An alternative way to tackle the problem of the high levels of tariffs resulting from tariffication is to expand the guaranteed market access which forms a part of the provisions of the Agreement on Agriculture. Removing the TRQs may not be an attractive option for the exporting countries. Expanding them, however, is one simple way of reducing their importance, at the same time lessening the impact of the high 'above-quota' tariffs. Doubling the minimum access quantities, for instance, would make many of the high bound over-quota tariffs irrelevant.

One possible approach is to continue the process of expanding minimum access as a proportion of consumption. An increase in TRQs, say, of one per cent of the level of domestic consumption in each year over a five year period would remove much of their restrictive effect. In most markets the quotas would become non-binding before the five-year period was over. In effect, tariffication would have taken place at the level of the reduced tariff applicable to the TRQ.¹⁴ The main political objection to this could be that the "within quota" tariffs were generally left to the discretion of the importing country to fix at levels which they judged would attract the guaranteed access quantity. This implies that some form of re-negotiation might have to take place on the level of these tariffs.¹⁵

The question of the allocation of TRQs has received some attention. Not only has the allocation been very different in different countries, but in some cases the method chosen seems to have been calculated to counter the market opening (see Hathaway and Ingco, 1997). It may not be possible to agree on a single method of allocation, but a set of acceptable methods could be agreed. These could range from such economically efficient methods as auctioning to the exporting firms, to the administratively simpler allocation on the basis of historical trade patterns.

¹⁴ It would also be possible to devise a way to give countries the option of TRQ increases or tariff decreases, as both lead to the same desirable end..

¹⁵ This of course also offers a possibility to start such tariffs for within-quota trade at a reasonable level in relation to other goods. All "within quota" tariffs could be bound at (say) 20 percent, and not reduced until they became the operative tariff for the bulk of agricultural trade.

The issue of state trading enterprises that have special or exclusive rights in import markets can be thought of as an extension of the problem of market access. Under WTO articles, state trading importers are not supposed to grant more protection than that given by the bound tariff (Article II:4, GATT 47). This was difficult to enforce when non-tariff barriers were allowed in agricultural markets. The state trading enterprise could be deemed to be administering such a non-tariff barrier. But with tariffication the situation is much clearer. The task of comparing the markup of the state trader with a fixed tariff is relatively straightforward, in particular in the light of the improved monitoring and reporting which has resulted from the establishment of a Committee at the WTO to oversee the implementation of state trading rules.

Countries could however go further than just ensuring that state trading importers do not give more protection than the bound tariff. It would be possible for instance to link the administration of the TRQs with the import operations of state traders, perhaps converting the TRQ into an obligation to import rather than an opportunity. This could reduce the suspicion that STEs might be responsible for the under-fill of the quotas. At the other extreme one could mandate that all (or a share) of the TRQ be marketed through private channels, thus providing some competition for the STE and allowing price and markup comparisons to be made. Ultimately, one could directly address the issue of competitive conditions in the importers market, by ensuring a degree of contestability in such markets, but that is likely to wait until basic trade rules for national competition policies have been agreed.

D. Analytical Issues

One obvious analytical issue related to market access is the comparison between alternative modalities for tariff reduction. The technique used will be based on many considerations, not least the impact on major countries. But it is possible to rank the methods of increasing market access according to the extent to which they generate gains from trade and improve the efficiency of world markets. One such issue which needs to be explored is that of “zero-for-zero” tariff reduction agreements. Do these represent constructive ways of moving toward freer trade? Or do they introduce new distortions between those products which are included and those which are

not? Another issue is to what extent the expansion of TRQs would substitute for the reduction of tariffs. How fast would TRQs have to expand before the high quotas on above-tariff imports would be made irrelevant? Combined with data on regional trade agreements the questions which could be addressed become even more interesting. What is the actual state of market access for agricultural goods when one takes into account the preferential access which most WTO members give to at least some other countries? How does the multilateral reduction of trade barriers change the degree of preference for such trade and therefore alter the economic costs and benefits of regional trade agreements? How are countries with non-reciprocal preferences impacted by the process of multilateral trade liberalization?

III. Export Competition

If the high level of protection sets agriculture apart, the widespread use of **export subsidies** is perhaps the most disruptive element in the operation of world markets. The practice of subsidizing exports of agricultural products has been constrained by the Uruguay Round, but most of the subsidies are allowed to continue in a reduced form. Countries that import agricultural products have been the gainers in economic terms from the subsidies, but even among these countries the disturbance of the domestic market has often caused problems. In the next round of negotiations, it will be more difficult than ever to persuade countries who export agricultural goods with little or no subsidy to allow countries such as the EU and the US to continue their market-distorting practices. A further push to rein in these subsidies is therefore likely to be high on the agenda of the Cairns Group. Similarly, the use of export credits has continued despite efforts to negotiate within the OECD some restraints on the benefits that some exporters get from such schemes.

A. The URAA and Export Subsidies

The Uruguay Round made a solid start to the process of removing export subsidies in agricultural trade. Two aspects are particularly noteworthy: the prohibition of the introduction of new export subsidies and the clearer definition of what constitutes an export subsidy. In addition, the

scheduled reduction in both the expenditure on export subsidies and the quantity of exports that can benefit from the subsidies have led to a reduction in their use. The Schedules establish the level of such subsidies deemed to exist in the base period. This is an important change, in that these base levels replace the "equitable shares" defined under GATT Article XVI:3 and the Subsidies Code, though few would argue that these existing market shares are indeed "equitable". By entering base levels of subsidized exports and of outlays on export subsidies into their Schedules, Members have agreed that the figures contained in the Schedules are an accurate representation of their export subsidization in the past. Hence, for the first time there can no longer be any doubts as to what (maximum) level of export subsidies a country can grant in agricultural trade.

However, several problems remain in the area of export competition. The question of single-desk selling agencies for agricultural products also is tied up with the issue of export subsidies. Different marketing practices among exporters are inevitable, and not in themselves undesirable. But international guidance is needed as to which practices of parastatal export agencies are consistent with agreed conditions of competition and which distort that competition. Now that the more clear-cut kinds of export subsidy have been identified and included in the country schedules of allowable subsidies, the next task is to clarify the definition as regards the actions of state trading exporters. This would ensure that such actions, if deemed to be hidden subsidies, could be counted against the schedule for that country.

The practice of export taxes and export restraints through quantitative controls also needs to be addressed in the New Round, and can conveniently be included under the heading of export competition. Within the GATT export controls are generally disallowed, though export taxes are deemed innocuous. Article XI of GATT 1947 prohibits quantitative export restrictions but makes an explicit exception for "export prohibitions or restrictions temporarily applied to prevent or relieve critical shortages of foodstuffs or other products essential to the exporting contracting party". As exporters do not usually complain about restrictions imposed on their competitors, most export restrictions go unchallenged. But there is a clear conflict between the ability of exporters to withhold supplies to relieve domestic shortages and the reliability of the

world market as a source of supplies for importers. In periods of general tight supply the effect of export restrictions would be to exacerbate the shortage. Moreover, it is inconsistent to ask producers in exporting countries to absorb the risks of low prices without subsidy but then deny those producers the rewards of satisfying a market in times of high prices.

B. The Current Use of Export Subsidies

The use of export subsidies has been significantly curtailed by the high prices of 1995 and 1996. The impact on export subsidy outlays is shown in Table 2. The use of export subsidies for cereals fell dramatically in these two years, with no such subsidies being reported to the WTO in the latter year. Subsidized quantities of exports of dairy products were between 25 percent (butter) and 80 percent (cheese) of the maximum levels allowed in the schedules. By 1996 even these commodities no longer needed export subsidies. Meat products also “required” subsidies on two-thirds of the permissible quantities of exports in 1995 but needed much less subsidy in 1996. Prices returned during 1997 to a more normal level, and the fall in prices in 1998 has threatened to return the situation to that of earlier periods where subsidies were regularly used to sell agricultural products. Coupled with the existence of “unused” export subsidy “entitlement” from earlier years, the need for early action to curb such practices is clear.

**Table 2: WTO Export Subsidy Commitments and Actual Outcomes,
1995 and 1996**

	Quantity (000 tons)		Quantity (000 tons)	
	WTO limit	Actual 1995	WTO limit	Actual 1996
Wheat	58,059	3,710	3,169	0
Coarse Grains	26,920	7,138	3,234	0
Rice	784	99	53	0
Oilseeds	2,712	0	432	0
Vegetable Oils	1,821	202	959	0
Oilcakes	360	0	74	0
Sugar	5,941	897	2,823	173
Butter and Butter Oil	631	155	85	2
Skim Milk Powder	754	399	243	20
Cheese	554	445	105	19
Other Milk Products	1,536	1,267	285	106
Beef	1,526	1,020	421	1
Pigmeat	567	379	24	1
Poultrymeat	658	443	186	0
Sheepmeat	26	1	23	0
Live Animals	33	15	32	11
Eggs	130	97	4	2
Fruits and Vegetables	6,616	1,555	4,422	835

Source: WTO Secretariat, based on Notifications as of November 1997

C. Reducing Export Subsidies in the Next Round

A somewhat similar range of modalities to those in the case of market access is available for dealing with the issue of export competition. Again, there could be distinct advantages in keeping to the base used in the UR and emphasizing continuity. Countries could then move unilaterally to reduce export subsidies and still get “credit” in negotiating terms.

The simplest way to continue the process of reducing the incidence of export subsidies would be to extend the schedule of reductions agreed in the Uruguay Round. As with the market access

improvement, this could be done using the same base. This would imply constraining the expenditure on such subsidies by another 36 percent, thus removing 72 percent of the subsidy expenditure that was used in the base period. Continuing the quantity restriction would imply that 40 percent of the volume of subsidized exports would have been removed from the market over the two periods of reform. But since the remaining 60 percent would have to be subsidized with only 29 percent of the expenditure, the disruption that could be caused by such subsidies would be significantly reduced.

One issue that is bound to come up is that of the “unused” export subsidy allowance. Under the present rules, subsidies not used in a particular year can be held over. The rules can therefore be easily tightened by removing this facility. Why countries should be able to carry-over dumping rights from years when they are not necessary is not clear. Further accumulation of export subsidy rights should not be encouraged. Other issues which need to be raised are the definition of export subsidies, and in particular the issue of “cross-subsidization” among markets.

The continuation of the process of reduction would be constructive, but may not be very ambitious. Elimination of export subsidies altogether would clearly have significant advantages. The pre-requisites for dispensing with export subsidies are a renewed confidence in world markets, with firmer and more stable price levels for the major products, and reduced dependence on intervention buying in domestic policies. The former condition depends on the success of the Agreement in increasing trade and reducing protection. As for domestic programs, it is possible that practice and sentiment in both the US and the EU may have moved away from the use of market support policies to other instruments by the turn of the century. If that were the case it could be politically easier to get effective curbs on the use of export subsidies by the time of the New Round. A new set of negotiations could, say, set the target to phase out export subsidies over a five year period, by 2005.

In the Uruguay Round the issue of export credits was found to be a form of export subsidy, but it did not prove possible to agree on constraints. The OECD countries have negotiated a code for non-agricultural export credits which puts limits on credit terms and the length of credit

extension. It has not been possible to include agriculture in this agreement. This leaves this topic as one to be dealt with in the next Round. It should be possible to agree on the allowable terms for such credit, and hence be able to calculate the magnitude of the subsidy which is involved if softer credit terms are offered. The best way to deal with the subsidy equivalent of such concessionary credit is to charge it against the export subsidy constraints in the schedules.

The quantification of export subsidies and their reduction has left more visible the distinction between those countries where exports are privately sold from those where a parastatal controls such exports. There is widespread concern in those countries where trade is by private firms that the state trading enterprises can obtain cheap credit from their governments, offer better terms to buyers, and generally compete unfairly with the private trade. To the extent that these practices could be labeled as export subsidies, the issue is one of monitoring and transparency. But some commonly used devices such as price pooling (giving the producer an average price over several destinations or time periods) are also seen as benefiting the producer an unfair advantage. It might therefore be a matter for negotiation as to whether any constraints need be placed upon STEs with regard to their producer pricing policies.

Restrictions on exports in times of high prices distort the trade system as much as subsidies that operate when prices are weak. Such restrictions can be through taxes or quantitative restrictions. In the case of quantitative restrictions, these are currently allowed in cases of supply shortage in the producing country. This may need to be revisited. It seems inconsistent to argue that exporters can withhold produce from the market in times of shortage and then to expect importers to open up their markets to trade. Export taxes are not presently controlled under the WTO. But they have a similar effect to that of export quotas, and are equally difficult to justify in an open global food system.

In the next Round, importers are likely to lead a movement to constrain the ability of exporters to restrict supplies. After all restraints on exports are no less inconsistent with an open trade system than restraints on imports. Export taxes should be included under the same qualifications as quantitative restrictions. The argument has already surfaced in connection with the Food

Security Declaration appended to the Uruguay Round Agreement (the Ministerial Decision on Measures Concerning the Possible Negative Effects of the Reform Program on Least-Developed and Net Food-Importing Developing Countries). It seems inconsistent to leave in place the possibility of export taxes and quantitative restrictions that have an immediate and harmful impact on developing country food importers.

D. Analytical Issues

Among the issues which would be interesting to explore in the area of export subsidies is whether the use of price pooling and other forms of cross-subsidization really form a significant impediment to efficient trade and market transparency. Even if such practices were seen to be deliterious to the trade system, the WTO can hardly extend its monitoring and impose its disciplines at the level of internal firm accounting. Can one make a distinction between within-firm cross-subsidies and those that take place across firms within the industry? Is it feasible to make the distinction between public and private marketing agencies in this regard? Is this a case where the problem will exist for as long as market access is so different for different commodities and countries?

In addition to the issue of the use of “internalized” export subsidies, the question of export credit needs to be explored further. To what extent is such credit a distortion of competition and to what extent is it a necessary way of offsetting the inherent financial risks involved in selling to certain countries? The OECD guidelines on credit for non-agricultural goods must be based on some such analysis in those markets.

IV. Domestic Support

It is one of the ironies of the Uruguay Round that, although the biggest conceptual breakthrough was the acceptance by countries that **domestic policies** were a legitimate concern of trade talks, the actual disciplines imposed on those policies through the reduction of the Aggregate Measure of Support (AMS) were rather weak. The key question for the next Round is therefore whether to strengthen or abandon the attempt to constrain domestic policies. The fact that the AMS

constraints have not been binding for the large majority of countries does not mean that the constraints on domestic support have been ineffective. The process of re-instrumentation of domestic support programs, away from those that most impede trade, has begun. The AMS constraint on domestic policy puts useful pressure on countries to continue this process.

A. The URAA and Domestic Programs

The attraction to countries of adopting “green box” policies is both to guard against challenge from trading partners and to avoid being counted toward the AMS. This suggests that the AMS constraint should in fact be tightened to avoid the temptation of backsliding and to promote further reforms. This tightening would make the “green box” much more effective. Exemption from the AMS and avoidance of challenge between them make a powerful case for making domestic policies conform with the green box criteria. The questions under this agenda item are whether to change the definition of the “green box” to avoid some slippage into potentially trade distorting programs such as crop insurance and environmental payments; whether to change the scope of the AMS constraint to make it commodity specific; and whether to continue to allow acreage-control payments to be sheltered in the “blue box”.

B. Further Domestic Reform Needed

The slow but fundamental changes that are taking place in the agricultural policies of the major industrial countries need the encouragement and underpinning of international agreements. The changes in these policies have generally been in the direction of improving the climate for agricultural trade, in contrast to the policy changes in the nineteen-sixties and nineteen-seventies which led to more trade conflicts. The Uruguay Round was able to take advantage of these changes, such as the 1992 Reform of the EU’s Common Agricultural Policy (CAP) and to get firm commitments on future policy directions and support levels. But this process of reform is still at an early stage and needs to continue in order to avoid a swing back toward the costly and ineffective policies of earlier times.

The magnitude of the task ahead can be seen by examining the calculations made by the Organisation for Economic Cooperation and Development (OECD) in their 1997 “Monitoring” report (OECD, 1997a). The size of total “transfers” to the farm sector from taxpayers and consumers as a result of the mix of agricultural policies used by OECD members has changed little in the last decade, averaging \$280 billion in 1986-88, at the start of the Uruguay Round, and rising to an estimated \$300 billion in 1996 (See Table 3).¹⁶ Agricultural policy transfers are greatest in the EU, with Japan and the US transferring income at just over one-half the European level. On a “per farmer” basis, corrected for part-time farming, transfers to Japanese farmers average about \$30,000 in 1996, well down from the previous year but still higher than in the late 1980s. US transfers per farmer have stayed rather constant over the period, at just over \$27,000. (Transfers per hectare are much larger in Japan, however, as a result of the much smaller farm size.) Inflation has reduced the value of those transfers (by 35 percent) and growth in income and population has reduced the burden on the rest of the economy from 2.2 percent to 1.3 percent of GDP. But the absolute size of the transfers to one small and declining part of the economy is still remarkable and vulnerable to both economic reform and straightforward budget-cutting pressures. The transfers effected through specific policies for a more limited range of commodities have for a number of years been captured by the OECD in their calculation of the “Producer Subsidy Equivalent” (PSE), the payment that would have to be given to offset the income effect of a removal of those policies. The total value of this part of the transfer rose slightly from \$160 billion to \$166 billion over the decade (see Table 4). Relative to the value of output, the PSE for the products considered for the OECD member states was estimated at 36 percent in 1996, down from 40 percent in 1995 and 45 percent in the period 1986-88 (OECD, 1997a). Expressed with the border price as a base, the level of protection (called by the OECD the Nominal Assistance

¹⁶ The measure of total transfers includes benefits from price support policies and subsidies as well as all farm-related government spending. Not all the benefit goes to farmers, of course, with input suppliers and marketing agents also being supported. Moreover, new entrants to the sector may already have “paid for” these benefits in the price of land and other assets. Landlords also should be presumed to benefit from higher rental rates as a result of the transfers. These are additional reasons why the move toward targeting and decoupling of payments described below is likely to make transfers more effective in the future.

Coefficient) for producers fell from around 80 percent to about 50 percent over the decade. Calculated on the basis of consumer prices (i.e. not including direct payments) the level of protection fell over the period from 60 percent to 30 percent. However, this improvement is largely the result of firm world prices in 1996, and could easily be reversed if these prices collapse.¹⁷

Table 3: Agricultural Policy Transfers by Country, 1986-1996

	1986-88	1993-95	1994	1995	1996
Total transfers by country					US\$ billion
EU	114.1	132.5	128.5	138.6	120.3
US	68.2	74.1	76.4	62.4	68.7
Japan	62.5	89.9	87.2	100.5	77.4
Canada	7.3	6.1	5.8	5.7	4.8
OECD	278.9	332.1	328.2	332.9	297.1
Transfers per farmer (Full Time Farmer Equivalent)					US\$
EU	12,785	18,657	18,336	19,478	17,474
US	27,892	29,384	30,285	24,742	27,240
Japan	17,280	31,647	29,402	38,440	30,091
Canada	15,742	14,085	13,750	13,318	11,225
OECD	11,100	15,651	15,440	15,955	14,493
Transfers per hectare					US\$
EU	851	953	944	951	825
US	159	174	179	146	161
Japan	11,705	17,553	17,013	19,618	15,107
Canada	99	84	80	78	66
OECD	236	284	280	284	254

Source: OECD, 1997a

¹⁷ These numbers tend to confirm the impression from the unweighted *ad valorem* tariffs of a level of protection of about 40 percent for agriculture as a whole.

**Table 4: Producer Subsidy Equivalent (PSE) and
Nominal Assistance Coefficients (NAC),
OECD Countries, 1986-1996**

	1986-88	1995	1996
PSE (US\$ billion)	159	180	166
PSE (percent)	45	40	36
NAC (Producer Prices)	1.8	1.6	1.5
NAC (Consumer Prices)	1.6	1.4	1.3

Source: OECD, 1997a

C. Re-instrumentation of Domestic Support

The constraints on domestic support through the Aggregate Measure of Support (AMS) are acknowledged to be the least effective of the Uruguay Round bindings. But this does not mean either that they will not be useful in the future or that a continued reduction would not be appropriate. A continuation from the same base would be a relatively modest move, and yet even that would have resulted in 40 percent of the “coupled” domestic support being removed or converted into less trade-distorting types of program. But it would be even more effective to “catch up” with the reductions in import barriers and export subsidies. Thus one could envisage an agreed reduction of (say) 52 percent in the expenditure on price-related policies.

The ‘blue box’ containing the US and EU direct payments which were granted exemption from challenges under the Blair House Agreement was a creature of its time, necessary to get agreement to go ahead with the broader Uruguay Round package. It is, however, still a somewhat awkward bilateral deal not appreciated in other parts of the world. Such an anomaly can surely be removed in the next round. The policies of the US and the EU themselves are changing for internal reasons. The new US Farm Bill goes further than ever before to make the payments to farmers decoupled from output and therefore compatible with the green-box. The EU is considering a similar move as a continuation of the reform started in 1992, as a way of making the CAP consistent with enlargement. The task for the New Round will be made much easier if the EU and US have both

modified their payments such that they meet the conditions laid down in the green box. The “blue-box” can essentially be emptied and locked.

The green box presently contains a number of policy instruments that, while probably less trade distorting than price or income supports still encourage an expansion of output. Sometimes they are related to such otherwise sensible programs such as crop insurance, but incidentally increase the incentive to produce by reducing risk. Other programs may be indirectly linked with production even though the main reason for payment is not output. This might be true of certain environmental payments, which could lead to an increase in output. But to re-open the definition of the green box might, however, allow countries to argue that it be expanded, to include food security policies and barely-decoupled support schemes designed to keep farming in certain areas.

This appears to be where much of the pre-negotiation rhetoric is targeted. The argument is usually shrouded in terms of the “multifunctionality” of agriculture.¹⁸ The concept of multifunctionality is not in itself particularly novel, as agriculture has always played a complex role in rural societies, and rural areas have a vital place in national social and political life. The question is “what does this mean for trade policy?” On the one hand it could merely be a recognition that a variety of programs will be maintained in most societies which target specific aspects of rural life. For the trade system to be seen to rule out such programs would seem to be as risky as seeming to go against concerns of human health and animal welfare. On the other hand, if trade restricting policies were to become the accepted instrument for maintaining multifunctionality then that would signal a regression to the time of expensive commodity market distortions. The green box was intended precisely to deal with such rural concerns. It would be better to confirm the criteria for the green box and encourage multifunctional policies to conform rather than opening the green box up to be a repository for an assortment of production related payments. If some production-related policies were felt to be the only way to achieve domestic

¹⁸ Another paper in this meeting discusses the issue of multifunctionality, and so it is only mentioned here in the context of the “size” of the green box.

objectives (including food security, perhaps) then the blue box, with its emphasis on limiting production increases might be more a appropriate location.

One constructive change in the constraints on domestic support could be a decision to make the AMS specific to individual commodities. This was the original intention in the Uruguay Round: it was at the Blair House negotiations between the US and the EU that the notion of aggregating the AMS over all commodities was introduced – essentially to weaken its impact. The AMS could thus be made more binding at a stroke by defining commodity specific amounts of “coupled” price support expenditure that could then be reduced over time.

D. Analytical Issues

The analytical issues that surround the measurement of domestic policies are very familiar to the OECD. The development and popularization of the concept of Producer Subsidy Equivalent (PSE) has proved useful in allowing more comparisons across countries with respect to the extent to which their agricultural policies support farm receipts. At one stage, in 1987, it looked as if this measure might do double duty as both a domestic policy index and a trade protection indicator. Of course the direct translation into a comprehensive measure which could be used for trade negotiations was always problematic, as the trade effect is not always captured accurately in the subsidy equivalent.¹⁹ The idea mutated eventually to the Aggregate Measure of Support, but the AMS is a somewhat confused hybrid of direct payments and the price effect of administered prices, and has little analytical content.

The PSE should continue to be calculated if for no other reason than it gives a valuable time series of policy effects, in particular when disaggregated into market and non-market measures in a way that has become common. Any changes in definition should lead to a recalculation of past values, as is commonly done with statistics. More elaborate measures such as the Policy Evaluation Matrix (PEM) are useful developments in the context of “multifunctional” policies that attempt

¹⁹ The original FAO work in this area in the 1970s actually recommended the use of tariff equivalents for trade purposes, rather than the PSEs.

to address many objectives. However, the scope for such measures in trade negotiations is limited. What is needed is more research into the link between programs introduced for environmental and other purposes on the structure of production and the composition of output. In this way it should provide a valuable perspective on the up-coming debate about such issues as the preservation of the “European farming model”.

V. The Prospects for Further Reform of Agricultural Trade

There is good reason to believe that the next round of trade talks could take the world a significant step toward global free trade. Although such an optimistic outcome may depend on the full and timely recovery of the Asian economies, the signs are in general more favorable than in the years before the Uruguay Round. The multilateral trade system is in much better shape than in the mid 1980s, when serious disagreements existed as to whether even to hold a new round of trade negotiations. For one thing the existence of the WTO gives the trade system the legitimacy that was lacking in the GATT, together with a stronger dispute settlement process and a policy coordination function.²⁰ The agricultural negotiations will both benefit from the participation of a wider group of countries. Not only are there more members of the WTO now than there were GATT contracting parties in 1986, but many more developing countries have open economies and feel themselves to have a major interest in the talks. The WTO is much more truly global in scope and covers a much greater proportion of world trade than did the GATT. It is in a much better position to chart the course for multilateral trade policy now than was the GATT in 1986.

Coupled with the objectives of the regional trade arrangements for achieving free trade, the WTO can at last define the goal to which all the previous negotiations were hesitantly moving. This goal could be as ambitious as to define the date at which free trade would be the norm. The pieces are fitting into place for a major push toward a liberal world trading system where tariffs are no

²⁰ The popularity of the dispute settlement process is indicated that the WTO has recently begun to consider the 100th dispute. Over half of cases have been initiated in the past three years, and about 60 percent of them concern some aspect of the food and agricultural trade.

longer a significant barrier to the movement of goods among countries. This time it may be difficult to omit agriculture from those plans.

Structural changes in the agricultural and food markets of the world will have a major impact on the next round of trade talks. One of these is the process of intra-industry reorganization that transforms isolated national markets into parts of an integrated global system. This is both driven by firms seeking lower production costs and broader markets over which to spread costs and also a consequence of the relaxation of investment and trade regulations. In other words, the food and agricultural sector is not escaping the pressures of globalization that have swept so many parts of the economy. It is true that agricultural products are rarely assembled from out-sourced materials, as happens with cars and computers. Farmers don't often move their activities offshore to take advantage of lower-wage labor, though it is not unknown.²¹ But through various more subtle changes a similar quiet revolution is underway.

The most notable indication of this change is that the growth in trade in high value added products is much greater than that in homogeneous bulk products. In 1985 trade in high value added products was barely one half of total agricultural trade. By the year 2000 it is estimated that this share will be around three-quarters of agricultural trade. Part of this is due to the effects of rising incomes, as consumers shift away from unprocessed foods. But much of the growth in high value added goods is due to increasing product differentiation as producers and food retailers attempt to convince consumers of the merits of particular geographical locations, recipes and brand names. Goods which were once considered "non-tradable" have found a place in foreign markets for ethnic and exotic foods. Product differentiation, segmentation of the market and quality attribution along with the growth of "non-traditional" trade is the key behind the growth of agricultural exports from many countries in Central and South America as they free up foreign exchange markets and begin enthusiastically to trade. It is also behind much of the rise in US

²¹ Many farmers and farm businesses in California saw the opportunity for the production of fruits and vegetables in Mexico for sale to the US market, even in advance of NAFTA. Moreover there is a large scale movement of feeder cattle across the US-Canada and US-Mexico borders which has many similarities to inward processing and other trans-border transactions.

agricultural exports, including to the old, saturated markets of Europe. Europe itself is enjoying a minor export boom in the same types of commodities, breaking out of the trap which for years had made it focus on a few undifferentiated products such as wheat, sugar, skimmed milk powder and butter which could only be sold with heavy subsidies.

This shift in the type of trade raises new issues that need to be resolved. These include the areas of intellectual property rights on seeds and genetic material, geographical origin protection, labeling of organic produce and of goods containing genetically-modified organisms (GMOs), as well as issues of animal and plant health and human safety. Another round of trade negotiations might well be justified on these grounds alone, regardless of the “old” issues of market access and export subsidies. The probability is high of significant tensions in this area if rules are not clear and widely accepted. Indeed the widespread use of crops that incorporate biotechnology may very soon collide with the equally widespread fears of consumers, often encouraged by those with other agendas, about their safety. Unless public authorities regain the confidence of the public, trade rules that aim to facilitate trade can themselves lose credibility in the public eye.

All these changes are in the direction of a more sophisticated agricultural industry aware that the future depends on satisfying a variety of consumer tastes and competing for the consumer dollar with other goods and services. More actors are becoming involved in the political process, and the center of gravity is shifting perceptibly away from the primary producer. Policy is becoming less “commodity” focussed and the emphasis is switching to adding value to the raw material and marketing the final product. These changes are crucial to the future of agricultural trade policy reform. In a situation where the “market” is an administered price supported by public purchasing agencies, free trade poses a real threat. In a world where farmers produce for the market, improvement in access to overseas markets compensates in part for more domestic competition. A freer agricultural market no longer means a collapse of prices and mass rural depression. Today it is more likely to spark rural entrepreneurship and healthy market development based on response to the changing food habits of middle-class consumers.

Just as the agricultural sector has been undergoing significant structural change, so the challenges faced by the trade system have been mounting. These challenges include the entry of China, Russia, the Ukraine and other countries into the WTO. The issue of the entry of these countries has a strong agricultural component. The prospective new WTO members are major players, actual or potential, in agricultural markets. Under what terms they join will influence the nature of those markets.

There are a few fixed points that give an indication as to the timing of the agricultural talks. The URAA itself mandated negotiations on agriculture to be started before the end of the transition period, i.e. in 1999. But starting the talks does not mean that they will move fast or far without further incentives or deadlines. It would be useful to get the talks off to a fast start, as soon as negotiating authority is received by the major actors, but there will always be elections or market developments which make it a bad time for some country or other to agree to liberalization. One of the few deadlines is 2003, when the Peace Clause expires. Thereafter the general WTO rules governing subsidies and dumping will apply to agriculture. This will presumably give a useful boost to negotiations if they are not complete by that date. The promise to renew the Peace Clause may also be a useful incentive for countries otherwise reluctant to continue reforms.

Does this mean that there will be little incentive to finish the negotiations once they have started? The US in particular is concerned that the incentives to delay are removed. A recent suggestion by President Clinton urged countries to continue the reduction schedule agreed in the Uruguay Round without any pause, while negotiations are proceeding. This is consistent with the approach discussed above of using the same base and percentage targets. The “no pause” policy however is likely to create political problems for those countries who might wish to slow down the reform process: it would seem to be necessary to prejudge the outcome. But there would also be no incentive for those who are seeking more radical reforms to speed negotiations up. Such an agreement would also need a time constraint as well as an initial agreement in principle on the objective. It is not clear how one could achieve all these preconditions.

Perhaps the main determinant of the timing of the agricultural talks is the decision as to whether they should be a part of a large, multi-sector negotiation or whether they will be self-contained. Most commentators argue that a negotiation that only included agriculture would be difficult to conclude. Countries that felt that they stood to lose would have no offsetting gains in other areas. However, no agreement has yet been reached on the scope for the next round, and so it is uncertain what “package” will be possible. Adding another complication, the timing of Chinese accession to the WTO could also influence the agricultural talks, as mentioned above. Though the content of the talks on agriculture is relatively independent of these other developments, the timing could be determined outside the agricultural arena.

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by

Tim Josling

(Professor and Senior Fellow,

Institute for International Studies,

Stanford University.)

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