

State Trading and the WTO:

Agricultural Trade Policy Aspects

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1. Introduction

The issue of State Trading has been around for as long as the GATT. The delegates to the Havana Conference in 1948 gave considerable attention to the matter. Some countries at that time wanted to clip the wings of the state trading enterprises (STEs) that had blossomed under wartime conditions, but too many others relied on these parastatals for control over the “commanding heights” of the economy as well as the management of trade and the opportunity was lost. Others tried to write into the treaty a mechanism to ensure that Central Plan Economies (CPEs), becoming more numerous at that time, built in some target rate of growth for imports to simulate the impact of trade liberalization. This too was rejected, though it has echoes in the way in which some Eastern European countries were later accommodated to the GATT System. But delegates did write into the Havana Charter (in Article 35) a set of rules in an attempt to address the issue of the behavior and monitoring of STEs. Like most parts of the Charter these rules represented an uneasy compromise between the emerging liberal views of the US negotiators and the more interventionist European view.¹ In the end the issue was rendered largely moot by the failure of the signatories to ratify the Charter, with only the convention on goods trade and the

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¹ Anne Krueger has pointed out the “ITO charter contained a great many provisions safeguarding governments’ ability to take trade measures to pursue virtually any domestic objective”, suggesting that it may have been just as well that the Havana Charter was never ratified. See Kreuger (1997).

negotiated tariff concessions surviving as the General Agreement on Tariffs and Trade (GATT).²

The issue of state trading seems however to have taken on a new lease of life in recent months. The imminent accession of China to the WTO has been a major factor in this resurgence of interest. But in addition, trade frictions have sprung up over marketing practices that have been tacitly accepted for years. In the US, Congressional hearings have been held to explore the “unfair” advantage gained in trade by those countries which practice state trading in agricultural products. Senior government officials in the US have argued that this is one of the main items for the agenda of the next set of WTO talks.³ Even in Europe the feeling is growing that the issue needs to be tackled, and for once the US and the EU seem to be on the same side.

This paper attempts to explore some aspects of this issue. The first section discusses the various contexts in the state trading issue seems to be arising. This is followed by an attempt to develop a framework for looking at the issues involved. A further section contains a brief discussion of the treatment of state trading in the GATT and the changes introduced by the Uruguay Round. The paper then discusses the options for further steps to moderate state trading behavior, and a final section looks at some of the links between state trading and other aspects of the WTO agenda.

The Recent Emergence of State Trading as an Issue for the WTO

Why has the issue of State Trading re-emerged onto the trade policy scene over the past two years? Certainly it would be difficult to argue, after several years of privatization and economic reform, that the prevalence of state trading has markedly increased. Indeed the

² The GATT did however include in Article XXIX a general admonition that the Havana Charter provisions would be respected where possible, including the obligations on STEs, and this indeed gives some basis for the renewed attempt to clarify the position of STEs in the trading system.

prevailing notions of economic policy might seem to be removing many of the trade problems associated with the practice. Yet the issue steadfastly refuses to go away, and may actually be getting more contentious.

Three developments may account for much of this resurgence of interest in state trading. First the prospect of full incorporation of the remaining centrally planned economies into the WTO has made countries wary about assuming that trading enterprises in these countries act just as do their counterparts in other countries. This is particularly the case with the anticipated accession of China in the near future and the probable entry of Russia, the Ukraine and other parts of the Former Soviet Union at a later date.

Despite the dramatic economic reforms which China has initiated in the last few years, the heavy hand of government control of the economy still exists. Trade is undertaken by a range of institutions including private firms under license, export-import corporations, local governments and trading enterprises owned by the state and the army. The presumption must be that private firms can not step far outside the rules without falling afoul of the authorities. Under such circumstances negotiated tariff reductions may mean relatively little. Similarly there is the fear that export firms may be able to benefit from hidden subsidies by reason of their close association with the government. Lack of transparency makes it difficult to prove such subsidies, and normal countervail and anti-dumping procedures may be hampered by lack of data.

Secondly, there have been some specific changes in the rules governing agricultural trade as a part of the Uruguay Round Agreement on Agriculture which have brought to the fore certain underlying problems of competition in world and domestic markets. Conversion of non-tariff barriers to tariffs has exposed the difference between state trading importers and others, and new rules on export subsidies have raised issues of whether state exporters have

³ Reuters news agency quotes Richard Rominger, Deputy Agriculture Secretary, as saying that “reform of farm monopolies in China and the former Soviet republics, along with marketing boards in Canada, Australia and New Zealand will be a US priority in the next round of world trade negotiations”. (Reuters, 1996)

an unfair edge in world markets. In addition there has been concern with questions about adherence of countries which practice state trading to their Uruguay Round commitments of market access and export subsidy restraints.

It is clear that much of this controversy comes from the establishment under the Uruguay Round of tariff-rate quotas (TRQs) in an attempt to force state traders to grant some minimum access. This seems to have backfired: some countries have set up state trading agencies specifically to handle the TRQs. One example illustrating the complexity of this issue is that of dairy imports into the US as a part of the opening up of that market. The New Zealand Dairy Board sells its US quota through a subsidiary, thus capturing the rent from the tariff rate quota agreed in the Uruguay Round. Domestic dairy companies in the US complained that this was another example of unfair practices by state traders. In effect the state control of markets was being extended to within the border of the other country. However this can only have any real effect if there are country-specific bilateral quotas in the importing country market. Hence the *fracas* over dairy imports into the US was as much a product of the Uruguay Round tariff-rate quotas as of the existence *per se* of the New Zealand Dairy Board.

Thirdly, the reduction in the role of governments in trade in the market economies has made the distinction between state and private firms more rather than less important. The removal of overt quantitative trade restrictions operated by governments exposes the difference between those firms that have to compete actively for business and those that can run implicit quantitative restrictions through their own exclusive trading rights. This problem lies at the interface of competition policy and trade: the lack of contestable markets represents a distortion of trade and the change in trade policy itself alters the conditions of competition.

The combination of these three developments has led to the possibility that the persistence of state trading poses a threat to the trade system. Distrust of the activities of China within the WTO could lead to an erosion of confidence in the trade rules. A feeling that countries that practice state trading could get an unfair advantage in implementing the agricultural

agreements would stoke the fires even more. If this apparent inequity is not addressed convincingly then the support for further liberalization within the US, in particular, could erode. More ominously, countries not currently state trading might decide to erect parastatals in order to reap the benefits. These outcomes could prove a weakness in an otherwise reformed trade system. State trading would have proved the Achilles' heel of the WTO.

A Framework for Analysis

To analyze these various concerns about state trading requires first that several different issues be clearly distinguished. Although the three developments mentioned above have emerged contemporaneously, and the policy conflicts have come up at the same time, the issues that they illustrate are analytically (and politically) quite distinct. They also involve very different institutions. It makes little sense to treat the limited powers of New Zealand's Kiwifruit Marketing Board in the same way as the lack of transparency of China's COFCO. Table 1 suggests a two-part classification, by institution and issue. The three main institutions involved are state trading countries, such as China, which have to be accommodated into the multilateral trade system; state trading importing enterprises which are common in Asia and Africa and import both agricultural goods and other products such as energy; and state trading exporters, typically marketing boards which sell agricultural products on world markets.⁴

The first issue is one of system compatibility. Do the articles of the WTO rest on the underlying assumption of imports and exports by private firms influenced in a transparent way by government taxes and subsidies on trade? If so, how can one apply the same articles to countries where the decision to import and export is made by government planners and implemented as a part of the overall control of the economy? This issue is as old as the

⁴ It is useful to keep importer and exporter agencies separate as they are covered by different rules in the WTO and engender different political reactions.

GATT, and has come up repeatedly with respect to other central plan economies. As Dam wrote some years ago, “when one considers state trading, the underlying assumption of the GATT system is no longer applicable” (Dam, 1970).

Table 1: Framework for Analyzing State Trading Issues

	State Trading Countries	State Trading Importers in Market Economies	State Trading Exporters in Market Economies
Compatibility with WTO System	<p>are regulations applicable to countries without liberal markets?</p> <p>will countries use non-transparency to gain commercial advantage?</p>		
Conditions of Competition in Domestic Market; Transnational Competition		<p>do they control domestic markets?</p> <p>do they have a monopsony position in imports?</p> <p>do they have market power in world market?</p>	<p>do they control domestic markets?</p> <p>do they have a monopoly position in exports?</p> <p>do they have market power in world market?</p>
Compatibility with Current WTO Obligations	<p>are obligations credible?</p>	<p>do they discriminate among sources of imports?</p> <p>do they give more protection than the bound tariffs?</p> <p>do they “satisfy” domestic demand?</p>	<p>do they discriminate among destinations?</p> <p>do they give export subsidies in addition to the agreed amounts?</p>

The question of China's accession is merely the latest manifestation of the problem. McKenzie, writing soon after China's recent re-application for membership is equally negative: "it would seem unlikely that a GATT-style regulation would impose any effective market discipline on a CPE" (McKenzie, 1990). It is difficult to escape the conclusion that any economy that employs quantitative controls and eschews price incentives on the domestic market can hardly be constrained by restrictions on price-related trade measures such as tariffs. Participation in trade negotiations is equally problematic for such countries: quantitative surrogates for the price effect of trade liberalisation are inevitable. Perhaps the key issue with China is whether the moves toward a market economy which have been made since the 1980s have gone sufficiently far to overlook the significant difference in economic structures that still exist. In other words, when can one stop thinking of China as a CPE and treat it as a country with a large and complex public sector coupled with a heavy-handed bureaucracy.⁵

The second issue is one of competition between private and state-sanctioned firms, and is of much more recent vintage. Do STEs have an unfair commercial advantage in that they can make use of the special privileges granted them by governments? Do they benefit from exclusive powers on the domestic market which give them a competitive edge? This issue has come up above all in agricultural markets, in particular as regards the behavior of export marketing boards. This issue also relates to market power in international markets, and to the possibility that some state trading agencies may be able to exploit their position in world markets and hence distort trade patterns. Although some of the agricultural conflicts, such as the suspicion of the Canadian Wheat Board by farmers in the US, have a long history, the broader issue, that of the international regulation of the degree of contestability

⁵ The recent announcement of the reduction in the number of public corporations from 14,000 to 3,000 is an indication of the direction in which the economy is moving. However the state owned firms that will be left will include some very large enterprises. Administrative control over the activities of private trading firms will still exist.

of markets, including internal markets, is relatively new. Competition policy as a needed adjunct to trade rules has only emerged as the trade system has reached a certain stage of international market integration (or globalization). One could hardly imagine a serious debate even a decade ago on the extent to which anti-trust laws should be harmonized across countries.

The third issue identified in the table is the least explored aspect of state trading. It has to do with whether state trading enterprises in otherwise market economies can provide protection to domestic sectors which is unbound and not subject to negotiated reduction. This issue has come up again particularly in the agricultural area, as countries have converted explicit non-tariff barriers to tariffs and hence exposed the implicit non-tariff barriers operated by state importing agencies. As such it is also of long-standing concern. However the state of agricultural markets prior to the Uruguay Round were such that it was impossible to say which problems were caused by state traders and which by government policies. In that sense the issue looks new but may be just the latest manifestation of a set of policies which have been around for many years.

In this case the distinction between the importer and the exporter issues is particularly useful. As discussed below, there are some explicit criteria for examining the question as to whether state trading importers are acting consistently with respect to the WTO obligations of their governments. For exporters there has been much less discipline until recently, but with the inclusion of limits on export subsidies in the bound schedules of each country the obligations of exporter state traders becomes more clear.

In what follows the emphasis will be on the last of these three sets of issues, that of compatibility of state trading with the current obligations of countries under the WTO. The issue of China's accession has been well covered elsewhere (see Morici, 1997) and in any case is in a state of flux as negotiations continue. The question of competition policy extends well beyond state trading enterprises and is mainly concerned with the actions of private trading enterprises. It is the third issue which is more subtle, and threatens to lead to

conflicts which could reduce confidence in the Uruguay Round outcome and thus perhaps begin at least in some key areas to undermine the credibility of the WTO system.

State Trading and the GATT

The GATT Articles that were rescued from the Havana Charter dealt somewhat incompletely with the issue of state trading. Nevertheless the Articles did try to impose some specific criteria for the performance of state trading enterprises (STEs).⁶ These criteria were (and are still) as follows:

- (i) that STEs should be subject to the GATT principle of non-discrimination, and therefore not discriminate among sources of imports or exports (Article XVII:1(a)),⁷
- (ii) that they should act on the basis of “commercial considerations” (Article XVII:1(b)), with respect to “price, quantity, availability, marketability, transportation and other conditions of purchase and sale”, and should “afford the enterprises of other contracting parties adequate opportunity in accordance with customary business practice, to compete in such purchases or sales”,
- (iii) that importing state traders should not grant protection above that given by the bound tariff Schedules (Article II:4), and
- (iv) that limits on the use of quantitative restrictions specifically extends to import restrictions by state traders (Interpretative note).

These provisions have generally proved inadequate to curb the activities of state trading enterprises and have been weakly enforced. The contracting parties of the GATT were expected to inform the Secretariat of the existence of state trading enterprises, but relatively

⁶ It is important to note that government imports for its own use are not covered by the GATT article on state trading. This is discussed in the final section of the paper.

⁷ There is some debate over whether the admonition to act in a non-discriminating way also implies that “national treatment” should be given to imports by STEs. Even when the importing arm of an STE practices non-discrimination, the domestic selling arm could discriminate against the imported product.

few countries made the effort, and the questionnaire developed in 1960 to be used for notification was somewhat undemanding. This led to several attempts over the years to strengthen and make more specific the constraints, but the efforts have so far proved fruitless.

A number of fundamental problems underlie this lack of success. First, the GATT lacked a clear definition of what activities or enterprises came under the rubric of state trading.

Article XVII applies in cases where a contracting party “establishes or maintains a State enterprise, ..., or grants to any enterprise exclusive or special privileges” involving imports or exports. But a definition of a State enterprise is not given, nor are the privileges defined. In effect, governments have interpreted the definitions in their own ways, to suit their own purposes.

One might suppose that at least there was no doubt that trading enterprises in central plan economies would come under the heading of STEs. But even this was not clear cut. Poland, in its 1972 notification declared that it had no state trading entities, arguing that its trading agencies followed commercial practice and had no exclusive privileges. Over time the scope of Article XVII appeared to be limited to developed countries, and central-plan economies were dealt with in a different way by retaining the right to impose quantitative restrictions if exports trade became too unbalanced. Countries where all trading was by the state, or under sufferance from the state, seemed not to come under the basic state trading rule.

Second, the GATT rules were less than precise as to what behavior of state trading enterprises (STEs) was to be sanctioned and what condoned. The admonition to use commercial considerations has been difficult to interpret. As many commentators have pointed out, it is not easy to see why countries should go to the trouble of setting up state trading enterprises just to have them use commercial considerations in their activities. The essence of a state trader is that political considerations are given precedence over commercial (or profitability) concerns. Forcing such enterprises to give up their domestic objectives

seemed more likely to risk marginalizing the trade rules than to change governmental behavior.

The third fundamental problem has been the lack of information on state traders, and hence the lack of quantitative data upon which to take action. The technique used until now has been self-reporting, with governments submitting information on STEs that they have themselves identified. This technique is unlikely to reveal much of interest about the activities of the STEs and may divert attention from the more analytical monitoring which may be necessary.

A fourth factor can be added to these weakness of the Articles. Most STEs trade in agricultural goods, with energy and alcoholic beverages also often traded by parastatals. This has also undoubtedly contributed to the lax enforcement of the existing regulations. As Vernon pointed out some years ago:

Perhaps the first major challenge to the hopes of those that would have reduced state trading to ordinary commercial activity came from the agricultural programs of the advanced industrialized states. Governments in many of these countries had developed programs for stabilizing and supplementing the income of their farmers, and had created state trading agencies to carry out some part of those programs. These state traders in agricultural products usually exercised control over competing imports, acted as discriminating monopolists in the export of products, and drew on the support of the public treasury whenever their costs exceed their revenues. Operating under an explicit mandate from their governments, these agencies as a rule had no great difficulty in resisting the application of the general trade principles to their situation.(Vernon, 1982)

This was however but a symptom of the underlying problem. For if agricultural policies were generally not controlled by trade rules then it would have been anomalous to have tight restrictions on the agencies which carried out the policies. This also gave room for the possible defense of STEs as administrators of non-tariff barriers allowed under Article XI:2. This perhaps more than any other factor has prevented the strict application of Article II:4 to agricultural trade. When dispute settlement panels considered the activities of state importers, such in the case of the Australian complaint against the Korean Livestock

Product Marketing Organization (LPMO) in 1989, they found that Article II:4 did not apply to quantitative restrictions legally applied under Article XI. When quantitative restrictions were present, the comparison of the mark-up and the bound tariff was not appropriate.

The Uruguay Round and State Trading

Despite the unsatisfactory nature of the treatment of STEs in the Articles, the issue was not pushed hard in the Uruguay Round. As Croome points out, the issues of the definition of STEs and the monitoring of their activities were raised, but in a relatively low-key way (Croome, 1996). Countries seemed generally to agree to an attempt to clarify the definition and make the monitoring more rigorous. The definition was refined to be more specific, including:

“Governmental and non-governmental enterprises, including marketing boards, which have been granted exclusive or special rights or privileges, ..., in the exercise of which they influence through their purchases or sales the level or direction of imports or exports”

In addition each member was to notify the WTO of existing STEs, and a Working Party was set up to review the notifications. The primary thrust of the Working Part to date has been in improving the “transparency” of such STEs and their activities through the notification process and through the challenge and counter-notification of STEs.

The main focus in the Uruguay Round talks on agriculture was of course on the more visible and less structural aspects of policy, such as conditions of market access, export subsidies and domestic support payments.⁸ These aspects of the agreement did however have a profound impact on the issue of state trading. They both exposed the problem and made possible the solution.

⁸ For a full discussion of the Uruguay Round Agreement on Agriculture, in the context of earlier attempts to write rules for this sector, see Josling, Tangermann and Warley (1996).

The conversion of non-tariff barriers into tariffs, and the binding of those tariffs, was clearly the most significant outcome of the Uruguay Round Agreement on Agriculture. But the process of tariffication itself highlights the issue of state trading. Tariffs presuppose a certain form of market structure and trade institution to be effective. They work best in situations where private traders operate in a competitive market environment. Many countries still channel imports of basic agricultural products through a parastatal import agency. 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 existence of a tariff in place of a quota will not change the behavior of the agency. Whether or not the tariff is paid, presumably as a transfer from one arm of the administration to another, 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.

For this reason the Uruguay Round Agreement also instituted tariff rate quotas (TRQs) in those situations where tariffs had replaced non-tariff barriers. For specified access quantities the tariff charged would be some fraction of that agreed as the bound tariff in the schedules. The quantity would increase over time, generally from three percent to five percent of consumption.⁹ The notion was to provide at least a modicum of market opening where previously the door had been shut.

However laudable the aim, the existence of a TRQ still does not guarantee that level of imports. STEs could still restrict trade below that level. Moreover, this mechanism might itself introduce or sustain behavior in the market which is less than competitive. The rents to be captured on the sale of the TRQ on the domestic market are likely to be substantial.

⁹ The TRQs are in fact a combination of three elements: the quantity of “current” access (so that tariffication does not actually reduce trade flows); the quantity of trade flowing under 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 are consolidated in the schedules, and are distinguishable only by the reservation of some trade flows for particular countries.

Though the existence of rents does not in itself imply imperfect competition (competitive traders could all bid for the import rights and the rents go to the government) the incentive is there for private firms to collude or for governments to assign those quotas in a non-competitive way. State trading agencies in the exporting countries could for instance capture the rents attributable to the import quota in the importing country - as indeed has been the case with the US TRQ on dairy products.¹⁰

The part of the Uruguay Round Agreement that constrains export subsidies also has a potential impact on the activities of state traders. Fixing maximum levels of export subsidies presumes that such subsidies are paid visibly to private firms and are a matter of public record. In a competitive market, private firms would bid for such subsidies subject to the WTO ceiling. Many countries, however, still operate policies which grant monopoly powers to an export agency, and hence can hide export subsidies from public scrutiny. Under these conditions the restraints on export subsidies may fall harder on those countries and on those commodities which do not have such parastatal export agencies. The question of state trading in export markets has indeed become more of an issue as visible and measurable export subsidies are reduced.

Compliance with Current Trade Rules.

The key issue then is whether state trading allows countries to circumvent the constraints imposed by the Uruguay Round. Just as tariffication has exposed the issue of state importing it might also have clarified the solution to this particular problem. In particular the abolition of non-tariff barriers has reduced the legitimate functions of the parastatals in agricultural markets. The little-used article in the GATT/WTO that states that no mark-up from a state trading importer should be larger than the bound tariff (Article II:4 of the

¹⁰ Even where tariffs have been bound and no TRQ exists to encourage non-competitive behavior there is still room for government activity. The practice of choosing “ceiling” tariff bindings for a large number of developing countries at well above their current levels leaves open the possibility of managed trade. Countries

GATT) could now come into its own. In the past countries were able to circumvent this by claiming that the parastatal was administering a non-tariff barrier. In any case, relatively few agricultural tariffs were bound. In a regime of bound tariffs and no non-tariff barriers this defense collapses. It should be fairly straightforward to compare mark-ups with bound tariffs in the future and hold state traders to sell imports on the domestic market at no more than the border prices plus the tariff.¹¹

Moreover in this situation countries must also abide by the language of the Havana Charter which mandated full disclosure of import costs and profit margins of state import firms (Article 31:4), and stated that the agencies themselves must import supplies adequate to meet “full domestic demand” for the product (Article 31:5). The applicability of the Havana Charter in this case has been confirmed by panel findings. A strict interpretation of these provisions would make it very difficult for countries to use such agencies for substantive protection of the domestic market.¹²

The question of the violation of the rules of international trade comes down to a straightforward comparison of how the actions of STEs match up to their obligations. STEs in import markets have the obligation to satisfy local demand for the imported product and a rigid constraint, to avoid giving more protection than the bound tariff. In addition there is the more general injunction that they should behave like commercial concerns, and they are supposed to respect *mfn* principles. Thus the analytical issue is therefore whether local demand is satisfied and whether the operation of the STE grants more protection than the

for instance are able to run variable levy and price band schemes which apply additional taxes to imports at times of low prices. These in turn encourage non-competitive behavior on the part of the exporter.

¹¹ This approach highlights the importance of reducing the very high rates of tariff: there is little point in holding state traders to such disciplines if the tariffs are too high to allow any trade.

¹² This would move far beyond the binding of the mark-up as already incorporated for countries such as Japan and Korea in the Uruguay Round schedules. Indeed the process of tariffication should have already done this for most countries. So long as the quantities of imports do not respond to the reduction of the tariff or mark-up, the benefits are not felt by other countries. Only the size of the transfer between domestic consumers and taxpayers is affected. But by comparing import and domestic prices and requiring imports until the difference does not exceed the bound tariff means that the state importer will in effect be acting as if there was private trade over a fixed import tariff.

bound tariff. The question as to whether they act commercially is best thought of as a combination of the two more precise conditions: if they import to satisfy the level of domestic demand which would face a private importer paying the bound tariff they could be deemed to be behaving “commercially”.¹³

STEs are subject to the constraint in export markets that they should not grant export subsidies that would exceed the allowable subsidies in the Schedules. The general injunction to behave commercially applies to STEs, but this can be taken to be a shorthand for a prohibition on the granting of subsidies. The analytical issue is therefore whether the STE in question grants an implicit export subsidy that is within the limits of the Schedule.¹⁴ (A note on the issue of measurement is included in an Annex to this paper).

The dilemma for agricultural trade is that though privatization may lead to tariffication, the reverse is not necessarily true. The problems in agricultural markets suggested above are a manifestation of this asymmetry. Tariffication in itself is only a first step towards the introduction of competition, and may need other actions to support it. These other actions undoubtedly include the regulation of the incidence of effects of state trading.

Controlling State Trade in the Future

If the main argument of this paper is correct the issue of state trading will come up at the multilateral level in a number of guises. It is already beginning to emerge at the regional level. One approach is to address the legality of the existence of state trading agencies . Despite widespread adoption of neo-liberal trade policies, in particular in Latin America, it still seems implausible that the members of the WTO would opt for an outright ban on state

¹³ To place further restrictions on importing STEs as to their behavior in dimensions other than import quantities and prices would seem to be outside the spirit of the WTO.

¹⁴ This is really a double test, as the exporting STE would have to comply with both the quantity and expenditure provisions of the Schedules. It is quite possible that an STE could grant a subsidy which in value terms did not violate the Schedule limits, but the quantity that benefited from that subsidy could be above the quantity allowed to be subsidized. If the CWB spent even \$100 on subsidizing exports could any of the sales by that agency be held not to have benefited from that subsidy?

trading. Too many countries would have to abandon too many powerful domestic agencies. Though the existence of different institutional structures in world trade can clearly lead to trade frictions, it is not clear how far one can proceed in the direction of harmonizing institutional trading structures as such. The most one could perhaps hope for is an agreement in principle that such agencies should not be created anew without some form of compensation to affected parties.

A second approach is to regulate directly the behavior of STEs. Current WTO articles try to regulate behavior in general terms, without notable success. In this regard the changes particularly in the agricultural sphere should enable a renewed effort to be made to discourage the use of state trading either for under-the-table export subsidies or hidden protection of domestic industry. One could for instance address directly the price enhancing ability of the parastatal. The tariff equivalent of the state import monopoly could be calculated, and then bound and reduced. Indeed the process of tariffication should have already done this for agricultural goods. But so long as the quantities of imports are not allowed by the STE to respond to the reduction of the tariff or mark-up the benefits will not be felt by other countries. In this case the parastatal might be deemed to be employing a non-tariff barrier, though whether one could ever uncover the quantitative decision is problematic.

A third and more radical approach would be to regulate the competitive environment in which the state traders operate. This would entail an attempt to regulate the use of market power in trade by parastatals. The question is what can one do and how can one do it? The most direct way is to end the monopoly on imports by state trading agencies. They could continue to exist but not have exclusive import rights. Countries could for instance agree to allow private firms to compete with the state trading body as a component of the further liberalization of trade. For example the TRQs arising from tariffication and the minimum and current access provisions could be allocated to the private sector and not to the parastatals. This would incidentally improve the ability of other countries to monitor the performance of parastatals and generate some vested interest in liberal trade within the

importing country. Allowing private firms to compete with the STE is on the increase. Many marketing boards in developing countries have been reformed recently to allow the private sector to compete in the export market.

Another potentially effective way to reduce the market power of a state importer is to expand the quantity of imports, under a minimum access scheme, until the monopoly power has no effect. The TRQ mechanism, or some similar quantitative device, could well prove an effective approach to the issue of state-controlled imports. The rents associated with the TRQs may be an invitation to state trading at present, but they could also be a step toward the replacement of state power by private trading. The key is to expand the TRQs beyond the quantity which the state trader would choose to import. Expanding TRQs weaken the parastatals' ability to keep prices high only when the point is reached when the lower tariff of the TRQ becomes the determinant of the quantity imported. Obligatory imports would in this way erode the quantity control aspect of managed trade.

In the case of exporters, another tack is likely to be required. The first issue is to consider whether the exporting board is in fact inconsistent with liberal trade. If the state agency can control (i.e. restrict below the competitive level) all sales of a particular country or region then there may be good reason for this to be treated as a matter of export restriction, which at least in principle is frowned upon by the WTO (in Article XI of GATT 47). However this situation tends not to cause problems overseas - foreign competitors would hardly object to the quantity restrictions of the marketing board. Only if the monopoly power of the state trading exporter extends to international markets, and can therefore influence the sales to and from others, might some degree of regulation at the international level seem warranted. More usually the export monopoly sells into a competitive market, and there is little reason for the international community to be concerned about the implications. Trade liberalization by opening up markets will weaken the power of particular exporter marketing boards, and any restriction on domestic production in these circumstances will rebound to the disadvantage of the domestic producer.

The issue of state trading exporters that is likely to appear on the agenda for the next round of trade talks arises not from the restrictive use of monopoly power (as in the import situation) but from the opposite phenomenon, the covert subsidization of exports. US farmers complain that the CWB undercuts them in foreign markets, not that they hold back Canadian grain to get a better price. The issue is therefore a straightforward one of measuring and restricting export subsidies. The practice of financial assistance to exporter boards is explicitly included as an export subsidy in the Uruguay Round Agreement, and the sums involved in the past should have been entered into the schedules. Countries can continue to subsidize up to this level with impunity. If the process of restricting such expenditures continues then the issue of the subsidized marketing board will vanish.¹⁵

Links with other Areas of the WTO Agenda

The linkages between the issue of STE and the agricultural agreement have been emphasized above. In addition there are important links with other aspects of the WTO. Of these the most important is with the area of competition policy, rapidly becoming a topic for future negotiations. Substantive links also exist with government procurement policy as well as with the issue of technical barriers to trade, often enforced by parastatals.

Of these the most significant link is with the issue of government procurement. Extensive amounts of trade bypass all GATT disciplines. The Tokyo Round Government Procurement Code made an attempt to bring specific areas of government procurement under some semblance of trade rules, but not all countries signed the Code. Negotiations held in parallel with the Uruguay Round tried to take the issue a step further, and the scope of the Code was modestly extended. However, unlike many of the other Tokyo Round Codes the government procurement agreement was left out of the global package and remains only applicable to those (mostly developed countries) who have chosen to sign it. As a result it

¹⁵ Some state export activity arises from the presence of state importers and some from the existence of export subsidies in other countries: removing the monopoly power of the importing parastatal and curbing export subsidies may reduce the attractiveness of the export board as a marketing device.

may prove difficult to frame any revision of the STE articles to cover government procurement.

The link between state trading and government procurement is in any case complex. At a superficial level it may be difficult to separate the role of state agencies in their purchase for their own use and their buying for the market. Governments and government agencies consume large quantities of imported products, and these imports are often purchased directly. But in addition it can be argued that whenever a government agency purchases an importable good it influences the conditions of international trade. It can choose from which country to import, avoiding normal GATT obligations, and whether to grant preferences to local suppliers (unless a signatory to the Code, in which case a limited form of “national treatment” may apply). Many of the same issues arise as with state trading. It is not difficult to imagine a long term solution which covers the activities of parastatals in the market place which would apply regardless of whether the consumer were “government” or the “market”.

Another complication which arises when revising the rules on state trading is that of the regulatory function of state bodies. There are therefore direct links among the state trading issues and those relating to technical barriers to trade (TBT) and, in the case of agricultural products, to sanitary and phytosanitary standards (SPS). The complication arises from the fact that if the same body is given authority to both trade and regulate then separating the two functions may be difficult. Controlling supplies coming on to the domestic market through the issue of licenses may no longer be legal, but if the agency which formerly issued licenses based on domestic market conditions still has to agree to the imports to avoid the importation of pests the net result may not be too different. It remains to be seen whether the WTO can handle the numerous cases of bureaucratic impediments to trade.

Conclusion

The Uruguay Round Agreement made a marginal improvement in the treatment of state trading, by improving the definition and tightening the monitoring requirements. However the potential problems posed by the accession of China and Russia, coupled with the renewed tension over state trading in agricultural goods, have made it likely that more will have to be done to prevent the issue from undermining confidence in the WTO.

The Agreement on Agriculture, in converting all non-tariff trade barriers to tariffs may have inadvertently exacerbated the state trading problem. All private trading countries will be subject to the process of liberalization over time as tariffs are reduced. State trading countries may be able to continue with instruments that restrict imports unless they are held to account. All visible export subsidies will have been removed, but hidden export assistance through state trading enterprises may remain unless rigorously monitored. Moreover, the removal of direct government intervention in agricultural markets at the border has in some cases revealed a web of state trading arrangements. The control of the activities of STEs will prove substantive items for the agenda of future trade negotiations at both the regional and the multilateral levels.

Fortunately the mechanisms for dealing with the issue of state trading are readily to hand. A strict interpretation of the provisions of Article II: 4, coupled with the act of tariffication, should constrain all state trading importers to act in a way that does not restrict imports more than would the bound tariff. Exporting state traders are constrained by the restrictions on export subsidies agreed in the Uruguay Round. The measurement of the level of protection given by STEs, in the form of a tariff equivalent, and the extent to which they subsidize exports, which can be expressed as an export subsidy equivalent, is straightforward to calculate.

The obligation to respect the bound tariff does not in itself offer much hope for further market access in agricultural goods in the short run. Tariffs are too high in many cases for this constraint to be binding. This suggests that an approach through the expansion of TRQs

might be desirable. This would have the benefit both of expanding market access and of reducing the need for state trading to be retained or introduced just to administer the TRQs.

In the longer run the issue of state trading needs to be considered as a part of the nexus of competition policies and government procurement. Identifying and monitoring the activities of STEs may not be enough to prevent distortions in the domestic and foreign market.

Applying rules that ensure that government agencies operate in contestable markets may be the appropriate long term goal for the trade system.

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