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EU Farm Subsidies and the interests of Developing Countries

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1. Introduction

The call for reform of industrial country's agricultural policies since the mid 1980s has been led by net food exporting countries including some of the developing countries. They see their prospects for trade being damaged by government intervention in many countries, including the EU, and have campaigned for reform. Much of the debate has been conducted at the level of agriculture in general rather than at the specific commodity level. However, recent statements by the EU Trade Commissioner, Mr. Pascal Lamy, have given a much sharper focus to the debate. His general stance is that liberalisation of agricultural trade policies would be beneficial:

> ***"What we can do, and what we must do, is to make sure that the way we support our agriculture is not harmful to developing countries; for instance, in providing total market access"***
>
> (World Bank Video Conference, 6 August 2003)

To this end, Mr. Lamy has a specific mandate to remove export subsidies on agricultural products where possible, but within an environment in which all countries start to reform their trade policies.

The overall and detailed pattern of comparative advantage and net trade position in food and agricultural products varies vary markedly across developing countries. Some are large net food importers, some large net exporters and some for which the net trade balance is small either way and varies over time. Further, there are potentially significant consequences for other trade policies and trade agreements. The most notable example here are the Protocols of the Lomé Convention, which provide many developing countries with guaranteed market access to the EU but crucially also offer prices to exporters that are related to those paid to EU farmers under the CAP. As the CAP is reformed, the benefits of the Protocols are likely also to be affected and again as Milner and Morgan (2003) show, there will be some who lose and some who gain from such reform. It is critical therefore that developing countries identify commodities of general export interest.

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[1] This is a shortened and modified version of a Report commissioned by the Commonwealth Secretariat on "EU Farm Subsidies and the interests of Developing Countries" by Professors Chris Milner and Wyn Morgan of the School of Economics, University of Nottingham. The views expressed here are not necessarily shared by the Commonwealth Secretariat.

2. Agricultural Export Subsidisation by the EU and Industrial Countries

The support given to farmers in many OECD countries, including those of the EU, takes many forms and is intended to achieve a number of different goals. The choice of policy instruments is very wide, ranging from income support, through price support and onto border measures either to limit imports or to remove surplus production via subsidised exports. Many countries use a combination of these instruments as part of their agricultural policy and there is a great deal of interdependence between them as a result. Unbundling one instrument from the rest does not necessarily lead to a simple pre-determined outcome and so attempts at reform must take into account the mesh of policy design. The common feature of all such policies though is that they act as an intervention into a free market and the resulting outcomes are often some way from market-determined equilibria. The implications of these distortions for budgets and trade can be significant, creating tensions amongst taxpayers, policy makers and trading partners alike.

Explicit and Indirect Supports

A distinction can be made between the explicit and implicit subsidisation of exports. Explicit subsidisation is the case where exports are sold onto the world market with the direct payment of a subsidy by a government agency. In this case, a specific amount of subsidy is defined such that a per unit, total value or total volume of subsidised exports is explicitly stated. In contrast, an implicit subsidy is where exports are sold onto the world market without a subsidy payment but where exporters can afford to receive the lower price due to the returns they obtain from the high (institutionally set) domestic price. Here there is no explicit statement of export support but because other domestic support policies exist that create an incentive to over-produce for the domestic market (such as a guaranteed price), exporters can use this to act as an implicit support for their export activities, a support that would not have existed in a free market, policy-free environment. Explicit export subsidisation of any domestic product at a particular point in time can be motivated by either domestic or international considerations. Some governments seek to export surplus production from the protected domestic market onto the world market to ensure high domestic prices are maintained. However, to do so they must subsidise by an amount equal to the difference between the high domestic price and the lower world price. As a result other governments can use a similar policy as a tit-for-tat response to subsidies paid elsewhere in the trading countries group.

EU Policies

Currently the EU's Common Agricultural Policy (CAP) supports a number of products with export subsidies. Table 1 shows that there are fifteen food product groups which receive export refunds. What is apparent from the total expenditure on subsidies is that there has been a significant decline, falling from a total cost of 5.5bn euros in 2000 to 2.8 bn euros in 2002. However, within this overall decline, there have been some notable examples of where the support has been relatively constant. Thus, while support for wheat and flour has fallen by a factor of 50, there has been little change in the total support for butter and butter oil. Further, while there has been a decline in support for sugar, the absolute expenditure on it is still the highest of all the food groups, costing 1.17bn Euros in 2002, or nearly three times the amount spent on the next most highly subsidised product (other milk products). For most products though the total expenditure is on a downward trend as world markets have firmed and the commitments to the agreed Uruguay Round limits on subsidies have started to take effect.

What is striking from Table 1 are the disparities between plant based products and animal based products. The former tend to receive much lower per unit subsidies than the latter, ranging form 5 to 310 euros per tonne (excluding sugar). By contrast, the animal products are more expensive to subsidise with a range from 74 to 799 euros per tonne (excluding butter and butter oil). The per unit subsidy represents the extent to which the protected domestic price differs from the world price and thus the higher the per unit subsidy the more out of line domestic prices are with world prices. In addition, the bigger the volume of subsidised exports released onto the world market, the more distorted world price will tend to become.

Table 1: Export Refunds in the European Union

	Total Exports Subsidy (Million EUR)		Subsidised Exports (000 tonnes)		Value of Subsidy (EUR/tonne)	
PLANT PRODUCTS	**2000**	**2002**	**2000**	**2002**	**2000**	**2002**
Cereals	824	99.3				
Wheat and flour	509	8.5	15,606.2	1,650.1	32.63	5.15
Coarse grains	730	112.8	18,379.2	3,922.4	39.73	28.76
Rice	26	41.1	140.4	132.2	188.03	310.70
Sugar	1,439	1,168	970.6	1,051.9	1,482.38	1,110.56
Fresh fruit & vegetables	33	29.3	872.6	704.4	37.59	41.60
Processed fruit & vegetables	13	17.1	108.4	78.7	122.69	217.28
Wine	22	25.0	2,386.7	2,283.1	9.01	10.95
ANIMAL PRODUCTS						
Skimmed milk powder	338	36.7	417.2	86.9	809.68	422.32
Cheese	236	188.6	305.2	279.5	772.61	674.78
Other milk products	905	402.2	1,104.0	763.8	820.11	526.58
Butter and butter oil	333	324.9	193.9	193.7	1,719.44	1,677.34
Beef and veal	661	386.7	766.1	483.5	863.20	799.79
Pig meat	243	27.3	694.0	71.6	350.14	381.83
Poultry meat	75	71.1	318.0	230.4	236.16	308.61
Eggs	14	6.0	100.6	80.2	140.16	74.81
TOTALS	**5,578**	**2,846**	**42,363**	**12,012**		

Source: WTO Notifications for EU, European Commission

Notes: (1) Butter and butter oil is in butter equivalents
(2) Beef/veal, pig meat & poultry meat are in carcass equivalents
(3) Eggs are in "shell eggs" equivalents
(4) Wine is in 000 hectolitres

The extent of the EU's share in these world export markets varies quite markedly (see table 2). The lowest share is in rice with just over 1% share, while by contrast there is a 16% share of world skimmed milk powder (SMP) exports and 19% of world wine exports. Further, the degree of explicit support for some of these exports also varies, with 88%, 95.6% and 90.0% of beef & veal, butter and egg exports respectively being subsidised.

About one third of the EU's rice exports and between a quarter and a fifth of sugar exports are subsidised, while wheat and pigmeat exports are mostly refund free[2]. It appears that the markets where there is the potential for greatest harm is where the export share is high and the proportion of EU exports accounted for by subsidised exports is also high. This would include skimmed milk power, beef and veal, cheese and butter.

Other OECD Countries

The approach of the OECD countries to their agricultural sectors varies greatly with some taking a very protectionist view (e.g. Norway, Switzerland, Republic of Korea) while others have a tendency to be less interventionist (e.g. New Zealand, Australia). While the WTO (2003) reports a decline in total

[2] A note of caution has to raised here in that the figures relate to a specific year and world market conditions dictate the level and volume of export subsidy (along with WTO commitments) and thus these proportions might vary over time.

Table 2: Export Markets in 2002 (000 Mt; wine in 000 HL)

	(A) World	(B) EU	(C) EU Subsidised	B as a % of A	C as a % of B	C as a % of A
Sugar	41920	4373	1052	11.3	22.3	2.5
Rice	27372	359	132	1.3	36.9	0.5
Wheat	133102	12955	1650	9.8	12.7	1.2
Other cereals*	110000	14200	3922	12.9	27.6	3.6
Beef and veal	5400	550	484	10.2	88.0	9.0
Poultry	9624	1169	230	11.3	21.2	2.4
Pigmeat	7764	1300	72	12.8	7.3	0.9
SMP	990	161	87	16.3	54.0	8.8
Cheese	3449	487	280	13.9	58.2	8.1
Butter	1356	219	194	15.0	95.6	14.3
Eggs	1019	88	80	8.6	90.9	7.8
Wine	66479	12879	2283	19.2	17.7	3.4

Source: FAO, Eurostat (* figures for 2001)

support for agriculture since the mid-1980s, the OECD still spent $318 bn on support measures to agriculture in 2002 or nearly 1.3% of GDP (OECD, 2004). Table 3 highlights the degree of OECD support. The values show total support and include domestic protection measures as well as support for exports. In specific terms, the major instruments for providing support continue to be market price and output payment methods, which in total comprised 69% of total support to producers. The WTO (2003) reports that these policies lead to OECD farm prices being some 31% higher than world prices in 2001. As for export subsides, WTO (2003) states that the EU accounts for 90% of OECD export subsidies and while not alone in using these, it is clear that even the Uruguay Round agreed levels of support will still amount to approximately $13bn of export support.

There is a wide range of explicit export support policies across the other OECD countries. Table 4 indicates those being used currently.

Table 3: Degree of Agricultural Support provided in OECD Countries

Country	Agriculture's Share of GDP (%)	Total Support Estimate (% share of GDP)
Australia	3.3	0.3
Canada	2.2	0.7
Czech Republic	3.6	1.2
EU	2.1	1.4
Hungary	3.7	1.4
Iceland	9.6	1.6
Japan	1.1	1.4
Korea	4.9	4.7
Mexico	5.5	1.3
New Zealand	7.2	0.3
Norway	1.5	1.4
Poland	4.1	1.0
Slovak Republic	3.6	0.9
Switzerland	1.2	1.9
Turkey	14.1	4.3
USA	1.4	0.9
OECD Average	N/a	1.3

Source: Adapted from WTO (2003), Table 11.4 p 21.

Table 4: OECD Explicit Export Support Measures

Country	Commodities Supported
Australia, Iceland, Japan, Korea, Mexico, New Zealand, Poland	None
Canada	Milk
Czech Republic	Total $80 m (inc. milk $65m, beef $9, barley malt $4.5m and potato starch $0.9m)
Hungary	Total $15m (Wheat, pigmeat, poultry, wine)
Norway	Total $36m (2001) (inc. cheese (promotion), meat, eggs, dairy (disposal of surplus))
Slovak Republic	Dairy, malt from barley, beef for slaughtering and frozen vegetables. Total $11m (93% to dairy and malt)
Switzerland	Dairy (50% cheese), fruits, potato products and seed potatoes. Total $59m
Turkey	Processed fruit and vegetables, fruit juice, olive oil, potatoes, apples, poultry and eggs
USA	Dairy $55m 2002. Wheat, feed gains, rice, pork, poultry and eggs

Source: OECD (2003)

3. Developing Country Interest in Agricultural Trade Reform

Developing countries' current interests in access to export markets lie primarily in either agricultural products or natural resources (minerals etc) or light manufactures (such as textiles, clothing and footwear). It is estimated (Anderson et al, 2001 using the GTAP model) that if all current trade barriers were eliminated, about half of the total welfare gain would come from the agricultural liberalisation in OECD countries (see table 5). This is despite the fact that agricultural production in OECD countries accounts for only about 4% of global GDP and agricultural products account from less than 10% of world trade.[3] The overall gains for the developing countries from OECD agricultural liberalisation would come from beneficial sectoral reallocation effects and improved terms of trade. The full liberalisation of high income country farm policies is estimated by the same study to raise world food prices on average by 5% in real terms. This would be in net terms; a terms of trade improvement for the developing countries (given the relative composition of the import and export basket of the developing countries in aggregate). By raising the internal relative price of agricultural and food products in developing countries it would also in general tend to lower any anti-agricultural bias and draw resources into activities of comparative advantage. Of course by raising domestic prices received by producers of farm products, this would in general tend to redistribute from consumers to producers in developing countries.[4]

Developing Country Interests Disaggregated

The aggregate picture painted in the previous section hides considerable variation across regions and sectors. This variation arises because there is significant variation in the price and market access implications of agricultural reform in different agricultural products, and because there is considerable variation in the composition of different developing countries import and export baskets. Although net (agricultural/food) exporting countries experiencing a terms of trade improvement will gain, developing countries that remain net food-importing economies after reform would lose from a terms of trade deterioration in their basket of traded food stuffs.[5]

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[3] Note, however, that the bulk of the static welfare gains from agricultural liberalisation in the high income countries accrue to the high income countries themselves in the form of consumer gains from lower domestic prices. (Indeed, in terms of welfare effects there are larger gains for the low income countries from the liberalisation of their own agricultural trade barriers (+$31.4 bill) than from OECD agricultural liberalisation (+$11.6bill).)

[4] The extent of this effect depending on the extent of transmission of world prices to domestic prices.

[5] There may of course be offsetting terms of trade effects in their non-agricultural trade.

Table 5: Sectoral and International Contributions to Economic Welfare Gains from Complete Removal of Trade Barriers (1995 US $ billions)

		Sector				
		Agriculture & Food	Other Primary	Textiles & Clothing	Other Manufactures	TOTAL
Liberalising	Benefiting Countries					
	High Income	110.5	-0.0	-5.7	-8.1	96.6
	Low Income	11.6	0.1	9.0	22.3	43.1
	(Total)	(122.1)	(0.0)	(3.3)	(14.2)	(139.7)
Low Income						
	High Income	11.2	0.2	10.5	27.7	49.6
	Low Income	31.4	2.5	3.6	27.6	65.1
	(Total)	(42.6)	(2.7)	(14.1)	(55.3)	(114.7)
All Countries						
	High Income	121.7	0.1	4.8	19.6	146.2
	Low Income	43.0	2.7	12.6	49.9	108.1
	(Total)	(164.7)	(2.8)	(17.4)	(69.5)	(254.3)

Source: Anderson et al (2001).

Note, however, that in the case of comprehensive trade reform there is scope for terms of trade losses to be compensated (in part at least) by offsetting gains. Thus for developing countries remaining as net food importers post-reform there is the opportunity for improving efficiency in domestic resource use (induced by own trade reforms and by the lowering of distortions in manufactured – in particular labour-intensive - goods in industrial countries). Further the terms of trade deterioration itself provides the incentive for currently net food-importing developing countries to raise efficiency and productivity in their import-substitute food sectors; the resulting rise in import-substitute production could reduce or even eliminate the deficit on the food and agricultural trade balance. As table 6 illustrates for the Sub-Saharan Africa region (excluding South Africa), complete liberalisation (including their own) of trade barriers is predicted by the GTAP model to improve the agricultural sectoral trade balances in most sectors (and in aggregate), and to increase output in most agricultural sectors (by over 10% in four sectors).

The comprehensiveness of trade reform is for most developing countries likely to increase the probability of net welfare gains. Table 7 shows the net welfare effects predicted by the GTAP model for individual developing countries or country groupings from comprehensive trade liberalisation, broken down by the source of gain (developed v. developing country and manufacturing v. agricultural liberalisation). China and the Middle East/N. Africa are the only net losers. Indeed most of the other developing country regions gain from both developed and developing country reform and from agricultural and manufacturing liberalisation.

Partial Reform and Developing Country Interests

As the comprehensiveness of the trade reform decreases, it becomes more difficult to specify the developing countries' interest. Although it is reasonably straight forward to identify the price and market access effects of product-specific reforms in qualitative terms, it is difficult to express with quantitative precision when partial reform or elimination of one or several sources of distortion may be involved and when the extent of contemporaneous reform in other sectors is uncertain. Similarly it is possible to identify which countries are currently (i.e. pre-partial reform) net importers and net exporters of specific products (potentially subjected to reform). In turn one can assess qualitatively how output and trade balances will adjust to a specific reform, but these effects will be quantitatively sensitive to how all of the specific reforms (and any other reforms) affect domestic relative prices.

Table 6: Changes in Agricultural Sectoral Outputs and Sectoral Trade Balances in Sub-Saharan Africa [1] from Complete Removal of Trade Barriers [2]

	Changes in Sectoral Trade Balance (1995 US $ million)	Changes in Sectoral Output (% difference)
Rice	+28	+1
Wheat	+44	+2
Other Cereals	+1,815	+85
Veg/Friut/Nuts	-8	0
Oil Seeds	+48	+3
Other Crops	-2,068	-8
Plant Fibre	+589	+11
Livestock	+365	+15
Other Food Prod.	+339	+2
Meat/Diary Prod.	+569	+14
Forestry/Fish	-54	0
Veg Oils/Fats	-22	0

[1] excluding South Africa [2] including own

Source: adapted from Anderson and Yao (2003).

Partial agricultural trade liberalisation would result in winners and losers, both within and between countries. Producers (consumers) in current (or potentially) exporting developing countries (of the particular liberalised product) will gain (lose). The net national interest of the developing countries depends on the post-reform balance of producer and consumer interests (in the commodity). Although the net impact on countries will depend on whether the country is a net-importing country (post-reform), the cost imposed on consumers will depend on what happens to prevailing trade barriers. Any rise in the world price could be offset in full or part by a lowering of the domestic tariff.

Table 7: Sectoral and International Contributions to Economic Welfare Gain from Complete Removal of Trade Barriers (by Developing Countries/Country Groupings) (1995 US $ billions)

	Industrial Country Liberalisation		Developing Country Liberalisation	
	Agriculture	Manufacturing	Agriculture	Manufacturing
China	-4.63	9.64	-3.60	-7.19
Taiwan, Hong Kong, Korea	0.77	6.09	11.97	12.12
Indonesia	0.16	0.47	0.22	1.16
Other South East Asia	-0.90	1.33	5.67	4.59
India	0.68	3.01	1.90	3.24
Other South Asia	0.12	1.25	3.02	2.20
Brazil	1.44	1.67	4.59	8.71
Other Latin America	14.25	0.57	2.75	1.73
Turkey	-0.59	0.71	0.60	1.33
Midd. East & N. Africa	-2.81	1.74	-0.35	-0.36
Southern African Customs Union	0.76	0.10	0.38	0.13
Other SSA Countries	1.58	0.14	1.23	0.27

Source: adapted from Anderson et al. (2001)

A final issue to be considered at this stage is the possibility of interdependence between alternative sources of distortion and as a result between alternative reforms. If, for example, export subsidies are used to accommodate over-production induced by the setting of domestic market supports at too high alevel, then reducing export subsidisation is also likely to require reforms of the domestic market support arrangements. Reduction or elimination of export subsidies may well therefore require reductions in tariffs. In which case analysis of partial agricultural trade reform will need to assess both the direct and indirect effects. The indirect effects may involve, for example, the erosion of bilateral trade preferences induced by multilateral tariff reforms.

The Elimination of EU Exports Refunds

Table 8 sets out the current aggregate trade balances for each of the product groups for which EU Export Refunds apply and summarises the proportion of developing countries that currently have a net surplus or deficit on the particular product group. Ideally we would want to report the post-reform situation, rather than base the discussion on the prevailing 2002 (pre-reform) conditions. The information is however indicative of developing country interests. Certainly for those products for which there is already a trade surplus (namely rice, sugar, fresh and processed fruit and vegetables and poultry meat), there is no ambiguity. One would expect an increase in world prices and improved market access opportunities (arising directly from reduced EU exporting to non-EU markets or indirectly from induced reduction in domestic support in the EU itself) to tend to increase the developing countries' aggregate trade surpluses in these products. For all the other product groups for which there is currently a net deficit for the developing countries as a whole, the overall implications of reform are ambiguous.

The existence of a current deficit does not however mean that the developing countries necessarily do not have an interest in reform. If the elimination of export refunds (either directly or indirectly) reduced EU exports sufficiently, and if this combined with the increase in world price stimulated developing country exports sufficiently, then the sign on the trade balance in some of these product areas may be reversed. As shown earlier, EU exports account for a significant proportion of world trade (>10%) in most of the subsidised product areas, and in some of these cases the majority of these EU exports (>50%) are subsidised (i.e. beef & veal, skimmed milk powder, cheese, butter and eggs). These are product areas in particular where the elimination of EU export subsidies might induce a change in the net trade balance of the developing countries.

Table 8: Net Developing Country Trade Balance in EU Subsidised Exports (2002, 000 $)

Products	Balance	Percentage of Countries (%)	
		In Surplus[1]	in Deficit
Cereals			
Wheat and flour	-7,360,925	12	88
Other cereals[2]	-4,951,085	16	74
Rice	+430,162	12	88
Sugar	+499,652	28	72
Fresh and processed fruit & vegetables	+11,156,684	38	62
Bananas	+1,968,270	40	60
Citrus fruits	-174,406	37	63
Processed tomato	-123,812	16	84
Wine	+198828	13	87
Animal Products			
Skimmed milk powder	-1,375,551	13	87
Cheese	-1,231,231	12	88
Other milk products[3]	-4,416,145	13	87
Butter and butter oil	-678,746	13	87
Beef and veal	-814,286	28	78
Pig meat	-772,443	25	75
Poultry meat	+309,949	14	86
Eggs	-93,545	26	74

[1] Current surplus or balanced trade [2] Total cereals less wheat and flours and rice
[3] Total milk products (code 2030) less skilled milk powder (code 898)

For all of the products and product areas, irrespective of whether there is a current trade surplus or deficit, there are conflicts of interest between the developing countries. Table 8 shows that for all product areas the majority of developing countries currently have a trade deficit. Although the proportion with a deficit could be expected to decline with the reform of EU export policies, it is most unlikely that there would not be a significant proportion of countries with post-reform trade deficits in many of these product areas. Indeed the smaller the developing country and the more concentrated its production and exports, the more likely the incidence of trade deficits post-reform. As argued in earlier sections, however, even these countries may experience offsetting gains in some product areas, higher prices on its restricted number of net exports offsetting in part at least the higher prices on its larger number of net food imports.

Existing surplus countries and countries with deficits but significant exports are identified as gainers or potential gainers on a product by product basis. There are clearly some countries (e.g. Argentina and Brazil) that are consistently identified as net exporters and gainers from reforms that increase world prices and export market opportunities. These tend to be dominated by the larger and more advanced developing countries that is by those countries that have already achieved some export development and diversification. It also includes a number of the transitional market economies. There are however a fair number of incidences of potential African gainers in specific products, and some small countries especially in the fruit and vegetable category. The number of gainers may be expected to grow in the longer term as export development and diversification takes place.

4. Policy Implications of Export Subsidy Reforms and Broader EU Farm Reform

Although the balance of effects of reform is likely to vary across countries, the issues are common to all the developing countries; namely how to increase the opportunities for export growth and diversification and how to respond to the effects on consumers, government revenue and poverty of higher prices of imported food. Note, however, that the poor would not only be affected on the consumption side by higher food prices. The incidence of poverty is often greatest in developing countries among rural communities and those working in agriculture. Higher world prices of agricultural products offers the direct potential for higher incomes of the agrian poor. To the extent that the reforms also induced higher growth then they may also alleviate poverty indirectly.

Conditions to Foster Export Growth and Diversification

Raised world prices of agricultural products may be a necessary condition for promoting agricultural development and growth in the developing countries, but it is unlikely to be a sufficient condition for bringing about export growth in existing products or for bringing about market entry for new agricultural exports. Increases in world prices of agricultural products may not for example be translated into equivalent increases in domestic producers' prices in developing countries, if the institutional and market conditions are not conducive of this. The removal of explicit export taxes and removal of official marketing boards with monopoly control over exporting has improved the transmission of world to domestic prices and reduced the overall taxation (explicit and/or implicit) of agricultural products in many developing countries. But the liberalisation and privatisation of marketing has not always produced competitive conditions, and there is sometimes an institutional void following the elimination of the pre-liberalisation marketing structures. Private traders may not always offer the type of credit facilities which allow producers to respond fully to changing market incentives. It is also important that there is an adequate infrastructure to allow for efficient domestic distribution of goods. Again the link between world and domestic prices can be weak if the distribution and transportation systems are inefficient and uncompetitive.

Commercial export opportunities tend to be highly restricted where the transport and other infrastructure is poor, and where as a result local markets are small and surplus output is only traded on the local market. Government support with road networks and irrigation etc is vital, but governments and NGOs can also play an important role in some of the now more diversified agricultural exporters in supporting the delivery of modern production methods and of product standards. These production and

product conditions are likely to be essential to satisfy export market (consumer) requirements and to overcome the policy standards set by the industrialised countries. An appropriate balance of market driven and public sector support (e.g. through extension services) is required to support the development of appropriate crop varieties and management, pest control and fertiliser use.

Having the capacity to produce goods of the quantity and quality/standards required reliably to satisfy export market requirements will not, however, ensure that the expected export growth takes place if improved market access and market entry for new products is constrained by defensive use of trade policy (traditional import barriers and non-tariff measures such as phyto-sanitatory requirements) in potential export markets. Further liberalisation of agricultural import policies (in both the industrial and developing countries) is required.

Responding to Higher Imported Food Prices

Consumers in developing countries, in particular the urban poor will be adversely affected by higher world food prices which translate into higher domestic food prices. To the extent that there is scope to do so, governments could ameliorate (or even fully offset) the domestic food price increases by reducing or eliminating any tariff or non-tariff barriers on food imports. Alternatively, if import barriers are protecting import substitution (IS) activity, then higher world prices would provide an incentive for increased import-substituting production and reduced imports. Of course rising world prices could be combined with reduced import protection (e.g. a lower tariff) to induce some (or no) increase in the domestic price received by the IS producers. Governments have therefore some flexibility in making adjustments to the domestic prices facing consumers and producers. Lowering import tariffs on agricultural food products to offset any world price rises is likely to reduce import duty revenues. The significance of this effect will depend upon the importance of agricultural/food tariffs in overall trade tax revenue, and upon the scope for governments to substitute non-trade taxes (e.g. domestic expenditure and income taxes) for trade taxes. This will be a greater constraint for small and lower income developing countries, especially in the short run.

Implications for Protocol Countries

In general, the Cotonou Agreement provides signatory producing nations with guaranteed export markets for specific commodities (rum, bananas, beef and veal and sugar); quotas to named exporting nations and the offer of the prices ruling within the EU market. While the Protocols would not necessarily be directly affected by CAP reform, reform would tend to lower the EU market price and therefore reduce the value of Protocol exports. However, as export subsidies are cut along with planned for reductions in output as a result of reduced EU domestic support, world prices are likely to rise, meaning that those Protocol countries that export also to non-EU countries will gain from higher prices received there. In addition, it is important to consider those countries that gain from reform of one commodity are potentially also importers of other Protocol commodities. The net effect for the Protocol Countries of wider reform is therefore ambiguous in general. For some of the major quota holders (e.g. Mauritius in the case of sugar), however, significant losses are likely to be experienced.

One of the major aims of the original Lomé Agreement was to ensure that former colonies of the EU countries did not suffer as a consequence of EU policies dominating earlier national policies. In that same spirit, some compensation for those countries that will lose as a result of EU agricultural reform may be needed and any such policies could mirror some of those undertaken for compensating EU farmers when price support has been reduced. Time-constrained transfer payments that are similar to the implicit aid flows embodied in the Lomé provisions but with specific conditions tied to sectoral adjustment and export diversification are an option.

5. Conclusions and Recommendations

The reform of the EU's export subsidy arrangements offers challenges for policy makers in developing countries. Although there is a general expectation that agricultural trade reforms are in the overall or aggregate interest of the developing countries, the developing countries are not an homogenous

grouping. The pattern of comparative advantage between agricultural and industrial products and within agricultural production varies considerably across the developing countries. There will be gains and losses in specific product areas for many countries, and there will be a non-negligible number of countries that will be net losers. In which case there is no unique list of products that is likely to bring gains for all of the developing countries.

In table 9 we summarise the study's assessment (product by product) of the degree of distortion of world food markets by EU export subsidies, and of the balance of developing country interests. There are relatively few products where there is both a high degree of distortion and where there is an aggregate developing country interest shared by a high proportion of developing countries in the removal of the world price distortion. Although some products appear towards the top of the listings several times (e.g. beef and veal, sugar, and fruit and vegetables) and others that come near to the bottom of the list several times (e.g. wheat and flour), most products cannot be characterised in this way.

Rather than being selective and trying to produce a restrictive list of products, one might argue for a wholley different approach; one that views the long run interest of the developing countries being with undistorted world policies and better access for its exports to the industrial countries' (and the developing countries') markets. Take the EU's offer and push for the elimination of all of its export subsidies. This will in turn increase the pressure for the EU to reduce its overproduction in agricultural goods and for the lowering of protection of the EU market. Such a process of agricultural reform would increase the pressure on the other OECD countries to reduce export subsidisation and to open up their agricultural markets.

Specific compensation or supports may be required for specific countries, in particular the current Protocol exporters to the EU. International support may also be needed with investment and institutional development in the least developed countries, so that they can increase their capacity to respond commercially to world food price changes. Increasing agricultural activity and incomes should be a vital element of poverty alleviation plans in developing countries. Of course developing countries are also rightly sensitive about the impact of rising prices of imported food on poor consumers, but liberalisation of their own agricultural trade policies is one obvious way of responding to that problem. What a virtuous cycle; removal of EU agricultural export subsidies leading to improved market access in the EU, which leads to reform of other OECD export subsidy and import policies, which ends with the developing countries further opening up their own agricultural markets. The developing countries should be bold and opt for the full Lamy!

Table 9: Summary of Rankings of Products

	Degree of Distortion		**Balance of Developing Country Interests**		
	Extent of Subsidy[1]	Extent of Subsidised Exports[2]	Aggregate Developing Country Trade Balance[3]	Percentage of Current and Surplus Countries[4]	
↑ more distorted	Butter	Butter	Fresh and processed fruit and veg.	Fresh and processed fruit and veg.	↑ greater interest
	Beef and veal	Beef and veal	Sugar	Sugar	
	Sugar	Skimmed milk powder	Rice	Other milk products	
	Cheese	Cheese	Poultry	Eggs	
	Skimmed milk powder	Eggs	Wine	Beef and veal	
	Other cereals	Other cereals	Eggs	Other cereals	
	Eggs	Wine	Butter	Wheat and flour	
	Poultry	Sugar	Pigmeat	Pigmeat	
↓ less distorted	Rice	Poultry	Beef and veal	Poultry	↓ less interest
	Pigmeat	Wheat & flour	Cheese	Cheese	
	Wine	Pigmeat	Skimmed milk powder	Rice	
	Wheat and flour	Rice	Other milk products	Wine	
			Other cereals	Butter	
			Wheat and flour	Skimmed milk powder	

[1] Value of export subsidy relative to value of world trade; the greater the value the greater the potential distortion
[2] EU subsidised exports as share of world exports; the greater the value the greater the potential distortion
[3] Trade balances taken from table 8; interest declines as trade surplus declines or deficit increases
[4] Based on evidence in the full report (Milner and Morgan, 2004), interest declines as proportion of current and potential surplus countries declines

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