

Agricultural trade, globalisation, and the rural poor

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At the outset let me thank the International Food Policy Research Institute (IFPRI) for inviting Oxfam to address this important seminar. Over the years IFPRI in general, and Per Pinstrup-Andersen in particular, have established a strong track record not just in conducting research on rural poverty, but in converting research into a tool for achieving policy change. As an agency that works closely with poor rural communities across the developing world, we have frequently drawn on on IFPRI's work in the development of our programmes.

Background

No issue merits more serious concern than the subject under discussion today. If the key development challenge of our time is the creation of a more inclusive world and the eradication of poverty, we need to develop a new road map for globalization. Maintaining our current course will lead towards a world of unstable co-existence between prosperity for a few, and marginalization and despair for many. Such a world will be inherently unstable and politically unsustainable.

For a group that accounts for three-quarters of world poverty the rural poor are conspicuous by their limited presence in the raging debates on trade and globalisation. Enthusiasts for globalization like to assert, often on the basis of flimsy data and high school econometrics, that greater openness is acting as a catalyst for equity and poverty reduction. Evidence from a wide range of countries points in a different direction, especially with regard to the rural poor. Even five star globalization success stories have seen rising inequalities between the rural poor and the rest of society – and these inequalities are slowing the rate of poverty reduction.

It is standard practice in debates on globalization to state one's faith at the outset, either in favour of globalisation or against it. Oxfam's position is one of agnosticism. There is no question that globalization is failing large swathes of the global poor. That failure is reflected in the slow rates of poverty reduction and widening of already obscene wealth gaps between and within countries. Oxfam's own programme experience bears testimony to the scale of the failure. Yet persistent poverty and inequality are not inevitable outcomes driven by the iron economic laws

of the globalization era. They are the result of political choice and a governance system that manages globalization in the interests of the powerful.

This is not to deny that one of the features of globalization is a gap between the economic forces driving it and formal political institutions (Birdsall 2002). Yet we do have a system of governance by default. The WTO is one part of that system – and its record is symptomatic of the deeper problems. Through the WTO, northern pharmaceutical companies have been able to globalize patent rules that will drive up the costs of basic medicines, playing treatment beyond the means of millions. Other companies are now using the same institution as a vehicle for prising open investment markets and opening up utility sectors in developing countries, including water. The IMF and the World Bank have used their loan conditions to impose trade liberalization and wider reforms on poor countries. And the IMF helped first to open up capital markets in developing countries, and then to collect debts on behalf of Wall street when they collapsed, regardless of the costs to the poor.

These are governance interventions undertaken on behalf of politically powerful governments and transnational companies. One struggles to think of similarly ambitious measures advanced in the interests of the world's poor, such as a commitment to increased aid, effective debt relief, the opening of northern markets, or measures to resolve the protracted crisis in commodity markets. These issues are beyond the scope of this paper and have been dealt with elsewhere. But some of the problems that I want to discuss today are the product of conscious market management, not of deregulated, free trade. Indeed, one of the features of globalization is that the strongest advocates of free markets in the corporate community, and among the political leaders of the industrialized world, are among the central architects of a rules-based system geared towards the pursuit of their own interests.

Introduction

In this short paper, I want to reflect on some of the problems associated with emerging trends in agricultural trade under globalisation, and to suggest some public policy actions that might help to resolve them.

As in other areas, globalisation in agricultural trade has been marked by continuity in the midst of revolutionary change. Old problems have taken on new, more complex forms. And failure to address old policy challenges has left the rural poor facing the imminent threat of accelerated marginalisation. Perhaps most obviously, globalisation has increased the benefits associated with access to productive assets and human capital – and it has increased the costs of deprivation in both areas. At risk of stating the obvious, in a knowledge based global economy there is a high price to be paid for illiteracy, not least because of the exclusion that it implies from new technologies, information and ideas. And evidence from a wide group of countries consistently points to the rural poor – especially poor women – as the most educationally disadvantaged group (Oxfam 2000)

One area in which continuity has been a more pervasive force than change is in the sphere on northern agricultural policy. In their rhetoric, industrial country governments seldom miss an opportunity to extol the virtues of level playing fields and open trade in world agriculture. Yet in their policies they display all the features of acute path-dependence, reflected in an inability to shake off the legacy of the past. The manner in which rich countries systematically encourage agricultural over-production and export dumping, destroys the local markets of smallholder farmers and denies poor countries an opportunity to benefit from trade. By undermining the dynamism of rural economies, northern agricultural policies not only generate short-term costs, but also obstruct the powerful multiplier effects that agricultural growth can generate for poverty reduction.

The Agreement on Agriculture (AoA) adopted at the end of the Uruguay Round was a prime example of path-dependence in operation. While much has been made of the extension of WTO rules to agriculture, in reality the agreement did little more than accommodate export dumping as practices by its two major exponents, the European Union (EU) and the United States. In truth, the AoA was a demonstration of global governance at work, with multilateralism being subordinated to the pursuit narrow self-interest in the world's richest countries. As in the past, the overarching aim is to reward the largest farmers for over-producing, and then to provide agribusiness export firms with subsidized access to the resulting surpluses.

This paper is divided into two sections. The first looks at some broad trends in world agricultural trade and their implications for the rural poor. It argues that globalisation is reinforcing the structures of disadvantage at the heart of rural poverty. The second part of the paper focuses on northern agricultural policy, highlighting its adverse impact on developing countries. It criticises the current direction of farm policy reform in the United States and the EU and the myth of 'decoupled' support on which it is based, and concludes with some observations on the (steadily worsening) prospects for the Doha round of WTO talks.

1 Agricultural trade, globalisation and the rural poor

Under certain conditions, agricultural trade has the potential to act as a powerful force for poverty reduction. Where production is widely dispersed and marketing arrangements protect smallholder farmers from monopolistic pricing, there is clear evidence that production for exports can enhance welfare. Because rural growth generates powerful multiplier effects, static trade gains can feed into dynamic longer-term benefits for poverty reduction (Delgado et al 2000). The positive links between rice exports and poverty reduction in Vietnam illustrate what can be achieved (Minot and Golletti 2000). However, individual success stories obscure some deep systemic problems that raise questions about the scope for agricultural trade to redress the deep inequalities emerging under globalisation.

Some elements of continuity

The past decade has witnessed a boom in world trade, with an average annual increase of just over 6 per cent in the volume of merchandise trade, outpacing the growth of global GDP by 4 per cent. In other words, trade is becoming an increasingly important determinant of the distribution of global income.

While some trade patterns are being transformed by the rise of intra-company trade, foreign investment, technology transfer, and the emergence of globalised production systems, others have remained constant, including the steady decline of agriculture in overall trade. Although it increased in real terms in the 1990s, agriculture now accounts for less than 9 per cent of total trade, or half the level in 1980 (OECD 2000). The very large group of low income countries that continue to depend heavily on agricultural exports are operating in a segment of the world economy that represents a diminishing share of value-added. They are, in effect, seeking to climb the downward escalator.

In some cases, the escalator has been gathering speed at a frightening rate. Take the case of coffee – a crop produced by 25 million farmers across the developing world. Taking inflation into account, the real price of coffee is now just 25 per cent of the level in 1960 – and probably lower than at any time since the Great Depression (Oxfam 2002).

Behind the numbers is a picture of desperate – and deepening – rural poverty. From Ethiopia and Tanzania to Vietnam and southern Mexico, the slump in world prices has resulted in deteriorating indicators for health and nutrition, children being taken out of school, and rising rural unemployment. As Oxfam's recent report on the crisis puts it: "The coffee crisis is becoming a development disaster whose impact will be felt for a long time." Of course, not all participants in the market are losers. For the giant coffee roasting companies such as Nestle and Kraft, lower world prices have translated into wider profit margins. Indeed, the gulf between corporate prosperity and rural misery in world coffee sector is becoming emblematic of the injustices at the heart of globalization.

The macro-economic effects of the coffee crisis are already being felt. Growth forecasts are being revised downwards and several countries benefiting from the Heavily Indebted Poor Countries (HIPC) Initiative – such as Uganda – have been pushed back towards debt unsustainability.

It has to be stressed that, while coffee is an extreme case, it is not untypical. Using the IMF's world price index, in 2000 prices for eighteen major commodities were lower in real terms than in 1980 (IMF 2001). Recent years have witnessed deep troughs in prices for tropical oils, tea and sugar. In each case, price slump has translated into rising poverty.

Behind the wildly fluctuating trend in commodity prices has been another element of continuity with the past: namely, a persistent decline in terms of trade. Primary commodity exporters have to export more and more volume to retain a fixed import capacity. While numbers vary according to the reference years and crops selected, it is difficult to find a good news story.

According to UNCTAD, Africa's terms of trade losses since 1970 have halved the region's share of world trade (UNCTAD 1998).

One other aspect of continuity in agricultural trade merits reference. Other things being equal, trade theory predicts that developing countries should be increasing their penetration of world agricultural markets. They have an abundance of 'unskilled' labour relative to other factors of production, and relative to rich countries. It follows that more agricultural trade should increase demand for exports embodying that labour, thereby generating increased income and employment.

In the event, real world economics has prevailed over text-book theory. Developing countries have increased their share of world trade, but at a modest rate. Their share of agricultural exports rose from 30 to 34 per cent between 1990-1994 and 1995-2000. This was slower than the rate of increase for manufactured goods. Moreover, the rise was driven by an increase in South-South trade. The international agricultural trading system continues to be dominated by rich countries, which now account for three-quarters of the total. Such outcomes reflect the continued recourse of rich countries to extensive production and export subsidies – an issue to which we return below.

Some new emerging patterns.....

Agricultural trade has not been immune to the broader changes emerging under globalisation. These changes have important implications for smallholder farmers – and hence for poverty reduction efforts.

One important development has been the emergence of high-value food products as a growth point in the agricultural trading system (Delgado, Minot and Wade 2001). This sector extends from fresh fruit and vegetables, to dairy and livestock. Export growth rates for some product groups are rising by 14 per cent a year, as witnessed by the proliferation of foodstuffs produced in poor countries on the supermarket shelves of rich ones. In the global agricultural system, HVFPs are the fast lane.

The rapid rise of HVFPs has been associated with important changes in the supply chains linking northern consumers to southern producers. Traders, processors and retailers are taking advantage of new opportunities provided by declining transport costs, improved communication systems, important liberalisation and more open foreign investment regimes. At the same time, mergers and acquisitions have reduced the numbers of multinational companies in global markets and increased the importance of intra-company trading.

Supermarket chains, together large-scale food manufacturers, occupy an increasingly pivotal role. The rise of large supermarket chains in industrialised countries is a dramatic example of concentration. In Britain, the top four retailers now account for nearly three-quarters of all food

sales – and 70-90 per cent of fresh produce imported from Africa (Dolan, Humphrey and Harris-Pascal 1999).

Less widely observed, but no less important, is the growing weight of supermarket chains in developing countries. In Latin America, supermarkets account for a population-weighted average of 60 per cent in food retailing, with five chains accounting for almost half of supermarket sales in Brazil, rising to over 70 per cent in Colombia and Argentina, and 80 per cent in Mexico (Reardon 2002). Foreign multinationals – such as Wal-Mart, Carrefour, and Ahold - have entered local markets on an extensive scale through a process of mergers and acquisitions. Complex new sourcing and marketing systems are emerging. Carrefour uses its global sourcing network to contract melon producers in north-east Brazil to supply its sixty-seven stores in that country and stores in twenty-countries. Major agro-exporters – such as Hortifruti in Chile – contract directly with national and global supermarket chains. In other cases, supermarkets contract farmers via large wholesale companies.

All of these changes have important implications for farmers in developing countries. To an increasing extent entry not only to export markets, but also to local retail markets is mediated through firms linked to, or owned by, major supermarket chains in industrialised countries. Once again, there is a marked trend towards concentration. In both Kenya and Zimbabwe, two of the largest suppliers of leguminous vegetables to the European Union, the top five exporters account for more than 75 per cent of fresh vegetable exports.

...and accompanying problems

All of these changes have important implications for the terms on which smallholder farmers enter world markets. For most producers, ‘the market’ is rapidly becoming a small number of large-scale processors and traders, or giant supermarket chains.

One feature of the trend towards concentration in processing and retailing has been the emergence of ‘buyer-driven’ supply chains, in which large numbers of producers interact with monopolistic marketing structures. These chains operate to transfer a large – and growing – share of value-added away from producers in developing countries to companies in industrialised countries.

The coffee supply chain, which is dominated by the ‘big four’ roasters – Nestle, Kraft, Proctor and Gamble, and Sara Lee – and supermarket chains demonstrates the problem. Ten years ago, coffee-producing countries earned \$10bn from a global market worth \$30bn. They now receive less than \$6bn in a market that has doubled in size – a decline from 30 per cent to 10 per cent (Oxfam 2002). Of course, it is easy for economists to explain how this trend is driven by the nature of marketing and the operation of a complex value chain in the global market. But modern economists are apt to forget one of the lessons that Adam Smith was at pains to teach: namely, producers and consumers are motivated by a sense of morality, justice and shared humanity as by an interest in market clearing rates.

Across the food sector, supermarket and large-processor are increasing their domination of retail markets, exercises further competitive pressures on small producers. In Brazil, the largest milk suppliers are Nestle and Parmalat, both of whom have links with global supermarket chains such as Carrefour and Wal-Mart that occupy a key place in the retail chain. While there is no evidence of price-fixing, market domination has enabled the processors and supermarkets to exercise a downward pressure on prices paid to farmers, with many small farmers being forced out of the sector (Farina 2002).

Supermarket purchasing policies can create huge barriers to market entry. These include:

- Demands for product homogeneity and compliance with complex health and safety requirements
- Maintaining post-harvest quality and preventing product deterioration, often including cold storage facilities
- Short-periods between picking and delivery of crops
- High rates of product rejection
- Procurement practices such as delays of up to ninety days in paying for products
- Short-term contracts that provide no guarantee of future markets, thereby raising the risks of investment

For reasons that are self-evident, poor farmers are not well-placed to meet such requirements. This is especially true when they are operating in rain-fed areas that are distant from markets and served by a weak marketing infrastructure. For poor households operating on limited cash budgets, protracted delay between product delivery and payment is not an option. Similarly, high rates of product rejection and short-term contract arrangements expose poor farmers to levels of risk and adjustment costs that few can absorb. Supermarkets themselves have an in-built preference for dealing with large-scale operatives since this lower the costs of monitoring quality.

Such factors explain why the growth of the HVFP market and the growing presence of supermarket chains has tended to exclude poor farmers. In Kenya – often held up as a good example – the four largest exporters of vegetable sourced only 18 per cent of their produce from smallholders, compared with 42 per cent on large commercial farms and 40 per cent on their own farms. In Zimbabwe, the smallholder share is less than 6 per cent. The rapid growth of fruit and vegetable exports from Mexico has been similarly driven by US-owned processors and distributors, usually contracting with large-scale agri-business firms (Appendini 1994).

Viewed in terms of the challenge of reducing rural poverty, the continuation of current trends poses grave risks. The obvious danger is that the rural poor will be excluded from the fastest growing, highest-value added markets, and that the lion's share of benefits from trade in this area will be captured by large-scale farms, and global supermarket and processing chains. This

will further erode the potential for trade to act as a force for poverty reduction, reinforcing the inequalities emerging under globalization.

Policy challenges

It goes without saying that there are no easy answers to the problems outlined in this section. What is clear is that the costs of failure to develop solutions, measured in terms of lost opportunities for poverty reduction, will be exceptionally high.

The starting point for identifying strategies aimed at achieving a more equitable distribution of benefits from agricultural trade has to be a recognition of the central problem: rural poverty itself. The rural poor typically lack access to land, assured supplies of water, and credit. Poor women farmers suffer particularly acute deprivation in each of these areas. As producers, they enjoy more restricted access to land, markets and inputs, with adverse consequences for productivity and equity (Rekha 1999; Udry et al 1995). The resulting losses of income are estimated by the World Bank to be equivalent to 1-2 per cent of GDP for sub-Saharan Africa (World Bank 1998). As such figures suggest failure to overcome the exclusion of women producers will further marginalize poor countries. This suggests that gender equity should be one of the fundamental building blocks for any strategy to make globalization work for the poor.

Equally fundamental is the central role of rural development and the redistribution of opportunity in favour of poor producers and more marginal areas. Most of the poor live in areas characterised by a weak institutional structure, including poor quality transport. High transport costs reduce the tradeability of much agricultural output, partly explaining the high correlation between remoteness and poverty (IFAD 2000). The same factor raises the costs of essential inputs such as fertilisers and seeds, and reduces farmgate prices for output. Sub-Saharan Africa faces especially acute problems in this area. The density of the region's rural roads network is only 55 kilometres per square kilometre, compared to over 800 kilometres in India. The weakness of rural infrastructure not only reinforces the exclusion of smallholders from global markets, but also leaves them unable to compete against imports in urban markets (Killick 2001).

Addressing these problems requires fundamental changes in the the distribution of public spending and, in countries where land ownership is highly unequal, the distribution of land and other assets. Yet there is little evidence of a commitment to redistributive rural growth strategies on the part of most governments, as witnessed by even the most cursory reading of their Poverty Reduction Strategy Papers (PRSPs). If governments – and the IMF-World Bank – are serious about prioritising rural poverty reduction, surely rural development should be accorded a far higher political priority.

In some areas, public policy has moved in a counter-productive direction. In the pre-globalisation era, input supply for smallholder farmers was often managed through parastatal market boards. The problems associated with these boards – such as they unbdue tax burden they placed on farmers and the fiscal burden imposed on the state - are well-known. Less well

documented, notably by the IMF-World Bank is the catalogue of failures associated with their own privatisation and liberalisation programmes. These have introduced a new wave of inefficiencies. All too often, input supplies have collapsed, starving efficient producers of capital, seeds, fertilisers and new technologies. The effects have been most severely felt in more remote areas that are less well served by private traders (Bryceson 1999, Kelly et al 1999, Howard et al 1999).

In some cases, market liberalization with regulation has been clearly justified. For example, the cotton marketing boards of East Africa had largely destroyed the sector by the early 1980s. With varying degrees of success, private sector investment has generated some recovery. By contrast, the cotton marketing boards of West Africa have achieved a fairly strong track record at several levels. Production and exports have both expanded, the input supply system has improved, and farmers are capturing a growing share of income. Despite this the IMF-World Bank are seeking to push through rapid liberalisation of state marketing systems. They cite as evidence of the need for radical action the fact that farmers in the region still receive a lower share of world prices than farmers operating in liberalized systems (IMF-World Bank; 2001; IMF 2002). What they do not acknowledge is that lower producer prices are in part a product of repayment for inputs that farmers in many other African countries without marketing agencies now lack. This would appear to be another case of ideologically driven liberalisation that threatens to exclude poor farmers from global market opportunities.

Without denying the case for market reforms, it is difficult to disagree with the conclusions of one commentator, who writes: the market liberalisation policies of the past fifteen years have generally been unhelpful to smallholders, throwing the baby out with the bathwater." (Kydd, Dorward and Poulton 2001). There is a strong case to be made for reviewing the received wisdom handed out from Washington on the role of the state in developing rural institutions, especially with respect to input supplies.

The depth, severity, and duration of the crisis in commodity markets makes the scale of the challenge self-evident. Northern governments remain wedded to a strongly non-interventionist stance, reciting the failures of the international commodity agreements in the 1970s. Yet whatever those failure, inaction would appear to be the worse-case scenario in the face of a problem at the centre of global inequality. As John Maynard Keynes once advised governments: "proper economic prices should be fixed not at the lowest possible level, but at a level sufficient to provide producers with proper nutritional and other standards" (Keynes 1944).

Current arrangements do not pass this test. There are signs that developing countries themselves are now developing more co-operative approaches. For instance, coffee exporters and the International Coffee Organisation have proposed measures to improve quality and control supply, including an element of stock destruction. Northern governments – and consumers - need to do something more than turn a deaf ear. Given the scale of the crisis in coffee, it is surely time to ask whether 'second best options' such as supply management may not be the preferred option to a rolling catastrophe.

Similarly 'non-interventionist' approaches govern approaches to the role of major processors and supermarkets in the global food chain. This too is unjustified. There is an urgent need for effective international anti-trust provisions to prevent collusion between the small groups of companies that now dominate most food markets. Similarly, there are strategies available for extending opportunities to smallholders in agricultural markets. And failure to implement those strategies will exacerbate rural inequalities.

To take one example, governments could do far more to promote good practice by supermarkets themselves. In the United States, supermarkets are required to pay suppliers within thirty days – and several developing countries are now enforcing this provision (Reardon 2002). Supermarkets themselves could do far more to set higher standards, including the provision of longer-term contracts. But ultimately it is up to government to implement legislation that controls the requirements placed by supermarkets on farmers.

Public-private partnerships are also needed. In Brazil, the state of Parana has developed a programme aimed at enhancing the capacity of smallholder suppliers to meet production, processing and packaging standards set by supermarkets, enabling them to capture a higher share of the value of their produce. On a smaller-scale, non-government organisations have also developed an expertise in this area. In Guatemala, Oxfam is working with a local partner – the Organisation for the Promotion of Trading and Research – which provides training and credit for small producers seeking to diversify production and enter export markets. Elsewhere – as in South Africa and the Philippines – farmer co-operatives have entered export markets, often working under contract for exporting firms, or exporting directly (Vogel 2000, Delgado, Minot and Wade 2002).

There is now a growing body of research evidence on good practice. It is crucial that governments and donor agencies draw on that evidence to help small farmers and entrepreneurs undertake the investments in equipment, technology and organisational development needed to redress the power imbalance with supermarkets.

Finally, the challenge of rural development cannot be separated from wider issues on the development agenda – notably the issue of development financing. International aid can play a critical role in creating the rural infrastructure that smallholders need to enter markets on more equitable terms. Yet the track-record of rich countries in this area is lamentable: the real value of aid disbursed to agriculture in the late 1990s was only one-third of the level a decade earlier. Unresolved debt problems pose a further barrier to rural development. In 2001, nineteen of the twenty-six countries receiving debt relief under the Heavily Indebted poor Countries (HIPC) Initiative, were spending 10 per cent or more of government revenue repaying debt. In some cases – as in Zambia, Nicaragua and Mauritania – the share amounted to one-fifth. And while the overall average is coming down, it will remain in excess of 10 per cent for all HIPCs in 2007 (World Bank 2002, Table 4). Given that this is a group of the world's poorest countries with the most pressing rural development needs, not to mention chronic deficits in health and

education financing, such an outcome would hardly appear to be consistent with a poverty-focused approach to debt relief.

2 Northern agricultural policies as a barrier to equitable globalisation

The rural poor live have highly diversified livelihoods (Kydd et al 2002; Bryuceson 1999). But most live and work in agriculture, often as smallholder farmers or agricultural labourers – or both. Integration through trade into international markets can have important implications through its influence on the price in the product markets in which the poor operate.

As a political entity, the rural poor do not figure on the radar screens of agricultural policy makers in rich countries. Public policy in this sphere is dominated by powerful special interest groups representing large farmers and agro-industrial concerns such as grain traders, and by complex rivalries between national governments (in the EU) and state-level governments (the United States) (Thurston 2002). The end result is an essentially inward-looking system of pork-barrel politics and corporate welfare payments. Yet northern agricultural policies have important implications for the rural poor in developing countries. The United States and the EU dominate global markets for a wide range of commodities, including wheat and corn (where the United States in the world's biggest exporter and the EU a major presence in wheat) and sugar and dairy produce (where the EU is dominant). It follows that the terms on which rich countries produce and trade has important implications not just for exporters, but also for staple food producers facing competition from imports.

Levels of support for northern agriculture

The agricultural policies of both the United States and the EU seek to achieve the twin goals of supporting farm income by driving a wedge between world and domestic prices, while at the same time protecting world market shares. Income support is intimately related to output, creating incentives for production and the generation of export surpluses, which then have to be disposed on world markets, usually at prices that bear no relation to costs of production. The upshot is that powerful agricultural exporting corporation are given access to surplus stocks financed by public subsidies.

Overall support for agriculture measured by the OECD's Producer Subsidy Estimate (PSE) ran at \$311bn in 200/2001 – a figure equivalent to around one-third of the value of farm output (OECD 2002).ⁱ The bulk of this support is directed towards meat, dairy, sugar and cereals. Between them, the United States and the EU account for around one-half of the total PSE. The PSE is both larger in absolute terms and as a proportion of output in the EU, but per capita subsidies to farmers are roughly equivalent.ⁱⁱ Contrary to a widely held belief, the PSE has not declined as a share of output since 1986-1988 (the reference period of the support cuts agreed under the Uruguay Round of world trade talks), and has increased in absolute terms (OECD 2002).

As has been widely observed, farm policies in the EU and the United States have been singularly ineffective in achieving their stated public policy goals, which include the protection of poor farmers and rural communities, support for the environment, and consumer health. In the EU, public opinion polls suggest that 80 per cent of people are in favour of governments supporting small farmers. It is likely that a similar proportion would regard the current distribution of spending as unacceptable. Just 2 per cent of farmers accounts for around half of all transfers. The French Agriculture Minister may extol the virtues of the CAP for 'the rural way of life' in his country (Financial Times, October 17, 2002), but only by turning a blind eye to the fact that the number of farmers has fallen by one quarter since the mid-1980s.

On average, the EU farms with the highest gross margins have the largest farm area and receive the greatest budget support (European Commission 2002). This is unsurprising given that support levels are a function of output and land area. In the United States the biggest 10 per cent of subsidy recipients account for almost three-quarters of total transfers, while 60 per cent of farms receive no support at all (Environment Working Group 2002). These figures reflect the close link between land area and output on the one side and subsidy transfers on the other. Current subsidy structures hurt small farmers in other ways. They are capitalized in rising land and land rental values, encouraging a high degree of concentration, and increase levels of mechanization and inputs of pesticides and chemical fertilizers. Apart from promoting large-scale agriculture this has been a source of environmental damage and consumer health fears.

Costs to developing countries – and the problem with modeling

While the costs of current farm policies are increasingly visible to the public in rich countries, those transmitted to developing countries are less apparent. Yet it is among the rural poor in developing countries that the most serious consequences of rich country profligacy are to be found.

Various attempts have been made to capture the costs of rich country farm policies for poor countries, usually through global model exercises using variable liberalization scenarios. For example, the IMF's 2002 World Economic Outlook used a general equilibrium model to estimate gains under a full liberalization for both developed and developing countries. Developed country liberalization was found to generate a welfare gain equivalent to 0.13 per cent of GDP for developing countries (IMF 2002). Using a partial equilibrium model, the World Bank has projected the effects of a 50 per cent cut in tariffs for all countries, arriving at the conclusion that this will generate a welfare gain of \$0.56 for all developing countries and \$0.12 for least developed countries (Hoekman et al 2002). Other exercises have reached broadly similar quantitative conclusions (IFPRI 2002; Anderson et al 2001).

What do these exercises tell us? In short, not a great deal. Like all global models operating at high levels of aggregation, the results are highly sensitive to assumptions made about supply and demand responses, many of which are little more than speculative leaps of faith (there is by definition no empirical evidence relating to the effects of 100 per cent liberalization by rich

countries). To the extent that any consistent picture emerges, it is presumably the opposite of what the authors intend: namely, that sweeping liberalization by rich countries will produce outcomes for developing countries that, using any reasonable margin of error, are close to zero. The reasons for small size of the overall effect are immediately apparent, given that agriculture is a small share of industrial country GDP, agricultural trade a tiny share of world agricultural production, and price shifts produce countervailing effects between net importers and exporters.

In terms of the wider debate on agricultural trade and globalisation, the political use of apparently technical econometric exercises by the IMF-World Bank raises further concerns. Both of the modeling exercises cited above reach the conclusion that developing countries stand to gain most in welfare terms by liberalizing their own markets through tariff reductions. At one level, this provides a convenient rationale for the use by the IMF-World Bank of loan conditions aimed at enforcing unilateral market liberalization (Oxfam 2002). But it ignores the potentially damaging implications for smallholder farmers of premature trade liberalization, especially when import prices are artificially depressed through production subsidies.

While the damage inflicted by northern agricultural policies varies across countries, the most important effects include:

- **Artificially depressed prices for staple food producers .**

EU and United States agricultural policies give grain exporters access to cereals at prices far lower than those received by farmers (see below) – and often below the costs of production. In the United States the target price received by farmers is around 30 per cent higher than the intervention price at which grain traders can buy cereals for export. As the world market price-setter for wheat and corn the United States occupies a particularly important role. For smallholder farmers in food importing developing countries, the United States export price sets the terms of competition in local markets.

That competition is highly unequal. In Mexico, import liberalisation under NAFTA has resulted in the United States capturing a growing share of the Mexican corn markets, with exports in 2001 three times their average volume in 1990-1993 (USDA/ERS). Rising imports from the United States have restricted market outlets for Mexican maize farmers, including those in the poverty-belt states of the south where over 40 per cent of corn farmers live below the poverty line (UNDP 1997). The competition between Mexican and American corn farmers is highly unequal given that the latter receive support of between \$6-9bn a year.

By denying domestic smallholders access to urban markets, subsidized exports undermine incentives for agricultural investment, restrict rural employment, encourage a transfer of food tastes to imported cereals, and promote import dependence. When Haiti liberalized its rice market under an IMF programme in the mid-1990s, the country was promptly flooded with heavily subsidized United States rice, destroying livelihoods and leaving the country

heavily dependent on imports. By the end of the 1990s imported rice accounted for almost half of national consumption (IMF 2001). In West Africa, local food staple producers have faced problems competing with imported rice and wheat, reinforcing other factors behind a long-run decline in per capita output (Reardon 1996).

Set against the costs to producers, economists often point to the potential welfare gains for consumers from lower prices. However, viewed in a broader poverty reduction context, there are two problems with the simplified consumer welfare approach. First, imports can break the link between urban and rural economies, isolating rural centers from growth points and restricting the development of dynamic linkages. Second, for low-income countries in particular dependence on food imports implies significant foreign exchange costs, with vulnerable populations exposed to the risks associated with world price volatility. Import liberalization in developing countries has been widely associated with deteriorating balances on food trade. One FAO survey of fourteen countries compared the food trade balance in fourteen countries for the period 1990-1994 with 1995-1998. It found a deteriorating in each case, amounting to over 80 per cent for Senegal and Bangladesh, and 50 per cent for India. Sub-Saharan Africa faces especially acute problems. Currently, there are nineteen countries in sub-Saharan Africa where food imports represent more than one quarter of export earnings (FAO 2001). Unless agricultural productivity can be increased, the region as a whole is unlikely to have the capacity to cover the gap between food needs and production through commercial imports. The central policy challenge is to develop the capacity to grow sufficient food in an environmentally sustainable fashion, not just to increase supply, but also to create income and employment.

- **Reduced and more unstable world prices for commodity exports.**

Subsidised over-production and export dumping drives down international prices and closes down market opportunities for developing countries. At the same time, government subsidies insulate producers and production decisions from world market trends, transmitting instability to world markets

The EU's sugar regime illustrates the problem. Under the CAP, EU sugar farmers – most of them very large-scale – receive high guaranteed prices for 12 millions tons of sugar. The marginal return is sufficient to create incentives to produce a further 4.7 millions tons of non-quota sugar, which is dumped on world markets, making the EU the world's largest exporter.ⁱⁱⁱ One model suggests that the CAP sugar regime operates to lower world prices by 18-22 per cent (Borrel and Hubbard 1999). Apart from large-scale farmers, the sugar processing industry is a major beneficiary of subsidies. Just one company in Britain – British Sugar – is estimated to receive \$100m annually (Oxfam 20002b). The losers in this arrangement include lower-cost developing countries – such as Thailand, Cuba and Mozambique - who lose markets and receive lower export prices. Meanwhile, high tariffs exclude some of the world's poorest countries from the EU

market. While that market has been liberalized under the Everything But Arms proposal, the pace of liberalization in sugar has been tailored to the demands of the sugar lobby. One estimate is that Mozambique is currently losing around \$106m annually as a result of lost export opportunities (Oxfam 2002b). Because EU producers receive a fixed price regardless of world price, they have been immune to the protracted depression in sugar markets and have maintained output forcing others to adjust.

- Restricted market access

Under the right conditions, access to northern markets can provide producers in developing countries with important opportunities for poverty reduction. At a household level, production for exports can support the diversification of livelihoods and create incentives for investment. At a national level, improved market access can help to diversify foreign exchange earnings and reduce the risk of dependence on a narrow range of commodities.

The problem facing developing countries is that tariff and non-tariff barriers in agriculture are exceptionally high. Average tariffs range from 16-20 per cent, with peaks in excess of 100 per cent a common feature. These tariffs are some five-to-six times the average tariff applied by rich countries when they trade with each other in the manufacturing sector, suggesting that the rural poor enter world markets carrying a weighty handicap.

The case of US cotton subsidies

The plight of Africa's cotton farmers highlights in a stark way some of the real human consequences of current farm policies in rich countries. As the world's largest exporter and largest subsidizer, the United States has helped to create one of the deepest and most protracted crises in world cotton markets since the Great Depression, reinforcing African poverty in the process (this section is based on Oxfam 2002c).

Cotton is grown by an estimated 10-11 million households in West Africa. During the 1990s, production in the region has almost doubled, mainly as a result of increased acreage being brought into cultivation (ICAC 2001). While there are serious social and environmental problems associated with cotton production, this expansion has contributed to rural growth and poverty reduction. Because cotton is grown alongside food crops in inter-cropping systems, there is no evidence of displacement of food production (University of Michigan 2001). In addition to its importance at a household level, several countries in the region – including Burkina Faso, Mali, Chad and Benin – are heavily dependent on cotton as a source of foreign exchange earnings.

While cotton yields in West Africa are low by international standards (at around one quarter of the average), the region is one of the world's most efficient producers. This is largely because of the of climate, and the advantages of non-mechanised smallholder agriculture in managing plant developments and the high quality crop assured by hand-picking. According to the IMF,

producers in West Africa can operate profitably at world prices as low as 50/cents a pound (IMF 2002). Few other exporters can rival this even with far higher levels of productivity this because of associated capital costs and lower quality crops.

In recent years, producers in Africa have had to adjust to the deepest and most protracted price depression in recent memory. While prices have marginally increased in recent months to 39 cents/lb, this is well below the long run average of 70 cents/lb. Several factors have been at play. These include new entrants to the market, rising productivity in China, and the impact of the global economic slowdown on world markets for garments and textiles. But the single biggest factor driving down prices has been the structure of farm subsidies in the United States

While there are a large number of countries growing cotton, just four – the United States, China, India and Pakistan – account for about two-thirds of total production. The United States occupies a special position in this group not just as a major subsidizer, but because it exports a large share of domestic production, amounting to one-half of the total. These exports account for almost one-third of total world exports. It follows that United States subsidies have powerful world market price effects.

Even by the heady standards of current farm policy, cotton producers occupy a special position. They receive the equivalent of \$225 per acre in subsidies, or some five times the rate for cereals producers (Figure *). This is also the sector with the most concentrated distribution of benefits. The largest 1 per cent of cotton subsidy recipients account for over one-quarter of total transfers, and the top 10 per cent for three-quarters. Ten individual farm corporations received payments in excess of \$17m in 2001.

While these subsidies clearly confer significant benefits on a few American farm corporations, they generate significant costs elsewhere. Estimates by the International Cotton Advisory Committee (ICAC) suggest that cotton subsidies in the United States reduce world prices by 26 per cent, or 11 cents/lb. Ironically, this has been one of the factors driving up the costs of the subsidy programme. In 2001-2002, payments to cotton growers from the Commodity Credit Corporation (CCC) amounted to \$3.6bn. The world market value of the United States crop for the same year was \$3bn. In other words, cotton was grown at a net cost to the American economy.

That cost pales into insignificance against the costs inflicted on Africa. Using the ICAC model, Oxfam estimates the total foreign exchange costs of American cotton subsidy programmes for the region at \$301m – equivalent to around one quarter of all United States aid to Africa. Eight countries in West Africa account for two-thirds of this loss (see Figure *). The small size of the economies involved and their high level of dependence on cotton produced extreme economic shocks. To illustrate the order of magnitude:

- Burkina Faso lost the equivalent of 1 per cent of GDP and 12 per cent of export earnings

- Mali lost 1.7 per cent of GDP and 8 per cent of export earnings

For a group of countries with some of the worst human development indicators in the world for rural poverty, child mortality, and illiteracy, economic losses on this scale clearly imply grave consequences. If anything, the financial loss figures understate the impact. This is because household income in rural economies generates linkages and creates demand that spread growth more widely through a series of multiplier effects. Research carried out by IFPRI found that \$1 additional dollar of farm income in Burkina Faso raised total income in the local economy by \$1.8 (Delgado 2000) This would suggest that the real losses in income sustained as a result of United States cotton subsidies has been far higher than suggested by the static loss. In addition, governments in the region have spent an estimated \$60-80m protecting their cotton sectors from world price trends, implying a significant fiscal burden and diversion of resources from spending in priority social areas.

United States policies on cotton subsidies raise far wider questions about tensions between development policy rhetoric and trade programme realities. Some countries in West Africa – such as Burkina Faso and Benin – have lost more as a direct consequence of these subsidies than they have gained in HIPC Initiative debt relief. Others – such as Mali – have lost more than they get in American aid. The experience of Africa’s cotton producers also provides an insight into the realities of the ‘level playing field’ in world agriculture. America’s 25,000 cotton farmers collectively received more in subsidies in 2001 than the total national income of either Mali or Burkina Faso, countries with populations of over 11 million people (Figure *).

When is a subsidy not a subsidy?

The ministerial declaration adopted at the launch of the Doha Round includes a superficially ambitious commitment: “we commit ourselves to comprehensive negotiations aimed at substantial improvements in market access; reductions of, with a view to phasing out, all forms of export subsidies; and substantial reductions in trade distorting support.” (WTO, 2001). Recent historical evidence suggests that the outcome may be less encouraging than the rhetoric.

Under the Uruguay Round AoA, specific targets were set in each of the above areas, including a 20 per cent decline in support and a 36 per cent decline in export subsidies. These targets have been met with something to spare, despite an increase in support for agriculture over the base period (1986-1988) set for measuring progress under the AoA (OECD 2002). How has this been achieved? In large measure by changing the definition of subsidies in general and export subsidies in particular.

The relevant phrase in the Doha declaration is ‘trade distorting support’. Under the AoA, which was the product of a compromise between the United States and the EU, certain categories of support were deemed to be outside of WTO discipline. Direct payments of the type provided by the United States were categorized as Green Box, ostensibly on the grounds that they had minimal effects on production. Another discipline-free box – the Blue Box – was created for EU

payments that included supply control measures, such as a requirement that farmers taken land out of cultivation. Both categories were given the status of 'decoupled' payments on the grounds that they had minimal effects on production and trade.

This redefinition of subsidies helps to explain the widening gap between the PSE measure of support used by the OECD, and the alternative measure – the Aggregate Measure of Support – used for WTO purposes (Figure *). In addition the 1986-88 base period was one of exceptionally low world prices and commensurately high tariffs, support levels, and export subsidies. This left industrialized countries with ample scope for meeting the AoA targets without having to make serious adjustments (Konradiates 2000).

Both the European Union and – more ambiguously – the United States are entering the Doha Round bent on excluding decoupled payments from future WTO disciplines. This has important implications for developing countries. In crude form, these implications can be demonstrated by Figure *, which captures the structure of support for American cotton farmers under current legislation. This shows that around two-thirds of total transfers to farmers will take the form of decoupled payments. The European Union operates a broadly analogous system in the cereals sector (Figure *), with a similarly heavy dependence on 'decoupled' payments during periods of low world prices. In 2000/2001 these payments raised farm incomes some 60 per cent above export price levels.

In the official view of the United States Department of Agriculture (USDA), the direct payments and counter-cyclical payments (which compensate farmers when world prices fall below specified levels) introduced under the 2002 Farm Security and Rural Investment Act (FSRI) retain all the features of decoupled payments. In theory, farmers can receive both transfers without planting any of their land at all, since payments are calculated on the basis of a formula using acreage and yield for a previous production period (known as the base period). When the farmer makes a planting decision, so the argument runs, there is no incentive provided by these payments to increase production at the margin, since the transfer is fixed in advance (USDA/ERS 2002).

There are several problems with this argument that apply with equal force to the EU's direct payments. First, decoupled payments provide farms with liquidity and can be used to finance investments that will raise future production. Second, the constant updating of the base period in the United States means that producers have an obvious interest in increasing crop acreage and yield, since this is what compensation rates are based on. Finally, production decisions today are clearly based on expectations about future support. To the extent that decoupled payments shield against risk they can be expected to encourage investment and generate higher output during periods of low world prices.

In reality, it is virtually impossible to design subsidy programmes that do not have some effect on production decisions and trade. Specific programmes defined as decoupled have important

effects in both areas (OECD 2001; Josling 2000). From the standpoint of an African farmer attempting to compete in world markets against American cotton subsidies or in local markets against European Union cereals, what matters is that the crop is being marketed at a price far below the income received by the producer in the exporting country. The net result is that they are competing against export dumping.

To the extent that direct payments facilitate levels of production that exceed domestic demand and the transfer of the resulting surpluses to world markets, they are production and export subsidies – and they should be treated as such for WTO purposes. The same applies to other interventions. For example, the EU, one of the world's highest cost exporters of sugar, claims to maintain its domination of global markets without export subsidies. In fact, it achieves this remarkable outcome by financing exports through a small tax on the guaranteed price paid to farmers, which is currently some three times higher than world market levels. This too is a transparent case of export subsidization by another name and should be treated as such.

Current farm policy directions in the United States and the EU give an added urgency to the challenge of addressing the problem of disguised export dumping. In the United States the FSRI is expected to provide \$73bn in additional support to agriculture over the next decade (OECD 2002). Moreover, by updating the base acreage for calculating direct and counter-cyclical payments, the new legislation has strengthened the link between government support and output. According to the USDA's own calculations, an additional 2 million acres will be brought into cultivation in 2003 as a result of the FSRI.

In the European Union the direction of farm policy reform remains uncertain, as witnessed by the failure to submit a negotiating proposal to the WTO in accordance with the Doha schedule. The European Commission's 'Agenda 2000' proposals envisage continued movement towards decoupled support, combined with the consolidation of the EU's global market position. In November, 2002, political leaders adopted a budget that will keep CAP spending at current levels until 2013 (adjusted for inflation). Whatever the outcome of the clash between pro- and anti-reformers, there would appear to be little likelihood of CAP reform significantly reducing export surpluses in core product areas.

Three principles for the Doha round and beyond

Reduced to its essentials, the central problem posed by agricultural policy in rich countries for the rural poor in developing countries is the in-built support that it provides for over-production and export dumping. Corporate traders in rich countries are currently being given access to surpluses for export on heavily subsidized terms that are detrimental to the interests of developing countries. It follows that the central challenge for the Doha Round is to address the dumping problem, while at the same time providing a framework in which developing country can achieve broader rural development objectives. Three measures suggest themselves:

- The phasing out of direct and indirect export subsidies. Industrialised countries should commit themselves to a schedule for phasing out export subsidies, including implicit subsidies and nominally decoupled support measures for production levels that exceed domestic demand
- A review of decoupled payments. There is a pressing need for independent technical work to decompose decoupled support measures so that implicit export subsidy levels can be more effectively estimated.
- Recognition of the special status of developing countries. For reasons dealt with in this section, there are strong grounds for developing countries to protect their food systems – where necessary through tariffs and quotas – for purposes of rural poverty reduction and food security. This would remain the case even if world markets were not distorted by industrialized country subsidies. One option, advocated by some developing countries, is the inclusion in the WTO of a ‘development box’ under which food security would take priority over any liberalization commitment. Another option, recently advocated by Sri Lanka is a special safeguards provision. This would be activated under pre-defined conditions, such as a surge in imports, or a fall in import prices below a national average level.

Ultimately, success in the Doha Round will depend on farm policy reform in rich countries. This does not have to be a zero sum game, in which poor farmers in rich countries lose as poor farmers in poor ones gain. There is scope for a huge redistribution of agricultural support away from large farms and agri-business companies towards rural livelihoods, small farmers, and wider public policy goals, such as environmental sustainability. The central challenge is to de-intensify production under a new, more sustainable system of production, under which support is geared towards lower levels of output.

It is readily apparent that agricultural exports are not a panacea for rural poverty in developing countries. The strength of the linkages between export activity and poverty reduction will depend critically on conditions in individual countries, including levels of inequality in access to productive assets and markets. However, the reform of rich country farm policies and a new WTO regime could help to create an enabling environment for pro-poor agricultural trade. The alternative approach of maintaining the current regimes will continue to marginalize the rural poor, further undermining the already strained credibility of the WTO in the process.

Conclusion

To conclude with the observation made at the outset, there is nothing predetermined about globalization. Market economics provides no rationale which dictates that smallholder farmers cannot benefit from global market opportunities. Indeed, it suggests that they may have advantages over large-scale producers. The problem at present is that political choices taken by governments and companies in production and marketing are skewing the playing field towards the latter. In the case of northern agricultural policy, there is a deep public interest in stopping the current cycle of surplus production and export dumping, both for domestic reasons and to

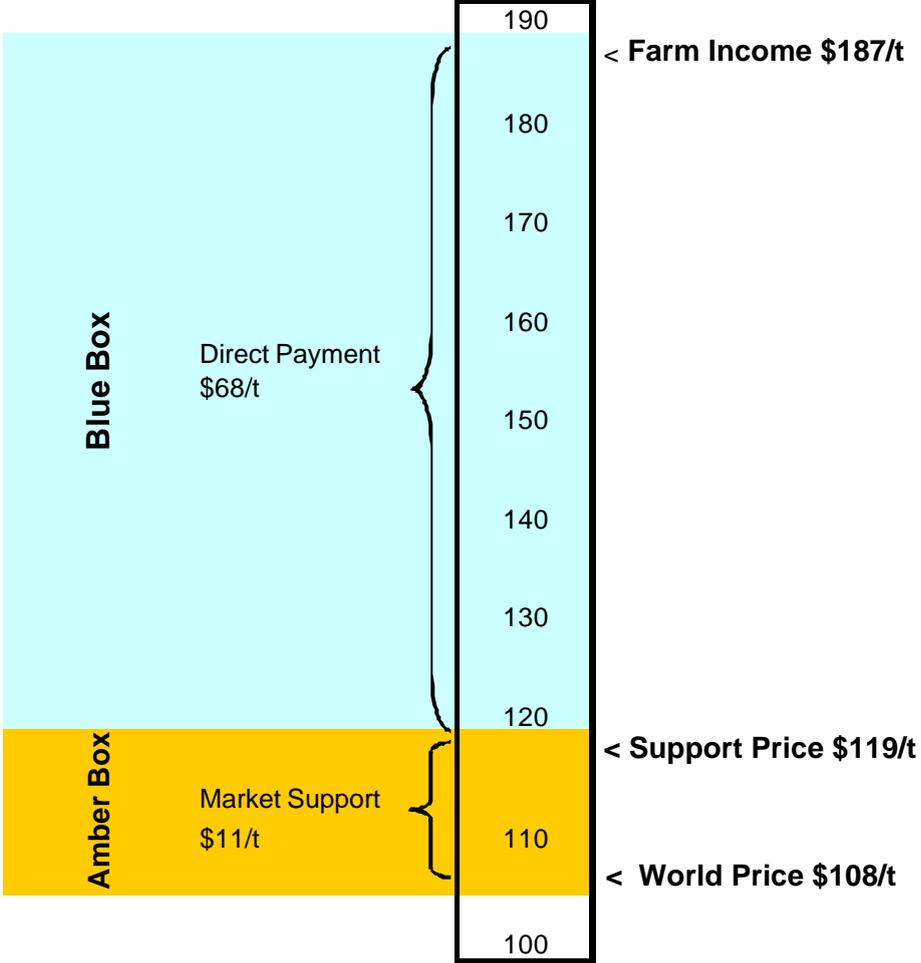
support international poverty reduction. Conversely, there is a powerful set of private interests seeking to maintain the current system of corporate welfare in the guise of farm subsidies. It is up to governments to assert the public interest and to change the rules of the game. Nothing is inevitable, except perhaps for the persistent poverty and deepening inequality that will attend failure to act.

ⁱ The PSE is an indicator of the annual monetary value of gross transfers from consumers and taxpayers to agricultural producers arising from policy measures that support agriculture, regardless of their impact on production. There is an element of double counting since subsidized exports drive down world prices and the PSE captures the effects of the tariffs that maintain a wedge between national and international prices.

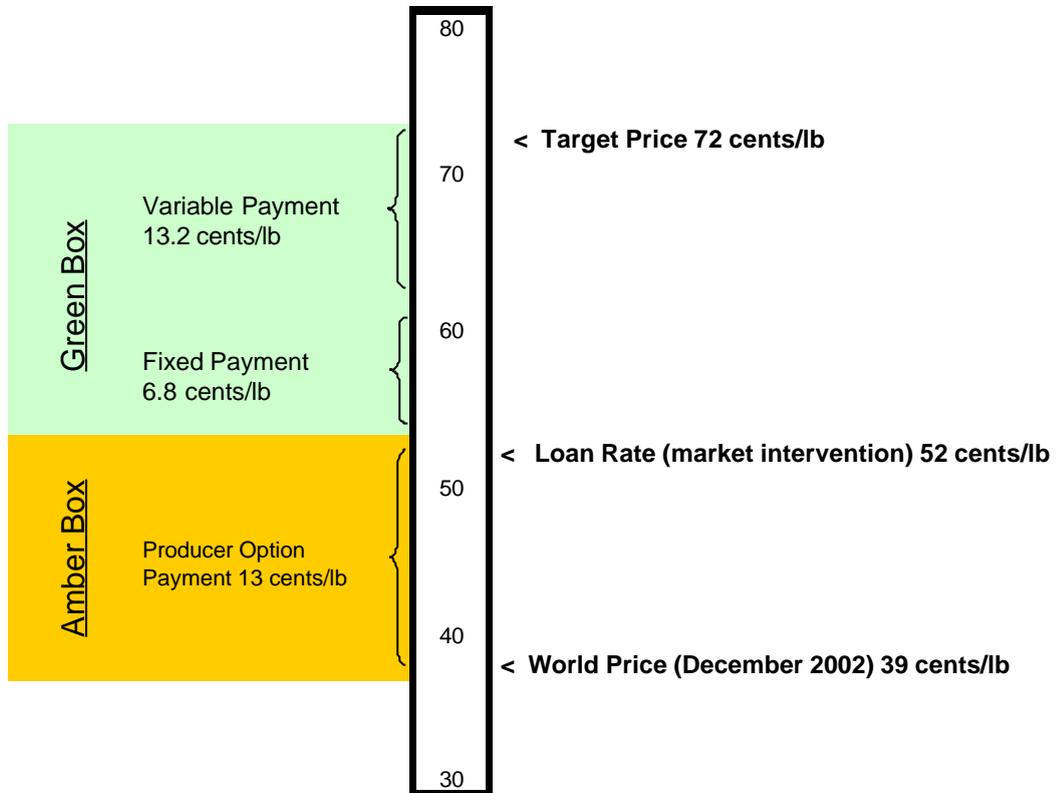
ⁱⁱ The EU's PSE represented 39 per cent of the value of farm output in 2000/2001 compared to 21 per cent in the United States, or \$100bn and \$49bn respectively.

ⁱⁱⁱ The EU also imports at domestic guaranteed prices 1.6 million tons of sugar from the African, Caribbean and Pacific (ACP) countries. An equivalent amount is then re-exported at prices currently approximating one-third of the domestic level.

Cereals sector support in the European Union (1999/2000)

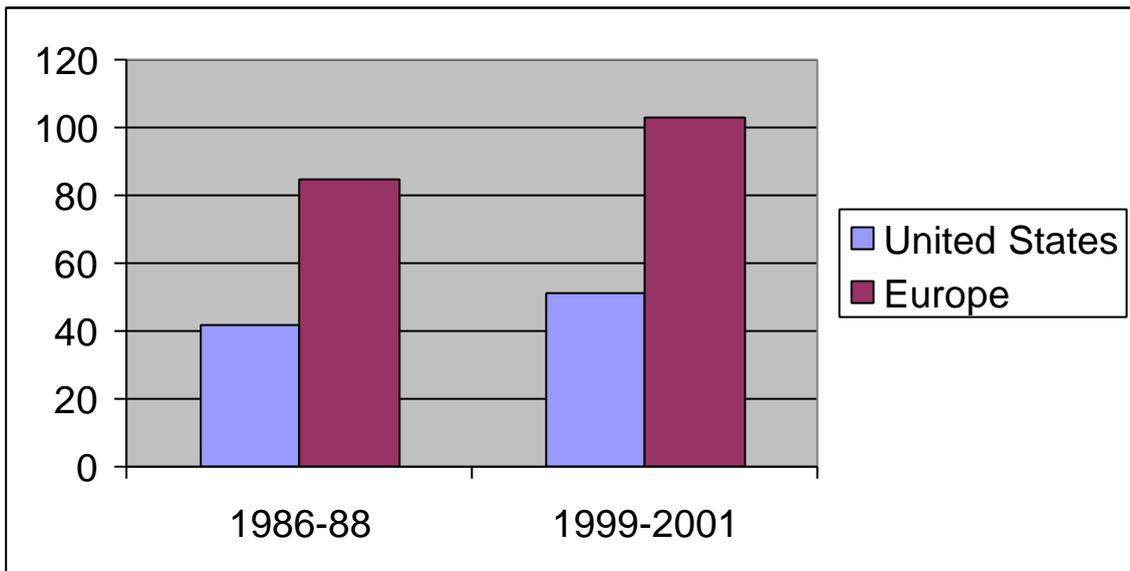


Support to US Cotton Farmers under the Farm Security and Rural Investment Act



Producer Support Estimate (\$bn)

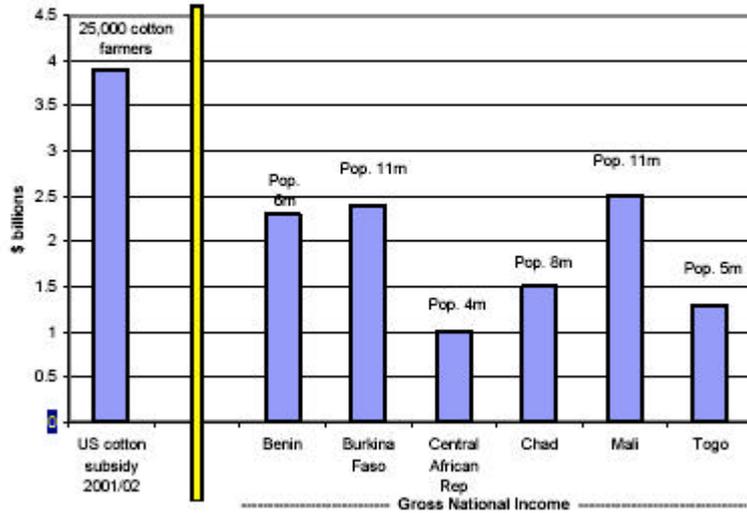
	1986-88	1999-2001
United States	41.8	51.2
Europe	84.9	103.1



Annex 5: Foreign exchange losses as a result of US cotton subsidies in selected countries in Sub-Saharan Africa (\$m)

Country	Actual cotton export earnings in 2001/02 (\$m)	Export earnings with the withdrawal of US subsidies (\$m)	Value lost as a result of US subsidies (\$m)
Benin	124	157	33
Burkina Faso	105	133	28
Cameroon	81	102	21
Central African Rep.	9	11	2
Chad	63	79	16
Congo	3	4	
Cote d'Ivoire	121	153	32
Ethiopia	18	23	5
Ghana	7	9	2
Guinea	13	16	3
Kenya	5	6	1
Madagascar	10	13	3
Malawi	6	8	2
Mali	161	204	43
Mozambique	23	29	6
Nigeria	55	69	14
Somalia	2	3	1
South Africa	17	21	4
Sudan	65	82	17
Tanzania	79	100	21
Togo	61	77	16
Uganda	18	23	5
Zambia	29	37	8
Zimbabwe	69	87	18
Total	1144	1446	302

Figure 3: US cotton subsidy and the gross national incomes for selected West African countries in 2000 (\$billions)



Source: World Development Indicators, World Bank, 2002, and US Department of Agriculture