

Module 2

The WTO Agreement on Agriculture (AoA)

Introduction

Global agricultural trade has increased dramatically since the end of WWII. Countries choose to trade because consumers benefit from having more choices and because some countries are better able to produce particular agricultural products than others. International rules governing trade are equally important as they are a major reason why smooth and efficient global exchange is possible. In this section we will introduce the World Trade Organization (WTO) Agreement on Agriculture (AoA). This is a set of rules governing global agricultural trade policies. Agricultural trade contributes a relatively small amount to total world trade in all goods; however, countries tend to be very sensitive to agricultural issues as many hope to maintain domestic agricultural production and protect their local producers.

Objective

After completing this module you should understand why the AoA was developed and why it is important to international trade in agricultural products.

Some key concepts you will learn about in this section are:

- the history of the AoA,
- specific provisions of the AoA,
- why a standard set of rules governing trade helps global commerce expand,
- a U.S. commodity that has seen significant growth in trade since adoption of the AoA.

Section 1 - The WTO and the AoA

Objectives

In this section you will learn about

- the history of the Agreement on Agriculture
- the nine organizing principles of the World Trade Organization (WTO)
- and, why the AoA is important to all members of the WTO

Introduction

The primary instrument for multilateral regulation of international trade in all products is the General Agreement on Tariffs and Trade (GATT), which was first negotiated following World War II. Between 1949 and 1994 the GATT was renegotiated seven times and, although not yet complete, a new Doha Round of negotiations was begun in 2002. A number of perceived weaknesses in the original GATT Agreements with respect to agricultural trade were addressed in the Agreement on Agriculture, contained in Annex 1 to the 1994 Agreement establishing the WTO. The goal of the AoA is to reduce current and future use of trade-distorting policies and move towards freer agricultural markets in accordance with the organizing principles of GATT.

Nine Principles of the WTO

Nine organizing principles have been recognized as the fundamental basis for commercial trade relations and negotiations between countries since World War II (Josling, Tangermann, and Warley, 1996). It is important to think about the influence of these principles in negotiations regarding global agricultural trade (Thornsbury, 1998).

1. People will enjoy a higher standard of living if they have free access to all the world's material and human resources through trade. The lowering or removal of barriers to trade should therefore be an objective for all governments, though they are not obligated to undertake it.
2. All countries benefit from the order, fairness, and predictability that come from trade relations based on rules rather than on economic weight alone. The principles and standards of acceptable conduct that guide international commerce should therefore be codified and embodied in international commitments of a legal character.
3. Market forces should be the major regulator of international commerce. Governments should be discouraged from erecting direct or indirect barriers to trade, and their interference with market forces should be permitted only in exceptional and specified circumstances.
4. If national efforts to promote economic and social objectives affect trade relations, they are of international concern. Countries should respect the legitimate trade interests of other countries in devising and implementing domestic policies and programs, and should seek to avoid harming them.
5. Where protection is given it should be afforded only by duties and similar direct charges. The tariff is a visible barrier that readily lends itself to negotiation. Indirect methods of protection should not be used save in exceptional circumstances and according to prescribed rules.
6. Trade barriers of all types should be administered on a nondiscriminatory basis. Imports should be treated in the same manner as national products in respect to charges and regulations. Any trade benefit conferred on one

country should be extended unconditionally to all other suppliers. New preferences should not be created by raising trade barriers, and all preferences should be progressively reduced and ultimately eliminated through the liberalization of trade.

7. When negotiations to reduce trade barriers are entered into, they should be carried out in such a manner as to establish a balance of mutual advantage.
8. If the balance of advantage established in negotiations is subsequently disturbed by the actions of a country, means should be provided for its restoration. If a mutual accommodation cannot be reached by consultation, balance can be restored by the measured release of the injured countries from some of their obligations.
9. Maximum use should be made of the opportunities for consultation and cooperation provided by the GATT for making the above principles effective, for solving common problems, and for resolving trade disputes.

The AoA is important because it helps level the playing field for all participating members by eliminating or reducing some unfair trade and support practices used by many countries in the past. A review of the concepts of comparative advantage and competitive advantage will help us understand why trade is important and how governments can influence trade through policies.

A comparative advantage in production means that the opportunity cost of producing that product is lower for the producer than for any other product they might produce. This concept helps explain why countries trade, since specialization in production along with exchange leads to better conditions for producers and consumers (see Module 1 for more detail).

A competitive advantage means that the rules or institutions shaping commerce between trading countries give one country an advantage over another. For example, policies that limit imports of wheat to a country mean that domestic producers are able to obtain a higher price and so can afford to produce more. Trade distorting support of agriculture by wealthy nations was the main impetus for development of the AoA.

Conclusion

The WTO was established in 1994 as the international body which oversees the development and application of trade rules and regulations between countries. The guiding principles of the WTO are important as they clearly outline the purpose and goals of the agreement. The Agreement on Agriculture was also developed in 1994 as the guiding document for trade rules addressing agricultural products and for future agricultural trade policy development.

Key Terms

Agreement on Agriculture (AoA) – Negotiated during the Uruguay Round (1986 – 1994), the goal of the AoA is to reduce current and future use of trade-distorting policies and move towards freer agricultural markets in accordance with the organizing principles of GATT

World Trade Organization (WTO) – The international body which oversees the development of rules on trade.

Quiz

1. The creators of the AoA recognized a common set of organizing principles for the agreement, how many were there?
(answer 9)
2. The WTO is the international body which oversees the development of rules on trade by individual countries.
(True or False, answer True).
3. Important organizing principles of the WTO include
 - a. Fairness
 - b. Free Trade
 - c. Non-discrimination
 - d. All of the above
 - e. None of the above

(Answer is D)

Section 2 - The Three Provisions of the AoA

Objectives

In this section you will learn about

- the Market Access Provisions of the AoA
- the Export Subsidy Provisions of the AoA
- and, the Domestic Support Provisions of the AoA

Introduction

Three distinct types of trade distorting policies that impact agricultural markets are addressed in separate provisions of the AoA: *restricted market access, export subsidies, and domestic support.*

Market Access Provisions

The *market access* provisions of the AoA were developed to reduce tariff and non-tariff barriers to trade. A tariff is a duty (or tax) levied by an importing country on goods transported from another country or customs area. Non-tariff barriers to trade are non-tax policies, such as quotas, governing commerce specific to each country or region that may be used to restrict trade, most often imports from other countries. Tariffs and non-tariff barriers raise the domestic price of a good, potentially making it less attractive to consumers than the same good produced within the country.

Export Subsidy Provisions

Export subsidies are a second broad type of policy addressed by the AoA. A government subsidizes exports by providing additional payments or benefits to domestic producers in addition to the market price they receive. Export subsidies work by effectively lowering the price of an agricultural good on the world market so that it is as attractive to consumers as goods produced at a lower cost in other countries. WTO member countries agreed to limit the subsidization of agricultural exports so that producers around the world could participate in “freer” trade. Provisions are made for emergency situations when the survival of an entire industry within a country or region is threatened.

Domestic Support Provisions

Rules on *domestic support* of agricultural production in the AoA limit the amount and types of support member countries can use to subsidize production within their own borders. The U.S., and other countries, support agricultural sectors through many different types of policies, including: purchases of surplus production, low interest operating loans, price supports for certain crops, and emergency payments made during extremely low price periods.

Conclusion

Three distinct types of trade distorting policies that impact agricultural markets are addressed in separate provisions of the AoA: *restricted market access, export subsidization, and domestic support.* Obviously, all of these provisions were developed to help even the terms of trade between countries. For producers in poor and developing countries, these provisions are

very important as they make them more competitive with producers in wealthy countries who have historically received larger amounts of domestic support.

Key Terms

Non-tariff barrier - non-tax policies, such as quotas, governing commerce specific to each country or region that may be used to restrict trade, most often imports from other countries.

Tariff - is a duty (or tax) levied by an importing country on goods transported from another country or customs area

Quiz

1. The three provisions of the AoA include
 - a. Market Access provisions
 - b. Export Subsidy provisions
 - c. Domestic Support provisions
 - d. Tariffication provisions
 - e. a,b,and c(Answer is E)
2. Rules on domestic support of agricultural production in the AoA limit the amount and types of commodities member countries can subsidize within their own borders
T or F (answer is F)

Section 3 - Why are Common Laws Regulating Trade Important?

Objectives

In this section you will learn about

- why common laws on trade are important and how they can be beneficial to all involved
- an example from U.S. history which illustrates the importance of common and consistent trade laws
- and, the importance of agricultural trade to the U.S. and Michigan.

Introduction

Common laws regulating trade are important because they help to level the playing field for all producers and they reduce the additional costs of doing business when a myriad of rules and regulations exist. The cost savings may then be passed on to consumers. You can imagine the difficulty of exporting a product to several different countries that all have slightly different requirements for the composition and appearance of a product. In addition, rules and regulations on trade can be used by countries to block products from their market when the imported goods compete with domestically produced goods.

Trade and Commerce Laws – An example from U.S. history

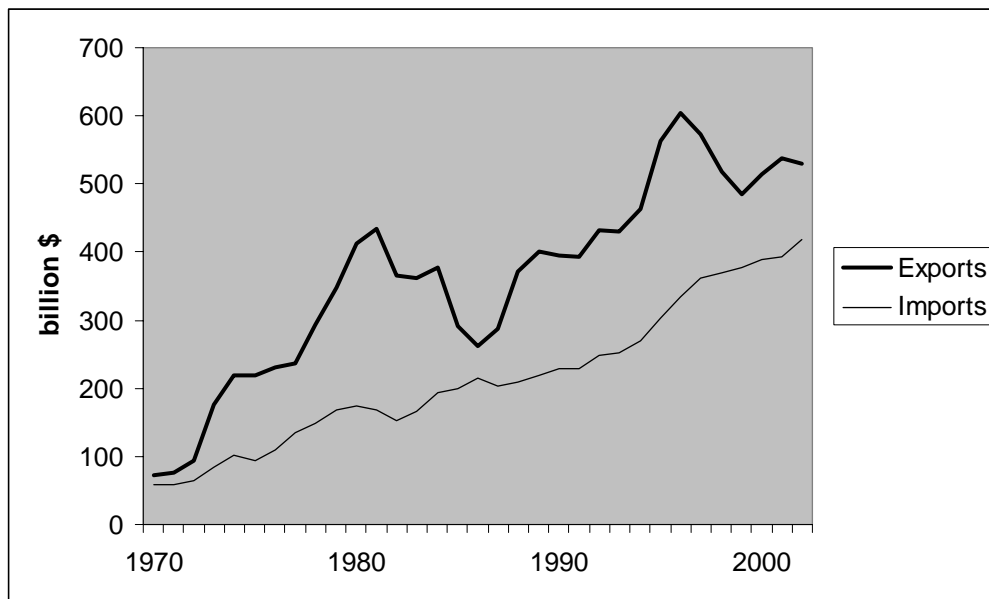
An excellent example of why common laws on trade are important can be taken from early U.S. history. Prior to the signing of the Constitution, the Articles of Confederation were the first documents developed to guide the U.S. in developing its laws and regulations. Under the Articles, states were given the right to develop their own laws governing interstate commerce. Each state developed protectionist policies aimed at maintaining favorable terms of trade for its residents, largely as a result of lobbying by interest groups. Some states minted their own currency during this time, making interstate commerce even more difficult, as there was no systematic way to establish conversion rates between the many different currencies. Recognizing the problems individual protectionist policies were causing for the Union, the writers of the constitution developed the Commerce Clause. This clause took the right to regulate commerce away from the states and gave it to Congress where a common set of rules was established.

As this bit of history illustrates, there are several reasons why a common set of rules is important for trade. Transaction costs are the costs of doing business and might include, for example, the time it takes a U.S. processor to find out about and comply with the diverse labeling laws of the seven different countries to which he or she ships products. A common law on all trade greatly reduces these often “hidden” costs.

Another reason why a common set of laws is important is that strategic behavior among special interests in a single country could lead to trading rules (like tariffs, for example) that are not in the best interest of all of the country’s residents. A common law administered by an objective party, like the WTO, helps ensure that the power of interest groups in one country is balanced by the interests of other countries, and so, levels the playing field for all the participants involved. This is especially important to developing countries who are resource poor or otherwise disadvantaged.

U.S. and Michigan Agriculture and the WTO

Trade is very important to agriculture in the U.S. and Michigan. As noted in Module 1, trade provides additional outlets for production, more choices for consumers, and allows producers to specialize in goods where they have a comparative advantage. More transparent and fair rules of trade increase the rate at which trade is possible. For example, graph 1 below shows how trade has grown over the past 30 years in the U.S. Of course technological innovations in production, more intensive management practices, and growing foreign incomes, explain some of this growth. This is also a period during which the U.S. entered into several trade promoting agreements, like those with Israel (mid 1980s) and the NAFTA group (early 1990s), in addition to the AoA in 1994.



Graph 1. Total value of U.S. agricultural exports and imports between 1970 and 2002 (Source: USDA-ERS)

Key Terms

Commerce Clause - Clause in the U.S. constitution which gave the power to regulate commerce between states to the federal government

Transaction Costs - the additional costs of doing business when a myriad of rules and regulations exist

Quiz

1. Between 1970 and 2002 U.S. agricultural exports increased by approximately?
 - a. \$100 billion
 - b. \$200 billion
 - c. \$300 billion
 - d. \$400 billion(answer is D)
2. A common law on all trade helps in reducing “hidden” costs in agricultural transactions. T or F (answer is T)

Conclusion

A common set of laws facilitates exchange by maintaining fair and consistent trade rules for all involved. Just as the U.S. is involved in negotiating the rules of the WTO, states were once involved in developing the Commerce Clause of the U.S. Constitution, which gave the power to regulate trade to the federal government.

Game

This is a matching question. Students will be given the list of commodities and asked to insert them next to the ranking of value.

Michigan's top agricultural exports in 2002

Correct answer

Rank	Commodity	Value (Millions of dollars)
1	Dairy products	712
2	Greenhouse/nursery	545
3	Soybeans	365
4	Corn	365
5	Cattle and calves	205
6	Hogs	166
7	Sugar beets	111
8	Wheat	104
9	Potatoes	93
10	Apples	71

Source: U.S. Department of Commerce, International Trade Administration (www.ita.doc.gov) and ERS Michigan State Fact Sheet. Available at <http://www.ers.usda.gov/StateFacts/MI.htm>

Anecdote: Michigan's exports: top destinations in 2002

Country	Percentage of Michigan total agricultural exports
Canada	77%
Mexico	6%
United Kingdom	4%
Italy	3%
Japan	3%
France	1%
Spain	1%
Germany	1%

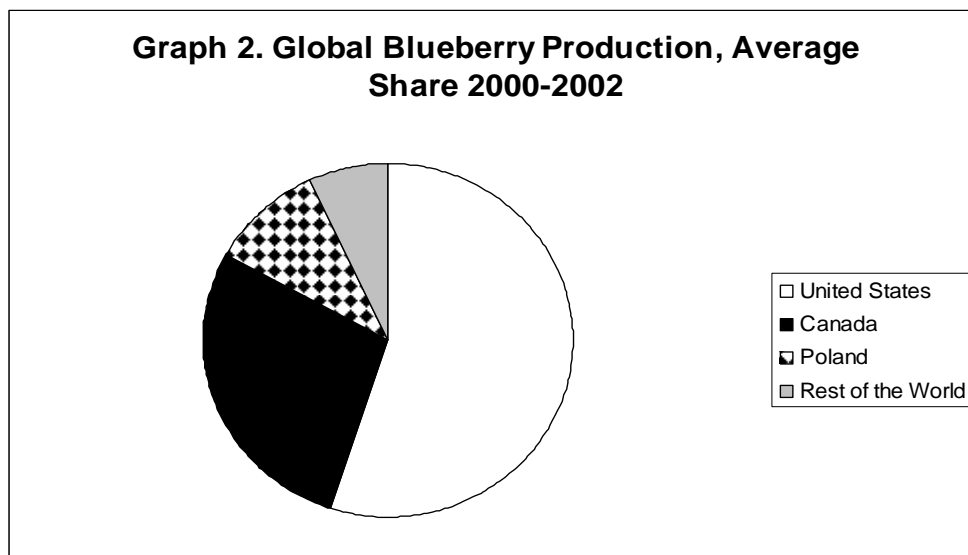
Source: Based on data from the U.S. Department of Commerce, International Trade Administration (www.ita.doc.gov)

Conclusions

In this module you have learned about the WTO AoA, and specifically about the three provisions of the AoA which have direct effects on U.S. agricultural trade. You have also learned something about why consistent rules on trade are so important for commerce between legal entities, be they competing states, or global trading partners, like the U.S. and Japan.

Case Study: Michigan Blueberries and the WTO

Blueberries are indigenous to North America and have been in commercial production since 1916 (ERS, 2003). Prior to 1970, Canada was the largest producer and exporter of blueberries in the world.

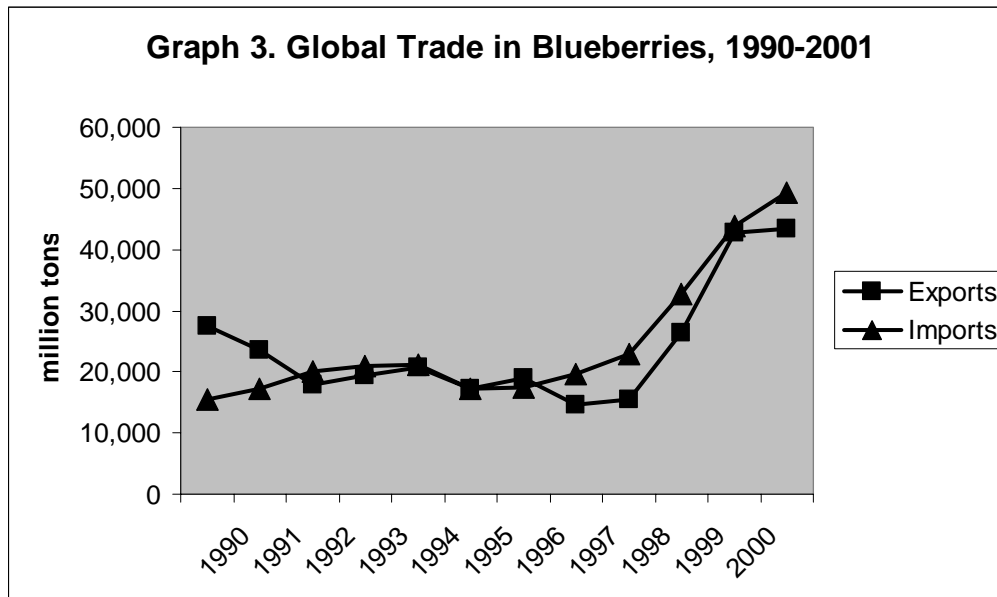


(Source: USDA-ERS Fruit and Tree Nuts Outlook, 2003)

Today, the U.S. is the world's largest producer of blueberries, and Maine and Michigan produce over half of total U.S. production. Following strawberries, blueberries are the most important berry crop in the U.S. in terms of value. Between 2000 and 2002, the value of blueberry production averaged \$200 million (ERS, 2003). Domestic demand for fresh and processed blueberries has been rising steadily since the mid-1980s. Reasons for expanded demand include technological improvements in production, expanded production (both acreage and variety), increasing consumer awareness of the health attributes of blueberries, and improved convenience of blueberry products.

Exports of blueberries have expanded since the mid-1980s as well (Graph 3). The largest market for exported U.S. blueberries is Canada, which imports both fresh and frozen product. Japan has developed as an important export market for U.S. blueberries, absorbing 40 percent of total exports in 2002. At least two factors can explain increasing demand for U.S. blueberries in Japan. First, there has been a concentrated effort by the U.S. blueberry industry to introduce

Japanese consumers to the product. Second, under the Uruguay WTO Round AoA, Japan agreed to lower its tariff on imported blueberries by 40 percent.



Sources:

USDA-Economic Research Service. "Commodity Highlight – Blueberries". July 30, 2003. Available at <http://www.ers.usda.gov/Briefing/FruitAndTreeNuts/fruitnutpdf/blueberry.pdf>. Accessed October, 2003.

USDA-Economic Research Service. "Fruit and Tree Nuts Outlook- 2003". Available at <http://www.ers.usda.gov/Briefing/FruitAndTreeNuts/>. Accessed October, 2003.

Questions

1. What are the three major provisions, or pillars of the AoA?
2. What are two reasons why a common set of rules governing global trade are important?
3. What are three reasons why global agricultural trade has increased over the past 50 years?
4. How have U.S. blueberry producers benefited from the AoA rules?

Glossary

Commerce Clause - Clause in the U.S. constitution which gave the power to regulate commerce between states to the federal government

Transaction Costs - the additional costs of doing business when a myriad of rules and regulations exist

World Trade Organization (WTO) – The international body which oversees the development of rules on trade.

Sources of More Information

Food and Agriculture Organization of the United Nations - www.fao.org

GlobalEdge - <http://ciber.msu.edu/globalEDGE/default.asp>

World Trade Organization website – www.wto.org

References

Food and Agriculture Organization of the United Nations. “Multilateral Trade Negotiations on Agriculture: A Resource Manual”. Rome, 2000

Josling, Timothy E., Stefan Tangermann, and T.K. Warley (1996). Agriculture in the GATT. New York: St. Martin’s Press, Inc.

Thornsbury, Suzanne "Technical Regulations as Barriers to Agricultural Trade" Ph.D. Dissertation, Department of Agricultural Economics, Virginia Tech, October 1998.

United State Department of Agriculture – Economic Research Service. “Trends in the U.S. Blueberry Industry”. in Fruit and Tree Nuts Outlook, July 30, 2003.

