

Chapter 1

Current agricultural policies: An overview of their impact and possible reforms

This chapter presents an overview of the main findings of the study. It first summarises the main changes that have occurred in agricultural markets and policies since 2000. Second, it provides an overview of the results of the assessment conducted to explore the impacts of current agricultural domestic support and trade policies on markets and countries and the implications these have for future multilateral reform efforts. Third, it explores the impacts of various reform efforts along with policy developments that see an increase in agricultural protectionism in some regions. The effects of these scenarios are explored for developed and developing economies.

1.1 Introduction

Since the latest round of WTO negotiations began in 2001, world agricultural markets have evolved significantly. Production, prices and trade flows have been transformed while over the same period countries have also altered their agricultural trade and domestic support policies substantially. This study focuses on developments in world agricultural markets and in the policies (defined as domestic support policies and trade policies) of major agricultural producing regions that have occurred since 2000. The impacts of these policies on global production, trade and welfare (proxied by private household consumption) are assessed along with the effects of possible multilateral trade reform scenarios. The assessments are made through an application of the OECD's computable general equilibrium model, METRO, in conjunction with the AGLINK-COSIMO model. What is not modelled is the range of non-tariff and behind the border barriers that can also influence trading patterns and therefore production and prices. These remain an area for future research.

A number of studies that have analysed the potential gains from agricultural liberalisation since the Doha round began. These studies have generally used models that have 1997, 2001 or 2004 as the base year on which the impacts are assessed. This study provides an update on this work through analysing the impacts of current policies and reform with reference to changes that have occurred in markets and policies since 2000. Further, it extends the analysis by making use of the OECD's METRO model that provides for a more detailed examination of trade flows better depict the greater interdependencies in trade that have been created with the increasing presence of global value chains (GVCs).

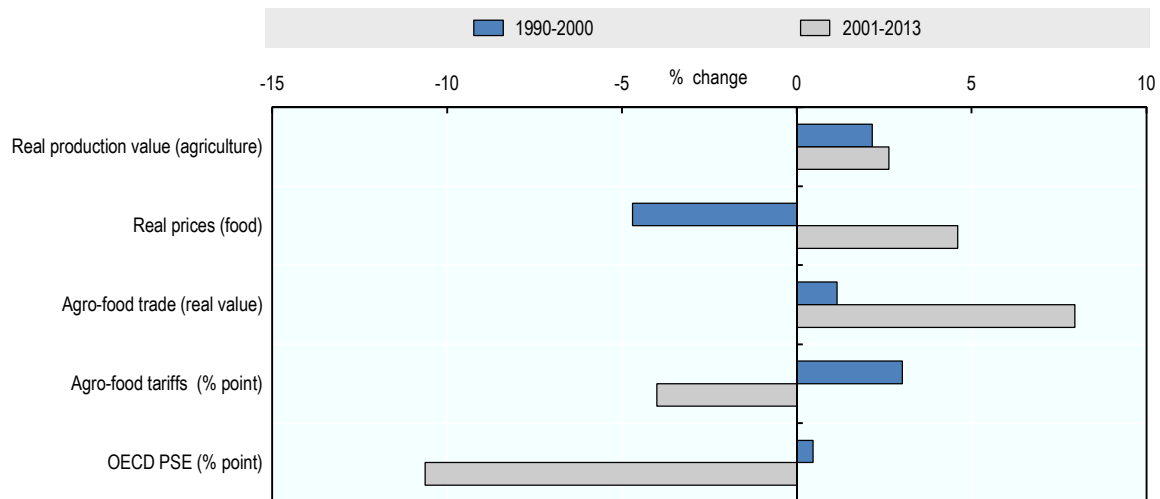
1.2 Important developments have taken place in markets and policies since 2000

Since 2000, global agricultural production has continued to increase and there have been shifts in the relative importance of regional production centres. There has been a rise in production in a number of developing regions, particular those of Asia and South America. Developed agricultural producing regions, on the other hand, have seen more modest to neutral growth, particularly when expressed in per capita terms.

Trade in agro-food products since 2000 has increased at a faster pace than in the previous decade (Figure 1.1). For agro-food products overall, trade has become less concentrated, with the share held by the top 20 importers and exporters declining by around five percentage points between 2000 and 2013. In terms of trading patterns, the rise of new production centres has increased trade between developing countries (so-called 'south-south' trade).

There has also been a significant shift in prices. The long term trend of declining prices came to an end in the early-2000s and was followed by a number of price spikes, most notably in 2007-08. These movements were driven by a confluence of mutually re-enforcing longer term structural changes in demand and supply, short term market shocks and, importantly, policy responses. Prices since then have generally remained at higher levels but are expected to decline gradually in real terms over the medium term on the back of sustained global productivity improvements. Further, while the price spikes during the 2000s also caused a surge in price volatility on world markets, post-2010, prices have been more stable and for most products have continued with what has been a long term decline in volatility. There are of course exceptions to this, with world maize prices exhibiting the opposite trend.

On the policy front, agricultural support policies in many countries have changed. Domestic support policies are more decoupled from production and begin to target environmental outputs; in some cases, support levels have also been reduced. However, in other countries support has risen. Overall, there has been a convergence in both the level and the nature of support between emerging and developed countries. Further, in many countries, policy interventions rely on production distorting support related to output and input prices rather than more decoupled payments or investments in the agricultural enabling environment.

Figure 1.1. Major changes in agro-food markets over the past two decades

Sources: OECD estimates based on FAOSTAT (<http://faostat3.fao.org/home/E>)| OECD Stat (<http://stats.oecd.org/>); and WITS data (<http://wits.worldbank.org/>).

Agro-food tariffs have fallen globally, but on balance they still remain high. For many countries, tariffs form an important part of their agricultural policy settings; there are also pockets of very high tariffs. On the other side of the ledger, export subsidies have become less prevalent although new forms of interventions in export markets, such as export restrictions, have been more widely used.

1.3 Current policies continue to significantly distort markets

An assessment of the impacts of current policy settings as present around 2011-14 in this new policy and market environment shows that agricultural support and barriers to agricultural trade still create significant distortions to world markets (Figures 1.2 and 1.3). Further, there remains much to be gained from pursuing reform. Four scenarios were explored in this study: *Without current policies*, which represents the removal of all trade-related and domestic support to agriculture; *Widespread partial policy reform*, which represents the partial removal of trade-related and domestic support across all countries worldwide; *Uneven partial trade and domestic policy reform*, which sees partial removal of trade-related and domestic support in developed countries with very limited changes in others; and *Policy drift*, which sees some large emerging agricultural producers increase tariffs and domestic support while other countries maintain their current policies.

The current suite of agricultural policies significantly negatively affects global agro-food trade. Overall, trade in all agro-food commodities would be higher in the absence of current support measures. Policies particularly limit trade in intermediate agricultural products. In line with generally higher applied tariffs on more processed products, trade in final food products is also significantly affected. These two effects suggest that the development of global value chains in the agro-food sector have been hampered by current policy arrangements.

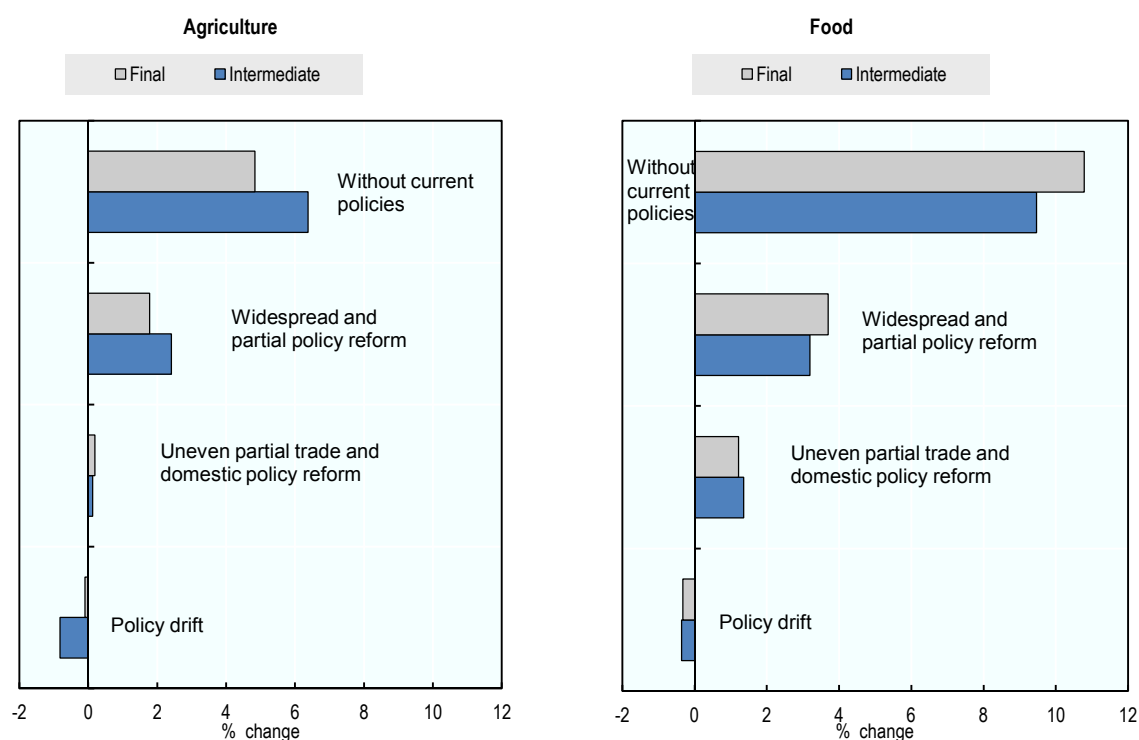
Policies also affect total global production and its location. A significant finding of this study is that while many trade and domestic support policies are aimed at increasing food production, from a global perspective they do not achieve this result. If current policies were not in place, the level of global production in agricultural products would be virtually unchanged. That is, support provided to agriculture in some countries does not increase production overall but rather displaces production from elsewhere in the world. Further, when broadening the lens to also include the production of food products, current policies are likely to be having a negative overall effect (driven by similar impacts to

those seen for agriculture). These conclusions are important for international debates on agricultural policy reform as some arguments in favour of trade and domestic support policies are premised around the illusion that such interventions can promote *global* food availability and thus contribute to *global* food security.

What policies do is to alter both the relative mix of products grown and the location of production activities. Policies promote some staple products such as rice and wheat at the expense of other production activities. Notably, the production of, and trade in, meat and dairy products are hindered by current policy settings. These products are also those for which future demand is projected to grow the strongest. If trends in rising demand for these products continue (from continued income growth), the costs of protection are also likely to escalate over time.

For agricultural products, current policies are likely to depress international prices, but the effects, on balance, are relatively small. Further, for some products (such as wheat and oilseeds), prices may actually fall if the current suite of policies were removed.

Figure 1.2. Impacts on agro-food trade of policies, reforms and drifts



Note: Four scenarios were explored in this study: *Without current policies*, which represents the removal of all trade-related and domestic support to agriculture; *Widespread partial policy reform*, which represents the partial removal of trade-related and domestic support across all countries worldwide; *Uneven partial trade and domestic policy reform*, which sees partial removal of trade-related and domestic support in developed countries with very limited changes in others; and *Policy drift*, which sees some large emerging agricultural producers increase tariffs and domestic support while other countries maintain their current policies.

Source: Author estimates from METRO.

Current policies are likely to negatively affect global welfare. Proxied through private consumption, the negative effect on welfare of current policies is now more uniform and is seen across most countries and regions studied – a result that differs to findings by other studies in the past. Both the policy changes and the changes in markets that have occurred since 2000 help explain these results. In particular, developed regions have reduced and changed the nature of their support; the European Union no longer makes use of export subsidies (with the recent agreement reached at the WTO permanently eliminating these globally); and developing countries trade much more with other developing countries.

These changes have reduced some effects observed in the past where, due to reform, some countries lost benefits from lower food prices or faced costs from the loss of preferences (preference erosion). At the same time, the changes have increased the exposure of developing countries to policies in place in other developing countries.

This study also highlights that for households in a number of countries the benefits from reforms to agricultural policies are critically linked to additional government action. This especially applies for parts of the population that receive a high proportion of their income from agricultural activities. In some regions, the sharing of tax revenue or expenditure reductions gains for government from reform is necessary to ensure gains to households are realised, such as in India and the People’s Republic of China. In others, households gain but governments suffer from falling revenues – such as in the Middle East and North African and Sub-Saharan African regions. Navigating these changes is important for policy makers and will also shape the political economy of reform.

1.4 Continued efforts for reform are needed

There is still much to be gained in concluding multilateral trade negotiations and reaching an agreement on partial reform of agricultural markets (Figures 1.2 and 1.3). Overall, modest reform scenarios – both unevenly applied focusing more on developed countries and those which are more widespread applying to all countries – are likely to offer modest total gains globally and to the countries involved. For all countries, the benefits from reform are created from a mix of their own actions and those in trading partners. Countries with high internal protections benefit from removing the restriction placed on their own markets, and if involved in trade, from the restrictions imposed by others. Given this, changes in world agro-food trading patterns have influenced the source of gains for some countries. For developing countries, in particular, the benefits on offer from reforms are now more critically linked to their own actions and the actions of other developing countries rather than actions by developed countries. Indeed, the effects for developing countries from their own liberalisation and actions from other developing countries have a greater impact than the effects of developed countries’ reforms. Critically, the results suggest that trade in intermediate products between developing countries is most hampered by current policies and thereby the development of GVCs in these countries could be significantly hampered in the absence of reform.

Simulations of possible policy drifts, based on trends that have already been observed, show that inaction can lead to losses. Indeed, for some sectors there is potentially more value in being able to lock-in the current set of policies than in reaching agreement on small decreases to protection. This is not to say that reforming agricultural protection arrangements should not be pursued, but rather, instead of further delays in trying to negotiate modest levels of reform, reaching a binding agreement first that ‘locks in’ current trade policies and levels of support is of value. The agreement reached at the November 2015 WTO Ministerial takes some steps in this direction but more are needed.

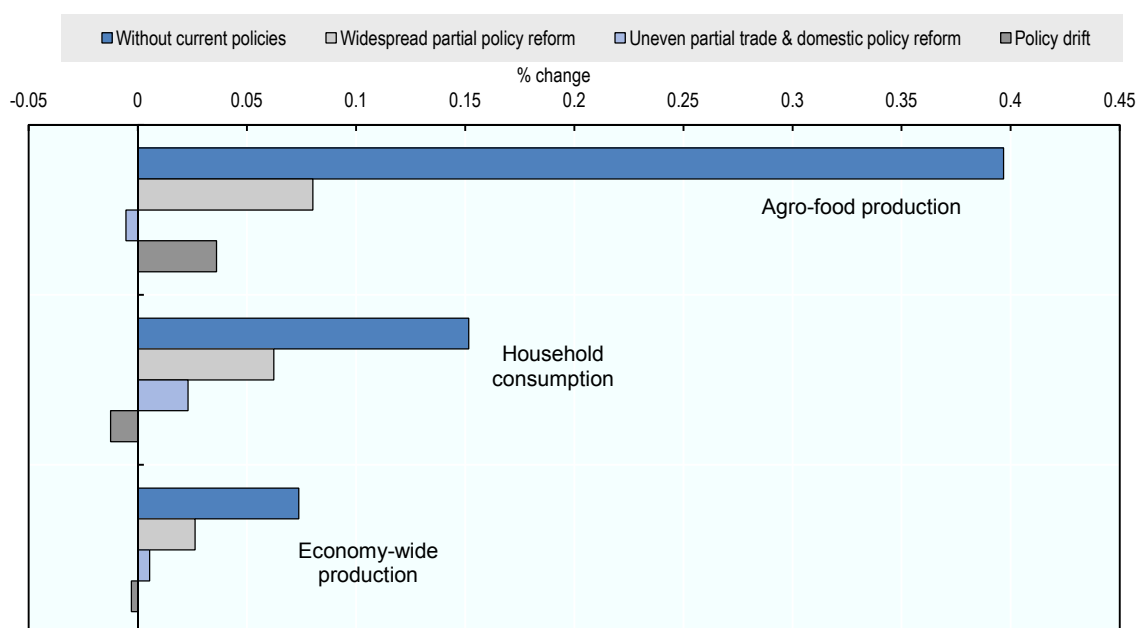
Findings on the impacts of current support policies in this study have a number of implications for further multilateral agreement on agricultural trade and domestic support policy reform.

- First, they suggest that there is still much to be gained for all regions from pursuing further multilateral reforms.
- Second, current policies particularly affect industries for which demand and trade is projected to grow strongly into the future, suggesting that the costs of the status quo are likely to increase over time.
- Third, from a global production perspective, policies are not promoting production, and indeed, looking at agricultural and food production together, could be reducing it.
- Fourth, for particular regions, the results suggest that calls for increased isolation or constraints on integration in regional or global markets are likely to be counterproductive. Increased interdependency means such an approach imposes costs on both the domestic markets of countries applying such measures and on their trading partners, including developing countries.

- Fifth, the world price effects of current policy measures are relatively small, suggesting that there is strong potential for beneficial trade reform to have fairly limited effects on some of the world's poorer populations. That said, prices in the absence of current policies would, in general, still be expected to rise and thus the food security of these groups should remain a policy priority globally. The analysis suggests that protection through tariffs and quotas is not the answer to problems of food insecurity: policies that promote productivity and flexibility in production systems; enable market engagement by producers (particularly small producers); and provide safety nets for vulnerable households provide better alternatives.

The results of the policy drift scenarios also highlight that those most negatively affected by increases in protection are the countries which impose such protective increases. For some countries, the results indicate that increases in protection in line with current practice also decreases total agricultural production. The actions taken have been in the name of increasing self-sufficiency as a vehicle to deliver greater food security. However, as seen in the results, total agricultural production falls in time and so does income. These income effects along with the effects on domestic prices from interventions in agricultural markets will work against the food security of households, in particular those in rural areas who will have fewer income generating options and face higher food prices.

Figure 1.3. Impacts on the world economy of policies, reforms and drifts

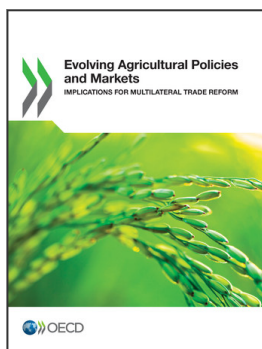


Source: Author estimates from METRO.

The impact of non-tariff and behind the border barriers has not been explored. These barriers range from quarantine and product safety requirements, to other requirements such as labelling. Some of those policies have also been increasingly the focus of regional and bilateral trading agreements. Exploring these barriers and possible reforms in the context of both multilateral and regional or bilateral agreements represents an area of future research. Similarly, the rural development, animal welfare and environmental performance of current policies have also not been examined.

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From:
Evolving Agricultural Policies and Markets
Implications for Multilateral Trade Reform

Access the complete publication at:
<https://doi.org/10.1787/9789264264991-en>

Please cite this chapter as:

OECD (2016), "Current agricultural policies: An overview of their impact and possible reforms", in *Evolving Agricultural Policies and Markets: Implications for Multilateral Trade Reform*, OECD Publishing, Paris.

DOI: <https://doi.org/10.1787/9789264264991-3-en>

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