



## Unfair Trade: Culprits and Victims

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Cogent justifications for continuing subsidies to U.S. crop farmers are difficult to find. Most analyses suggest that our farm programs lead to greater concentration, higher land prices and cash rents, increased production of supported commodities, and lower market prices. And as we have pointed out in recent *Iowa Ag Review* articles, current subsidy programs provide a quite inefficient safety net: overcompensating producers in low price–high production years and undercompensating them in high price–low production years. In addition, farm subsidies go predominantly to farm families that have higher wealth and income levels than the average U.S. family. And finally, there would be no major changes in aggregate food production or food prices in the United States if subsidies were ended tomorrow.

Most supporters of farm subsidies no longer attempt to justify them by appealing to any broad public purpose. Rather, many now argue that it would be unfair to eliminate them. It would be unfair to those farmers who are counting on continued high land prices and cash rents for their retirement. It would be unfair to farmers who paid high prices for land in the expectation that subsidies would continue to prop them up. It would be unfair to regions where production would decline dramatically if the subsidies were withdrawn. And finally, it would be unfair to U.S. farmers to have their subsidies taken away when farmers in other countries continue to enjoy production subsidies and protec-



tion from international competition through high import tariffs.

An “unfair” playing field in international competition is now the most common justification given for U.S. subsidies. A recent international example of an unfair trading practice is Argentina’s decision to tax wheat exports but not flour exports. Not surprisingly, flour exports increased significantly. Millers in Chile suddenly found themselves at a competitive disadvantage because of this discriminatory export tax. To level the playing field, the Chilean government placed a countervailing duty on Argentina’s flour exports. U.S. producer groups are quick to point out unfair trading practices. For example, the American Sugar Alliance argues that sugar import quotas are justifiable because otherwise U.S. consumers would be able to pay artificially low prices for their sugar. North Dakota wheat growers argue that they need subsidies to partially offset the damage they suffer from unfair Canadian wheat exports. And almost all agricultural groups argue that it would be foolish to “uni-

laterally disarm” until other countries agree to cut their subsidies. Given that the European Union has been the most egregious provider of domestic subsidies, this last argument really amounts to: “let’s not cut ours until the E.U. cuts theirs.”

### Who Faces Unfair Competition?

A recent study by my FAPRI colleagues at CARD and the University of Missouri helps provide insight into when the argument of unfair competition holds water. (See the article by John Beghin in this issue for details.) The study estimated what would happen to U.S. and world agriculture (grain and oilseeds, livestock, sugar, and cotton) if the recent U.S. WTO proposal were fully implemented. The United States proposed significant cuts in both domestic subsidies and tariffs for most products. Commodity prices under the U.S. proposal would be higher than the status quo because the decrease in production from protected farmers is greater than the production increase from competitive farmers.

Regarding the fortunes of U.S. farmers under the proposal, we can measure the extent of damage from unfair competition by looking at the effects of the U.S. proposal on production and net exports (exports minus imports). Farmers who would respond to liberalization with increases in production and net exports are the farmers who are currently most damaged by foreign protectionism. Those farmers who would experience declines in production and net exports are the ones who are not justified in arguing for compensation because of unfair competition. This second set of farmers could be considered as providing unfair competition to foreign

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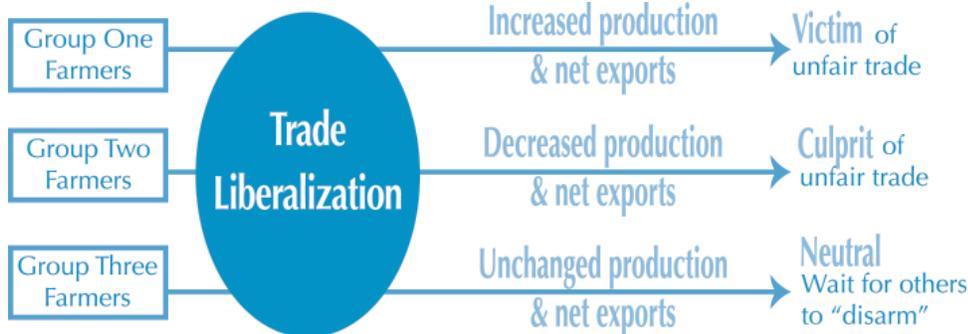
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producers. A third set of farmers are those producers who would produce just about the same amount under liberalization as they produce now. For this group the impetus to produce more from liberalization is about equal to existing production incentives of farm programs. This last group may be justified in arguing for giving up their subsidies when others give up theirs.

The results of the FAPRI study indicate that U.S. livestock producers belong to the first group of producers. U.S. beef and pork exports would increase by about 25 percent under the U.S. proposal, while broiler exports would increase by about 8 percent. Cattle and hog prices would increase by between 4 and 5 percent while broiler prices would increase by approximately 2 percent. The livestock results indicate that E.U. production subsidies and high tariffs on meat imports around the world currently harm U.S. livestock producers. California rice producers also belong to this first group because they would find expanded demand for their product in Japan and South Korea.

Milk producers and most grain and oilseed producers belong to the third set of producers who would find that their production levels and net exports would largely be unchanged under the U.S. proposal. For dairy, currently high E.U. support prices create surplus dairy products that have to be exported with subsidies. Elimination of these surplus exports would significantly raise world prices. This price increase would

just about compensate U.S. dairy producers for cuts in the U.S. dairy program. For grains and oilseeds increased liberalization under the U.S. proposal has a small impact on demand. Thus U.S. dairy, grain, and oilseed producers could legitimately argue that they would be willing to give up their subsidies if the E.U. and other countries gave up theirs.

Cotton and sugar producers belong to the second group of producers because under the U.S. WTO proposal, production and net exports would decline. One can conclude from this study that for cotton and sugar, U.S. farm programs create an unfair playing field for the rest of the world. For sugar, the situation is complicated because the net effect of trade barriers and subsidies around the world is a depression in world prices, which would seem to provide an argument in favor of continued U.S. support. However, it is clear that a move to lower production subsidies and trade barriers would result in a sharp increase in U.S. sugar imports and significantly lower prices for U.S. sugar buyers.

### Not All Our Competitors Are Subsidized

Enough examples of unfair trading practices and production subsidies exist around the world to give some credence to the common portrayal of U.S. farmers under siege from unfair competition. High Japanese import tariffs, large E.U. export subsidies, and seemingly endless E.U. production subsidies certainly exist and depress demand for U.S.

products. However, there are many examples of competing countries that provide very little support for their agricultural sectors, and some competitors are actually placed at a competitive disadvantage by their governments' policies.

New Zealand and Chile are perhaps the two best examples of countries that have found agricultural success without subsidies. Their consumers have easy access to imported food products so their producers must compete with foreign producers for sales in their domestic markets, and export-oriented producers must export at world prices. New Zealand farmers export dairy products, lamb, fruit, wine, and produce grains and vegetables for their domestic market. Chile is best known for exporting fruit and wine, but Chile is looking at export markets for pork, beef, and dairy products also.

Brazil and Australia are two agricultural powerhouses that have thrived with minimal production subsidies. According to the Organization for Economic Cooperation and Development, government support accounts for 3 percent of farm receipts in Brazil and for 4 percent in Australia. But farm groups often complain about the unfair competition from these two countries. For example, the American Sugar Alliance—the lobbying organization for the U.S. sugar industry—has complained about the \$82 million in sugar subsidies Australia provided in 2002. But this amounts to less than 0.7¢ per pound of Australian sugar. Complaints about Brazil range from infrastructure investments, to currency devaluations, to subsidized credit. But infrastructure investments are a proper function of government, and Brazilian monetary policy is not determined by how it helps or hurts the agricultural sector. Credit subsidies for purchasing machinery provide much less production stimulus than do U.S. loan rates.

Argentina provides a near-perfect example of a major agricultural com-

petitor that actually reduces the competitiveness of its farmers through both official and unofficial policy interventions. Besides the damage caused by Argentina's macroeconomic policies, official Argentine agricultural policy levies a 20 percent tax on beef, dairy, soybean, and grain exports. The purpose of the tax is to raise revenue for the government and to help hold down food prices for Argentine consumers. The impact on agriculture is lower investment, productivity, production, exports, and farmer income. Unofficial policy in Argentina can be equally damaging. Argentina is tied for 97th place on Transparency International's global Corruption Perceptions Index (see [http://www.transparency.org/policy\\_and\\_research/surveys\\_indices/cpi/2005](http://www.transparency.org/policy_and_research/surveys_indices/cpi/2005)). This low ranking compares to 17th place for the United States, 21st place for Chile, and 62nd place for Brazil. One example of Argentine corruption involves the recent campaign to hold down inflation by pressuring companies to reduce prices. Some food companies were told that their expansion plans were not going to be permitted unless they agreed to reduce their prices. In contrast to the positive attitude in Chile and Brazil about agriculture's future, Argentine farmers and food companies have a fatalistic view of the future. Despite enormous potential for productivity gains in Argentine agriculture, the attitude of the people who would have to do the hard work and investments to achieve the gains is that the government will never allow them to reap the profits from such endeavors.

### Two Paths

U.S. agriculture faces two possible future paths. One follows the direction laid out by the recent U.S. WTO proposal. This path would involve less direct government management of prices and production through guaranteed prices, a gradual rationalization of U.S. agriculture that would emphasize production of

those products that U.S. farmers are relatively good at producing, and a gradual lowering of barriers to trade around the world. This path would require gradual investment adjustment by processors, acreage adjustment by farmers, and, depending on the willingness of Congress to support land prices, some financial adjustment by farmers in some regions.

An alternative path is gaining momentum among some U.S. farm groups. This path would increase government control over the direction of U.S. agriculture. Export markets would not be seen as growth opportunities. Trade agreements would be de-emphasized or ignored. Imports would be restricted. Prices would be set by a combination of paid land diversions, loan rates, and biofuels subsidies. At a recent Iowa Corn Growers Association crop fair, one corn grower, seemingly an advocate of this second path, stated that expanded U.S. exports only damage the farmers in the importing countries, and imports only damage U.S. producers; so why, he wondered, should we ever allow trade in food?

Given the current lack of support for trade liberalization in Congress, and in key E.U. countries such as France, it is not clear that a new WTO agreement will be achieved. If not, U.S. farm programs will continue to be vulnerable to WTO cases under the current agreement. Advocates of the second path for U.S. agriculture could then find themselves in a stronger position, arguing that the U.S. Congress should write farm policy, not the WTO. The large difference in direction represented by these two paths means that all of us with an interest in the future of U.S. agriculture should closely follow what happens in the next six months of WTO negotiations. ♦