

## **Moving on from Cancun: Agricultural Trade and the Poor**

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I'm delighted to be here this evening. My only regret is that I wasn't able to join you for the intensive discussions you have had during the day. The timing of this workshop is significant, as all of you know. It comes as the multilateral trade framework established after the Second World War is facing one of its greatest challenges. Failure to resolve the problems left in the wake of the Cancun meeting would have serious repercussions for the world economy. And I think we can all agree that progress on agricultural trade issues is central to progress in the Doha round as a whole.

I'd like to start by sharing with you one of my favorite—and most telling—illustrations of the folly of agricultural support. Somebody has taken the trouble to do some calculations putting the cost of farm support in the OECD countries into context. It turns out that those countries spend enough to send every one of the 56 million cows in the OECD's dairy herd on a first class round the world ticket—complete with \$1450 spending money—**every year**. Given the damage that such subsidies do to the world trading system in general, and to the poor in particular, luxury holidays for cows might be worth investigating.

More seriously, the subsidy we're talking about—\$2.7 per cow per day—is more than twice the average daily income of a small and marginal farmer in the third world. Such subsidies, as I'm sure you have discussed today, are economic nonsense.

Tonight I hope, as far as possible, to avoid going over the ground you have already covered. I want to try to place the discussions here in a broader context: to explain why I think there is an urgent need to move forward from Cancun; to say why we at the Fund think progress on agriculture is important both in terms of the political process and in terms of delivering economic prosperity; and to outline the contribution which we in the IMF are seeking to make to the resolution of the current standoff.

### **Cancun**

Cancun was clearly a serious setback. I attended the opening day on behalf of the Fund, and announced a new initiative by the IMF, about which I will say more in a moment. The abrupt end to the talks came as something of a surprise—not just to me, of course. The mood at the start of the meeting was optimistic. A number of private meetings I had with individual delegates suggested a common desire to work constructively for a solution. One key figure told me that there was a "disposition for dialogue".

What went wrong will keep the historians happy for some time, but it is not our main focus here. It is clear, though, that agriculture was a major sticking point. Put simply, the developing countries are determined that they gain access to developed country markets. The industrial countries seem determined both to resist this and to resist the idea that developing countries should have dispensation to maintain much tighter restrictions on trade. Both sides, it seems to me, are dodging the main issues, both at the political and at the economic level.

At the global level, the failure of Cancun is worrying because it puts the Doha round itself at risk. Few now seem to think that the original timetable—which envisaged completion of the round by January 2005—remains feasible. Timetable slippages are hardly a new phenomenon in multilateral trade negotiations, of course. But the gulf separating the two main camps is wide and there is, as yet, little sign of a willingness to compromise.

Prolonged delay, or even worse, a complete breakdown of the Doha round, would pose serious risks for the global economy. The future prosperity of both developed and developing countries depends on the continued expansion of trade—as it has during the whole of the postwar period. Without it we run the risk of beggar-thy-neighbor policies that did so much damage in the 1930s.

Remember, the recovery now under way is still tentative. The outlook is somewhat brighter than even a few months ago, mainly because there are now fewer downside risks to the central expectation of steadily accelerating growth. But one of those downside risks is clearly a decision to abandon multilateral trade talks.

The breakdown of talks at Cancun also, in my view, poses a risk to the multilateral trading system itself. If we do not successfully revive the multilateral negotiating process, one result could be a proliferation of regional trade agreements, with their own preferential arrangements. This would be a dangerous retrograde step. We have already seen the United States, for example, step up the drive to conclude bilateral free trade deals. I do not need here to emphasize how undesirable this is: partly because it undermines the multilateral framework and partly because it does so in a way which, ultimately, penalizes developing countries.

But Cancun was also an intellectual setback. If it is too soon to say that the proponents of free trade lost the argument, it is clear that they failed to win it. Some of this results from the failure of key countries to put their money where their mouth is.

### **Costs of protectionism**

Yet protectionism, as we know, is costly both for taxpayers and consumers; and it is disproportionately costly for the poor. Even in rich countries, agricultural support penalizes the poor, because it is the poorest in society who spend the largest proportion of their incomes on food. Protection, by way of subsidies, and barriers to trade, hurts poor

consumers and producers most. It is also important to remember that agriculture subsidies and price supports invariably benefit rich farmers far more than poor ones.

Even for those of us who accept this argument it sometimes comes as a shock to realize quite how expensive protectionism is for the taxpayer. Cows aren't specially favored. It has been estimated, for instance, that every one of the 2,300 jobs saved in the American sugar industry through barriers to imports in the 1990s cost \$800,000 dollars a year. It is just possible that retraining those workers would have been a little cheaper!

And these calculations take no account of the fact that a job saved in one sector by this means, could easily result in several jobs lost downstream—let alone overseas, for manufacturers or food producers denied export opportunities.

The same sort of results would come from calculating the impact of European Union or Japanese trade barriers.

But protectionism particularly hurts the developing country poor, very largely because of the focus on agricultural protection. Food accounts for about 10% of household expenditure in industrial countries, but more than 30% in most developing countries. About three-quarters of the world's poor live in rural areas, heavily dependent on agriculture.

### **Benefits of trade liberalization**

Contrast this with the clear benefits of trade liberalization. Yet developing countries themselves are as reluctant as industrial countries to liberalize. They are right to demand access to industrial country markets, of course. But the row over this distracts attention away from the contribution that developing countries could make to their own economic welfare by liberalizing. After all, nearly 40% of developing country exports now go to other developing countries.

And developing country trade barriers are often even higher than those in industrial countries. Reducing the 25% tariff on cocoa in Korea and Turkey, for instance, would benefit African producers who currently face lower tariffs on their exports to the US and the EU.

I know you've had intensive discussions about the figures involved today. But I cannot forebear to mention the scale of the benefits to be had from developing country trade liberalization. Work done in the Fund, for example, shows the potential gains from removal of agricultural trade distortions would be heavily skewed to developing countries. Using the GTAP model, the removal of distortions worldwide in 1997 would have shown developing country gains of \$122.2 billion in export earnings: over 80% of those gains would have come from the removal of such distortions in developing countries themselves.

Again using the GTAP model, the World Bank estimates developing countries could see their 2005 GDP rise by around 0.5% from agricultural trade liberalization alone in the wake of a Doha deal, and by 1.3% if we include manufactured goods as well.

If we try to include dynamic gains arising from productivity improvements, the figures rise substantially. By 2015, the World Bank reckons that the gains from global trade reforms which brought agricultural tariffs down to 5% in the industrial countries and 10% in developing countries, would be significant. Low and middle income countries could see real incomes (in 1997 dollars) rise by \$80 billion in terms of the static effects and by \$167 billion in terms of the dynamic effects. These are much higher than the gains for the industrial countries.

In all the different calculations, the sums involved far outweigh what these countries get in the form of development aid and debt relief.

### **Moving forward**

As we try to find a way forward, I think it is clear the battle has to be fought on two fronts. The case for movement by the industrial countries is incontrovertible. The benefits to be had from the reduction of trade-distorting subsidies and barriers are enormous. Look at just two examples.

I mentioned the cost to American taxpayers of sugar protection. The United States is hardly alone: sugar is one of the most policy-distorted of all commodities. OECD support for domestic sugar producers is roughly equal to the total value of developing country sugar exports. Moving to free trade in sugar would raise prices by close to 40%, increase the sugar trade by 20% and generate around \$4.7 billion in welfare gains for the poor in developing countries.

American subsidies for domestic cotton growers, as you know, turned out to be one of the most contentious issues at Cancun. Hardly surprising, when we look at the numbers. At \$3.7 billion annually, those subsidies are three times as large as US aid to Africa, and are nearly a fifth of the total value of world cotton production. The EU also subsidizes cotton, as do several developing countries. In total, the IMF estimates that these subsidies have depressed the world price by about 12 cents per pound—meaning the price is at least 20% lower than it would otherwise be. In West Africa, this has led to income losses for poor farmers of around \$250 million a year. In Benin, where cotton accounts for 40% of exports and 7% of GDP a 1% rise in the price of cotton raises per capita income by half a percentage point and reduces poverty by 1.5 percentage points.

These are politically sensitive issues in the industrial countries. And they come at a difficult time in the political cycle. In my view there will have to be some progress within the Doha round if we are to be able to convince developing countries that they too should start to dismantle trade barriers.

### **Agricultural trade liberalization in developing countries**

But we should not wait to make the intellectual case to developing countries for unilateral liberalization. I think there are three broad areas where the world's poorer countries should be acting to free up agricultural trade and where currently, many farmers in these countries suffer from the impact of their governments' own policies.

The first issue is the exchange rate. In addition to coping with a distorted global market for their products, farmers have often struggled with the effects of fixed exchange rates at home, in the context of domestic inflation.

Second is the high price of inputs that too many developing country farmers face. Import substitution policies to protect manufacturing, for instance, push up the prices of materials that farmers need to buy to produce their crops. This creates a bias against productivity improvements.

Third is protectionism at home: all too often, this penalizes the poorest consumers at the expense of larger producers.

And fourth is the way tax revenues are often spent in poor countries. Government spending is often highly-skewed in favor of urban populations—at the expense of the poorest rural farmers.

### **The IMF's role**

What can we in the Fund do to help this process? We have, of course, been supportive of the WTO's efforts in the Doha round—as, indeed, we have been in all previous trade rounds.

But the Fund's interest in free trade is often overlooked. In fact the promotion of trade is one of our "core purposes" as defined in the Articles of Agreement, signed almost sixty years ago. The Fund's overarching objective is global financial stability—the essential pre-condition for trade growth and growing economic prosperity.

And we have some leverage with some of our 184 members. Each year, as you know, we conduct what we call Article IV consultations with each of our member countries. The surveillance process is an opportunity to draw attention to economic policies about which we have doubts. In practice, though, such doubts can only carry much sway when a country is involved in, or negotiating for, a Fund program of financial assistance. At such times, we can apply greater pressure for governments to avoid, for example, market distorting policies.

Let me give you just one example, which also touches on the broader problem of market-distorting protectionism in developing countries. Not that long ago, Fund staff successfully persuaded a government to postpone indefinitely plans to increase tariffs on poultry products. Such tariffs would have brought tangible benefits for the one large domestic poultry producer at the expense of the poorest consumers. Similar distortions have been resisted in other Fund program countries.

## **The IMF and Doha**

More recently, the Fund has become directly involved in supporting the Doha round negotiations. We have done so, I should add, with the full support and encouragement of the WTO.

Our involvement stemmed from the concern that many poor countries have consistently expressed about the implications for them of a Doha settlement. They are particularly concerned about the possible costs involved in coping with the short-term consequences of the Round and the loss of preferences in particular. They worry that these costs would be high, and painful to live with; or that they would be beyond their capacity to meet.

Based on what we know of previous liberalizations, and from preliminary research undertaken at the Fund, we do not expect the temporary costs of adapting to a Doha settlement to be significant for the vast majority of countries. Indeed, we expect gains for most, even in the short-term. The lowering or elimination of tariff and non-tariff barriers as a result of Doha will take place over several years which itself mitigates many of the potentially negative impacts. And these changes to the trading environment will be planned: so any policy response to mitigate the impact can also be planned.

But it became clear that such assurances were not likely to be enough. The WTO and we were concerned that ignoring the fears that remain could undermine the prospects for a successful round.

Hence my announcement in Cancun. In essence, the IMF is prepared to undertake a new trade initiative to make financial assistance available to developing countries that face a challenging adjustment to the impact of any Doha round deal. We would commit to provide financial support in the context of new Fund-supported programs, or existing programs, to those members that face a net negative impact on the balance of payments in the near term from the effects of the Round. And we are prepared to offer additional financial help in those circumstances where the actual impact turns out to be greater than anticipated.

The initiative is complementary to the program of technical assistance and policy advice on trade policy issues that I have described. It is specifically tailored to address temporary external imbalances that might result from the multilateral trade reforms we all believe are ultimately desirable.

As I said, we don't believe these costs are likely to be large, even for the small number of countries affected. But we are prepared to help meet them where they materialize and so provide what is in effect contingent insurance. The aim was to reassure those countries that are participating in the multilateral trade round that they will have access to additional financial help in addressing any near-term transitional costs that might, in some cases, accompany a Doha agreement.

Of course, the fundamental point is that such liberalization will have substantial payoffs over time, and one of the challenges is to get this point across. Chile's experience is an interesting example of the payoffs that liberalizing trade, and greater private sector involvement, can bring: in the decade from 1975, Chile's fruit sector increased its share of merchandise exports from 4.9% to 11.7%, helping to reduce the economy's dependence on mining exports. The fruit sector's share of exports has declined a little since, to 8.4% in 2000: but mining's share has continued to fall.

### **Where next?**

I think I used the word "battle" a little earlier. I think it is a battle—and one we have to wage on several fronts simultaneously.

In the short term, I think it is essential that the Doha negotiations restart as soon as possible—either on the basis of the WTO Secretariat's draft or on the chairman's text presented at Cancun. We cannot sit by and watch the Doha process disintegrate.

Here, too, the IMF, in co-operation with the World Bank, has found itself with a new role. At our annual meetings in Dubai, our main Ministerial policy-making body, the IMFC, agreed that the Managing Director of the Fund and the President of the World Bank would send a joint letter to all WTO heads of government and their trade ministers, urging them to restart the talks as soon as possible. This letter will go out shortly.

At the same time, a campaign of persuasion is needed, in both industrial and developing countries. Rich country governments need to overcome their sensitivity to agricultural lobbyists and other powerfully entrenched interests. This will not be easy, but economists could contribute by helping to make more explicit the balance between those who benefit and those who bear the costs of such protection.

A similar effort is needed in developing countries: and here, it seems to me, the work at this two day workshop can be of critical importance. Identifying gaps in research—and then filling them, of course—is a vital part of the struggle to win hearts and minds. Vested interests will always find it easier to argue against generalized statements rather than detailed analysis. Economic policies in developing countries must be genuinely pro-poor. For me, that means delivering macroeconomic stability above all. One important ingredient of that is an end to market-distorting policies.

Yes, the industrial countries have to play their part in this process. But developing country governments cannot be allowed to hide behind rich-country obstinacy and avoid confronting difficult issues on their own doorstep. All the evidence over many years shows that the benefits of trade liberalization are real, substantial and are significant even when carried out unilaterally. Governments in poor countries that pander to their own rich constituents are harming their poor far more than any industrial country tariff regime can.

Thank you very much.