4. Developed countries experiences

4.1 Comparative study on regulation of agriculture in the United States, Canada and the European Union

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Summary

What has been done? In the 1990s, the governments of these three countries set out to limit budget spending without affecting the incomes of farmers: a task easier said than done.

With the reform of the CAP in 1992, the European Union (EU) adopted a system of direct income aids, like those used by the United States (US). The two major powers came to an agreement on this basis, and imposed it on the world by including it in the “blue box” category, set up under the Marrakech Agreement. Initially, the EU measure involved compensatory aid to farmers, as a way to convince them to accept the price difference that might exist between the European domestic market and the global market. The aids were designed to be temporary. It was expected that European producers would gradually manage to offset the price difference by exporting larger volumes. But hopes for global market expansion proved overly optimistic. Markets for agricultural raw materials, and especially cereals, have barely increased since the early 1980s.

How has it been implemented? After a period of heavy market intervention, governments were seeking solutions that made producers more accountable. Public storage systems and the export subsidies used in some sectors in the United States and the European Union were phased out. So-called shared responsibility mechanisms and crop insurance schemes were set up. The problem was that these schemes could only operate at a high cost to their governments. Recently, however, governments have encouraged the processing of bio-fuels through heavy subsidies. The US has also sharply increased consumer subsidies on food for the poor.

What were the effects? The three countries studied have, over time, changed the instruments used to regulate their agricultural sectors, either as a response to internal pressure (often budgetary), or the international context (increased market competition and multilateral agreements on agriculture). In both the EU and the US, this first led to a decrease in the level of price support, replaced by an increase in the level of direct payments, with the objective of maintaining a guaranteed income to farmers. Gradually, direct payments have evolved and have been decoupled from production, to meet the constraints set by the Agreement on Agriculture of the Uruguay Round. This change is just about complete in the European Union, with the introduction of single payment

entitlements. It is still only partial in the United States, which has maintained countercyclical payments. In Canada, the picture is somewhat different. Price support policies, which target a few products (milk, poultry and eggs), continue intact to this day. Income support policies for other sectors of agricultural production, however, have also evolved towards decoupled payments.

What recommendations could be derived? At first glance, these regulatory instruments appear to have reduced economic distortions. But this statement must be qualified. If we look at the changes to levels of total support to agriculture in the three countries, it becomes clear that while all three have respected the commitments they made at the WTO on domestic support, they have not decreased overall support throughout the period.

In fact, for all three countries, total support granted to agriculture exceeds the level of commitments. Canada, the EU and the US have managed to respect their commitments, thanks to the "box game": to agree on priorities for reducing domestic support, types of aid were categorized in three boxes. The orange box was for aid that cause the most distortion and should be reduced first; the blue box included support measures considered less harmful and therefore still tolerable for a short period of time; the green box was for support deemed to cause little market distortion. The result has been a rise in green box aids everywhere.

The total support to agriculture remains as high as it was in 1995 in the European Union and even higher in Canada and the United States, before the sharp increase in agricultural commodity prices in 2007 and 2008. These results reflect a reality: the governments concerned consider the agricultural sector still needs support.

4.2 Corn markets in the United States

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Summary

What has been done? World corn production has exceeded that of wheat and rice. Production could reach 811 million tons in 2010-2011, which would be 2 million tonnes below the record high established in 2009-2010. This is exactly double 1980 production levels. Despite these perspectives, prices are soaring on the world market and exceeded $7.40 a bushel in early March 2011, compared to $3.70 a bushel in early March 2010, and $3.25 in early July 2010. Prices have doubled in a year.

Unlike other cereals, corn production is highly concentrated in a small number of countries. The United States and China account for more than 60% of global harvests. With more than 40% of the total, the US is by far the largest player in the market. It is an interesting case study. Corn, which has become the most abundant food on the planet, depends essentially on the world's largest economy. But curiously, American supremacy in corn production has not yielded impressive results in terms of entering new foreign markets or improving the performance of the agro-food industries that rely on them. It is therefore relevant to see how agricultural policy has evolved in this country and its consequences on the world market.

How has it been implemented? Since the mid-1980s, the government has tried to reduce subsidies, hoping to develop demand in foreign markets. This new policy was fully formalized in the 1996 Farm Bill, entitled the "FAIR Act" to indicate that the US was ready to embrace competitive practices. Results were disappointing. Just two years later, prices collapsed and emergency measures were needed to once again support farmers' income. Unlike the EU, which has decoupled direct aid, the bulk of aid to US farmers is countercyclical, which takes into account market prices.

What were the effects? This strategy, aimed at developing export markets, has not been successful. US corn exports have not increased for 30 years and the overall balance of food products from the United States is in decline due to a relative inability to expand exports of processed products, which now make up most of the market.

Figure 7 : Corn prices in the US and France

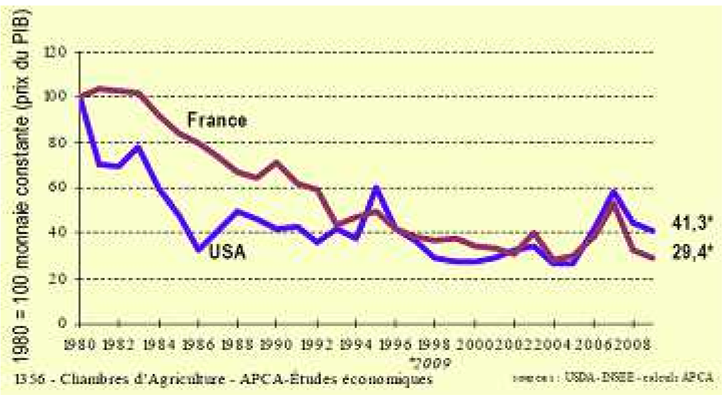

Figure 6 : Main corn exporters 2009

What recommendations could be derived? This new policy has another major drawback. It resulted in a long period of excessively low prices on the global market, which serves as a worldwide reference, despite representing just 10% of total production.

It took a sudden demand for corn from the domestic non-food market to turn things around. Starting in 2003, ethanol production began to absorb more than than 10% of annual corn production. In 2007, this table grew to 20%, and exceeded 40% in early 2011. This new demand now accounts for almost three times the tonnage of US corn exports. It is causing a decline in stocks that worries importing countries. This is what explains the prices spikes, even though harvest levels are record.

Due to a substitution effect, the increase has affected all types of grains. Furthermore, the absence of buffer stocks in both the US and the EU has encouraged speculation. Altogether, these factors have led to rising food prices in importing countries. What is ironic in this new scenario based on ethanol production is that market regulation is clearly easier when it relies on domestic demand rather than exports. Even when it comes to the world's largest economy.