Market Price Support in Large Developing Countries

By Raul Montemayor

In the run-up to the Bali Ministerial Meeting in December 2013, various proposals were presented to resolve the predicament of some developing countries that were at risk of violating WTO rules on domestic support because of their public stockholding programmes, which provide market price support to domestic producers. In Bali, WTO Ministers decided to temporarily shield such programmes from challenges until a “permanent” solution could be found. This paper summarizes the findings of a larger study conducted to provide policy-makers, negotiators and other stakeholders with an impartial, evidence-based analysis of policy options for such a “permanent solution” (Montemayor 2014).

Under the WTO Agreement on Agriculture (AoA), the distortive effect of market price support programmes can be quantified into a product-specific Aggregate Measurement of Support (AMS). This is equal to the difference between a fixed external reference price and an applied administered price multiplied by the quantity of the product that is eligible to receive the administered price. The resultant AMS figure must not exceed the de minimis for such product, which is a monetary value equivalent to a prescribed percentage of the value of annual production of the said product. In other words, the AMS as a percentage of the total annual production value must not exceed the prescribed de minimis percentage.

Figure 1: Formula for computing AMS as a percentage of production value

Because the external reference prices were based on import prices during a distant base period (usually 1986–88), the gap between these prices and the current administered or buying prices increased over time. When the variance was multiplied by the “eligible” production, some countries found themselves at risk of breaching their de minimis limits. Several proposals have been raised to address this problem. The following sections assess the effect of some of these proposals on the behaviour of AMS and the capacity of countries to comply with the AoA rules on domestic support.

The simulations cover five developing countries with existing public stockholding programmes that provide price support to producers. Only food staples, particularly wheat and rice, were included in...
the analysis. Relevant data on import prices, administered prices, production volumes and values, foreign exchange rates and other information was culled from the FAO Statistical Database and submissions of countries to the WTO.

Table 1 provides a profile of the countries (coded from A to D) and commodities covered by the study. Notably, the public stockholding programmes of Countries A, C and D for rice covered a relatively small proportion of total domestic production (ranging from one to five per cent). In turn, procurement of rice in Country B and wheat in Countries B, C and E ranged from one fifth to one third of local production.

### Table 1: Profile of the countries and commodities covered by the study

<table>
<thead>
<tr>
<th>Country/Product/Crop Year</th>
<th>% Procurement</th>
<th>Administered/Reference Price</th>
<th>Administered/Import Price</th>
<th>Administered/Producer Price</th>
</tr>
</thead>
<tbody>
<tr>
<td>Country A – Rice, 2011</td>
<td>5%</td>
<td>26.53</td>
<td>1.33</td>
<td>1.21</td>
</tr>
<tr>
<td>Country B – Rice, 2010–11</td>
<td>22%</td>
<td>4.58</td>
<td>0.32</td>
<td>0.55</td>
</tr>
<tr>
<td>Country C – Rice, 2008</td>
<td>1%</td>
<td>0.87</td>
<td>0.48</td>
<td>0.79</td>
</tr>
<tr>
<td>Country D – Rice, 2011</td>
<td>2%</td>
<td>5.87</td>
<td>1.14</td>
<td>1.15</td>
</tr>
<tr>
<td>Country B – Wheat, 2010–11</td>
<td>26%</td>
<td>3.11</td>
<td>0.84</td>
<td>0.92</td>
</tr>
<tr>
<td>Country C – Wheat, 2008</td>
<td>37%</td>
<td>0.88</td>
<td>0.45</td>
<td>0.90</td>
</tr>
<tr>
<td>Country E – Wheat, 2010–11</td>
<td>25%</td>
<td>7.55</td>
<td>0.59</td>
<td>0.79</td>
</tr>
</tbody>
</table>

Except in Country C, administered prices were significantly higher than the corresponding reference prices. Country A registered the highest ratio with a derived administered price of almost 26 times the reference price in 2011. In turn, administered prices were generally lower than the equivalent prices of imports, except for rice in Countries A and D. A similar result was found when administered prices were compared to producer prices.

### Figure 2: Base scenario results

![Graph showing AMS as a percentage of production value for different countries and crops, with de minimis indicated.]
The simulations confirm apprehensions that a literal and strict application of the AMS formula for market support price programmes could lead most of the developing countries covered by the study to breach their *de minimis* allowances for product-specific AMS. In this base scenario, no adjustments were made for reference and administered prices, and “eligible” production was set to total production on the assumption that price-support programmes were open-ended and available to all producers. As shown in Figure 2, only one country was able to comply consistently with the *de minimis* rule despite agreeing to a lower threshold (8.5% of total production value versus 10% for the others), mainly because its administered prices were significantly lower than its reference prices. The other countries ended up with *de minimis* percentages of 40% and above.

Adjusting reference prices alone had mixed results. The use of three-year rolling averages for import prices produced the most positive outcome, although one country remained in breach of its *de minimis* cap primarily because of the unusually large gap between its reference and administered prices for rice. Adjusting reference prices for inflation, whether by using producer price indices or converting prices and monetary values to US dollars, also had generally positive effects but this was not sufficient to allow two of the five countries to comply with the *de minimis* rule for their rice products.

Setting “eligible” production to actual procurement volume worked in favour of countries whose public stockholding programmes covered only a small proportion of local output. Three of the five countries that absorbed less than 5% of local production fared best in this scenario. In turn, the two other countries that purchased about one fourth of local wheat produce exceeded their AMS caps.

**Figure 3: 3-yr average import price plus actual procurement**
The only scenarios where all countries and commodities registered AMS within their *de minimis* was when the “eligible” production was equated to the actual procurement volume and reference prices were adjusted simultaneously, either by applying producer price indices, converting prices to US dollars, or using three-year or five-year rolling average prices of imports. Figure 3, for example, shows that, if reference prices were set to the average prices of imports in the preceding three years and the “eligible” production was pegged to the actual volume procured, all countries would be able to comply with the *de minimis* rule. In fact, only Country A ended up with a positive AMS equivalent to 2% of its annual value of rice production, which was nevertheless significantly below its 10% *de minimis* percentage cap.

In terms of crafting a “permanent solution”, an Appellate Body ruling in a dispute involving Korean beef opened the possibility for countries to officially set a limit to the scope of their price-support programmes. On this basis, they could legally declare their “eligible” production to be a certain portion or percentage of local production. By setting the “eligible” production to a suitably low level, the gap between the administered and reference prices could be effectively overcome so as to arrive at an AMS falling within the *de minimis*. In fact, the simulations show that this option, which would require any change in AoA rules, could even allow countries to increase their procurement over current levels and still comply with AMS rules. This option appears to be the most practical and feasible approach for countries that want to maintain their price-support programmes but do not plan to absorb large portions of domestic production.

If this option is not able to adequately address the concerns of some countries, the least contentious alternative would be to allow the use of US dollars in notifying prices and monetary values in AMS calculations and to equate “eligible” production only to the proportion of local output that is actually marketed by producers. These two adjustments would not be sufficient to resolve the problems of three countries, but they would at least bring one country’s support programme, which was in breach in the base scenario, in compliance with *de minimis* rules.

Another possible area of compromise would be to exempt developing countries from *de minimis* caps if their actual procurement does not exceed a given percentage of local production. This would address the concerns of countries whose procurement programmes are small and arguably contribute little to market distortions. However, since this option requires a change in AoA rules, the previous suggestion for countries to simply set a limit to their “eligible” production appears to be preferable as it would largely achieve the same result.

Rebasing reference prices to a more recent period, adjusting them for inflation through the use of producer price indices, or replacing them with three-year or five-year Olympic averages for historical import prices may be difficult to pursue since this runs counter to the “fixed” nature of reference prices. In turn, increasing *de minimis* levels has minimal effects and would conceivably provide only temporary relief from breaches.

Aside from adjusting the AMS formula, developing countries have the option to convert their buying programmes to green box measures by removing administered prices altogether. This will address fears that the price-support programmes of developing countries could lead to significant market distortions and even harm other developing countries if they involve large volumes that would eventually get dumped in export markets. Developing countries have the option to replace these
trade-distorting measures with practically unlimited amounts of input subsidies as long as these are extended to low-income or resource-poor farmers. Using budgetary outlays as proxies for the AMS through the "equivalent method of support" modality could be another option that could resolve the dilemma.

The study concludes that the public stockholding issue is solvable and that developing countries have many options, both within and outside the AMS formula, to continue providing support to their farmers. At the same time, the pursuit of a "permanent" solution to the public stockholding issue should be viewed in the light of calls from several developing countries to rectify existing imbalances in the domestic support allowances accorded to developed vis-à-vis most developing countries. Care should nevertheless be exercised so that such programmes do not end up unduly distorting markets and even harming other developing countries.
References