

## **Current subsidies in the agricultural sector of the global trade system\***

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**ABSTRACT.** This article focuses on the provisions of the WTO agreements regulating the use of subsidies in the agricultural sector by the member-states. It analyzes current practices of the WTO member-states' in subsidizing their agricultural production. It also outlines the main trends in improving the practices of subsidizing agricultural producers in the leading countries of the world. The article also describes the major coalitions within the WTO that actively participate in the development and improvement of international trade rules in agricultural produce. In the current context whereby Ukraine seeks WTO accession, the structure of domestic measures in support of agriculture pursuant to the requirements of this international organization is given special attention. The article also considers the prospects for further liberalization of international trade in agricultural produce.

**KEY WORDS.** WTO, subsidy, agricultural production support, total AMS, food aid, Cairns group, Ukraine, liberalization prospects.

In the world economy's current phase of development, and especially in light of the latest events concerning economic relations within the World Trade Organization (WTO), such measures of state policy as

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subsidization, in the realm of agriculture in particular, attract special attention.

This has been studied by a great number of foreign and Ukrainian scholars and experts, among them C.R. Milner<sup>1</sup>, Soren Kjeldsen-Kragh<sup>2</sup>, J. Bhagwati, A. Panagriya, D. Sharma<sup>3</sup>, A. Makhmudov, S. Mikhnevich<sup>4</sup>, R. Bingham<sup>5</sup>, and L.M. Kucher<sup>6</sup>

Kjeldsen-Kragh in his work *International Trade Policy* focuses on the negative consequences of agricultural subsidies, and demonstrates his argument with a case study of the Common Agricultural Policy (CAP). Sharma in his research shows that the practice of subsidizing the agricultural sector, when used by developed countries, impede the economic and, as a result, the social development of a great number of less developed countries whose well-being primarily depends on agricultural exports. Bhagwati, on the contrary, points out the negative impact of subsidized exports from developed countries on the economies of exporting countries which have abandoned subsidization, and further insists that such measures of state support also have positive effects. Therefore, he says, the complete cancellation of subsidies may bring negative results, too. In particular, he draws our attention to the fact that subsidized exports flow to the least developed countries at prices lower than non-subsidized exports, thereby enabling the recipient countries to save costs.

Aware of the potential benefits of international trade, various countries strive to maximize their positive effect by way of capturing the leading positions in the world markets. Unfortunately, this effort is not always accompanied by an observance of the free market rules nor of fair competition. Subsidization is one of those measures which, in most

<sup>1</sup> Milner C.R. (ed) *Export Promotion Strategies: Theory and Evidence from Developing Countries*, Brighton, 1990.

<sup>2</sup> *International Trade Policy*/ Soren Kjeldsen-Kragh. Copenhagen Business School Press, 2001.

<sup>3</sup> Devinder Sharma Bhagwati, *Globalization and Hunger // Dissident Voice* — <http://www.globalpolicy.org/socecon/trade/subsidies/2005/0329bhagwati.htm>

<sup>4</sup> Mikhnevich S. *Liberalization of international agricultural trade and the problem of food safety // IE&IR ( МЭИМО) №1, 2003*

<sup>5</sup> Bingham R. *Financing of economic development: Trans. from Eng. L.: Litopys, 2003. — p.416.*

<sup>6</sup> Kucher L.M. *Specifics of regulation of agricultural trade within the WTO /Economics of AIC (Agro-Industrial Complex), 2005, №5.p.144-151*

cases, exert a negative influence on the development of mutually beneficial trade relations by distorting the competitive environment and the free market rules.

First and foremost, we should define what a subsidy is. Quite a broad range of definitions of this term are found in professional publications. A dictionary of economics identifies an export subsidy as a grant to a producer or trader of exported goods which compensate for part of the production or sales costs with a view of raising the goods' competitiveness in foreign markets<sup>7</sup>. In accordance with another definition, an export subsidy is a financial allowance granted by a government or private institutions to exporting companies when they ship certain goods abroad<sup>8</sup>. According to the definition given by O. Shnytko, «a subsidy is a money payment aimed at supporting national producers and indirectly discriminating against imports<sup>9</sup>». This same author identifies an export subsidy as «a specific financial battering-ram which is meant to breach the gate of the fortress of protected foreign markets, since receiving an export subsidy enables national exporters to sell goods to foreign buyers at a price lower than in domestic markets which, in turn, dramatically boosts export» (9, p.105). The following definition of an export subsidy should also be pointed out: an export subsidy is a financial deposit or something similar which leads to the lowering of prices for exported goods to foreign buyers<sup>10</sup>. Throughout this paper we shall apply the definition of a subsidy specified in the agreements of the WTO which will be considered further on.

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<sup>7</sup> <http://www.economics.com.ua/lexicon/detail.php?id=1100>

<sup>8</sup> [http://www.glossary.ru/cgi-bin/gl\\_sch2.cgi?R1dRyoszr](http://www.glossary.ru/cgi-bin/gl_sch2.cgi?R1dRyoszr)

<sup>9</sup> Shnytko O.C. National competitive power: essence, problems, mechanisms of realization. — K.: «Naukova Dumka», 2003. p.334

<sup>10</sup> Tsygankova T.M., Petrashko L.P., Kalchenko T.V. International trade: Educational guide. — K.: KNUE, 2001. — p.488.

### Provisions of the WTO Agreements that regulate subsidies

With regards to the contemporary international trade system, the definition of subsidies is formulated in the Agreement on Subsidies and Countervailing Measures (SCM Agreement), which clarifies Article XVI of GATT. In accordance with Article I of the SCM Agreement, a subsidy is a financial contribution by a government or other public body within the territory of a WTO member, where: government practice involves a direct transfer of funds (e.g. grants, loans or equity infusion) or potential direct transfers of funds or liabilities (e.g. loan guarantees); government revenue that is otherwise due is foregone or not collected (e.g. fiscal incentives such as tax credits);

the government provides goods or services other than general infrastructure, or purchases goods;

the government effects payments to a funding mechanism, or entrusts or directs a private body to carry out one or more functions illustrated above, which would normally be vested in the government, and the practice, in no real sense, differs from practices normally followed by governments; and a benefit is thereby conferred<sup>11</sup>.

Since this article is primarily concerned with the use of subsidies in agriculture, we should first pay attention to the provisions of the WTO Agreement that regulate these issues. In many countries of the world, agriculture is a «sensitive» sector of the economy which requires protection and adverse means of support and assistance. Therefore, issues related to its subsidization are governed by specific provisions of the Agreement on Agriculture. Three main categories of subsidies are considered in this Agreement: «green» (do not distort trade, actionable); «blue» (do not distort trade, actionable); «amber»

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<sup>11</sup> Global trade system: development of institutions, rules, instruments of the WTO: Monograph/corporate authors and scientific editing Tsygankova T.M. — K.: KNUE, 2003. — p.660

(have negative impact on trade, subject to reduction) (8, p. 205).

The possibility of applying «green box» measures by the WTO members is provided for in Article 6 «Obligations as to Domestic Support» and Annex 2 «Domestic Support: Prerequisites for Exemption from Obligations as to Reduction of Support». According to the Agreement these measures are exempt from mandatory reduction and «shall not exert distorting impact on trade or production or this impact must be brought to minimum»<sup>12</sup>. Subsidies included in the «green box» have to meet two main criteria: support shall be provided through state programs, which are financed by government (including the government's rejection of revenues), and not by consumers; such approach shall not involve price support to producers.

«Green» subsidies are granted through state programs for: the provision of services, part of which are general services; the creation of state reserves to ensure food safety; domestic food aid; direct payments to producers; decoupled income support; government financial support of income insurance and income safety-net programs; payments (effected directly or through the state's financial participation in agricultural yields insurance programs) for compensation of damages from natural calamities; assistance in structural reforms of programs pertaining to the withdrawal of producers from agricultural production; financing structural reforms through investments; payments within environmental protection programs; payments in accord with regional development programs<sup>13</sup>.

Apart from the above, so-called «*de minimis*» measures are also related to the «green box». These are measures that have minimum affect on the production and trade of agricultural goods and are, in fact, domestic subsidies not related to particular goods if they do not exceed 5 % of agricultural production cost, 10 % for developing countries. These measures are not subject to reduction.

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<sup>12</sup> World trade system: Practical guide/ Trans. from Eng. — K.: K.I.C., 2002. — xxiv, p.348

<sup>13</sup> Global trade system: development of institutions, rules, instruments of the WTO: Monograph/team of authors and scientific editing by Tsyhankova, T.M. — K.: KNUE, 2003. — p.660

Another category of subsidies which distorts agricultural international trade are the «blue box» measures whose application, however, is allowed for WTO members. The Agreement on Agriculture states that direct payments in accordance with «programs for limited production» of agricultural produce may be attributed to «blue box» subsidies, if these payments are attributed to fixed areas and yields, and are effected at 85 % or less of the baseline production level, and payments for livestock are calculated based on a precisely defined amount of livestock heads.

The «blue box» measures should be part of the program and limit production by way of specifying the maximum production volumes or oblige farmers to leave part of their land uncultivated.

All other measures that do not comply with the definition of the two categories mentioned above are attributed by the Agreement to the «amber box» and are subject to reduction.

Therefore, these subsidies include the following types of grants: for cattle-breeding and plant cultivation, pedigree cattle-breeding, non-elite seed-breeding, compound feedstuff, etc.; compensations for part of the cost of mineral fertilizer and means of chemical protection of plants, for energy and costs of improvement of land fertility, and also compensations for the cost of machinery which had been acquired by way of a barter deal for agricultural produce; for costs of leasing, costs of repair and routine maintenance of melioration systems, creation of seasonal stocks of spare parts and material and technical resources; and for capital investment in production, except for costs of melioration and water farms;

price support: compensation for the difference between purchase and market prices for agricultural produce; providing producers with goods (services) at prices below market prices; purchasing goods (services) from producers at prices higher than those in the market; preferential crediting of agricultural producers by different level budgets organizations, including writing off and debt exten-

sion; allowances for transportation of agricultural produce<sup>14</sup>.

As provided for in the Agreement on Agriculture governments may extend certain kinds of support to national economies, although the volume of this support must be limited to certain values. Such values are measured by the Aggregate Measurement of Support (AMS) index, which «is calculated per specified product as the difference between the fixed world reference price and that of the applied regulated price, multiplied then by the production volume. To obtain the value of the AMS, all external subsidies unrelated to specified goods are added to the total sum of subsidies, calculated on an individual basis for each product»<sup>15</sup>.

Subsidies attributed to measures of «green and amber boxes» and «de minimis» subsidies are not included in AMS. Furthermore, developing countries may exclude the following from AMS: «investment subsidies which are mostly granted to agriculture; subsidies for agricultural raw materials which are normally granted to producers with a low income and a poor raw material base; subsidies that promote diversification from the cultivation of narcotic plants»<sup>16</sup>.

Since export subsidies are considered the most destructive for international trade, their reduction is one of the main prerequisites for the effective development of trade between countries. As specified in the Agricultural Agreement the following categories of export subsidies are subject to be cut by WTO members:

governmental direct subsidies which depend on export indexes; the sale by governments of non-commercial agricultural produce stocks (which remain in state ownership) at prices lower than similar goods being sold to domestic buyers;

payments for exporting specified agricultural products which are financed by government irrespec-

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<sup>14</sup> Results of the Uruguay round of multilateral trade negotiations: Texts of official documents.K.: «Dimension», Secretariat of interagency commission for Ukraine's WTO accession, 1998. p.520.

<sup>15</sup> The same.

<sup>16</sup> Results of the Uruguay round of multilateral trade negotiations: Texts of official documents.K.: «Dimension», Secretariat of interagency commission for Ukraine's WTO accession, 1998. p. 520.

tive of whether «state funds» have been used, including expenditures that are financed from taxes on similar agricultural goods or from which export articles are made;

granting of subsidies to compensate for costs of agricultural sales and export (with the exception of broadly available services for export promotion, and consultative services), including expenditures on loading and unloading goods, quality improvement and other expenditures for processing, and also expenditures for international transportation and freight;

expenditures on domestic transportation and freight of export supplies, which are granted or established by governments on conditions that are more favourable than conditions for domestic deliveries; subsidies for agricultural products which depend on whether or not they are enlisted with the export production program<sup>17</sup>.

#### **Measures of the WTO member-states in support of agriculture**

The contemporary agricultural world trade is distorted by protectionist measures to a great extent. Almost all industrially developed countries have certain «closed» sectors which they are trying hard to protect. For instance, in Canada it is the production of dairy products, poultry industry and egg production, in Japan – rice cultivation, in the U.S. – sugar and nuts, in Europe – almost all products from plant cultivation and animal breeding.

In 2000, the WTO members initiated a new round of negotiations on the issues of agriculture. The main issues listed on the agenda of these negotiations included, among others, those related to access to markets, export subsidies and domestic support.

Quite a number of countries use subsidies, yet emphasize the fact that their trade partners tend to grant greater support to their own farms. According to the OECD, the volume of support granted to pro-

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<sup>17</sup> The same, p. 159



ducers in the OECD zone in 2004 amounted to US\$ 279 billion or EUR 226 billion<sup>18</sup>. Including support for general services which are extended to agriculture, such as research activities, infrastructure, inspection, marketing and promotion – the total volume of support of agriculture by OECD countries in 2004 constituted 1.2 % of GDP of those countries.

The average index of support granted to agricultural producers in OECD countries in 2002 – 2004 amounted to 30 % of total inflows in agriculture. In some countries this index reached the following numbers: in Australia and New Zealand – 5 %, in Canada, Mexico, U.S. – 20 %, in Turkey – 25 %, European Union – 34 %, Japan and Korea – 60 %, Iceland, Norway and Switzerland – about 70 %. As stated in the latest report of the OECD, since 1986 – 1988, the level of support for agricultural producers has decreased in most countries, with the exception of Norway where this level stayed intact, and Turkey where the level has risen. The greatest decrease for support of producers has taken place in Canada. Total volume of support granted to the agricultural industry of OECD countries compared to 1986 – 1988 has decreased from 2.3 % of GDP in 2002 to 1.2 % in 2004.

The smallest decrease in support levels was reported in EU countries. Subsidized exports from the EU countries lowers the world prices for agricultural products, thus creating hardships for farmers from the U.S., Canada, Australia, New Zealand, countries of Eastern and Central Europe, and Eastern Asia. Based on research from 2000, it was concluded that had those practices been relinquished, dairy exports from the above-mentioned countries would have been 91 % higher; meat exports would have increased by 67 %. Protectionist measures of Europeans have created a situation where dairy production in Australia and New Zealand has dropped by 50 %, and the number of livestock heads in Eastern Europe – by 22 %<sup>19</sup>. At the current stage of development of the world economy

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<sup>18</sup> Agricultural Policies in OECD Countries: Monitoring and Evaluation 2005 — ISBN-92-64-009558 OECD 2005 — <http://www.oecd.org/dataoecd/49/21/191050.pdf>

<sup>19</sup> Whetstone L., ed. Reforming the CAP. 2000. [http://www.iea.org.uk/record.jsp?type= publication&ID=118](http://www.iea.org.uk/record.jsp?type=publication&ID=118)

the countries of the EU are at the same time members of the WTO, and within the framework of this organization they are allowed the largest support to their farmers – approximately 3.5 times more than in the U.S.<sup>20</sup>. Governed by the reform of the Common Agricultural Policy the majority of the EU countries in 2003 agreed to administer a unified payment system. All the EU countries except for Malta and Slovenia already apply the unified payment system per square unit (SAPS) for all agricultural lands using a specific fixed tariff which averages 48 EUR per hectare of land<sup>21</sup>.

Subsidies that wealthy countries grant to their farmers very often appear to be the major part of their income, thus creating a distorted competitive situation in the world market, and force farmers in these countries into agricultural overproduction. In the U.S., for instance, direct governmental subsidies to farmers form up to 23 % of their income, in the EU countries this number amounts to 40 %, and in Japan – 63 %<sup>22</sup>.

In the U.S., subsidies to agricultural producers play quite a notable role in the development of this sector of the economy. The main function here is fulfilled by the Department for Agriculture which implements the subsidization of agricultural production and exports using three main streams: the granting of direct financial support to farmers and exporters; state crediting and export guarantees; and food aid<sup>23</sup>.

The main programs for subsidizing agriculture in the U.S. are as follows: programs for insurance of yields and farmers income; export development; promoting the export of milk and other dairy products; access to markets; food aid to developing countries;

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<sup>20</sup> The agreement is reached on some progress at negotiations at WTO// <http://usinfo.state.gov/russian/Archive/2005/Dec/19-724608.htm>

<sup>21</sup> Agricultural Policies in OECD Countries: Monitoring and Evaluation 2005 — ISBN-92-64-009558 OECD 2005 — <http://www.oecd.org/dataoecd/49/21/191050.pdf>

<sup>22</sup> Abaturov V. Developing countries in «free trade»//Economic Research Center <http://www.review.uz/archive/article.asp?y=2005&m=51&id=108>

<sup>23</sup> <http://www.prompolit.ru/146870> Alexander Kuryayev. Crisis of GATT system/WTO

«Food Program for Peace»; «Food Program for Progress»; a program for «emerging markets»<sup>24</sup>.

The access to markets programs have become most effective over the last years and hold a significant place in governmental expenditures. They also create real opportunities for American farmers to penetrate foreign markets, mainly by means of informational and analytical promotion.

The most disputed item on the above list are the programs for food aid. Disputes arising from the issue of their use have become a characteristic feature of our world. Opponents of these subsidies emphasize that these programs stipulate either direct subsidizing of farmers or free food aid to the developing countries by means of purchasing goods meant for those countries from domestic producers, at prices higher than those in the market which, in fact, is subsidization. Thus, the American government stimulates the production of farm produce on its territory, exporting the surplus products to other countries.

One of the possible consequences of cancelling agrarian subsidies by developed countries is their full-fledged activities in the markets of foreign countries in terms of purchasing lands and the most productive farms in developing countries. Therefore, the governments of those countries are facing the necessity of developing aid programs to farmers who could be forced out from their lands (retraining programs, for instance).

In general, the cancellation of agricultural subsidies may also lead to increased pressure on the environment, concentration of lands in the hands of a small number of owners, an explosion in the migration of small farmers to cities, thus activating the process of urbanization in the world.

The main weak point in such a policy of the American government, as stated by its opponents, is the actual injustice in the distribution of financial aid. Therefore, disregarding the statements of the state administration, which emphasizes that this

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<sup>24</sup> WTO member's expertise in protection of national interests in domestic and world markets (magazine version of monographic research)// World economy and international relations, 2002, №8, p.36 — 37

policy is mostly aimed at maintaining a proper level of national security and supporting small farms, the lion's share of subsidies, in practice, flow to large farms (17 % of all farms), which provide for 80 % of the total agricultural production in the U.S. Farms with US\$ 500,000.00 annual sales volume constitute only 4 % of agricultural enterprises, produce 50 % of farm produce and are the actual beneficiaries of the American model of agricultural support. In 2000, 57,500 farms received subsidies in the amount of more than US\$ 100,000.00 each, and 154 farms – more than US\$ 1 million. Over 1996–2000, the Tyler Farms company received US\$ 23.8 million, for which it had create 66 legal entities<sup>25</sup>«.

Let us take a closer look at the programs for agricultural subsidization in the U.S. (Table 1)<sup>26</sup>.

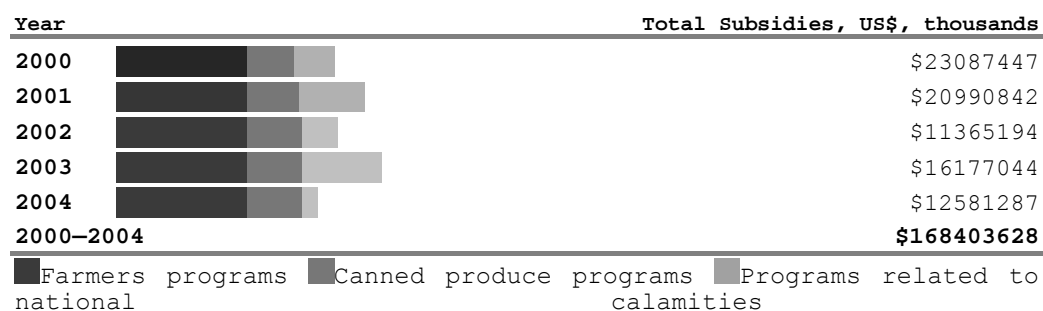
**Table 1. Farm Service Agency Programs\*  
for payments to producers, as per program and item,  
in 2000–2004, in US\$ thousands**

Program & item	2000	2001	2002	2003	2004
Agricultural managerial assistance	–	1376	2984	2864	1185
Quality loss	–	52 478	96 956	81	76
Seeds of oil cultures	–	422 392	209	1	1
WAMLAP III	–	16 442	343	5	0
Marketing aid, peanut		53911	14	–	0
Tobacco		128259	71	–	0
AMLAP		95079	–	–	0
Losses of citrus cultures in California		2154	–	–	0
Wool and mohair	7424	2838	–	–	0

<sup>25</sup> <http://www.prompolit.ru/146870> Alexander Kuryayev. Crisis of GATT system/WTO

<sup>26</sup> Based on information of the United States Department of agriculture official web-site — <http://www.usda.gov>.

Program & item	2000	2001	2002	2003	2004
Canned produce	60 627	31 183	38 869	32 067	24 015
Improvement in environmental quality	95 516	97 079	58458	331	324
Animal breeding by Indians	5334	885	—	—	0
Potato	—	11327	—	—	0
Countercyclical programs	—	—	570 512	9 002 616	6 502 679
Profit loss, dairy products	—	—	336 903	877 229	204 108
Countervailing payments, animal breeding	—	—	836 063	272 521	468
Access to markets	—	—	98 727	98 906	128 568
Sugar cane	—	—	—	521 721	0
Winter wheat	—	—	—	3535	6317
Cattle feedstuff	—	—	—	6	0
Countervailing payments, bird flu	—	—	31 420	22 014	0
Other programs	22 918 546	20 075 439	9 293 665	5 343 147	5 713 546
Total cost of all programs	23 087 447	20 990 842	11 365 194	16 177 044	12 581 287

Figure 1<sup>27</sup>:

<sup>27</sup> Based on information of the Environmental Working Group official web-site — <http://www.ewg.org/farm/region.php?fips=00000>

As is evident from Figure 1, farm subsidy programs were the largest throughout 2000 to 2004 were farm subsidy programs aimed at producing certain agricultural products, among which the largest recipients of state funds were producers of corn, wool, soybeans and grain cultures which are traditionally considered the dominant farm produce in the U.S.

Elimination of different kinds of protectionist measures in agriculture, including subsidies, will promote the development of the majority of less developed countries since the huge markets of the developed countries will be opened to them for their exports. Nonetheless, one should not forget about the other possible side of the elimination of agricultural subsidies – the probability of price increases for farm produce which in its turn may negatively influence the developing countries that import foodstuff. According to some experts' forecast over the period of the next ten years prices for foodstuffs may rise by 5 %. On the other hand, the price increase may stimulate investments to this industry since potential investors will have a chance to obtain larger profits. As an example of the apparent change in the world trade structure resulting from the essential liberalization one can cite countries joining free trade zones. For example, after accession of Spain and Portugal to the EU in 1986 and Mexico's accession to the North Atlantic Free Trade Agreement (NAFTA) the dairy exports of these countries increased considerably.

#### **Coalitions of WTO members at negotiations on Agricultural Subsidies**

At the present stage of its development, the WTO has 150 members, countries and tax territories, the majority of which are developing and least developed nations. Thus, it is quite obvious that in order to adequately present the interests of one's own state at this world forum the countries tend to unite in certain coalitions. Such informal groupings help countries stand up for their mutual interests which otherwise are very difficult to promoted on one's own. Different groups of countries exist – those

concerned with a limited range of issues (trading in goods, services), and also those interested in most of the issues that are brought to discussion.

The main informal although most active group which is concerned with the questions of agricultural support and consists of WTO members is the so called Cairns Group. It was created in 1986 at the Ministerial Meeting in Cairns, Australia and unites 18 agricultural exporting countries among which are: Australia, Argentina, Bolivia, Brazil, Canada, Chile, Colombia, Costa Rica, Guatemala, Indonesia, Malaysia, New Zealand, Paraguay, the Philippines, South Africa, Thailand, and Uruguay<sup>28</sup>. The group calls for radical and total liberalization of international agricultural trade by means of cuts on import tariffs, the elimination of export subsidies, the cancellation of tariff quotas and limits to the domestic support of national producers in the agricultural sphere. One of the most active members in this group is Australia. This country has decreased its own practice of subsidizing agricultural production and now demands this same step from other countries in order to create equal rights and opportunities for agricultural producers in the whole world, and thus establish a free market environment. This grouping involves both developed and developing countries from five different continents. The aggregate share of these countries in the world agricultural export is 24.5 %<sup>29</sup>.

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<sup>28</sup> Based on information from «Export Opportunities of Russia» search system-  
[http://www.exportsupport.ru/law.tv?n\\$docid=194334](http://www.exportsupport.ru/law.tv?n$docid=194334)

<sup>29</sup> The Cairns Group official web-site — <http://www.cairnsgroup.org>

**Table 2: Cairns Group and leading national economies, share in the world agricultural exports, 2004<sup>30</sup>**

Country (group of countries)	Share of agriculture in GDP (%), 2004	Share of agriculture in total exports (%), 2004	Share in the world agricultural exports (%), 2004
Cairns Group	6.0	18.9	24.5
EU	2.0	6.5	10.0
Japan	1.0	1.0	0.7
U.S.	1.2	9.7	10.2
Global total	4.0	8.6	100

One other group which is calling for the further liberalization of agricultural trade is the Group of 22 (G-22) – consisting of 22 developing countries among which the most prominent are Brazil and India. Other members of the group are such countries as China, Egypt, Pakistan, Argentina, Mexico, Venezuela, Chile, Uruguay, Cuba, Paraguay, Bolivia, Thailand, Indonesia, the Philippines, Tanzania, South Africa, Zimbabwe, and Nigeria. The coalition was formed during the Ministerial Conference in Cancun in 2003<sup>31</sup>. This group supports the cancellation of agricultural subsidies but demands special treatment of developing countries and the least developed countries. They have worked out a special formula for reducing state agricultural support. According to this formula, countries where total support exceeds the amount of US\$ 60 billion have to cut it by 80 %, countries with total support of US\$ 10 to 60 billion – by 75 %, and those with less than US\$ 10 billion – by 70 %<sup>32</sup>. Also, the G-22 members proposed a differentiated approach to the reduction of AMS with regard to «amber box» measures. Their demands could be illustrated in the following table:

<sup>30</sup> Based on the Cairns Group official web-site — <http://www.cairnsgroup.org>

<sup>31</sup> <http://wto-consulting.ru/index.php?fuseaction=forum&mid=56&page=1>

<sup>32</sup> G20 Proposals on Agriculture (Market Access, Domestic Support) Martin Kohr. Third World Network // <http://www.globalpolicy.org/soecon/bwi-wto/wto/2005/1310domestic.htm>



**Table 3. Proposed reduction of AMS**

AMS sum, US \$, billion	Reduction, %
More than 25	80 %
15–25	70 %
0–15	60 %

Other informal groupings in the framework of the WTO should also be mentioned here – although they are not engaged solely in the decision making process with relation to agriculture, but rather play a notable role in multilateral negotiations particularly on the issues concerning the agrarian sector. The most outstanding among them are:

«Five Interested Parties» (FIPs): U.S., EU, India, Brazil and Australia;

«Quad» : traditional group of the four most developed countries such as: U.S., EU, Canada, Japan;

«New Quad»: U.S., EU, India and Brazil;

«Group 10» (G-10): Japan, Switzerland, Korea, Bulgaria, Israel, Iceland, Norway, Taipei, Mauritius, Lichtenstein. At the initiative of this group some «non-trade aspects» were included on the agenda of negotiations on agriculture, including protection of the environment, landscapes, and traditional living conditions in rural areas<sup>33</sup>.

The activities of these groups are different but, since their influence on the general functioning of WTO is quite substantial, it would be reasonable to observe their activities and to consider their possible reaction to the initiatives of different countries and groupings.

### **Perspectives on the liberalization of agricultural trade within the WTO**

As a result of the regular rounds of multilateral trade negotiations within the framework of the WTO which were held in 2005 in Hong Kong, the members of

<sup>33</sup> Based on information from [http://wto-consulting.ru/index.php?fuseaction= forum&mid=56&page=1](http://wto-consulting.ru/index.php?fuseaction=forum&mid=56&page=1)

this international organization signed a declaration which demands the elimination of export subsidies for agricultural goods by 2013. Originally the developing countries insisted on 2010 but the EU, accounting for about 90 % of such financing, agreed to sign the declaration if the year was changed to 2013<sup>34</sup>. The declaration also provides for food aid. For instance, the relevant chapter states that any rules established during negotiations in the WTO must not impede the receipt of foodstuffs by people who are starving or in dire straights, but must eliminate commercial displacement by way of a free transfer of surplus of goods<sup>35</sup>. Representatives of the EU demand the restriction of such aid to its monetary value, whereas the U.S., which actively uses different food programs to sell the surplus of their farm produce and maintain high prices for this produce in the domestic market, expressly object to the EU's initiative.

### **Ukrainian agricultural support measures**

Firstly, agriculture plays quite a significant role in Ukraine's economy. This could be explained both by a number of factors related to the historical development of the country and the availability of such a substantial resource potential. A peculiar feature of the Ukrainian agrarian sector is the considerable amount of people engaged in it – approximately 20 %, whereas this index in developed countries constitutes about 3-4 %<sup>36</sup>. Such a difference in value, unfortunately, does not favour Ukraine and may characterise the industry with low productivity and excessive human resources.

The history of the development of agricultural support measures applied by Ukraine goes back to 1990, although most relevant measures have been used

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<sup>34</sup> The agreement reached some progress at WTO negotiations // <http://usinfo.state.gov/russian/Archive/2005/Dec/19-724608.htm>

<sup>35</sup> *ibid.*

<sup>36</sup> Okhlopkov, A. Unprofitableness of Agriculture — A Deliberate Business Strategy of the Industrial Lobby/ *Mirror of the Week* — electronic version of the article -<http://www.zn.kiev.ua/n/show/446/38745>

by the government since 1998. The agrarian sector in Ukraine has since become a major recipient of state subsidies. Statistics show a reduction in subsidies in percentage of GDP; on the other hand the amount of subsidies in absolute values has been increasing (see Figure 2)<sup>37</sup>.

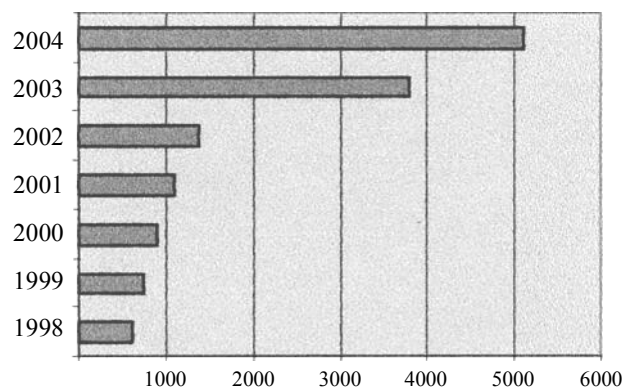


Fig 2. Subsidies to agriculture in Ukraine, 1998-2004, UAH, million

One interesting peculiarity of government subsidy measures is that a considerable part of those payments never reach the target recipients. According to the State Committee for Statistics, almost 36 % of annually declared subsidies were never granted over the period of 2001-2003.

The state support of agriculture in Ukraine includes budget financing of programs and measures aimed at the development of the industry, privileged taxation, partial compensation for interest rates for credits in commercial banks, and writing off bad debts to budget and social funds. Budget funds are needed for maintaining the restoration of agriculture on the one hand, and for deterring the inflation processes and protecting the interests of agricultural consumers on the other.

The following support measures for farmers are practiced in Ukraine: development programs for plant

<sup>37</sup> Report: Agricultural subsidies: Analysis of the existing legislation in Ukraine as per compliance with the WTO agreements. B. Spinhua, K. Shkurupiy, O. Ustenko/Ukrainian — European consultative center on legislative issues

cultivation; cattle and animal breeding; fishery development; gardening support; social sector and agrarian science development; village infrastructure; and machinery producers' support<sup>38</sup>.

The development programs for plant cultivation has the largest share – almost 16 % of the total volume. Expenditures in the amount of about UAH 50 million are budgeted for the development of animal and plant breeding. Some of these programs are quite stable and average up to 25 – 30 % of the total support volume<sup>39</sup>.

In general the volumes and measures of the Ukrainian agriculture can be illustrated in the following table:

**Table 4. Distribution of funds  
from the Ministry of Agrarian Policy, pursuant  
to the State Budget of Ukraine in accordance with WTO  
rules<sup>40</sup>**

	2004		2005		2006	
	%	UAH, mil- lion	%	UAH, mil- lion	%	
Budget of the Ministry of Agrarian Policy	2952.1		5175.1		5817.0	
Budget of the Ministry of Agrarian Policy – Compensation to Pension Fund	2952.1	100.0	3967.7	100.0	4221.1	100.0
Amber box:	1070.4	36.3	1563.8	39.4	1474.5	34.9
Reduction of Commercial banks credit costs	141.5	4.8	350.0	8.8	500.0	11.6
Financial support of farms	5.1	0.2	27.3	0.7	28.0	0.7
Financial support of animal and plant breeding	421.0	14.3	689.5	17.4	639.5	15.1
Laying of new orchards, vineyards, berry and hop plantations	109-1	3.7	175.0	4.4	185.0	4.4

<sup>38</sup> Report: Agricultural subsidies: Analysis of the existing legislation in Ukraine as per compliance with the WTO agreements. B. Spinhua, K. Shkurupiy, O. Ustenko/Ukrainian — European consultative center on legislative issues

<sup>39</sup> Ibid.

<sup>40</sup> Report of O. Nivyevesky. Disbursements for agriculture and the WTO. Institute for economic research and counseling.

	2004		2005		2006	
	%	UAH, million	%	UAH, million	%	
Partial compensation for machinery and mineral fertilizer cost	393.7	13.3	270.0	6.8	102.0	2.4
Financial support for the development of dairy factories	0.0	0.0	10.0	0.3	0.0	0.0
Agrarian Fund	0.0	0.0	42.0	1.1	20.0	0.5
Green box	1677.8	56.8	2252.6	56.8	2576.1	61.0
Research and development, creation of scientific programs for certain categories of products	61.8	2.1	113.0	2.8	134.6	3.2
Protection against pests and diseases	86.3	2.9	131.4	3.3	136.0	3.2
Selection in animal and plant breeding	152.7	5.2	224.0	5.6	224.0	5.3
Broadening of experience and consultative services	7.9	0.3	16.3	0.4	38.0	0.5
Services in general inspection and inspection of certain types of products for their compliance with health preservation norms, safety, quality level and standards	606.9	20.6	737.9	18.6	893,1	21.2
Training, retraining, and postgraduate courses for specialists and workers in production and social spheres in villages	603.1	20.4	881.5	22.2	1005.4	23.8
Land reform	1.8	0.1	5.0	0.1	5.0	0.1
Infrastructure development in villages	15.6	0.5	17.0	0.4	17.0	0.4
Environmental protection	24.4	0.8	26,5	0.7	29,0	0.7

	2004		2005		2006	
	%	UAH, million	%	UAH, million	%	
Programs for income insurance	0.0	0.0	54.0	1.4	54.0	1.3
Creation of state reserves to provide for food safety	50.0	1.7	25.9	0.7	20.0	0.5
Disaster assistance	67.3	2.3	20.0	0.5	20.0	0.5

Based on this Table, one can conclude that a positive tendency is observed in Ukraine regarding an increase in measures attributed by the WTO Agreements to the so-called «green box». This tendency is apparent both in relative (from 56.8 % of the total volume of agrarian subsidies in 2004 to 61 % in the 2006 budget) and absolute terms – UAH 1,667.8 million in 2004 and UAH 2,576.1 million in 2006. Above all, in accordance to pre-planned measures, part of the «amber box» subsidies must decrease throughout 2006 which corresponds to the world trends of a decline in this type of measure.

In order to implement a comprehensive program of agricultural support in Ukraine the Law of Ukraine «On State Support of Agriculture in Ukraine» was adopted in 2004. The Law identifies the basis of the state policy in budget, credit, price, insurance, regulatory and other spheres of state management in terms of stimulating agricultural production and agrarian market development, and also ensuring food safety of the population and the country on the whole. Particularly, the Law establishes the regulation of wholesale prices for certain agricultural produce by way of establishing minimum and maximum limits for purchasing prices. The essence of the state price regulating measures lies in state interventions by the Agrarian Fund in volumes that allow to set prices at a level not lower than the minimum purchasing price and not higher than maximum purchasing price. Apart from price regulation the Law envisages credit support to agricultural producers (credit subsidy) which includes a partial payment of interest for short-term and mid-term credits granted

by banks in the national currency. The credit subsidies are granted in amounts of up to 50 % of interest rate. It should also be mentioned that the above legislation does not contain a program for long-term credit support – more than five years – which, to our mind, is crucial for agricultural producers to fulfil material and technical re-equipment, which at the current stage serves as a prerequisite for a competitive economy. Moreover, the Law identifies the possibility of state intervention by means of temporary administrative price regulation through:

a) restriction of sales mark-up (or discount) in wholesale or retail markets for certain objects of price regulation;

b) establishing limits of profitability to cost ratio;

c) establishing non-tariff limits (quotas) for imports or exports that are subject to state price regulation.

A significant step forward is the adoption of the Law of Ukraine #5483 «On the Introduction of Changes to Some Laws of Ukraine for the Taxation of Agricultural Enterprises and Maintaining Social Standards of Its Workers» which introduces the new scheme of VAT payment and brings solution to a number of social issues like, for example, mandatory state pension insurance. In order to improve the transparency of availing grants to agricultural producers, Decree #239 of the Cabinet of Ministers, «On the Approval of the Order of Use of State Budget Funds in 2006 Allocated for Financial Support of Plant Cultivation by Means of Grants» was adopted on March 2, 2006. The Decree defined a mechanism to minimize distortions in grants' distribution resulting from abuse of power or submitting deliberately distorted information to relevant state bodies. The drawback of the existing system for subsidizing domestic producers is a *de facto* orientation of these measures towards large producers at the expense of the needs of small private farms.

It should also be mentioned that at the current phase of the negotiation process on Ukraine's accession to the WTO the country strives to gain the advantage of measures for agricultural support in the

amount of US \$ 1.14 billion; in other words, the predetermined measures attributed to «amber box» could be implemented<sup>41</sup>. Nonetheless, certain countries which are calling for a radical reduction of such measures, Australia in particular, demand that Ukraine cuts the «amber box» subsidies to US\$ 265 million which may result in the Ukrainian government's having to revise the complexity of measures aimed at agricultural support.

### Conclusions

For a long time there has been no global agreement governing agricultural trade and only during the Uruguay round of multilateral trade negotiations in the framework of the WTO did a document emerge which means to regulate trade issues in one of the most sensitive spheres of economics – agriculture. It has led to a situation where state measures that violate fair rules of international trade, subsidies in particular, were specifically limited alongside certain allowances of their use. Nevertheless, incompleteness of the process of subsidies elimination enabled some countries to use their substantial financial resources for capturing a dominant position in the world agricultural markets.

By subsidizing their agrarian sectors, developed countries such as the U.S. and the EU can influence world agricultural prices, lowering them, thus reducing the export profits of a great number of developing countries for which financial inflows from agricultural exports appear to be one of the most important indexes that promote the development of their national economies.

In order to avoid the further proliferation of such trends in some agricultural exporting countries, developing countries have created a number of informal coalitions in the framework of the WTO with a view of promoting their interests in the arena of

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<sup>41</sup> Report of O. Nivjevsky. Disbursements for agriculture and the WTO. Institute for economic research and counseling  
[http://www.ier.kiev.ua/Ukraine/RT/rt28092005\\_present/rt\\_28092005\\_ukr\\_nivjevskiy.pdf#search=%D1%81%D1%96](http://www.ier.kiev.ua/Ukraine/RT/rt28092005_present/rt_28092005_ukr_nivjevskiy.pdf#search=%D1%81%D1%96)



international negotiations. Their demands, in the first place, concern the further liberalization of international agricultural trade and a preferential approach to the least developed countries. The Cairns Group and the G-22 belong to these groups.

Given Ukraine's aspiration for WTO accession and the importance of agriculture for this country, reforms in the support of the national agrarian sector to comply with requirements of the WTO may require a drastic decrease in «amber box» measures in Ukraine and a gradual transition to solely «green» subsidies if these rules are adopted.

Taking into account the functioning of different informal groupings within the WTO and after Ukraine acquires membership in this international organization, it would be reasonable for Ukraine to join the G-22. Having its own business lobby in this quite «young» and ambitious club, Ukraine will have the opportunity to defend its own interests against countries and organizations which pursue an active protectionist policy such as the U.S. and EU, and to increase the agricultural exports to the world market.

WTO membership does not require Ukraine to totally cancel all kinds of state support of agricultural production, thus relevant bodies of power should set the right priorities and ensure state support for those industries that have strategic importance for the food safety of the country.

To create a competitive agrarian sector in Ukraine a number of normative and institutional transformations should be accomplished:

- it is expedient to enhance the potential of perspective sectors of the world economy (for example, resuming flax production);
- diversify the geographical structure of international agricultural trade, especially exports, thereby strengthening the economic safety of the country;
- foreign representations and embassies of Ukraine should search for potential buyers of agricultural produce, render support and develop diplomatic relations with genuine partners, create the image of

Ukraine as of a powerful world exporter of agricultural products.

Under current circumstances, the main task still to be fulfilled by Ukraine is to continue with the negotiation process with WTO member-states and develop provisions which would not contradict its own national interests.

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