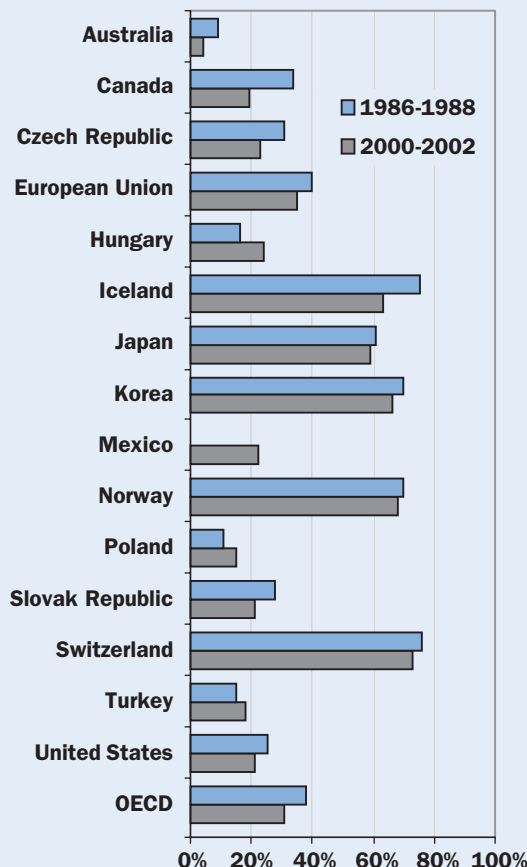


Producer Support Estimate (PSE) by Country (% of value of gross farm receipts)



Source: PSE/CSE Support Estimate Database, OECD 2003

Subsidies to Agriculture: Why?

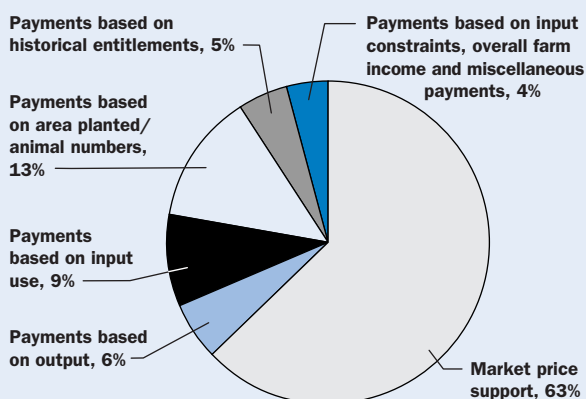
Agricultural policies in OECD countries continue to transfer large sums of money to agricultural producers. In 2002 this support totaled \$235 billion, of which \$100 billion was accounted for by the European Union and \$40 billion by the US. These transfers come from consumers, through higher prices, and from taxpayers, through budgetary allocations to agriculture. This support is currently estimated at 31% of total farm receipts in the OECD area, 18% in the US and 36% in the EU.

Why are governments providing this large amount of support to farmers? Mainly because they want to support farm incomes and promote the services that agriculture can provide to society, such as landscape values. However, farm household incomes in OECD countries are generally well in line with those of other families. And services to society can rarely be promoted efficiently by forms of support that provide incentives to expand the production of wheat and milk. Yet, such support is still predominant. Two thirds of producer support comes in the form of price support or output payments. Payments directly targeted to what policies want to achieve are still very limited—a strong case for reform.

The 2002 US Farm Act further institutionalized payments to agricultural producers and increased the extent to which payments are coupled to farm output. It thus provides farmers with incentives to expand production and can potentially depress world market prices. But even with these policy changes, the United States is only in the middle of the pack of OECD countries in providing support to producers.

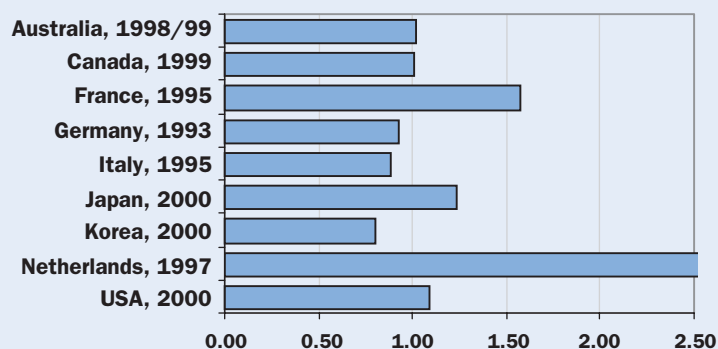
OECD, Paris (2003), *OECD Agricultural Outlook 2003-2008*, ISBN: 92-64-10302-3, \$46.00

Composition of Producer Support Estimate in OECD Countries, 2000–2002



Source: *Agricultural Policies in OECD Countries: Monitoring and Evaluation*, OECD 2003

Total Income of Farm Households Compared to Total Income of All Households*



*1.00 Represents Total Income of All Households

Source: *Farm Household Income*, OECD 2003

Agriculture, The Rich Getting Richer

The distribution of producer support is often proportional to a farm's production capacity. In the US, this means 90% of agricultural support goes to the largest 25% of farms. The support ends up having the perverse effect of taxing relatively poor food consumers in order to raise the incomes of well-off producers. Production based support is not only inefficient in addressing the poverty concerns of rural agriculture, but it also creates a wide income gap between large-scale and small-scale farmers.

Additionally, the *transfer efficiency* of support (the proportion of support that ends up as extra income for the farm household) is far from the ideal of 100% of every dollar in support going to agriculture. In reality, with price support, the most common policy, no more than twenty-five cents for every dollar of producer support ends up in the farmer's pocket. Even more efficient support measures transfer less than one-half of that dollar to farm households.

This is because producer support encourages additional production that inevitably leads to higher prices for land and larger production costs. Farmers therefore eventually pay out the lion's share of the benefits from support transfers to land owners, input suppliers, and wasted resources. This allows the suppliers of those inputs to capture a large part of the support intended for the farmers themselves.

Rural policies which target low income households, as opposed to the whole agricultural sector, are thus a more efficient means of reaching low-income farm households.

OECD, Paris (2003), *Farm Household Income, Issues and Policy Responses*, ISBN: 92-64-09965-4, \$21.00

Subsidies vs. Sustainability

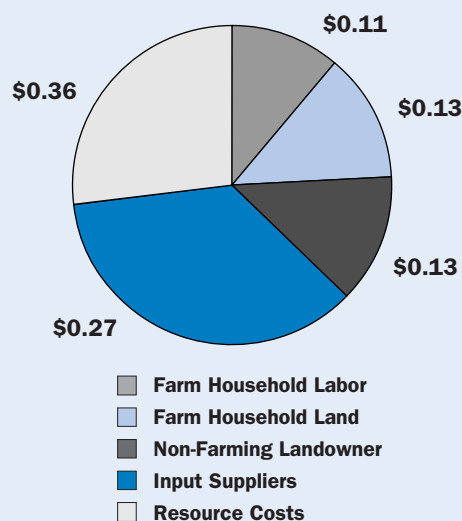
Agriculture uses 46% of the land and 40% of the annual water supply in the US. Like in many other OECD countries, subsidies to farmers contribute to water pollution, and farmers pay substantially lower water prices than other users. Recently, the OECD reported that while nitrogen run-off, pesticide use and agricultural greenhouse gas emissions have fallen since the mid-1980s in most OECD countries, they have increased in the United States.

This trend may continue on the back of subsidies and production-based payments which create artificial incentives for farmers to increase production and weaken the sustainability of the land and water resources used in agriculture.

The 2002 US Farm Bill, while institutionalizing new and additional subsidy payments, also gave a much greater prominence to improving the environment. Funding to clean up environmental pollution, encourage and train farmers to adopt environmentally friendly practices and to produce renewable energy crops is planned to increase by 80% over the next six years, totaling US\$ 21 billion.

OECD, Paris (2003), *Agricultural Policies in OECD Countries, Monitoring and Evaluation*, ISBN: 92-64-10229-9, \$69.00

**Where Does the Money Go?
Market Price Support
Transfer Efficiency***
(cents on the dollar)



* Farm Household Land and Labor as a % of Total Transfer

Note: 'Resource Costs' and 'Input Suppliers' refer to the portions taken up by the equipment, seed, water, power, and other providers as a result of increased production.

Source: *Farm Household Income*, OECD 2003

Agriculture and the Environment

	Agriculture Share of Water Use	Agriculture Share of Greenhouse Gas Emissions
	1990s % Total Use	1990s % Total Use
Belgium	0 ¹	7.3
Canada	8	10.4
Denmark	37	15.4
France	12	16.0
Hungary	8	7.8
Ireland	15	31.5
Japan	63	1.5
New Zealand	73	55.2
Poland	9	5.2
Sweden	6	11.6
UK	1	8.2
United States	40	8.9
EU²	32	9.6
OECD	44	8.9

¹ Includes Luxembourg

² Does not include Austria and Netherlands

Source: *Agricultural Policies in OECD Countries*, OECD 2003

More Progress Needed on Tariffs

Studies have shown that reducing tariffs on agricultural products provides greater benefits, both globally and to individual liberalizing countries, than either reforms of domestic support or reduction of export subsidies. The quicker countries can reach agreements to further reduce tariffs and expand market access, the sooner they can begin to enjoy the fruits of more open markets.

The WTO Uruguay Round Agreement on Agriculture (URAA) successfully capped and reduced tariff levels, while also converting non-tariff barriers into tariffs. The agreement's ultimate goal was an average reduction of 36 percent of tariffs by 2000. Even with these reductions, tariff levels in major OECD countries for temperate zone products have remained very high.

Presently, although market access seems to be liberalizing, there is much room for improvement. The high levels of border protection are an important issue in the ongoing WTO negotiations.

The average tariff rate on temperate zone products for most OECD countries in 2000 was more than 95 percent. Among the Quad countries (Canada, European Union, Japan and United States), Japan, with an average rate of more than 190 percent, was the highest, while the United States with an average rate of 28 percent was the lowest.

Mega tariffs, exceeding 100 percent, are prevalent in the agricultural markets of developed countries. In 2000, more than 30% of the tariff lines in both Canada and the EU had mega tariffs, and almost 40% in Japan. The US among the Quad countries had the lowest share with about 10% of tariff lines being mega tariffs.

OECD, Paris (2002), *Agriculture and Trade Liberalisation, Extending the Uruguay Round Agreement*, ISBN: 92-64-19709-5, \$47.00

WTO and OECD Support Indicators

The OECD approach to support measurement is primarily 'economic', as its purpose is to enable policy developments to be monitored and evaluated in economic terms. The WTO employs a 'negotiated' or 'legal' concept that classifies support into various defined 'boxes' of different colors for the purpose of ensuring compliance, in legal terms, with agreed international commitments.

At the WTO, domestic support that is considered to be most damaging in terms of production and trade distortions falls into the 'amber box', and is subject to agreed limits. These policies are generally those that support prices or make production payments directly to farmers. The agreed reduction commitments are expressed in terms of a "Total Aggregate Measurement of Support" (Total AMS). Compared to OECD's Producer Support Estimates (PSE) which compares actual market prices to world prices, this is a negotiated measure which compares government-set prices to a fixed external reference price.

The 'green box' subsidies are those that "do not distort trade, or at most cause minimal distortion", and as such are allowed without limits and without reduction requirements. These policies have to be government-funded, must not involve price support, and must comply with defined policy-specific criteria.

The 'blue box' includes support that is available on condition that farmers limit production, on the basis that such support is somewhat less distorting than 'amber box' policies. Reduction commitments have not been agreed upon, although countries are not supposed to increase spending under this heading.

Although no country has been found to be in breach of its WTO domestic support commitments, OECD results show that many countries are still maintaining high and relatively unchanged levels of support, with only limited shifts to less trade distorting policies.

Subsidies Draining Fisheries

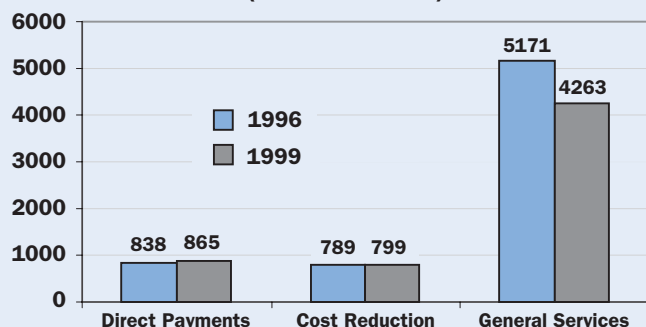
Fisheries is another area of food production where subsidies are controversial. Fisheries subsidies can contribute to excessive fishing capacity, fish stock depletion and illegal, unreported and unregulated fishing. By reducing the cost of fishing operations with subsidies of \$6.2 billion, OECD countries in many cases encourage the unsustainable use of fisheries resources, oceans and living marine resources. The value of fisheries subsidies as a percentage of the gross value of production in the OECD area was about 20 percent in 2002.

A better understanding of the links between subsidies, fisheries management and resource impacts is prerequisite to establishing effective regimes that nationally and internationally ensure a more sustainable resource use.

OECD, Paris (2003), *Review of Fisheries in OECD Countries, Policies and Summary Statistics*, ISBN: 92-64-10140-3, \$75.00

OECD Government Financial Transfers to Fisheries*

(millions of US\$)



* Total Transfers as a % of Total Landed Value has increased from 18% of Landed Value in 1996 to 20% of Landed Value in 1999

Poverty Reduction through Policy Reform

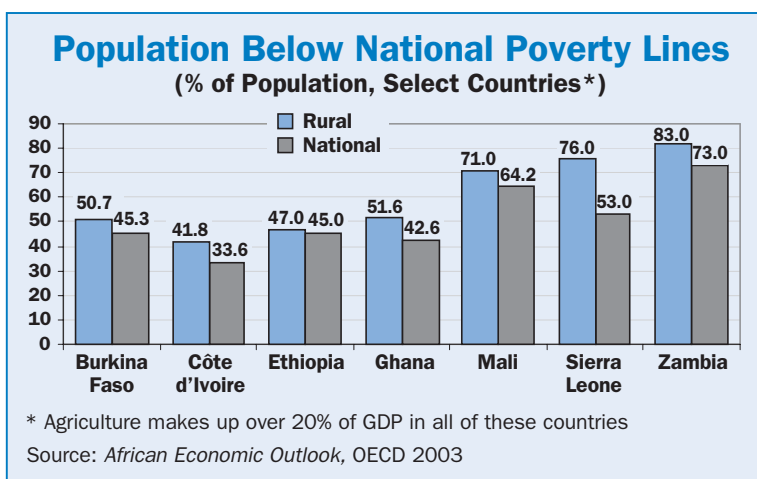
In the poorest countries, up to 90% of those in poverty live in rural areas where agriculture is the main source of income. Besides income, further spillover effects such as landscape, biodiversity cultivation, cultural preservation, rural development, water accessibility, and food security also accompany agriculture into rural areas. There is a vicious circle between food poverty and factors such as war and conflict, weak governance, and HIV/AIDS that needs to be broken.

Growth in agricultural production has proven effective in lifting people out of poverty through more efficient uses of resources. Exports can contribute significantly to growth. Yet, agricultural markets are among the most distorted in the world with both developed and developing countries maintaining high levels of protection. Agricultural policies also matter to poor urban and non-farm households because food is a major household expenditure.

Many OECD countries impose high tariffs on developing country agricultural exports. Along with this, developing countries had to compete last year with \$235 billion in agricultural support in the OECD area. This support alone is equivalent to the value of developing country agricultural exports in 2002 and three times the value of Official Development Assistance (foreign aid) provided by OECD countries. It is unlikely that large strides will be made in poverty reduction in agriculture centers and rural areas of the developing world without targeted policy reform.

OECD, Paris (2003), *African Economic Outlook 2002/2003*, ISBN: 92-64-10003-2, \$70.00

OECD, Paris (2003), *Agricultural Trade and Poverty*, ISBN: 92-64-19733-8. \$45.00



ORGANIZATION FOR ECONOMIC COOPERATION AND DEVELOPMENT

OECD Washington Center
2001 L Street, N.W., Suite 650
Washington, DC 20036-4922
Phone (202) 785-6323
Fax (202) 785-0350
Book Orders Only (800) 456-6323

OECD Washington Center Contacts

Press and Information Contacts:

Sandra Wilson (202) 822-3866
sandra.wilson@oecd.org

Joachim Doll (202) 887-3466
joachim.doll@oecd.org

Stanford Swinton

Contributions by:
Sheena Ahmad
Anna Reeves

OECD Member Countries

- | | |
|----------------|-----------------|
| Australia | Korea |
| Austria | Luxembourg |
| Belgium | Mexico |
| Canada | Netherlands |
| Czech Republic | New Zealand |
| Denmark | Norway |
| Finland | Poland |
| France | Portugal |
| Germany | Slovak Republic |
| Greece | Spain |
| Hungary | Sweden |
| Iceland | Switzerland |
| Ireland | Turkey |
| Italy | United Kingdom |
| Japan | United States |

OECD Washington Center
2001 L Street, N.W., Suite 650
Washington, DC 20036-4922

OECD in Washington



Non-Profit Org.
U.S. Postage
PAID
Washington, D.C.
Permit No. 8038