CEREAL POLICIES REVIEW

1997-98

FOREWORD

The 1997-98 edition of the *Cereal Policies Review* is the seventh of an annual series on recent developments in national cereal policies. The series is a response to the considerable interest in developments in cereal policies, in both the national and international arena. We hope that the information provided will be of use to policy-makers and others concerned with the broader issues of agricultural development and food security.

The first chapter of this *Review* consists of a survey of developments in national cereal policies during the past year. The materials are organized under various sections, each examining the main target variable of policy instruments: production; consumption; marketing and stocking; and trade. The information was collected from a variety of sources, including FAO policy questionnaires, news agencies, government and FAO reports.

In addition, as the question of state trading enterprises (STEs) in agriculture is gaining momentum as a possible area of focus for the next round of multilateral trade negotiations, the second chapter examines the current role of cereal state trading enterprises in the cereals sector. The third chapter highlights the recent reforms in food subsidy policies and examines the requirements and policy options for designing such programmes in light of their impact on the domestic economy.

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1. REVIEW OF DEVELOPMENTS IN NATIONAL CEREAL POLICIES

1.1 Introduction

This chapter examines the main trends in national cereal policies, which have emerged over the past year. The policies are reviewed in distinct categories, i.e. production; consumption; marketing and stocking; international trade and other agricultural policy programmes, to map out specific themes in national policies.

A major theme in agricultural policies in both developed and developing countries in recent years, has been the reduced role of government intervention in domestic and international agricultural markets as a result of the Uruguay Round Agreement. By and large, the trend was not altered by more recent factors influencing agricultural markets such as the El Nino weather phenomenon and the deterioration in the world economic outlook.

1.2 Production Policy

1.2.1 Policies Affecting Producer Prices and Production Incentives in Developing Countries

In the developing countries, policy initiatives concerned with domestic cereal production during the 1997-98 period have followed the same pattern exhibited during the previous period (1995-97). However, in a number of countries where the impact of the weather and financial exigencies were felt strongly, reforms slowed down.

In Sub-Saharan Africa, the Government of **Mali** decided in May 1998 to restart wheat production in its low-rainfall Timbuktu region to cut imports by 20 percent. About 50 000 hectares in lake areas fed by the Niger River would be turned over to wheat production. The plan includes the creation of 2-4 hectare smallholdings fed by water-pump irrigation. The Government would provide financial backing for crop marketing. In April 1998, the Government of **Zimbabwe** announced the doubling of producer price of maize to Z$2 400 (US$138) per tonne. This is the first increase in the producer price in two years.

In **Asia**, producer support policies were strengthened in several countries. The Government of **India**, in an effort to increase wheat procurement, in April 1998 provided a procurement bonus of 550 Rupees (US$14) per tonne, thus increasing the effective support price for the 1998/99 marketing year to 5 100 Rupees (US$129) per tonne compared to 4 750 Rupees (US$121) in 1997/98. The Government of **Indonesia** decided in May 1998 to raise the prices for unhusked rice from 700 Rupiah (US$0.14) per kilogram to 1 000 Rupiah (US$0.20) per kilogram starting in June, in order to boost incomes. This move aimed at encouraging farmers to plant more rice and at improving their living standard. Prices of rice rose sharply since the crisis earlier in 1998, in which the Rupiah fell by more than 80 percent against the US dollar. In early 1998, the **Philippines** Government introduced a package of reform measures targeting the institutional and policy framework for its grains sector development. The main highlights of this proposed policy package are presented in Box 1 below. In an effort to promote the use of high-yielding maize hybrids, **Thailand**'s Ministry of Agriculture and Co-operatives in June 1998 offered maize seeds to farmers at a price of 8 Baht (US$14 cents) per kilogram, which amounted to a subsidy of about 90 percent. However, the Ministry plans to reduce the subsidy to 50 percent by 1999/2000.

In **Latin America**, the Government of **Argentina**, in May 1998 suspended for forty days an earlier measure to reduce the value-added tax (VAT) on agricultural inputs by 50 percent. Among the items to benefit from the 50 percent reduction were purchases of fertilizers and chemicals, transport, seeds and veterinary products. To assist producers affected by lower international prices, the **Mexican** Government, in June 1998 raised the support price for domestic sorghum by 7 percent to 960 Pesos (US$108) per tonne.

Box 1: The Government of the Philippines new institutional and policy framework for the grains sector development[1]

Policy Reform Objective	Policy and Institutional Measures
1. Price stabilization and affordable prices for low income consumers	• Adjusting grain prices to compensate for the 1997/98 exchange rate movements and changes in world market prices for imported rice. • Enable market-oriented pricing policy for the disposal of old stocks of rice. • Setting the release price for regular milled rice at no less than twice the National Food Authority's (NFA) domestic paddy procurement price (inclusive of any seasonal paddy price premium); or the world market price ex-warehouse Manila plus a reasonable return to capital, whichever is greater. • Establish a nation-wide food safety net programme for the poor, which should be adequately funded.
2. Seasonal domestic procurement pricing and volumes for paddy	• Set the domestic rice procurement price equal to a three year weighted average of (a) the prevailing unit production cost of paddy (inclusive of returns to farmers' land and labour) and (b) the world market price (based on Thai 25 percent broken, fob Bangkok) ex warehouse Manila converted to the farm gate paddy price using the prevailing milling ratio and marketing cost. For the world price, the weight is the proportion of the average volume of imported rice to that of domestic rice production in the last three years. • The procurement volume in a given year should be set on 1 July in a given crop-year to no more than the average annual volume of the base period from 1991/92 to 1997/98. In the event of a surplus crop-year, the procurement volume will be limited to no more than the requirements of a thirty-day strategic rice buffer stock.
3. Transparent and timely rice import policy	• Assessment of the projected gap between production and consumption of rice in a given year based on which a Presidential decision to import the required volume or rice to stabilize rice supplies and prices and a public announcement of such a decision no later than 30 April in a given year.
4. Private sector participation	• Enable the private sector to import a set rice quota required to stabilize the market after setting aside the volume that the NFA requires to fill its 30-day strategic rice buffer stock. This is subject to the conditions that, the NFA will auction the import volume allocated to the private sector to licensed traders; and rice importation by the private sector is subject to the prevailing custom duties. • Set-up a voluntary private sector rice buffer stock programme. The programme requires that private sector importers deposit 10 percent of their imported rice in an NFA warehouse and pay storage charges. Withdrawal of programme rice stocks are not allowed before 1 July in any given year and the NFA has priority access to the programme stocks at acquisition cost plus a 5 percent margin.
5. Tariffication	• Replace the quantitative import restriction (QR) on rice with a tariff by no later than 31 December 2004. Enable, through simple and transparent auction system, a minimum import access volume (MAV) consistent with the WTO and a provision for increasing this volume based on assessment of local supply and demand for all sensitive agricultural products. The tariff rate on the MAV for rice should be set at no more than 50percent for fancy varieties and 3 percent for other varieties. For maize, out-quota tariff reductions already in place are as follows: from 30- 20 percent in 1998, 15 percent in 1999 and 10 percent in the year 2000.
6. Structural reform	• Break up the NFA into two agencies – one a government agency with regulatory function and the other, a corporation from the propriety part of the NFA with private sector equity of no more than 51 percent.

[1] Source: Ministry of Agriculture, the Philippines.

Elsewhere, in the **Syrian Arab Republic**, procurement prices for the 1997 crop were kept at the 1996 levels of US$240 per tonne for soft wheat and US$262 per tonne for hard wheat. This policy was intended to encourage the farmers to increase production and to enable the Government to purchase as much grain as possible.

In May 1998, the Ministry of Agriculture in **Turkey** announced support prices for grains for 1998/99. Although these were substantially higher than in the previous year and includes additional monthly increments, the sharp devaluation in the value of the Turkish lira means that prices weakened in terms of the US dollar. Thus, the price for Hard White Wheat at lira 58 300 per kilogram represents a decline from US$257 to US$232 per tonne and, similarly, white barley will go down from US$176 to US$159 per tonne, even though prices in lira rose.

1.2.2 Policy Initiatives in Developed Countries

In several developed countries, above average crops and weak export demand during 1997-98 pushed domestic grain prices to close to their minimum support levels. In this context, producer support policies were strengthened in a number of countries, while in others, the emphasis was on production control.

In a move aimed at supporting bread wheat producers, **Bulgaria**'s State Agricultural Fund allocated 5 321 million Levs (US$3 million) in early 1998. This amount covers 70 percent of the average production costs and the producers are required to sell their 1998 harvest to the state at a fixed price of 230 000 Levs (US$29) per tonne. In a further effort to stimulate the use of production inputs, the Government distributed vouchers to all landowners to be used for purchases of seeds, fertilizers, agro-chemicals and fuel, or to pay for various services related to crop production. Landowners were allocated three vouchers for each hectare of land. Two of the vouchers, valued at 150 000 Levs (US$19) were for use during the spring/summer period and the third, valued at 83 000 Levs (US$10), was for planting winter grains in late 1998. The vouchers cover about 8-10 percent of average production costs.

With effect from December 1997, **Canada** increased initial payments for barley by C$15 (US$10) per tonne for two-row varieties to C$178 (US$124), and by C$20 (US$15) for six-row varieties to C$158 (US$110) per tonne. Initial payments are guaranteed by the Government and are paid to producers on delivery of their grain.

Furthermore, in July 1998, the Canadian Wheat Board (CWB) announced further increases to the 1997/98 initial payments for wheat, including durum. This was the fourth adjustment for durum, and the third for other wheat. The new payments for the base grades in the wheat pools are shown in the table below.

Table 1: Initial Payments for Wheat in 1997/98

Grade	CAN $		US $	
	August 1997	July 1998	August 1997	July 1998
Wheat				
Nº 1 CW Red Spring	130	172	94	118
Nº 3 CW Red Spring	119	161	86	110
Nº 1 CW Amber	179	260	130	178

In June 1998, the **EC** Council of Ministers adopted the farm price package for 1998/99 (July/June). With regard to grains, the intervention price remained unchanged at 119.19 Ecus (US$143) per tonne, and the monthly increment for storage remains at 1.00 Ecu per tonne. The set-aside rate for 1999 will be 10 percent, double that of the previous season. According to calculations by the Commission, the higher rate should result in an increase of 1.5 million hectares in the area set-aside, and reduce grain production by 8 million tonnes.

In February 1998, the Government of **Hungary** set the guaranteed procurement price for the 1998 maize crop at 16 500 Forints (US$76) per tonne for December 1998, 16 710 Forints (US$77) for January and 16 780 Forints (US$78) for February 1999. Procurement at the guaranteed price would apply only to feed maize of a standard quality and to members of the National Cereal Council who had declared the size of their cultivated land as of end May 1998. According to the regulations, a single producer is allowed to offer for purchase up to 3.2 tonnes of maize for every hectare planted, at the guaranteed price, which covers about 80-90 percent of average production costs.

In August 1997, the Government of **Japan** reduced the producer prices for wheat and barley by 0.95 percent from the previous year. The new price for wheat was set at 9 023 yen per 60 kilograms (US$1 300 per tonne) and for barley at 6 748 yen per 60 kilograms (US$933 per tonne). The Government's purchase price for rice was also reduced by 2.5 percent to 15 800 yen per 60 kilograms (US$2 083 per ton). The Government plans to reduce stocks of rice over the next three years from about 3.7 million tonnes expected at the end of October 1998 to 2 million tonnes by October 2000. As a result, a further 170 000 hectares of land may have to be moved out of rice farming.

In July 1998, the Government of **Romania**, reacting to the low international wheat prices relative to those for domestic supplies, provided subsidies to cover purchases of 150 000 tonnes of wheat, with a subsidy of 200 000 Lei (US$25) per tonne.

The Government of the **Russian Federation**, in July 1997 passed a law that sets out the legal basis for ensuring the safe use of pesticides and agricultural chemicals in order to protect people and the environment. In particular, the law forbids the use of pesticides and chemicals not in the state official catalogue, reinforces licensing requirements, standardization and certification in the use of pesticides and chemicals.

In June 1998, the Federal Republic of **Yugoslavia** announced that it would purchase the 1998 wheat crop in three installments. The first installment of 40 percent of the value would be due by the end of August and the second and third installment of 30 percent each by the end of September and October. The country's commodity reserve agency plans to purchase 600 000 tonnes of the 1998 wheat crop. The Government had set a guaranteed price for the best quality wheat at 1.1 Dinars (US$0.18) per kilogram and 0.9 Dinar (US$0.15) for second and third categories.

In September 1997, the **United States** Government announced that the sign-up period for its Conservation Reserve Programme (CRP) would be held from 14 October to 14 November 1997. After deducting contracts reaching expiry, around 11.3 million hectares remained in the CRP as of 1 October 1997 compared with the programme limit of 14.7 million hectares. In January 1998, it was announced that 2.8 million hectares had been accepted at the latest sign-up for entry into the CRP by 1 October 1998. The USDA confirmed that at least 2.2 million hectares would be allocated for entry under a continuous sign-up process to cover high priority conservation practices.

1.3 Marketing and Stocking Policy

Policy initiatives regarding marketing and stocks indicate somewhat diverse trends among developed and developing countries, although, the general direction of change is still toward reduced market intervention.

In June 1998, following an earlier relaxation of **China's** State controls, private traders have been allowed to purchase about a third of all grain sold by producers. The official procurement and distribution system had incurred substantial losses in recent seasons, estimated at around US$2.5 billion. In order to curb these losses, several policy changes were introduced. Regulations issued by the State Administration of Industry and Commerce stipulate that grain procurement from farms will be limited to official grain enterprises. However, an element of decentralization had been adopted whereby local authorities will be allowed to set prices paid to farmers based on prices established by the central Government. Private traders failing to conform to these rules would lose their business licenses.

In November 1997, the Government of **Indonesia** announced that, as part of its official privatization programme, BULOG, the state commodity agency, would lose its monopoly on imports of wheat. An import duty of 10 percent was introduced on imports of wheat flour from 1 January 1998, which will be reduced to 5 percent by 2003. BULOG will continue to purchase wheat flour from millers at an agreed price, which will then be sold to wholesalers and retailers at a lower price. The Government will provide a subsidy to cover the difference in prices.

In late April 1998, BULOG increased the prices at which it sells wheat flour, and rice to traders for the second time. Earlier in April, BULOG had raised the price of wheat flour by 76 percent and rice by 20 percent. Traders obtain rice from BULOG, which has a monopoly on rice imports, while wheat is channeled to traders through the Association of Indonesian Sugar and Wheat-flour Distributors (Gapegti), an arm of BULOG. As a result of the second price increase, a 25-kilogram bag of wheat-flour was selling at 34 687 (US$7) Rupiah, against 19 657 (US$4) Rupiah and 100 kilograms of rice at 120 000 (US$24) Rupiah against 100 000 (US$20) previously.

Furthermore, in late July 1998, Indonesia bought 745 000 tonnes of wheat at tender from the United States, Canada and Australia for August, September and October shipments at between US$129 and US$171 per tonne, on a cost-and-freight (C&F) basis. The tender, conducted through BULOG, was the first under the new Government's policy of transparency in acquiring commodities.

The Government of **Myanmar**, in late 1997, announced a new sealed tender bidding process for the procurement of paddy. Implementation of this new procurement system was granted to the Myanmar Agricultural Products Trading (MAPT), a state agency under the Ministry of Commerce. Although the new policy provides for no changes to the Government export parastatal, i.e. the Myanmar Export Import Services, the inclusion of quality standards and limited private sector involvement was expected to enhance the country's rice production and export potential.

The new procurement policy replaces the previous quota system in which the MAPT procured paddy directly from farmers. Under that quota system, farmers were required to supply MAPT with a certain quantity of paddy at a specified price that were often below market levels. This system acted as a disincentive to plant rice as farmers were under no obligation to surrender portions of competing crops to the Government for less than their market price and hence, preferred to switch to these crops.

The new system frees farmers from the quota obligation and allows them to sell all of their rice at market prices. Further, the MAPT introduced incentives for improved quality by establishing premiums for meeting export quality specifications and requiring that paddy be delivered bagged and labeled with the supplying company's name. This new focus on quality was to provide an incentive to farmers and to improve supplies for the milling industry.

The Government of **Turkey**, in a bid to reduce its stocks of grain in the 1997/98 marketing year, provided incentives to increase sales in both the domestic and export markets. The state agency, *Topak Mahsullei Ofisi* (TMO), was authorized to sell grain on the domestic market through a combination of deferred payments and reduced sales prices. In addition, in early March 1998, TMO introduced a new programme under

which it planned to sell wheat from its stocks at the world market price to millers and exporters. Unlike the deferred payment programme, this new programme will be available to millers only if they re-export the wheat in the form of flour and other wheat products.

In response to widespread over-booking of rice contracts, the Government of **Viet Nam**, in early 1998, announced plans to create a Rice Marketing Board, which was to commence operations by the end of 1998. According to the Government, the Board's main role would be to provide market information to buyers and sellers of Viet Namese rice. Viet Nam currently controls rice exports through quota allocations to provincial and state-owned companies and to two large central food corporations. The move to introduce additional state control through a Rice Marketing Board came at a time of limited opening of the export regime to allow some private sector participation. Two private sector companies had been approved to export rice.

In March 1998, wheat farmers in **Zimbabwe** expressed concern over the Government's plan to obtain cheaper wheat from outside the country, indicating that this would disadvantage domestic wheat producers. Wheat farmers have been gradually abandoning wheat in favour of other crops, citing problems of rising production costs. The Government had tried to stabilize bread prices in the wake of food riots in January but the programme was subsequently abandoned.

With effect from 1 October 1997, the **Australian Wheat Board** (AWB) began trading in grains from other origins. The AWB also planned to expand sales on a C&F basis in order to retain profits from ocean freight operations. The C&F sales were estimated at 20 percent of all shipments in 1996/97 (October/September), and the target is to eventually trade 80 percent on this basis.

In May 1998, the Board was privatized with ownership transferred to growers. A public company was established with two subsidiaries, AWB (International) Ltd. and AWB (Australia) Ltd. The creation of AWB Ltd. was designed to lead to more marketing opportunities for Australian grain growers, both through innovative contractual arrangements and through the enhancement of its marketing strategies through the wheat pools. AWB Ltd. will be responsible for all funding and the provision of businesses and corporate services. The company will act as borrower for the AWB group and will lend to the subsidiaries, particularly the pools subsidiary, AWB (Australia) Ltd., to fund advance payments to growers. AWB (Australia) will be responsible for domestic wheat and other grain trading and the export of non-statutory grains, as well as other commercial ventures undertaken by the group. AWB (International) will be responsible for the wheat export pools and will be focused on maximizing pool returns.

Bulgaria's Government, approved a legislation in late May 1998 aimed at facilitating grain trade, making it more transparent before the planned privatization of grain silos by the end of 1998. Around 80 percent of the grain silos, which were run by state-owned trading firms, were planned to be sold. The bill provides for all grain silos to be licensed and listed in a public register; silo owners applying for a license should have a minimum capital of 100 million Levs (US$563 000). In addition, all grain traders, with the exception of producers should also register with the Government in order to provide adequate information on traded volumes.

In **Canada**, amendments[2] to the Canadian Wheat Board (CWB) Act were adopted in June 1998. A comparison of this new structure of the CWB and the new structure of the AWB are presented in Box 2 below.

[2] See Cereal Policies Review 1995-97, p. 11.

Box 2: A Comparison of the New Privatized AWB and the Amended CWB[3]

Australian Wheat Board	Canadian Wheat Board
Structure Grower- owned private corporation with two subsidiaries (wheat pooling/export and domestic trading/commercial). Operated under Corporations Law. Commercially focused on creating returns for shareholders.	**Structure** Mixed enterprise. Operated under the Amended CWB Act. Legislative objective is orderly marketing of wheat and barley in Canada within which the CWB attempts to maximize returns to producers of wheat and barley.
Financial Resources No government guarantees of pools and borrowings. Underwrites its own borrowing on its own capital base. The Wheat Industry Fund (WIF) will be converted to share capital and the levy on wheat sales for WIF will cease on 30 June 1999. Raises funds through bonds/notes in domestic and international financial markets. Additional capital provided from class B shares.	**Financial Resources** Borrowings underwritten by the federal government. Initial payment, set at the start of a pool period, guaranteed by the federal government. Adjustment and interim payments also guaranteed but will be removed when the Minister deems the contingency fund is adequate. Contingency fund will be used to cover losses arising from cash trading, early pool cash outs, and adjustments to initial payments during the crop year without government approval. Subject to the approval of the Minister of Finance, raises funds or invests moneys through bonds, debentures and notes in the domestic and international financial markets, and uses risk management tools such as options, futures contracts, forward contracts, and currency and commodity and interest rate swaps.
Marketing Functions Single desk monopoly for exports of wheat but subject to the National Competition Policy Review in 1999-2000; wheat for domestic use may be sold privately or to the AWB. Cash trading in the domestic market; may trade grain originating in other countries. Voluntary pool or cash trading in oats, sorghum, canola, cottonseed, tritcale, pulses, and other crops.	**Marketing Functions** Single desk monopoly for domestic human consumption of wheat and barley grown in western Canada (including wheat and barley products for export). Cash trading authority; can buy wheat and barley from any source. Certain types, classes, or grades of wheat and barley may be removed from the single desk monopoly. Single desk monopoly and/or pooling may be extended to include other crops.
Operational Modalities Pool Account Flexibility: (harvest, post-harvest, and final payments) may close pools during a season. May provide early pool cash-out options and deferred payment pools. May offer forward contracts prior to sowing. Operating expenses paid by shareholders. Coordinates grain logistics from the Bulk Handling Authority to ship. Ownership of commercial rights to wheat varieties. Investment in downstream processing.	**Operational Modalities** Pool Account Flexibility: (initial, adjustment, interim, and final payments) may increase initial payments quickly when conditions warrant. May close-out accounts at any time. May provide early pool cash-out options. May issue negotiable producer certificates. Operating expenses paid by producers. Participates in the coordination of grain movement from farm to ship. No ownership of plant varieties-CWB administers research. No authority for downstream processing investment from contingency fund

Hungary introduced a competitive bidding system for setting export subsidies to replace the flat-rate subsidy method with effect from January 1998. A special commission was established to monitor the new system, with overall responsibility passing from the Ministry of Industry, Trade and Tourism to the Ministry of Agriculture. The commission will subsequently be granted intervention authority to correct imbalances in the domestic market.

[3] Source: The Bi-weekly Bulletin, 30 January 1998, Vol. 11, #2, Agriculture and Agri-Food, Canada.

In July 1997, the Government of the **Russian Federation** passed a decree on the state regulation of agricultural production and on the safe use of pesticides and agricultural chemicals. The decree covers the mortgage of agricultural products and raw materials; the use of special prices (normative indicators) to ensure price parity between industrial and agricultural products, the granting of agricultural subsidies and compensation; as well as state regulation of insurance in the agricultural sector. In order to stabilize the market for agricultural products, the law also calls for "*purchasing* and *commodity intervention*". *Purchasing intervention* would be used when market prices for agricultural products, raw materials and food fall below a certain minimum level, or when producers cannot sell their products due to a drop in demand. *Commodity intervention* would be used when there is a shortage of goods on the market, or when market prices rise above a certain level.

In May 1998, the Federal Republic of **Yugoslavia** announced that it would bring food staples out of its commodity reserves and grant subsidies to food producers in an attempt to stabilize prices and supplies following the March 1998 devaluation. The Government decided to set aside a monthly amount of 20.6 million Dinars (US$1.9 million) to subsidize the production of milk, bread, sugar and oil.

1.4 Consumption Policy

There have been few changes reported in national consumption policies, some related to the deterioration in the economic situation.

1.4.1 Consumer Price Decontrol and Subsidy Measures

In March 1998, **India's** interim 1998/99 budget envisaged a food subsidy of 75 billion Rupees (US$1.82 billion), the same as in 1997/98. The Government provides food subsidies to state-run grain distribution agencies to sell foodgrains through official ration shops.

During 1998, negotiations between **Indonesia** and the IMF resulted in commitments to liberalize Indonesia's wheat and flour regime, hitherto controlled by BULOG. The wheat subsidy, which reduces the price of flour by about 40 percent, will be phased out over three months beginning in October 1998. Under this arrangement the Government pays the exchange rate differences between the actual market rate and the fixed rate of 5 000 Rupiah per US dollar for the import of strategic commodities. The subsidy would be gradually reduced by up to 70 percent should the Rupiah strengthen. For 1998 the subsidy amount was 5 200 billion Rupiah (US$1.04 billion), with 1 790 billion Rupiah (US$350 000) for rice, 1 720 billion (US$344 000) for wheat flour, 341 billion (US$68 000) for imported maize and the rest for other important commodities and medicine.

In May 1998, the **Mexican** Government raised the price of *tortilla* by 18 percent to 2.60 Pesos (US$0.28) per kilogram. Prior to this, the price of t*ortilla* has been increased in February 1998 from 1.90 Pesos (US$0.21) to 2.20 Pesos (US$0.24). The move was targeted to improve the production capacity of maize flour and tortilla shops and to provide job security for the *tortilla* industry workers. Furthermore, the Government indicated that it would continue to spend 1 580 million Pesos (US$174 million) on the *tortilla* subsidy and would give away 1 kilogram of *tortilla* per week to 1.7 million people who earn less than 70 Pesos (US$8.14) per day.

In addition, the Government offered 360 000 tonnes of subsidized locally grown white maize for sale in the domestic market on a tender bid. Maize bought under this tender agreement would have to be paid for by the end of June 1998. Only traders registered in Mexico could bid for the maize and most of the quantity sold were for use in the local *tortilla* industry or for feed grains industries. The price paid to the farmers for the maize was set at 1 315 Pesos (US$145) per tonne in the tender, of which traders had asked for an average subsidy of 350 Pesos (US$39) per tonne.

In July 1998, the **Romania** Government set up a fund worth US$23 million to encourage mills and bakeries to buy local wheat and flour. The fund also allowed bonus payments to mills and bakeries of 200 Lei (US$0.02) per kilogram for wheat and flour.

In February 1998, the Government of **Saudi Arabia** increased the retail price of barley to 26 Riyals per 50-kilogram bag (US$136 per tonne) from 25 Riyals (US$132 per tonne). Previously, in early 1997, the barley retail price has been raised by 39 percent from 18 Riyals per 50-kilogram (US$96 per tonne) to 25 Riyal. Also, the price of a 50-kilogram bag of barley sold to licensed distributors directly from plants was increased to 23 Riyals (US$120 per tonne) from 22 Riyals (US$115 per tonne). The increases were aimed at saving the Government needed cash, by prompting farmers to look for alternative feed sources.

In **Sri Lanka**, the Government, following an earlier plan to subsidize wheat consumption while at the same time reducing fiscal expenditures in 1997, allocated 6 billion Rupees (US$102 million) for the subsidy programme. To achieve the desired reduction in expenditures, the retail price of wheat flour was raised by 2 Rupees to 18.95 Rupees (US$0.32) per kilogram, while that of a loaf of bread was increased by 0.75 Rupees to 8.25 Rupees (US$0.14). Both increases came into force on 10 August 1997.

In July 1997, the Government of **Uzbekistan** raised the price of a 600-gram loaf of bread by 42 percent to 20 Sums (US$0.31). In addition, the Government also ordered increases in the minimum wage, pensions and student grants by 50 percent in order to cushion the impact of the bread price increase on consumers.

1.5 International Trade Policy

Reflecting the relatively depressed world market conditions, some countries provided incentives to exports, while in countries facing food emergencies, import measures were relaxed.

1.5.1 Trade Regulations Affecting Imports and Market Access

In May 1998, the **Algerian** Government announced that importers of cereal products, such as semolina and flour would have to get Government authorization before being allowed to sell them on the local market. The move, which came into effect in July, allowed the authorities to inspect importers' credentials before granting import permits.

In July 1998, the Government of **Argentina** imposed a duty of US$123 per tonne on imports of wheat gluten from the EC. The duty would come into effect in September 1998 for a period of five years.

Faced with a food deficit of up to 2.5 million tonnes in the fiscal year 1997/98 (July-June), after local rice production was cut by bad weather, the Government of **Bangladesh** in February 1998 exempted the import of rice from a *development surcharge* to increase the supply in the market. Previously, a 2.5 percent tax had been imposed on imports of rice.

In January 1998, the Government of **Colombia** authorized paddy imports of up to 200 000 tonnes for delivery in the following months. Colombia has been a rice importer since the mid-1990s, typically purchasing from Venezuela and Ecuador. Under an existing bilateral agreement, Venezuela was given the opportunity to supply approximately half of the authorized amount. Imports from Venezuela can be milled, husked or paddy, but purchases from other countries are limited to paddy rice. The Government controls rice imports through an import licensing system and potential importers must have purchased domestic rice during the past season to participate in the import programme. For those meeting this requirement, the Government allocates import quotas based on their market share in purchasing last year’s domestic crop. This method helps ensure that mills

utilize the domestic crop before turning to imports. The authorized imports must be delivered prior to local harvest, which typically begins in June.

The Government of **Chile,** in May 1998, announced that it would lower its 1999 market year price bands for imports of wheat because of declines in international prices for these commodities. The new floor and ceiling prices for wheat imports in 1999 will be US$198-$224 per tonne against US$213-$251 per tonne in force previously. The band will be in force until 15 December 1999. Chile's price bands for wheat, oils and sugar help to stabilize import price fluctuations. If the import price is lower than the floor of the band, customs duties are imposed on the imports up to the lower limit. Conversely, if the price is above the ceiling band, duties are reduced.

In **Ecuador**, the Government maintains a common external tariff with Andean Pact[4] countries, including a *price band* system on selected agricultural products, including wheat. Under the price band system, an extra duty above the flat rate of 10 percent is charged when the international reference price falls below the floor price, and with reference prices above the ceiling, the importer only pays the flat 10 percent duty. The reference price is based on US fob Gulf prices. The floor price is based on domestic production costs. As the world wheat price fell during 1997, import tariffs under the price band system rose to almost 30 percent. Under pressure from the milling industry, the Government implemented a temporary tariff rate maximum of 19 percent from July through December 1997.

In August 1997, the Government of **Honduras** announced a new schedule of duty rates under its price band mechanism for imports of grains and selected grain products (Table 2). The new schedule became effective on 1 September 1997 and would remain in effect until 31 August 1998. Subsequently, from 1 September 1997 to 31 January 1998, the minimum allowable duty was adjusted to 20 percent for maize and 15 percent for all other products. From 1 February 1998 to 31 August 1998, the duties were allowed to fluctuate inversely with changes in price.

Table 2: Minimum and Maximum Reference Import Prices for Honduras

	New Price Band		Old Price Band		Effective Duty (%)
Commodity	**Min. Price**	**Max. Price**	**Min. Price**	**Max. Price**	**Duty**
Maize	134.80	158.24	131.84	145.32	20.5
Maize Flour	134.80	158.24	131.84	145.32	15.5
Sorghum	130.49	156.55	127.64	144.73	15.5
Milled Rice	381.12	482.81	372.03	451.48	20.5
Brown Rice	304.90	386.25	297.62	361.18	20.5
Paddy Rice	228.67	289.69	223.22	270.89	20.5

In March 1998, the Government of **Kenya** announced that it would waive all taxes and duties on maize imports for three months from 1 April to 30 June to allow emergency supplies and imports by the private sector to make up a production shortfall. The Government had estimated a 630 000 tonne deficit in maize production for 1997/98 because of drought and unusually heavy rains since October 1997.

To protect local farmers, the Government of **Morocco,** in March 1998 increased the customs duties on hard wheat to 50.5 percent from 17.5 percent and for soft wheat to 101 percent from 64 percent.

In **Nigeria**, the rebate on the wheat import duty was increased from 25 percent in 1996/97 to 35 percent in 1997/98, resulting in a reduction in the duty from 10 to 7.3 percent. Also, the custom duty on rice was

[4] The Andean Pact Countries are Bolivia, Colombia, Ecuador and Venezuela.

reduced from 100 to 50 percent in 1997, plus an additional 25 percent duty rebate for imported rice. Furthermore, the ban on barley imports was officially lifted in 1998.

In September 1997, the Government of the **Philippines** announced that it would allow 300 000 tonnes of maize to be imported at a tariff rate of 35 percent, in addition to its existing 155 000 tonnes (35 percent) tariff rate quota. But as the Peso devalued maize imports were not effected, even at the lower tariff (the out-quota tariff is 80 percent). The Government adopted a new measure that would allow the 300 000 tonnes of maize to enter duty free by 1 July 1998 before the local crop came on the market. Under the plan, the National Food Authority (NFA) would, if necessary, increase the imported maize price, or charge a fee to private importers in order to protect producer maize prices.

Furthermore, in June 1998, the Government lowered food wheat import duties from 10 to 3 percent. At the same time, the duties applying to feed quality wheat and coarse grains (except maize) were lowered from 40 and 35 percent, respectively, to 20 percent. The duties on these feed grains are scheduled to fall further, to 10 percent, in the year 2000. The tariff on wheat flour had already been cut earlier this year, from 20 to 10 percent. The duty reductions on feedgrains were aimed at reducing costs to poultry and livestock producers, and ultimately, the price of their products to consumers.

In the **Republic of Korea**, the Government, in a move to ease financial difficulties in the livestock feed industry and to dampen inflationary pressures, eliminated the import tariffs on maize and feed quality wheat from July to December 1998. The existing tariffs on maize and feed quality wheat were 2.6 and 2.5 percent, respectively.

In January 1998, the Government of **Saudi Arabia** adopted an *agricultural calendar* system of import tariffs to coincide with domestic harvests of various crops. A supplementary tariff of 25 percent would apply during the relevant harvesting period. Exceptions are import duties on wheat and flour, which remain unchanged throughout the year, although in February 1998, the Government increased the import duty on wheat and wheat flour from 12 percent to 100 percent, and banned private traders from importing wheat. The Government indicated that a lifting of the ban on private sector imports would not be considered, as long the imported price was less than the support price.

Due to the substantial import requirements in 1997/98, **United Republic of Tanzania** lifted its maize tariff. In conjunction with the tariff change, the Government also banned exports and offered importers storage facilities free of charge.

In July 1997, the Government of **Thailand** authorized the importation of 150 000 tonnes of maize to offset a shortage of domestic supplies. Earlier, during the same year, 200 000 tonnes of maize imports had already been authorized. The imports were duty-free, provided the whole process was completed by 31 August 1997, before the next crop was harvested. In February 1998, the Government announced a 300 000 tonne maize import quota at zero duty from 1 March to 15 July 1988. Also, in 1998, importers were required to inform the Government of the amount that they expected to import. If an importer's allotment were under-used, the quota would be reduced the following year by a like amount. In the case of wheat, which has an import duty of 1.00 Baht per kilogram (US$25 per tonne) since early 1998, the Government granted an import tax rebate to mills exporting wheat by-products (e.g. bran pellets) during the period 1 March to 31 August 1998. The rebate was set at 431 Baht (US$11) per tonne. The tariff on wheat flour is currently 3.13 Baht per kilogram (US$75 per tonne).

In August 1997, the Government of **Turkey** raised the import duty on wheat from 35 to 45 percent for milling wheat and from 30 to 40 percent for durum. The increase was designed to encourage traders and food manufacturers to make greater use of domestic supplies. The official Government agency TMO intended to purchase up to 2.5 million tonnes of wheat from producers in 1997/98 compared with 650 000 tonnes in the

previous year. By contrast, in May 1998, the Government reduced the import duty on maize in an effort to satisfy domestic demand. The new rate was set at 20 percent, compared to 35 percent previously.

With a view to enhancing bilateral trade in the grain sector under the North American Free Trade Agreement (NAFTA), **Canada** announced in August 1997 the suspension of tariff rate quotas (TRQ) on imports of barley and barley products from the United States. Previously, a lower tariff applied to imports of up to 271 000 tonnes annually of US barley. The Canadian Government retains the right to re-impose the TRQ. Box 3 presents an update of recent changes under the NAFTA agreement between Canada, Mexico and the US.

Box 3: Updates on the Status of the North American Free Trade Agreement

For non-durum wheat from Mexico, the U.S. tariff of 77 cents per kilogram was eliminated on January 1, 1998. In addition, the 77 cents per kilogram imposed by the US on durum wheat imports from Mexico will be phased out over 10 years. There is no duty levied by the US on maize imports from Mexico. The US tariffs on rice imports from Mexico are on a 10-year phase-out period and Mexico's tariffs of 10 percent for US rough rice and 20 percent for US refined rice are also being phased out over a 10-year period. For 1998, the Mexican tariffs are 4 percent for rough and broken rice and 10 percent for brown and milled rice.

Under NAFTA, Mexico converted its import-licensing regime for wheat imported from the United States and Canada to tariff-only treatment. U.S. wheat exports to Mexico were initially subject to a 15-percent tariff, which is being reduced to zero in equal installments over a 10-year transition period. The 1998 Mexican tariff on wheat is 7.5 percent. Canada eliminated its import-licensing requirement for wheat imported from Mexico. Canadian import licensing requirements on imports from the United States were eliminated as part of the earlier US-Canada Free Trade Agreement.

As part of the NAFTA, Mexico converted its import-licensing regime to a transitional tariff-rate quota (TRQ) for maize imports from the United States and Canada. The TRQ will be in effect for 15 years. The quota, initially 2.5 million tonnes, grows at a 3-percent per annum over the 15-year transition period. The quota for 1998 was set at 2.8 million tonnes. US exports to Mexico in excess of the quota are assessed a tariff initially equal to US$206 per tonne, but not less than 215 percent of the value of the excess amount. For 1998, the over-quota tariff is US$165 per tonne, but not less than 172 percent.

When the NAFTA came into effect, Mexico converted its import-licensing regime for barley and malt imported from the United States and Canada to a transitional tariff-rate quota to be in effect for 10 years. The initial quota of 120 000 tonnes grows at 5 percent annually over the 10-year transition period. The1998 quota for barley and malt is 145 861 tonnes. US barley and malt exports to Mexico in excess of the quota are assessed a tariff initially equal to US$155 per tonne, but not less than 128 percent the excess quota value for barley, and US$212 per metric tonne, but not less than 175 percent the excess value for malt. For 1998, the over-quota tariff for barley is US$124 per tonne, but not less than 102.4 percent, and for malt, US$170 per tonne, but not less than 140 percent the over quota value.

Source: NAFTA Fact Sheet, USDA/FAS.

In July 1997, the **EC** extended for a further six months its association agreements with six Central and Eastern European (CEE) countries (Bulgaria, Czech Republic, Hungary, Poland, Romania and Slovakia). This agreement was extended for successive periods of six months pending negotiation and implementation of new agreements and sets tariff quotas for specified agricultural products from the six CEE countries into the EC. The tariff quotas for cereals and products for July-December 1997 were set at 169 068 tonnes, which benefits from an 80-percent reduction in import duties. Of this total, a quota amount of 4 500 tonnes of millet imports, specifically from Hungary, carries a fixed import levy of 65 Ecus (US$76) per tonne.

As part of an agreement with the EC, in force since January 1996, Turkey grants duty-free entry for specified annual volumes of EC grain before the end of each May. The quantities for 1998 comprise 200 000 tonnes of milling wheat, 100 000 tonnes of durum, 46 000 tonnes of malting barley, 20 000 tons of rye and 52 000 tons of maize.

The EC offered tariff quotas of 50 000 tonnes a year for 1997 and 1998 for malting barley. Imports of barley will benefit from a 50 percent reduction in the relevant duty.

In early 1998, the **Polish** Government reinstated tariffs for maize after they had been set at zero level throughout 1997. With effect from January 1998, maize imported from Hungary carried a duty of 20 percent. For maize imported from the Czech Republic and Slovakia, the effective date (also a 20 percent tariff) was 1 February 1998. Furthermore, on 6 June 1998, the Government introduced minimum prices for imports of agricultural products, including grains. Respective minima for major grains were as follows (per tonne): wheat 568.79 Zloty (US$162.51), barley 426.60 Zloty (US$121.89) and rye 488.09 Zloty (US$139.45). These prices would remain in force until the end of the year, and are designed to strengthen prices on the domestic market.

In June 1998, the **Romanian** Government announced an increase in duties to 25 percent on wheat flour of EC origin and a decrease to 15 percent for that from CEE countries. Tariff levels had previously been set at 15 and 25 percent respectively. The duty increases would be in force until the end of 1998. In addition, in early July, a further increase in duties to 60 percent was announced, this time covering all types of wheat and flour and will remain in effect until the end of June 1999.

With effect from April 1998, the Government of **South Africa** raised the specific duty on wheat by 50 Rand (US$5) to 105 Rand (US$18) per tonne and that on wheat flour from 50 percent ad valorem plus 50 Rand per tonne to 50 percent ad valorem and 105 Rand per tonne. The tariff increases on wheat and flour is a temporary measure to enable the sector to adjust to recent deregulation. It uses the Argentine Trigo Pan as a reference price, whose decline led to the increase in the tariffs on wheat and flour.

Also, according to an existing formula, an import tariff of US$5 per tonne on maize is activated when the export price (fob) at the US Gulf falls below US$110 per tonne, on a twenty-one day moving average over a period of three weeks. The import price was fixed in Rand on the day that the tariff was implemented. If the international (fob Gulf) price falls below US$100, using the formula, the tariff increases to US$15, but it is removed if the price exceeds US$110. The system was formulated to take account of variations in international prices.

The **Ukrainian** Government, in July 1997, passed a law to regulate imports of agricultural products. The law introduced seasonal import duties on agricultural products at the full import duty rate for a term of no less than 60 days and no more than 120 days. Under this new law, the duty on grains was set at the rate of 10 percent, but no less than US$48 per tonne. A year later in July 1998, the Government announced that import duties on some agricultural products would be doubled during the period from 1 September to 1 December 1998. However, duties for wheat, rye, oats and maize would rise to 60 percent.

In June 1998, the **United States** introduced a quota on imports of wheat gluten for a period of three years. In the first year, the global quota will be 57 272 tonnes. The quota is set at 28 315 tonnes for Australia, 24 513 tonnes for the EC and 4 693 tonnes for other suppliers. The initial quota is equal to the average US imports from all sources during 1993-95, but will be raised by 6 percent each year before expiring on 1 June 2001.

1.5.2 Trade Measures Influencing Exports

Bulgaria waived its 10 percent tax on wheat exports from 1 January 1998.

In April 1998, **China** announced a range of aid agreements with Indonesia, including export credits of US$200 million, to promote trade. This is part of a US$4 billion commitment by China to help countries affected by the Asian financial crisis. China also proposed barter trade with Indonesia on essential commodities as part of its aid offer.

In February 1998, the Government of **Hungary** announced that it would subsidize the export of 500 000 tonnes of feed quality wheat. According to the plan, wheat exporters would receive a 1 500 Forints (US$7) per tonne subsidy for feed quality wheat bought from producers at 15 000 Forints (US$68) per tonne. Export licenses for the subsidized wheat were valid from 12 March through 30 June, with exporters paying a deposit of 500 Forints (US$2.25) per tonne on the licensed amount, to be reimbursed when at least 80 percent of the wheat had been exported. On 26 June 1998, the Government further announced that export licenses for up to 1 million tonnes of wheat would be available in July. Also in July, in addition to the 500 Forints deposit, exporters were required to purchase domestic wheat at prices not less than 18 000 Forints (US$84.50) for B1 and B2 quality and 16 000 Forints (US$75.11) for Euro quality. The first two grades were eligible for an export subsidy of 2 000 Forints (US$9.39) per tonne, while the rate for the latter was set at 1 500 Forints (US$7.04) per tonne. These levels would be re-calculated monthly in relation to price trends on the domestic and international markets. The Government decided to help wheat and maize exports by suspending the export-licensing procedures from 1 August.

In an effort to ensure domestic supplies, **Indonesia** in July 1998 imposed a ban on the export of unhusked and milled rice, wheat flour and wheat.

In 1997, **Romania** produced a record harvest of 12 million tonnes of maize but producers were unwilling to sell the grain at the going market price. In order to encourage sales, the Government agreed to grant an export subsidy of 150 000 Lei (US$19) per tonne for 1 million tonnes. The Government rejected a request from producers for a similar programme for wheat.

In September 1997, the **United States'** announced spending limits for agricultural export programmes for the 1998 fiscal year (October 1997/September 1998). The Export Enhancement Programme was allocated US$150 million, while the PL480 food assistance programme received US$889 million. A sum of US$5.7 billion was agreed for USDA's export credit programmes, while the Market Access Programme received US$90 million.

In addition, under the Commodity Credit Corporation's (CCC) Facility Guarantee Programme (FGP), credit guarantees for export sales of US capital goods and services could be granted to improve existing agriculture-related facilities in emerging markets. In December 1997, the USDA announced authorization of US$150 million in credit guarantees to three regions, as follows: Caribbean (Jamaica, Trinidad and Tobago): US$20 million; Central America (Costa Rica, El Salvador, Guatemala, Panama): US$30 million; Mexico: US$50 million; Peru: US$10 million; Southeast Asia (Indonesia, Malaysia, Philippines, Thailand): US$40 million. The FGP will assist improvement in such matters as storage capacity and grain-handling facilities primarily used for imports from the United States.

1.6 Other Agricultural Policy Initiatives

In late 1997, the World Bank granted the Government of **Argentina** a loan of US$75 million to provide assistance to small and medium-sized agricultural businesses. The total amount, which was supplemented by US$25 million from Government funds, will be used to improve the financial viability of about 40 000 small farms. Part of the money will also be used for rural infrastructure projects.

In addition, in May 1998, the Government reduced the value-added taxes levied on the agriculture sector by 50 percent. The reduction applies products and services linked to the sowing and harvesting of crops, including the use of agrochemicals and fertilizers.

The Government of **Brazil**, in July 1998, made available the first installment of US$500 million from an allocated total credit of US$10 billion for 1998/99, to producers through the central bank to help improve agricultural infrastructure. An amount of US$5.5 billion will be loaned by commercial banks to producers at rates of interest subsidized by the Government. The Government will loan the remaining US$4.5 billion to producers at interest rates set between 5.75 and 8.75 percent.

In late 1997, the central Government of **China** granted a loan of 950 Yuan million (US$114 million) at discounted interest rates to the north-eastern region of the country where most grain is grown, to help improve its storage capacity by about 1.5 million tonnes. Furthermore, China and Japan agreed to jointly finance a project (with each country providing about US$46 million) aimed at expanding grain production on some 900 000 hectares of land in northeast and Inner Mongolia, where the predominant crop is maize.

Furthermore, in July 1998, the Government introduced a number of measures to control the amount of farmland being switched to other uses. Rigorous procedures of prior official approval must now be followed before land can be developed for industrial or recreational purposes, and such changes were banned for twelve months. The Government had previously indicated that the area sown to grain should be stabilized at 110 million hectares. However, up to 300 000 hectares of land may have to be reclaimed each year in order to offset land area used for other purposes.

In **Indonesia**, an important factor contributing to the high cost of poultry feed and limited maize imports was an earlier regulation limiting the scale of operations of poultry feed manufacturers, with the exception of those producing poultry feed in pellet form, to small-scale enterprises with capital investment below 30 million Rupiah (US$705 000). This policy inhibited the development of economies of scale in the poultry feed industry. In late 1997, the Government lifted this restriction, opening the way for increased investment in the feed sector.

To boost its agricultural sector, the Government of **Pakistan** announced plans to provide 40 billion Rupees (US$903 million) in credit to farmers in 1998/99 compared to 30 billion Rupees (US$677 million) in 1997/98.

In **Saudi Arabia**, by January 1998, the amount outstanding owed by the Government to farmers and contractors for grain was estimated at 12.5-15.5 billion Riyals (US$3.3-4.1billion). During July and August 1998, the Government allocated 5.3 billion Riyals (US$1.4 billion) to cover contracts for grain from the 1996 and 1997 harvests.

In early 1998, the Government of **Thailand** approved a plan for Thailand's agricultural development. About 146 billion Baht (US$3.65 billion) has been earmarked for agricultural projects. Box 4 presents the key objectives of the plan.

Starting in the April 1998, the Government of **Japan** adopted measures to revitalize the country's paddy fields. Under the plan, the Government will help prefectures create funds for the conservation of water and soil in terraced-paddy field regions. Of the funds' total, which amounts to 24 billion Yen (US$192 million), the Government provided about one-third and the remainder was to come from local governments. Operating income from the funds would be used for the protection of terraced paddy fields as well as to cover costs of local government sponsored programmes enabling urban citizens to participate in hands-on farm work.

Box 4: Key Objectives of Thailand's Agricultural Development Plan

- The establishment of integrated agricultural zones for exports so that farmers would be close to processing, packaging, marketing and export services. Cost savings will be made through eliminating middlemen and long-distance transport.
- Research and development to raise production and cut costs by using new technology, including biotechnology.
- Raising product quality and processing. The Agriculture Ministry will establish a centre to control quality from the raw material stage to the finished product.
- Restructuring the Agriculture Ministry to modernize its management and services. Its departments will cover four areas: research and development, management of natural resources, personnel development, and other forms of support.
- Encouraging farmers to use less chemical fertilizer while promoting natural alternatives and organic production. This would protect the environment and reduce imports of fertilizer and chemical products.
- Improving management of land use and ownership, natural resources, irrigation and coastal areas. The ministry hopes to give land ownership rights to 700 000 farmers by 2002.

The Government of **Romania**, in August 1997 allocated credit and *soft* loans amounting to US$90 million for purchasing and storage of the 1997 harvest. Of the amount allotted, US$69 million were made available as a revolving credit to grain traders and milling companies. The balance is to cover on-farm storage costs for a period of eight months, to enable producers to maintain the quality of their grain and encourage its timely marketing. The grain market was recently liberalized, which resulted in the elimination of fixed support prices, the removal of retail price controls on bread and the termination of the State monopoly on the purchase and storage of grain.

In July 1997, the **Russian Federation**'s Agroprom Bank lowered its special lending rate for agriculture from 14 percent to 10 percent. The bank planned to allocate 1 500 million Rubles (US$24 million) to farmers at a lower interest rate by August of that year. The bank, a Government agency for the servicing of a special soft credit fund for agriculture, lent 1 600 million Rubles (US$26 million) for the 1998 spring sowing, of which 1 000 million Rubles (US$16 million) went directly to farms.

In April 1998, the Government provided 1 300 million Rubles (US$21.4 million) from the budget to the agricultural soft loan fund as well as funds from the sale of regional farm bonds issued to repay credit granted in 1996. Three months later, the Government announced that the second series of soft credits from its special fund for farmers should be released to farmers.

Furthermore, the Ministry of Agriculture and Food unveiled a plan of action to help farmers with insufficient fuel, availability of lubricants and machinery, to bring the 1997/98 harvest in on time and to increase the volume of grain harvested. Due to the shortages, only up to three-quarters of the available machinery could be used, and combine harvesters had to cope with 311 hectares on average, and in some regions as much as 500 hectares compared with the standard 130-150 hectares. Under the plan, the Government provided 3 500 million Rubles (US$576 million), of which 85 percent went to factories to enable them to continue to assemble new harvesters. In addition, the Ministry, in conjunction with oil companies, developed a system to supply fuel to farms, with total requirements of 4.7 million tonnes of diesel and 2.2 million tonnes of gasoline.

2. CEREAL STATE TRADING ENTERPRISES

2.1 Introduction

This chapter examines the role of State Trading Enterprises (STEs) in agriculture, especially for those in the cereals sector. Since the early 1980s, the extent of state regulation of economic activity has been reduced substantially in developed and developing countries as well as in the transitional economies. Yet State Trading Enterprises are still common, and their presence is most pronounced in agriculture[5], as Table 3 demonstrates. The WTO has noted that, based on the evidence of the notifications: "agriculture is by far the most important category of state trading in the developed and developing countries alike", and "stems from the belief that state trading is an appropriate means by which governments can meet agriculture-related policy objectives"[6] The same document notes that this emphasis on state trading in developing countries has its origin in their concern with food security objectives.

Table 3: STEs Notified to the WTO[7]

Category	No.	Percent
Agriculture	101	62.7
Petrochemicals	13	8.1
Alcohol	11	6.8
Minerals	10	6.2
Tobacco	10	6.2
Utilities	9	5.6
Drugs	3	1.9
Other	4	2.5

At present, 53 countries have notified a total of 159 STEs. As is apparent from Table 4, cereals STEs dominate in terms of numbers. The fact that many developing country members have still to report to the WTO Working Party on State Trading Enterprises is unlikely to change the preponderance of cereal-based agencies in the total. At present they constitute 21 percent of the number of all STEs.

Table 4: Distribution of Agricultural STEs

Category	No.	Percent
Cereals	33	25.8
Fruits	12	9.4
Dairy	11	8.6
Sugar	9	7.0
Meat & Livestock	9	7.0
Potatoes	7	5.5
Textiles	7	5.5
Oils & Oilseeds	7	5.5
Beverages	6	4.7
Other	27	21.0

Source: United States Dairy Trade Coalition
Note: * The 'other category includes fish and a list of tree and vegetable crops.

[5] For information regarding the membership of the WTO, and the proportions which have reported on state trading activities, see Box 1, annexed to this Section.
[6] WTO, 1995, p. 2.
[7] Source: United States Dairy Coalition. The numbers in the table totals 161: this is because two STEs reported activities covering two of the categories defined.

While STEs remain important agents in the cereal markets of developing countries despite the privatization trends of recent years, the biggest STEs are located in developed countries.

2.2 Definitions and Categories of State Trading Enterprises

When considering the definition of a State Trading Enterprises, it is appropriate to take as a starting point the WTO definition as set out in the Uruguay Round Agreement in the Understanding on the Interpretation of Article XVII of the General Agreement on Tariffs and Trade, 1994. This uses the following as a working definition: "Governments and non-governmental enterprises, including marketing boards, which have been granted exclusive or special rights or privileges, including statutory or constitutional powers, in the exercise of which they influence through their purchases or sales the level or direction of imports or exports."[8].

As a working interpretation, the WTO definition is quite broad, since it potentially encompasses almost all categories of STE. This definition is used to inform member governments of the WTO in meeting their obligations to submit notifications of all state trading activity. These notifications take the form of a questionnaire response, and the latter and counter notifications are monitored and reviewed by a Working Party set up under the Council for Trade in Goods, in 1995, specifically for this purpose.

There are a number of key elements regarding this definition.

1. The issues of ownership and of control raised the question as to whether STEs are confined to those enterprises, which are government owned, or is it sufficient that they are controlled by government? If the latter, to what extent? Clearly the above definition includes a wide spectrum of possibilities, from enterprises which are directly owned and administered by an arm of government to those privately owned but operating under contract with government through which they are granted trading privileges.

2. There is also the question as to whether a State Trading Enterprise influence largely international trade or whether it is an institution engaged primarily in intervening in domestic trade included? Many STEs will undertake actions, which affect both international and domestic trade, but others, which might be so described, will be solely concerned with one or the other. As with the issue of ownership and control, there is a spectrum of activities or enterprises ranging, in this case, from those purely concerned with regulating international trade at one end to those engaged in regulating domestic markets. One result of the Agreement on Agriculture, however, is the widespread recognition that domestic market intervention will affect, at least potentially in the great majority of cases, the international trade regime. Again the WTO definition points towards a broad interpretation of what constitutes an STE.

The WTO has also provided a functional classification of STEs, describing them as falling into the following main categories: (i) a range of marketing boards, including statutory, export and regulatory; (ii) fiscal (financial) monopolies; (iii) canalising agencies; and (iv) foreign trade enterprises[9]. The terminology used by governments to describe STEs varies, as does the degree to which each of these categories is involved in domestic or international agricultural trade.

The majority of STEs involved with agricultural commodities fall in to the first category, with a substantial proportion of these being statutory marketing boards. These are frequently endowed with some responsibility for domestic marketing as well as, in some cases, the foreign trade in the commodity concerned. They are relatively comprehensive in their activities compared to export marketing boards (concerned only with the exports) and with regulatory boards, which do not directly engage in trading operations but contract out these activities to private operators.

[8] WTO, 1994, p. 250.

[9] WTO, 1995, p. 4. There are other types of STE included in the WTO list, but these are not generally involved with agricultural commodities.

Fiscal monopolies are largely concerned with the control of the production, marketing and distribution of commodities for which there are health regulations or implications. Examples of food and agricultural commodities include alcoholic beverages or tobacco. Canalising agencies are invested by governments with monopoly rights for the import or export of a specific product, frequently an agricultural product, with the objective of stabilising domestic prices or domestic supplies. They also regulate trade in the specific commodity on the basis of the availability of foreign exchange. Foreign trade enterprises were more common in current and former centrally planned countries, and consequently are much fewer in number now than in the past. Monopolistic enterprises like statutory marketing boards, vary greatly in the range of activities for which they exercise control, and in their degree of autonomy from government.

Within the classification above, state trading agencies undertake a wide range of activities. A list of such activities has been compiled by the WTO[10] based on notifications to the organisation (see Box 5). The activities have been categorised according to whether they are concerned with foreign or domestic trade, and are normally conducted for a specific commodity or group of related commodities. The range of STE activities is broad, and many STEs covers both foreign and domestic trade.

Box 5: Range of STE Activities Based on Notifications to the WTO

Activities pertaining to foreign trade	Activities pertaining to domestic trade
♦ Direct handling of imports and/or exports, or the issue of permits for private traders to carry out foreign trade. ♦ Negotiates and/or administers long-term bilateral contracts for exports and/or imports. ♦ Engages in marketing and promotional activities for exports. ♦ Undertakes activities necessary to fulfil contractual obligations entered into by the government.	♦ Enforces the statutory requirements of an agricultural marketing scheme and/or stabilisation arrangement. ♦ Authorizes or manages domestic production and/or the processing of domestic production. ♦ Handles domestic distribution of domestic production and/or imports; engages in marketing and promotional activities for domestic consumption. ♦ Effect purchases and sales of domestic production based on pre-determined floor or ceiling prices; determines the purchase price and/or sales of domestic production. ♦ Issues credit guarantees for producers and/or processors. ♦ Maintains emergency stocks of certain strategic and/or agricultural goods.

2.3 Historical Coverage of STEs in the GATT

Interest in the activities of state trading enterprises and their implications for the conduct of international trade is not new to international trade fora, although there are particular reasons why interest is becoming more sharply focused on this issue[11] and Article XVII of the GATT is the starting point for international law on the subject.

Article XVII recognizes STEs as 'legitimate participants' in international trade but, at the same time, describes what is acceptable conduct for such entities. Such conduct implies that STEs:

[10] WTO, 1995, p. 21-22.
[11] See Section 2.4.

- do not discriminate between trading partners in accordance with the GATT directive on non-discrimination;
- act according to commercial criteria
- should not afford protection over and above that provided by bound tariffs.

There has been debate over the interpretation of these paragraphs over the years, as well as with respect to the difficult issue of the verification of the conduct of state agencies involved in international trade. Article XVII was incorporated into the GATT Agreement of 1994 following the Uruguay Round of Multilateral Negotiations, and an Understanding on its interpretation included as Annex 1a[12]. The latter established the working definition of STEs (see section 2.2) and set up notification procedures designed to ensure transparency in their operation. In addition, there are further references to state trading in the Agreement on Agriculture:

- "the definition of non-tariff barriers subject to conversion to tariff equivalents includes non-tariff measures maintained through STEs;
- export subsidy disciplines are applicable to governments and their 'agencies';
- when providing information to the Committee on Agriculture regarding implementation, WTO members are asked to explain the administration of market access and export subsidy commitments, including details about STEs and their relevant activities"[13].

2.4 Changes in the Activities of STEs Pre- and Post-Uruguay Round

In the past two decades the role of STEs particularly in Latin America, but to a lesser extent in Africa, has substantially diminished. In contrast, in much of Asia the extent to which privatisation and liberalisation have been pursued over the last decade has varied substantially. Generally the picture gained is one of caution and a reluctance to relinquish a substantive involvement in domestic and international cereal markets. This is not to say that there has not been some reduction in the extent of state trading, but generally what changes have occurred appear to be a moves towards a greater degree of openness and a relinquishing of monopoly powers, rather than an abandonment of the principle of state involvement in cereal markets.

In Africa, since the 1980's, the policy environment has been dominated by the structural adjustment framework, under which substantive reform of domestic economic policy including the liberalisation of domestic and international marketing of agricultural products took place. Even if not fully implemented always, their impact has generally been to reduce substantially the extent of market intervention and regulation. In Latin America economic reforms have generally occurred earlier, and have been more far-reaching. They have been driven more by a perceived desire for greater openness in multilateral trade, than by domestic economic imperatives.

2.4.1 Cereal STEs in Asia

In those cases where the same STEs are operative in both domestic and foreign markets, they do not have monopoly powers in the domestic market, being primarily responsible for maintaining a floor price. While there have been attempts to make STEs more financially accountable, and to open up foreign trading to the private sector, there is little evidence of the 'rolling back of the state' which has occurred in other regions of the developing world.

[12] Multilateral Agreements on Trade in Goods. See WTO, 1994.
[13] Dixit and Josling, undated, p. 5.

The following table summarizes the activities of cereal STEs in Asia for the periods prior to and since the Uruguay Round. Of course, even when there is any change indicated in these activities following the Agreement on Agriculture, that change is not necessarily caused by the Agreement.

Table 5: Operational Activities: Asia

Criterion	Pre-WTO Agreement	Post WTO Agreement
Vertical Integration	For imported commodities STE activity is common in both foreign and domestic markets.	Little change.
Horizontal Integration	Cross-commodity responsibilities are less common than in some regions, upstream linkages rare.	No change.
Monopoly Control	Generally not an issue for domestic marketing, but common for foreign trade.	Some trend towards greater competition in the export sector.
Direct Handling	Common in domestic and import markets, exports often handled under license.	No change.
Commercial/Social Criteria	Social rather than commercial objectives.	No change, but subject to increasing financial scrutiny.

The reasons for the maintenance of state trading organisations in **India** make substantive reference to the possibilities for realising economies of scale in trading operations, as well as ensuring food supplies[14]. The Food Corporation of India has a substantial jurisdiction with respect to most cereals (excluding feed grade maize) to stabilize domestic prices and control foreign trade. It is not a monopoly purchaser in the domestic market, but has monopoly control over cereal imports based on its food security concerns. Private operators may operate in foreign markets subject to license

In the justification for maintaining an STE in its notification to the WTO, the **Indonesian** Government mentions the thinness of the international rice market and the need to maintain domestic stability in the context of international market instability. "The main objective of the Government of the Republic of Indonesia in granting exclusive rights to the Badan Urusan Logistik (Bulog) is to ensure food security.....to minimize excessive food price fluctuations, particularly for staple foods, so as to provide certainty with regard to future prices.....operations are also aimed at protecting consumers through stable food prices.....and to ensure food availability throughout the country." Apart from introducing greater flexibility into Bulog's trading parameters, there have been considerable changes in its role and modus operandi following the recent Asian economic crisis[15].

The National Paddy and Rice Board in **Malaysia** held a monopolistic position in the past with respect to both the domestic rice market and foreign trade. Since the early 1990s, the situation has been changing rapidly: the agency was dissolved in 1994 and its regulatory functions transferred to the Ministry of Agriculture[16]. Much of its intervention activities were subsumed by a newly constituted STE, Bernas, which itself is due for privatisation. At present, however, the agency has monopoly control of imports, and purchases up to 45 percent of domestically produced paddy. Imported rice is sold on to wholesalers. Procurement of imports is through short-term contracts following the receipt of tenders. Although increasingly required to operate according to commercial criteria, part of Bernas' responsibilities include management of the rice reserve and disbursement of domestic producer subsidies. It has its own mills, but competes in the domestic market with other millers.

[14] WTO Notification, India, 1996.
[15] Various sections of Chapter I of this review.
[16] WTO Notification, Malaysia, 1995.

In the **Philippines** the National Food Authority (NFA) has responsibility to " look after the food security requirements of the country through a grain (rice and maize) buffer stock"[17]. This involves purchasing on the domestic market to the extent necessary to stabilize prices, and to carry out imports and exports according to domestic requirements. Private traders may export or import maize subject to regulation and in the context of a domestic surplus or shortfall. The NFA has a monopoly over foreign trade in rice, the main staple. There is no apparent involvement in upstream commodities.

In the **Republic of Korea**, the control of the rice market is vested in the Ministry of Agriculture and Forestry and Fisheries (MAFF). The agency has monopoly control over rice imports and purchases approximately 30 percent of the domestic crop, which it sells on at subsidized prices. Domestic prices are determined by MAFF, which also determines the quantity of imports according to domestic consumption requirements, and fulfils the country's import tariff quota. With respect to barley, both foreign trade and the domestic market are more open, with private traders allowed to import part of the quota. Trade is conducted on short-term contracts only to ensure equal opportunities for all exporters, and has been substantially influenced by the WTO Agreement, before which trade in cereals was discouraged. Only in 1995 were rice imports permitted under the country's minimum access commitments[18].

2.4.2 Cereal STEs in Africa

In east and southern regions of Africa there has been a marked trend towards a diminution of the role of STEs with respect to domestic trading activities. "In Africa, 15 out of 28 countries classified by the World Bank as undertaking adjustment had imposed significant restrictions on participation in staple food marketing in the early 1980s, and in a further five there was market intervention by government buying agencies. By 1994, all these countries had lifted the main restrictions on market participation, and the share of production purchased by state agencies had fallen, and in all but a few cases become insignificant."[19]

Typical changes in STE activities have involved the removal of monopoly purchase powers to be replaced by the role of 'buyer of the last resort' This has been accompanied by removal of restrictions on private sector trading, not always with unqualified success. Too often the retrenchment of state trading has not been met with the expected private sector response, consequently the importance of a (albeit more limited) state role is increasingly being recognized[20]. One area where the WTO Agreement may have had some influence is with respect to foreign trade restrictions. While STEs remain important agents of government in the overseas cereal trade, there has been a gradual replacement of quantitative trade barriers by tariffs. This process preceded the Marrakech Agreement, however, and its impetus came primarily from economic reform programmes.

Elsewhere in the African region the process of change has generally been slower and, from the limited evidence available, it appears that state trading organisations still have a substantive and often monopolistic role in the cereal trade, and that the motivation for maintaining the status quo in this respect stems from developmental and social objectives such as producer incomes and urban food security.

[17] WTO Notification, Philippines, 1995, p.1.
[18] WTO Notification, Korea, 1995, and USDA, 1997b.
[19] Jones, 1995, p551.
[20] See for example, World Bank, 1997.

Table 6: Operational Activities: Africa

Criterion	Pre-WTO Agreement	Post-WTO Agreement
Vertical Integration	Common for same STE to manage/regulate domestic and foreign trade in cereals.	Some trend towards reduction of domestic role.
Horizontal Integration	Cross-commodity and upstream links common.	Frequency of upstream responsibilities much reduced.
Monopoly Control	Frequently substantial for both domestic and foreign trade, although many administrative problems.	Increasing competition in domestic trade, where some privatisation of functions.
Direct Handling	A characteristic feature, and usually associated with price determination role.	Remains a common feature, particularly linked to strategic reserves.
Commercial/Social Criteria	Major importance of social objectives.	Increase in recognition of commercial criteria, but social objectives remain paramount in many cases.

The Agricultural Marketing Corporation (AMC) of **Ethiopia** represented a state trading entity with widespread monopolistic powers. Its operations included sole rights regarding: the domestic purchase and sale of a range of agricultural products including cereals; the export, import and distribution of agricultural products; the purchase and sale of agricultural inputs; and the maintenance of a strategic grain reserve. Its main functions were to stabilize domestic prices and subsidize urban consumers[21]. Since 1991 the AMC has been replaced by the Ethiopian Grain Trade Enterprise (EGTE) whose main functions were to stabilize cereal prices at both producer and retail levels through the maintenance of buffer stocks and through regulation of international trade in cereals. Its involvement in domestic procurement has gradually diminished.

STEs still play an important role in both the domestic and foreign trade in cereals in Ethiopia, although the scope for market manipulation has greatly diminished. The EGTE maintains a domestic marketing and price stabilisation role, although in competition with the private sector. It also continues to maintain the strategic grain reserve and provide a channel for the newly re-emerging cereal export surplus. In terms of transparency, there has been a substantial shift to greater openness.

The rolling back of state activity has proceeded intermittently since the early 1980s in **Tanzania**. Successive government policy initiatives have resulted in a system which has moved "away from government administered monopsonistic marketing channel and pricing regimes towards a competitive multi-channel marketing system with prices largely determined by market forces"[22].

The main STE involved with cereals in Tanzania, the National Milling Corporation, (NMC), was structured in 1973 with monopoly powers to buy and sell grain. It worked predominantly within a two-tier marketing structure using a network of local administrative or co-operative agents, which changed with periodic attempts at restructuring. The NMC was also responsible for the import and export of cereals and management of the strategic grain reserve (SGR). Reforms have gathered pace since the late 1980s: activities of the NMC are now confined to grain milling, although it no longer has a monopoly in this respect. The agency is scheduled for privatisation. Responsibility for the SGR has been transferred to the Food Security Unit within the Ministry of Agriculture. The latter has no mandate to intervene to stabilize prices, although it does purchase from more disadvantaged regions where private-sector traders are less active. Imports and exports are handled by private sector traders.

[21] Information regarding Ethiopia is taken from Wolday Amha, 1997.
[22] Temu and Ashimogo, 1997, p. 9.

Changes in the functioning of agricultural STEs are also underway in **Namibia**[23]. The Namibian Agronomic Board (NAM) controls the marketing boards for maize and wheat which were established to promote domestic production, food security and employment. While these were given powers to purchase the whole crop, these powers have not been used and domestic procurement is solely concerned with maintenance of a floor price. The perception is that the role of the boards will gradually orientate to one of facilitation rather than direct intervention. The NAM issues permits to importers and exporters, although import requirements are met on a free-market basis.

Liberalisation has also been very pronounced in **Zambia**. The process of change has mirrored that in Tanzania, even if events have unfolded more rapidly. The main parastatal controlling domestic and foreign cereal trading, ZAMBOARD, was abolished along with its trading monopoly in 1989, and domestic marketing placed in the hands of regional co-operative unions. Responsibility for the food security reserve was vested in a Food Reserve Agency (FRA), with powers to buy and sell stocks on the basis of open trading: i.e. any agency may sell or buy from the FRA under prevailing market conditions. Both domestic and foreign trade has been privatised, with traders having to register with the government, and domestic maize traders registering with the FRA[24].

Elsewhere in Africa the pace of change has often been slower. In **Malawi**, the state board previously had monopoly control over all trading activities associated with both maize and fertilisers. In a difficult period of transition over the last decade, the responsibilities of the parastatal have been substantially reduced to 'buyer of the last resort' with respect to maize, a role expected to diminish as private sector marketing increases. It also maintains an important regulatory role in foreign trade. In **Kenya**, the National Cereals and Produce Board (NCPB) has undergone a stop-go pathway of change, with its marketing monopoly enhanced and retrenched intermittently. It has finally seen its position substantially reduced and private sector marketing has grown accordingly[25].

Outside of southern and eastern regions of the continent the role of STEs remains significant. A possible exception is in West Africa, where the Government of **Ghana** eliminated import licensing in 1989, and abolished state agency monopolies, although parastatals continue to dominate cereal imports, albeit on a commercial basis[26]. Elsewhere, STEs are substantially involved in managing and controlling trade in cereals. In **Mauritius**, the State Trading Corporation has sole responsibility for managing the import of rice, the basic staple[27]. Similarly, in **Tunisia,** the Grain Board has a monopoly over the import of the two major cereals for that country: wheat and barley[28]. In addition, it purchases wheat on local markets at prices fixed by the government and sells at subsidised prices to consumers. Private traders may, under certain circumstances, import cereals on behalf of the Grain Board, in which case, import prices are determined through commercial negotiation. The resale value of imported cereals is the same as for local production.

2.4.3 Cereal STEs in Latin America

The process of trade liberalisation is further advanced in Latin America than in other developing regions of the world. This process precedes the WTO Agreement on Agriculture, although it may well have been accentuated by the multilateral negotiations. A more profound influence has been the various regional trade arrangements, particularly MERCOSUR and the Andean Pact, as well as NAFTA. At the same time, the main instrument in promoting more open trading arrangements has been a profound shift in government economic policy throughout much of the Region, involving a smaller role for direct state intervention.

[23] WTO Notification, Namibia, 1997.
[24] FAO, 1997.
[25] Lewa and Hubbard, 1996.
[26] Valdés and McCalla, 1996.
[27] WTO Notification, Mauritius, 1995.
[28] WTO Notification, Tunisia, 1997.

There has been a significant change over the last decade with respect to all the transparency criteria. Of the remaining STEs there is currently little vertical integration following substantial withdrawal of parastatals from direct involvement in international trade (in most cases). To the extent that horizontal integration existed prior to the last decade, it is much less of a feature now. The remaining STEs frequently have responsibility for a range of cereals, but their involvement has been reduced to the extent that any possibility of market manipulation as a result of this range of responsibility is remote. Linkage of upstream-downstream activities does not appear to feature. The extent of monopolistic powers has been reduced considerably in most countries, and while many STEs continue to have a direct role in the purchase of domestic cereals, the proportions of local production purchased are generally small. It is difficult to ascertain from the available evidence the extent to which the remaining STEs are subject to commercial or social criteria in their operations, but the general policy shift towards greater austerity in public finances would indicate that commercial criteria play a greater role than in the past.

Table 7: Operational Activities: Latin America

Criterion	Pre-WTO Agreement	Post WTO-Agreement
Vertical Integration	Liberalisation measures stem from the late 1980s in most cases. Prior to this period, vertical integration was a common feature.	Reduction in role of STEs in international trade, complete withdrawal in some cases.
Horizontal Integration	Cross-commodity responsibilities common, upstream links less so.	Little apparent opportunity for market manipulation.
Monopoly Control	Frequent in the past, particularly in international trade.	Considerable trend towards partial or full privatisation and de-regulation. Little remains in terms of monopolistic activity.
Direct Handling	Typically a feature.	Much reduced role, including in domestic markets.
Commercial/Social Criteria	Major importance of social objectives in the pre-reform period.	Remaining STEs appear to be increasingly subject to commercial constraints.

In **Argentina**, a programme of trade liberalisation began in 1989, export taxes (most importantly for wheat) have been removed, and as have import licensing arrangements. Similarly, in **Chile**, where support for domestic marketing is maintained for cereals through purchase of a small proportion of the domestic crop (less than 2 percent in all cases), there is no regulation of international trade. A substantial shift in government policy has also taken place in **Mexico**. Here the principal agricultural state agency, CONASUPO, has been gradually divested of its powers of intervention with respect to cereals. It now longer has any role in imports or exports and, following the Uruguay Round Agreement, any remaining import restrictions have been replaced by tariffs. With respect to the domestic market, it has gradually shifted from a major price stabilisation role to one of providing market information. A subsidiary provides direct payments to farmers (based on historical area),and another parastatal purchases all barley production, but since 1995 wheat and product prices have been liberalised and now reflect world prices.

Typical of some countries of the region is the current situation in **Bolivia**. Here, although domestic marketing of maize and wheat remains in the hands of parastatals, export licensing arrangements for maize and rice have been removed, and de-regulation has encouraged private sector involvement. Wheat imports continue to be handled by a state agency, but these are primarily in the form of food aid shipments. Similarly in **Peru**, most trade barriers have been removed, and import quotas and licensing replaced by tariffs. The STE monopoly in cereal imports has been revoked.

A less open trajectory of events has taken place in other countries of the region, although the trend reducing the extent of STE regulation is also evident. In **Colombia**, for example, although cereal trade

restrictions such as licenses and quotas have been removed since 1990 and replaced by a price band system designed to stabilize domestic prices, the STE which formerly held an import monopoly with respect to cereals (IDEMA) still has a regulating function with respect to private traders. IDEMA also intervenes in the domestic market in order to provide price guarantees to domestic producers. Partial liberalisation has also been evident in **Ecuador**, where the cereal parastatal (ENAC) no longer has monopoly control over imports. In **Venezuela**, Liberalisation measures have been initiated and then withdrawn, imports remain subject to a licensing system and domestic prices are controlled through parastatal intervention.

2.4.4 Cereal STEs in the Developed Countries

Among the developed countries, the role and activities of the Australian and Canadian Wheat Boards have undergone extensive reforms in recent years. The description of these reforms can be found in chapter 1 (Box 2) and in earlier issues of the review[29].

In the **Czech Republic,** the functions of the State Fund for Market Regulation (SFMR) includes market stablilization, administration of the state loans and subsidies and the setting of minimum guaranteed prices for cereals and other agricultural commodities. In addition private traders are free to export or to import under competitive terms and normal market conditions. The SFMR is owned and financed by the state.

The Food Agency of **Japan** maintained its STE status with respect to rice, wheat, barley and their products market. The agency engages in international trade in these products especially for the trade in rice and the in-quota imports[30] of wheat and barley. It also collects part of the over-quota tariffs and is responsible for sanitary inspection of commodities.

The main activities of the of the Agricultural Marketing Agency (AMA) of **Poland** are similar to that of the SMFR in the Czech Republic. In addition, however, the AMA conducts market research and analysis and assists the Government in designing and implementing policies for the agricultural sector. Since 1994, intervention purchases by the AMA have been carried out in three ways. First, it uses authorized elevators as agents to purchase and store grain on its behalf until it is ready to acquire them. Second, farmers who agree to store grains on it behalf are granted incentives, such as advance loans with the stored grain as collateral. Third, the AMA is making direct purchases from farmers at the intervention price.

In **Romania,** the state grain board, ROMCEREAL, was partially privatised in January 1996. The new agency, the National Agency for Agricultural Products (NAAP), took over the activities of the former board and acquired the 44 joint-stock companies created from ROMCEREAL. In addition, the NAAP retained 25 percent of ROMCEREAL's grain storage facilities with the rest sold to the private sector.

In the **United States**, the role of stabilising, supporting and protecting farm income and prices is carried out by the Commodity Credit Corporation[31] (CCC), which is a Government-owned entity, operating within the US Department of Agriculture. This agency administers US farm and commodity support programmes, which are contained in various "Farm Bills"[32].

[29] In addition, changes in the activities of the South African Wheat and Maize Boards have also been examined in previous issues of the *review.*

[30] The Food Agency import cereals under the minimum access commitments as established in Schedule XXXVIII-Japan, in the WTO Agreement. See also, chapter 2 of *Cereal Policies Review*, 1994-95.

[31] The 1995 US notification to the WTO include the CCC as a state trader but the 1997 notification does not.

2.5 Issues Associated with STEs

While Article XVII of the GATT basically enjoins STEs to behave like private commercial organisations subject to the discipline of market competition. The problem arises because (a) STEs are usually created in order to undertake trading activities in a way which private companies would not: i.e. their objectives are likely to differ from those of commercial criteria by definition; and (b) it is, in any case, very difficult to test for 'commercial' behaviour. Much depends on whether the agency is exporting or importing the commodity concerned.

For export-oriented STEs, the concern revolves around the competitive advantages that STEs might gain derived from their position as part of, or close to, government:

- the possibility of facilitating export sales from the proceeds of monopolistic rents;
- greater opportunity for discretionary pricing facilitated by domestic price pooling;
- greater certainty regarding sources of supply as a result of their legal mandate, and thus increased scope for discriminatory long-term agreements with importing countries;
- increased scope for "predatory pricing" through accessing short-term government subsidies;
- the possibility of benefiting from preferential interest rates, and other government subsidies.

With respect to import-oriented STEs, concerns focus on the extent to which market access is distorted or restricted on account of their activities. The perceived problems arise primarily from when the STE in question has monopoly status:

- it may be difficult to ascertain whether the quantity of imports are determined by demand or by government policy or constraint;
- the possibility that there will be discrimination among importers, for example for the allocation of Tariff Rate Quotas (TRQs);
- control of grades and standards governing imported products may allow preferential access to favoured importers.

The performance of public enterprises did not always live up to expectations and, consequently, to a certain degree in many countries the state has withdrawn from involvement in domestic agricultural marketing. If the manner and extent to which the state intervenes in agricultural markets has changed over the last decade, however, the motivation for intervention and control remains similar to that which made the state enter into these functions in the first place. These can be summarised around the following headings:

- **strategic considerations:** including public health issues and natural resource management, but perhaps more significantly, under this heading could be grouped access to, and control over, investible resources: this includes manipulation of the terms of trade, as well as direct access to funds through direct taxation of imports and exports.
- **poverty reduction**: typical concerns are urban food security and increasing the level and stability of farm incomes;
- **operational efficiency**: efficiency gains made possible by the rationalisation of trading operations, particularly with respect to foreign trade activities, but in the context of domestic trading where non-state operations are characterised by market failure.

The mechanisms for achieving the strategic objectives are diverse, but they are often to do with changing the inter-sectoral terms of trade. This is usually a substitute for direct taxation in contexts where the tax base is very narrow, and taxation at the border is often more achievable as a vehicle for public acquisition of investment funds because of administrative constraints in developing countries. Strategic considerations also

[32] For a review of the recent changes in the US farm Bill, see *Cereal Policies Review*, 1995-97 chapter 3.

include public health measures, the implementation of which frequently involve STEs of some description, particularly those associated with tobacco and alcohol related commodities. Finally, the Republic of Korea has stated that one of the functions of its agricultural parastatals is the promotion of processing industries[33].

Typical activities in relation to poverty reduction include producer price stabilisation and the regulation of food supplies to urban consumers to ensure adequate supplies at affordable prices. The logic of stabilising prices when the target is more stable incomes is questionable[34], but the provision of floor price support can provide an important safety net for rural incomes, as well as an incentive for expanding domestic food supplies. In the case of food importers, border controls are a common mechanism for regulating supplies and protecting domestic producers.

The food security objective is often made explicit in the notifications to the WTO on state trading by cereal importing countries. For example: in Mauritius, intervention in the rice trade has been aimed at making it available to "the economically weaker sections of the community at the lowest possible price" while ensuring regular supplies and quality standards. In Tunisia, the Grain Board is required to ensure a "security stockpile and execute the State policy of guaranteeing a minimum income to producers" and in the Philippines the National Food Authority was set up to look after the food security requirements of the country through a buffer stock for rice and maize, a buffer stock which is used "to address calamities and emergencies". Stability of food supplies is also a significant objective, for example India lists among its reasons for introducing and maintaining STEs: "ensuring security of supplies through multiple contracts with diverse sources"; and "ability to handle crisis situations effectively and protect the country from disruptions in supply[35].

The efficiency gains associated with scale and with institutional costs may be of equal significance as far as cereal commodities are concerned. The scale issue is straightforward: STEs can be an organisational vehicle for grouping the efforts of potential exporters or importers, allowing commodity export and import to be accomplished more efficiently through reducing operating and handling costs.

With regard to institutional economies, of principal importance will be transactions costs, for analytical purposes divided into information, negotiation and enforcement costs. The complexity of the trade regulations, and the technical knowledge and expertise required to implement them imply that for many developing country traders the costs associated with acquiring relevant information will be high, as may those associated with conducting negotiations in a highly specialised and complex environment. The problems of enforcement, where appropriate, may be equally daunting, particularly for the those in least developed countries with little or no international bargaining power, or with few resources to effectively monitor the changing context.

2.6 Conclusions

The reasons why state trading operations have grown to be of substantial significance in international trading activity range from lack of private sector expertise coupled with various manifestations of market failure; the desire to take advantage of economies of scale; to attempts to achieve a wide range of social objectives which would not be possible without some form of state intervention.

While it is apparent that the scope of STE activity has receded substantially in some parts of the world over the last decade, it is also evident that many countries still perceive state trading to be an important arm of policy and one that they wish to continue to use.

[33] See the Notification to the WTO by the Government of South Korea, 1995, p. 2.

[34] While a partial and short-run analysis suggests that incomes may be de-stabilized, some evidence suggests that in the medium- to long-term investment in agricultural production is higher as a result of stable producer prices. See Jones, 1995, p. 556-558.

[35] See the following WTO notifications with respect to state trading: Mauritius, 1995, p.1.; Tunisia, 1997, p.6.; and India, 1996, p.2.; and the Philippines, 1995, p. 1.

In any event, the Agreement on Agriculture made some advances in subjecting agricultural trade to greater openness and transparency. The principal ways in which STEs gain the opportunity to manipulate markets to their own competitive advantage broadly revolve around the extent of vertical and horizontal integration and the degree of monopoly power[36]. What is perhaps the context, which creates the greatest possibility for covert 'market distortion', is where these attributes are combined. A typical example is where a parastatal agency with monopoly powers controls both domestic and foreign trading.

In the cereal markets of most of the countries reviewed, however, the state no longer has a monopoly interest in both domestic and foreign trading. In Latin America the withdrawal has been from STE involvement in foreign markets, and in Africa from domestic marketing. In Asia, the state still maintains a preponderant role in both, but only in a few cases do STEs possess monopoly powers of procurement with respect to domestic production. In the developed countries, despite the increased pace of reforms as a result of the Uruguay Round Agreement, STEs still continue to play a dominate role in both the domestic and international cereal markets.

[36] Closeness to government is often cited as an additional reason, but this is a rather difficult attribute to define or recognize. It matters little whether we are talking of an STE or a private firm providing the government has the power to influence its activity.

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3. FOOD SUBSIDY POLICIES IN DEVELOPING COUNTRIES

3.1 Introduction

Governments in many countries attempt to influence the price consumers pay for food through the use of food subsidies. The goals of subsidy programmes and policies vary among countries and over time and may include desires to improve the real purchasing power of all or certain groups of consumers, to reduce or eliminate calorie and nutrient deficiencies in low-income population groups, to maintain low urban wages, to assure social and political stability, and a number of other goals.

However, governments faced with tight fiscal constraint since the 1980s have been forced to review their food subsidy policies with the hope of reducing expenditures while keeping the programmes efficient. As food subsidy programmes vary from country to country, the actions taken by governments to reduce food subsidies may also be rather specific. This paper is intended to highlight the reforms in food subsidy programmes undertaken by several countries in recent years. Section 3.2 discusses the main types of such programmes followed in section 3.3 by a discussion of the requirements and policy options for designing the programmes. Section 3.4 examines the implications of food subsidy programmes for government policy and the conclusions of the study follows in section 3.5.

3.2 Types of Food Subsidy Programmes

There are two general approaches to subsidize the cost of food: price-specific programmes and food and income distribution programmes.

(a) Price Subsidies

Under this approach, governments fix the consumer price of the subsidized foods and reimburse marketing intermediaries for the difference between market prices and subsidized prices. A price subsidy scheme can take one of several forms:

(i) General (unrestricted) food price subsidies

In an unrestricted food price subsidy scheme[37], unlimited amounts of subsidized food are available at below-market-prices to anyone who chooses to buy it. The subsidy may offset a portion of total production, storage and marketing costs and, as there are no limits on quantity, consumption effects can be substantial. Thus, to avoid domestic supply shortfalls as a result of the subsidy, prices paid to producers as well as investment in food production capacity are often maintained by means of explicit government subsidy. Under this system, benefits are provided to everyone, but only the well off pay the cost. Empirical evidence (Gaiha, 1993) have shown that an unrestricted subsidy programme is most suitable to areas where a very high proportion of the population is needy so that the cost of targeting is likely to exceed the savings from excluding ineligible people. It may be appropriate where local administrative capacity is so weak that rationing or eligibility determination is simply not feasible. Examples of programmes that appear to have been successful in improving nutritional adequacy include the untargeted,

[37] This type of subsidy scheme was in place in Pakistan and Egypt prior to 1991 for cereals and products. Pakistan replaced this system with a direct income transfer programme while in Egypt, various combinations of the different types of subsidies schemes are in place.

un-rationed wheat subsidy in Egypt prior to reforms in 1995 and the former untargeted rice and wheat subsidies in Sri Lanka.

(ii) Rationing

In a rationed subsidy programme, the quantity of food available at the subsidized price is restricted to a per caput or per household limit. The biggest advantage of rationing is cost control. Rationing limits the total cost of the subsidy and makes the cost more predictable and usually limits shortfalls by restricting demand to match available supply. An important food rationing schemes is India's Public Distribution System (PDS) and the Targeted PDS (see Box 6 for an example of the PDS). Rationing is also usually targeted either by limiting the ration to the poor or by self-targeting i.e., where the relatively well off consumers are not prepared to wait in line or travel to ration or *fair price shops.* Quantity limitation through rationing can have the effect of reducing leakages in the sense of reducing excess consumption.

(b) **Direct Distribution and Income Transfer**

(i) Direct Income Transfer

Direct income transfer programmes targeted towards low-income families are rare at present, although Algeria replaced its general price subsidy programme with a direct income transfer programme in 1993. The advantage of such schemes is that it leaves the choice to the consumer as to the proportion of additional income spent on food and other essentials. The main disadvantage is that such schemes require accurate income measurements, which might not be available in some developing countries.

(ii) *Direct distribution*

This is one of the most widespread schemes in developing countries, usually administered by governments in conjunction with an external aid agency. For example, in March 1998, the Mexican State of Guanajuato along with the United Nations International Children's Fund (UNICEF); Banamex (a private bank); Maseca, the maize flour division of Grupo Gruma; and the National Nutrition Institute signed an agreement for a project to distribute subsidize enriched *tortillas* to below-poverty-level populations. For this form of subsidy programme, quantities of food are distributed free to consumers in combination with welfare related programmes such as health, education and family planning. Distribution of food can also be used as an incentive to participate in other programmes, with costs shared among these different programmes. A perceived advantage of direct food distribution is that the benefits are received by the target household or individuals in the form desired by the programme, in contrast to income subsidies, where the income benefits may be spent on non-food items. This advantage is somewhat illusory in that, if the quantity distributed is very large and entails high transaction costs for resale, the distributed food may be resold or food purchases from other sources may be reduced.

(iii) Food Stamps

A food stamp programme is one that distributes stamps or coupons that have a cash value when used for purchasing food at commercial stores. The buyer uses the stamps instead of cash, and the seller can redeem the stamps for cash from banks or government offices. This programme makes use of the existing food marketing system, thereby reducing the administrative demands on the government to procure, ship, store and sell food as in the US food stamp programme. Food stamps augments the purchasing power of the target group, permitting both sellers and buyers, including both programme participants and non-participants, to respond

to market signals rather than to government directives. A major disadvantages of a food stamp programme is that it requires some form of bureaucratic targeting and an administrative system for keeping records, printing and distributing stamps to eligible households.

Box 6: The Public Distribution System in the Indian State of Andhra Pradesh

The Public Distribution System (PDS) in Andhra Pradesh was designed to provide essential commodities to the vulnerable groups at reasonable prices. Rice, Wheat, Edible Oils, Sugar and Kerosene are being distributed through the PDS.

Every family residing in the State is entitled to a ration. All ration cardholders are advised and given appropriate guidance regarding the Fair Price Shops (FPS) at which they could register their cards for obtaining supplies of the subsidized commodity. Special cards of different identifiable colours are issued to families at various levels below the poverty line and entitle them to obtain the essential commodities at special subsidised rates.

The State's Commissioner of Civil Supplies allocates the stocks of essential commodities to the various districts, where the rationed commodities are then re-distributed among the various municipalities. Depending on the number of ration cardholders (white and pink cards) registered with each FPS dealer, the municipalities re-allocate the commodities to each FPS. The details of the commodities allotted to each FPS are communicated to the members of parliament and members of the legislative assembly having jurisdiction in the municipalities.

On receipt of the commodities by the FPS, the shop dealer issues a certificate of receipt and inform the cardholders of the arrival of the rationed commodities either by the beat of a drum (tom-tom) in the villages and also over a public announcement system in cases where they exists. The consumers are free to redeem their ration in a single instalment for a month. However, for the white cardholders, usually those at the bottom of the poverty scale and whose financial disposition does not permit them to draw all their ration in a single instalment, they are permitted to purchase rice up to 5 instalments and wheat up to 4 instalments in a month.

Below are the criteria used to identify eligibility for the Rice Scheme of the PDS:

(a) Family income of 11 000 Rupees (US$275) and below per annum.

(b) All those owning wet land up to 0.6 hectare under assured sources of irrigation

(c) All those owning wet lands up to 1 hectare under all other sources of irrigation like tanks and wells.

(d) All those owning up to 1.2 hectares of dry lands which are fit for raising commercial crops like tobacco, chillies, etc., and

(e) All those owning up to 2 hectares of dry lands.

White ration cards are given to those who satisfy any of the above requirements. Others are given pink ration cards. In 1996, the Government increased the issue price for rice under this scheme from 2.00 to 3.50 Rupees (US 5 to 8 cent) per kilogram. The cardholders are entitled to a minimum of 4 kilograms per month with a maximum ceiling of 20 kilograms per card per month. Under this scheme, there are some 113 million white cardholders, covering a population of 53.7 million who are beneficiaries.

A quantity of 180 000 tonnes of rice is distributed per month under this scheme. The economic cost of rice on an average is estimated to be about 6.52 Rupees (US$0.16) per kilogram. With the PDS issue price of 3.50 Rupees (US$0.08) per kilogram, the subsidy borne by the State Government amounts to 3.02 Rupees (US$0.06) per kilogram for white cardholders. In addition to this scheme, the State Government, through the PDS supplies rice to Social Welfare Hostels at 4.00 Rupees (US$0.09) per kilogram with an annual requirement of 100 000 tonnes. It is estimated that, for 1998, the subsidy for the rice scheme will be about 7 billion Rupees (US$176 million).

3.3 Requirements and Policy Options for Designing Food Subsidy Programmes

Basic Conditions

The conditions that should be considered include food purchasing and food consumption patterns of the population, whether food is domestically produced or imported, food transportation, storage and marketing infrastructure and the availability of trained personnel.

Geographic, social, cultural and economic conditions and the volume of available resources determine what is possible and efficient in a given country. Administration of an income-based eligibility criterion for programme participation by means of a formal process of application and verification works well in the U.S. food stamp programme because most of the population is literate and records of income are routinely kept. In a country where much income is received irregularly and in kind, such bureaucratic targeting may be less successful. The point may be extended to regional variation within countries. Where significant regional differences exist, it may be necessary to implement more than one system. In Bangladesh, ration shops serve primarily the urban population, whereas the rural population benefits from both food-for-work programmes and free market sales.

Costs

As noted by Pinstrup-Andersen (1988), there are two types of costs associated with a subsidy programme: (a) fiscal or explicit costs; i.e. those that can be identified as budget items and that involve cash outlays and (b) implicit costs, which include income forgone by farmers, middlemen or others as a result of market manipulations that reduce the income they might otherwise have received. Implicit costs may be hidden, but they can have severe consequences. It is usually better to make the costs of a subsidy as explicit and visible as possible. Even though this may be politically difficult, it makes it much easier to evaluate the cost effectiveness of the subsidy and to avoid unintended side effects.

Explicit costs of a subsidy may be divided into those that are fixed and those that are variable. Fixed costs may include investment in warehouses and shops and long-term commitment to wage earners. The main variable cost is the subsidy itself; i.e., the difference between the cost to the government of making the food available to the consumer and the price paid by consumers. Different methods of subsidizing food will have different balances between fixed and variable costs. A ration shop system that requires the creation of a nation-wide network of warehouses and retail outlets will have higher fixed costs than a food stamp programme that relies on existing private-sector marketing. Criteria for deciding on a particular subsidy form include the amount of fixed cost that can be supported by the government and the degree to which facilities are available in the private sector.

An objective of the programme design should be to minimize costs consistent with achieving the goals of the programme. Cost can be controlled by keeping the size of the benefit small and by narrow targeting. For maximum cost effectiveness, the size of the subsidy and any quantity limitation should be carefully considered. Another area in which costs can be controlled is administration. There are two main sources of administrative cost in subsidy programmes. One is the cost of procuring, storing, and distributing food, which requires staff, warehouses, vehicles and shops. The other is the cost of monitoring and enforcement, including administering and determining eligibility, which includes staff and office space. The first type of cost can be minimized to the extent the subsidy can rely on existing food supply and distribution mechanisms, generally in the private sector, as is the case with the U.S. food stamp programme.

Targeting: Issues and Policy Options

Successful targeting of a subsidy involves maximum coverage of the target population and minimum leakage to non-target households. Minimizing leakage reduces costs and improves cost effectiveness; maximizing coverage increases costs but also improves the overall effectiveness of a subsidy. These goals conflict with each other to some extent, since restriction on eligibility is likely to exclude some members of the target group along with those who are ineligible. This partly arises from difficulty of accurately assessing eligibility and partly from the fact that inconvenience will discourage some people who are eligible. Also, a programme that identifies and separates the needy from the rest of the population may be unacceptable even to the needy it is intended to serve, thereby reducing coverage and, thus, programme effectiveness.

Further, a programme serving only the poor risks being reduced or eliminated in times of fiscal constraint because it may have no powerful advocates. These arguments for an untargeted programme are balanced by the powerful cost argument in favour of targeting, especially where the needy are relatively few in number. The political dangers of targeting to the needy will vary depending on the cultural acceptability of programmes for the poor. The trade-off between cost effectiveness and political acceptability should be based on local judgement about the consequences of a comprehensive versus a targeted programme.

There are several alternatives for targeting a subsidy to the poor and excluding the well off. Probably the most attractive method is to select for subsidy a food that is in high demand among the target population but not preferred by the better off (for example, *baladi* and *shami* bread in Egypt). This should be a food with a high price elasticity of demand among the target group. It should be economically inferior, i.e.; have negative income elasticity at higher income levels and it should have a relatively high intensity of consumption among the target group, that is, the target group should consume a high proportion of the total supply. The advantage of this method is that the subsidized food essentially targets itself. The subsidy is available to everyone, but usually only the poor take advantage of it. This saves the expense and resource drain of bureaucratic determination of eligibility.

There are disadvantages, however. Targeting by this method is only approximate; each household itself decides whether or not to use the subsidy and the well off who are willing to consume the subsidized food obtain a benefit. The more affluent may also benefit by buying the inferior food and reselling it to the poor at a price higher than the subsidized price but lower than the open market price. The degree to which this kind of resale takes place depends in part on how stringent are the quantity limitations on subsidized purchases. If the ration is quite generous, then the poor have no need to purchase more at a higher price. The size of the subsidy also affects the likelihood of a food being purchased for resale. Given transaction costs and the fact that the resale price must be at least slightly below that on the open market, any profit to be made may be quite low if the subsidy is small. In any case, the cost of these two kinds of leakage is a trade-off against the administrative savings.

Another problem is political: the government may not wish to publicize the fact that it is promoting inferior foods for use among the poor. The political consequences of subsidizing an inferior food, i.e.; in its consumption pattern, not in nutritive value, will probably not be as serious in areas where the need is severe. In Bangladesh, for example, experimental distribution of the inferior grain sorghum was well accepted by the low-income population. In a relatively more affluent setting, such targeting by food selection might be impractical not only for political reasons (resentment on the part of the target group) but also because it may not be possible to identify any important food whose consumption pattern is strongly biased toward the needy.

Another option is to limit eligibility to a particular income group and to establish a procedure whereby people apply and are certified to receive the subsidy. The appeal of this system is that it avoids the leakages that can occur with self-targeted foods (which can be substantial) and that, in theory, the subsidy benefit can be provided on a sliding scale: since eligibility is based on income, households can qualify for a greater or smaller subsidy depending on how far below the income cut-off they fall. There are serious disadvantages to such

bureaucratic targeting in most developing countries. First, the system depends on having staff who can communicate effectively with the client group. To reach throughout the country, the staff needs to be large, thus creating costly bureaucratic undertakings. Second, accurate estimation of income is not easy even in developed economies, where most people work for a regular cash wage and records are routinely kept. Where work is less formal, where many of the poor are self-employed, or where a large share of income is earned in kind, determining income with acceptable accuracy simply is not possible. At best, there will be considerable cheating, and the system will discriminate against those people whose wages are recorded.

An alternative to the calculation of income is to determine eligibility based on land ownership, ownership of other assets or tax status. In cases where land ownership accurately reflects economic status, use of land as a proxy for wealth may well be effective. This method is clearly only appropriate in rural areas. The difficulty of verification is a serious barrier to using ownership of other assets, such as cars or houses, in this way. The problem with using tax status is that in many countries the taxpaying population is extremely small so that tax status is not a good indicator. Local conditions are clearly the determining factor: literacy levels and degree of participation by the low-income group in the formal sector indicate the suitability of bureaucratic targeting.

A third method of targeting is by geographic region. The region can be as narrow as a single urban neighborhood, as was the case in the LICONSA subsidized milk programme in Mexico City; or a whole village, as in the experimental Philippine food price discount programme. The success of geographic targeting is contingent on being able to identify areas where a high proportion of the population is needy and on controlling leakage outside the target area. In Mexico City, leakage was controlled because of the difficulty of storing fluid milk long enough to transport or trade it. Limiting the volume sold to one individual meant that travelling to the target area to purchase the low-priced milk was not economical. In the Philippine case, target villages were those with high rates of under-nutrition. These were identified using information on the growth status of children available from a growth-monitoring programme already in place. Members of the target villages were identified with ration books. Even so, there was leakage, as family members from neighboring villages moved in to take advantage of the subsidy.

Enforcing a geographic price subsidy by preventing leakage at the borders of the subsidized area is difficult. It is more successful if the commodity is perishable if it is sold in limited quantities and if there are natural barriers to trade with other areas. There may also be political problems with geographic targeting, especially if the geographic area coincides with an ethnically or otherwise distinct population subgroup. In such cases, geographic limitations on a subsidy may exacerbate tensions between groups within a country.

Where the budget constraint on dietary adequacy is seasonal because food prices or incomes fluctuate, seasonal targeting may limit programme costs without reducing the nutritional effectiveness of the programme. Seasonal targeting means making the programme available only during the lean season, for example; by issuing time-limited coupons. It should be recognised, though, that severe seasonal food price variations might indicate inadequacy in the food storage and marketing system. This constraint should be addressed directly at the same time as the subsidy programme alleviates the effects of variability in the short term. Care should be taken not to eliminate the impetus to improve seasonal availability of food.

There may also be administrative difficulties to implementing some kinds of subsidy programmes seasonally. Food-for-work programmes, for example, typically aim to employ rural unskilled labour when private sector employment is lacking. This may be during the rainy season, however, when many kinds of public employment, for example road construction and construction of irrigation systems, are also not possible in some countries. If subsidized shops are privately operated under a franchise type arrangement with the government, the operators may resist a seasonal shutdown that would reduce their profits. In cases where the shops sell other goods as well as the subsidized food, as in Egypt and in some provinces of Pakistan, seasonal availability of the subsidy would be less of a problem because there are other sources of profit. In either case, the possibility should

be considered of reducing, rather than eliminating, the ration in the good season. Seasonal targeting is appropriate only in particular circumstances.

Programmes that use the nutritional status of pre-school children as a basis for targeting households for subsidized food distribution, such as the Philippine food price discount and the Colombian food stamp programme, involve considerable administrative expense because of the requirement of regularly evaluating the growth of the children. Such programmes generally use growth monitoring as an educational tool to teach mothers the importance of appropriate child feeding and as a means of individualising health and nutrition education. Subsidized food distribution is ordinarily just one component of the programme, and so the costs of growth monitoring should not be weighed solely against the benefit of targeting the subsidy. Growth monitoring is often considered valuable as a health intervention by itself, but it is probably not suitable as a targeting mechanism for a household oriented subsidy on a national scale, unless, as in the Philippines, a system already operates in the country. One problem with such programmes is that they may establish an incentive for poor households to keep at least one child below the weight-for-height criterion in order to qualify for the subsidy. It would be difficult to document the strength of such an incentive, as compared with the educational value of growth monitoring. Of course, such programmes also discriminate against households without infant children. Although these programmes are more nutrition oriented than the usual household consumption subsidy, similar design considerations apply.

3.4 Implications of Food Subsidy Programmes for Government Policy

Effect on Government Expenditure

Since the early eighties, expenditures on food subsidies decreased in most countries whether measured in absolute terms or as a percentage of total government expenditures or gross domestic product (Thompson and Manfred, 1997). While these decreases were due largely to falling real prices of food procured by the governments, the available evidence shows a few countries, notably Sri Lanka, made explicit cost-saving modifications in their subsidy programmes, including a shift from ration shops to food stamps with a fixed nominal value, liberalization of food prices and exclusion of about half the population from the programme. In the case of Sri Lanka these modifications reduced costs from 15 percent of government expenditures during the late 1970s to less than 3 percent in 1985.

The Sri Lankan experience illustrates two approaches to reducing subsidies with very different effects on the poor. One is targeting the poor and the other is reducing the real value of the subsidy received by a target household. While both may be very effective in reducing costs, the latter results in reduced benefits for the poor while the former need not. These reductions may be severe, as experienced in Sri Lanka, where the real value of food stamps decreased rapidly after 1979 due to large price increases and a fixed nominal value of the stamps.

The evidence from country studies[38] show that the untargeted or poorly targeted food subsidy programmes found in most countries are not the most cost-effective means to reach the goals of indirectly transferring incomes from better-off to poor households, improving food consumption among the poor or improving their nutritional status. This does not mean these programmes have not been effective in reducing poverty and improving food consumption and nutrition among the poor. Many of them have. But it means that these accomplishments could have been achieved at lower fiscal and economic costs. In some of the programmes for example, the ration shop schemes appear to have been rather cost effective in improving household food security, particularly among urban households (Suresh, Bahl and Mruthyunjaya, 1993).

The opportunity cost of the fiscal resources and the sources of financing the subsidies are important considerations. Foreign aid has been an important source of financing for many of the larger programmes,

[38] See, Ali and Adams, (1996); Aziz, (1990); and McDermott, (1992).

including those in Bangladesh and Egypt[39]. However, except for food aid, it is difficult or impossible to link subsidy costs to specific revenue sources, because subsidies are financed out of the general treasury. Furthermore, it is not clear from available information how the funds used for explicit food subsidies would have been spent in the absence of the subsidies.

Finally, it should be noted that explicit food subsidies have made it possible for some governments, for example, those of Egypt and Bangladesh, to keep wages lower in the public sector by providing what might be viewed as in-kind payment in the form of food subsidies. Where this occurs, existing estimates overstate the net fiscal cost of subsidies. This is illustrated by Pinstrup-Andersen (1988), who estimated that a large share of the savings in costs associated with a shift from untargeted ration shops to targeted food stamps in Sri Lanka was spent on increasing wages in the public sector to compensate for the losses in subsidy benefits.

Effect on Wages

Since most food subsidies are linked to staples, they can have a depressing effect on real wages. If this occurs, benefits to consumers are less than the value of the transfer, and existing estimates overstate consumer benefits. The subsidies may be viewed in part as wage subsidies, with a corresponding positive effect on employment and economic growth. The extent to which benefits or costs from food price changes are captured by consumers rather than passed on in the form of lower or higher wages varies among countries, and empirical evidence is scarce. The period of adjustment of wage rates is likely to vary depending on institutional and other aspects. Some evidence (Pinstrup-Andersen, 1988) indicates that public sector wages would be adjusted if food subsidies were changed. As mentioned above, such adjustments were in fact made in Sri Lanka when the subsidies were changed in the late 1970s.

Effect on the Agricultural Sector

The effect on the agricultural sector varies greatly among the programmes, depending on agricultural prices and procurement policies, price-depressing effects of imports and food aid, the degree of subsidy targeting, supply response and a series of fiscal and macroeconomic relations. While foodgrain subsidies in India and Bangladesh were supported in part by domestic procurement at relatively low prices, the ration-shop schemes in Sri Lanka were managed alongside relatively high producer prices, thus requiring higher government subsidies. In Mexico, producer and consumer price subsidies for maize co-existed during some years. Price policies for wheat in Brazil resulted in a shift from producer to consumer subsidies over a period of a few years.

There is no consistent pattern among the programmes with respect to the effect on the agricultural sector. It is clear, however, that explicit consumer food subsidies need not have adverse effects on agricultural incentives. On the contrary, such subsidies enhance the purchasing power of consumers who, in turn, increase their demand for food and, thus, provide opportunities for increasing prices to producers. Implicit consumer food subsidies, on the other hand, are likely to be harmful to producers because they are usually maintained through artificially low producer prices, which in turn result in lower production and lower farm incomes. Countries having explicit subsidies frequently also have implicit ones, but the net effect of these on agricultural incentives is often inconclusive.

Effect on Inflation

Whether and to what extent explicit food subsidies influence the rate of inflation depends on the way they are financed. As already discussed, it is very difficult or impossible to identify the specific source of subsidy financing within government revenues. If it is assumed that subsidy costs are financed by deficit spending and that deficit spending is financed through increased money supply (a reasonable assumption in some but not all cases), then the subsidies will cause inflation. Thus while the prices of the subsidized goods are

[39] See, Gaiha, (1993); and Ali and Adams, (1996).

kept low, the prices of other goods will increase and the net benefits derived by consumers will be lower than the value of the actual transfer. This effect is often overlooked in the debate regarding food subsidies. In fact, governments often justify subsidies in part as a measure to control inflation by keeping food prices low.

The apparent contradiction originates from confusion between a one-time change in the prices of certain commodities caused by subsidies and a continued rate of change in the general price level caused by monetary expansion to finance the subsidies. Empirical evidence of the inflationary effects of food subsidies is scarce. Results from Egypt and the Republic of Korea indicate that the effect can be large (Pinstrup-Andersen, 1988).

Effect on International Trade

The effect of food subsidies on international trade depends on the nature of the subsidy programmes and other economic policies. Reduced consumer prices result in increased demand, which is often met through expanded imports. In the case of general price subsidies, the resulting increases in imports may be very large, as exemplified by the subsidized wheat in Egypt and Brazil. Moreover, fixing consumer food prices can affect the expenditures on imports of non-subsidized goods. In Egypt, it was estimated that a 10 percent increase in the cost of imported food would result in a fall of 1 to 2 percent in industrial output as importation of raw materials is reduced to provide the necessary foreign exchange for food imports (Ali and Adams, 1996).

Implicit subsidies effected through trade policies can have an even stronger effect on trade because, in addition to encouraging consumption, they tend to reduce domestic supply through lower producer prices, thus reducing self-sufficiency. For example, Thailand used to maintain implicit consumer subsidies through export taxes on important food commodities, thus, reducing exports while keeping domestic prices low. Decreasing exports or increasing imports results in greater demand for foreign exchange and pressures on the exchange rate. Such pressures may also occur due to the financing of explicit subsidies.

3.5 Conclusions

The above discussion reflects many of the lessons that countries have learned from operating food subsidy programmes, whether targeted or not. Food subsidies may influence national economic growth and employment in a variety of ways: through price distortions and reduced investment in the agricultural and other sectors, through improved nutrition, through the effects on wages and inflation and/or through the availability of foreign exchange for the import of capital goods, raw materials and even other food items. Overall, there is no strong evidence that expenditure on food subsidies per se either impedes or fosters national output and growth. What is more certain is that pressures to streamline their food subsidy policies are likely to further increase under the current trend of domestic market reform and the tight financial situation in many developing countries.

If national governments wish to undertake a policy review of their food subsidy programme and examine options for changes, the following guidelines for step to be taken may be useful:

- Analysis of the existing system, its costs and benefits
- Identification of the objectives of government policy including target groups
- Analysis of the basic conditions of the economy, including information on the situation of target groups
- Design of alternative policies to meet the objectives, drawing on the experiences of other similarly placed countries.

All food subsidy programmes should contain provisions for terminating eligibility and for permitting newly eligible people to enter the programme. As households' needs and incomes vary over time, so should their eligibility for benefits. In the case of programmes targeted by food quality, it is assumed that people will voluntarily stop participating when they are able to buy higher quality food. In bureaucratically targeted

programmes, it probably makes sense to establish eligibility for a specified, limited period of time, after which the household must re-apply. This puts the burden on the recipient and avoids the resentment and resistance (and possible programme abuses) that would be encountered if programme officials themselves decided when to review a household's eligibility. Local economic conditions should dictate the length of the eligibility period. A system for removing and adding participants is essential if the programme is to continue to serve the needy and exclude those no longer eligible.

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