



Why the Fixed External Reference Price of 1986-88 should be Challenged

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To solve the conflicting positions of the developed countries and the G-33 on the fundamental issue for Nairobi of placing in the green box and not in the amber box (or AMS, aggregate measurement of support) "*the difference between the acquisition price and the external reference price*" of public stocks for food security purposes, it is necessary to challenge the four concepts of "administered price", "market price", "reference price" and "fixed external reference price" (FERP). Indeed the present rule of the Agreement on Agriculture (AoA) Annex 2, paragraph 3, footnote 5 makes a clear distinction between the food purchases at "market prices" – which is presented as the situation in the United States (US) – and at "administered prices", which is presented as the situation in India (and in other countries). Let us illustrate the issue for wheat.

Indeed there is no reason to differentiate between the "administered prices" paid to farmers in developing countries (DCs) and the so-called "market prices" paid in developed countries (paragraph 4 of Annex 2 of the AoA) as the latter are not actual market prices, being heavily subsidized.

1 – The concept of "administered price"

Investopedia defines an administered price as "*The price of a good or service as dictated by a governmental or other governing agency. Administered prices are not determined by regular market forces of supply and demand... When supply and demand for the good change, the administered price may change to subsidize the supplier or protect the consumer*"¹.

The concept of agricultural "administered price" is not defined in the WTO although it works in opposite ways in developed countries and DCs. Whereas in DCs the administered prices – the Indian MSPs (minimum support prices) for example – are fixed *above* domestic market prices to ensure remunerative prices to small farmers, particularly just after the harvest, and to force the private traders to pay higher market prices, in developed countries they are minimum prices fixed *below* the prevailing market prices in order to reduce their level or security nets when the market prices fall too low. But – here lies the fundamental difference – these lower administered prices were accepted by Western farmers only because they were offset by domestic subsidies, including by the alleged *decoupled*² fixed direct payments in the EU and US (before the 2014 Farm Bill) plus *coupled* subsidies, such as the US various types of marketing loan benefits, countercyclical payments and insurance subsidies. In developed countries administered prices are always triggering subsidies, apart from the other means necessary to render them effective: import duties, export subsidies or restrictions, land set aside, production quotas, etc. Indeed the US Farm Bills and EU CAP reforms since the 1990s have consisted in lowering by steps their administered prices to increase their domestic and external competitiveness – importing less and exporting more – through massive compensatory alleged non-trade-distorting subsidies of the *blue* and *green* boxes³.

¹ <http://www.investopedia.com/terms/a/administered-price.asp>

² A subsidy is *coupled* when related to the production or price levels, and *decoupled* in the opposite case.

³ The *blue box* corresponds to the EU fixed direct payments per hectare (cereals and oilseeds), cattle head (bovines and ovines), or litre of milk decided by the CAP (common agricultural policy) reforms of 1992, 1999 and 2004 to offset the reduction of administered ("intervention") guaranteed prices but farmers received them only if they produced the corresponding products. The *green box* covers two types of alleged non-trade distorting subsidies: 1) the traditional *green box* of in-kind aid to general agricultural services benefitting to farmers collectively: agricultural infrastructures, schools, research, agri-environment, calamities, phytosanitary warnings, etc.); 2) the *green box* of decoupled income support in place in the US from 1999 to 2014 and in the EU since 2005 where farmers continue to receive the average amount of blue box direct payments received in 2000-02

2 – The concept of "market price"

To know what a "market price" is the best source are the US and EU anti-dumping provisions on "non-market economies" which are considered not to use prices in line with their "normal value". Thus, in the US antidumping manual, "*For the merchandise under investigation or review, there must be virtually no government involvement in setting prices*"⁴. Or, in the 2009 edition, according to David A. Gantz: "*Commerce requires for purposes of the affected sector a showing that there is no government involvement in determining prices or production quantities; there is private or collective (rather than full government) ownership; and that all significant inputs are subject to market-determined prices*"⁵, and here we must include the subsidies to the largest input, feed (cereals, oilseeds meals and pulses), which have reduced a lot the price of animal products (meats, eggs and dairy). Another text of the US anti-dumping manual gives the definition under 19 USC §2703a (d): "*A market-based economy that protects private property rights, incorporates an open rules-based trading system, and minimizes government interference in the economy through measures such as price controls, subsidies [not underlined in the text], and government ownership of economic assets*"⁶.

Clearly the same can be said of the EU agricultural prices which are even more subsidized per tonne than the US ones. In its Communication to the Council and the European Parliament, the European Commission wrote in July 1991: "*Community has to run a price policy which would be founded on the necessity to face the competition to which it cannot escape neither on its own market nor on the world markets... A system of compensatory payments will be instituted for existing farms in order to compensate their income losses linked to the reduction of institutional prices... The income loss for cereals will represent the difference, i.e. 55 ecus/t, between the new indicative price of 100 ecus/t and the average present purchase price of 155 ecus/t*"⁷. The Bonn University's contribution to the European Commission's assessment of the Agenda 2000 added that "*Further reduction of intervention prices for grains increases the chance to export without subsidies... most of the time and will be able to participate in the rapidly growing demand on the world market. Furthermore, the reduction of grain and other feed prices close to world market prices will be an important step to increase the competitiveness of the European pork and poultry production*"⁸.

3 – The concept of "reference price"

The fundamental problem lies in the way OECD selects the "world reference price". As Tim Wise stresses, "*The PSE and MPS assume that the chosen reference price is the undistorted market price for a given commodity. The measures are very sensitive to the selection of the appropriate reference price. In the world of agricultural commodities, it is very difficult – some would say impossible – to determine a world price. The OECD tends to select the most competitive price, which is generally the lowest price among exporting countries*"⁹. For dairy products OECD has chosen the New Zealand price as the world reference price from which it computes the MPS in all OECD countries. And, for cereals other than rice, it has chosen the US FOB prices (in the OECD PSE data for US wheat you see that the reference price at farm gate has been the same as the producer's price at farm gate since 1996 so that the MPS was zero).

without being obliged to produce anything or being allowed to produce other products than those having benefitted of blue payments.

⁴ US Department of Commerce, *Normal value*, AD Manual, chapter 8.

⁵ <http://ia.ita.doc.gov/admanual/2009/Chapter%2010%20NME.doc>;

http://works.bepress.com/cgi/viewcontent.cgi?article=1000&context=david_gantz

⁶ <http://uscode.house.gov/view.xhtml?req=granuleid:USC-prelim-title19-section2703a&num=0&edition=prelim>

⁷ Commission des CE, *Evolution et avenir de la politique agricole commune. Propositions de la Commission*, 2/91.

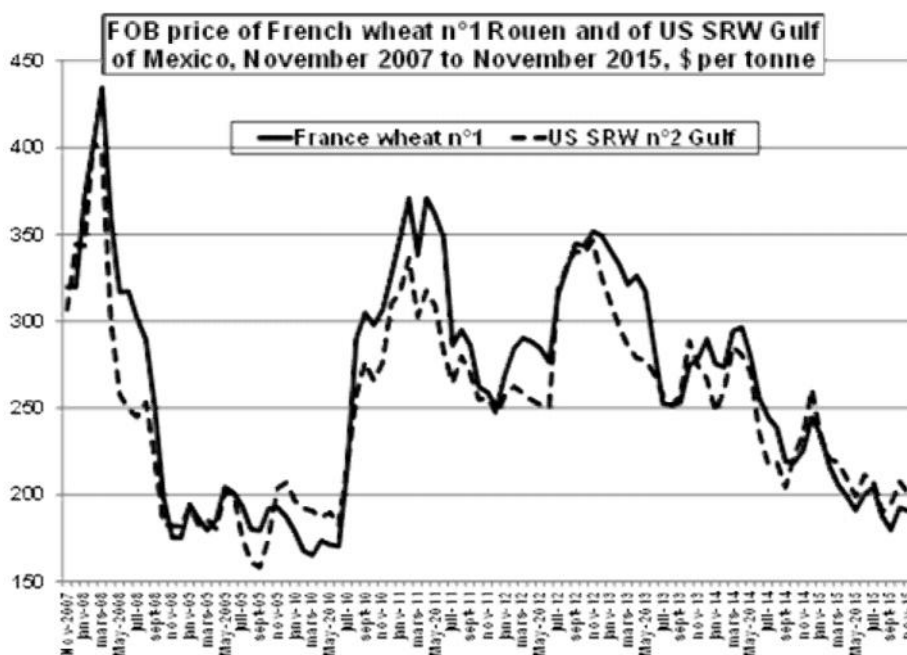
⁸ Wilhelm Henrichsmeyer and Heinz Peter Witzke, *Overall evaluation of the Agenda 2000 CAP reform*, Institute for Agricultural Policy, University of Bonn, European Commission, *Impact analyses of Agenda 2000 decisions for CAP reform*, February 2000, http://ec.europa.eu/agriculture/publi/caprep/impact/summary/sum_en.htm.

⁹ Timothy A. Wise, *The Paradox of Agricultural Subsidies: Measurement Issues, Agricultural Dumping, and Policy Reform*, Global Development and Environment Institute, Tufts University, Working paper N° 04-02, February 2004 (<http://ase.tufts.edu/gdae>).

4 – The concept of "fixed external reference price" (FERP)

There is a consensus that the US is price maker of the world wheat prices so that the FOB and CIF prices of other countries are largely based on the US FOB price of each variety of US wheat, particularly of HRW and SRW, plus the transport and insurances costs between US FOB and the other countries' FOB and CIF prices, plus clearly the impact of exchange rates variations. So that the "fixed external reference price" (FERP) or wheat is largely the US FOB price or derived from it.

The comparison of the EU (France, Rouen) wheat n°1 FOB price and the US SRW FOB price from November 2007 to November 2015 confirm the strong correlation in the two prices, despite the recent depreciation of the euro to the dollar, the average gap between the two over these 8 years being of \$12.7 per tonne, reflecting largely the freight from Gulf to Rouen, with an average gap of \$19.7 per tonne from November 2007 to September 2014 and then of -\$8.7 from October 2014 to November 2015, due to the depreciation of the euro to the dollar¹⁰.



file:///C:/Users/berth/Downloads/GIEWS_price_data%20(2).pdf

A previous paper from 9 September 2002 to 21 September 2007 showed also a strong correlation between the same prices¹¹.

Another paper comparing the Australian wheat price and the US HRW price confirms that "*Australia can largely be considered a price taker on the traded wheat market, with the world wheat price dominated by the domestic price in the United States, given its role in the traded wheat market*" and that "*the exchange rate \$Aus/USD does not act as an insulator to world price variances*"¹².

Now the WTO Annex 3 paragraph 8 states: "*Market price support: market price support shall be calculated using the gap between a fixed external reference price and the applied administered price multiplied by the quantity of production eligible to receive the applied administered price*". The issue here is that the US FOB price is not a "market price" but a de facto "administered price" for which the farmer has already pocketed the subsidy.

It is why several US and international reports have underlined the necessity to internalize in domestic agricultural market prices the subsidies granted to the corresponding products:

¹⁰ file:///C:/Users/berth/Downloads/GIEWS_price_data%20(2).pdf

¹¹ <http://www.bath.ac.uk/economics/research/working-papers/2009-papers/11-09.pdf>

¹² <http://ageconsearch.umn.edu/bitstream/123139/2/Frost%26Paron%2005.pdf>

- The OECD did it in a 2011 report where the concept of domestic price is defined as "*producer price plus payments linked to the production of a specific commodity*"¹³.
- In the US cotton case, the Appellate Body's report underlined that "*During the oral hearing, the United States accepted that farmers decide what to plant based on expected market prices as well as expected subsidies*" (paragraph 440)¹⁴.
- A FAPRI¹⁵ Report of October 2013 assessing the two Farm Bills adopted in 2013 by the House and the Senate presents tables of the expected "*average crop revenue in dollars per acre*"¹⁶, tables where the expected subsidies are added to market sales.
- A World Bank paper of November 2008 incorporates the decoupled subsidies in the indicator of agricultural prices distortion (the NRA, nominal rate of assistance): "*Since the decoupled part of support in agriculture is steadily increasing in high-income countries, it is of particular importance to integrate this part of support, even though it is less market- and resource-distorting than other distortion measures*"¹⁷.
- And USDA has used extensively the concept of "*Net Budgetary Expenditures per Commodity*"¹⁸ incorporating the subsidies with the farm price.

Indeed the US wheat prices cannot be considered as the world reference prices without adjusting them of their subsidies component, particularly for the FERP in the 1986-88 period, where the OECD data on US indicators of wheat support show that the US average wheat market price support (MPS) was of \$882 million for 54.526 million tonnes or of \$16.2 per tonne, corresponding essentially to export subsidies. And the US Schedules of commitments notified to the WTO in 1994 gives an average of \$594 million for the EEP (export enhancement programme) in 1986-88 for 19.580 million tonnes of subsidized wheat exports, hence at \$30.3 per tonne, implying that only 58% of exports received export subsidies¹⁹. For conservative reasons we do not add the subsidy component of the US GSM export guarantee programmes that some researchers have evaluated to be of 4% of these credits²⁰. But, on the basis of actual total exports of 33.775 million tonnes, the subsidy per tonne was of \$17.6, not far from the \$16.2 given by the OECD MPS. And the US Schedule shows also that the domestic subsidy per tonne was on average of \$80.1 – of which \$61.9 for the AMS and \$18.1 for the green box subsidies allocated to wheat for its 4.1% share in total agricultural production value in that 1986-88 period –, which raises the total subsidy per tonne of exported wheat at \$97.7 and the total subsidies to wheat exports at \$3.300 billion.

Given the average FOB price of \$114 (export value of \$3.849 billion for 33.775 million tonnes), the average dumping rate was of 85.7%! So that, to be considered as the world reference price in that period, the US HRW FOB price should be increased by \$97.7 to \$211.7! Given that the USDA data base does not provide the FOB price of SRW wheat from 1986-87 to 1988-89 but only from 1988-89 whereas the FOB prices of HRW wheat are only available from 1992-93, we will rely on the average FOB price of all wheats of FAOSTAT even if the HRW price was higher by about \$10 than the SRW in the 90s. In fact the US wheat FOB price had never been so low since 1973.

Now it is clear that this US FOB price of \$211.7 in 1986-88 would have implied an Indian FERP of at least \$230 (to account for the gap from FOB Gulf to CIF Mumbai), a level which would practically be the same as the

¹³ Jean-Pierre Butault, *Evolution of Agricultural Support in Real Terms in OECD Countries and Emerging Economies*, OECD, 2011, <http://www.oecd-ilibrary.org/docserver/download/5kgkdgf25x20.pdf?expires=1385386110&id=id&accname=guest&checksum=476FE82E1A92E7409C7AAE4E85F48958>

¹⁴ WT/DS267/AB/R, 3 March 2005

¹⁵ US Research Center dependent from the US government.

¹⁶ http://www.fapri.missouri.edu/outreach/publications/2013/FAPRI_MU_Report_06_13.pdf

¹⁷ Kim Anderson and Signe Nelgen, "*Estimates of Distortions to Agricultural Incentives, 1955-2011*", updated in June 2013, http://siteresources.worldbank.org/INTRES/Resources/469232-1107449512766/Note_summarizing_core_updated_database_0613.pdf; *Distortions to agricultural incentives in Asia*,

<http://econ.worldbank.org/WBSITE/EXTERNAL/EXTDEC/EXTRESEARCH/0,,contentMDK:21960058~pagePK:64214825~piPK:64214943~theSitePK:469382,00.html>

¹⁸ http://www.fsa.usda.gov/Internet/FSA_File/pb12_tbl35.pdf;

<http://www.fsa.usda.gov/FSA/webapp?area=about&subject=landing&topic=bap-bu-cc>

¹⁹ https://www.wto.org/english/tratop_e/agric_e/schedule_e/usa.pdf

²⁰ <http://ageconsearch.umn.edu/bitstream/30791/1/24020506.pdf>

present Indian minimum support price (MSP) of Rs 1,450 a tonne in 2014-15²¹ or \$231.9 at the average exchange rate of Rs 62.514 to the US\$²².

If for the most recent years the US did not use explicit export subsidies, nevertheless the US domestic subsidies to wheat were of \$2.772 billion on average from 2010 to 2014, or of \$48.2 per tonne, implying total export subsidies of 1.412 billion.

Table 1 – US subsidies to wheat from 2010 to 2014

\$ million	2010	2011	2012	2013	2014	Average
Wheat product-specific (PS) subsidies						
Wheat CCC subsidies ²³	1280	1378	905	1116	1089	1154
Wheat insurance subsidies	688	1421	2162	1664	1020	1391
Total wheat specific subsidies	1968	2799	3067	2780	2109	2545
Share of wheat in total agricultural production value						
Wheat production value	11021	13494	16538	14024	11910	13397
US whole agric. production value	318430	363710	399325	403018	420146	380926
" % of all agric. production value	3,46%	3,71%	4,14%	3,48%	2,83%	3,52%
Non-product-specific (NPS) subsidies to wheat*						
Agricultural fuel	2375	2375	2375	2375	2375	2375
Irrigation	1000	1000	1000	1000	1000	1000
Agricultural loans	155	155	155	155	155	155
Promotion of agricultural products	1353	1250	1373	1267	1020	1253
States' farm expenditures	1304	1262	1224	1226	1226	1248
Export Programmes	405	551	454	437	238	417
Total NPS subsidies	6592	6593	6581	6460	6014	6448
Wheat NPS subsidies	228	245	272	225	170	227
Total wheat subsidies						
PS + NPS wheat subsidies	2196	3044	3339	3005	2279	2772
Share of exports in wheat production						
Production in 1000 tonnes	58834	54210	61254	58072	55107	57495
Export "	35115	28587	27526	31987	23229	29289
Export/production	59.7%	52.7%	44.9%	55.1%	42.2%	50.9%
Wheat subsidies						
\$ per tonne	37.3	56.2	54.5	51.7	41.4	48.2
Total to wheat exports in \$ billion	1.311	1.605	1.500	1.655	961	1.412

Source: OECD and USDA. 2010 is for the marketing year 2010-11 and so on...

<http://www.ers.usda.gov/data-products/farm-income-and-wealth-statistics/cash-receipts-by-commodity.aspx>

<http://www.fas.usda.gov/programs/export-credit-guarantee-program-gsm-102/yearly-activity-reports>

* *Why the US rejects the agricultural modalities of December 2008*, Solidarité, February 15, 2015, http://www.solidarite.asso.fr/Papers-2015?debut_documents_joints=20#pagination_documents_joints

However, for the three years period 2011-12 to 2013-14 the average total subsidies were of 3.002 billion for an average production of 57.995 million tonnes, i.e. of \$51.8 per tonne, and the total export subsidies were of \$1.474 billion for 28.474 million tonnes.

Table 2 – US subsidies to wheat from 2011-12 to 2013-14

	2011-12	2012-13	2013-14	Average
Total subsidies in \$ million	3191,5	3172	2642	3002
Production in 1000 tonnes	57732	59663	56589,5	57995
Subsidy in \$ per tonne	55,3	53,2	46,7	51,8
Exports in 1000 tonnes	28056.5	29756.5	27608	28464
Subsidies to exports in \$ million	1551	1582	1289	1474

²¹ <http://farmer.gov.in/mspstatements.html>

²² <http://www.ers.usda.gov/data-products/agricultural-exchange-rate-data-set.aspx>

²³ <http://www.fsa.usda.gov/about-fsa/budget-and-performance-management/budget/ccc-budget-essentials/index>

Table 3 compares the annual wheat production costs and revenues per planted acre (without Government payments) on average from 1998 to 2014 and shows the necessity of wheat subsidies, despite the high prices from 2010 to 2014. We see that, on average the deficit was of \$42.03 per acre or \$1.04 per ha, of which of \$1.69 in 2014²⁴. For an average yield of 2,875 kg/ha, of which of 2,936 kg in 2014²⁵, the average deficit per tonne without Government payments was of \$36.2, of which of \$57.6 in 2014.

Table 3 – US wheat annual production costs and revenues without government payments: 1998-14

\$ per planted acre	1998-03	2004-08	2009-14	1998-14	2014
Gross value of production	105,39	191,42	268,92	188,41	247,53
Total costs	175,88	224,84	289,67	230,44	315,78
Balance (without Gov. payments)	-70,49	-33,42	-20,75	-42,03	-68,25

Source: <http://www.ers.usda.gov/data-products/commodity-costs-and-returns.aspx>;
<http://www.ers.usda.gov/data-products/wheat-data.aspx#25171>

We will not develop here the EU wheat subsidies but they were even higher per tonne than the US ones in the base period 1986-88, at €132.1 per tonne of which €118.8 in export subsidies and €13.1 in domestic subsidies, corresponding to a dumping rate of 114.2%. So that the combined US+EU wheat subsidy per tonne was of \$110.7 with a dumping rate of 97.4%! It has also been estimated that the US EEP programme alone explained 35% to 40% of the increase in the EU wheat export refunds. And, as the combined US+EU wheat exports reached 52.204 million tonnes, about half the total world exports (much more if we included the wheat processed in other exported products), the combined US+EU FOB wheat price on which the WTO Members are forced to align their FERP is unacceptable.

As Tim Wise acknowledges: *"Policies in exporting countries that reduce export prices can have the perverse effect of increasing the estimates of farm support in other countries, particularly developing countries"*²⁶.

The conclusion is that, if we are to comply with the AoA rules and at the same time with the legal definition of market price according to the US and the EU anti-dumping laws, we must add the subsidies per tonne to this so-called US FOB "market price". And, given that the US is the price maker of wheat for all the other countries, their reference prices should be raised by as much.

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24 <http://www.ers.usda.gov/data-products/commodity-costs-and-returns.aspx>

25 <http://www.ers.usda.gov/data-products/wheat-data.aspx#25171>

26 Timothy A. Wise, *The Paradox of Agricultural Subsidies: Measurement Issues, Agricultural Dumping, and Policy Reform*, Tufts University, May 2004, <http://www.ase.tufts.edu/gdae/pubs/wp/04-02agsubsidies.pdf>