

## World Agriculture & Trade



# Commodity Policies Of the U.S., EU, & Japan— How Similar?

Commodity policies of the U.S., the European Union, and Japan address some of the same goals, but there have always been key differences in approach and in their policy instruments. In recent years, all three have made significant changes to their commodity policies. Efforts to encourage freer trade in agricultural commodities, particularly the disciplines agreed to under the Uruguay Round Agreement on Agriculture (URAA), have led each to move toward programs that are less trade-distorting. Although differences certainly remain, some of the factors influencing development of agricultural policy may be pushing their commodity policies in a similar direction.

### Similarities: Shifts from Price To Income Support

Most commodity policies can be categorized as either income support or price support. A key trend in commodity policy in the last decade has been the move from primary reliance on price support to increased use of income support, which is less trade-distorting. All three have

reduced the use of price support for several commodities, replacing at least a part of their price support with income support through direct payments to producers. The European Union (EU) and Japan remain more reliant on market price support than the U.S.

The U.S. provides a number of income support measures. Direct payments (similar to production flexibility contract payments) and counter-cyclical payments both provide support to producers based on historical production. Direct payments are decoupled from current production and prices, while counter-cyclical payments are decoupled from current production but linked to current prices. Marketing loan benefits provide payments to producers based on current production and prices. Ad hoc disaster assistance and subsidized crop and revenue insurance support income by reducing risk and losses from weather and other disasters. Planting flexibility, a companion reform to decoupled payments, allows producers to plant almost any crop or leave land fallow without losing eligibility for direct payments.

Price support programs have declined in importance in U.S. farm policy, continuing only for sugar, tobacco, and dairy.

In the EU, income support measures include compensatory payments, which compensate for reduced price supports with direct payments to crop producers based on historical production, and livestock headage payments to beef cattle and sheep producers based on number of animals. Livestock payments will be expanded to include dairy producers beginning in 2005. Neither of these measures is related to current prices, but they are linked to current area planted and livestock numbers, subject to area caps and ceilings on number of eligible animals. EU producers have a limited form of flexibility that allows them to receive payments as long as they continue to plant some type of arable crop or put land in set-aside.

EU price support programs include intervention purchasing and product withdrawal, production and marketing quotas, import protection, and export subsidies. Prices for major commodities such as grains, oilseeds, protein crops, dairy products, beef and veal, and sugar depend on the EU price support system, although with recent reforms, price support has become less important for grains, oilseeds, and beef. Other mechanisms, such as subsidies to assist with temporary storage of surpluses, as well as consumer subsidies paid to encourage domestic consumption of products like butter and skimmed milk powder, supplement the direct price-support instruments.

Japan maintains two kinds of income support programs. Commodity-specific income stabilization programs, introduced since 1998, compensate farmers when current market prices fall below a moving average of previous years. The government provides the bulk of funds for these payments, but participating farmers also contribute based on their output. Traditional deficiency payment programs pay producers of certain commodities the difference between current market prices and a fixed reference price, rather than a moving average as with income stabilization. Both deficiency payments and income stabilization payments allow market prices to be freely determined, similar to U.S. marketing assistance loans and loan deficiency

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cy payments. As in the U.S., subsidized crop and livestock insurance reduces risk for Japan's farmers.

Price support programs, though less prevalent than in the past, continue in Japan. Production limits for a few key commodities, including rice, are designed to keep market prices high by controlling supply. Government corporations continue to manage prices in sweetener, wheat, and dairy markets, chiefly through import control. Most importantly, high tariffs raise the price of imported products and reduce competition with domestic products that might pressure prices.

### Differences: Supply Control & Border Measures

In contrast to the shared trend toward substituting income support for price support, approaches to supply control, surplus disposal, and border measures (including export subsidies, tariffs, and tariff-rate quotas) illustrate continuing policy differences.

The U.S. eliminated its use of land set-asides as supply control measures in 1996; its remaining land retirement programs—the Conservation Reserve, Wetland Reserve, and Grassland Reserve programs—are based on an environmental protection rationale. The EU, which previously had supply control programs only for dairy and sugar, extended supply control to arable crops with a voluntary set-aside program in 1988 and a mandatory set-aside in 1992. It applied a weaker form of supply restrictions to the livestock sector, imposing limits on the number of beef cattle and sheep eligible for payments. Japan uses supply control programs for rice and milk.

U.S. use of export subsidies has been limited in recent years to dairy products and poultry. The EU continues to use export subsidies for many price-supported commodities, although World Trade Organization (WTO) obligations have required reductions in subsidy levels. Japan, an importing country, does not use export subsidies, although it donates some of its rice imports and production to other countries as food aid rather than releasing them into the domestic market.

The three differ in their reliance on import tariffs and tariff-rate quotas to support domestic prices. Although all maintain tariffs, EU and Japan tariffs are higher, on average, and include a greater number of megatariffs (tariffs over 100 percent).

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While all three provide moderately high support to their agricultural sectors, the EU and Japan maintain higher overall support, and provide more support that is coupled or partially coupled to production than the U.S. A common measure of government support to domestic agriculture—the OECD Producer Support Estimate (PSE)—indicates the U.S., EU, and Japan provide support to their farmers at 21, 35, and 59 percent of the value of their agricultural production.

### The Burdens of History, Trade Agreements, & Budget

Many factors shape agricultural policy formation, but among the most significant for these three have been historical differences in policy context and constraints from budget limits and trade agreements (including planned enlargement of the EU).

Current commodity policies in the U.S., the EU, and Japan are the result of developments and policy changes during the last century. U.S. commodity policy is rooted in price support programs established in the 1930s in response to the Depression-era collapse of farm prices. Chronic surpluses, steadily increasing government stocks, and rising agricultural spending resulting from these programs, however, led to growing pressure for change.

The 1996 Farm Act introduced nearly complete planting flexibility and promised continued government efforts to enhance access to international markets.

Redesigned support programs encouraged greater market orientation, along with fixed income support payments that were no longer tied to production. The 2002 Farm Act, while introducing new counter-cyclical payments, continued planting flexibility and basing program payments on historical production.

The EU's Common Agricultural Policy (CAP) arose in response to post-World War II concerns about food security, poor productivity, and low farm incomes in an agricultural sector characterized by small, fragmented farms. Since the inception of the CAP in the 1960s, however, managing surpluses has replaced food security as a major preoccupation of EU agricultural policymakers. The EU has shifted from being a net food importer to one of the world's largest exporters of wheat, sugar, meat, and dairy products.

Japan, which also experienced food shortages after World War II, is increasingly reliant on imports for its food supply. Today, about 60 percent of Japan's aggregate calorie intake comes from imports. Japan has argued that goals of self-sufficiency in agriculture are needed to maintain a significant production base in the event trade becomes difficult. However, another major focus of Japan's agricultural protection has been a desire to support farm incomes and rural economies. Japan's postwar land reform created a very small-scale farm structure, and small farmers' incomes have been maintained principally through very high price support, chiefly by border measures.

For all three, fiscal constraints have figured prominently in commodity policy changes. The need to reduce U.S. government expenditures in the face of persistent fiscal deficits made it difficult for legislators to increase spending on agricultural programs in the 1990s. Budget surpluses by the end of the decade permitted significant increases in funding commitments for agricultural programs in preparation for the 2002 Farm Act. With the return of deficits, however, pressure may again develop to reduce spending on agricultural programs.

In the EU, supporting agriculture has also required large outlays, and as EU support has shifted toward producer support poli-

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## Farm Policies in the U.S., EU, and Japan—Key Similarities and Differences

Similarities	Differences		
	U.S.	European Union (EU)	Japan
<b>Price support</b>			
All have reduced their use of direct price supports in recent years	Direct price support maintained only for dairy, sugar and tobacco; marketing loan rates, which determine marketing loan gains and loan deficiency payments, do not act as market floor prices	Direct price support maintained for many commodities; intervention price acts as market floor price	Relies heavily on price support, provided partly through producer quotas and state trading, but primarily through border barriers
<b>Income support</b>			
All have increased their reliance on income support through direct producer payments	Direct payments program is decoupled from current production (based on historical entitlements); counter-cyclical payments are decoupled from current production, but linked to current market prices; marketing loan program is coupled to current production and prices	Compensatory payments are partially decoupled (based on current area planted or livestock numbers, but subject to limits)	Income stabilization and deficiency payments compensate for price declines through direct payments to farmers, without raising market prices
<b>Border measures</b>			
The U.S. and EU continue some use of export subsidies	Provide export subsidies primarily for dairy and poultry	Provide export subsidies across a wide range of commodities, accounting for 90 percent of all WTO-notified export subsidies; may also impose export tax (infrequently used) to stabilize domestic market prices	Provide no export subsidies, although rice is donated as food aid to developing countries
All maintain tariffs on agricultural products	Agricultural tariffs average 12 percent	Agricultural tariffs average 30 percent	Agricultural tariffs, averaging less than 50 percent, are hard to measure because of widespread use of compound tariffs and temporary rates
All have some tariffs greater than 100 percent (megatariffs)	24 megatariffs maintained	142 megatariffs maintained	An estimated 73 megatariffs maintained
<b>Total support</b>			
All three maintain moderately high to high support levels for agriculture (measured by OECD's Producer Support Estimate (PSE) as percent of value of production)	Lowest support of the three (21.2 percent of value of production); significantly greater reliance on income support	Support higher than U.S. but lower than Japan (35 percent of value of production); significantly greater reliance on price support	Highest support of the three (59.4 percent of value of production); heaviest reliance on price support through border measures
All countries devote significant budget outlays to supporting agriculture (in US\$)	Budget outlays lower since 1987	Budget outlays higher since 1987	Budget outlays higher in 1990s for structural adjustment
All have been shifting basic policies away from production-linked (coupled) price support toward less directly linked programs, but continue to provide substantial coupled support to parts of agricultural sector (as measured by 1998 WTO notifications)	Most decoupled (green box) support of the three	Most coupled or partially coupled (amber or blue box) support of the three	Coupled or partially coupled (amber or blue box) support matches that of the U.S.

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cies funded by taxpayers rather than consumers, the capacity of the budget to provide that support may be further strained. The EU also faces a unique circumstance in the anticipated budget effects of its impending enlargement. Unlimited price support with the entry of several new agricultural producing members will place an even greater burden on the EU budget.

Japan's government deficit has soared to worrisome levels at the same time agricultural commodity policy moves toward income support. Unlike current market price support, which is paid mostly by consumers through high tariffs on imports, a program of income support relies on tax money that is in increasingly short supply. Replacing market price support with income support could require much higher government expenditures and place a greater strain on government resources.

Trade is important to all three. As increases in agricultural output have outpaced the growth of domestic demand in the U.S. and the EU, the share of production that is exported has risen. With continued growth in productivity, both these countries will have to find outlets for additional production if they are to maintain strong agricultural sectors. Japan's situation as a net food importer is fundamentally different—and its government policy is aimed at increasing the scale and efficiency of farms in order to help them survive and provide a greater share of Japan's needs.

The URAA was the first meaningful multilateral agreement covering agricultural trade. Although URAA disciplines did not require major changes in U.S. policies in the early years of the agreement, the 2002 Farm Act explicitly acknowledged URAA constraints on future U.S. farm support. The Act requires the Secretary of Agriculture to reduce expenditures on commodity programs to ensure they do not exceed allowable levels.

The EU's Agenda 2000 reforms explicitly acknowledged the importance of the URAA, citing the need to reduce support prices to comply with Uruguay Round commitments to cut domestic support to agriculture (AO October 2002). Constraints on subsidies imposed by the URAA have led to increasing concern

among policy makers about the competitiveness of EU agriculture. This concern underlies the additional support price cuts of the Agenda 2000 program.

Japan passed a new Basic Law on agriculture in 1999, which outlined goals for Japan's agriculture, including greater attention to multifunctional aspects of farming, such as preserving rural landscapes and supporting rural economies. Traditional support for commodity production now must share the agriculture budget with such non-commodity specific goals. The new legislation also emphasized the need to reduce Japan's reliance on food imports by strengthening the competitiveness of its agriculture.

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### **New issues, including environmental concerns, food safety and quality, rural development, and changing farm structure, are increasingly shaping commodity policy.**

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As the three continue to provide support for their farm sectors while complying with tightening limits on trade-distorting support, they may seek to work increasingly through policies such as environmental or rural development programs, which may qualify for exemption from WTO reduction commitments. Additional trade agreement disciplines that limit the potential differences among countries in level and type of trade-distorting programs may lead to convergence in commodity policy approaches and could contribute to less contentious trade relationships and negotiations.

### **New Issues Shaping Policies**

New issues, including environmental concerns, food safety and quality, rural development, and changing farm structure, are increasingly shaping or promising to shape commodity policy of all three.

In the U.S., the 2002 Farm Act increased support for conservation programs by about 80 percent. U.S. attention to biosecurity issues and recent outbreaks of foodborne illnesses and animal disease

may generate changes in policy that affect production practices. Policymakers have also begun to look beyond traditional commodity support programs to encourage rural development, as nonfarm activities increasingly dominate the economic life of many U.S. rural communities.

Public pressure regarding these new issues is perhaps most fully developed in the EU, where the Berlin European Council of 1999, which adopted the Agenda 2000 reform program, endorsed policies aimed at producing a "multifunctional, sustainable and competitive agriculture." The EU Agenda 2000 policy reforms strengthened links between producer support payments and environmental protection requirements.

Concerns related to the safety and quality of food have occupied EU officials for the last several years, as "mad cow disease," outbreaks of foodborne illnesses, and the foot-and-mouth disease crisis shook Europeans' confidence. Policy changes aimed at promoting less intensive livestock production, combined with stricter standards on animal feeds and meat hygiene, have been instituted to address these concerns.

Through its policy of "modulation," the EU allows member countries to shift some funding from commodity support to rural development programs, including agri-environmental programs and programs aimed at promoting increased diversification.

Japan has begun to subsidize environmental improvements made by livestock farmers and has launched policies to preserve farming in hilly and mountainous areas that have difficulty competing even within Japan's protected markets. While these policies support some commodity production, their larger aim is the elimination of externalities of production, such as odor and water pollution, as well as the preservation of societal benefits such as landscapes and rural welfare. Food safety has also become a pressing issue, leading to the creation of a new food safety commission and to government pledges to focus more attention on consumer needs.

Traditional domestic support and trade concerns will undoubtedly continue to play a primary role in commodity policy

direction for all three, and trade goals and constraints will likely have the greatest influence on whether commodity policies become more similar. However, the pressure of public demands for attention to such issues as environmental impacts and food safety will likely gain influence.

The U.S., EU, and Japan have in some cases moved toward similar approaches to meet the goals of commodity policies in recent years. Their policies still differ, however, in significant ways—particularly in the extent of their reliance on income versus price support, reliance on border measures, and use of surplus disposal and supply control. They face similar pressures from tight budgets, trade constraints, and increasing public connection of agricultural policy with issues beyond traditional goals for supporting production agriculture. Whether these pressures will lead to similar policy responses remains to be seen. So far, they have not done so consistently, in part because the level of public interest and pressure they face has differed, reflecting differences in current conditions and recent experiences.

In the U.S., debate on the impacts of the 2002 Farm Act will continue to influence

the future of U.S. farm policy as budget outlays, trade negotiations, environmental and consumer concerns, and production issues fuel discussions of appropriate and effective agricultural programs. In the EU, a reform proposal arising from the 2002-03 mid-term review of the CAP is spurring a similar debate, offering the prospect of comprehensive reform or, if Member States reject the Commission's proposal, the possibility of further marginal change. In Japan, the government continues to introduce new measures to speed consolidation of farming into more efficient, lower cost operations.

In the midst of these debates, the future direction of farm policy is unclear. But while significant differences will undoubtedly remain, some of the discussion suggests that the U.S., the EU, and Japan could be headed in a similar direction.

#### AO

Anne Effland (202) 694-5319

[aeffland@ers.usda.gov](mailto:aeffland@ers.usda.gov)

Mary Anne Normile (202) 694-5162

[mnormile@ers.usda.gov](mailto:mnormile@ers.usda.gov)

Edwin Young (202) 694-5336

[ceyoung@ers.usda.gov](mailto:ceyoung@ers.usda.gov)

John Dyck (202) 694-5221

[jdyck@ers.usda.gov](mailto:jdyck@ers.usda.gov)

For further information on U.S. and EU commodity policy, see the following briefing rooms on the ERS website:

#### U.S. policy

[www.ers.usda.gov/briefing/farmpolicy/programprovisions.htm](http://www.ers.usda.gov/briefing/farmpolicy/programprovisions.htm)

#### EU policy

[www.ers.usda.gov/briefing/EuropeanUnion/policy.htm](http://www.ers.usda.gov/briefing/EuropeanUnion/policy.htm)

For further information on Japan's commodity policies, see:

#### Sweetener Policies in Japan

[www.ers.usda.gov/publications/so/view.asp?f=specialty/sss-bb/\(9/10/02 supplement\)](http://www.ers.usda.gov/publications/so/view.asp?f=specialty/sss-bb/(9/10/02%20supplement))

#### Vegetable Policies in Japan

[www.ers.usda.gov/publications/vgs/oct02/vgs293-01/](http://www.ers.usda.gov/publications/vgs/oct02/vgs293-01/)

*For an initial assessment of the 2002 Farm Act...*

## THE 2002 FARM ACT PROVISIONS AND IMPLICATIONS FOR COMMODITY MARKETS

A new report on the Economic Research Service website

- An evaluation of effects on agricultural commodity markets
- A discussion of major commodity programs (Title I of the Act)
- An overview of provisions on commodities, conservation, and trade

Available at [www.ers.usda.gov/publications/aib778/](http://www.ers.usda.gov/publications/aib778/)

Further information on farm policy at [www.ers.usda.gov/briefing/FarmPolicy](http://www.ers.usda.gov/briefing/FarmPolicy)