

# WORLD TRADE ORGANIZATION

RESTRICTED

WT/CTE/W/24

20 March 1996

(96-1010)

---

## Committee on Trade and Environment

### COMMUNICATION FROM ARGENTINA ON ITEM 6 OF THE COMMITTEE'S WORK PROGRAMME

The environmental benefits of removing trade restrictions and distortions,  
including tariff escalation, subsidies, state trading, and  
excessively high tariffs

#### PROCEDURAL REMARKS

1. On this Issue, as with many others, we believe that a simple methodology of analysis should be followed. The first step would be to identify existing problems, if any, related to the matter. Accordingly, the second step should be the identification of possible solutions, or options to the problems identified. The third and last step, should be the selection, on a pragmatic basis (i.e. feasibility, both technical and political), and eventual recommendation of some of the solutions which have been identified. We believe that this simple methodology would cater to the objectives set in the terms of reference of the Committee on Trade and Environment (CTE).

#### INTRODUCTORY REMARKS

##### Striking a balance

2. The introduction in the WTO of an environmental perspective in the consideration of trade distortions, which up to the end of the Uruguay Round had only been considered in the GATT through the classical trade perspective, is due to the approval at the Marrakesh Ministerial Conference (April 1994) of the Decision creating this new Committee and establishing a very comprehensive and balanced programme of work.

3. Two very important reasons make this issue both challenging and very particular:

a) All the rest of the CTE's agenda can be summarised by an implicit question, namely: "when and in what circumstances would WTO Members be prepared to accept restrictions on trade as consistent with WTO rules for the sake of an environmental advantage?". Conversely, this point confronts the CTE with a question much more in line with the WTO's objectives, namely: "which of the existing trade restrictions are we prepared to remove in order to obtain environmental advantages?" Given that the WTO is a forum in which free trade is to be promoted, the answer to this question should not be avoided.

b) The greater the capital wealth, the greater the possibilities for a given society to sacrifice immediate returns for the sake of future returns or, for the sake of an immediate environmental advantage. Thus, normally our discussions end up concentrating on the negative environmental consequences of shortage of capital wealth, with the obvious imbalance that this represents for developing countries.

4. In other words, even not intending so, by focusing our debate on process and production methods (PPMs), the shortage of capital is implicitly placed at the dock. The resulting consequence is that developing countries, paradoxically, although bearing less responsibility for the deterioration of the earth's environment, frequently feel uneasy about attempts to put trade in line with environmental objectives.

5. Conversely, as is argued in this document, the analysis of this issue, namely "environmental benefits of removing trade restrictions and distortions", leads us straight to a discussion of the negative environmental consequences of the irrational use of excessive capital. This makes this issue an unavoidable part of the final outcome of the CTE's work.

## I. IDENTIFICATION OF THE PROBLEM

### (i) Theoretical background

6. "In general, trade is not the root cause of environmental problems, which are due to market and intervention failures. Market failures stem from deficiencies in the market's ability to properly value and allocate environmental resources and the failure to internalise environmental costs in the prices of goods and services. Intervention failures occur when government policies (environmental, trade and other types of policies) do not correct for, create or exacerbate market failures."<sup>1</sup>

7. By distorting prices, a governmental policy (an "intervention failure") is capable of altering the remuneration distribution system of the factors involved in the production process. Indeed, despite market failures, when the price of traded goods reflects the real cost of the factors involved in their production and distribution we may assume that there is an efficient allocation of remuneration and resources, and international trade is consequently helping in spreading this achievement. This tends to promote the exploitation of natural resources wherever their productivity is the highest and, consequently, where their economic exploitation takes the lowest toll on the environment. Market failures, which could only be addressed after removing intervention failures, are responsible for externalities that are not taken into account and internalised (i.e. overuse or degradation of natural resources to which access is "free"). Actually, the price formation mechanism determines the appropriate retribution of each remunerated factor involved in the production process (i.e. land and other natural resources to which access is not free), but falls short with those other factors (i.e. air or water) to which access is normally beyond property rights (or there is a vacuum in regulation or enforcement).

8. Nevertheless, an incorrect governmental policy could make things even worse. For instance, if a subsidy were to "create or exacerbate market failures" (i.e. an "intervention failure" in OECD terms), we would be confronting an accumulation of errors. An "intervention failure" (i.e. a subsidy or a tariff escalation scheme) which resulted in lowering the remuneration of a factor beneath its reproduction cost (in the case of renewable resources), or its replacement cost (in the case of non-renewable resources) would be responsible for causing the over-exploitation of the resource in question. International trade would transmit this price distortion, acting as a vector that multiplies and spreads the negative environmental effects of this inefficient allocation of resources, namely those resulting from agricultural subsidies.

---

<sup>1</sup>OECD, *The environmental effects of trade*, Paris, 1994, page 8.

9. For instance, supposing a country subsidises the use of a fertiliser (that is normally considered a substitute for the factor “land”) to the point that the remuneration of the “land factor” in the composition of the crop in question is altered. As, in the cost breakdown of this particular crop, the land factor is highly relevant, the alteration will affect the price of the crop. If this country is also a large producer and has sufficient capital to maintain this policy over an extended period of time, its “intervention failure” will end up affecting international prices for that crop, and will thus force producers located beyond its jurisdiction to adopt one of the following alternatives: either they, too, will have to apply equivalent subsidies (assuming that they have sufficient financial resources to do so) or, conversely, they will have to cut back on the remuneration of the “land factor”, thus causing the resource to be over-exploited, or else they will just have to abandon the market. Those producers located within the market paying the subsidy will be encouraged to increase their use of fertiliser, with all the environmental disadvantages it implies, such as pollution of the ground-water, waterways and coastal zones.

10. Unfortunately, those producers located outside the subsidized market, which have been forced to lower the prices for their crops, also are “encouraged” to adopt environmentally damaging practices (over-exploiting land, abandoning crop-rotation methods, using marginal land for crop-growing or turning their attention to cultivating other crops for which their land is less well-suited). If these happen to be located in a developing country, or any other country without the possibility of matching this irrational use of abundant capital, they will simply have to migrate to urban conglomerates, which has obvious negative, social and environmental consequences.

11. This unfortunate situation has been widely recognised by international organisations which cannot be considered biased against high income countries. “Agricultural policies in some OECD Member countries have had certain negative effects on the environment and sustainable development, for example, to distort world agricultural trade patterns, depress returns to developing country and other exporting country producers, inhibit badly needed investments in agriculture, and contribute to the spread of low-yield farming and ranching into ecologically vulnerable tropical forests.”<sup>2</sup>

12. This may not be the case of governmental policies applied by developing countries that are not capable of distorting price formation systems and that are aimed at supporting traditional agriculture and farming. In developing countries the income effects of policies may be as significant as the relative price effects. If producers react primarily to income constraints then requiring that they internalise environmental costs may exacerbate environmental problems. For example, increasing the cost of fertiliser may lead to the abandonment of farms, deterioration of land, and greater overcrowding of cities.<sup>3</sup>

13. Conversely, in developed countries, the internalisation of environmental externalities is, in large part, a matter of “getting the prices right”<sup>4</sup>. Far away from this, governmental policies applied by large producers, which, due to their abundance of capital, can maintain this irrationality over an extended period of time, virtually export this environmental distortion to international markets. It should also be clearly stated that by no means can this argument lead to the conclusion that the problem can be solved by applying additional trade restrictions and countering the subsidies, even though this is what unfortunately happens, triggering subsidy wars

---

<sup>2</sup>OECD, “Trade, Environment and Development Cooperation,” OECD/GD(95)7, Paris, 1995, page 12.

<sup>3</sup>Larry Karp, *et. al.*, “Internalization of Environmental Damages in Agriculture,” Department of Agricultural and Resource Economics, University of California, Berkeley, UNCTAD/COM/53, 25 April 1995, page 4.

<sup>4</sup>Karp, *Ibid.*, page 4.

among the major exporters.<sup>5</sup> These additional trade distortions, apart from generating a negative spiral for the entire international trade system, do little to isolate the phenomenon, specially when such “intervention failures” are exported by major producers.

14. Moreover, “the ability of developing countries to internalise environmental costs is affected by the conditions under which they are able to export their products. Developing countries facing trade restrictions in external markets will have fewer resources to devote to the environment. Tariff and non-tariff barriers to imports from developing countries, particularly on labour-intensive, semi-processed goods in which developing countries have a comparative advantage, can have harmful effects on the ability of developing economies to implement sound environmental policies. Such protection can inhibit economic diversification into more sustainable activities, delay entry into the export-oriented processing industries which are most accessible to developing countries, and force producers of natural resource-based commodities to become over-dependant on these unprocessed commodities for export earnings.”<sup>6</sup>

15. Consequently, trade restrictions and distortions, namely subsidies and tariff escalation schemes which affect commodity pricing pose serious environmental threats, whose consequences go far beyond the local environment. Three economic reasons ground this assertion: (i) As commodities are at the bottom of the productive chain, a distortion in the way their prices are formed has a potential effect on the supply of products for which they are used as an input. (ii) Given the cost structure of commodities, any distortion in the valuation of the environmental factor has a considerably higher relative effect than an equivalent distortion would have on the cost structure of a manufactured product. (iii) Given the fungibility of commodities (easily comparable products), any distortion created by a subsidy is immediately transferred to the international price-formation systems, which means that its possible negative environmental effects are easily projected through international trade.

#### (ii) Factual background

16. There is plenty of evidence to sustain the existence of a negative relationship between distorting commodity pricing and the environment. Regarding the local environmental consequences of these distorting practices, there is not much to add to what has already been recognised by government officials of those countries which subsidize, as well as by several international organizations. For instance, concerning what is possibly the cornerstone of the agricultural trade distortion panoply, in recent studies published by the OECD it has been recognised that the Common Agricultural Policy (CAP) of the European Union “encourages excess production in the subset of commodities receiving this support; this excess production reduces the diversity of cropping practises on-farm, and encourages continued planting of crops with reduced rotations. Export subsidies and import levies are necessary to insulate the EU from foreign competition [...] extremely high levels of fertiliser and chemical inputs are applied,<sup>7</sup> the

---

<sup>5</sup>The USA’s EEP “was designed to counter the export subsidies of the European Union and other countries, regaining US competitiveness in international markets”. See “Competitiveness and Environmental Quality: The Role of Export Subsidies”, Susan Leetmaa, Barry Krissoff (Economist at the Economic Research Service, USDA) and Monika Hartmann (Co-Director of the Institute of Agricultural Development in Central and Eastern Europe), paper provided by the USTR office in Geneva.

<sup>6</sup>OECD, “Trade, Environment and Development Cooperation,” OECD/GD(95)7, Paris, 1995, page 11.

<sup>7</sup>Figures are extremely clear. Fertilizer use increased 550 % in the EU most important agricultural production countries (France, Germany, the UK, Italy and the Netherlands) between 1951 and 1989, while pesticide use increased 20 to 125 % between 1975 and 1988, according to the OECD. See Szmedra Philip, “Agriculture and the Environment in the European Union, *Agriculture Information Bulletin* Number 708, United States Department of Agriculture, page 1.

demand for which is derived in part from the levels of subsidy paid to output.”<sup>8</sup> The Food and Agricultural Organisation (FAO), at its 16th Regional Conference for Europe, identified four major environmental problems resulting directly from European agricultural production:

- pollution and contamination of soil, water, air and food resulting from increased agrochemical use and livestock effluents;
- degradation of natural resources, and particularly, deterioration in the quality of soil, water, forests and traditional rural landscapes;
- disturbance and reduction of biotopes and wildlife habitats; and
- reduction in wildlife species and loss of biological and genetic diversity.<sup>9</sup>

Encouragingly, high ranking EU governmental officials seem to be aware of the problem, at least concerning its local effects.<sup>10</sup>

17. In the United States, pricing and income policies are also encouraging intensive cropping: “in the U.S. deficiency payments are based on base acreage. [...] Once base acreage is established, farmers must continue to plant program crops to maintain their eligibility to receive deficiency payments. Consequently, farmers have little incentive to experiment with crop rotations that may be more environmentally friendly.”<sup>11</sup> “Input subsidies, which reduce the cost of chemicals, irrigation, or credit, can also have negative environmental effects. Subsidized chemical prices can encourage chemical overuse, which can lead to surface and groundwater pollution, soil contamination, eutrophication, reduced soil fertility, food contamination, and human exposure to chemicals. Overuse or improper use of irrigation can lead to salinization of water and soil, increased nitrate pollution of groundwater, depletion of water supplies and contributions to water logging, soil erosion, and landscape degradation.”<sup>12</sup>

18. Regarding the non local environmental consequences of agricultural trade distorting practices, there is also much to be said. “Production based on support policies not only acts against the environment of other countries in which it is applied but also hurts the environment of other countries by creating distorted markets. For example, subsidized prices reduce the possibilities of selling competitive goods (such as sugar) in the world market and force certain countries to allocate more land to produce that crop in order to boost production and maintain the export earnings necessary to meet their individual balance of payments requirements.”<sup>13</sup> For instance, the Royal Society (UK) for the Protection of Birds,<sup>14</sup> has been studying the case of

---

<sup>8</sup>Ford Runge, “The environmental effects of trade in the agricultural sector,” in OECD, *The environmental effects of trade*, Paris, 1994.

<sup>9</sup>Runge, *Ibid.*

<sup>10</sup>“Intensive agriculture had led to over-exploitation of the soil that cannot be sustained indefinitely,” Franz Fischler, EU Agricultural Commissioner, *Financial Times*, 29 September 1995, “EU transition entry span of 7-10 years envisaged”.

<sup>11</sup>Barry Krissoff, Nicole Ballenger, John Dunmore and Denice Gray, “Exploring linkages among Agriculture, Trade and Environment: Issues for the Next Century,” Natural Resource and Environment Division, Economic Research Service, U.S. Department of Agriculture. October 1995, page 25.

<sup>12</sup>Krissoff, *et. al.*, *Ibid.*, pages 25 and 26.

<sup>13</sup>Carlos Sersale di Cerisano, “The environment and International Trade: Implications of Protectionism,” North South Center, University of Miami, *Difficult Liaison: Trade and the Environment in the Americas*, Miami 1993.

<sup>14</sup>Royal Society for the Protection of Birds, “Memorandum of Evidence to the House of Commons Environment Committee Inquiry on World Trade and the Environment,” London, February 1996.

international beef trade and the problems of grassland conservation in Argentina, which are “very important for many species and are farmed by a system of extensive cattle ranching”. Their study states that: “EU beef export subsidies, combined with restricted market access to Europe, are leading to reduced beef profitability in Argentina, and the transformation of marginal grasslands to eucalyptus plantations or cropped lands. Beef production in core producing areas in Argentina is probably intensifying, with all the usual attendant environmental problems.”

19. Moreover, “beef production in the EU is becoming more intensive. This is stimulating the market for soya, including the transformation of lowland tropical forests in countries such as Bolivia and Brazil to soya growing. Earlier over-production of EU beef caused problems for developing countries when the surplus was dumped in sub-Sahel markets.”<sup>15</sup> Actually, according to the African Development Bank, the EU exported 120,000 tones of meat to sub-Saharan Africa in 1991.<sup>16</sup> Ministers and officials from Mali, Cote D’Ivoire, Burkina Faso, Benin, Niger, Togo and Ghana, major meat producers and consumers in the region, took part in a West African conference in Abidjan in August 1994, and complained that the “dumping of cheap beef from Europe continues to pose a problem to the development of the cattle industry in the sub-region”.<sup>17</sup>

20. Again according to the cited African Development Bank report, the EU has almost a monopoly of meat supply (90%) in west and central Africa, “through a subsidy mechanism instituted in 1968”. In recent reports, also the FAO condemns the dumping as “it is destroying the only means of survival for Sahelian countries.”<sup>18</sup> This kind of trade distortion has undoubtedly negative effects which go far beyond trade itself. Food security is affected, income and social stability are also affected, and the environment is definitely damaged. People who are expelled from traditional ways of ranching find other means to live. Cropping firewood, overcrowding cities, hunting endangered species, are simply illustrative examples. The threat posed by this kind of trade distortion, due to over abundant and irrational use of capital, goes even further than beef production. For instance, “although most West African countries are unable to grow wheat, or only at a high cost due to an ‘unfavourable climate’, wheat imports are supplanting traditional coarse grains, such as millet, sorghum and maize because despite import duties wheat is still cheaper for urban consumers”.<sup>19</sup>

21. Concluding, and drawing on OECD studies,<sup>20</sup> trade measures applied to protect domestic supply have caused a “misallocation of agricultural resources and disincentives for the adoption of certain environmentally favourable technology and practices (e.g. lower input of fertilisers and pesticides). Thus, in some countries agricultural production exceeds the natural carrying capacity of the environment, while in others natural resources suitable for farming or husbandry are under-utilised.”

---

<sup>15</sup>Royal Society for the Protection of Birds, *Ibid.*, pages 12 and 13.

<sup>16</sup>“Trade: Stop beef -dumping appeal to EU,” International Studies and Research Unit for Trade Information Management (CINERGIE), *South North Development Monitor*, 31 August 1994, Geneva.

<sup>17</sup>“South North Development Monitor,” *Ibid.*

<sup>18</sup>*Ibid.*, page 10.

<sup>19</sup>“EU what subsidies hurt African farmers,” Peter Blackburn, *Reuters*, Brussels, 22 November 1994.

<sup>20</sup>OECD, “Agricultural and Environmental Policy Integration: Recent progress and new directions,” Paris, 1993, page 18.

## II. IDENTIFICATION OF POSSIBLE SOLUTIONS

22. Environmental Ministers of the OECD have “underlined the need for governments to identify and eliminate those subsidies, taxes or other market interventions that distort the use of environmental resources, thereby impacting adversely on environmental policy objectives [...] getting the price right for raw materials”.<sup>21</sup> In fact, if high income countries removed this panoply of trade restrictions and distortions, prices “would get right”, which in economic terms means that private marginal cost of production would be in line with market prices. This is a minimum threshold necessary to undertake environmental intervention policies. It has been argued that trade reform could simply lead to a reallocation of production, hence offsetting the environmental benefits obtained in those countries in which prices would decline (relative to pre-reform levels), with an increase in production, both extensive and intensive, in those other countries which would see domestic prices increase.

23. There is no evidence to sustain this. Moreover, there is sufficient ground to argue that a reduction in rich industrial countries agricultural profitability would render two immediate environmental benefits:

a) Domestic environmental benefits: would streamline a reallocation of farm labour and capital “to the relatively unpolluting services sector or in industrial activities which for the most part already have environmental protection policies in place. [...] In practice, however, little land would be taken out of agriculture: its supply is much less responsive to changes in the changes in the aggregate price of farm products than is of capital or labour to agriculture. As a consequence, most of the change in farm product prices is captured in the price and hence rental value of farm land. Thus a price fall leads even in the short run to less use being made of land substitutes”.<sup>22</sup>

b) Overseas and Global Balance Environmental Benefits: would result from the reallocation in those developing countries where food production would expand, of “capital required for that expansion [which] might otherwise be employed in smokestack manufacturing or mining activities, [that] could well be more pollutive than farming at the margin if adequate environmental protection policies are not in place and enforced in those industries”.<sup>23</sup> Besides, rural workers would otherwise “be eking out a subsistence income by squatting on marginal hillsides [...] and] increased value of rural labour would raise the real price of wood for fuel<sup>24</sup> [...] and] cleaner fuels such as kerosene would then be used more and forests would be depleted less.”<sup>25</sup>

24. Moreover, deforestation is unlikely to occur for the stake of expanding the area for farming. Empirical studies made in Argentina “suggest that land area is by far the least responsive factor to changes in far output prices. At least in Argentina, a 10% permanent increase in the real price of agricultural products would cause the area farmed to have increased

---

<sup>21</sup>OECD, *Ibid.*, page 16.

<sup>22</sup>Kym Anderson, “Agricultural Trade Liberalization and the Environment: A global Perspective,” *The World Economy*, January 1992, (vol. 15, no.1), pages 155 and 156.

<sup>23</sup>Anderson, *Ibid.*, page 156.

<sup>24</sup>According to ITTC figures, more than 80% of the wood produced in developing countries is used as fuel.

<sup>25</sup>Anderson, *Ibid.*, page 156.

by less than 5 % even after two decades (compared with increases in farm labour and capital equipment use of 15 and 18 %, respectively).”<sup>26</sup>

25. As a general concept, the following trend has to be remarked: “The more lightly populated a country, the lower its price of farm land, *ceteris paribus*, and hence the less use it would tend to make of environmentally damaging farm chemicals and other land substitutes per unit of output. Such land substitutes are unlikely to have an adverse environmental impact until they reach a certain threshold per hectare, and even after that their adverse effects would be minor at first and then gradually increase exponentially. For that reason the relocation of production from more to less-densely populated countries would, *ceteris paribus*, tend to reduce the use of farm chemicals and intensive feeding of livestock in global food production even if liberalisation led to farm product prices being equalised around the world.”<sup>27</sup>

26. This is quite a familiar conclusion for the WTO. Indeed, in the GATT 1990-91 *International Trade Report* it is stated: “It is not unreasonable to conclude from such evidence<sup>28</sup> that the positive environmental effects of the decline in the use of chemical inputs in the high income countries are likely to be substantially greater than the adverse environmental effects of the increased use of such inputs in the low income countries following a liberalisation of world food trade. In other words, these several findings point to the conclusion that existing agricultural protection not only fails to help the environment, but almost certainly is an important source of environmental degradation.”

27. Finally, we are by no means trying to suggest that food trade liberalisation is sufficient to guarantee sustainable agriculture. Argentina, as stated in previous meetings of the CTE is keen to jointly undertake further agricultural trade liberalisation and sustainable agricultural practices. Nevertheless, doing away with trade restrictions and distortions that negatively affect, not only the earnings of agricultural producers, particularly those located in developing countries, but also environment, is a necessary and essential condition that will open the possibility of improving agricultural practices world-wide.

### III. PROPOSAL FOR FURTHER ACTION

28. Recently, regarding farm policy reform, a high ranking EU official stated on this matter: “the important thing is to have a public debate and establish a consensus before 1999”.<sup>29</sup> We agree. There is an urgent need to promote this debate in order to lay the groundwork for further fundamental reform of the sector.

29. The CTE should contribute to this debate, ventilating the environmental benefits that are hindered by existing trade restrictions and distortions in agricultural trade. Despite some progress made in the Uruguay Round, agricultural trade and practices are still highly distorted by support and protectionist policies. Therefore, the analysis of the environmental consequences that existing trade restrictions and distortions in agricultural trade are responsible for has to continue.

---

<sup>26</sup>Domingo Cavallo, “Agriculture and Economic Growth: The experience of Argentina 1913-1984”, in *Agriculture and Governments in an Interdependent World*, A. Maund and A. Valdes (eds.), London, 1989 (cited by Anderson, *Ibid.*, page 166).

<sup>27</sup>Anderson, *Ibid.*, page 157.

<sup>28</sup>Particularly referring to Anderson *op. cit.*. See “Trade and the environment,” GATT, *International Trade 1990-91*, Geneva, 1992, page 37.

<sup>29</sup>“EU has four - year ‘window’ for farm policy reform,” quoting Mr. Russell Mildon, Director of International Affairs Relating to Agriculture, *Financial Times*, 7 February 1996.



30. Consequently, we believe that a balanced Report of the CTE should include a clear acknowledgement of:

- a) the negative environmental consequences, due to trade restrictions and distortions in agricultural trade; and
- b) the need to feed the fundamental, ongoing reform process of the sector, looking forward to producing environmental benefits.

31. On this basis, the CTE has to be mandated to develop a work programme on the identification of ways and means to reduce/eliminate the environmental damage due to trade restrictions and distortions in the agricultural sector, as a contribution to future negotiations agreed upon by the WTO Agreement on Agriculture.