WHY IS AGRICULTURAL POLICY STILL SO DIFFICULT TO REFORM?
Jonathan Brooks, Directorate for Agriculture, Food and Fisheries, OECD

1. Why is agriculture in need of reform?

In many OECD countries, the basic structure of farm programmes has changed little for several decades. The original motivations for these programmes included the need to support rural incomes during the depression of the 1930s and the desire to boost agricultural production in the aftermath of the Second World War. The needs of farm policy in the 21st century are very different, but in many cases the basic mechanisms of support remain the same. Agricultural policy has tended to accumulate and to be revised at the margin – radical overhaul has been relatively rare.

In 1986-88, total transfers to the sector, as calculated annually by the OECD, cost consumers and taxpayers USD 298 billion, representing 2.3% of GDP. In 2002, the corresponding figure was USD 318 billion, or 1.2% of GDP.¹ Three-quarters of these transfers are provided as support to farmers, accounting for one-third of their gross receipts, with general expenditures on items such as research, marketing and infrastructure accounting for the rest. There has been some shift away from market price support and payments based on output or input use towards budgetary payments that are less linked to production, but overall, output and input-related measures still account for three-quarters of all support.

However, the vast majority of agricultural policies in OECD countries fail to address their purported objectives efficiently. The stated objectives of farm policy fall into two categories: those concerned with the incomes of farm households, and those designed to address other societal concerns such as the environment, the provision of rural amenities, land and water management, food safety and food security. In each case, governments justify their policies on the grounds that private markets alone may not lead to optimal outcomes.

Yet the majority of policies fail to correct clearly identified market failures, or to raise the welfare of farm households, in an efficient or equitable manner. With respect to household incomes, OECD work has shown three things very clearly. First, that there is no evidence that farm households have systematically lower incomes than other households, so policies to support incomes across the whole sector are unnecessary. Second, sector-wide policies are highly inefficient at transferring income to farmers. In particular, only about one-quarter of the value of market price support translates into additional household income with much of the increase in receipts paid back out to input suppliers or capitalised into land values. Third, that when support is linked to output the distribution of that support is heavily skewed towards larger (and typically richer) farmers. Yet despite these well documented policy failings, approximately two-thirds of all support is provided through sector-wide policies that support prices to all producers at higher levels than would otherwise prevail. Furthermore, these same instruments which fail to address domestic objectives also cause the greatest harm in terms of international trade distortions.

¹ This sum is approximately twice the value of all developing country agricultural exports to OECD countries, and six times the value of ODA. The latter ratio is routinely brought up in discussions of coherence with respect to developing countries.
OECD Ministers have recognised the need for fundamental reform, and in 1987 agreed on a set of principles for reform based on the notion of “market orientation”, principles which have been periodically reaffirmed over the past 16 years. Yet reform in practice has been slow and piecemeal, and in many cases the underlying commitment to agricultural commodity programmes has not been questioned. The relative lack of progress highlights the need to think not just about the case for reform, but also about why reform has been difficult to achieve, and how reform might be put into practice.

2. Why has reform been so modest?

The gathering weight of evidence that agricultural policies fail to meet their stated objectives efficiently (much of it produced by the OECD Secretariat) has in many cases failed to elicit fundamental change. Why has reform been so intractable? A major reason must be that there is a gap between the officially articulated objectives of agricultural policy, and the implicit priorities of policymakers, who often feel obliged to respond to political imperatives.

The political implications of structural change in agriculture go some way to explaining the persistence of inefficient and inequitable support policies. With economic development, incomes increase and consumers spend a smaller share of their budgets on food. Thus whereas consumers in developing countries typically spend about half their income on food, the figure for OECD countries is around 15 percent. Increasingly, consumers are “rationally ignorant” that they are paying more for their food than necessary – i.e. it is not worth the effort of becoming informed.

On the supply side, competition leads to productivity growth, which in turn stimulates supply. The combination of supply and demand effects means that agriculture has become a “declining” industry (i.e. a successful one). Many developing countries have over half their workforce employed in agriculture, whereas the share in OECD countries is typically around 3%. Thus a given transfer to producers imposes a progressively smaller burden on the overall economy. Also, the competitive process, which puts pressure on less efficient farmers, increases those farmers’ incentives to seek government support.

At the same time, the decreasing size of the agricultural constituency increases the scope for collective action by farmers. This is because farmers have fewer incentives to “free-ride” on the benefits of lobbying by other members, as larger per capita gains can be achieved, organisational costs are likely to decrease, and “shirking” on political activity among members becomes easier to monitor and control.

These factors explain the obvious asymmetry that, for example, sugar producers are more likely to protest against the removal of support than sugar consumers and/or taxpayers are likely to mobilise in favour of it. However, the reasons for the political imbalance go further than straightforward economic incentives. If policy-makers respond to these political pressures, then they are put in the position of having to defend existing policies. One way of doing this is to claim that the policies being pursued are in fact consistent with stated policy goals. This can introduce “noise” into the public debate and prevent objective economic analysis from registering.

An important manifestation of such “noise” is the exploitation of an agrarian ideology that emphasises the moral richness and cultural contribution of family farming. Of course, every country is entitled to hold its own social values. The problem arises when these values turn into myths. Agrarian myths include the misrepresentation of the nature of modern commercial
agriculture, and the suggestion that current agricultural policies serve to uphold fundamental social values.

Agricultural interests can exploit agrarian myths to generate public support for existing programmes and to forge common links around otherwise unrelated narrow policy benefits. Political pressure can then lead politicians to collude in propagating agrarian myths. Once politicians are lured by the support of vested agricultural interests, they too have a stake in ensuring that the public is convinced of the agrarian worth of their policy actions.

The political economy / public choice perspective can also explain some policy nuances. For example, whereas farmers tend to become more politically influential as their numbers diminish, larger groups are nevertheless more effective if they can overcome the obstacles to collective action. Complex policies can reduce the incentives for free-riding, which may explain why the dairy sector – where programmes often vary by region, or by some other factor that divides sectoral interests (such as quota allocations) – is relatively highly protected.

The institutional environment can also influence the process of policy formation. In some cases, agriculture ministries can come to see themselves as defenders of farmers’ interests, and their role to involve claiming the maximum possible budget for their activities. When decisions are made at the supra-national level, as in the European Union, individual countries may also have an incentive to expand their share of a collectively agreed upon budget. If a country receives more than it pays in, this can limit the incentives for restraint.

Economic analysis, ideology, political pressure – and even nostalgia – all feed into the process of agricultural policy formation, making it difficult to infer which motive dominates any particular policy decision. Nevertheless the failure of agricultural policies to address legitimate economic and social objectives in an efficient manner implies that the root cause of current support policies must be seen as political.

3. How is the political balance evolving?

As economic growth continues, the forces outlined above continue to operate, and it becomes ever easier for OECD countries to waste money on agricultural policies. In addition, domestic and trade policies have tended to become ever more complicated, which further increases the incentives for rent-seeking by organised interests.

Against this, some of the traditional myths about agriculture are gradually being eroded, partly because of health scares such as BSE and concerns about the effects of biotechnology on food safety and the environment, but also because some of the trade-offs between the interest of developed and developing countries are being brought into sharper relief, notably in the more protected sectors such as sugar, dairy and cotton. However, there is also a danger of new myths taking hold, including those associated with biotechnology and the anti-globalisation movement.

A further reason for believing that the log-jam over agricultural policies can be broken is the increased cohesion of developing country interests, manifested by the emergence of the G22 group in Cancún. This grouping of countries has a diverse set of views about the benefits or otherwise of liberalising its own farm policies (with India for example tending to be more protectionist than Brazil), leading some observers to question whether it can survive. But the popular convention to insist on the “heterogeneity” of developing countries may hide a deeper truth. It is true that some developing countries have relatively high incomes while others are very poor, some are net exporters while others are net importers, some benefit from trade preferences
while others do not, and so on. Yet all developing countries would benefit from greater access to OECD country markets, and all worry about the effects of liberalisation on poor farmers in uncompetitive (import-competing sectors).

Indeed, the defence of current agricultural policies in some OECD countries on the grounds that reform would hurt food importers and lead some exporters to lose their preference margins may become less tenable, as these “losers” become more aware that trade preferences and subsidised imports are poor ways of fostering long-term development, and that there are potential mechanisms within a WTO framework for smoothing the transition to more productive activities, and offsetting short to medium-term losses.

4. What does this imply for OECD work?

The OECD Agriculture Directorate’s programme of work traditionally has involved evaluating the performance of agricultural policies in attaining their explicit (i.e. stated objectives). Thus, among other things, the Secretariat has undertaken studies looking at the distribution of support (does support go to poor farmers?), the efficiency of support programmes (how much of that support translates into additional household income?), and the effects on the environment (are support policies beneficial or harmful?).

There is a continued need for such work. But as the evidence that current policies are ineffective in attaining explicit objectives becomes overwhelming, there is also a need to think in terms of the implicit objectives – i.e. to consider the causes of policy as well as the consequences. The question of how reform can be facilitated is in fact to be analysed within the current programme of work, and a political economy perspective suggests a few factors that may be important.

First, it is clear that compensation can ease the process of reform. In the United States, the 1996 FAIR Act involved a switch towards less market distorting forms of assistance. But the return to more coupled instruments under the 2002 Farm Act highlights the need to think not just about compensation but even more importantly about effective adjustment assistance. If people can be helped into more remunerative activities (in or out of agriculture) that are not only good for them, it also makes it less likely that they will make demands for protection at some point in the future.

For similar reasons, it is important that policies be simplified. Market price support sounds like a simple policy, but the historical experience has been that it requires a range of other instruments to keep it in place, both at the border (e.g. tariffs, tariff-rate quotas, export subsidies) and internally (e.g. production controls). Transparent payments for the provision of identifiable public goods, or as an income safety net, may have more administrative requirements, but if everyone is treated equally the incentives for rent-seeking should diminish.

OECD work has demonstrated that a significant share of farm support is capitalised into asset values, including farmland and other sector-specific investments. Hence there is also a need to look beyond direct income effects when considering the implications of reform, and take account of the impacts on non-farming landowners, quota holders or industry suppliers.

Finally, it is essential to look beyond the immediate interests of OECD countries and take a global perspective. It is natural that OECD member countries’ concerns should be at the heart of OECD work, but some issues that have assumed high importance (such as the “multifunctionality” of agriculture) have had little resonance at the global level. At the same time, work on how OECD country policies affect developing countries has, until fairly recently, received relatively less attention and funding.
The OECD’s assessment of the Uruguay Round Agreement on Agriculture was relatively upbeat, describing the Agreement as a “watershed” in that agriculture was finally brought under the auspices of WTO rules, despite the fact that it left high levels of support and protection intact. However, that optimistic assessment was predicated on the assumption that, having established a system of ground rules, the next round would tackle protectionism more forcefully. The tough stance taken by several OECD countries in the run-up to Cancun, with the EU/US joint proposal offering no elimination of export subsidies, and the US refusing to scale back its subsidies to cotton farmers, suggests that this optimism may have been misplaced.

With countries’ positions in danger of becoming even more entrenched, there is a need for greater openness in acknowledging the importance of political factors in the decision-making process. Such openness could (hopefully) foster a climate in which countries are willing to share and discuss their national policy-making experiences with a view to discovering the kinds of circumstances and initiatives that can make reform more palatable.