ALTERNATIVE TRADE POLICIES: THEIR IMPACT ON U. S.
AND WORLD PRODUCTION AND TRADE

by D. Gale Johnson

I. Introduction

It is not now possible to discuss alternative trade policies without discussing alternative domestic farm policies of the major trading nations. In a sense it has never been possible to entirely divorce the domestic and international aspects of national measures affecting agriculture.

For centuries governments have attempted to influence the development of agriculture through the control or direction of international trade. Import duties, quotas and embargoes and export subsidies have an ancient and almost uninterrupted history in the major nations of the world. Free trade in agricultural products, as practiced by the British after the abolition of the Corn laws, has been the exception rather than the rule.

But compared, say, to the end of the nineteenth century, the interconnection between trade and agricultural policies are now much more intimate and all pervasive. Trade restrictions and inducements are now only one of the numerous tools in the policymaker's kit. And perhaps most important, trade interference is now largely determined by or accommodated to a whole series of domestic interventions in the markets for agricultural products. At one time it was possible to negotiate on tariff rates on agricultural products without becoming involved in a complex set of national legislation and administrative actions. Now a negotiation about variable levies is a negotiation about the level of price supports in the European Economic community or a negotiation about U. S. trade restrictions on peanuts is a negotiation about the U. S. program of acreage allotments and price supports for peanuts.

It is not difficult to determine why these interconnections have become more direct and complex. Most governments of industrial countries have accepted the responsibility for reaching certain income objectives for their farm populations. A nation can have such objectives -- and pursue and attain them -- without interference with international trade. However, most nations are attempting to achieve their farm income objectives primarily by influencing, that is increasing, farm product prices. It is the use of the price system to achieve income objectives that necessitates

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import restrictions or export subsidization. No nation can long afford to increase the world price for an important commodity; sooner or later some means for separating domestic and international prices must be resorted to.

If any important trading nation or area relies upon higher farm product prices as a means of achieving farm income objectives there are certain obvious effects upon international trade. First, domestic output is encouraged. If the country is an importer, this means that less will be imported; if the country is an exporter, this means that more will be exported. Either of these consequences limits the export markets for third countries. Second, unless deficiency payments are used, domestic consumption is reduced. Again, if the country is an importer, less will be imported; if the country is an exporter, more will be exported.

It is often argued that the response of either output or consumption to higher prices is relatively small and thus little weight should be given to such effects. It is true that in the richer countries people tend to vary quantities purchased of farm products very little as prices change. But this, by itself, is not an adequate indicator of the effect of high consumer prices on the amount of product imported or exported. If before a price increase imports accounted for 20 per cent of a nation's consumption of a product, the percentage effect of the price increase on imports would be approximately five times the percentage effect on national consumption.

The same "multiplier" effect occurs as a result of output increases due to higher prices. A given percentage increase in production in importing countries can have a much larger proportional effect on quantity imported; the same statement applies to the effects of increased production in exporting countries upon the change in their exports.

The consumption and output effects of higher farm product prices are additive and this is true whether a nation is an importer or an exporter. Thus even if demand and supply are both quite inelastic in a given nation, the impact upon the volume of foreign trade can be significant.

This has been a long introduction to make a rather simple point, namely, that if governments use manipulation or support of prices received by farmers as the means of meeting income objectives, modifying trade policies require modifying domestic farm programs. While the point is a simple one, it is hard to overemphasize its importance. The point explains why the EEC has had so much difficulty in arriving at a common agricultural policy; it explains why there are so many tensions in the present round of trade.

\[2\] In more precise economic terms, the price elasticity of demand is very low.

\[3\] Thus if the price elasticity of demand were \(-0.2\) and the price increase were 20 per cent, national consumption would decline by 4 per cent. Imports, assuming no change in local production, would decline not by 4 per cent but by 20 per cent.
negotiations when the problems of agricultural trade are under discussion. And the above discussion also indicates why exporting nations are legitimately concerned with the domestic agricultural policies of other countries, whether those countries are importers or exporters.

There is one other point of an introductory nature that merits attention. There exists quite different views concerning the effects of U. S. farm programs upon our farm output. Officially we have taken the position that our acreage allotment and other governmental programs have restricted total farm production. There is a great deal of skepticism about this conclusion by other governments. Until we conduct the sophisticated and detailed studies that can determine whether the aggregate effect of all of our governmental programs has been to restrict total output, we are not likely to convince others that they have any responsibility for avoiding measures that encourage farm production. I feel that we have here a serious source of misunderstanding between the EEC and the U. S. And until this misunderstanding is cleared away we are not likely to make much progress in convincing the EEC and other major importing areas that they have an obligation not to encourage high cost agricultural production.

In the outline that was sent to me by the program organizers I was asked to discuss the following major topics:

1. Continuation of expanded trade -- effect on commodities
2. Selective import restrictions
3. Market-share doctrine based on rights established because of market development costs
4. The gains and losses from alternative policies

I shall restrict my comments to the above four topics.

II. Continuation of Expanded Trade -- Effect on Commodities

How much has agricultural trade expanded in the post World War II period? This is a seemingly simple question, but the answers are quite complex and differ for different commodities and different countries. Obviously in this chapter I can do nothing more than to indicate some of the differences that appear if one approaches the question from different viewpoints.

The volume of world agricultural exports increased by about 43 per cent between 1953 and 1963, when valued in 1957-59 average prices of U. S. imports or exports. It may be noted that the 1953 volume of world exports of agricultural products was approximately the same as the 1934-38 volume.

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4 Price supports, acreage allotments, conservation and acreage reserves, agricultural conservation program, soil conservation, small watersheds, irrigation and reclamation.
The increase in the value of world exports of agricultural products between 1953 and 1963 was less than 43 per cent since world export prices of agricultural products declined by roughly 5 per cent during the period.

The growth in exports of food and other agricultural products has been quite uneven. For example, between 1953 and 1960 the value of food exports changed as follows:

<table>
<thead>
<tr>
<th>Description</th>
<th>Per cent change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total world food exports, excl. exports of Eastern Trading bloc*</td>
<td>25.3</td>
</tr>
<tr>
<td>EEC to EEC</td>
<td>119.9</td>
</tr>
<tr>
<td>Industrial to Industrial</td>
<td>44.8</td>
</tr>
<tr>
<td>Non-industrial to industrial</td>
<td>6.2</td>
</tr>
</tbody>
</table>

* But includes imports of the Eastern Trading bloc

Of the $4,458 million increase in world exports of food, as defined, $2,522 million represented increases in trade among industrial countries and only $475 million from non-industrial to industrial areas. While the value of food imports of the Eastern Trading bloc was still small in 1960, the increase in value of exports by non-industrial countries to the bloc was $320 million during the period or about two-thirds of the increase in food exports to the industrial countries. The other large component of the increase in food exports was the increase of $807 million in exports from industrial to non-industrial areas. A large fraction of the latter increase was due to increase in food shipments by the U. S. under our various foreign aid activities.

A study made by the Food and Agriculture Organization of the changes in the value of world exports of the main agricultural products among the major regions between 1952-53 and 1960-62 is of interest in assessing the growth of trade. This study was concerned with broad world regional groupings -- Western Europe, North America, Latin America for example. Thus trade among nearby countries, such as trade between Canada and the U. S. or among the EEC members, was excluded. The increase in the interregional trade in agricultural products (not just food) was $3,283 million during the period. This increase may be described as follows: (1) The increase in the agricultural exports of the less developed countries was only $815 million; (2) the increase in commercial exports of the industrial countries was $1,097 million, and (3) the increase in the value of products made available as economic aid or surplus disposal by the U. S. was $1,371. It would appear that a very large fraction -- perhaps two-thirds -- of the increase in commercial exports was due to larger exports by the United States.
While I do not want to underemphasize the importance of trade among nearby countries, the above material indicates that the growth of agricultural exports from the less developed to the industrial countries has been very modest during the past decade and that much of the increase in inter-regional exports by the industrial countries has been captured by the U. S. And much of the increase in U. S. interregional exports has been in terms of economic aid and surplus disposal.

It is clear from all the available data that the increase in exports of agricultural products during the past decade has been much smaller than the increase in exports of industrial products. Excluding exports by the Eastern Trading bloc, world exports of agricultural products increased 32 per cent between 1953 and 1961 while the world exports of manufactured products increased 67 per cent.

The slower growth of trade in agricultural than in industrial products is what one would expect. In general the demand for agricultural products grows much more slowly than per capita income.\(^5\) In fact, for a number of farm products per capita consumption declines as per capita incomes increase.\(^6\) In most industrial countries it appears that food grain demand has this characteristic.

The relatively slow growth in international trade in agricultural products, especially in the exports of less developed countries, has been partially due to the tendency of industrial countries to provide increasing protection for their farmers. This increased protection has been associated with a decline in the share of the total food supply imported by Western Europe. Before World War II, Western Europe imported 31 per cent of its food supply; the region now imports significantly less than 25 per cent. U. S. imports of agricultural products have remained approximately stable in value terms for the past decade, while exports have increased by 60 per cent -- even more if the very high export level of 1964 is considered. Thus the U. S. has added very appreciably to the supply of agricultural products moving in international trade, but it has not added to the demand. Most of the stability in the value of our agricultural imports has been due to strictly economic factors -- demand growing more slowly than per capita income and declining product prices; but not all. We have clearly used trade barriers to restrict our imports of sugar, many dairy products and peanuts.

\(^5\) In economic terms, agricultural products have low income elasticities of demand.

\(^6\) That is, they have a negative income elasticity.
As population increases and real per capita incomes grow in most parts of the world, and especially in the industrial countries, international trade in agricultural products will continue to grow and perhaps at the recent rate of 2.5 to 3.0 per cent per year. Some of the important agricultural raw materials and beverages -- cotton, oilseeds, copra, tea, coffee and rubber -- are subject to relatively limited trade barriers. Increasing per capita incomes will probably result in increased international trade in feed grains and perhaps for some kinds of meat.

But a significant expansion in commercial international trade in agricultural products must await a reduction in barriers to that trade and a reduction in the degree of subsidization of agriculture in the industrial countries. If the industrial countries gradually dropped their protection of sugar, international trade would expand and real national incomes would be increased in both the importing and exporting countries. If the agriculture of Western Europe were given less protection and subsidization, international trade in wheat, feed grains, fruits, tobacco and poultry would expand significantly. If the U.S. provided less protection for certain parts of its agriculture, international trade in dairy products, peanuts, wool, fruits, vegetables and nuts would expand considerably.

III. Selective Import Controls

It is my opinion that the introduction of additional quantitative import controls -- whether "voluntary" or unilateral -- would be a serious mistake and should be resisted by all who are concerned with the maintenance of an efficient and prosperous U.S. agriculture. Certainly we cannot expect other nations to eliminate or reduce quantitative restrictions on the importation of agricultural products when we resort to the same technique. While much remains to be done in the elimination of quantitative restrictions, there can be no denying that substantial progress has been made in the last decade. In the face of this gradual progress, it is little short of tragic that we have resorted to voluntary import restrictions on beef, veal and mutton and certain dairy products and now have legislation providing for beef, veal and mutton import quotas under certain conditions. Even if the meat quotas provided in the legislation are never imposed, the legislation authorizing the quotas has been and will be a costly venture for us. The existence of the legislation, which I interpret to be inconsistent with our GATT obligations if applied, provides an excuse for others to resist our efforts to induce them to eliminate such barriers. Obviously we are not opposed to quantitative restrictions on principle; we are only opposed to such restrictions when it is in our interest. Or so at least will run the argument of our trading partners who have quantitative restrictions that they wish to maintain for domestic political reasons. For example, the domestic political reasons for France maintaining restrictions on the imports of fruit are undoubtedly as respectable and forceful as are our political reasons for providing import controls on meat.
Selective import restrictions -- under the guise of the euphemism, market sharing arrangements -- have gained some popularity in certain circles. It is sometimes argued that the greatest potential for maintaining or expanding our trade in certain farm products with the EEC is to negotiate a series of market sharing arrangements which would allocate a specific quota to imports, with this quota increasing as utilization grew as a consequence of increased population and income.

Such arrangements have the effect, if effective, of freezing the share of national consumption supplied by imports. Future changes in relative costs will affect the amount and flow of international trade only slowly and uncertainly, if at all. Would we have been willing to enter into such an arrangement with the EEC for feed grains in the mid-50's? We were then exporting about 2.1 million metric tons of feed grains annually to the EEC; by now a growth sharing formula might have increased our share to about 3.0 million tons. I doubt if anyone would now want to accept this figure as our negotiated share of the EEC market for imported feed grains. Even the imposition of very substantial variable levies on feed grains has not had the effect of reducing our feed grain exports to the level that we might have accepted had we negotiated a market sharing arrangement with the EEC in 1958.

When domestic political and economic pressures are strong enough, few nations can resist violating international economic agreements if such violation permits a solution, even a very short-run solution, of a domestic problem. The long inclusion of the escape clause in our reciprocal trade legislation was an open recognition of this fact. How much confidence could we have that freely and sincerely negotiated market sharing arrangements would, in fact, be observed in the face of farm income and price problems in the importing nation? Suppose that in a given year domestic output of feed grains equalled expected use in an importing country that had signed such an agreement. Thus the entire import quota would have to be stored or exported. If exported, the exporting nations signatory to the agreement have gained little or nothing. Are importing nations likely to incur the heavy storage costs that would be required if the imports were stored? Perhaps, but I doubt if we can have any certainty that such would be the case.

Negotiation of market sharing arrangements may turn out to be superior to any other alternative with which we may be faced. Nevertheless, I feel that we need to approach such agreements with caution and with recognition of the fact that enforcement of them may be nearly impossible.

IV. Market-sharing Doctrine Based on Rights Established Because of Market Development Costs

I find it hard, and I should say so at the outset, to take this idea seriously. The allocation of markets, either nationally or internationally, on the basis of market development costs (or should I say advertising costs?)
impresses me as a way to maximize waste and to minimize international good will. It is one thing for the United States to impress the Japanese with the desirability of U. S. wheat and then try through quality control of the product and effective pricing to retain the market developed; it is quite another for the Japanese to guarantee that if we spend ten times as much as the Canadians to develop or expand the Japanese market for wheat that we should from then on export ten times as much wheat to Japan as Canada.

One consequence of such an arrangement would be to enrich the Japanese or the German equivalent of Madison Avenue. What export nation could stand by while another nation was engaged upon a market promotion campaign if they knew what future market shares would depend upon costs incurred in developing the market? The only way to prevent wasteful expenditures would appear to be a cartel arrangement among the potential exporters -- an arrangement that would result in agreed market shares. Why not approach the matter of market share directly?

But assume that the above brief comments are beside the point and one takes the idea seriously. The administration of such a scheme would surely present a number of difficult problems.

One issue that would arise is how to handle the expenditures from P. L. 480 counterpart funds generated by our food aid program. Are the expenditures from these funds for market development and trade fairs legitimate and real expenditures made by the U. S. ? If we claim these to be real expenditures, do we then reduce our claims concerning the amount of foreign aid provided under the Food for Peace Program? Could the U. S. count some of the value of food or other agricultural products provided under Title I as market development costs? Who would decide what was a legitimate expenditure? How would the market development costs of various nations be compared? Would costs incurred by private firms in promoting branded products be included?

If the contribution of foreigners to the development of a market is to be used as the criterion for the allocation of import shares, the most appropriate claim for a given share would be the effect of the various promotional devices upon the development of the market. The use of costs is obviously a very imprecise guide and one chosen, presumably, because we have no way of measuring the effectiveness of market development programs.

I have so far interpreted this market-sharing doctrine in terms of allocation of shares in a volume of imports determined by any arbitrary rule. I suspect that the promulgators of this rule have something more in mind, namely that the total market -- including that supplied by domestic producers -- should be allocated in terms of relative market development costs. I find it hard to believe that any important nation would accept such a rule. Such a rule would guarantee foreigners a
definite claim against the growth of a market that was due to increasing population and rising per capita incomes. Does any one really believe that the recent growth in per capita meat and wheat consumption in Japan is due primarily to market development expenditures rather than to increasing per capita income and, in the case of wheat, the rationing of rice?

It is probably true that U. S. private and public efforts to introduce broilers into West Germany had some effect upon the growth of poultry consumption in that country. But was the contribution of these market development efforts so considerable and so certain that the costs of these efforts constitute a legitimate or reasonable claim for a share of German poultry market? Per capita poultry consumption in West Germany increased by 160 per cent between 1956 and 1961, but in the Netherlands -- an important poultry exporter where I suspect that we did not engage in market development activities -- per capita poultry consumption increased threefold. And in Belgium and Luxembourg the absolute increase in per capita consumption of poultry was almost half again as large as in Germany, though the relative increase was only 70 per cent.

I do not want to be misunderstood. I believe that poultry producers should receive the full support of the U. S. Government in obtaining access to the West German poultry market under reasonable conditions. They deserve that support because on the basis of price and quality they can deliver poultry to West Germany on terms that are fully competitive and because it is our national policy to promote trade to gain the advantages of international specialization. But I do not think that poultry producers have an ethical or economic claim to any part of the German poultry market because of expenditures on market development.

V. The Gains and Losses from Alternative Policies

Unless there is a significant modification of the trade and agricultural policies of the major industrial nations, we can look forward to only a modest absolute growth in the value and volume of commercial agricultural trade. With existing policies, Western Europe will continue to expand the relative importance of domestic production in total consumption. This trend is important, of course, to the major agricultural exporting countries such as Canada, Australia and the U. S. But this trend when combined with increased efforts on the part of the U. S. to expand agricultural exports through surplus disposal and the payment of subsidies on several important export products is of critical significance to the less developed areas of the world.

If the less developed areas of the world are to achieve the kind of economic growth envisaged in the Alliance for Progress, for example, these areas must be able to finance a significantly larger volume of imports of capital goods and related items for the investments in agriculture, industry, transportation and communication that are essential for rising per capita incomes. Except for the small part of the world
with petroleum or minerals to export, such areas must rely primarily upon export earnings from agricultural products to finance the required capital imports. The deliberate subsidization of agriculture by most of the important industrial nations clearly limits the export earnings from such areas.

Thus one of the important losses of the continuation of the trends in agricultural policies of the past 15 years, including trade policies, is the adverse effect that such policies have upon the growth rates of the poorer areas of the world.

A second loss that is and will be suffered by a failure to remove some of the impedients to an efficient allocation of agricultural production in the free world is the real loss in income suffered by the area. Western Europe is involved in encouraging high cost production of many agricultural products rather than exchanging industrial output for farm products on a much larger scale. But the U. S. is guilty of the same type of action. Recently we have encouraged the expansion of sugar production even though over the long run we could probably import our sugar requirements at about 60 per cent of what it is now costing us to produce it. Nor can our highly subsidized rice production be justified in terms of efficient use of our resources or the resources of the free world.

A third loss from the existing agricultural and trade policies is the barrier that these policies present in the path of achieving effective economic integration of the free world. The present round of trade negotiations are burdened by the high priority that most participants to those negotiations give to maintaining their current farm programs.

I do not believe that selective import restrictions or market-sharing arrangements such as those described earlier can do anything but to aggravate the losses described above. Such arrangements, in my opinion, will have the effect of contracting rather than expanding trade.

There are clearly substantial gains to be achieved by expanding economically justified trade in agricultural products. However, we must not make the error of assuming that any and every increase in trade is beneficial. Some of the increases in agricultural trade within the EEC has probably replaced products from relatively low cost sources by relatively high cost products. Some of our P. L. 480 shipments have displaced lower cost products by relatively high cost products from the U. S.

But it is all too clear that it is not going to be easy to achieve the modifications that are required before international trade in agricultural products will both expand and be redirected to permit demands to be met by relatively low cost producers. To achieve these ends require substantial modifications in the agricultural policies of most industrial nations, especially the nations of Western Europe and the United States.
Where income support for the farm population is deemed essential, it must be achieved in ways that do not encourage production or discourage consumption. Many of the industrial countries have followed policies that encourage too many resources, especially labor, to be retained in agriculture. It is difficult to now extricate themselves from this situation. But the long run gains, both directly to the countries involved and to the free world as a whole, are sufficiently important for industrial countries to give greater weight to the international implications of their domestic agricultural policies than it has been their practice in the past.