CHAPTER 5

Reducing Trade Distortions in OECD Countries

5.1. Introduction

Among the OECD countries, agricultural protection is an important issue of trade negotiations. In fact, the OECD Council of Ministers has given the secretariat a mandate to study the impact of agricultural trade liberalization by OECD countries. Thus, a scenario to explore the impact of agricultural liberalization by OECD countries is of specific policy interest.

The countries of the OECD together are sufficiently large actors in world trade that, when they liberalize trade simultaneously, world prices will change, though the direction of change cannot be easily predicted. One cannot predict *a priori* whether, in the resulting equilibrium, a country within the OECD will gain or lose in welfare from trade liberalization. In describing the results of this scenario on trade liberalization, the following questions are addressed:

(1) How do the world market prices change?
(2) What is the impact on agricultural production and trade in the world and in the individual countries? How do market shares change?
(3) What is the welfare gain, if any, for the various OECD countries?
(4) How are farmer incomes and parity affected?
(5) What is the impact on other countries, particularly the developing countries, of trade liberalization by OECD countries?

5.2. Higher World Market Prices under Trade Liberalization by the OECD

With trade liberalization by the OECD countries [Australia, Austria, Canada, EC, Japan, New Zealand, and the USA, for which explicit models exist in the BLS (Turkey is excluded from liberalization as one of the less-developed OECD countries); the other OECD countries are included in a country group model

K. S. Parikh et al., *Towards Free Trade in Agriculture*
© Springer Science+Business Media Dordrecht 1988

and also liberalize], the world market prices of agricultural products relative to nonagriculture would be higher by 9% by the year 2000 compared to the reference run (see *Table 5.1*). This modest average increase, however, is misleading because its modest level is strongly influenced by the very small increase in the price of the commodity group with a high weight and facing relatively low protection in the OECD countries – namely, "other food", dominated by fruits, vegetables, and tropical products.

Table 5.1. Percentage changes in world market prices and global net exports in 2000 under OECD trade liberalization relative to the reference scenario.

Commodity	*Relative prices*	*Net exports*[a]
Wheat	18	–2
Rice	21	37
Coarse grains	11	–5
Bovine and ovine products	17	35
Dairy products	31	13
Other animal products	–0	17
Protein feed	13	5
Other food	5	10
Nonfood agriculture	–2	5
Total agriculture[b]	9	–
Nonagriculture	0	17

[a]Changes in quantities, except for net exports of total agriculture for which change in the aggregate export index weighted by 1970 world prices is reported. [b]Price weighted by production.

In fact, for the commodities of primary importance to the producers in OECD countries, such as cereals, protein feed, and animal products, the increases in world market price compared to the reference scenario are of the order of 10–20% and, for dairy products, more than 30%.

The movement of the index of relative prices (with 1980 as base) compared to the reference run is shown in *Figures 8.1–8.9.* These figures show that the transition to trade liberalization more or less stabilizes world market prices by the early 1990s.

The long-term development of prices in a scenario, as discussed in Chapter 4, is the outcome of the interplay of demand shifts due to population and income growths and supply shifts due to technical progress and factor allocations. Since the differences in income growth between the OECD trade liberalization and the reference scenario are relatively small (and population growths are the same), even at the country levels the demand shifts should be similar in the two runs. Explanations for the differences in the prices between the runs have thus to be sought mainly from the way supply shifts develop in response to changes in prices between the two runs.