An Introduction to State Trading in Agriculture. Karen Z. Ackerman and Praveen M. Dixit. Market and Trade Economics Division, Economic Research Service, U.S. Department of Agriculture. Agricultural Economic Report No. 783.

Abstract

State trading enterprises are far more prevalent in agriculture than in other industries. STEs account for significant shares of world trade in grains, dairy products, and sugar. Attempts to measure the impacts of STEs and their activities on international agricultural trade have just begun. This report presents a classification scheme for STEs that provides a qualitative index of an STE's ability to control domestic markets and its ability to influence external trade. We applied the classification scheme to nine major agricultural STEs and concluded that only a few of them are able to affect international trade substantially. Recent policy reforms have eroded some of the nine's powers to influence trade.

Acknowledgments

The authors thank several important contributors and reviewers. Tim Josling deserves our appreciation for his contribution to the analytical framework underlying this study. Nicole Ballenger, Mary Bohman, Joy Harwood, Jim Stout, Ron Trostle, John Wainio, Tom Worth, Ed Young, and Steve Zahniser of ERS commented constructively on several earlier drafts of this study, as did Will Martin of the World Bank and Tom Grennes of North Carolina State University. The authors appreciate their interaction with university economists who participated in an ERS workshop on state trading in November 1996, in a December 1996 meeting of the International Agricultural Trade Research Consortium, and in a workshop at Stanford University cosponsored by the North America Forum and the California Agricultural Issues Forum in November 1998. We also thank our colleagues at USDA's Foreign Agricultural Service, the Office of the Chief Economist, and the Office of the U.S. Trade Representative for their helpful comments on this paper. Lastly, the able edits of Brenda Powell and Tom McDonald significantly improved this report.

Washington, DC 20036-5831 October 1999

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Summary

State trading is more prevalent in agriculture than in other industries because many countries use state trading enterprises (STEs) as a means to achieve policy objectives such as domestic price support, efficiencies in agricultural marketing, and affordable food supplies for low-income populations. STEs account for significant shares of world trade in grains, dairy products, and sugar.

In 1995 and 1996, more than 30 countries notified the World Trade Organization (WTO) of almost 100 agricultural enterprises or other agricultural organizations that could be defined as STEs. Some of the largest export STEs reported to the WTO are in Australia, Canada, Indonesia, Japan, South Korea, and New Zealand. Countries seeking accession to the WTO (like China) also control their agricultural trade through STEs.

STEs are government or private enterprises that have been granted special or exclusive privileges by their governments, such as exclusive trade authorities and government underwriting of operational costs. The special domestic market, trade, and financial authorities allow STEs to influence, through their purchases or sales, the level or direction of trade in their commodities.

STE activities affect trade by influencing domestic and international prices. An STE that restricts imports into a country will have an effect on the domestic price just like that of an import tariff. Similarly, an STE that expands exports will have an effect on domestic price that resembles an export subsidy. Several factors influence the tariff/subsidy equivalents associated with an STE, including its degree of control over the domestic market, its policy objectives, the extent of its international market power, and its range of authorities and government support.

Attempts to capture the quantitative impacts of STEs and their activities on international agricultural trade have just begun. Such information, when available, will show what types of activities are most trade-distorting and would require disciplining. An alternative means of understanding and analyzing qualitatively the market effects of an STE is to develop a classification scheme for STEs. This report presents a classification scheme for STEs based on their ability to control domestic markets and their ability to influence external trade.

Four general types of STEs are established under our classification scheme. Type I STEs control neither the domestic market nor trade and have little, if any, capacity to affect the market. Type II STEs control domestic markets only and their potential to distort trade is low. Type III STEs allow competition in the domestic market but not in external trade, giving them the potential to moderately distort trade. The actual extent of their trade distortion depends on the extent of their international market power, the range of their exclusive privileges, and the importance (share) of external trade in domestic consumption and production. Type IV STEs have exclusive or special authorities over both trade and the domestic market, which give them a greater capacity to distort trade than the other three groups. However, a Type IV STE which has a small share of the global market may distort trade less than a Type III STE which is a big player in world trade.

For illustrative purposes, we applied the classification scheme to four major export-oriented STEs, four major import-oriented STEs, and China's state control of grains. All the STEs used as illustrations for this paper were classed as Types III or IV, although recent policy changes eliminated exclusive trade authorities for three of the import-oriented STEs, effectively changing their classifications to Type I. As countries unilaterally dismantle their STEs' trade-distorting authorities, more STEs will move into the Type I and II classes, which have little, if any, capacity to distort external trade.

State trading as an issue will continue to garner attention. These enterprises form the cornerstone of the agricultural systems of many countries, and abolishing them—either through further trade reform in the WTO or under the structural reform programs of international institutions like the International Monetary Fund or the World Bank—is not likely to occur soon. Consequently, discussions on STEs are likely to revolve around strengthening WTO rules governing these enterprises and imposing additional disciplines on their exclusive authorities and the policies they implement.

If the objective is to minimize global trade distortions arising from the activities of STEs, what goals might policymakers pursue for STEs? Clearly, Type I STEs have little, if any, capacity to distort external trade and hence might not require scrutiny vis-a-vis current rule violation. Type II STEs also operate without the support of trade controls. Hence, scrutiny vis-a-vis current rules violations, especially as they relate to international trade, is not necessary, although an examination of domestic competition policy might be desirable.

Type III STEs can moderately distort trade but are not as distortionary as Type IV STEs. The policy goals for Type III STEs might be to examine the extent of market control they exercise and how their institutional characteristics might contribute to additional trade distortion. Type IV STEs, which maintain control over both the domestic and external markets, can distort trade the most because of their exclusive marketing authorities in both markets. The policy goal here might be to address entry restrictions into the markets. Institutional characteristics, while important for Type IV STEs, do not necessarily constitute the overriding impediment to a move toward free trade.

STEs extend well beyond agriculture, and the issue is likely to get added attention when other sectors, such as services, come to the forefront of negotiations. If this were to occur, chances are that STEs will also be discussed under rules on competition policy for private firms. Clearly, the scope for future work on STEs is vast; the challenge before us is to use simple tools to enhance our understanding of state trading and elucidate alternative schemes to curtail the trade-distorting capacity of such enterprises.