

MAP - Brief

Monitoring Agri-trade Policy



Understanding the market access debate

Criticised by exporters for lacking ambition and third countries for retaining the walls of old 'fortress Europe', the EU's last market access proposal was condemned almost before it had hit the table. But is the criticism justified, or is it just another attempt to shift the responsibility for stalled talks onto someone else's shoulders?

This MAP Brief takes what is arguably the most complex element of the agricultural trade talks and analyses the reasoning behind the EU's proposal on market access. It asserts that it is the EU, and not others, that offers the most realistic, practical and, at present, complete, solution to the problems underlying agriculture's third pillar.

The EU offer: Missing the mark or misinterpreted?

Broadly speaking, each of the main market access proposals is based on four tiers, each of which is defined by a certain tariff threshold and all require the tariff cuts to be proportional to their current level.

On the basis of each proposal, average tariff cuts can be defined for each country/group of countries, as shown in table 1.

Table 1: How average tariff cuts misrepresent the results of the tiered formula

	Average	tariff	cuts
	EU	G20	US/Aus
EU	39 %	52%	67%
US	37 %	48%	67%
Canada	38 %	50%	63%
Japan	40 %	53%	65%
Brazil	30 %	30%	?
India	36 %	36%	?

Table 1 appears relatively straight-forward. Indeed the figures it contains are those that have often been used to compare the relative level of ambition of each of the different groups in recent weeks. And, taken at face value, it is clear why the U.S and Australian proposals seem the most appealing while the EU's has been highly criticised.

However, to define the level of ambition in the respective proposals is, unfortunately, a little more complex than simply cutting figures out of the context and pasting them into a comparative table. It requires first a definition of the parameters used to classify tariffs – that is the thresholds and relative cuts – and second, a thorough analysis of the feasibility and consistency of the method used to establish each sequence of tariff cuts.

Different methods of calculation...

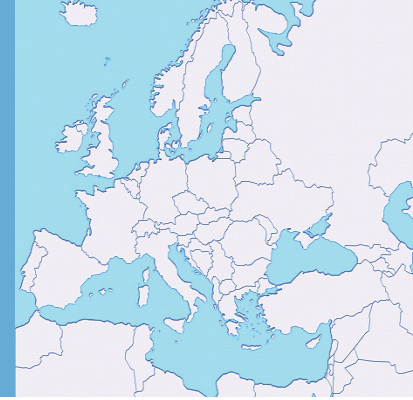
Two different methods of tariff calculation are currently used – one to measure the average cut per tariff line, the other to measure the average of all tariffs before and after all the cuts are implemented. Both are in essence correct, but they provide very different results with very different implications for the market access negotiations.

Table 1 uses the first method – the average cut per tariff line – which is the method used in the implementation of the Uruguay Round (UR) agreement. It highlights two major differences in the proposals. The first is in the level of cuts: the U.S and Australia apparently propose substantially higher cuts than other groups, and the second is in the content: in particular, the question mark hanging over the U.S and Australian proposals regarding the apparent lack of special and differential treatment for developing countries.

Two other observations can also be made. The first is the explicit similarity in the treatment of developing countries between the EU and G-20's proposals (because the EU incorporated this aspect of the G-20 proposal into its own). The second is the implicit effect that the U.S and Australian proposals would have not only on their own domestic economies, but also on third country ones, notably developing countries who at present benefit from a number of preferential market access arrangements.

...and different levels of ambition

What is not clear in table 1 however, is the fact that the G-20 proposal overlooks the so-called 2/3 rule (i.e. that developing countries undertake 2/3 the level of commitment of developed ones, as per the UR approach). Under the G-20's proposal, which requires developed countries to undertake tariff cuts of 75 % for all tariffs over 75 %, while developing countries would only be obliged to make 40 % cuts in tariffs of over 130 % and 35 % on tariffs over 80 %, this ratio would in fact be reduced to 1/2 instead.



So finally we come to the EU’s proposal, which is based on the second method - the average of all tariff cuts, before and after implementation – and should be viewed as fair, transparent, consistent with objectives and, most importantly, ambitious.

Ambitious, firstly in the magnitude of the cuts it proposes for developed countries:

- Tariffs above 90 % would be reduced by 60 %;
- Tariffs between 60 % and 90 % would be reduced by 50 %;
- Tariffs between 30 % and 60 % would be reduced by 45 %; and
- Tariffs below 30 % would be reduced by an average of 35 %.

It is the average of these cuts that results in the 39 % shown in table 1.

For developing countries, the proposed tariff cuts are 40 % for tariffs above 130 %, 35 % for those between 80 % and 130 %, 30 % for those between 30 % and 80 % and 25 % for those under 30 %.

And ambitious secondly in the way the cuts are implemented (i.e. larger cuts on higher tariffs) which results in a far more significant reduction in protection than many of the critics imply. This fact can be illustrated in two different ways: numerically and graphically.

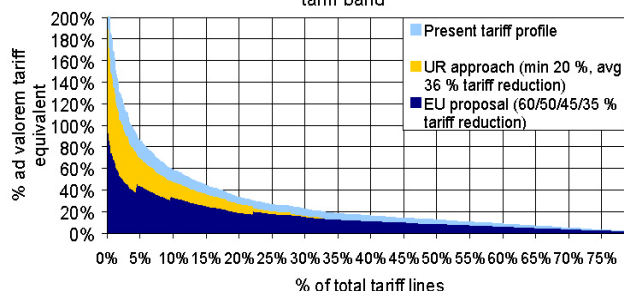
Table 2 quantifies the level of “ambition” numerically, showing that the EU proposes to halve its own agricultural tariffs by bringing the tariff schedule down from 23 % to just 12 % by the end of the implementation period.

Table 2: Measuring average reduction of tariff schedules under the EU proposal

	before cuts	after cuts	average reduction
EU	23 %	12 %	47 %
US	11 %	6 %	48 %
Canada	9 %	5 %	52 %
Japan	61 %	20 %	66 %
Brazil	37 %	28 %	25 %
India	116 %	73 %	38 %

The difference in the average reduction is the result of the difference in each of the tariff profiles, as shown in graph 1 which indicates once again the level of ambition of the EU’s proposed tariff cuts.

Graph 1: EU tariff profile under alternative reductions per tariff band



Here, the EU’s present tariff profile is shown in the upper (light blue) envelope, sorted by the decreasing AVE of the EU’s current tariffs. The middle (orange) envelope is the EU tariff profile were tariff cuts to be implemented in the same manner as they were under the UR (i.e. low cuts on high tariffs, high cuts on lower ones) and the lower envelope (dark blue) represents the EU’s tariff profile if cuts are implemented on the basis of the EU’s proposal for the DDA.

And despite the similar average tariff cuts for the UR (36 %) and the DDA (39 %), there is clearly a significant difference between the approaches which is evident in the orange slice – the section of the graph which clearly indicates the EU’s level of ambition.

The EU’s proposal: fair, transparent & consistent

So what the EU achieves in its proposal, by applying special and differential treatment to developing countries and by applying the so-called 2/3 rule, is a result that is fair to developing countries, realistic, transparent, consistent with prior agreements and still extremely ambitious in economic terms.

And the questions it therefore leaves are:

- Is the G-20 really fair, transparent and consistent in its proposal while they continue to overlook the 2/3 rule and underplay the relative level of ambition that is required from certain developing countries as well?
- And are the U.S and Australia really that ambitious, or are they simply unrealistic (and safe in the knowledge that such cuts would never be accepted anyway), and unclear on the issue of special and differential treatment of developing countries?



...And how to deal with sensitive products?

A second essential element in determining the level of ambition in a proposal is the treatment of sensitive products. For this, the Framework Agreement defines two general principles:

1. the self-selection of a limited number of tariff lines (i.e. sensitive products) for which a lower level of tariff reduction would be permitted;
2. the fact that substantial market access should also apply for sensitive products – to be achieved through the combined effect of an implied lower tariff cut and an expansion of the TRQ.

Although it does not define precisely the meaning of “substantial market access,” it is logical to assume that this means that sensitive products should be entitled to significantly increased market access but that this access should still be lower than that afforded by a full tariff cut. In addition, the EU assumes that TRQ expansion is also consistent with the Framework Agreement in so far as it should take into account all the relevant parameters relating to market access for the product in question – in other words its tariff profile, the actual level of trade and the degree of deviation from the normal tariff cut.

The flawed approach...

Two approaches have been proposed for sensitive products. The first links Tariff rate Quota (TRQ) expansion on a one-to-one basis to the present level of TRQ; the second links TRQ expansion to a fixed desired level of consumption, but both are fundamentally flawed.

Firstly, by assuming a one-to-one link between the percentage deviation from the normal tariff cut and the percentage increase in the TRQ, this approach ignores all the other parameters that come into play in the market access debate.

Secondly, as far as consumption is concerned, not only are the consumption figures aggregate at best and absent at worst, they are also influenced by a series of other factors that are linked not to trade (the key issue here) but instead to domestic developments. Consequently both fail to put the issue of TRQ expansion into context because they do not and cannot guarantee the consistent treatment of sensitive products across all tariff lines.

...and the EU approach

In contrast, the EU approach does link the trade-off between a lower tariff cut and TRQ expansion in such a way that respects both market realities and the Framework Agreement. It leaves the choice of tariff cut deviation to members on the basis of a sliding scale range, and it expresses TRQ expansion as a percentage of total current imports with values derived from the following formula:

$$\text{TRQ Increase (\% of imports)} =$$

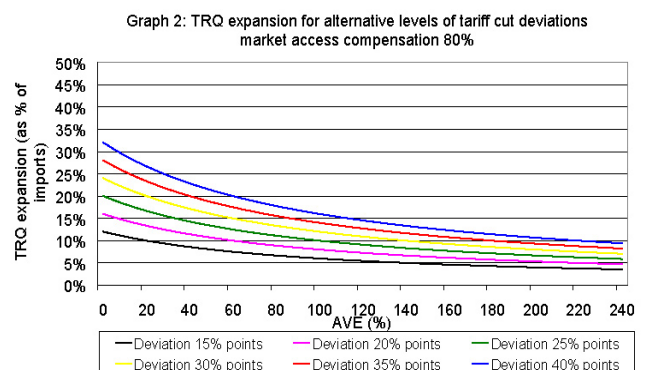
$$\frac{80\% \times (\text{Full Tariff Cut \%}) - \text{Reduced Tariff Cut \%}}{(100\% + \text{Initial AVE \%})}$$

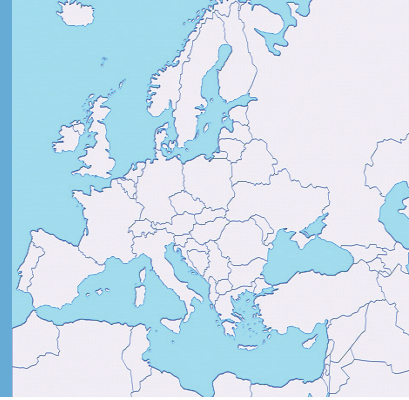
On this basis, TRQ expansion is derived from two different factors:

1. the desired degree of market access compensation for sensitive products (80 % in the EU proposal) and
2. the proportion of the tariff cut deviation in relation to the initial effective border protection.

Such an approach produces results that are entirely consistent with the Framework Agreement, are transparent in terms of the trade-off between TRQ expansion and tariff cut deviation, and take explicit account of market related factors, including the specific tariff profile of a sensitive tariff line. Finally, both the tariff cut deviation and the initial AVE (and thus also the effective border protection) are known parameters for every tariff line, as is the level of imports.

Graph 2 shows the results of the EU proposal, indicating the trade-off between alternative levels of tariff cut deviation for the 80 % market access compensation scenario.





Simple, consistent & effective

What conclusions can we draw? Firstly, that the EU's formula is not as complex as others like to make out. All formulae look complex to the untrained eye if taken at face value, but in fact the EU has based its proposal on readily available data, and its formula simply requires the division of the tariff cut deviation by the initial effective border protection.

Secondly, it is clear that the EU approach is entirely consistent with the principles of the Framework Agreement. In other words, it does not explicitly impose an arbitrary consumption effect on the tariff cut as other proposals do; it implicitly reflects the consumption effect through the impact that tariff cuts have on imports and prices.

Thirdly, the EU proposal guarantees that the overall level of market access for a sensitive product will not exceed the level that would be implied by a full tariff cut.

This is confirmed in the following numerical example, which demonstrates how the EU formula for the treatment of sensitive products works, and how it compares to other approaches for the treatment of sensitive products. The basic variables (consumption, imports, import price before duty, initial levels of AVE and TRQ), are summarised in table 3:

Table 3: Hypothetical example of sensitive product

Variable	Unit	Value
Consumption	000 mt	7 000
Imports	000 mt	600
TRQ	000 mt	250
Import price	€/mt	1 500
AVE (%)	%	90

Assuming a normal tariff cut of 60 %, and a reduced tariff cut - if the product is declared sensitive - of 30 %, the implied TRQ expansion, based on the EU formula, is the following:

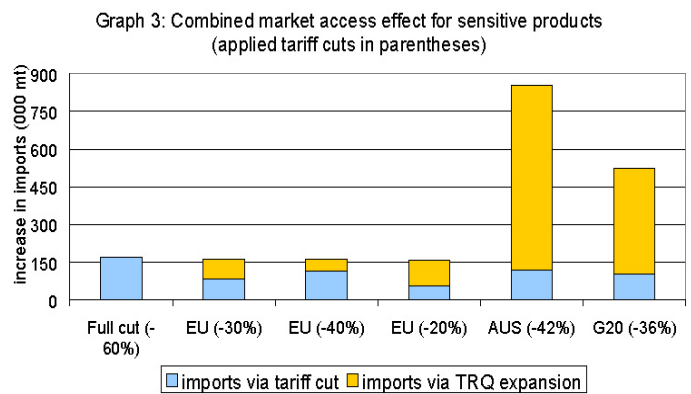
$$\begin{aligned} \text{TRQ expansion (as percentage of imports)} &= 80 \% \times (30 \% / 190 \%) \\ &= 12.6 \% \end{aligned}$$

This implies a 30 % increase in the existing TRQ, or an increase of 75 800 mt (600 thousand mt x 12.6 %).

Two questions arise from this example. What market access increase would result from the lower than normal tariff cut, and how does the overall combined result of tariff cut and TRQ expansion compare to the impact of the full tariff cut?

The answer to both questions is found in the following graph, which compares the full impact of a 60 % tariff cut (based on a unit elasticity of import demand) to the tariff cuts resulting from alternative tariff cut deviations (50 % deviation, 40 % and 30 % for the EU, G20 and Australian proposals, respectively).

It is evident from the graph that the level of TRQ expansion resulting from both the Australian and G20 proposals bear no relevance to the market access impact resulting from the full tariff cut. TRQ expansion under these proposals is simply derived as a result of a fixed target of TRQ expansion which is arbitrary, irrelevant to the parameters in question and simply excessive.



The derivation of the formula for TRQ expansion proposed by the EU and additional graphs comparing alternative elasticity values for the above example can be found in the "Technical notes" section on the DG Agriculture website: http://europa.eu.int/comm/agriculture/publi/map/index_en.htm.

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