Oxfam Briefing Note

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Who will be left to cheer the end of illegal US cotton subsidies?

Why African cotton farmers cannot afford US inaction on cotton subsidies

March 3, 2005

"It is very clear that cotton is very important for the development and success of Benin. It is good to try to diversify, but we have to deal with the fact that they exist today too."
Robert B. Zoellick, USTR, Cotonou, Benin

"We cannot continue with the current situation. If we have to wait another 6 or 7 years for a solution, we are being condemned to stop producing cotton."
Tiasse Coulibaly, Cotton farmer, representative of National Producer Association, AOPP, Mali.

Eighteen months ago at Cancun, rich countries promised African cotton farmers that the WTO would solve all the problems being caused by US subsidies. Despite the fine words from US Trade Secretary Robert Zoellick, nothing has changed for African farmers. The US has put "cotton" on the WTO negotiating table - but only to buy time to continue supporting its cotton farmers at the expense of the world's poorest countries. If agricultural negotiations proceed as planned, a new agreement could enter into force as late as 2008. The US might not even have to implement the agreement until 2013. At this snail's pace, there will be no African farmers left to cheer the end of US cotton dumping.

US cotton subsidies declared illegal by the WTO[1].

The final decision released by the WTO appellate body on March 3 will add legal grounds to the African position in these negotiations – and hopefully some impetus toward a successful final

[1] This section is based on the cotton panel findings as communicated by the WTO in September 2004. While there is a chance that some of these findings will be overturned by the Appellate Body, it is expected that most of them will be upheld.

deal. After two-and-a-half years, the WTO has confirmed the obvious: that US subsidies were causing significant price suppression of world cotton prices.

The WTO Appellate body also confirmed that the US used hidden export subsidies on cotton to circumvent its Uruguay Round commitments. As a result, the US will have to eliminate export credits and “Step 2” programs by July 1, 2005. According to evidence used by Brazil in their case against the US, the impact of these programs depressed world prices by about 4%.

Finally, the WTO appellate body found that the US misreported certain programs as “non-trade distorting”, when in fact they were. These direct payments, notified in the ‘Green Box’ by the US, will instead have to be reclassified as ‘Amber Box’ support.

US inaction leads to the demise of African farmers

Since 2001, when the slump in cotton prices started, Africa looses on average $441 million a year because of trade distortions on cotton markets. Since the launch of the Sectoral Initiative in 2003, the four West and Central African producers (Benin, Burkina Faso, Chad and Mali) have suffered export losses of around $382 million because of US inaction. If the four West and Central African country producers have to wait until 2013 to see a meaningful reduction in US subsidies, projected losses could amount to $1,528 million. These figures, based on FAPRI modeling, estimate the average effect of removal of trade distortions between 2001 and 2012.

Today, cotton prices are at their lowest levels again– down by 30% between 2004 and 2005, at an average of $48cents/pound. According to recent ICAC estimates, these prices will stay at very low levels for the next 5 years, between $48c./pounds and $54c./pounds. This slump has had a terrible impact on African countries. More than 10 million people depend on cotton for their livelihoods in West and Central Africa. There are few alternatives for them to generate other income. Cotton exports are critically important to the balance of payments for many African countries, constituting more than one-third of Benin’s total exports and nearly one-third of Burkina Faso’s. Depressed cotton prices have cost these countries millions of dollars, critical to pay for social services such as education and healthcare, and to maintain macro economic stability.

In the meantime, the counter-cyclical nature of US cotton subsidies means that the US government will provide generous support to its cotton producers this year, cosseting them from market forces and lower world prices.

Immediate steps are needed to save the cotton sector

The West and Central African governments originally asked for compensation for the losses incurred as a result of rich country cotton subsidies, pending the subsidies being phased out. This did not receive a sympathetic hearing at the WTO’s Cancun meeting, either by the US or the EU delegations. They explicitly ruled it out.

In the meantime, the price crisis has continued in global cotton markets. After a brief recovery in 2004, it worsened again in 2005. While the US has been using every trick in the book to resist change, cotton companies, government and producers in the world's poorest countries have all been bearing the costs of world price declines, for which subsidies are in large part responsible.

The only reason why the West and Central African cotton sector still exists is because of mechanisms designed to protect producers and companies from the effects of low prices. These mechanisms have allowed losses to be partially offset and producer prices maintained at a minimum level, enabling them to cover costs and continue producing. However, even where direct prices to producers have remained stable, producer incomes have suffered because annual bonuses have no longer been paid and input costs have risen reducing producer margins. Moreover, cotton companies' reserves have been exhausted or else have had to be covered by government deficits, drawing funds away from other urgent priorities. Governments and producers have now been pressured to accept lower prices – as in Mali – where the producer price will fall by 25% or more for the next 3 years, as a result of world market conditions. Producer price has also gone down from 15% in Benin and 6% in Chad over the last 5 years. The economic and social consequences of this could be dramatic.

Given this background of cumulative losses, the West and Central African cotton sectors justify a support fund. West and Central African countries have recently estimated that the cotton sector will lose $400 million in 2004/2005 because of low prices and exchange rate problems. This fund could help ensure the macroeconomic stability of highly cotton dependent countries in the medium term, and prevent a collapse of incomes for small cotton producers until US subsidy reform is complete. The support fund would have to ensure ownership of all stakeholders and ensure that cotton farmers and their organizations have a degree of direct control over the money, as well as being direct beneficiaries. The establishment of such a fund should not be linked to new conditionality, such as adoption of GMO technologies or cotton sector privatization.

WTO negotiations proceed at a snail's pace

While almost every WTO member, at some point, has made some positive declarations about the cotton initiative, nothing is really moving. The framework agreement signed last July fails to include a strong commitment to rich country cotton subsidies being drastically reduced. This was simply the last in a long list of disappointments.

Cotton has been folded into overall agricultural negotiations and the only "special treatment" it has been afforded is the creation of a cotton subcommittee. West and Central African countries have had to give up on expecting anything more because the US government made it plain that cotton was a 'red line' not to cross, threatening them that a step too far might lead to the collapse of the whole July framework.

The cotton sub-committee met for the first time last February. Rich countries showed no sign that they were ready to ease their position. The US tried to dilute the sub-committee's mandate by trying to include other issues for discussion. This, together with the EU's move to limit the role of the sub-committee to one solely of monitoring, is a very bad omen for African cotton producers.

The way forward

If the US is serious about concluding the Doha Round by the end of 2006, they must deliver some substantial reforms of their cotton programs before the next Ministerial in Hong Kong. The US must implement the WTO appellate body ruling. Negotiations should complement the ruling rather than become a substitute for it.

The minimum result should be:

- Phase out the use of all trade-distorting cotton subsidies, including marketing loan programs and counter-cyclical payments, on a fast-track basis.
- Reform or eliminate direct payments so they are truly decoupled from production decisions and do not create an implicit encouragement to grow cotton in the US.
- Finally, a support fund should be launched early in 2005 by the international donor community to prevent the collapse of cotton sectors in Africa.

The Cotton as clear case for agricultural reform

The panel ruling will have profound political implications beyond the case of the US and cotton. Some of the findings in the cotton case are also relevant for other farm programs in the US. Commodities like soybeans, rice, oilseeds or grains could be targeted by future WTO cases because they do not comply with the rules on agriculture negotiated during the Uruguay Round.

The cotton ruling, together with the upcoming sugar appellate body decision against the EU, established that developed countries failed to abide by subsidy rules that they crafted during the Uruguay Round. Developing countries have had an important moral and legal victory and as a result should be in a stronger position in current multilateral negotiations. The US and the EU must agree to improved rules that will effectively end export dumping, reduce trade distortions, and ultimately allow developing countries to trade their way out of poverty.

Oxfam also urges the EU and the US to negotiate in good faith new rules in the current WTO agricultural negotiations that would put an effective end to dumping.

This means:

- A credible end date for export subsidies must be agreed to by the European Union as expeditiously as possible. The United States should not use smokescreens to refuse elimination of subsidized export credits and the introduction of disciplines on the commercial use of food aid.
- Ambitious figures for the reduction of domestic support must be negotiated, addressing all instruments and commodities, so that dumping effectively disappears.

Published by Oxfam International March 2005
Published by Oxfam GB for Oxfam International under ISBN 978-1-84814-729-4