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COTTON, SUGAR, AND GROUNDNUTS
A Political Economy of Credibility

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INTRODUCTION

First, let me thank the organizers of this important and timely event for bringing us together to reflect upon what may very well be the single most important economic issue of our time, as it takes us to the core of the validity of capitalism in a post-communist world, and also at the heart of globalization. For many years, development economics has received bad publicity, especially in the academic world, not least for its perceived incapacity to produce a miracle solution to hunger, economic misery, and under-development. With the ABCDE conference now widely acknowledged as one of the world’s most important intellectual events, the World Bank has brought development economics back into mainstream thinking and enriched the agenda of world affairs. Mr. Wolfensohn and his team certainly deserve a lot of credit for their persistence and efforts.

Second, I must thank our speaker Mr. Watkins not only for providing us with a very thoughtful piece of analytical work on today’s topic (trade flows) but also for being such a compassionate advocate of the moral imperatives of free and fair trade. Speaking here as a citizen from one of the so-called poorest countries in the world, I can only tell him how much I am grateful for his very convincing plea for economic justice.

I would like to keep my remarks in the broader spirit of this year’s conference: “Economic integration and social responsibility”. I truly believe that these words sum up nicely the complex issues of trade flows and commodity prices that we are discussing this morning, and also the challenges ahead of us. Indeed, regardless of where anyone stands on these questions, it would be naïve to think that economic theory alone explains what is at stake, or that politics and social choices made by all governments should not be taken into account.

As a discussant on this panel, my goal is neither to carry out an in-depth analysis of the issues at hand, nor to challenge the views expressed by the previous speakers (especially since I tend to agree with most of what has been said), but to simply help spark the debate on these important problems that must be addressed by the international community if we are serious about achieving the 2015 Millenium Development Goals (MDG).

I will limit my comments to three commodities with huge economic, political, and social implications for developing countries—especially those in Sub-Saharan Africa where millions of lives depend on the international prices of these products: cotton, sugar, and groundnuts. I also chose these three because they provide ample evidence of the type of distortions that occur in economics when policymakers in the developed world give priority to their national political calculus, instead of looking at the big picture and helping address the social needs of the developing world. Finally, I focus on these three commodities not only because of their economic, financial, political (and I would even say symbolic social importance) in the context of fighting poverty in Africa, but also because they illustrate some of the main challenges ahead in the Doha round of the WTO trade negotiations. My hope is that our discussion during this conference and similar events will contribute to the search for solutions to a problem which is putting the credibility of the world community and the commitment to the wonderful MDG at risk.
Since I have limited time, let me give you my four main points, some of which are quite similar to those made by Mr. Watkins in his presentation:

- While Western countries are advocating free trade and open markets in the South, they have maintained high levels of protection and provided huge subsidies to their own farmers, thereby encouraging over-production of agricultural products. This in turn has been depressing commodity prices, weakening fragile economies in Sub-Saharan Africa, and aggravating poverty.

- From the perspective of farmers and peasants in Africa, there is little difference in the impact of US and EU agricultural subsidies: there would be no point in trying to choose between two terrible diseases. That is why on April 30, 2003, four African ministers in charge of trade (from Benin, Burkina Faso, Chad and Mali) filed an official complaint against the US and the EU for violating WTO rules on cotton trade and depriving their countries of an estimated loss of $1billion a year.

- Globalization or economic integration has made the world a large, big family, and we should all be aware of that. Nowadays, when people are sick in China or Hong-Kong, the next day, people die of the same disease in Canada. Likewise, when people suffer hunger in northern Mali or in southern Senegal, they will do whatever it takes to migrate to France, Belgium, or the United States. Unless policymakers in the West understand the urgency of helping to improve the welfare of people in the developing world (especially those who rely on commodities for their livelihood), the entire planet will have to pay the consequences of inaction.

- In an ideal world, the solutions to this problem would be straightforward: banning the sale of products at prices below their cost of production, and all forms of export support including export credit subsidy programs (along the lines of the OXFAM solutions). However, having been involved in politics myself, I must recognize that policymakers and politicians do not make decision on the sole basis of technical or economic variables. They do not act in a vacuum like characters in the movie The Matrix, or in paintings by Francis Bacon! They factor in the political context in almost everything they do. Therefore, my proposed solutions will try to take into account the need for a realistic and more effective approach to reforms.

Focusing on cotton, sugar, and groundnuts, my remarks are organized around three questions: what are the key issues at hand and where do we stand? What is the cost of inaction, from the perspective of Subs-Saharan Africa? And where do we go from here?
I-) KEY ISSUES: WHERE DO WE STAND?

Cotton. Unlike some other commodity markets, the cotton market is not affected by distorting trade policies like high tariffs or quotas but as pointed out by Mr. Watkins in his contribution, the United States and the European Union use domestic measures to support their cotton sector. It is estimated that in the US and the EU, support averaged $3.6 billion during the three seasons from 1999-2000 to 2001-02. During the 2001-02 season, producer prices in the US were 91 percent higher than world prices (and almost 145 percent higher in Greece, 185 percent higher in Spain).

Such levels of support have led to over-production and declining prices. Adjusted for inflation, world cotton prices have fallen to their levels of the 1930s. Indeed, real cotton prices have declined sharply over the past four decades. According to a recent World Bank study\(^1\), they are currently about half their 1960s level. This has created a vicious cycle: because of declining prices, several developing countries like Brazil, Mexico, Egypt or Turkey have now decided to introduce support to their cotton sectors.

Sugar. The world sugar market is a textbook example of one of the most distorted: producers in the US, the EU, and Japan receive more than double the world market price due to production quotas, government guaranteed prices, import controls, etc. The US provides $1.3 billion of support per year and the EU $2.7 billion. OECD support to sugar producers amounts to $6.4 billion, which equals exports from developing countries.

Protectionism is an old issue here: for the past two centuries, farmers from western countries who produce sugar from beets have been unable to compete with their counterparts from tropical countries who extract sugar from cane. In fact, even today, the cost of production of sugar from beets is almost twice that of sugar from cane. It is estimated that government support or transfers from consumers in OECD countries have amounted to an average of $6.4 billion a year in 1999-2001. This is more than the total value of sugar exports from developing countries, and 55 percent of the annual world sugar trade ($11.6 billion).

Attempts to reduce sugar protection have been fiercely resisted by vested interests and consumers who pay high prices have not been heard, especially since the share of the food budget spent on sugar in increasingly small.

Groundnuts. The world market has been distorted by government subsidies, import controls, and price support aiming to stimulate production. Again, this has resulted in the lost of market share for African producers. While it is true that the 2002 US Farm bill has suppressed some protective features from the previous legislation (production quotas, high support prices for American farmers), it has also introduced new distortions which a World Bank expert considers to have “a potential to depress world market prices and

subsidizing US peanut exports in situations of low world prices (e.g. counter cyclical payments and floor price mechanism that become effective when world prices are low.”)²

II-) COST OF INACTION FOR SUB-SAHARAN AFRICA

Why agriculture is so important in Africa? In his paper, Mr. Watkins has rightly emphasized the relative importance of agriculture in various parts of the world. While its contribution to growth and welfare in industrialized countries has consistently diminished over the 20th century, agriculture remain the main source of livelihood, government revenue, foreign exchange, and employment in most of Africa. In my own country Burkina Faso, it is an important pillar to help expand economic opportunities for the poor. Commodities like cotton are key ingredient to economic growth. In fact, recent evidence from many African countries suggests that the sectoral composition of growth matters in terms of the impact on the incomes of the poor, given estimates of elasticities of poverty reduction with respect to growth—a 1 percent increase in the contribution of agriculture to GDP can yield a 1.6 percent increase in the incomes of the poor above the GDP increase in industry or services, which increases incomes of the poor by 1.2 percent and 0.8 percent respectively. These differences are related to the linkages of agricultural growth on small-scale non-agricultural sector of the rural economy. These linkages come from rural households spending their expanding income on locally produced non-tradable goods and services. In Burkina Faso, household-level data indicate that 45 percent of any increase in rural household incomes is spent on farm non-tradables (e.g. dairy products, millet) and 22 percent on non-farm non-tradables (e.g. locally processed foods, services, locally manufactured items). Growth multipliers for Burkina Faso indicate that for each dollar of income generated in the agricultural tradable sector $1.88 of additional income will be generated in the local non-tradable sector due to linkages.

Again, let me consider the three agricultural products in turn:

*Cotton* accounts for 40 percent of total export earnings in Burkina Faso and Benin, and 30 percent in Mali or Chad. Its contribution to GDP in these countries is high, ranging from 5 to 10 percent. It supports the livelihoods of 2 million of people in my own country where it is also the main cash crop.

- In Central and West Africa, more than 10 million people depend on cotton for their livelihood. West African countries are among the lowest-cost producers of cotton. Yet, in spite of their comparative advantage, they are loosing market shares and poverty among hard-working farmers is rising.

- Let me quote a recent study by Oxfam: “America’s cotton farmers receive more in subsidies than the entire GDP of Burkina Faso […], three times more in subsidies than the entire USAID budget for Africa’s 500 million people.”³


Using data from an International Cotton Advisory Committee model, Oxfam has estimated the cost to Africa of US subsidies in 2001-02: it amounts losses of over $300 million. Eight cotton-producing countries in West Africa accounted for about two-thirds ($191 million) of overall losses. Mali lost 1.7 percent of GDP and 8 percent of export earnings; Benin lost 1.4 percent of GDP and 9 percent of export earnings; Burkina Faso lost 1 percent of GDP and 12 percent of export earnings.

**Sugar.** The costs of protectionist sugar policies on Sub-Saharan Africa is similar to what I have described for cotton (loss of market share and exports, declining prices, balance of payment difficulties, loss of Government revenues and more external debt). There is also the mimetic effect of poor countries trying to emulate bad policies, that is, imposing their own distortionary policies, in a clumsy attempt to protect their domestic markets. Lower-cost African producers have been deprived of export opportunities because of the huge distortions in the international sugar market.

**Groundnuts.** Like cotton and sugar, groundnuts provide livelihood and cash income to million of poor farmers in Sub-Saharan Africa. In Senegal, it is estimated that one tenth of the population are involved in its production and processing. Groundnuts accounts for about 2 percent of GDP and 9 percent of exports.

Clearly, if nothing is done to address these problems, Sub-Saharan Africa and many countries in the developing world will experience tougher economic and financial difficulties in the future—and the incidence of poverty will rise. As Mr. Watkins reminded us in his contribution, agriculture plays a minor role in western economies, yet governments in these countries spend $1 billion a day on agricultural subsidies, that is six times the amount allocated to aid. Most of this financial aid goes to large producers who do not really need help. And according to a recent study by a British think tank, the world community would have to double the amount of resources currently devoted to foreign aid ($50 billion a year) in order to meet the MDG. According to some studies, since the world community started discussing the MDG in the early 1990s, the number of poor people (living with $1 a day) has increased by more than 100 million.

African countries have lost an estimated 20 percent of its market share in world trade over recent decades, the value of which is much more than what the continent has received in foreign aid over the same period. Had the continent kept its share of world trade it had in the late 1960s, its exports and income would be some $70 billion higher today. Clearly, the fight against poverty would have benefited from more funding and would have been more credible and successful. Furthermore, in spite of its positive, catalytic effects under certain circumstances, foreign aid can only complement (and should not be a substitute to) government resources. Because foreign aid is fungible, domestic resources are often diverted from priority sectors and allocated to “political” investment projects, as many government leaders assume that the donor community will

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take care of some of their own responsibilities and provide funding for the projects with the highest developmental impact.

An other opportunity cost of inaction is the squandering of resources invested in the various *filières* by African countries over the years to build institutions in rural areas, organize producers, train farmers, establish financing schemes, with the goal of improving agricultural productivity and output. All this social, financial, and human capital is being destroyed by US and EU policies of subsidies.

**III-) WHERE DO WE GO FROM HERE?**

Everyone here knows what the world should do to solve these problems. Mr. Watkins, our main speaker has articulated some of the most straightforward solutions. I can sum them up in a few words: getting rid of all types of trade distortions, subsidies that contradict the letter and the spirit of WTO agreements, and even export support that lead to over-production and declining world prices.

But political equations tend to supersede economic and financial calculations. Therefore, we should try to be realistic in our expectations: complete elimination of subsidies and other forms of government support to cotton, sugar, and groundnuts farmers in the US and in the EU is unlikely. After all, politicians need to do certain things to get elected, even in democratic countries! Moreover, the US has approved the 2002 Farm Bill which will guarantee generous financial support to many farmers for the next 6 years. In the EU case, none of the EU accession countries are cotton producers so there will be no pressure to increase funding for the cotton sector or to reopen the discussion on that topic.

African countries have implemented ambitious reforms over the past decade to reduce their agricultural production costs and become more competitive. These reforms have generated a large supply response and increased exports—unfortunately at a time when prices were collapsing. There is always here and there a little room left for them to increase the efficiency of their agricultural sectors. But we should all recognize that the real solution to the current structural problem of depressed world markets should focus on cutting the large subsidies in the US and the EU. African farmers do not have the political voice and the financial means that their counterparts in Europe and the US have. They only have their good faith, commitment to hard work under extremely difficult circumstances, and their naive belief in fairness. In the western world, there are powerful vested interests who can influence economic policies and the design of international trade rules (including at the WTO). It is really a Battle between David and Goliath.

*For cotton,* it is clear that international prices would be much higher if current government policies in the US and in the EU were to be eliminated as advocated by OXFAM. But since this is unlikely to happen any time soon, we need to look for realistic solutions. In this regard, I would like to refer you to the remedies suggested by the four African trade ministers who have just filed a formal complaint on cotton with the WTO.
• First, it would be important for western countries to recognize the existence of the problem and to acknowledge the fact that poor farmers throughout the world are suffering from the terrible consequences of their agricultural policies. The next step would be to agree on a general progressive framework for ending (or at least, substantially reducing) all types of subsidies and trade distorting measures. To quote James Wolfensohn, “Give us market access; give us a level playing field for our products and goods; give us a trade partnership that is more than just in name. That is what [African] leaders are saying. Is anyone listening?… We cannot ask Africans for more than we ask of ourselves. It is time to stop the hypocrisy on trade that says “do as I say, not as I do.”5

• There is a need to design mechanism to estimate and compensate for the financial losses incurred by African countries because of support schemes in existence in the West and for which Mr. Watkins has provided a very nice typology in his paper. International financial institutions (World Bank, IMF, other multilateral and bilateral donors) should also liaise with the US, the EU, and Japan, to design a partnership to fund and support some essential programs aiming at developing capacity not only in the cotton sector.

• I would also consider examining the type of “decoupled support solutions” already implemented in the framework of the 1992 EU Common Agricultural policy. The idea is for Governments to make income transfers based on past production levels and prices, so that they do not affect current production decisions. Success has been limited so far because not all support mechanisms were substituted with decoupled support. Also, it would be wise to limit the duration of these programs so that everyone understand their temporary nature.

• In the meantime, African countries should pursue their reform programs even further by: reducing production costs in state-owned cotton companies to make them more competitive; getting the private sector involved in cotton-related activities (ginning, transport, purchase and distribution of inputs, marketing); strengthening capacity in farmers association; finding new and creative ways of financing the sector.

For sugar, the prospects for solving some of the existing problems are good: sugar policies in the EU and in US will have to be reformed in the medium-term given the increasing pressures of international agreements and production increases. The timing is good, as a revision of the current EU policy on sugar is scheduled for 2006 while the US Farm Bill will expire in 2007.

• One piece of very good news is the fact that under its initiative called Everything But Arms (EBA), the EU has decided to allow the 48 least developed countries duty-free access to its sugar market by 2009. It is estimated that this could result

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in as much as an additional 2.4 million tons of sugar imports.\(^6\) An encouraging step in the right direction is the fact that in September 2002, the EU has started negotiation of Economic Partnership Agreements with 77 ACP countries to extend duty-free access of the European market to all ACP and allow an additional 6 million tons of sugar into the EU—though this will have to be met with cut in production quotas or much lower prices.

- Another good sign in the medium-term is the fact that the 2004 EU enlargement will further add to pressures for reforming the current sugar policies by increasing production and exports.

- There are also some positive signs in the fact that the US is now facing a big challenge to its sugar program because domestic production is increasing faster than consumption. Furthermore, under the North American Free Trade Agreement, Mexico should be allowed unlimited duty-free access of the US market in 2008—which will probably lead to a huge increase in imports from Mexico if world prices remain low. Indeed, even before the 2008 deadline, the over-quota tariff rate is scheduled to decline by 15 percent a year. Clearly, the US will have to make substantial changes in its existing policies (reducing quotas for domestic production, or lowering sugar prices).

**For groundnuts**, the responsibility of western countries in the current state of affairs is slightly different from what it is for other commodities. Unlike US farm policy for cotton or sugar, liberalization of the US market for peanuts would not have a big impact on world prices nor on exports of African countries. The 2002 Farm Bill has suppressed the production quota for food-quality groundnuts.

- Indeed, the optimal solution may be for the US, the EU, and the international community to pressure the two largest developing economies (China and India) to reform their policies. A new study by Beghin et al.\(^7\) concludes that following full trade liberalization, world market prices would increase by about 19 percent for peanuts, 18 percent for meal, and 17 percent for oil, respectively. The study also indicates that removal of trade distortions by China and India is essential in the peanut products markets. The net welfare gains of liberalizing the markets may be limited in western countries but they would be large for small agrarian economies in West Africa.

- In my view, beyond the liberalization of the market for the raw commodity, it is even more important to push to for the liberalization of the value-added markets.

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\(^6\) It is worth noting, however, that these imports would have to be offset by about 17 percent lower production quotas or increased non-food uses in order to comply with the ACP/EU Sugar Protocol and WTO commitments.

(groundnut oil and groundnut meal). Clearly, in a country like Senegal for instance, this would result in a large welfare gain. Beyond the additional cash income derived from increased exports, African farmers would reap the benefits of job creation, new investments, higher productivity, while national economies would improve their balance of payment and fiscal positions.

With the adoption of the Millennium Development Goals (MDG), the international community has made a bold commitment to fight poverty throughout the world. To me, these goals reflect more than a political statement. They truly represent a moral statement and the foundations of a new social contract between all citizens of the world. They embody what is best in human nature and they symbolize our common quest for higher ideals than ourselves.

Unfortunately, the current US and EU policies for cotton, sugar, groundnuts, and other agricultural products stand in the way of achieving these objectives. Less money for cotton farmers in Burkina Faso, Mali, or Benin means less export earnings, less income for the poor, less government revenues, less money for education, health, and the delivery of other public services. It also means more macroeconomic problems for African countries, more external debt, and more poverty—which in the end cannot lead to a stable and peaceful world.

I understand that solving these difficult problems would imply dealing with political economy issues in the US and EU: but political leaders in the West who are only eager to please constituencies in rural areas should realize that what is at stake here is more important than winning an election. I would even dare say that the credibility of the entire western, capitalist system is at stake, as the credibility of the MDG and other major initiatives like the HIPC. In fact, what we are really dealing with is an issue of global governance, and the need for all governments to find ways of reinventing a multilateral way of addressing burning issues. In this post-September 11 era, it is critical that we all join forces to establish a level playing field for all people of the world (especially farmers from the developing world) so that despair and helplessness do not lead more extremists to give up on humanity’s highest ideals.