



## Note

# Domestic Support in Agriculture: Challenges and Opportunities for East Africa at the WTO

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### Summary

This paper provides a brief overview of the negative impact of trade-distorting domestic support on the agriculture sector in the East African Community (EAC), and how multilateral trade negotiations could be leveraged to reduce the global level of such support so as to boost the agricultural development plans in East Africa.

## Introduction

Agriculture is the backbone of the economic growth in the East African Community (EAC). The sector accounts for 36% of the region's GDP, and almost 60% of its total export income<sup>1</sup>. In addition, 80% of the population in the member countries relies on agro-business activities for their livelihood – most of them are small-scale farmers in rural areas<sup>2</sup>. The agriculture sector is also at the forefront of the fight against hunger in the region, as it provides a food source for both direct consumption and as raw materials for processed foods.

Despite the abundant natural potential of the region, which is endowed with vast arable lands and water bodies appropriate for agriculture and the importance of the sector for economic growth, food security and poverty reduction; the productivity of agro-industry remains relatively low in the EAC region. This is due to several factors including, lack of access to modern technologies, under-developed water management systems, high post-harvest losses, lack of access to finance, climate change effects and trade policies<sup>3</sup>.

When it comes to trade policy and development of the agriculture sector in the EAC region, global trade distortions caused by domestic support measures in developed countries and large developing economies have negatively impacted the region. This issue is one of the main reasons why the region is a net food

importer, which has also caused an agricultural trade deficit and widespread food insecurity in the EAC member countries.

At the national level, designing and implementing domestic support measures such as food-stockholding and subsidies on raw materials, is a common method for East African countries to tackle the food security issue, improving their domestic production and eventually bridging the agricultural trade imbalance between import and export. However, this challenge elevates to a higher level in the region through ways in which developed countries expand their agriculture sector. Many developed countries provide massive subsidies and other forms of protection on agricultural products, which is resulted in a global oversupply of agricultural exports –especially in the EAC region- and correlative lower prices in international markets. With no doubt, this is not in favour of agricultural development efforts in Africa, particularly in East Africa. It also raises the question of whether and how East African countries should continue multilateral economic liberalization in the face of continued agricultural support measures by developed countries<sup>4</sup>. That being said, further development of the agriculture sector in the EAC and expansion of agro- products export from the region, largely depend on how the WTO negotiations on domestic support evolves, and how LDCs and developing countries could potentially push for disciplines to address trade

<sup>1</sup>“Investment in Agriculture”, <http://www.eac.int/sectors/investment-promotion-and-private-sector-development/why-east-africa/investment-opportunities/agriculture>

<sup>2</sup> CUTS International (2009), “Leveraging the Agricultural Sector Through Trade: Opportunities and Challenges in the EC-EAC EPA.”

<sup>3</sup> The African Capacity Building Foundation (ACBF), “The State of the Agricultural Development and Food Security in the East African Community”

<sup>4</sup> FAO (2011), “Why Has Africa Become a Net Importer? Explaining Africa Agricultural and Food Trade Deficit”

distorting domestic support measures.

The on-going agriculture negotiations in the Doha Round seek to further reduce tariffs and trade distorting domestic support<sup>5</sup>. In this context, the EAC member countries seek to ensure that their concerns and interests will be addressed in the negotiations including.

The aim of this brief paper is to shed some light on the impacts of domestic support on the EAC's agriculture sector, and the need to seek redress through strengthened disciplines in the multilateral trading system.

## **Impact of Domestic Support on Agriculture Development Efforts in EAC**

The agriculture sector in EAC is predominantly based on small-scale and semi-subsistence farmers, faced with multiple challenges that have affected their productivity. This has manifested in the region becoming net food importers despite its underutilized potential.

The above scenario makes the EAC dependent on imports and hence vulnerable to price fluctuations and shortages on international markets.

It is well established that amongst the root causes for continued small scale and semi-subsistence agricultural practices in the EAC and other similarly situated regions, is due to lack of incentives to invest in the agriculture sector despite existing potential. This is due to the fact that subsidized agriculture commodities on the

international markets often suppress prices, making un-subsidized agricultural products uncompetitive.

Effectively integrating the EAC in world markets with no doubt boost the regions productivity. This would however call for the region to develop productive capacity through access to requisite technologies, inputs and finance. Importantly, such remedies would have to be complemented with undistorted international markets so as to make the regions products competitive.

Addressing trade distorting support in agriculture that displaces products from the EAC on global markets requires a multilateral approach, for unlike other issues, bilateral or regional arrangements would not suffice. If bigger countries continue to subsidize agriculture products, international market prices will be suppressed resulting in the current cycle that has made the EAC food import reliant despite its potential.

In addition, the EAC member states often suffer from lack of sufficient currency reserves that makes paying for imports even more difficult. Moreover, the region's export is mainly based on traditional agricultural products such as cotton, tea and coffee. The export income of such products, in the light of current price fluctuations in international markets, is not constant and reliable<sup>6</sup>.

The complex matrix of paying for import bills, providing domestic support and advancing other development plans at the same time

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<sup>5</sup> CUTS International (2012), "WTO Agricultural Disciplines and Negotiations: Implications for Equitable Agricultural Development in the East African Community (EAC)"

<sup>6</sup> FAO (2011), "Why Has Africa Become a Net Importer? Explaining Africa Agricultural and Food Trade Deficit"

becomes even more complicated and problematic when adding to the mix trade distortion domestic support measures in developed countries and some of large developing economies.

When as a result of domestic support policies in developed countries and advanced developing economies, an overflow of agro-products comes to international markets, prices drive down. At this point, the export of such agro-products decline in countries whom their similar products do not meet the global price competitiveness. Instead, they become the importer of such agro-products. This phenomenon –often in LDCs and developing countries- results in a set of negative outcomes including, food trade deficit, and reduction of domestic production of agro-products, as well as economic loss for farmers.

For instance, in 2014, LDCs' food trade deficit reached to US\$ 37 billion<sup>7</sup>. In another study conducted by European Commission, by 2023, Africa's trade deficit in volume terms will increase to 44 million metric tons (MT) for wheat and 18 million MT for rice.<sup>8</sup>

A bold example of such market disruption in EAC is the recent trade distortion effect of importing cheap Thai rice in the region. In mid-2013 Thai rice export surged and prices of Thai rice dropped by up to 41.5% from July 2013 to May 2014. That was due to Thai government's disposal of an accumulated rice stock that was bought through a boosting income program from farmers in rural areas. By May 2014 Thai

rice was trading between 29.6% and 39% below average Thai rice prices in the same period two years earlier. Not to mention that this led to down-warding global rice prices. In April 2014, Tanzanian farmers started to complain that they are struggling to sell their rice in the market as the result of imported cheap Thai rice. In an interview, the CEO of Kilombero Plantations Limited (KPL), which supports the development of smallholder rice production in Tanzania, mentioned that “a whopping 4 billion shilling loss -about €1.8 million- as a result of Asian rice imports”. He added that his company holds on to “1,000 MT of rice from the 2012 season and another 5,000 MT from the 2013 harvest, which cannot be sold at a profitable price due to a saturated local market”. Eventually the Thai rice stock disposal program ended in May 2014<sup>9</sup>.

The negative impact of trade distortion domestic support on the economy of LDCs and developing countries is widely acknowledged and some efforts are being made to remedy the situation. FAO data shows that OECD farm support has been declining over the past few decades. Since the mid 1980's, OECD support on agriculture has been shifted from a highly distortive commodity-based support to a decoupled support which reforms agricultural policies so that they less intervene with production decisions- a method which has a lower distortionary effect on trade and production. However, in order to expand non-distortionary support to more OECD countries and more agricultural products, further development of decoupling support should be encouraged<sup>10</sup>. The ideal solution would be to

<sup>7</sup> FAO (2015), “The State of Agricultural Commodity Markets”

<sup>8</sup> European Commission (2014), “Agri-food trade in 2014: EU-US interaction strengthening”

<sup>9</sup> CUTS International (2015), “WTO Agriculture Negotiations Securing EAC Countries' Interest”

<sup>10</sup> FAO, “Farm Support Policies that Minimize Global Distortionary Effects”

agree on multilateral disciplines to abolish and prevent trade distorting support in agriculture.

## Conclusion and Recommendations

It is through the multilateral trade negotiations that the issue of trade distorting domestic support in agriculture can be effectively addressed. Eradication of trade distorting domestic support measures will help the EAC member states to develop the agriculture sector in the region, expand the region's export income on agro-products and eradicate poverty among others.

In the meanwhile, other strategies could be pursued to mitigate the impacts of trade distorting agriculture subsidies on the EAC, these include the following:

- Agricultural production should be more diversified and include more “non-traditional” export products such as organic agro-products flowers, rice, semi-processed fruits and vegetables, so that the region's economy can resist more

effectively when some of the region's agro-products hit by international trade distortions. Kenya is a good example of a member county that has successfully developed its “non-traditional” export commodities.

- Engage with and promote international dialogues that are geared towards redressing negative impacts of trade distorting domestic support on products of interest in the EAC.
- Using a multi-stakeholder approach in formulation and implementation of agricultural development policies, especially domestic support measures.

## References

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