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US must fall in line on cotton subsidy

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The US' farm support legislation is due for revision later this year. Cotton exporters like India should take a cue from Brazil and pressurise the US into bringing down its market-distorting subsidies.

With WTO's Doha Round negotiations stalled till the new US President assumes office, all hopes of a reduction in US cotton subsidy rest on the upcoming revision of current farm support legislation that expires on September 30, 2012.

Though the issue has not received much media attention in India, it has long-term implications for India's cotton and manmade fibre producers already suffering from unsold stocks and slowing demand.

The US Senate Committee of Agriculture has cleared the new farm bill, called 'Agriculture Reform, Food and Jobs Act 2012'. The bill seeks to eliminate direct and countercyclical payments to the farm sector.

However, it proposes increase in support to crop insurance, extension, and horticulture which can become contentious. Although cotton would be one among the list of commodities that would see the largest subsidy cut, there are indications that a subsidy cut on cotton would not be sufficient to completely remove trade distortions.

Among countries that should be watching the US farm bill deliberations is Brazil, which is embroiled in a long-drawn battle over US cotton subsidy at the WTO.

Another Grouping that is closely watching the developments are Cotton-4 (a consortium of four cotton producing African countries Benin, Burkina Faso, Chad and Mali). They had already submitted a proposal to the WTO calling for a global agreement to end all production-related support for cotton in all WTO member nations, but have not met with much success. It would be pertinent to revisit the Brazil-US WTO cotton subsidy dispute.

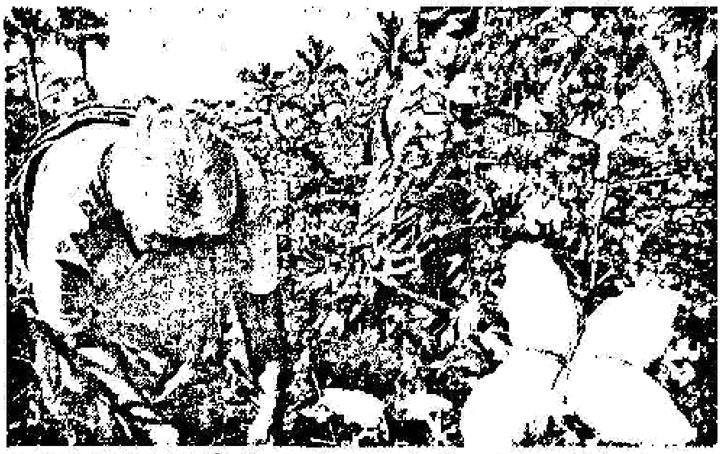
DISPUTE WITH BRAZIL

The origin of the dispute can be traced back to September 2002 when Brazil first took the US to the WTO over latter's trade-distorting subsidies for cotton. Later, Argentina, Australia, Benin, Canada, Chad, China, Chinese Taipei, European Union, India, New Zealand, Pakistan, Paraguay, Venezuela, Japan and Thailand joined the dispute as third parties.

After losing at WTO, the US made some changes in its cotton programme. For example, it abolished payments to induce purchase of relatively high priced US upland cotton ('Step 2'), export credit guarantee programme ('GSM-103'), the fee cap on another export credit guarantee programme ('GSM-102') and supplier credit guarantee programme (SCGP). However, the US introduced some new subsidy schemes in its 2008 Farm Bill, such as countercyclical payments and provisions for marketing loans. Unhappy with the US actions, Brazil asked for a WTO compliance panel, which found that the US has not fully complied with the WTO rulings.

Subsequently, on March 3, 2009, Brazil claimed the right to take retaliatory trade measures. Disagreement over the nature and extent of the retaliation led to both parties requesting for an arbitration panel. The panel permitted Brazil to use countermeasures with respect to trade in goods. It also allowed relaxation in Brazil's commitment under TRIPS and GATS. This forced the US to come to the negotiating table.

As a result, Brazil agreed to postpone the retaliatory actions till the revision of US farm legislation, in return for an annual payment of $147.3 million in technical assistance and capacity-building aid to the Brazilian Cotton Institute.



India's producers of cotton and manmade fibres take a hit due to artificially depressed global prices.

EFFECTS OF US SUBSIDY

Thus, Brazil has somewhat been compensated, but other cotton producing countries have been left in cold. Such countries too can challenge the US cotton subsidy, but that could be expensive and time-consuming.

COTTON SUBSIDY DISPUTE: A CHRONOLOGY

- September 2002: Initiation of WTO dispute by Brazil
- September 2004: Preliminary ruling against the US
- March 2005: WTO Appellate Body ruled against the US Cotton Programme forcing the US to make changes in its subsidy regime
- August 2006: Not satisfied, Brazil requested for a compliance panel that vindicated Brazil's stand
- March 2009: Brazil claimed the right to retaliate that led to setting up an arbitration panel to determine the nature and extent of retaliation
- August 2009: Announcement of arbitration award
- June 2010: Brazil agreed to postpone retaliatory action till the revision of US farm support legislation in return for annual payment of $147.3 million

As per a recent estimate by the Congressional Research Service (CRS) between 1994-2008, US cotton subsidy averaged $5 billion and accounted for roughly one-fourth of its total farm support. Though the US is the third-largest producer of cotton, next to China and India, it is the largest cotton exporter and accounts for 30-40 per cent of the world export of cotton, despite being a relatively inefficient producer.

Of late, the US has been exporting an increasing share of its annual cotton production mainly because of the declining demand of domestic mills. Its exports of cotton as a share of total production have averaged 67 per cent since 2001, up from a 40 per cent average during the early 1990s. To be fair to the US, many other countries such as China or European Union also provide farm subsidies including that for cotton. India is no exception either; however, its subsidy is well within its WTO commitments.

High US subsidy on cotton keeps the international price of the cotton artificially low. This adversely affects the export competiveness of competing cotton-exporting countries, including India, which accounts for roughly 20 per cent of the world export of cotton, or Australia with 7 per cent, Brazil (6 per cent) and West Africa including C-4 countries (5 per cent). For C-4 countries cotton is the key export item. The low international price of cotton (on account of US subsidy) also depresses the demand for and price of other manmade fibres, in particular of viscose staple fibre which is blended with cotton to make yarn, fabric and garments.

When India is faced with a burgeoning trade deficit, every exportable item counts. However, continuing US subsidy on cotton, despite a series of adverse rulings by WTO, hurts India's exports of cotton as well as those of blending materials like viscose staple fibre, or in some cases, synthetic fibres. As if India's export curbs and policy flip flops are not enough, artificially suppressed price of cotton on account of US subsidy deprives the producers of cotton and manmade fibres from getting remunerative prices for their products.

Such market-distorting policies lead to sub-optimal allocation of resources and adversely affect the prospect of the cotton (and manmade fibres) sector that provides livelihood support to millions in India and other poor developing countries in Africa.

In the long run, it will also lead to less acreage being allocated to cotton farming that will jeopardise the steady supply of raw material to India's textile sector, and expose the sector to the fluctuations in international markets. It's time India engaged with US policymakers to get trade-distorting US cotton support substantially reduced or completely removed in this farm bill revision.

It should be noted that 80 per cent of the US cotton subsidy is appropriated by 10 per cent of the farms, hence there's not much justification for its continuance.

The US, being the staunchest proponent of free trade, needs to bring its farm support policy in compliance with its WTO commitments and strengthen the global trade regime.

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