CIDSE and Caritas Europa

Briefing Note on the Reform of the EU Cotton Regime

Cotton is a crucial issue at the WTO that provides a litmus test for the good faith of European and other trade negotiators for the resumption and pro-development conclusion of the Doha Round.

Cotton has become a central development issue in the Doha round. At Cancun, four of the poorest West African states (Burkina Faso, Benin, Chad, Mali) succeeded in converting the elimination of cotton production subsides, their "only specific interest" in negotiations, into a specific agenda item, supported by the 13 other Central and West African countries.

Pascal Lamy and the EU have presented themselves as allies with West African states in their demands at the WTO, stating, "the EU view is that [their] concerns … regarding the cotton sector should be addressed".

However, the demand of the West African countries at the WTO was and still is "for phasing out support for cotton production with a view to its total elimination".[1] Aside from using rhetoric supporting the West African case, the European Commission has so far showed no willingness to accept this proposal. Commissioners Lamy and Fischler are only prepared to "pursue a reduction in trade distorting subsidies within the WTO"[2] and are proposing 60% of payments 'decoupled'[3] from cotton production. This briefing note will explain why the current EC proposals are far from sufficient. We believe that only 100% decoupling of current cotton subsidies would meet the demand of the West African countries.

Cotton is of great strategic importance for development and poverty reduction in many LDCs.

Developing countries in West Africa and elsewhere are very dependent on the world market for cotton for effective poverty reduction and economic development.

There are 2 to 3 million cotton producers in West Africa, whilst some 15 million people depend directly of indirectly on the cotton sector; many of these belong to the

[1] WTO Document TN/AG/GEN/4 of 16 May 2003. The second demand in the this statement was as a transitional measure "until cotton production support measures have been completely eliminated cotton producers in LDC should be offered financial compensation to offset the income they are losing, as an integral part of the rights and obligations resulting from the Doha Round"

[2] 'Proposal for an EU-Africa partnership in support of cotton sector development' European Commission 2004 http://europa.eu.int/comm/trade/issues/global/development/pr120204_en.htm

[3] 'Decoupling' is a term that applies to subsidies that break the link between farm payments and production levels and production decisions. Recent EU CAP reform has been based on this principle, moving away from a system in which producers were paid for what they produced (for example giving money for every bushel of wheat grown) to a direct income payment to producers regardless of their level of production (based on their historical subsidy receipts).

poorest sectors of society.[4] Cotton production in West and Central Africa is often farmed on smaller holdings, in poorer regions, with lower per capita incomes and very limited agricultural diversification options.[5]

Burkina Faso, Benin, Chad, Mali are some of the world's poorest countries, with a Human Development Index ranking of 169, 158, 166 and 164 (out of 173) respectively.[6] These countries accounted for 10% of total cotton exports in 2001. Cotton exports account for 42 % of exports for Mali, 34% for Chad, and 45% for Burkina Faso and 65% for Benin. Due to their non-diversified economies, it is a major source of foreign exchange and government revenue, accounting for more than a third of total export receipts and forming 5-10% of their total GDP[7].

As a recent paper to the European Council by the French delegation stated "the collapse of these sectors would have severe consequences in terms of impoverishment of rural areas, intensification of migration… and destabilisation of [the] concerned countries".[8] It is clear that current trade distortions in the global cotton sector are leading to large-scale loss of revenue for these West African states.

Rich country subsidies are undermining their livelihoods

Cotton subsidies have contributed to a slump in the price of cotton and the erosion of export markets. Since the mid 1990's, the cotton market has suffered from chronic price depression. In 2001/2002 average cotton prices (adjusted for inflation) were lower than at any time since the Great Depression of the 1930s, reaching 42 cents per pound.[9] This has led to 'serious difficulties' for the cotton sector in West and Central Africa.[10] According to the International Cotton Advisory Committee, cotton would have fetched 31 cents more per pound in 2001/02 without subsidisation. [11]

The prime culprit for these distortions is the USA (USD 3-4 billion in subsidies spent annually, with US exports increased by 23% between 1991 and 2001, making the country the biggest cotton exporter[12]). **Nevertheless the European Union's cotton regime also has a significant and measurable impact (EUR 0.8 billion in subsidies spent annually (mainly to Greece, Spain and Portugal), with exports from Greece increasing by 209% between 1991 and 2001[13]).**

A recent study by a respected development institute has shown that EU cotton subsidies have a disproportionate and significant impact on developing country cotton production. Due to the segmentation of the world cotton market, Europe's impact on West Africa is more concentrated (because of its historic trade and transport links and role as an traditional export market) than its total global impact.

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[4] Proposal for an EU-Africa partnership in support of cotton sector development' European Commission 2004 http://europa.eu.int/comm/trade/issues/global/development/pr120204_en.htm

[5] "Understanding the impact of OECD agricultural and trade policies on developing countries and poor people in those countries – piloting an approach with cotton" ODI February 2004

[6] Human Development Report 2002, UNDP 2002

[7] "Understanding the impact of OECD agricultural and trade policies on developing countries and poor people in those countries – piloting an approach with cotton" ODI February 2004

[8] Cotton: European Initiative 'Cotton sector and development in Africa' – Non paper by the French Delegation for the members of the Working Party on Commodities' 29 October 2003, Doc no 88/03 PROBA

[9] 'Cultivating Poverty, the impact of US cotton subsidies on Africa' Oxfam 2002

[10] Proposal for an EU-Africa partnership in support of cotton sector development' European Commission 2004 http://europa.eu.int/comm/trade/issues/global/development/pr120204_en.htm

[11] "Understanding the impact of OECD agricultural and trade policies on developing countries and poor people in those countries – piloting an approach with cotton" ODI February 2004

[12] China is the biggest producer of cotton, but this is mainly for domestic use (only 1% production is exported)

[13] "Understanding the impact of OECD agricultural and trade policies on developing countries and poor people in those countries – piloting an approach with cotton" ODI February 2004

The EU is one of the biggest cotton importers, with nearly 13% of world cotton imports Whilst about a third of the EU's cotton imports come from West Africa, between 20% and 80% of cotton exports from Mali, Burkina Faso, Benin and Chad are being sold on the EU market.[14] The EU accounts for roughly 3% of global cotton production[15]. In terms of volume, however, EU production represents approximately 47% of the EU's internal cotton needs[16] and about 70% of West and Central African exports. So, reduced EU production would allow for substantial growth in imports from the four African countries.

According to a study conducted by the Overseas Development Institute (ODI), a Europe in which cotton production was not supported by subsidies is estimated to contribute to 38% of the projected increase in West and Central African production stemming from the global removal of support for cotton production. In other words, 100% decoupled support in the EU, and the move away from cotton production that this would entail, would mean that significant and disproportional development benefits can be expected for West and Central African countries. Removal of cotton subsidies in Greece and Spain would lead to substantial gains for West Africa, with one projected annual increase in income of US$5 million for Mali, US$8 million for Burkina Faso, US$9 million for Benin and US$12 million for Chad.[17]

Europe's cotton regime has become a damaging system that encourages overproduction.

European cotton farmers receive by far the highest level of support per kilo in the world. Prices paid to cotton farmers in the EU were 154% above world prices in 2001/2002, significantly higher than prices paid in the US.[18] On average, aid for cotton production amounts to an average of EUR 600 million for Greek producers and EUR 200 million for Spanish farmers[19].

Cotton subsidies within Europe are much higher than competing crops which could be grown as an alternative, this encourages a shift into cotton production. A recent report on cotton by the European Court of Auditors showed that current subsidy levels permit a profit margin over twice that of competing crops in the main cotton growing regions whilst "the aid for cotton is 3 to 4 times that paid for crops grown as an alternative"[20]

These incentives have meant that EU production (concentrated in just three countries: Greece, Spain and Portugal) has been increasing significantly throughout the 1980s and 1990s, with annual production of cotton in the EU tripling. This is despite the continued decline in world prices.

Cotton production also has a negative environmental impact, with high levels of chemical use and problems of soil degradation which according to the European

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[14] 'Proposal for an EU-Africa partnership in support of cotton sector development' European Commission, 2004 http://trade-info.cec.eu.int/doclib/docs/2004/february/tradoc_115806.pdf

[15] Special Report No 13/2003 concerning Production Aid for Cotton, European Communities Court of Auditors, Luxembourg, 2003.

[16] Ibid.

[17] "Understanding the impact of OECD agricultural and trade policies on developing countries and poor people in those countries – piloting an approach with cotton" ODI February 2004

[18] 'Proposal for an EU-Africa partnership in support of cotton sector development' European Commission, 2004 http://trade-info.cec.eu.int/doclib/docs/2004/february/tradoc_115806.pdf

[19] Special Report No 13/2003 concerning Production Aid for Cotton, European Communities Court of Auditors, Luxembourg, 2003.

[20] Id.

Commission are "examples of the most negative environmental impacts of agriculture"[21].

Current reform proposals will not lead to significant change

The Commission has put forward proposals for change that will be debated at the 22nd March Agriculture Council next month.

The Commission proposes a move to (60%) decoupled income support measures accompanied by 40% production aid per hectare of cotton.

Partial decoupling as proposed by the Commission will not have any significant impact on the level of cotton under production.

In order to continue receiving the available subsidy package, farmers will be required to continue producing cotton. As the Commission states, "the level of the new area payment has been fixed in order to allow cotton production to continue" albeit "on a reduced area than at present". However this reduction amounts to *only 4% less* than the area under production in 2002/03. [22]

With 40% coupled support a shift from cotton to other less developmentally damaging crops, like maize or durum wheat, is unlikely to occur. The coupled area payment (amounting to almost 600 euros per hectare in Greece and nearly 900 euros in Spain) is significantly higher than the support per hectare for durum wheat, maize and other possible crops.

Rather than supporting West African demands for a "total elimination" of cotton subsidies, the EU proposal will continue to support production at levels very similar to present day production. As the Commission itself notes in relation to cotton "subsidies linked to production can have a distorting effect on markets since they can lead to increased production and exports." [23]

Rather than support a shift away from cotton production, the current proposal supports the status quo. It will have little effect on current EU production and trade patterns and will not create significant additional export opportunities for the West African cotton producers.

What would 100% decoupling mean?

100% decoupling would involve the transfer of current EU subsidies for cotton production into a 100% decoupled income support measure. This would take the form of a Single Farm Payment for farmers, based on cotton areas cultivated in 2001-03. The Single Farm Payment would replace all forms of subsidy paid for cotton produced, achieving two goals.

1. A fall in EU cotton prices in line for world market prices.

This would remove the current high incentives to produce cotton, and encourage a shift of production to alternative crops. It would also allow the EU to achieve the

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[21] See 'Communication from the Commission to the Council and the European Parliament - accomplishing a sustainable agricultural model for Europe through the reformed CAP – the tobacco, olive oil, cotton and sugar sectors http://europa.eu.int/comm/agriculture/capreform/com554/554_en.pdf

[22] Id. The EU proposals put forward a coupled area payment of EUR 280 million for 425,360 hectares. This is only 4% less than the current area planted with cotton (445,134 hectares in 2002/03). In addition there are no sanctions for exceeding the national maximum area; the only consequence is that the average payment per hectare is proportionally reduced.

[23] Proposal for an EU-Africa partnership in support of cotton sector development' European Commission 2004 http://europa.eu.int/comm/trade/issues/global/development/pr120204_en.htm

request of West African countries at the WTO for "the phasing out support for cotton production with a view to its total elimination".

2. A maintenance of income for current cotton producers, guaranteed at income levels based on cotton area cultivated in 2001-03.

This would maintain farmer incomes, allowing the continuation of a healthy rural economy in current cotton growing areas.

In addition the funding for rural development measures, contained in the current EU proposal, would be maintained.

What CIDSE and Caritas Europe ask for:

The Need for 100% Decoupling

CIDSE / CE ask for fully decoupled income support in the cotton sector.

- 100% decoupling is imperative to achieve a development friendly outcome to cotton reform. Only 100% decoupling would enable the shift to other crops that would create a significant move away from cotton production.

- This would reduce world market distortions; create new market opportunities in Europe to West African producers; and provide a signal of good faith from the EU in WTO negotiations, adding to the pressure on the US for change.

This would not negatively impact on small farmers in Europe

- 100% decoupling would see subsidy payments to EU cotton farmers and former cotton farmers continue and their incomes maintained at current levels. But these would not be linked to the growing of cotton, enabling them to produce less developmentally damaging crops (such as durum wheat or maize).[24]

[24] The move away from cotton production would mean a restructuring of current cotton processing industry in Greece and Spain. The current EU proposals provide a generous financial envelope for this process - totalling EUR 107.3 million (EUR 103 million for restructuring measures plus EUR 4.3 million for support to inter-branch organisations of cotton farmers and ginners)