EPRC
ECONOMIC POLICY RESEARCH CENTRE
Towards Sustainable Development

POLICY BRIEF

Issue No. 102 June 2018

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How will the adoption of the Nairobi WTO 10th Ministerial Conference decisions on cotton impact on the East African Community?

Executive Summary

In December 2015, the World Trade Organization (WTO) held its 10th Ministerial Conference (MC10) in Nairobi, Kenya. The meeting adopted the "Nairobi package" of decisions targeting agriculture, cotton and issues related to least-developed countries. This brief examines the implications of the Nairobi package for the development of cotton sector in the East African Community (EAC). The results indicate that the removal of subsidies would reduce cotton production among the top producing countries, reducing their export earnings while increasing both production and export earnings in the EAC. Therefore, the EAC needs to monitor the implementation the agreement and increase cotton production to take advantage of the opportunity.

Introduction

The December 2015 World Trade Organization (WTO) 10th Ministerial Conference (MC10) adopted the Nairobi package. The resolutions included; a commitment to abolish export subsidies for farm exports i.e. export competition.[1] Others include the decision to maintain the Peace Clause on public stockholding for food security purposes, which was agreed in Bali in 2013[2]; a Special Safeguard Mechanism (SSM) for developing countries, and measures related to cotton. The measures related to cotton included: duty free and quota free access for cotton from LDCs to developed countries; reducing trade distorting domestic subsidies for cotton production; and strengthening development assistance for cotton. The Nairobi package obliges rich countries to abolish export subsidies immediately while developing countries have until 2022 to eliminate their own export subsidies. It should be noted that subsidies by the major cotton producers, including the United States (US) and European Union (EU) i.e. for Spain and Portugal, Brazil, India, China etc. were estimated at US$6.5 billion in 2013-14, down from a record US$ 7.4 billion in 2012-13.[3] The above decisions stress the vital importance of the cotton sector to the Least Developed Countries (LDCs).

Countries in the EAC have been engaging in cotton production, trade, and other activities since colonial times and thus the declaration may have significant implications towards their economic development. This brief is based on a titled study "***Outcomes of the Nairobi WTO 10th Ministerial Conference: Implications for the EAC Cotton Sector Development***". This study investigated the implications of the adopted "Nairobi Package" decisions on the development of the cotton sector in the EAC. The study was based on a desk review as well as simulation of the potential effects of removal of subsidies on cotton production, prices and export earnings in the EAC.

Impact on cotton production.

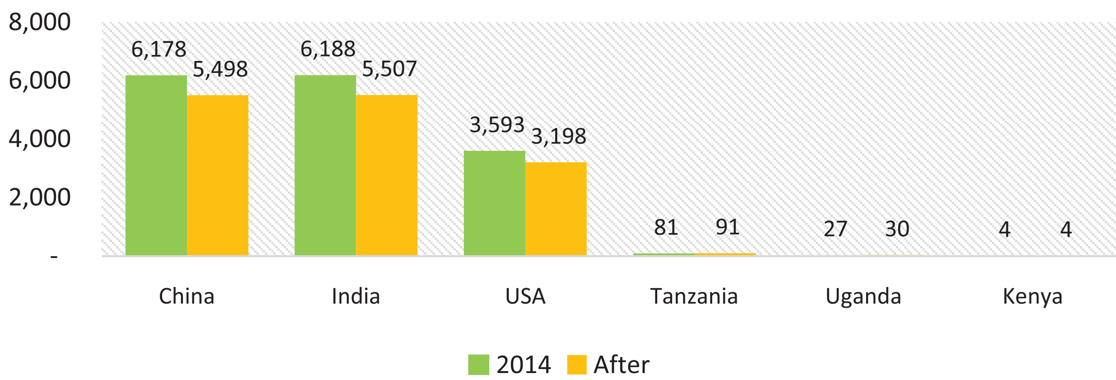
Elimination of subsidies is expected to reduce production among top cotton producers while increasing production among other countries in the EAC. As depicted in Figure 1, representing 2014 production levels, China's and India's cotton lint production would decrease from about 6.18 million to 5.5 million tonnes in each country. The US, which is the leading subsidy granting country would decrease production from 3.6 million to 3.2 million tonnes. In Tanzania, the production would increase from 81,000 tonnes to 91,000 tonnes while in Uganda, it would increase from 27,000 tonnes to 30,000 tonnes. The increase in production in Kenya is negligible.

The reduction in production amongst the major producers as a result of eliminating subsidies is quite significant in terms of cotton supply to international markets. This is because of the big country effect, leading to a reduction in global cotton supply. This is consistent with the findings by FAPRI (2002) which indicated that US cotton production would decline by 11 percent with the removal of subsidies.[4] A reduction in production levels by major producers corresponds with an increment in production levels by small producers in the EAC. Although, the increase in production by EAC producers is not significant in the global scale, it is still positive for producers in the region as it corresponds with an increase in prices.

Impact on exports.

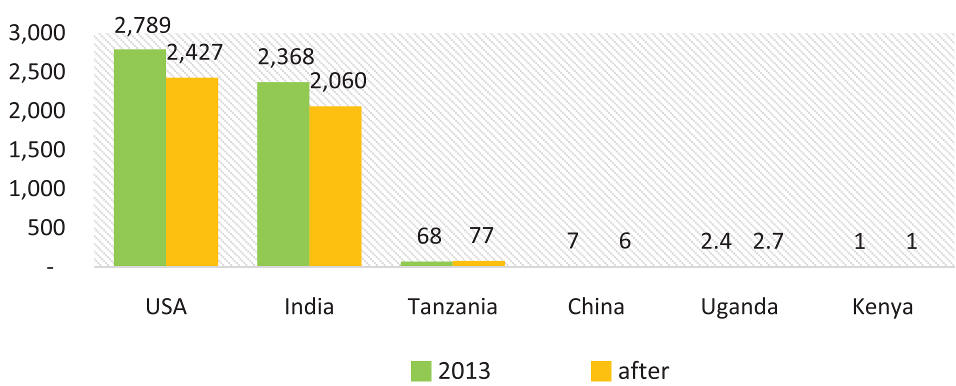
In addition to decreasing the production levels of cotton, a drop in subsidies would lead to a reduction in the amount of cotton exports among top producers and exporters while increasing the export quantity of non-subsidizing cotton producers in the EAC. Figure 2 shows that US, the world's top exporter of cotton would have its exports reduced from 2.79 million tonnes to 2.43 million tonnes with India's export volumes reducing from 2.37 million to 2.1 million tonnes. China's export quantities would not drop much as most of the cotton produced in the country is consumed domestically. This could be because producers in subsidizing countries would experience an increase in the unit

Figure 2: Export quantity after drop of subsidies - (cotton lint '000)



Source: authors' computation from FAO, 2016

Figure 1: Cotton lint production after drop of subsidies- ('000) tonnes



Source: authors' computation from FAO, 2016 cost of production hence the need for additional costs in terms of input if they are to maintain the same level of production.

In the EAC on the other and, export quantities increase overall. In Tanzania, export quantities would increase from 68,000 tonnes to 77,000 tones while in Uganda, exports would increase from 2,400 tonnes to 2,700 tonnes. Kenya's exports would not change much. This is consistent with FAPRI (2002) which found out that with the elimination of subsidies, US cotton export would decline by 13 percent, EU by production by 79 percent while exports from Africa would increase by 12.3 percent.

Impact on EAC cotton production and export earnings

As indicated in Table 1, cotton production per kilogram would increase in the EAC with the elimination of subsidies among developed countries. Export earnings would also increase at each assumed percentage increase in prices i.e. 15 percent, 20 percent and 25 percent. In Tanzania, production would increase from 68 million to approximately 77 million kilograms. Export earnings of US$125 million would increase to US$161 million to US$169 million and US$175 million with assumed increment in prices at 15 percent, 20 percent and 25 percent respectively. In Uganda on the other hand, elimination of subsidies in developed countries would increase production from 2.7 to 3 million kilograms. Export earnings of US$5.5 million would increase to US$5.7 million, US$5.9 million and US$6.1 million with a respective price increment of 15 percent, 20 percent and 25 percent. In the case of Kenya, removal of subsidies would increase production from 1million kilograms to 1.1 million kilograms while export earnings would increase from US$1.8 million to US$2.3, US$2.4 and US$2.5 million with a respective price increment of 15 percent, 20 percent and 25 percent. The increase in production and export earnings for EAC countries with the removal of subsidies is more significant because it corresponds with a decrease in production and export earnings of major cotton producers and subsidizing countries. This would facilitate the development of the cotton sector in the region. EAC countries must therefore put in place additional measures to take advantage of this expected scenario with the implementation of the Nairobi package.

Conclusion and policy implications

The results based on our simulation, suggest that the removal of subsidies would lead to an increase in cotton prices to the benefit for producers in the EAC. This is because the major cotton producing and subsidizing countries would experience a drop in production and export quantities while EAC countries would experience an increase in production and export quantities. Our findings are consistent with a theoretical understanding of subsidies and their effect on production. Moreover, they supports previous studies of the effect of subsidies showing that the elimination of subsidies would lead to an increase in prices as production levels amongst major producers would decrease.

Table 1: Cotton lint production and export earnings with the elimination of subsidies

	Production in Kilograms		Export earnings in 2014 (USD millions)			
	With subsidy in developed economies	Without subsidy in developed economies	With subsidy in developed economies	Without subsidy and 15% increase in price	Without subsidy and 20% increase in price	Without subsidy and 25% increase in price
Tanzania	68,000,000	76,700,900	124.6	161.6	168.6	175.6
Uganda	2,695,200	3,000,000	5.5	5.7	5.9	6.2
Kenya	1,000,000	1,123,000	1.,8	2.4	2.5	2.6

Source: Authors' computation from Index Mundi (2017)

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Although cotton production in the EAC has fluctuated over the years, elimination of export subsidies presents a good opportunity for EAC cotton farmers as this would increase both the prices and quantities produced. To develop the EAC cotton sector using the Nairobi package, the following measures should be considered;

i) The EAC countries need to monitor the implementation of the decision on the elimination of export subsidies by the WTO. This is because the removal of subsidies, as demonstrated by the study leads to better cotton prices in world markets.

ii) There is a need to increase cotton production to take advantage of increased markets upon the elimination of subsidies. As the study demonstrates, major cotton exporters notably the US will experience a decline in exports after eliminating subsidies. This void could be filled by smaller countries in the EAC who should be able to increase their export quantities.

Endnotes

1 WTO (2015). Tenth WTO Ministerial Conference, Nairobi 2015, The Nairobi package, available at, https://www.wto.org/english/thewto_e/minist_e/mc10_e/nairobipackage_e.htm (retrieved on 11/04/16).

2 This is a decision by WTO members, reached during the 9th Ministerial Conference in Bali where members shall refrain from challenging through the WTO Dispute Settlement Mechanism, compliance of a developing member with its obligations under Articles 6.3 and 7.2 (b) of the Agreement on Agriculture (AoA) in relation to support provided for traditional staple food crops in pursuance of public stockholding programmes for food security purposes.

3 (International Cotton Advisory Committee. 2014). Production and trade policies affecting the cotton industry. Washington DC: International Cotton Advisory Committee.

4 FAPRI (2002), 'The Doha Round of the World Trade Organisation: Appraising Further Liberalisation of Agricultural Markets', Working Paper 02-WP 317, Food and Agricultural Policy Research Institute, Iowa State University and University of Missouri-Colombia.

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