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Countervailing Measures

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COMPLAINT OF THE EUROPEAN COMMUNITY AGAINST THE UNITED STATES CONCERNING SUBSIDIES ON THE EXPORT OF FLOUR

This paper is submitted by the Delegation of the European Community with a view to enabling the Committee to review the facts of the case in accordance with the provisions of Article 17:1 of the Agreement on Interpretation and Application of Articles VI, XVI and XXIII of the General Agreement on Tariffs and Trade (hereinafter referred to as "the Code") and to facilitating conciliation.

I. THE FACTS

On 17 January 1983, the United States signed a "Memorandum of Understanding" regarding the sale of one million metric tons of wheat to Egypt over a period of twelve to fourteen months beginning on 1 March 1983.

The Agreement contains a price clause offering the buyer the option between a price of US\$160 C&F per metric ton under highly preferential credit conditions (20 per cent of the credit being interest-free) and a price of US\$155 C&F per metric ton with the credit guarantees usually accorded by the United States. The second alternative was chosen and the agreed price is therefore US\$155 C&F per metric ton of flour.

The Memorandum of Understanding explicitly states that the United States Government Agency which signed it and which is responsible for its execution (the Commodity Credit Corporation (CCC)) shall provide a subsidy, in payment or in kind, to assure export at the agreed price.

(a) The existence and the nature of the export subsidy are thus clearly demonstrated and, what is more, were recognized by the United States in the bilateral consultations held, which produced the following details.

The export subsidy will be awarded by tender, in kind in the form of wheat from government stocks furnished free of charge to the successful bidder. United States millers participating in the transaction must undertake to supply a certain quantity of flour at the price per metric ton of US\$155 C&F Egypt and, in compensation for the loss suffered because of this selling price, they ask for a payment in the form of the donation of a certain quantity of wheat from government stocks; the miller or millers which ask for the lowest quantity win the contract and receive the wheat free of charge. As this wheat constitutes a payment, it is not necessarily used for making the flour actually delivered to Egypt, which can come from other wheat.

In view of the way in which it is granted, the amount of the subsidy cannot be precisely established in advance. It may be calculated only by determining, on the basis of prevailing prices, the value of the quantities of wheat received by the successful bidders free of charge, and, to date, according to the information provided in the consultations, no tender has been consummated. Nevertheless, this amount can be estimated by various means, one being by comparison with the selling prices at present charged by United States millers exporting to Egypt.

Owing to their competitive position, United States millers, up to the conclusion of this Agreement, supplied Egypt only through sales on preferential terms (i.e. PL480 sales, so named after the United States public law which instituted them). These sales are made on long-term credit conditions (fifteen to forty years) and at very low interest rates (2 to 3 per cent), which, in effect, means a price reduction of the order of 40 to 70 per cent. Nevertheless, PL480 selling prices are real prices for the United States supplier, who is paid immediately by the credit-granting agency (the CCC) and are arrived at by tender at Washington.

In its issue of 25 January 1983, the professional publication of the United States milling industry, "Milling and Baking News", made such a price comparison: "The midpoint price in the most recent PL480 flour transaction with Egypt was \$245 a tonne f.a.s. (free along side) gulf. Ocean freight costs on bagged flour moving to Egypt have been in a range of \$45 a tonne, which would bring the delivered cost to \$290 a tonne, based on the market at the time of the PL480 business. Subtracting \$155 a tonne to be paid by Egypt would require a payment-in-kind subsidy equal to about \$135 a tonne of flour".

The situation described is based on market value in January 1983, and, while the selling price is unalterable, market value may change, along with freight costs, especially as the United States Government has just decided that 50 per cent of deliveries must be made by United States flag vessels, which means significantly higher freight charges.

Under these conditions, the amount of the subsidy can be reasonably estimated today at US\$130-150 per metric ton, and this does not take into account the additional subsidy entailed by the United States flag clause.

(b) The quantitative effect of the "Memorandum of Understanding" entered into by the United States authorities with Egypt means a quasi-doubling of world exports of United States flour and a total takeover of the Egyptian market.

Article II of the "Memorandum of Understanding" stipulates that the quantity specified (one million tons), when combined with other United States sales under PL480 and with humanitarian donations, shall comprise the entire quantity of Egyptian imports for the duration of the Understanding. If import needs prove to be greater than those envisaged, the Article provides that new negotiations shall be held to enable the United States to meet them.

Moreover, in the bilateral consultations, the United States did not deny that Article II would enable it to become the exclusive supplier to Egypt.

Egypt is the biggest market in the international flour trade, accounting at present for approximately 20 to 25 per cent of world trade. The annexed table surveys the sources and development of Egypt's flour supplies.

The Egyptian market has traditionally been a very important export market for the European Community, in fact its biggest export market, since it has accounted for approximately 25 per cent of the Community's total exports. What is more, the Community has been Egypt's main supplier for more than fifteen years.

The emergence of the United States as the second supplier of the Egyptian market is more recent (1975 and 1976). It is essentially due to the rapid and massive expansion of exports reported to the World Wheat Council as exports under special conditions, i.e. for the most part PL480 sales, with only a small proportion of donations. What are termed commercial sales of United States flour remained relatively small and, while they have been irregular, their appearance coincides with that of exports under special conditions.

Whatever one's views may be about the distinction between commercial sales and special sales and their consequences for the calculation of traditional shares of the market, in any case the fact remains that the purpose and effect of the "Memorandum of Understanding" is clearly to enable the United States, during the term of the Understanding, to secure for itself the totality of the Egyptian market's requirements and the monopoly of commercial sales.

In these circumstances, the displacement of the exports of other suppliers, who thus find themselves thoroughly shut out of the market, is therefore manifest, and even intentional.

(c) The effect of the "Memorandum of Understanding" in terms of selling prices is measured by comparison with the selling prices usually charged on the Egyptian market.

United States special sales to Egypt under PL480 can obviously not serve as a basis for determining the prices prevailing on the Egyptian market since they are, on the one hand, firm prices resulting from tenders organized at the Egyptian Embassy in Washington and limited to United States suppliers only and, on the other, theoretical prices to the buyer, who, because of the considerable credit granted, will actually be paying only a fraction of those prices.

On the other hand, international tenders open to all constitute a realistic basis for determination, especially as they involve nearly the totality of Egypt's commercial purchases, and that country makes very extensive use of the mechanism of international tender to cover its import requirements.

The Community has reviewed the last tenders by invitation of international bids held in the months preceding the signature of the Memorandum of Understanding in dispute. The prices are as follows:

- tender of 20 November 1982: 50,500 t awarded, comprising:
 - 24,000 t (Spain) at \$169.90/t
 - 8,000 t (Italy) at \$169.94/t
 - 6,000 t (Italy) at \$170.40/t
 - 12,500 t (Netherlands) at \$171/t;

- tender of 18 December 1982: 62,500 t awarded, comprising:
 - 10,000 t (various origins, including Community IPT) at \$168.90/t
 - 6,000 t (Italy) at \$174/t
 - 6,000 t (Italy) at \$174.85/t
 - 6,000 t (Italy) at \$176.95/t
 - 6,000 t (Italy) at \$177.25/t
 - 10,000 t (Spain) at \$177.90/t
 - 6,000 t (Italy) at \$178.50/t
 - 12,500 t (Netherlands) at \$179/t;

- tender of 15 January 1983 (two days before the signature of the "Memorandum of Understanding"): 46,000 t awarded, comprising:
 - 8,000 t (Italy) at \$175.48/t
 - 2,000 t (Italy) at \$179/t
 - 10,000 t (Spain) at \$177.90/t
 - 8,000 t (Spain) at \$179.90/t
 - 8,000 t (Spain) at \$180.90/t
 - 10,000 t (France) at \$181.53/t.

It can be seen that, for a quantity of approximately 150,000 t, i.e. comparable to that of one phase of the delivery schedule of the "Memorandum of Understanding", the prices charged by the traditional commercial suppliers fall within a range of \$170 to \$180 C&F Egypt. It should be noted that these prices do not relate only to suppliers from the European Community (Spain, 60,000 t) or to Community wheat (IPT flour).

Although it is true that commercial flour prices - which are affected by wheat prices - are subject to certain fluctuations over time, the fact remains that at the moment the United States fixed its selling price at \$155 C&F, the prices on the Egyptian market (and on other world markets) were \$15 to \$25/t higher.

The above difference has been intentionally underestimated so as to avoid any contestation. The estimate does not take into account the difference in quality between European flour (produced from less expensive soft-type wheat) and United States flour (produced from more expensive qualities of wheat - Hard Winter or Dark Northern Spring), which actually increases that difference.

Moreover, the price of \$155/t is not only below the usual prices for flour on the Egyptian market, but even below world quotations for wheat. The C&F price Egypt corresponds to a price of approximately \$120/t f.o.b. or f.a.s. United States "Gulf", according to United States estimates, which by the way are underestimates since freight costs between United States and Egypt actually amount at present to more than \$40/t. However, quotations for wheat f.o.b. Gulf, reproduced in the wheat market report published by the International Wheat Council, showed the following levels:

- Hard Red Winter (ord.) f.o.b. Gulf: 167 at \$165/t
- Soft Red Winter, f.o.b. Gulf: 132 at \$138/t
- Western White, f.o.b. Pacific: 169 at \$172/t

If one bears in mind that, as a general rule, between 1.25 and 1.5 tons of wheat, depending on differences in the ash content of the flour, are needed to make one ton of flour, the undercutting is abundantly proved by the fact that under this "Memorandum of Agreement" a ton of flour is being sold more cheaply than a ton of wheat of the least expensive quality (although the flour will in actual fact be produced from wheat of more expensive qualities: Hard Red Winter or even Dark Northern Spring).

Under these circumstances, it emerges very clearly that the price of \$155/t for flour C&F obtained with the help of export subsidies cannot but undercut the usual prices of other suppliers to the Egyptian market.

II. COMPATIBILITY OF THE "MEMORANDUM OF UNDERSTANDING" WITH THE PROVISIONS OF THE GENERAL AGREEMENT AND THE SUBSIDIES CODE

The sales of flour under this "Memorandum of Understanding" are effected with the help of export subsidies, and the Community does not at all question the right of the United States, or of any other contracting party, to make use of export subsidies for agricultural products provided that the disciplines of Article XVI:3 of the General Agreement, as interpreted by Article 10 of the Code, are observed.

(a) Both Article XVI:3 and Article 10:1 specify that the granting of export subsidies must not make it possible to have more than an "equitable share" of world export trade in the product in question.

Examination of the facts has clearly demonstrated, however, that the purpose and effect of the "Memorandum of Understanding" was to displace the exports of the traditional suppliers to Egypt. Consequently, this agreement clearly falls under the provisions of Article 10:2(a) of the Code and, in the opinion of the Community, is therefore incompatible with the provisions of Article XVI:3 of the General Agreement and Article 10 of the Code.

¹ 24 February 1983, document PNR115, page 7.6, table 7.5

(b) Article 10:3 of the Code also states: "Signatories further agree not to grant export subsidies on exports of certain primary products to a particular market in a manner which results in prices materially below those of other suppliers to the same market".

Examination of the facts of the situation prove that the United States is engaged, under the agreement in dispute, in granting an export subsidy for the Egyptian market which makes possible, and is even aimed at, a price materially below that of other suppliers, and what is more is even very definitely below world price levels for the primary product used.

The "Memorandum of Understanding" thus constitutes a violation of the obligation resulting from Article 10:3 of the Subsidies Code.

III. INJURIOUS EFFECTS RESULTING FROM THE USE BY THE UNITED STATES OF SUBSIDIES INCOMPATIBLE WITH THE CODE

There are numerous injurious effects, a number of which are analysed below:

(1) The displacement of Community flour exports resulting from the total take-over of the Egyptian market for the benefit of the United States means a loss in export volume for the Community equivalent to the displacement.

Of the million tons of flour envisaged by the "Understanding" for "commercial" sale by the United States to Egypt, it can be reasonably estimated, on the basis of "commercial" exports traditionally effected by the United States to the Egyptian market, that more than 900,000 tons are the object of an improper take-over to the detriment of other suppliers to Egypt. That figure is provisional and intentionally underestimated to avoid any contestation, for if one examines the data recorded by the International Wheat Council (see Annex) and expressed in terms of wheat equivalent, one finds that the United States had sales, regarded by it as "commercial", of the order of 100,000 t of flour (or approximately 140,000 t of wheat equivalent) only two times, during the 1975/76 and 1978/79 marketing years.

This loss of 900,000 tons in trade volume may (on the basis of an average cash price of \$175 per ton of flour) be roughly estimated at US\$175.5 million, most of it borne by the European Community, which is by far Egypt's main supplier.

It thus seems incontestable, without having at this stage to determine more precisely the injury suffered in loss of export-trade volume by the European Community, that the injury is considerable.

(2) The injury suffered by the European milling industry (production sector) also deserves examination. The loss in flour export volume suffered by the Community inevitably means, for the European milling industry, an effective reduction in its output, its sales, its market share, its profits, the return on its investments and the utilization of its capacity.

On the basis of the "milling margin", i.e. of the value added in processing wheat into flour, that injury may be globally estimated at approximately ECU 30 million.

(3) Lastly, the price of \$155 C&F charged by the United States for a quantity of 1 million tons, or almost a quarter of the world market, exerts a powerful depressing effect on world prices for flour, and even for wheat, for it is clear that many buyers of flour will want to obtain prices, if not similar to at least closer to, the United States price on the Egyptian market. If, however, one notes that this price is clearly below the very cost of the primary product, as is shown by the international wheat quotations, it is obvious that all flour exporters are suffering very serious injury. Moreover, it is not excluded that the price charged by the United States may also do injury to exports of wheat or prices of wheat, inasmuch as it makes flour cheaper than wheat.

Although it is difficult, without thorough economic analysis, to quantify this third form of injury, it is nevertheless very real and very onerous.

IV. In conclusion, the European Community considers that, by the sale of flour to Egypt under the "Memorandum of Understanding" in question, the United States has granted an export subsidy in a manner incompatible with the provisions of the General Agreement as interpreted and applied by the Code and, in so doing, has injured the European Community.

It notes that in the bilateral consultations held on 1 March 1983 no mutually satisfactory solution could be arrived at, for the United States was not able to provide any new elements that could justify its conduct. In particular, while proclaiming that it considered the conditions under which it granted its subsidies on the exports to Egypt consistent with the provisions of the Code, it refused to identify the provisions of the Code which, in its opinion, justified those subsidies.

Lastly, the United States rejected compromise proposals aimed in particular at repairing the injuries sustained, without advancing any counter-proposal.

That is why the Community wishes the Committee, in keeping with the spirit and letter of Article 17 of the Code, to review the facts of the case and to lend its good offices for the development of a mutually satisfactory solution.

To that end, and while remaining prepared to consider other proposals, the Community wishes the United States to be encouraged, in the absence of renunciation or modification of the disputed sale, to compensate the injury suffered by the Community and its flour exporters.

Imports by the Egyptian Arab Republic of wheat
and wheat flour (wheat equivalent)

('000 tonnes)

Imports by the Egyptian Arab Republic of wheat
and wheat flour (wheat equivalent)

('000 tonnes)

		82/83		83/84		84/85		85/86		86/87		87/88		88/89		89/90		90/91		91/92							
		W	F	W	F	W	F	W	F	W	F	W	F	W	F	W	F	W	F	W	F						
Commercial	EEC ¹	1,407	308	281	355	4	480	937	529	751	400	840	655	709	675	50	540	95	652	666	936	984	634	818	1,393	43	801
	US	-	-	-	-	-	-	267	-	566	1	593	-	489	140	325	-	687	79	313	341	283	117	1,065	94	1,314	67
	Canada	-	-	-	-	-	-	-	-	-	-	-	-	-	-	89	-	466	-	64	-	-	-	-	1	73	-
	Australia	-	-	1,318	-	1,850	-	729	-	736	-	848	-	1,015	-	1,034	-	1,194	-	1,230	-	1,649	-	1,821	-	1,547	-
	Argentina	-	-	-	-	-	-	-	-	-	-	16	-	-	-	64	-	-	-	-	-	-	-	-	-	-	-
	USSR	-	-	-	-	44	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
	Romania	-	-	-	-	-	-	138	-	203	-	139	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
	Bulgaria	-	-	-	-	35	-	62	8	121	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
	Spain	46	227	-	99	44	-	21	-	-	38	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
	Turkey	-	-	-	-	-	-	113	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
		1,453	535	1,599	454	1,977	480	2,267	557	2,378	439	2,436	655	2,213	815	1,562	540	2,442	731	2,273	1,077	2,936	752	3,724	1,468	2,977	868
Special	EEC	MD	10 ²⁾	4	218	5	110	11	166	-	78	5	102	3	95	32	64	-	-	MD	MD	MD	MD	-	150	-	206
	US	-	14	-	16	-	5	-	6	-	16	301	29	457	125	1,173	560	789	426	1,106	406	956	450	751	550 ³⁾	1,071	660
	Canada	16	16	459	31	-	44	-	28	-	-	-	6	9	69	53	4	54	1	34	2	35	-	6	-	30	-
	Australia	-	-	10	-	10	-	-	-	-	-	-	10	-	-	-	-	20	-	22	-	20	-	25	-	40	-
	Finland	-	-	-	-	-	-	-	17	-	3	-	16	-	-	-	-	-	-	-	-	-	-	-	-	-	-
	Sweden	-	36	-	2	-	-	2	24	2	29	-	30	-	16	-	4	-	8	-	-	3	-	4	-	2	-
	Switzerland	-	-	-	5	-	-	-	-	-	-	6	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
		16	86	474	272	15	159	13	224	2	140	306	172	476	261	1,274	681	813	409	1,129	442	978	489	776	710	1,111	898
Commercial and special	EEC	1,407	318	285	373	9	590	948	693	751	479	844	757	712	770	82	604	95	652	666	936	984	635	818	1,343	43	1,007
	US	-	14	-	16	-	3	267	6	566	17	894	29	946	265	1,498	560	1,476	347	1,419	549	1,240	567	1,836	644 ³⁾	2,385	727
	Canada	16	16	459	31	-	44	-	28	-	-	-	6	9	158	53	467	54	65	34	2	35	-	7	73	30	-
	Australia	-	-	1,328	-	1,860	-	729	-	736	-	848	-	1,025	-	1,034	-	1,216	-	1,233	-	1,649	-	1,846	-	1,547	-
	Argentina	-	-	-	-	-	-	-	-	-	-	16	-	-	-	64	-	-	-	-	-	-	-	-	-	-	-
	Finland	-	-	-	-	-	-	-	17	-	3	-	16	-	-	-	-	-	-	-	-	-	-	-	-	-	-
	Sweden	-	36	-	2	-	-	2	24	2	29	-	30	-	16	-	4	-	8	-	-	3	-	4	-	2	-
	USSR	-	-	-	-	44	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
	Romania	-	-	-	-	-	-	138	-	203	-	139	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
	Bulgaria	-	-	-	-	36	-	62	8	121	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
	Spain	46	227	-	99	44	-	21	-	-	38	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
	Turkey	-	-	-	-	-	-	113	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
		1,469	620	2,073	726	1,993	639	2,280	761	2,350	579	2,742	821	2,689	1,076	2,836	1,221	3,255	1,140	3,403	1,519	3,914	1,241	4,500	2,198	4,088	1,766

Source: IWC Record of operations.

¹Ten-member EEC²UK³Figures corrected by US