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The European Agricultural and Trade Policies

at a crossroads

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August 31, 2011

The European Agricultural and Trade Policies

at a crossroads

1. Brief CAP history
 2. The necessity of a new reform
 3. Concluding remarks on the post-2013 CAP
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The European Agricultural and Trade Policies

at a crossroads

1. Brief CAP history

- 1.1 CAP objectives and principles
- 1.2 Rapid relative success...
- 1.3 ...but limits which lead to timid adjustments
- 1.4 The decisive *McSharry* Reform (1992)
- 1.5 The Agenda 2000
- 1.6 The 2003 Reform

2. The necessity of a new reform

3. Concluding remarks

(1.1) CAP objectives and principles

□ Rome Treaty (1957)

Treaty establishing a European Economic Community : common market, customs union and common policies (trade, transport and agricultural policies)

5 Objectives assigned to a CAP:

- increase agricultural productivity by promoting technical progress and ensuring the optimum use of the factors of production, in particular labour
- ensure a fair standard of living for farmers
- stabilise markets
- assure the availability of supplies
- ensure reasonable prices for consumers

□ Stresa Conference (1958)

- Single prices
 - Community preference
 - Financial solidarity
-

(1.2) rapid relative success...

Common Organization of Agricultural markets (COM)

→ Markets regulation tool (production, marketing, export, etc.).

→ **Guaranteed Price**

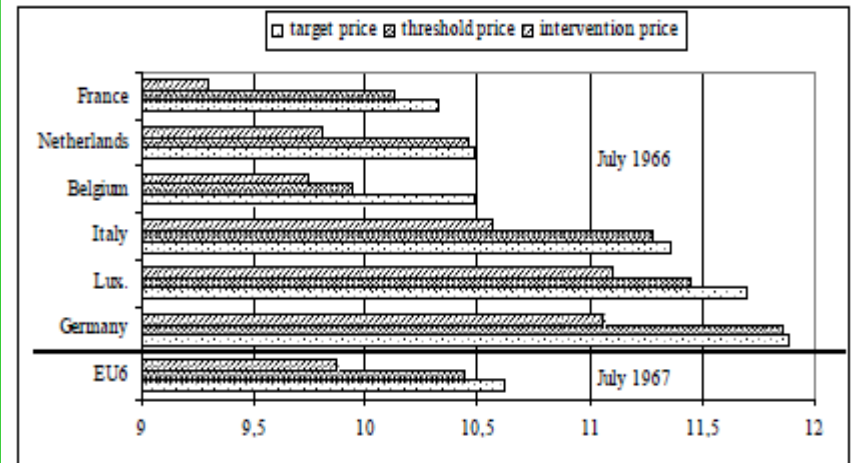
Rapid positive results:

→ stop food shortages

→ self-sufficiency achievement

→ structural adjustment and modernization

National and common institutional prices for wheat other than durum, July 1966 and 1967, prices in units of account per 100 kg



Source: European Commission (1966, 1967).

Degree of self sufficiency for selected agricultural products in EU, France and Germany, 1956-1960, 1971-1972, 2001-2002, per cent

	EU6/15			France			Germany		
	1956-60	1971-72	2001-02	1956-60	1971-72	2001-02	1956-60	1971-72	2001-02
wheat	90	111	116	109	164	186	70	93	133
rye	98	105	147	103	118	115	107	103	175
barley	84	110	123	123	184	260	65	84	121
grain maize	64	68	99	105	174	237	2	20	84
total cereals	85	98	114	110	164	200	77	83	124
sugar	104	122	128	118	164	210	92	101	149
whole milk powder	nd	nd	201	115	191	369	63	93	145
skim milk powder	nd	nd	132	131	139	120	93	198	279
beef and veal	92	89	109	102	112	117	87	90	171
total meat	95	94	106	101	96	113	86	87	94

Note: Due to lack of data, 2001-2002 degrees of self sufficiency for sugar on the one hand, whole and skim milk powders on the other hand, are those for 1999-2000 and 1998-1999 respectively.

Source: European Commission (1975, 2000, 2001, 2003).

European vs. world prices, 1967/68

**Table 1. European threshold price as a % of world price
1967/1968 marketing year, CU/100 kg**

Agricultural products*	European threshold price	World price**	European threshold price as % of world price
soft wheat	10.73	5.79	185 %
durum wheat	16.14	8.07	200 %
rice	17.96	15.34	117 %
barley	9.07	5.67	160 %
grain maize	9.01	5.63	160 %
white sugar	22.35	5.10	438 %
cattle	68.00	38.82	175 %
pigs	56.71	38.56	147 %
poultry	72.33	55.00	131 %
eggs	51.14	38.75	132 %
butter	187.44	47.25	397 %
olive oil***	115.62	69.84	166 %
Oilseeds***	20.19	10.11	200 %

* The marketing years varies accordingly to the agricultural product.

** The world price corresponds to the European threshold price minus taxation or support.

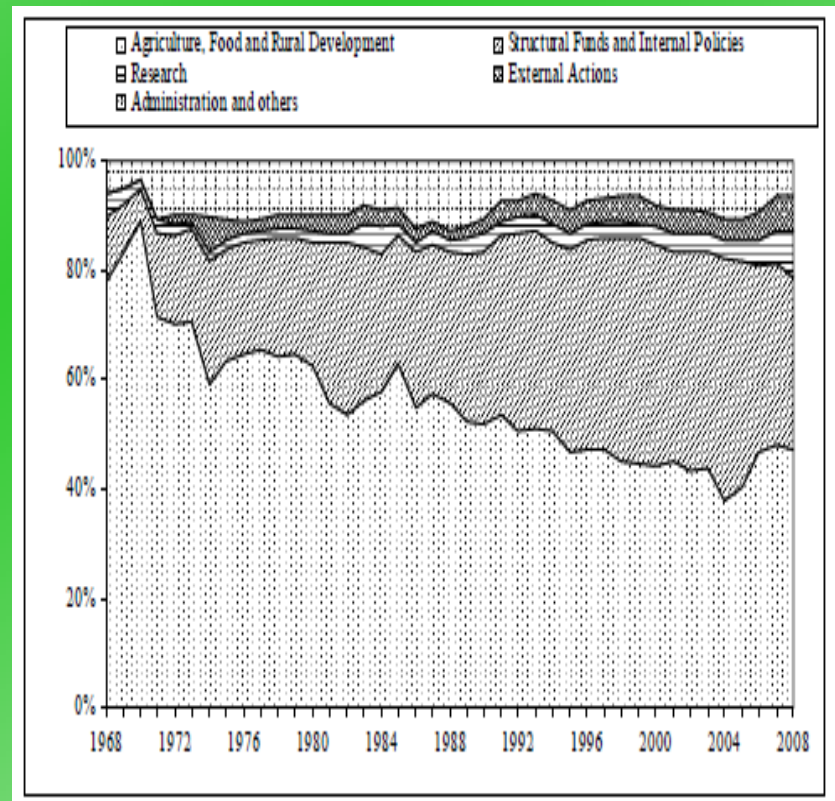
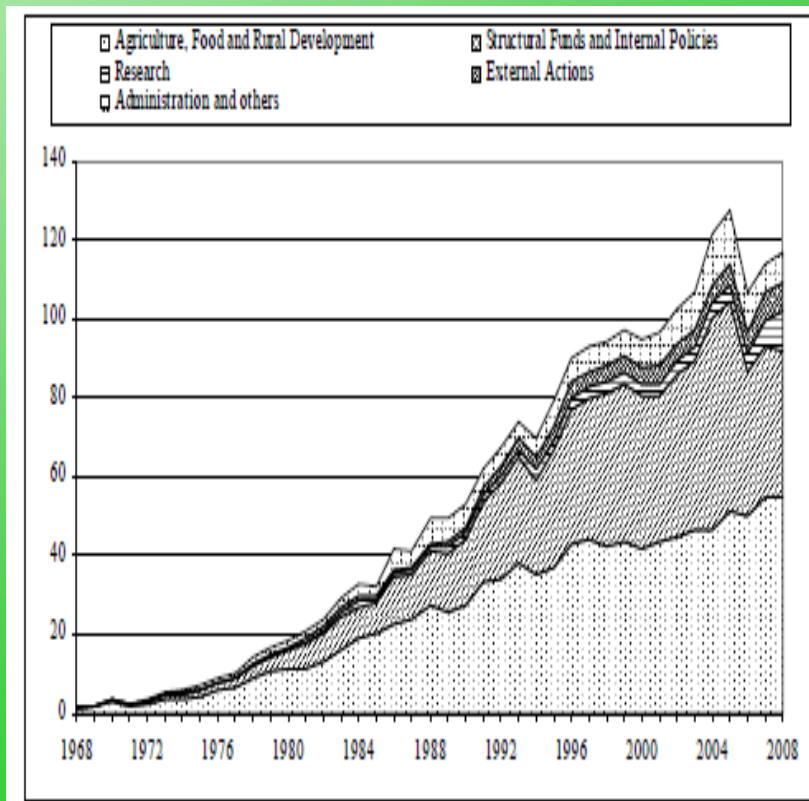
*** The prices include direct support to European producers.

Source: European Commission, 1970

(1.3) ...but **limits** which lead to **timid adjustments**

- ❑ **Excessive production (→ stock)** due to high guaranteed prices (without quantitative limitation)
 - **quotas**,
 - **export subsidies**,
 - other measures (co-responsibility levies, stabilization process or maximum quantity guaranteed, voluntary set-aside, retirement incentives, diversification and extensification subsidies)
 - ❑ **Third countries criticisms** because of high tariffs on the borders (traced by high guaranteed prices) and export subsidies (unfair competition) → "*Farm fortress*"
 - ❑ **Budgetary tensions** because of intervention without limits, CAP expenditures absorbed 2/3 of the European budget
 - British rebate (1984), unbalanced budget (1988)
-

Evolution of European budget expenditures, 1968-2008, billion euros, %



(1.4) The decisive *McSharry* Reform (1992)

- ❑ Shift from price support to **direct payments**
 - crops: guaranteed price cut by 35% + compulsory set aside
 - beef: guaranteed price cut by 15%

 - However, direct payments are linked to acreage (area), production and number of livestock. (coupled payments → Incentives to over-production are still existing).

 - ❑ **Agri-environmental** measures implementation

 - ❑ The 1992 Reform contributed to the conclusion of the **Uruguay Round** (1994) which disciplines, for the first time at the multilateral level, agricultural policies through an **Agricultural Agreement**.
-

(1.5) The **Agenda 2000**

- ❑ Mainly in order to prepare **EU enlargement** to central and eastern European countries. Also to prevent WTO dispute with the end of the “peace clause” (2003) → New CAP Reform (1999) which deepens the 1992 Reform.
 - New cut in price support compensated by direct payments (bringing closer EU prices and world prices)
 - Statement of 2 pillars within the CAP :
 - Pillar 1 : market support and direct payments
 - Pillar 2 : rural development measures

 - ❑ Recognition of a **multifunctional** agriculture → maintenance of landscape and countryside, territorial cohesion, environmental protection, animal welfare, public health, etc.

 - ❑ Implementation of **voluntary** modulation → reorientation of funds from Pillar 1 to Pillar 2 (quasi not used)
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(1.6) The 2003 Reform

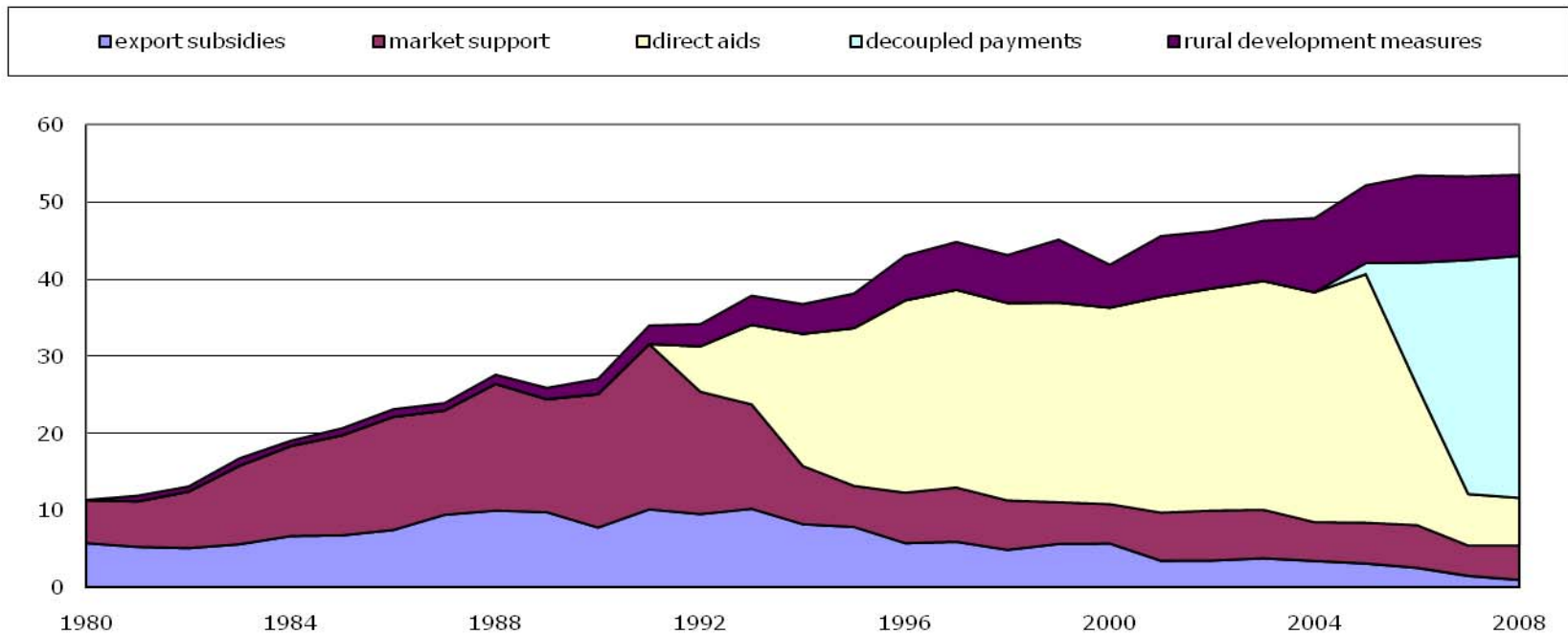
- This Reform deepens previous ones (1992, 1999) and challenges the **internal inconsistencies** of the CAP regarding public opinion will.
 - **Single Farm Payments** (SFPs) cut the link between support and production of specific products (**partial decoupled** subsidies). The new Member States will apply a simplified **Single Area Payment Scheme (SAPS)** until 2010
 - Direct payments are conditioned on the maintenance of the the land under good agricultural conditions and on the respect of EU standards relative to public health, animal and plant health, environment and animal welfare (**cross-compliance**).
 - **Compulsory** set-aside: requirement for arable farmers to leave 10% of their land fallow
 - **Compulsory** modulation (5% per year by 2007): shifting money from direct payments to rural development measures

 - A “**health check**” in 2008 introduced further adjustments
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Evolution of CAP expenditures, 1980-2008, billion euros

Evolution of CAP expenditures, 1980-2008, billion euros

(source: EC, DG Agri, Unit I.1)



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1. Brief CAP history

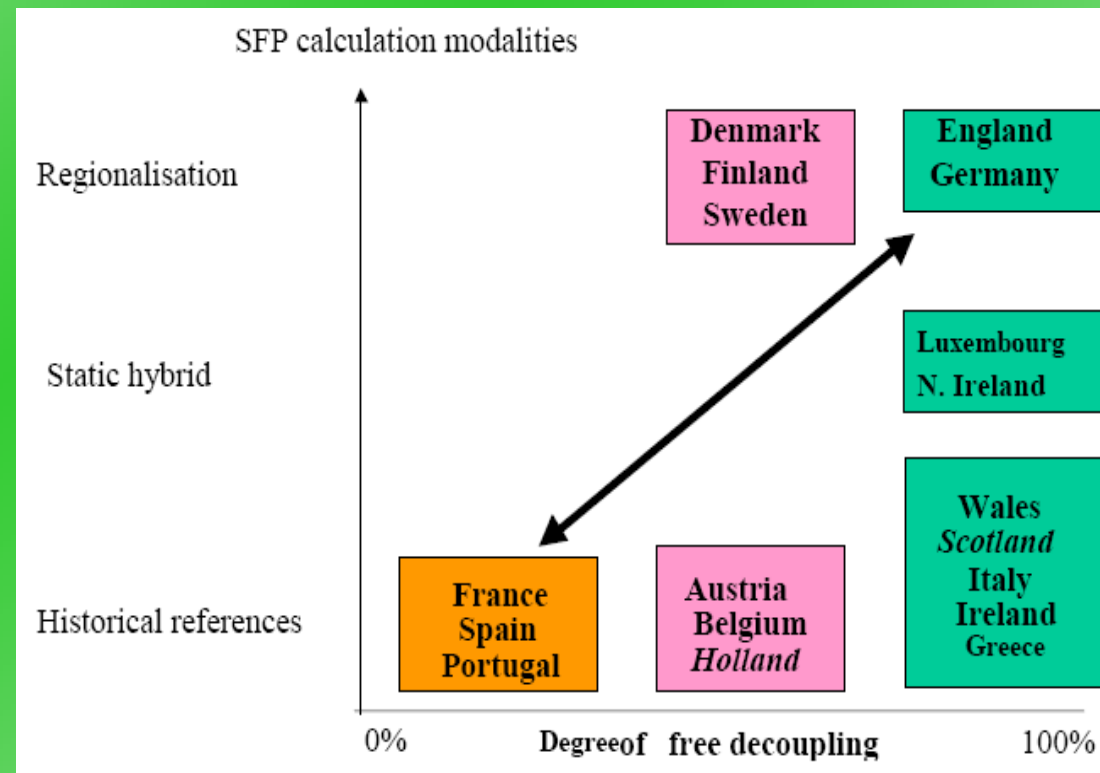
2. The necessity of a new reform

- 2.1 Efficiency issue
- 2.2 Equity issue
- 2.3 Environmental issue
- 2.4 Rural Development issue
- 2.5 Budgetary issue
- 2.6 International issue
- 2.7 The 2008 "Health Check"

3. Concluding remarks

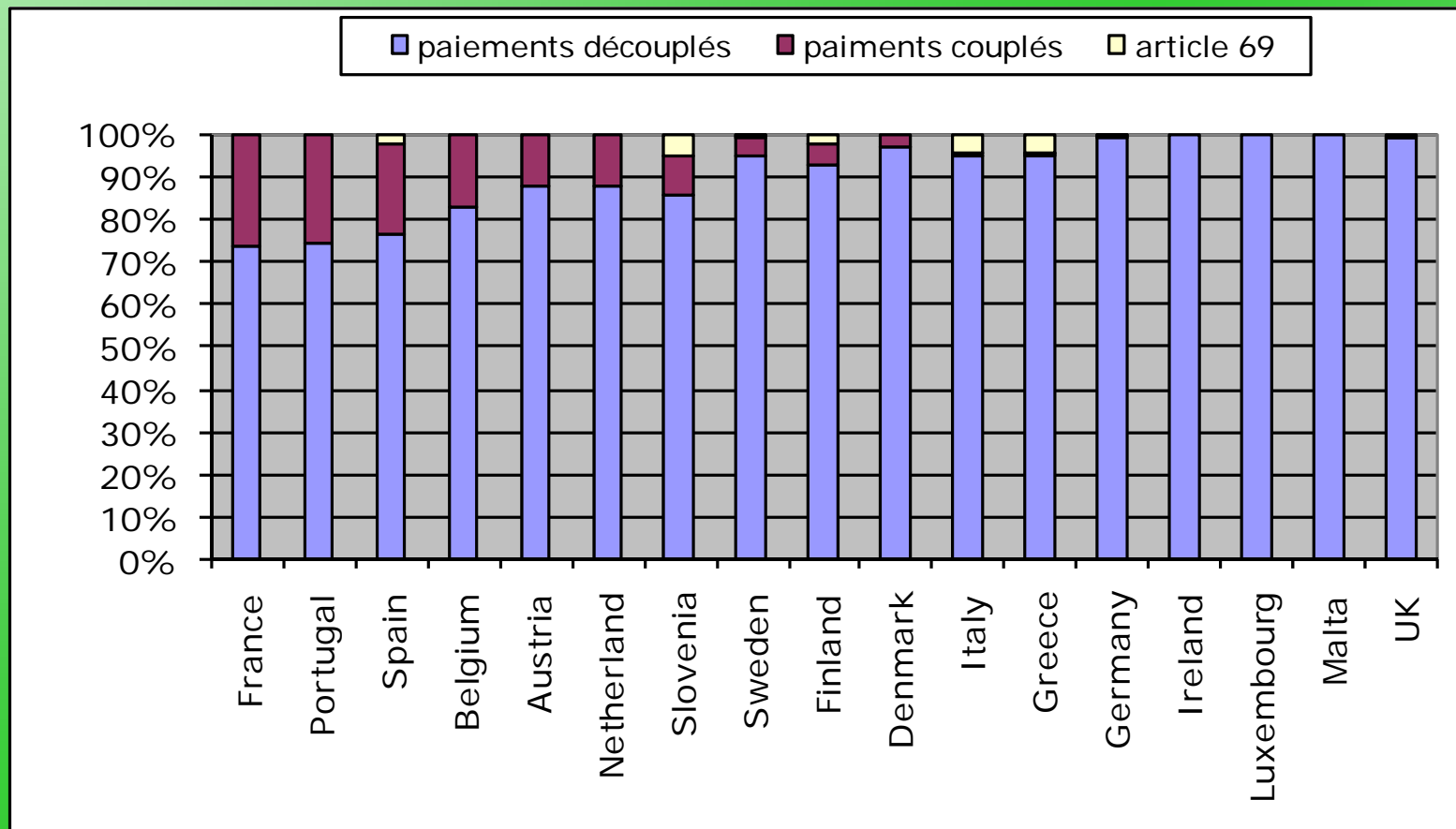
(2.1) Efficiency issue : national implementation of decoupling

- full versus partial decoupling
- historical (individual) references versus regional (mutual) references
- Competition distortions
- Premises of **CAP Re-nationalization...**
- For NMSs, **rural development** measures are more pertinent...



(2.1) Efficiency issue : direct payement targeting

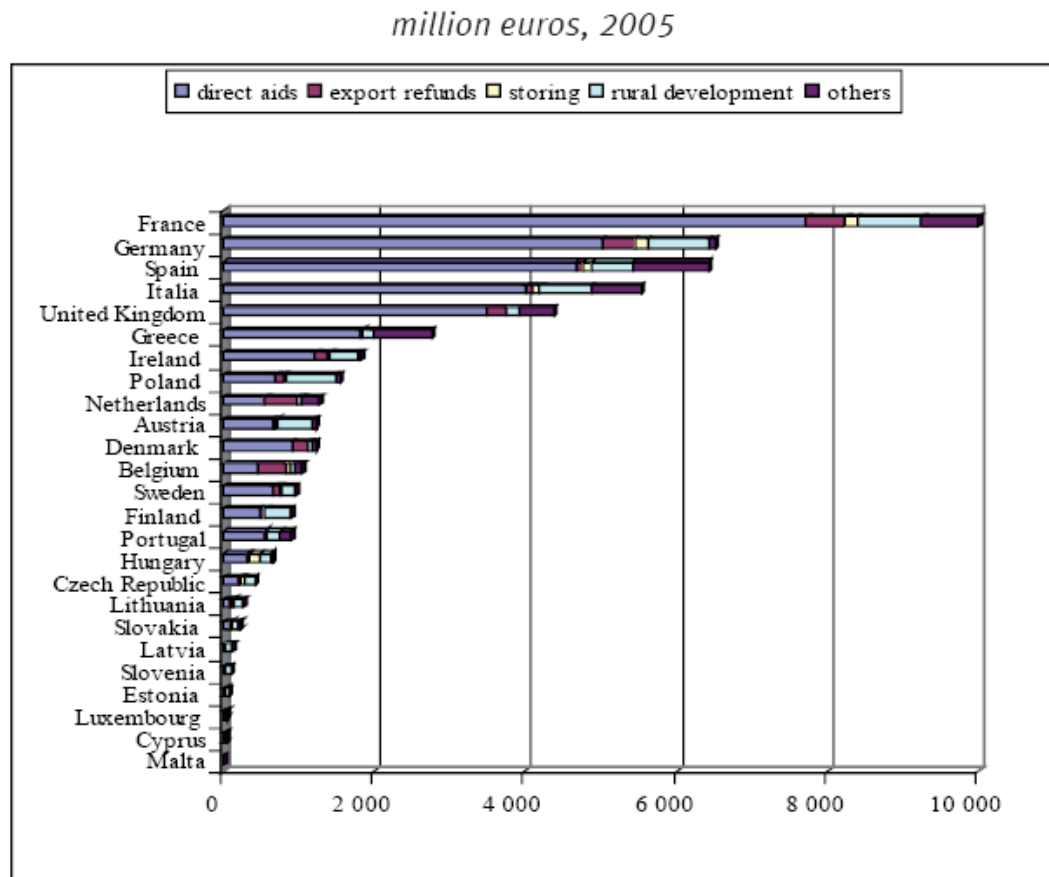
Data: 2007



(2.2) Equity issue

→ Distribution of support among MS and instruments

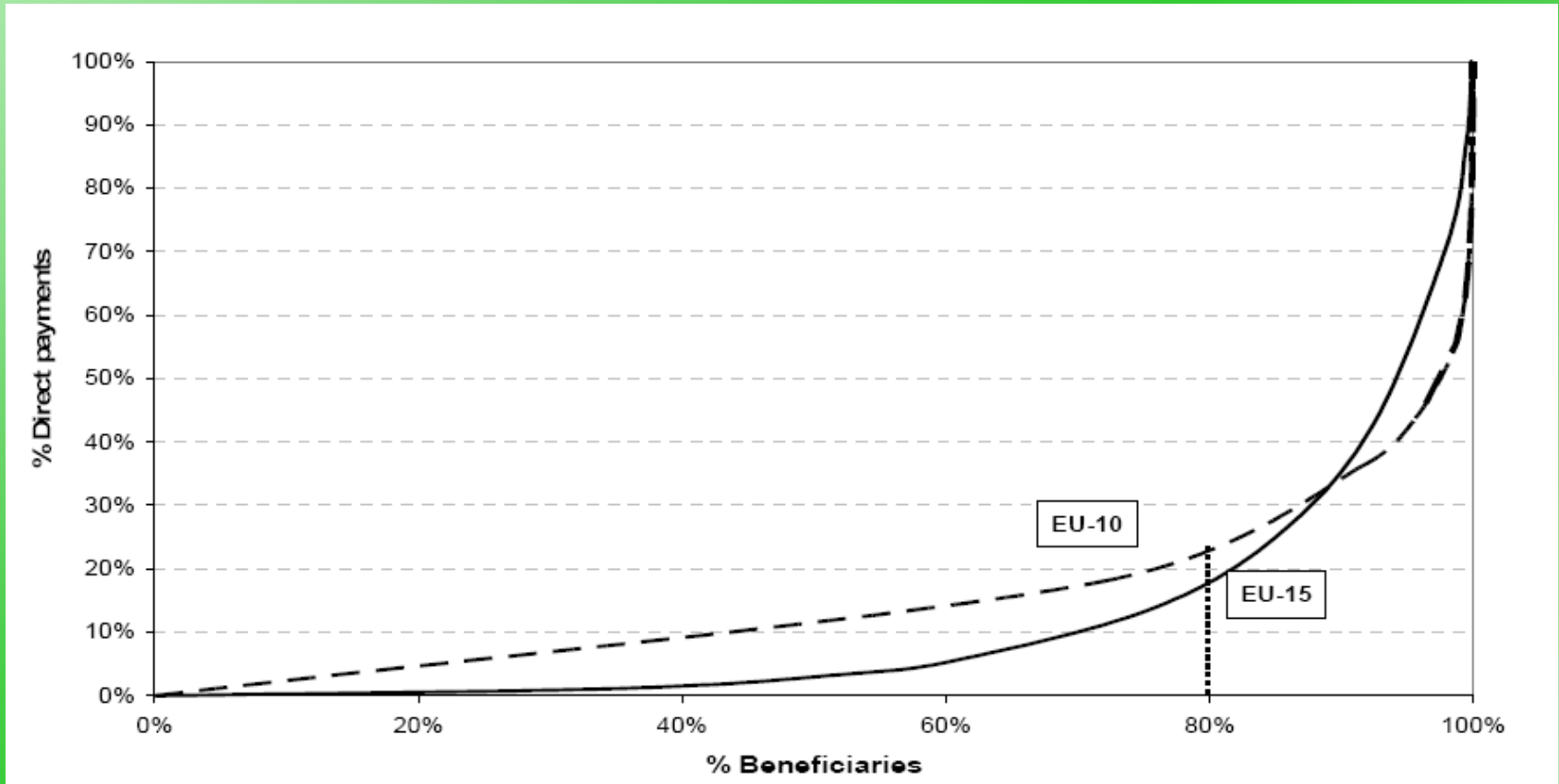
Figure 4: CAP expenses allocated by Member State and measure category



Source: European Commission

(2.2) Equity issue

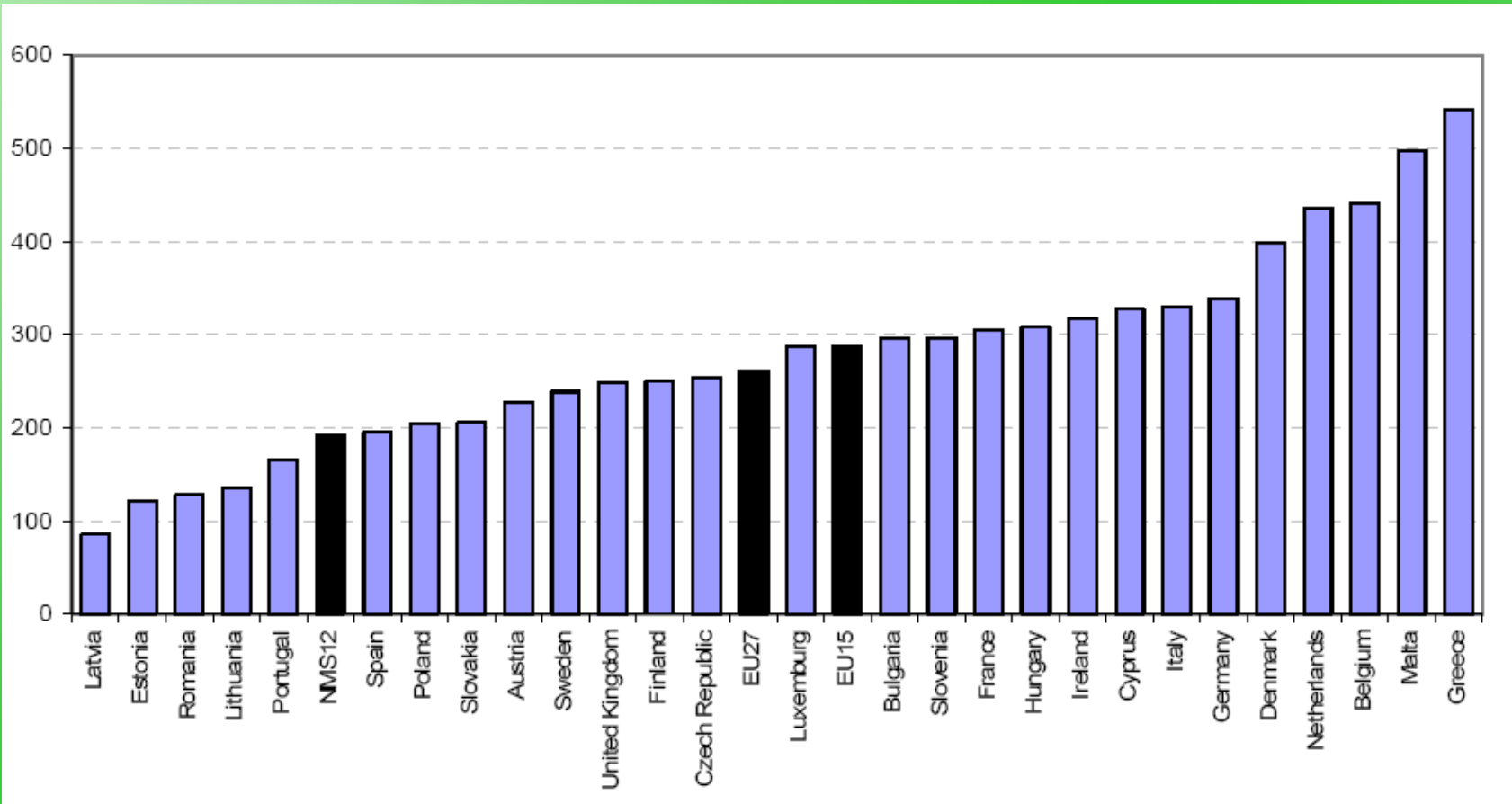
→ Distribution of direct payments among beneficiaries



source: Velazquez, 2008

(2.2) Equity issue

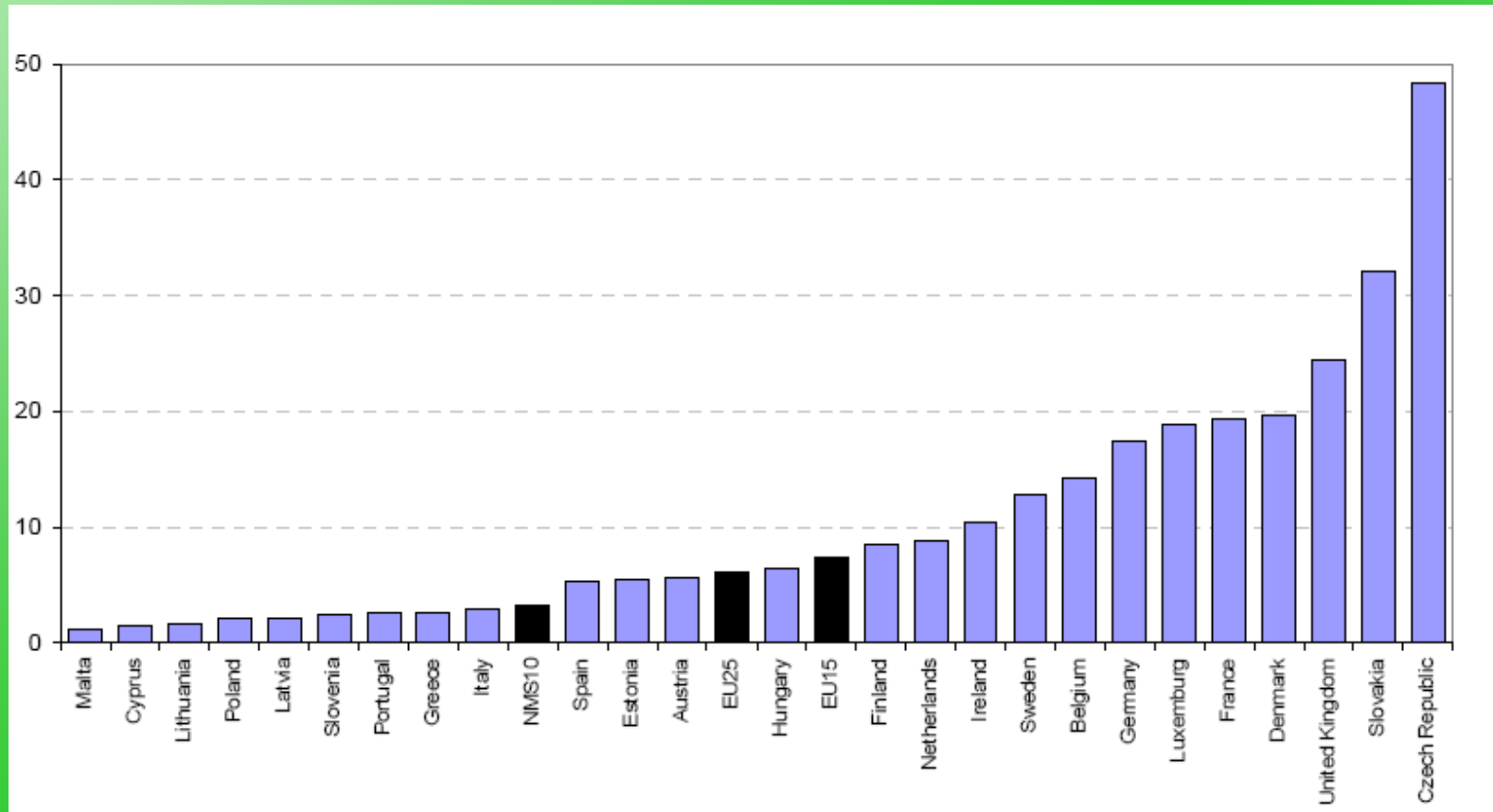
→ Average direct payments per MS (in € per hectare)



source: Velazquez, 2008

(2.2) Equity issue

→ Average direct payments per MS (in €'000 per beneficiary)

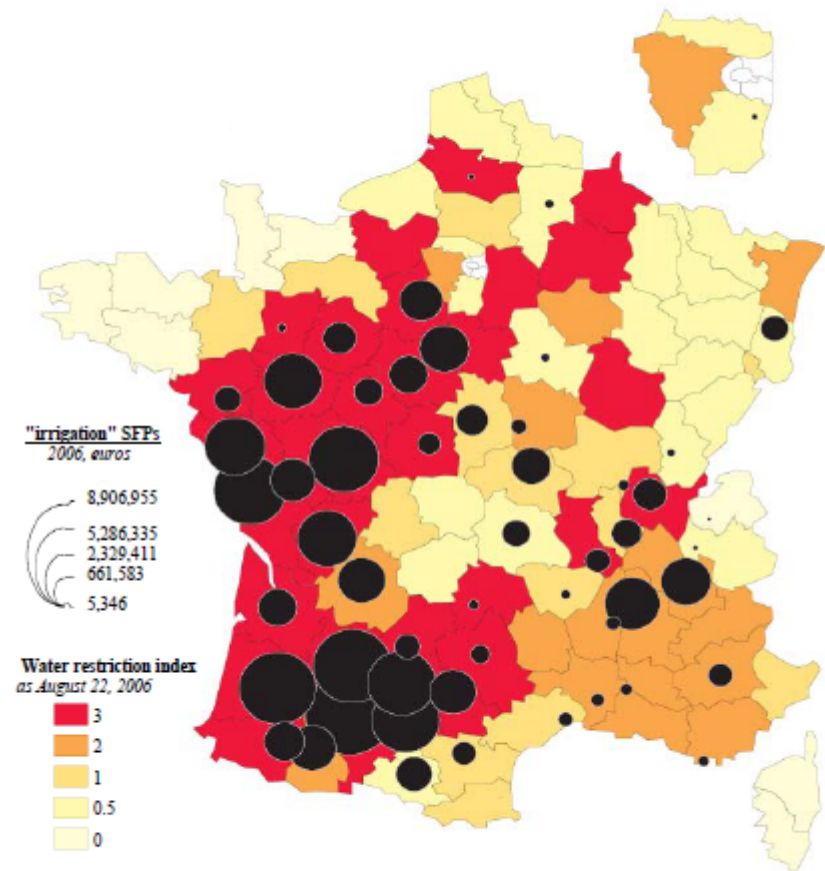


source: Velazquez, 2008

(2.3) Environmental issue

- Historically, the CAP contributed to:
 - an increase in the used of chemical inputs
 - an increase in intensification and regional specialization of production
 - an increase in irrigation
- Agri-environmental measures challenges
- Harden Cross-compliance

Irrigation SFPs and drought,
2006, euros



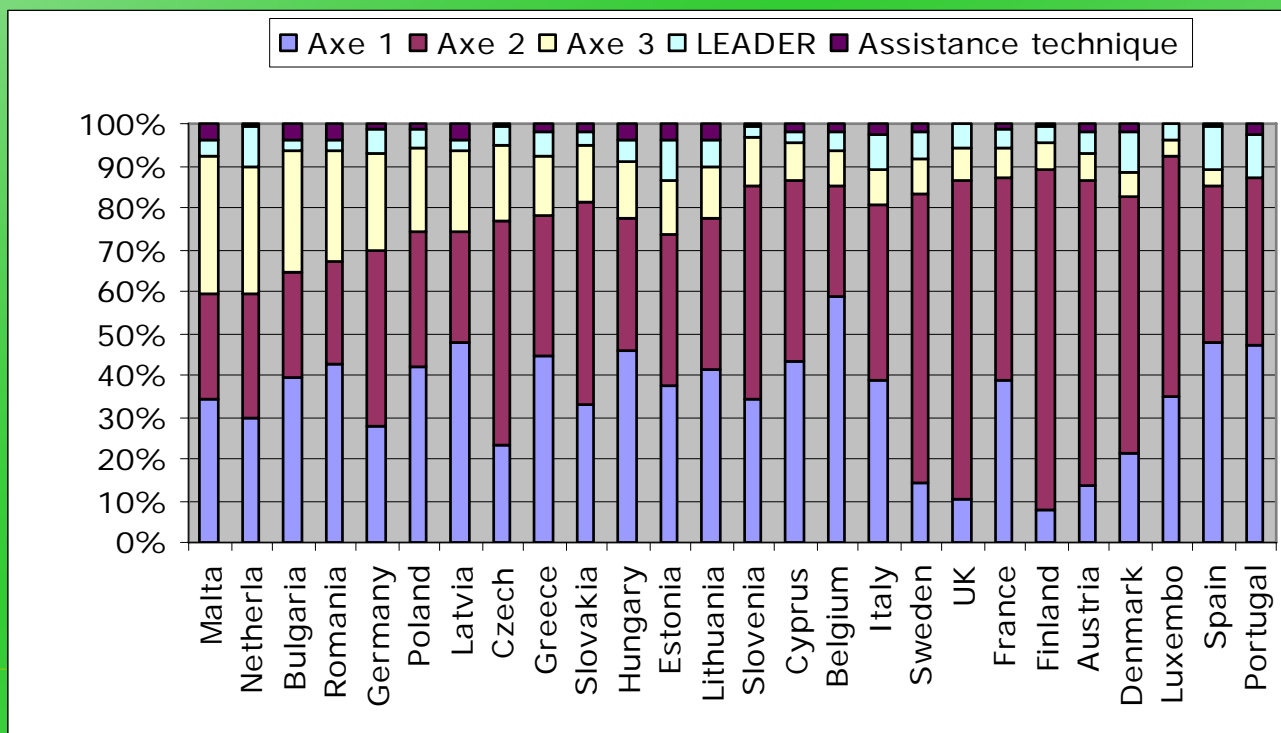
Map prepared with Philcarto: <http://philcarto.free.fr>

Source: Data from French Ministry of Food, Agriculture and Fisheries and French Ministry of Ecology and Sustainable Development; Author's calculations.

(2.4) Rural development issue

2007-2013 financial period

- Axis 1) Improving the competitiveness of the agricultural and forestry sectors
- Axis 2) Improving the environment and countryside
- Axis 3) Improving the quality of life in rural areas and encouraging diversification
- Axis 4) Leader approach

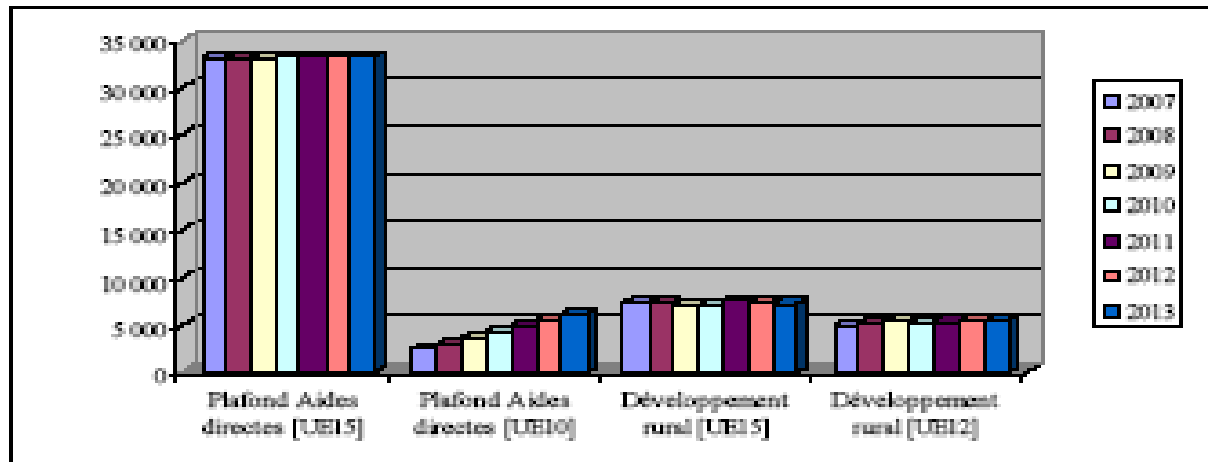


Source: European Commission

(2.5) Budgetary issue :

→CAP expenditures fixed until 2013

Répartition pour la période 2007-2013 des fonds alloués aux paiements directs, aux mesures de développement rural, par groupe de pays membres millions d'euros, prix de 2004 (PD), prix courants (MDR)



*UE15 : Etats membres avant le 1^{er} mai 2004.

UE10 : Etats membres adhérant au 1^{er} mai 2004.

UE12 : Etats membres adhérant au 1^{er} mai 2004 et 1^{er} janvier 2007.

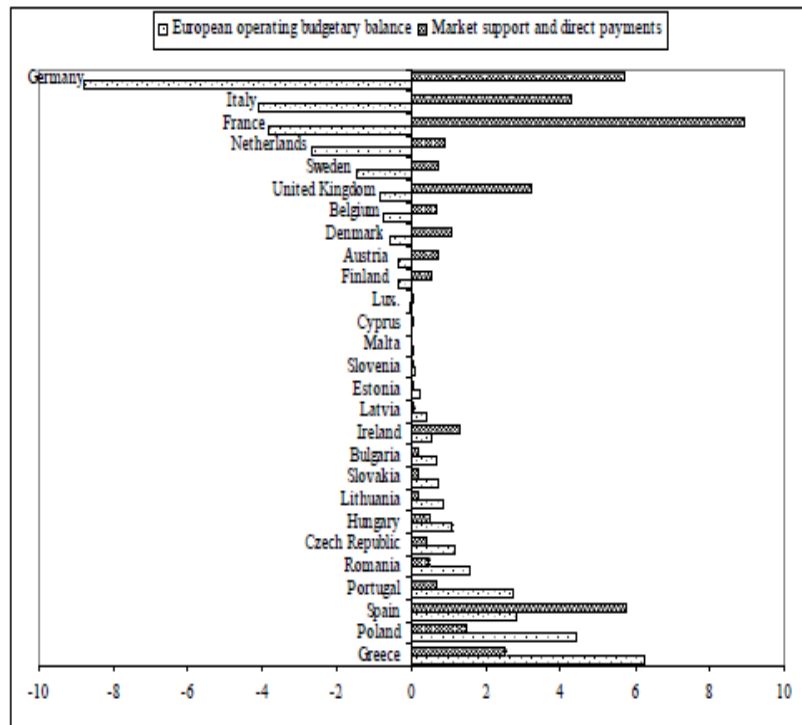
Source : Règlement CE 1782/2003 revu, Décision 2006/636/EC.

- Lack of funds for **rural development** measures
→ increase in modulation rate (compulsory vs. voluntary ; flat vs. progressive rate)
- Applying co-funding to the first pillar?

(2.5) Budgetary issue :

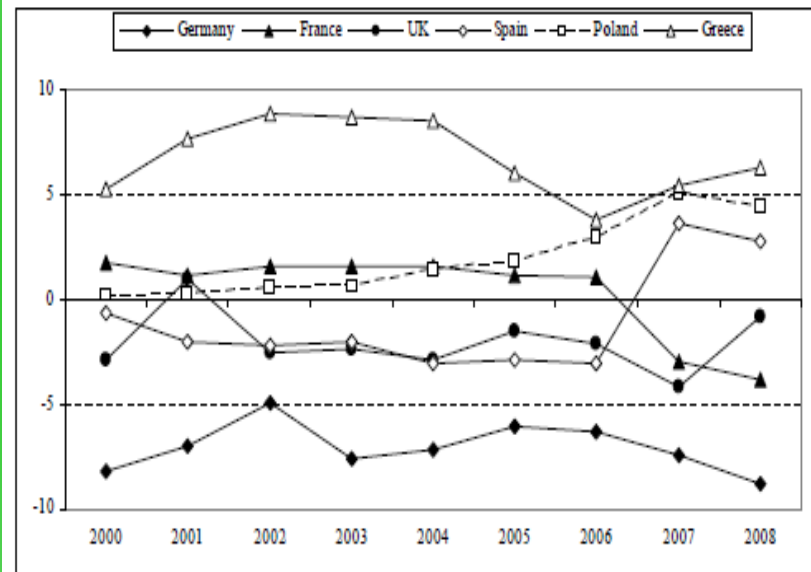
→ budgetary balance and return

Operating budgetary balance by Member States along with market support and direct payments, 2008, billion euros



Source: Commission of the European Communities, Financial Report 2008.

Evolution of operating budgetary balance for selected Member States, 2000-2008, billion euros



Source: Commission of the European Communities, Financial Report 2008.

(2.5) Budgetary issue :

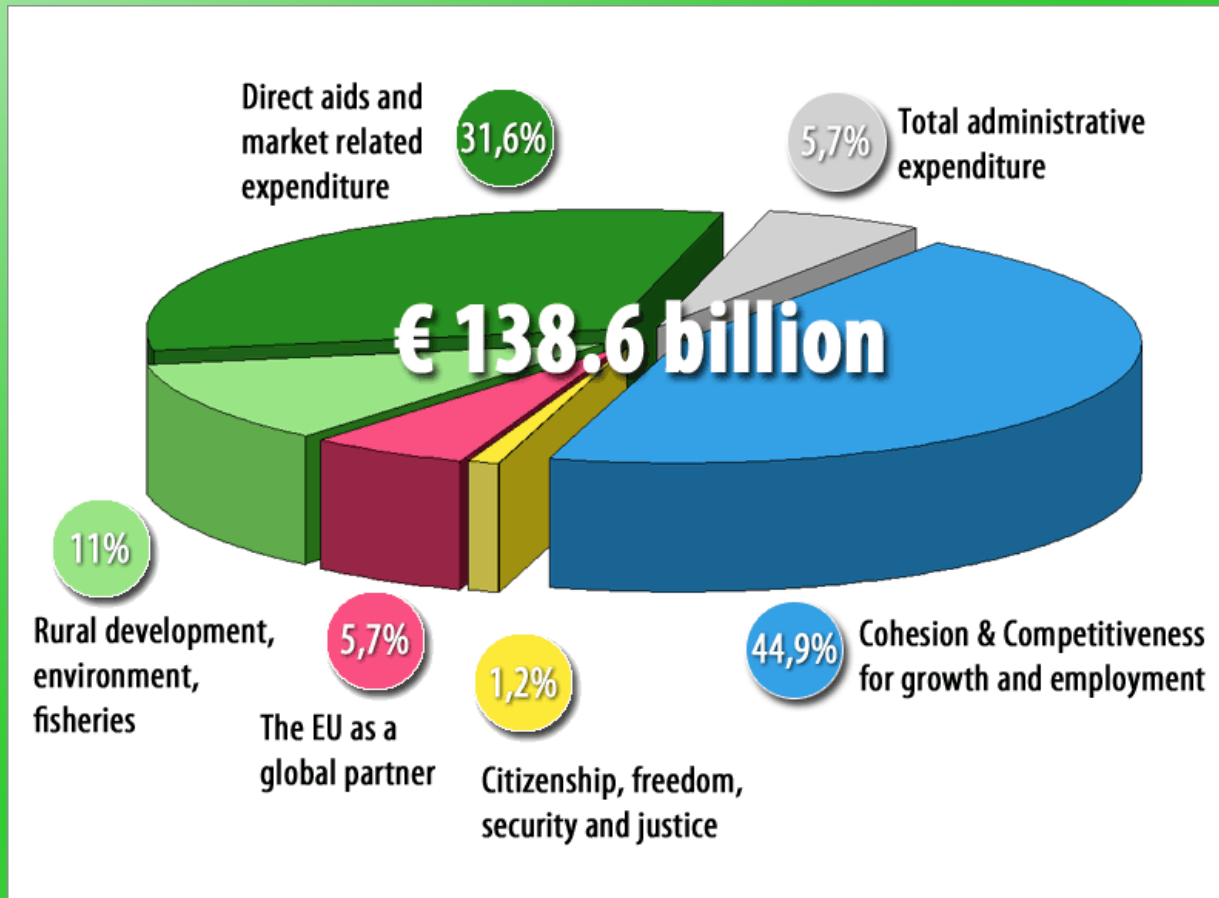
→EU budget review

The “Lisbon Strategy”, launched in 2000, aimed at making the European Union (EU) the most competitive economy in the world and achieving full employment by 2010. Which accurate funding?

Now: The 2020 Strategy

- In May 2006, the European Parliament, the Council and the Commission agreed that the Commission should undertake a fundamental **review of the EU budget**. The Commission was invited *“to undertake a full, wide ranging review covering all aspects of EU spending, including the CAP, and of resources, including the UK rebate, to report in 2008/9.”*

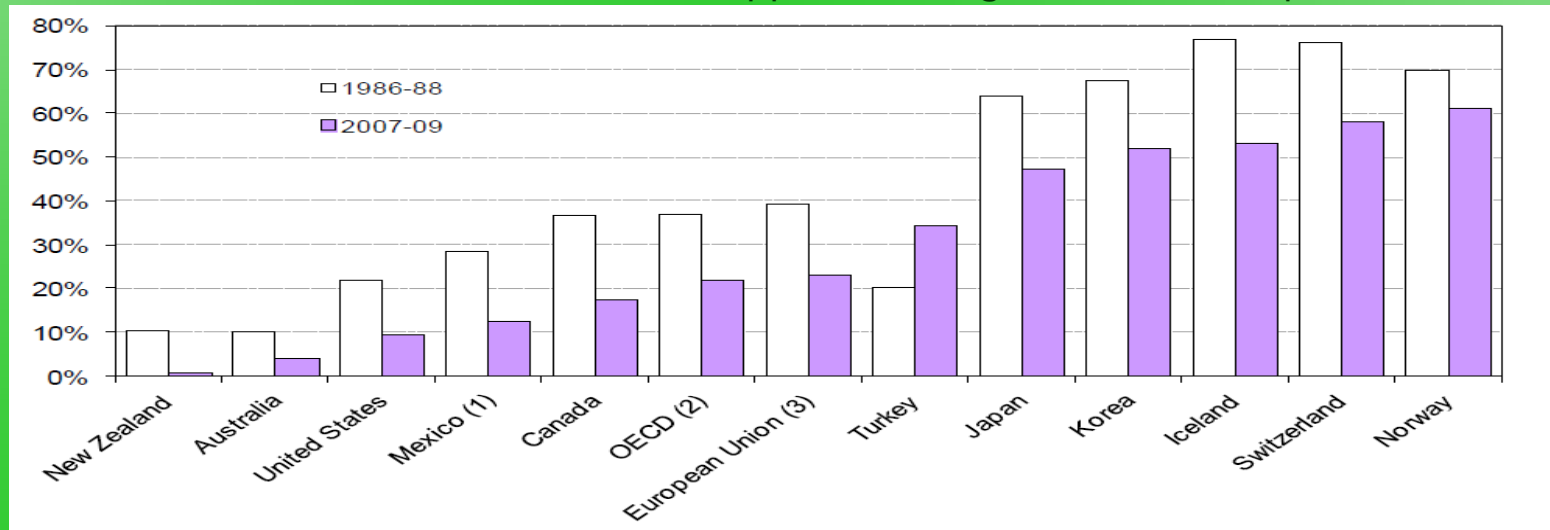
2010 EU Budget



(2.6) International issue

- **Price distortions** on world food markets induced by the CAP
- **Developing countries** considerations
- SPS and environmental regulations: hidden protectionism?
- Does CAP mechanisms respect **WTO's** Agricultural Agreement?
→ Amber, Blue, Green boxes

OECD Producer support (% of gross farm receipt)



(2.7) The 2008 CAP Health Check

- This agreement deepens previous reforms (1992, 1999, 2003)
 - **Compulsory full decoupling** of support (with the exception of suckler cow, goat and sheep premia)
 - Recoupling of payments for sectors with problems/disadvantaged regions/vulnerable types of farming/risk management schemes (article 68): **shift from past broad commodity support to targeted support**
 - **Milk quotas phasing out** by April 2015 through a “soft landing”: increase in quota by one percent per year until 2014
 - Abolition of compulsory set-aside
 - **Increase in compulsory modulation** (10% by 2012 , An additional cut of 4 percent for payments above €300,000)
 - Adoption of **new challenges: climate change, renewable energy, water management, biodiversity, innovation**, accompanying measures in the dairy sector (benefit from increase in modulation + higher EU co-funding rates)
 - SAPS extension until 2013 + additional funding for EU-12 farmers
 - Simplification of cross-compliance

3. Concluding remarks on the post-2013 CAP

- Positive **calendar** for a sound reform of the CAP after 2013
 - Budgetary framework ends in 2013
 - EC legal proposals for a reform of the CAP are foreseen by mid-2011; an agreement by 2012 (EC-EP co-decision with the Lisbon Treaty)
- Concluding the Doha Round is crucial **in 2011**
 - Securing and promoting **market access**: tariff binding; tariff cut (tiered formula: caution with sensitive products because 30 products represent 69% of a potential import increase in the EU (Gouel et al., 2010))
 - Banning **export refunds** (e.g. the EU is allowed to spend 2.3 billion euros per year in dairy export refunds)
 - Locking-in effect of **domestic support** decoupling

3. Concluding remarks on the post-2013 CAP

- A **new rationale for and distribution of SFPs**
 - From a broad income support to (European) public goods (environmental amenities, areas with natural constraints, small farm holdings (?), etc.)

- An increased **market orientation**
 - Improvement of food chain functioning
 - Simplification of CAP procedures
 - Addressing risk management
 - Promoting income diversification

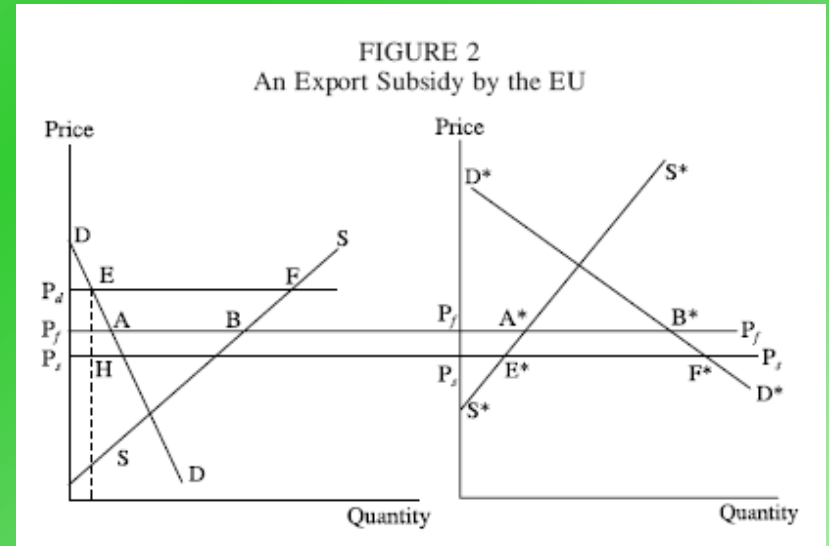
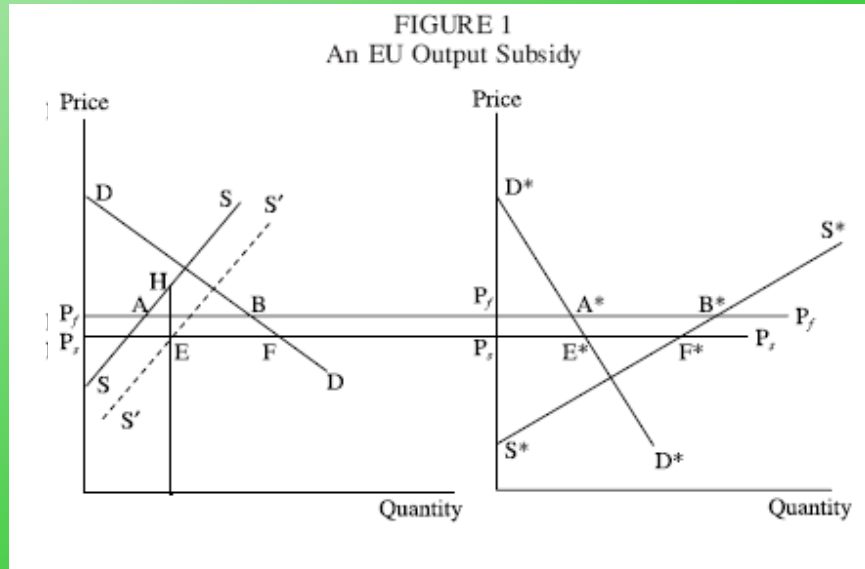
- A focus of rural development measures to new challenges: **climate change, water, biodiversity and innovation**
 - Improving coherence with other EU policies

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Appendix 1: Microeconomic effects of output and export subsidies



Source: Panagariya, 2005

Appendix 2: 2007 counterfactual experiment: CGE model (GTAP)

(Costa et al., 2009)

- **Ex-post cost benefit of removing unilaterally the most distortive instruments of the CAP**
- If one wants to know what liberalizing the CAP might mean, **estimated costs become benefits.**

□ Methodology

□ Data

□ Main Results

- European allocative efficiency benefit: 38 billion euros
1/10th Austrian GDP or 1/11th Swedish GDP
 - European economic welfare benefit: 21 billion euros
more than the Estonian GDP
 - World economic welfare benefit: 17 billion euros
-

Modeling strategy

- 2007 counterfactual experiments: analytical separation of most distorting CAP elements
- Four modeling scenarios are undertaken with the unilateral elimination of:
 - Direct payments
 - Export refunds
 - Border protection
 - Total
- Main limits
 - Decoupling issues
 - Cross compliance effects
 - Other CAP spending (rural development measures)
 - Specific-commodity measures: set-aside, production quotas

Database

- GTAP database v.7: 2004 base year, 113 regional economies, 57 industries
- Data aggregation
 - 40 regional groups: EU 15 Member States (MS) represented individually, new MS (NMS) aggregated into a single region
 - 24 industries
 - For ease of presentation, results are further aggregated into 9 regions and 6 industries
- Direct payments (2007)
 - 2007 average rates of domestic support equalized across all sectors
 - Measured as the share of payments in gross agricultural output
- Export refunds and border protection (2004, GTAP v.7)

Results

□ Resource allocation

Within a country, protecting a sector is to the detriment of the non-protected rest of the economy:

- Manufacturing, services but also forestry, fishing, and non-supported agriculture.
- Why? Protected sectors enjoy unfair advantages when competing for capital, land and labor.

Countries being a bunch of sectors, “favoring” some sectors is “favoring” some MS to the detriment of others: EU15 vs. NMS12; France vs. rest of the EU

□ Efficiency costs

- CAP lowers world farm and food prices

□ What follows assumes no change in foreign farm policies

- Further gains would emerge from increased market access if EU liberalisation prompts other economies to do so

Effects of removing CAP's distortive instruments on sectoral output (1)

2007 baseline, % changes

		<i>Crops</i> (+2.08)	<i>Livestock</i> (+3.91)	<i>Food process</i> (+0.83)
a. Direct payments				
	Opposite effects			
NMS12		0.49	1.98	0.29
EU15		-1.92	-2.52	-0.76
Latin America		0.73	0.44	0.15
b. Border protection				
	Similar but unequal effects			
NMS12		-2.48	-2.41	-5.56
EU15		-6.23	-4.93	-4.92
Latin America		2.25	11.88	4.14
c. Total CAP				
NMS12		-1.97	-0.64	-5.61
EU15		-8.09	-7.64	-6.02
Latin America		2.78	12.70	4.51

Effects of removing CAP's distortive instruments on sectoral output (2)

2007 baseline, % changes

	Manufacturing (-0.10)	Services (-0.18)
a. Direct payments		
NMS12	-0.26	-0.01
EU15	0.29	0.05
Latin America	-0.19	-0.01
b. Border protection		
NMS12	1.29	0.20
EU15	1.02	0.10
Latin America	-2.39	-0.06
c. Total CAP		
NMS12	1.12	0.19
EU15	1.35	0.15
Latin America	-2.64	-0.06

Effects of removing CAP's distortive instruments on world economic activity and welfare

2007 baseline, % changes, million euros in 2007 price changes

	'Efficiency' GDP		'Welfare' GDA	
	Per cent	€ million	Per cent	€ million
NMS12	0.44	3,739	0.32	2,882
EU15	0.30	34,395	0.16	18,666
Latin America	-0.06	-1,429	0.26	6,380
Australia-NZ	..	-28	0.19	1,352
East Asia	-0.01	-651	-0.03	-1,803
Rest of Asia	-0.03	-664	0.10	1,865
North America	-0.01	-945	0.03	3,574
Rest of Europe	-0.09	-2,042	0.06	1,327
Africa	-0.01	-115	0.05	410
World	0.08	33,037	0.08	33,037