



Accession to European Union in the Field of Agricultural and Rural Policies

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B. Policy developments and reforms

CAP milestones and issues



Motivation

Common Agricultural Policy (CAP):

- one of few complex policies which are dealt with only at EU the level
- after the EU accession is the end of national sovereignty in the agricultural policy
- combination of hard internal competition, partial border protection, and high budgetary resources
- 40 years of specific development
- 50 % (and more of the actual EU budget, 40 % in the future)
- 75 % of yearly legal texts

What are the main characteristics of the development of the CAP?

What are the economic and other impacts of this EU policy?

What is the future of the CAP, especially after the next EU enlargement?

Content



a. **Historical roots and objectives of CAP**

b. **CAP milestones**

- **Price Support (1962-1983)**
- **Supply Management (1984-1992)**
- **Direct Payments (1993-2004/6)**
- **Single payment scheme (2005/7-2013)**

c. **Future of CAP**

- **Impact internal and external factors**
- **Potential policy reforms**



a. Historical roots and objectives of CAP



Historical roots

Support for Agriculture - tradition before EC/EU:

- Germany: higher tariffs since 19th century
 - response to the increase of international trade (cheap imports of cereals from USA)
 - increasing demand from growing urban population
- France followed and as agrar exporter developed extensive protectionist approach
 - export subsidies, market interventions, central administration
- GB has preserved the liberal attitudes, NL and DK restructured the agriculture (modern livestock technology, technological development)
- Importance of food security in crisis (1st and 2nd World War, “The Great Depression”, “Cold War”)



Historical roots

■ At the beginning EC/EU (1958-1962):

- customs unions not without agri. support
- support - how strong?
- decisions: German prices and France regulations system

■ Conference in Stresa (1958)

- Family farm as a model of European agriculture
- Two pillars of measures:
 - Market-price policy (primary instruments)
 - Agricultural structural policy

■ 10 years of CAP establishment

- The level of prices (the highest – German – selected)
- Common market organization for all important product groups
- Long-term impacts of decisions



Objectives

Treaty of Rome (1958)

- increase of productivity
- fair income for rural citizens/farmers
- market stabilization
- food security (self-sufficiency)
- suitable prices

the objectives remain the same until now!

conflicts between the objectives



European model of agriculture

■ With the CAP reforms in 90's new reasoning of policy was developed (mainly by Commission). Different terms, the same meaning:

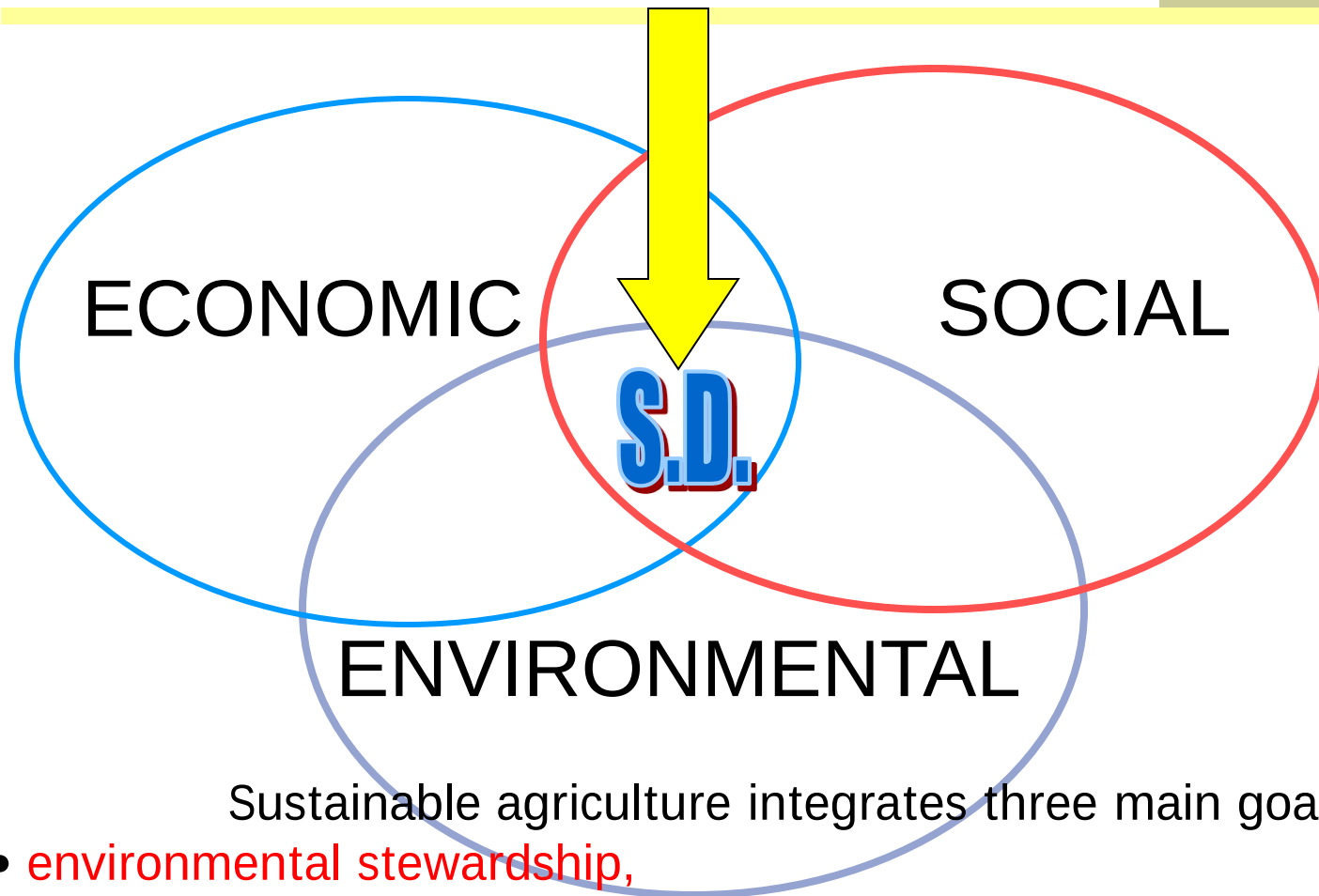
- European model of agriculture
- Sustainable agriculture
- Eco-social concept of agricultural policy
- Multi-functionality of agriculture.
- Public goods concept? (actual discussion)

■ The agriculture provides besides the economic outputs also external benefits related to environment, landscape, rural development, social structures.

- In economics, an **externality** is a side effect from one activity which has consequences for another activity but is not reflected in market prices. Externalities can be either positive, when an external benefit is generated, or negative, when an external cost is generated from a market transaction.



Sustainable development in agriculture?



Sustainable agriculture integrates three main goals:

- environmental stewardship,
- farm profitability,
- and prosperous farming communities (rural areas).



b. CAP milestones



The evolution of the CAP over 40 years

Productivity

Competitiveness

Sustainability

**The Early
Years (1960s)**

**The Crisis
Years (1980s)**

**The 1992
Reform**

**Agenda
2000**

**CAP Reform
2003**

Food security
**Improving
productivity**
**Market-
stabilisation**
**Income
support**

**Over
production**
**Exploding
expenditure**
**International
friction**
**Structural
measures**

**Reduced
surpluses**
Environment
**Income
stabilisation**
**Budget
stabilisation**

**Deepening of
the reform
process**
**Competitive-
ness**
**Rural
development**

**Market
orientation**
**Consumer
concerns**
farm income
**rural
development
environment**



CAP milestones

- I. **Price support (1962-1983)**
- II. **Supply management (1984-1992)**
- III. **Direct payment (1993-2004/6)**
- IV. **De-coupling of direct aids
(Single payment scheme) (2005/7-2013)**



Price support (1962-1983)

Problem

- Food security, poor farm efficiency, low farm income

Aims

- Increase of production, income support, market stabilization (original Rome objectives)

Instruments

- Price support (higher prices) done by import tariffs, market interventions, export subsidies

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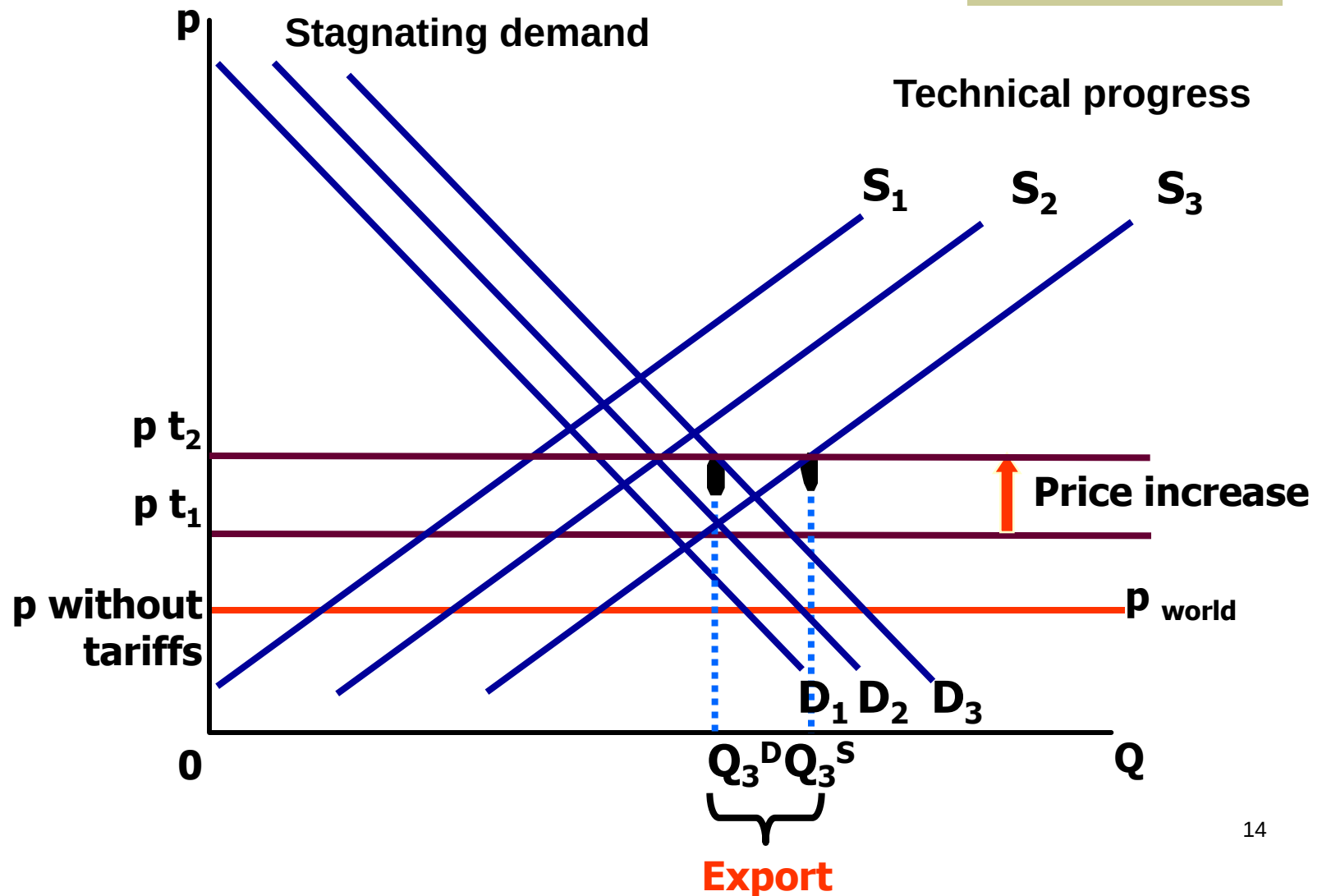
- production increase
- market stabilization, structural changes,
- net food exporter

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- costs for consumers (additional tax)
- unfair distribution of support:
 - 80% goes to 20% biggest farms
- international trade disputes (lower prices)
- surpluses & budget “explosion”!

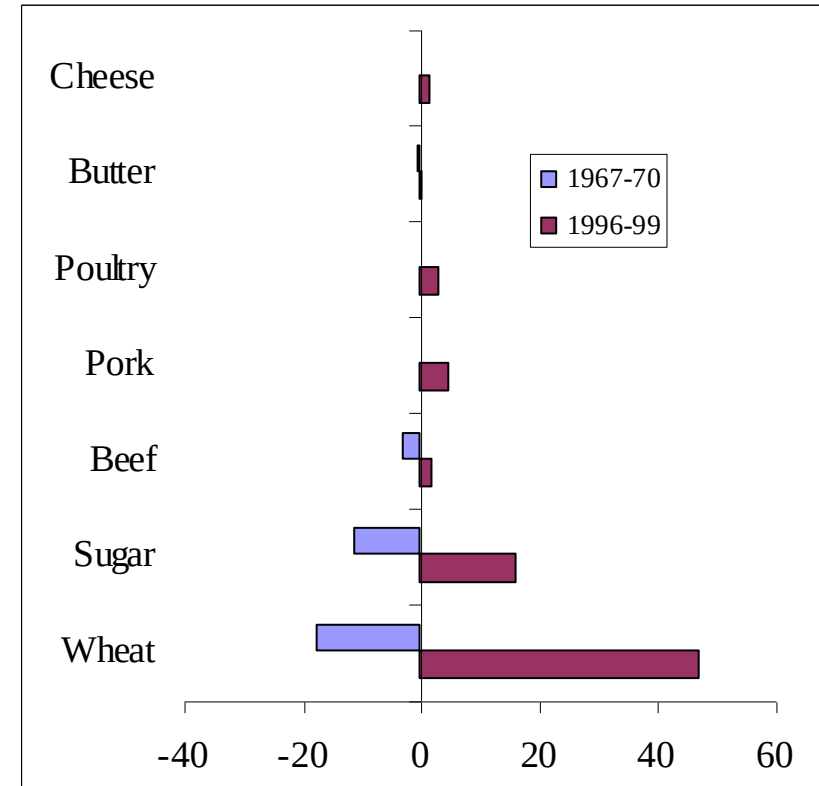
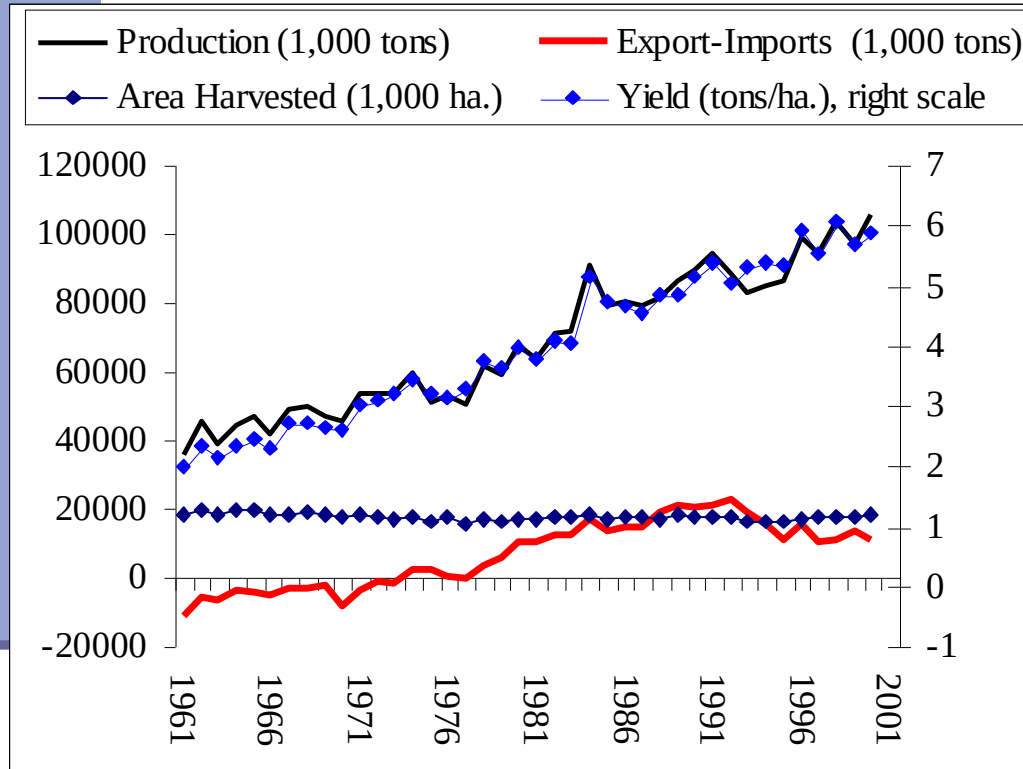


Price support is increasing production





Follow-on problems of oversupply



■ **EU switches from net food import to exporter in most products**

Follow-on problems: World market impact



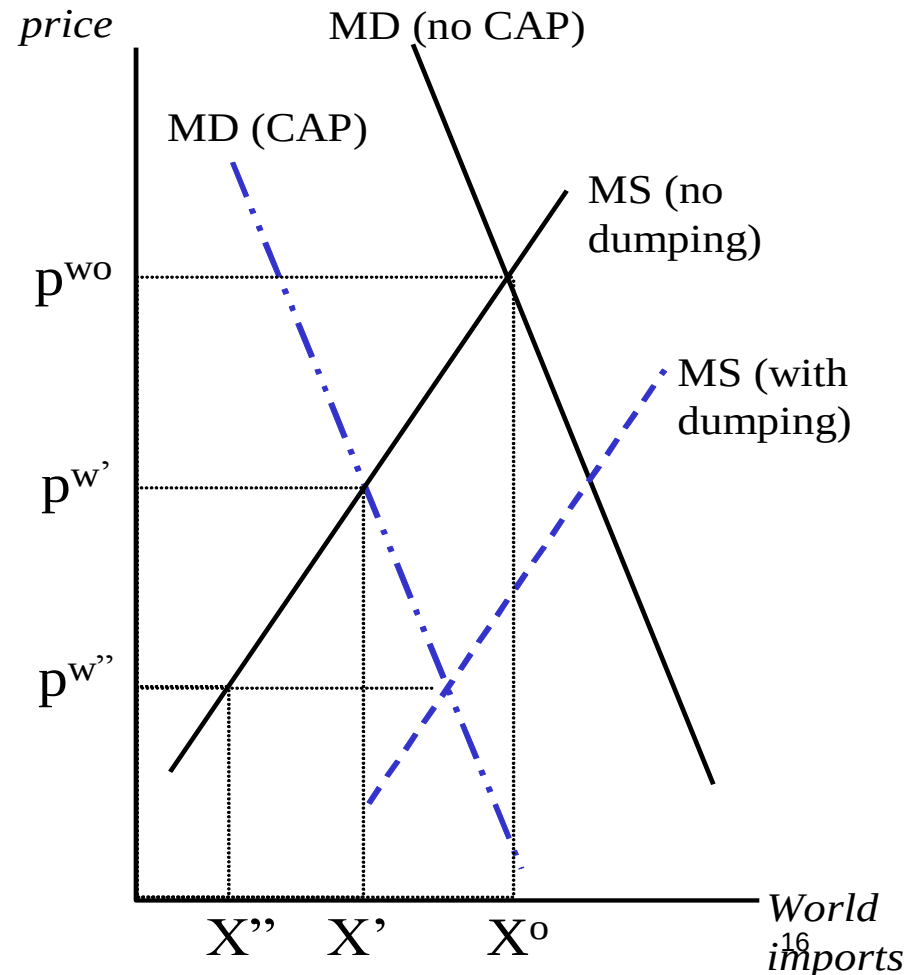
Import protection insufficient for price support

CAP becomes major food buyer

- Some of this is dumped on world market

CAP protection and dumping depresses prices on world markets

- Harms non-EU food exports





Price subsidies (1962-1983)

(cont.)

CAP impacts on world price level (1978-82)

	Cereals	Sugar	Milk	Beef and Sheep
- research number	9	5	4	/
% increase of world prices, if CAP is abolished	6,4 0,7 - 13,2	7,5 2,6 - 12,0	18,9 10,5 - 28,3	
- research number	5	2	2	4
% price volatility to existing CAP	34,1 19,8 - 50,0	13,6 5,0 - 22,2	55,0 50,0 - 60,0	22,5 11,0 - 37,4

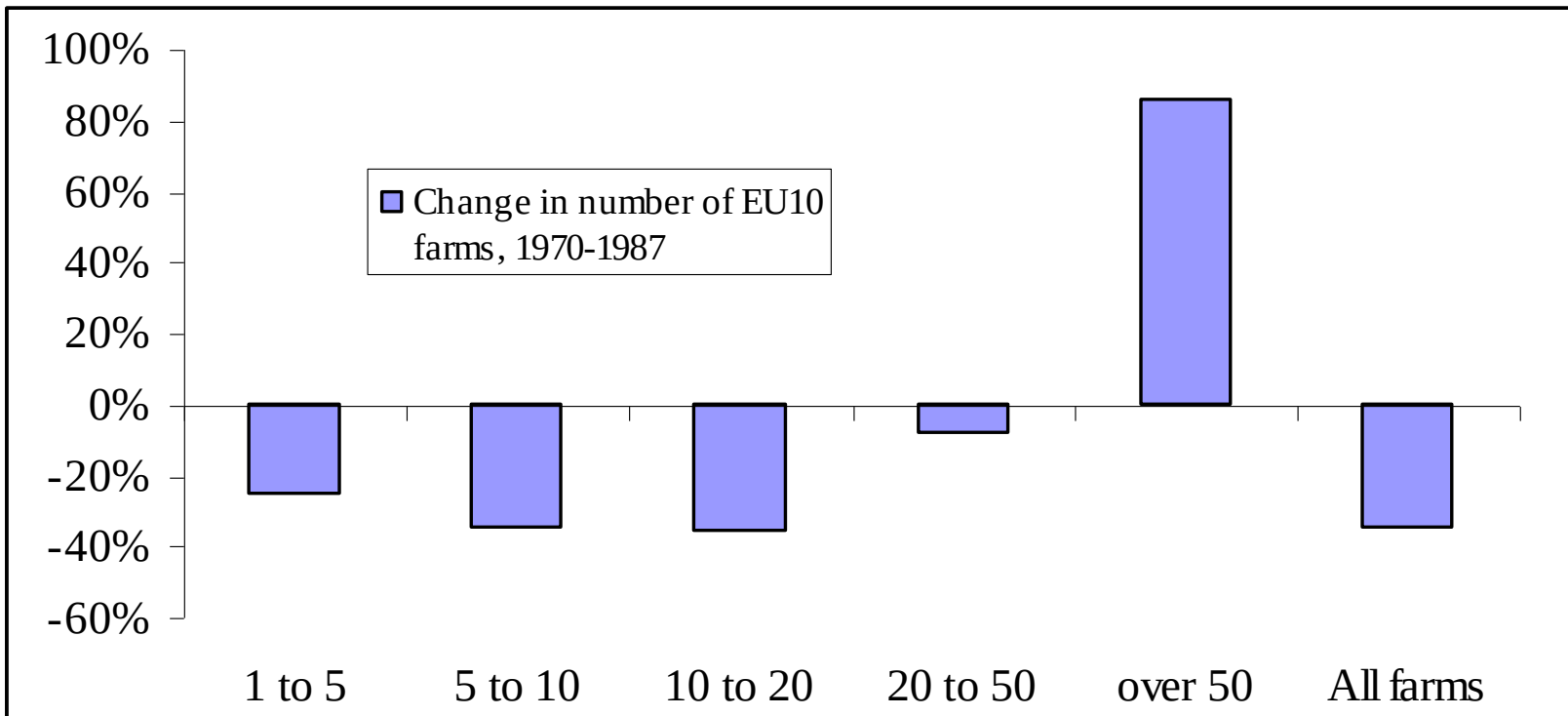
Atkin (1993), Rosenblatt et al (1988)



Other CAP problems

The farm income problem

- Average farm incomes fail to keep up despite huge protection and budget costs
- Most of money goes to big farms that don't need it
 - CAP makes some farmers/landowners rich
 - Keeps average (i.e. small) farmer on edge of bankruptcy
- Farmers continue to exit farming (2% per year)



Farm incomes & CAP support inequity



- **Also reformed CAP support still goes mostly to big, rich farmers**

- payments intended to compensate, so inequity continued

- **Half the payments to 5% of farms (the largest)**

- **Half the farms (smallest) get only 4% of payments**

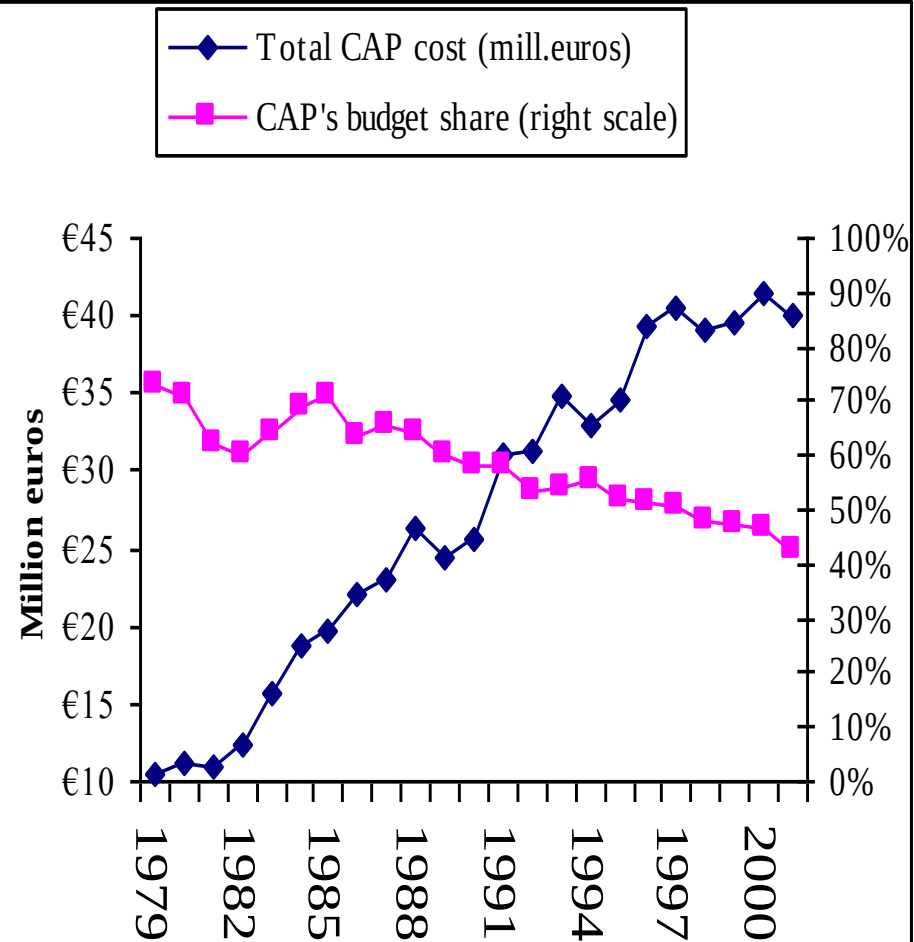
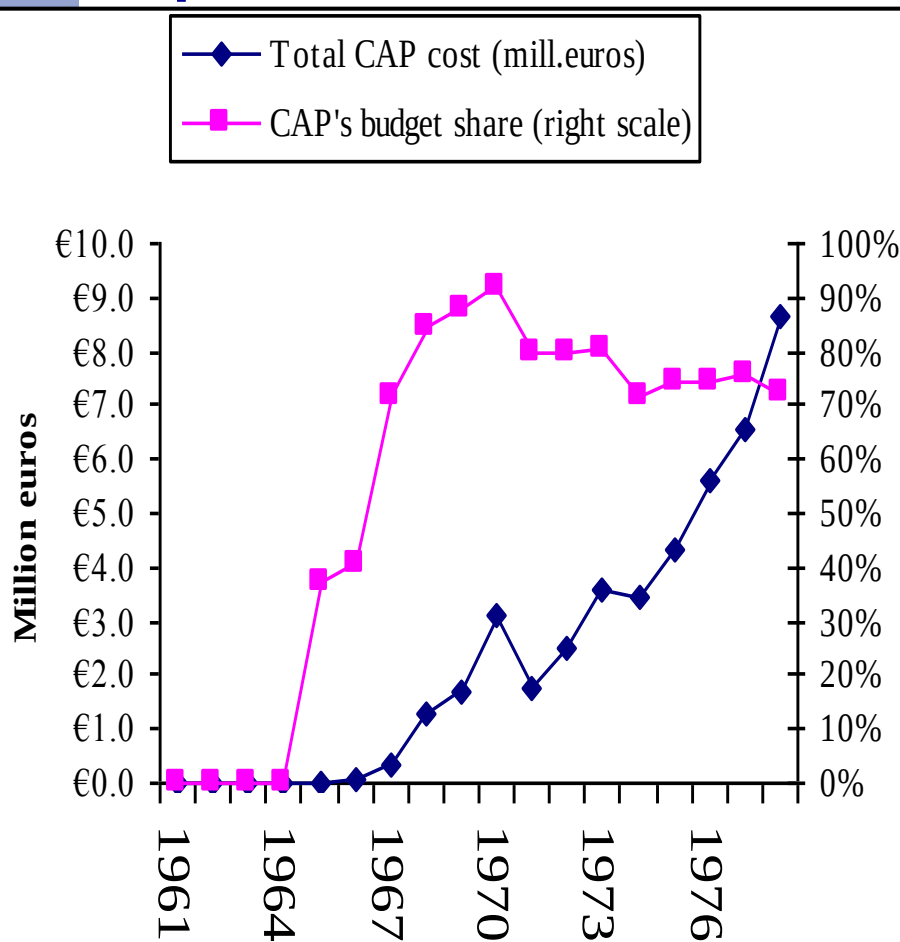
- **Recent studies show that only about half of these payments go to farmers**

- Rest to non-farming landowners and suppliers of agricultural inputs (seed, fertilisers, agri-chemicals, etc.)



Follow-on problems: Budget

Buy and storing or dumping food becomes increasingly expensive.





Price subsidies (1962-1983)

(Budget)

	1978	1982	% changes
<i>EU-Milk production- q_s</i>	100	110	10
<i>Domestic use - q_d</i>	90	90	0
<i>Self-sufficiency- $q_s/q_d * 100$</i>	111	122	10
<i>Producer prices - milk</i>	9	9,90	10
<i>World price - milk</i>	3	3	0
<i>Producer revenues</i>	900	1089	21
<i>Consumer costs</i>	810	891	10
<i>Worldmarket revenues</i>	30	60	100
<i>CAP costs (export subsidies)</i>	60	138	130

Surpluses lead to serious budgetary problems!



Price subsidies (1962–1983)

Are the objectives of Treaty of Rome reached?

- increase of agricultural productivity (Yes)
- fair income for rural citizens/farmers (No/yes)
- market stabilization (Yes!)
- food security (self-sufficiency) (Yes!)
- reasonable prices (No!)

Why price support is inadequate farm income policy?

- Price support is ...
 - unnecessary:
farm household incomes not generally low
- inefficient:
 - \$ 1 of extra price support transfers only \$0.25 to farm income
- inequitable:
 - largest farms receive most support



Supply management (1984–1992)

Problem

- Surplus and budgetary costs

Aims

- To stop the increase of production (milk, cereals, beef) and control the budget

Instruments

- Quotas, set-aside, price support

Policy effects

- Milk problem solved. Other problems remain! (budgetary costs!)



Direct payments (1993–2003)

Problem

- Budgetary problem. Pressures from international partners to change the CAP.

Aims

- To conclude GATT/WTO negotiations. To stabilize budget costs. More transparent policy. Farm income.

Instruments

- Reduction of price support. Direct payments per ha or per head. Set-aside. Environmental and LFA payments.

Policy effects

- Budget stabilization. Income stabilization. Other problems remain.



Single payment scheme (2005/7-2013)

Problem

- Complaints by MS net payers, consumers (food scandals), international partners (new WTO round, enlargement).

Aims

- New concept of policy. Multi-functionality. Food safety.

Instruments

- **Production decoupled payments:**
 - Single payment scheme on historical basis OR
 - Regional single area payment scheme (payment per ha) – **obligatory for New Member States!**
 - Possibility to retain part of payments production-coupled
- **General requirements:**
 - **Modulation:** “taxation” of all receipts above 5000 €, thus saved funds allocated to rural development; with additional taxes above 300.000 EUR
 - **Cross-compliance requirements:** CAP support is now dependent on meeting quality, environmental and food safety guarantees
- **Reforms of CMO:** new support schemes, partial liberalization

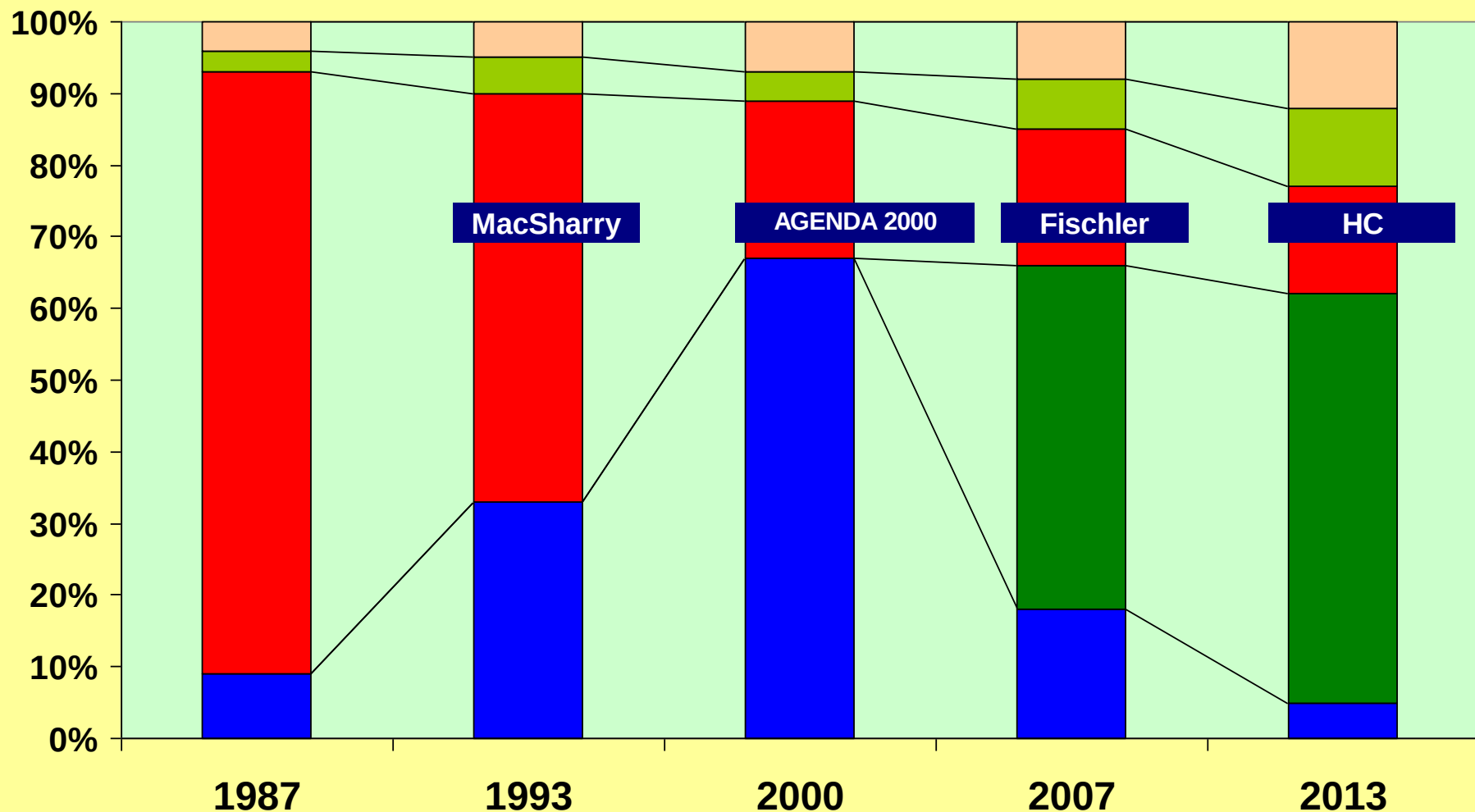
Policy effects

- CAP remains! Changes in means not in the importance and costs. Less production and exports. Speculations.

Standing CAP reforms since 1984



Shares in CAP budget for main items



■ Per ha and head pay.

■ Historical payments

■ Market interventions

■ Axes 2 Rur.Devel.

■ Other RD support



Features of CAP

CAP reform is a consistent process...

- direction of reform from more to less trade distorting policies
- with progress towards more equity in support distribution
- closer links to the production of public goods
- and same principles extended to more and more sectors

CAP reform is an irreversible process...

- budgetary disciplines more constraining than WTO...
- ...leading to higher transfer efficiency in policy instruments

but CAP impact on world markets lower than claimed...

- impact on world prices best proof of policy significance...
- ...yet in the majority of sectors, CAP has minimal impact on world prices...
- ...including products of interest to developing countries!



c. Future of the CAP

Institutional frame for reforms



- CAP until 2013 is determined by Health-Check revision (from Nov. 2008):
 - Conservative approach.
 - No changes in allocation of budget between MS, but reallocation from 1. to 2. Pillar through modulation.
- CAP after 2013 will be determined very close with the EU budget for post 2014:
 - Commission proposal (strategy) by October 2010...; legal in July 2011
 - ...Agreement in 2012 (in the frame of new financial perspective?)!



CAP decision factors

Future reforms depend on internal and external factors!

Policy reform freezers:

- pressures to keep the farm income
 - Farmers being less important social and political group...
 - however they remain organized and influential
- pressures to make common decisions
 - The conservative countries could block (limit) the reforms
 - European Commission more reform oriented

Policy reform pushers

- budgetary limitations, impact of economic crisis
- external pressures (USA, trade)
- pressures by consumers (voters) and environmental pressures group: climate change

Reform actors and factors



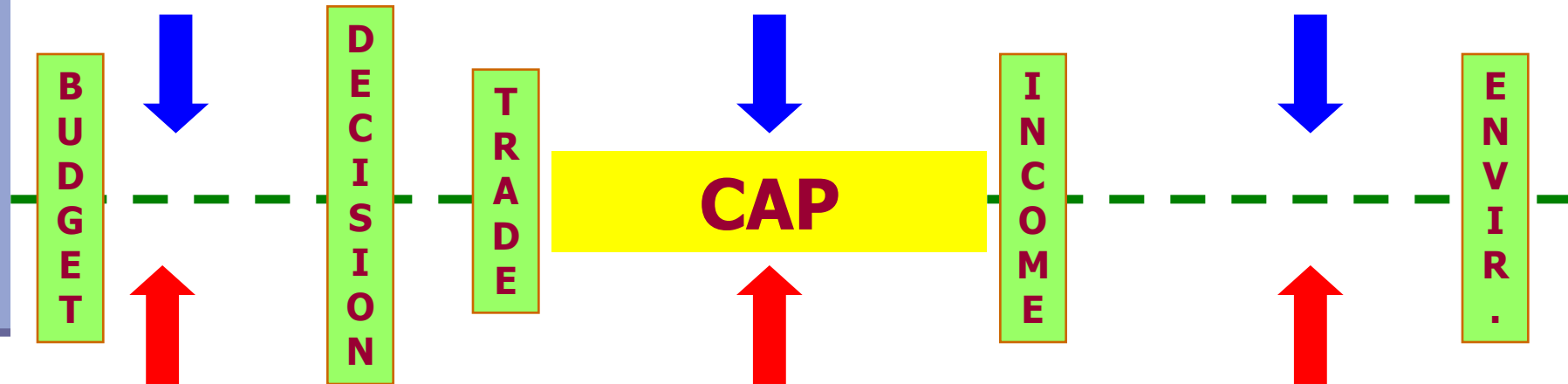
(multi-national level)

Reform pushers

**MS - Net payers
(budgetary costs)**

**WTO members
(trade liberalisation)**

**NGOs
(environment, LDCs...)**



Policy freezers



National interest in agriculture

Depends on:

- General net budgetary position in relation to EU:
 - net payers: D, Ni, UK, It, Swe, B
 - neutral position: A, Lux, F, Fin, DK
 - Net recipients: Ir, Por, Sp, Gr, new MS
- Power of national farm organisations and the influence of rural votes on national elections
 - very strong: F, D, B, Lux, Irl, Sp, NMS
- Power of agrarian bureaucracy:
 - very strong: F, strong: all others
- General economic importance of agriculture:
 - very strong: F, Ni, Dk, Irl, Pol, Hun



CAP national positions

■ 8 *reform oriented* MS (anti-CAP – “Stockholm club”)

- UK (prices, budget), Den, Nie (budget, efficient producers)
- Swe, Est, Lat, Cze, Slk (budget, liberal orientation)

■ 7 *conservative* MS (pro-CAP)

- Fra, Irl (budget, policy power, farm interests, market), Ben, Lux (farm interests, benefits from EU institutions), Spa, Por, Gre (budget)

■ 12 MS *with changing positions* (changing mentality, depends on government and person)

- Closer to reform oriented (Ita, Hun, Lit)
- Closer to conservatives (Ger, Pol, Aut, Fin, Slo, Mal, Cyp, Rom, Bul)

■ Power relations - Anti-CAP: Pro-CAP; 2009: 11: 16

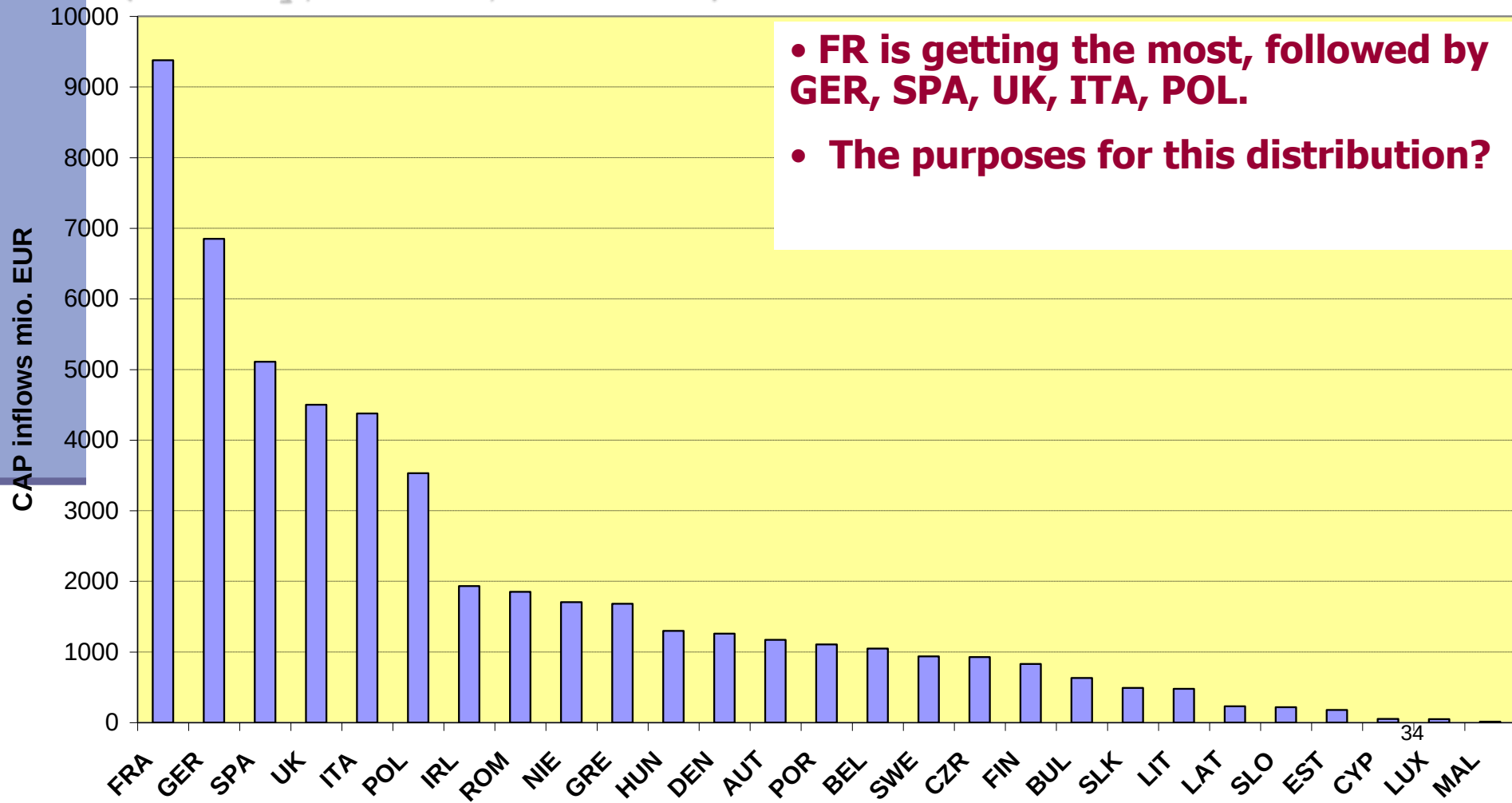
■ *Commission* is mostly conservative in general approach and budget, but more reform oriented in instruments.



CAP – Budget dispute

CAP budget inflows

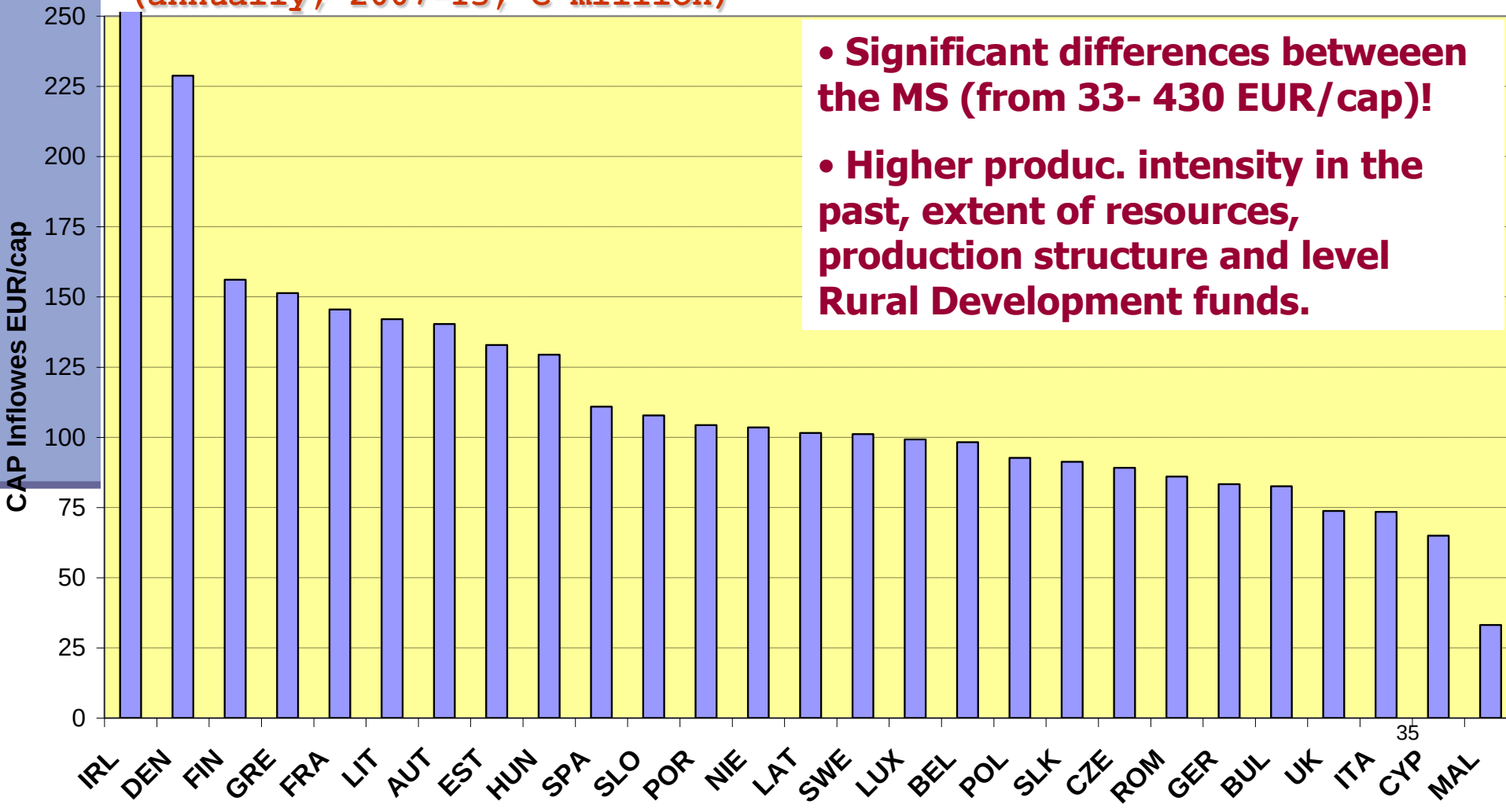
(annually, 2007-13, € million)





CAP – Budget dispute

CAP budget inflows per capita (annually, 2007-13, € million)

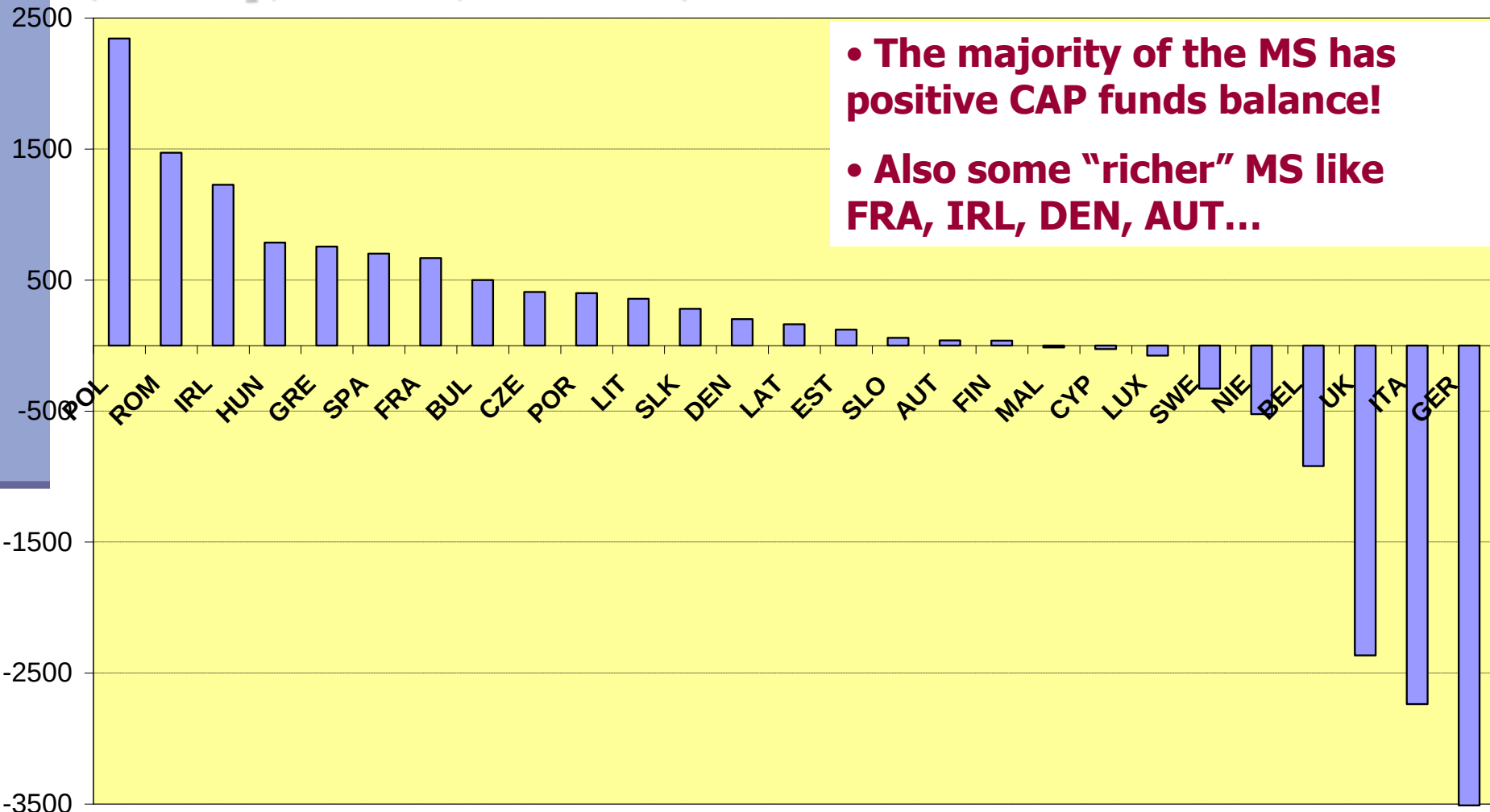




CAP – Budget dispute

CAP budget net balance

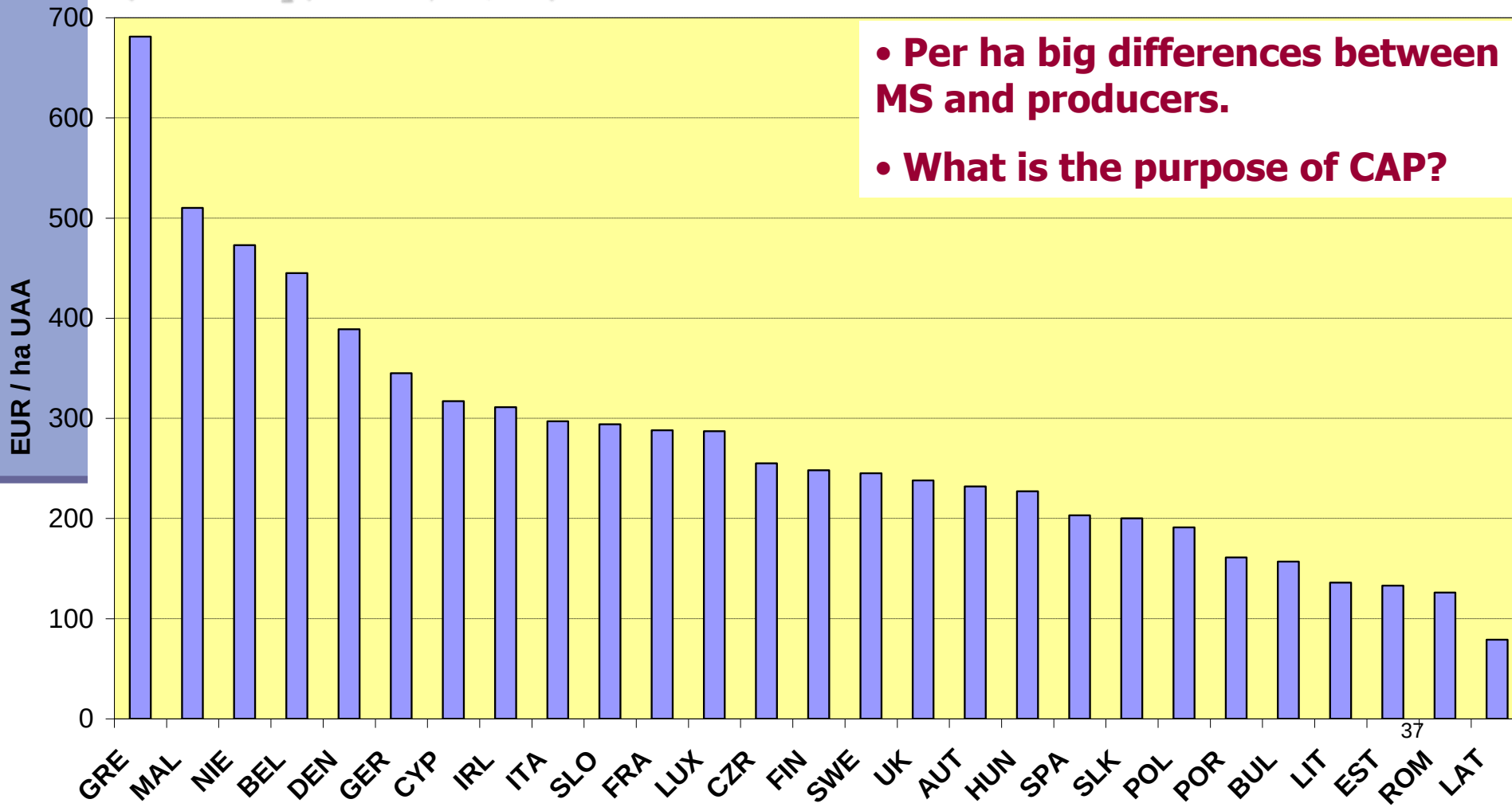
(annually, 2007-13, € million)





CAP – Budget dispute

CAP Direct payments per ha UAA (annually, 2013, €/ha)





External pressures

■ External pressures are determined by the international trade negotiators (WTO) and partners

- played important role in the past (MacSharry reform)
- will be important in the future: growing interest for developing countries (especially, the net exporters like Brazil, but also new economic giants like China, India)

■ Doha round WTO negotiations are blocked for the moment, however they give the orientation for the future reforms!

■ Three elements of trade liberalizations:

- Domestic support
- Export support
- Market access



External pressures

Domestic support

- the division of the measures from the more (red box) over partial (amber and blue box) to less market distortion (green box measures)
- Partial and blue box measures will be reduced (problem for USA).
- CAP: Fischler reform sufficient until 2013

Export support

- Gradual abolishment
- CAP: agreed by the Commission, the problem is when (2013?)

Market access

- Tariffs and levies
- Reduction agreed, the problem how deep and for which products
- CAP: the market access protection will be significantly reduced, however certain level will be preserved for sensitive products (milk, beef, sugar, etc.).



Changing consumers' concerns

Consumers and public increase their requirements for agriculture and CAP

Consumers:

- the CAP must serve the new, more consumer, environment and rural-orientated objectives more efficiently
- integration of agricultural policy and rural development objectives
- multifunctional role of agriculture – agriculture as provider of public goods
- call for better consideration of the environment, the landscape, rural communities and rural employment

Impacts?

- Increase influence, especially from environmental organisations!
- Modern policy can not be determined without this new elements! Conservative block of CAP is not really in favour of this policy re-orientation...



CAP post 2013?

Pillar 1

■ **Market liberalisation:**

- abolition of export refunds and significant decrease of import protection
- end of traditional market interventions, supply manag. measures
- safety net measures (for the time of market distortion)?

■ **Single targeted area payments**

- EU wide flate rate with differences according to purchasing power parity
- Top ups for additional services (public goods)?

Pillar 2

- New targets and frame of rural development policy (no big changes)

Budget

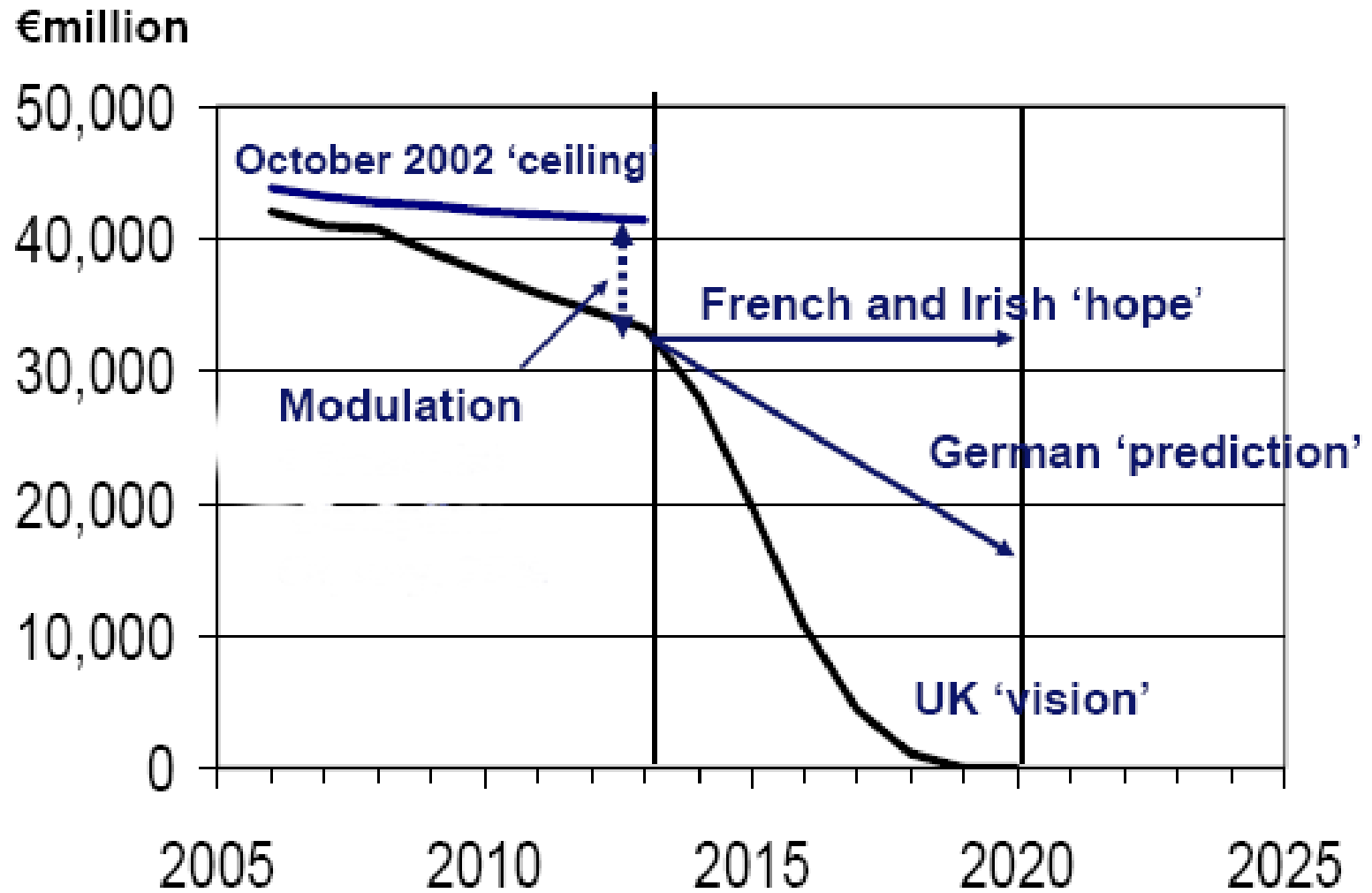
- Diminishing of budgetary resources
- **Renationalisation** of the policy (important share is payed by MS)?

The purpose of the policy? „

- Providing public goods or income policy?



Possible Trajectories for Pillar 1





Scenarios 2014–2020

Baseline scenario,,

- 1. Pillar - the level in 2002 (Chirac - Schroeder agreement) with nominal increase (1 % p.a.). Financial discipline for direct payments and market intervention. Increase of DP for ROM and BG.
- Market interventions are reduced to 50 % level of 2013.
- Rural development funds like in 2013 (modulation as proposed by Commission in 2008, agreed values are lower!

Reform scenario

- DP are gradually reduced to the level of 100 EUR/ha UAA.
- Market interventions are reduced to 50 % level of 2013.
- RD like in 2013. Increase for 50 % for measures for axis 2 (environmental and other DP)

Method

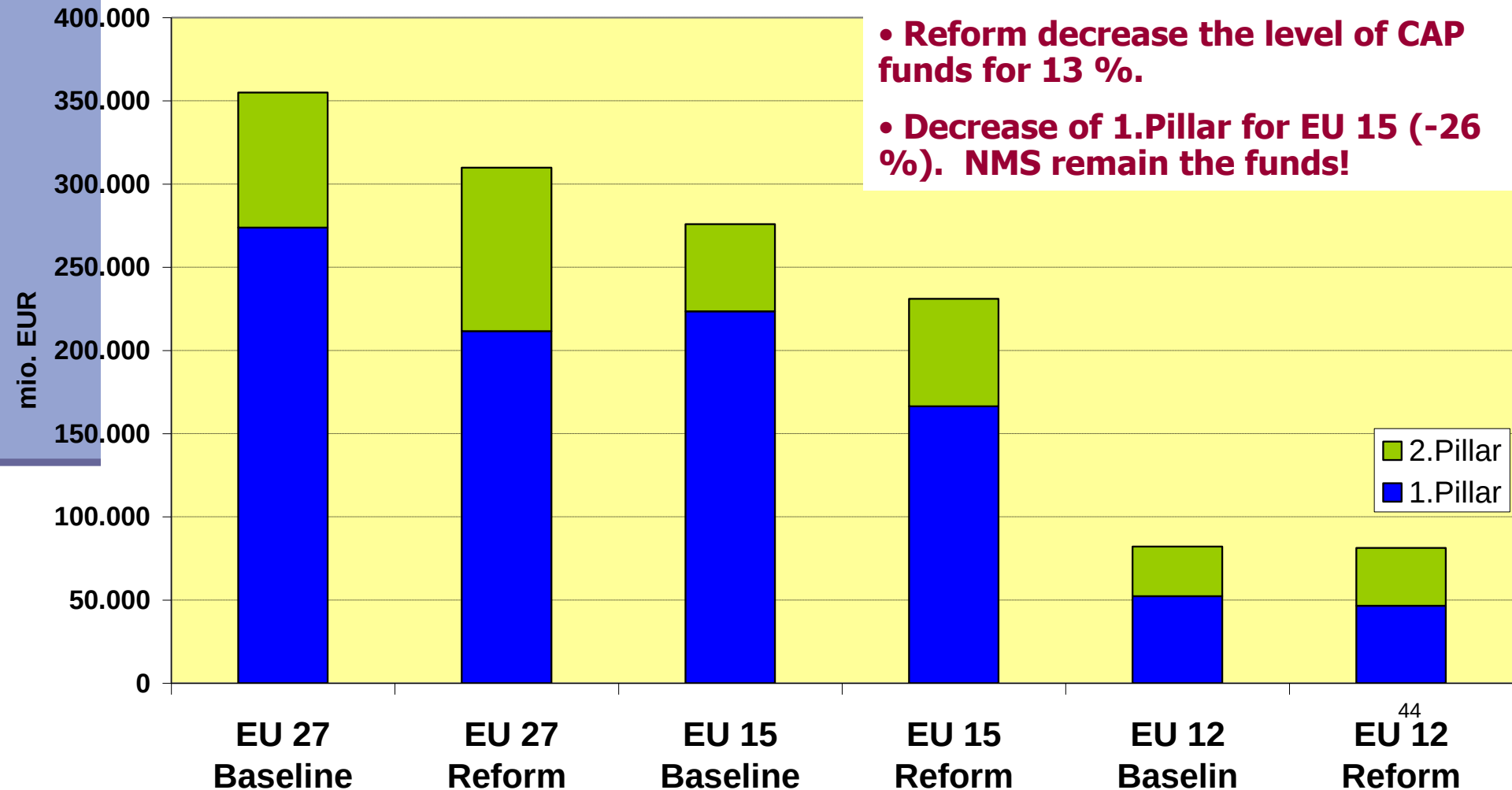
- Simulation model of EU budget (Rant et al. 2008)



Scenarios 2014-2020

Results - total

CAP budget inflows by pillars (2014-2020, € million)





The questions to be answered

1. What do you understand under price subsidies? Explain the market effects of price subsidies. What are the key problems related to this policy mechanism?
2. Why was the reform of initial CAP policy necessary and in which direction the reform process was taken?
3. How was the budgetary problem (standing increase of necessary funds) of CAP solved?
4. Explain de-coupling of direct payments? What are single payments schemes
5. What are public (consumer) concerns related to the agriculture and CAP? What is the European model of agriculture?
6. What are the key features of the existing CAP? Is the reform of this policy necessary? If this is true, what are the drivers behind?
7. Which policy measures you can expect for the period 2015 and further when Western Balkans EU Enlargement could take place?