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**Article — Digitized Version**

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Intereconomics

*Suggested Citation:* Beißner, Karl-Heinz; Hemmer, Hans-Rimbert (1981) : The impact of the EC's agricultural policy on its trade with developing countries, Intereconomics, ISSN 0020-5346, Verlag Weltarchiv, Hamburg, Vol. 16, Iss. 2, pp. 55-60, <https://doi.org/10.1007/BF02924711>

This Version is available at:

<https://hdl.handle.net/10419/139727>

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## EUROPEAN COMMUNITY

# The Impact of the EC's Agricultural Policy on Its Trade with Developing Countries

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**The European Community has frequently been blamed for impairing, through its highly protectionist agricultural policy, the development chances of Third World countries. Our article analyses whether, and to what extent, this reproach is justified.**

The Common Agricultural Policy of the European Community was conceived as the motor of European integration. Its objectives were defined in Art. 39 of the EEC Treaty of 1957:

- Increase of agricultural productivity,
- A fair standard of living for the agricultural population,
- Stabilization of the markets,
- Safeguarding of supplies,
- Reasonable prices for the consumer.

To this list must be added one further objective since agriculture has not been excepted from the general aims of the EEC Treaty which noted in Art. 110 that "by establishing a customs union between themselves the Member States intend to contribute, in conformity with the common interest, to the harmonious development of world trade, the progressive abolition of restrictions on international exchanges and the lowering of customs barriers". A comparison of the various objectives of agricultural policy shows that some of them are not easily compatible. This is especially true of the objectives with an internal economic bent on the one hand and the aim of developing and liberalizing world trade on the other. Conflicts between diverging objectives are thus practically built-in in the policy.

For the implementation of the objectives of Art. 39 the EEC Treaty provided in Art. 40 for the creation of a common organization for the agricultural markets in the place of the market orders of the individual states which had existed previously. This postulate was met

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by the creation of European agricultural market organizations which now apply to about 91 % of the agricultural production<sup>1</sup>.

The individual market organizations were drawn up with the medium-term market situation of the various products in mind. This explains the diversity of the arrangements<sup>2</sup>. Cardinal to all market organizations are however<sup>3</sup>:

- Demarcation of the EC market from the world market,
- Balancing of supply and demand inside the EC market,
- Stabilization of agricultural prices.

Internal intervention systems and flexible measures of external protection are operated for this purpose. The system may be illustrated by the arrangements for wheat as shown diagrammatically in Figure 1.

The *guide price* (in other market organizations called orientation price, producer price, basic price, target price or reference price) is fixed every year by the Council of Ministers on the basis of a proposal from the EC Commission. It tallies with the anticipated market price in the principal Community area in short

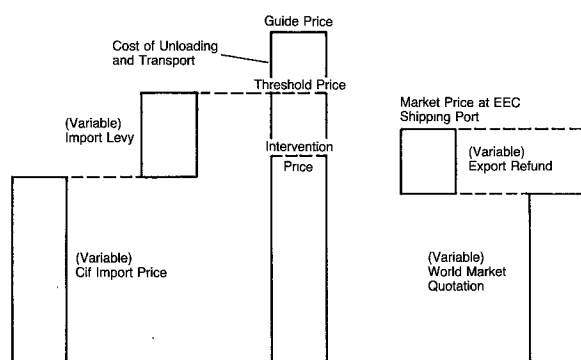
<sup>1</sup> D. Strasser: Die Finanzen Europas (Europe's finances), Bonn 1979, p. 245.

<sup>2</sup> A good summary of the various arrangements is found in P. Hrubesch: Regelungen des Außen- und Binnenhandels der Europäischen Gemeinschaft mit Agrarprodukten (Regulations concerning the external and internal trade of the European Community in agricultural products), in: Vierteljahreshefte zur Wirtschaftsforschung, Year 1975, p. 33 ff.

<sup>3</sup> H. E. Buchholz: Agrarmarkt: EWG-Marktordnungen (The agricultural market: EEC market organizations), in: Handwörterbuch der Wirtschaftswissenschaft, Vol. 1, Stuttgart 1977, p. 90.

supply. In the case of grains this is the price in Duisburg because this is the area which has to draw on other regions for the largest amount of grains. In addition, an *intervention price* is fixed in order to keep the actual market price as determined by supply and demand from falling too far below the desired guide price. If the price reaches the intervention level, the intervention authorities start buying and thereby withdraw supplies from the market. In consequence the market price cannot drop below the intervention price which is thus a guaranteed minimum price. The intervention prices are seasonally graded so as to offer an inducement to farmers to undertake the storage of the harvested grains. All major market organizations do in practice provide for withdrawal of supplies from the market through intervention. At times of heavy overproduction putting a strain on limited storage facilities it is possible to curtail the obligatory intervention purchases by very strict interpretation of the quality stipulations<sup>4</sup>.

**Figure 1**  
**Levy and Refund Arrangements for Wheat**



Source: Die Agrarpolitik der Europäischen Gemeinschaft (The Agricultural Policy of the European Community), Europäische Dokumentation 2/79, 2nd ed., 1979, p. 13.

A special problem arises in the intra-EC trade in agricultural products because the prices are tied to the common *European Unit of Account* (EUA). This caused no difficulties so long as the member states did not have to change their exchange rate parities. However, when some countries devalued in 1969, the farmers in these countries benefited from a depreciation-induced rise of the producer prices paid to them while those in countries whose currencies had been upvalued had to cope with lower prices. This hit the West German farmers especially hard; compensatory payments were therefore made to them

<sup>4</sup> Cf., i. a., K. Köhler: Europäische Agrarpolitik – Unbewältigte Vergangenheit und ungeklärte Zukunft (European agricultural policy – an unresolved past and an uncertain future), in: Europäische Wirtschaftspolitik – Programm und Realität, Bonn 1973, p. 293 f.; P. Hrubesch, op. cit., p. 35 ff.

**Table 1**  
**EC Import Prices and World Market Prices**  
**of Selected Agricultural Products**

(in EUA per 100 kilograms)

	1974/75	1975/76	1976/77	1977/78	1978/79
Butter: (1) EC Import price	236.58	264.19	292.25	304.26 <sup>b</sup>	309.17
(2) Offer price of third countries <sup>a</sup>	74.76	82.49	72.92	78.42	76.71
(1) in % of (2)	316	320	401	388	403
Soft Wheat: (1) EC import price	15.70	17.41	18.98	19.72	20.23
(2) Offer price of third countries <sup>a</sup>	14.64	14.04	9.28	9.14	10.50
(1) in % of (2)	107	124	204	216	193
Barley: (1) EC Import price	14.29	15.91	17.26	18.12	18.40
(2) Offer price of third countries <sup>a</sup>	13.40	13.61	11.75	8.78	8.19
(1) in % of (2)	107	117	147	206	225
White Sugar: (1) EC Import price	33.28	38.75	42.16	41.78	42.62
(2) Offer price of third countries <sup>a</sup>	80.52	35.63	24.00	16.38	15.44
(1) in % of (2)	41	109	176	255	276

<sup>a</sup>Normally the annual average of the lowest offer price of third countries used in the context of agricultural market management.

<sup>b</sup>Authors' own calculation; the figure given in the Commission's report is 30.91.

Source: EC Commission: Die Lage der Landwirtschaft in der Gemeinschaft (The situation of agriculture in the Community), 1979 report, Brussels, etc. 1980, p. 222 f.

for four years in succession. Moreover, "Monetary Compensatory Amounts" were introduced in order to eliminate the price differences between member states for products subject to fixed prices<sup>5</sup>.

The EC guide prices for agricultural products are as a rule much higher than the corresponding world market prices. Table 1 shows the EC import prices for several products compared with their prices in the world market.

To maintain the high level of the guide prices the internal market of the EC has to be screened from the world market. *Threshold prices* are derived from the guide prices for this purpose. These threshold prices are somewhat lower than the guide prices. In the case of grains it is assumed that the imports can be offered in the principal short-supply area – Duisburg – at the guide prices. The threshold prices are the basis for calculating the variable *import levies* to be imposed in order to close the gap between the cif import price and the threshold price. The levy system allows of flexible adjustment to changing world market conditions as the

<sup>5</sup> P. Hrubesch, *ibid.*, p. 37 f.

EC Commission is free to adjust the levy rate – depending on the particular market organization – daily (e. g. for grains or sugar), weekly, monthly or quarterly<sup>6</sup>.

The sugar market organization provides for a variable export levy as well as an import levy. Variable export levies may however also be imposed under all the other market organizations by virtue of special safeguard clauses. This had to be done in respect of a few products during 1973-75 when the EC price was below the world market level. Exports were even for a while put under an embargo in order to forestall shortages inside the EC<sup>7</sup>. Normally however this does not happen. Table 1 shows that since 1975/76 the EC import prices of the selected products have been above their world market prices, and in most cases the margin has been widening constantly.

As a result of the high guaranteed prices various products are in the EC in surplus production. In 1978 the EC was self-sufficient for instance in pigmeat (100 % of requirements), poultry (103 %), butter (119 %), skimmed milk powder (107 %) and cheese (108 %)<sup>8</sup>. EC surplus outputs which are not denaturalized or given away have to be disposed of in the world market. Given the existing price structure this means in most cases that the exports must be subsidized. The requisite *export refunds* are calculated in like manner as the variable levies.

In addition to the system of variable levies, various formalities act as an impediment on imports and exports of agricultural products. Licences are obligatory for imports and exports under the market

organizations; they serve the purpose of enhancing the market transparency and the surveillance of product movements. The licences entitle and obligate the holder to import or export a certain product quantity, as applied for, during the validity of the licence; bonds to be deposited at the time of issue are forfeited if the licence is not used. For imports proof of the country of origin is required. Embedded in all market organizations are safeguards which can be invoked if imports or exports threaten to cause serious market disruptions. The measures available to the Commission in such a situation range all the way, right up to suspension of imports and exports<sup>9</sup>.

### Obstacles to Imports into the EC

It is true that imports of agricultural products into the EC are in principle not subject to quantitative restrictions because these would in the given circumstances be incompatible with GATT. EC countries wishing to import such products have however to cope not only with the cost burden of the levies but with miscellaneous problems which may in many cases well have serious consequences, especially for developing countries:

- A good deal of practical experience and of flexibility is needed for dealings with the EC bureaucracy, and many marketing agencies in developing countries have only a limited store of these. The grain and sugar levies for instance are fixed daily by the customs authorities, so that foreign suppliers have to adapt to new prices all the time<sup>10</sup>.
- In phases of increasing surplus production the import licences are an important instrument for the

<sup>6</sup> P. Hrubesch, *ibid.*, p. 35.

<sup>7</sup> P. Hrubesch, *ibid.*, p. 36.

<sup>8</sup> Deutscher Bundestag: Materialband zum Agrarbericht 1980, Drucksache 8/3636, Bonn 1980, p. 79 f.

<sup>9</sup> H. E. Buchholz, *op. cit.*, p. 92.

<sup>10</sup> The need for an immediate response is reduced slightly by the provision in most market organizations that the risk of levy changes can be covered for some time ahead by means of advance fixing.

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Wolfgang Schaft

### INTERNATIONAL BANKS

A Documentation of their Foreign Establishments

Large octavo, 315 pages, 1980, price paperbound DM 36,—

ISBN 3-87895-193-0

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planning of restraints on trade. Besides, their extreme complexity makes the very existence of the licence regulations a grave obstacle to trade<sup>11</sup>.

□ As the calculation of the import levies is based on the cif import price of the lowest representative world market quotation, higher-priced supplies from third countries must necessarily be offered in the EC at prices above the guide price<sup>12</sup>.

□ Finally, countries exporting to the EC can never be certain that the EC Commission will not put the "safeguard clause" in force and bring imports to a halt if it deems one of the objectives of Art. 39 of the EEC Treaty to be in jeopardy. The EC Commission may even go so far as to infringe its treaty undertakings towards third countries. This happened for instance in dealings with Latin American countries which – not least because of definite take-up commitments by the EC – considerably enlarged their beef production and were later hit by an import stop on beef<sup>13</sup>.

### Special Arrangements for Developing Countries

No consideration has so far been given to the various agreements between the EC and developing countries by virtue of which EC imports from the latter receive preferential treatment. Among such agreements are those with the former colonial territories of EC member states (the first and second Yaounde agreement, the Arusha agreement, the Lomé conventions, the partial association agreements with Tunisia and Morocco, the association agreements with Mediterranean states (Greece, Turkey, Malta) and the preference agreements with Mediterranean states (Spain, Israel, Egypt, Lebanon, Algeria). Besides, a Generalized System of Preferences (GSP) in favour of imports from developing countries was put in operation by the EC on July 1, 1971<sup>14</sup>. For the developing countries as a whole the Lomé conventions and the GSP have been of the greatest importance; their provisions for the agricultural sector shall therefore be examined here.

The basis of the *Lomé conventions* are the special relations of European countries with their former colonial territories. The first Lomé convention (of 1975) originally favoured 46 states in Africa, the Caribbean and the Pacific (the ACP states). A new ACP-EEC convention (Lomé II) was signed on Oct. 31, 1979. The

ACP group includes by now 61 states; their number is still increasing as former colonial territories are admitted to the existing agreement on attaining their independence<sup>15</sup>.

In the context of the EC's agricultural imports three points are of special importance:

□ The EC grants unilateral exemption from customs duties and charges to imports of ACP origin (Art. 2 (1) of the agreement) but expressly excluded from this arrangement are the goods which are subject to a common market organization according to Art. 40 or to a special arrangement for EC imports in the framework of the implementation of the Common Agricultural Policy (Art. 2 (2)). Moreover, the Community has reserved the right to operate safeguards if the application of the agreement gives rise to serious disruptions in an economic area of the Community or one or several member states (Art. 12)<sup>16</sup>.

□ The Lomé convention provides for a fund for the stabilization of the export earnings from selected products (Stabex). The financial volume of this fund has been raised from EUA 375 mn (for 1975-80) to EUA 550 mn (for 1980-85); the annual allocation has thus been increased from EUA 75 mn to EUA 110 mn. The principles underlying the operation of the system are: Earnings to be balanced for individual products, automatic entitlement to compensation, use of these payments by the recipient state not tied to specific purposes, payments received to be paid back. The least developed countries are exempt from the "replenishment" duty. Recourse to the fund is subject to the products concerned accounting for a certain proportion of exports and the proceeds from their sale declining by at least 6.5 %; there are however exceptions also from this rule<sup>17</sup>. The Stabex system currently applies to 44 products – amongst them the following agricultural products: groundnuts, cocoa, coffee, cotton, and coconuts.

□ A particularly favourable arrangement has been reached for the sugar producers in the ACP group. Under the sugar agreement concluded as an appendix to the Lomé I Convention the EC has undertaken to purchase and import certain quantities of sugar at guaranteed prices. Maximum annual deliveries have

<sup>11</sup> P. Hrubesch, op. cit., p. 36.

<sup>12</sup> K. Köhler, op. cit., p. 310.

<sup>13</sup> P. Hrubesch, op. cit., p. 36.

<sup>14</sup> M. Feldsieper: Zollpräferenzen für Entwicklungsländer (Tariff preferences for developing countries), Tübingen 1975, p. 98 ff.

<sup>15</sup> BMZ (German Federal Ministry for Economic Cooperation) (ed.): Lomé II, Materialien zur Entwicklungspolitik, No. 66, Bonn 1980; R. Hasse, R. Weitz: The Renegotiation of the Lomé Convention, Experiences and Demands, in: INTERECONOMICS, Nr. 11/12, 1978, p. 273 ff.

<sup>16</sup> Bundesrat-Drucksache 160/80, in: BMZ (ed.): Lomé II, op. cit., p. 17.

<sup>17</sup> Bundesrat-Drucksache 160/80, ibid., p. 55 f.

been specified for the individual countries; they total 1.2 mn tonnes a year. This generous arrangement is a concession to Great Britain's traditional sugar suppliers<sup>18</sup>.

This concession for ACP export products does not however constitute a permanent easing of the protectionist agricultural market regime of the EC. Table 2 which summarizes the major EC imports of agricultural products from ACP countries shows that except for sugar the EC has retained in the Lomé conventions its external protection for the most important products that are subject to market organizations. The German Federal Minister for Economic Cooperation put the situation in the following words: "... only in regard to some products subject to market organizations was the Community unable to jump over its shadow"<sup>19</sup>.

Through the Generalized System of Preferences (GSP)<sup>20</sup> the EC accords to the developing countries a preferential treatment in trade with the intention of helping them to increase their export earnings and to quicken their economic growth. This is to be achieved by industrialization in particular; the tariff preferences therefore focus on industrial semi-finished and finished products, corresponding to items 25-99 of the Brussels Tariff Nomenclature. In addition, the EC permits selected agricultural products (items 1-24) to be imported under this scheme.

While the industrial products covered by the GSP can be imported duty-free, the preference for agricultural products consists for the most part of a tariff cut which in 1971 amounted to four percentage points. In the course of time the EC has made more far-reaching concessions so that now part of the agricultural products can also be imported free of duty<sup>21</sup>. In view of this it may be taken for granted that

the EC is, within limits, ready to facilitate imports of agricultural products from the ACP states with which it has traditionally close links. The GSP which by now encompasses almost all developing countries however provides hardly any concessions of this kind. In consequence of the EC's agricultural policy and out of consideration for the ACP countries the GSP preferences are much smaller. As far as products subject to market organizations are concerned, the conflict between the objectives with an internal economic bent and those relating to the EC's trade with third countries, referred to in the beginning, has been most certainly decided in favour of seclusion for the internal market<sup>22</sup>.

### Development Effects

By pursuing this kind of agricultural policy with a relatively high internal price level shielded from the outside world by protectionist measures the EC is preventing an improvement of the world-wide division of labour. It may be presumed that if the EC gave up its protectionist shield, the law of comparative cost advantages would in fact function in such a way as to replace a not inconsiderable part of its agricultural production by imports. Many developing countries could in this case take the place of producers inside the EC. Products covered by EC market organizations accounted in 1970 after all for about one-third of the agricultural exports from developing countries. The existence of EC market organizations constitutes quite an important handicap for the developing countries as far as their export capacity is concerned because they are thereby deprived of – in part substantial – marketing and specialization opportunities<sup>23</sup>. The result under international aspects is sub-optimal factor allocation.

The worsening of their export position has a noticeable retarding effect on the development of the developing countries. For one thing, they have less

**Table 2**  
**Major EC Imports of Agricultural Products**  
**from ACP Countries**  
(in 1977)

	Value of Imports (in EUA '000)	Share of Total Imports from ACP countries (in %)
Coffee	2,006,474	16.10
Cocoa products	1,268,733	10.16
Sugar	382,110	3.06
Groundnut products	354,938	2.84
Cotton products	231,375	1.85
Tea	205,221	1.64
Bananas	89,786	0.88
Total imports	12,460,825	

Source: Statistical Office of the EC (ed.): Analysis of Trade between the European Community and the ACP States, 1979.

<sup>18</sup> Bundesrat-Drucksache 160/80, *ibid.*, p. 50 f.

<sup>19</sup> R. Offergeld: Lomé-Abkommen hat Modellcharakter (Lomé Convention can serve as a model), in BMZ (ed.): Lomé II, *op. cit.*, p. 4.

<sup>20</sup> Cf. on what follows A. Borrmann et al.: Das Allgemeine Zollpräferenzsystem der EG (The EC Generalized System of Preferences), Veröffentlichungen des HWWA-Instituts, Hamburg 1979.

<sup>21</sup> For the majority of agricultural products the EC left however a backdoor open: by means of the escape clause it can rescind the preferences in full or part. The EC can invoke the escape clause to deal with unfavourable situations in associated countries or an economic sector of the EC itself.

<sup>22</sup> P. Hrubesch, *op. cit.*, p. 36.

<sup>23</sup> Among the few exceptions from this interaction is the position of the sugar producers in the ACP group to whom the EC is, thanks to the sugar agreement, offering an attractive market.

chance of earning from exports of their agricultural products the foreign exchange which they need to finance their development projects. This is especially true of the countries in which the potential for self-financed development is curbed primarily by limitations in the foreign exchange field. The detriment to their development chances is all the greater because they cannot expect to close the foreign exchange gap by increased foreign aid in the form of grants.

For another, the developing countries come in this kind of situation under increased pressure to assign to import substitution a higher priority in the selection of sectoral preferences than would be advisable on grounds of factor endowment. This could not only impair the potential market for goods from EC industries in developing countries, it would, besides, force the developing countries to content themselves with a sub-optimal factor allocation in the internal sphere, which would impede the development process.

Special attention should be paid in this context to the possible – in part substantial – negative distributive effects inside developing countries. If developing countries abstain from support for the (export-oriented) agricultural sector and instead promote (import-substituting) manufacturing industries, the result is often that rural areas are neglected to the benefit of the towns. As clearly shown by many empirical studies, the problem of absolute poverty in the developing countries, which has been assailed so strongly in the last few years, is primarily a rural problem. Selective measures against absolute poverty must therefore focus on the agricultural production. Not only must the production of food for domestic consumption be increased but it should be examined how far an expansion of export-oriented agricultural production could contribute to improved living conditions in rural areas. There would however be no point in this if large economic regions like the EC apply protectionist measures as a shield against the outside world.

The problems broached here are aggravated by the offer of EC surpluses at reduced prices in the world market made possible by the system of export refunds. The EC's agricultural policy thus not only hampers the exports of these products by the developing countries to the EC but exposes them to competition by EC surpluses in the world markets. To dispose of these surpluses in competition with products from other countries – including developing countries – the EC products have to be subsidized. As a consequence the export opportunities of suppliers competing with the

EC in third-country markets are being impaired. The EC export subsidies amount in fact to large sums. In 1968/69 the export refunds amounted to DM 47 for each DM 100 of foreign currency received for exports of selected EC agricultural products to third countries<sup>24</sup>. This puts the world market prices of the products concerned under pressure, and the foreign exchange position of competing suppliers is adversely affected.

The EC's agricultural surpluses are also a major determining factor in food aid allocation. The EC provides most of the foodstuffs in question as "bulk supplies", bearing in general the cost of the transport up to the border of the recipient country. The distribution of the foodstuffs is in most cases the concern of the recipient countries. Under development aspects this kind of food aid can have negative effects, especially if continued for any length of time as the EC is tempted to do by the constant surpluses. If food aid is provided indiscriminately for many years, there is a danger that, on the one hand, the government of the recipient country, having become accustomed to it, will relax its own efforts to increase agricultural production and that, on the other hand, competing agricultural products in the recipient country have to be sold at very low prices. This keeps many farmers from producing surplus food for sale. Both these effects lead to increased dependence on agricultural imports whereas in the international discussion it is widely agreed that in the long run the food situation in the developing countries can only be improved by raising the internal production of staple foodstuffs.

Aid in the form of food poses another problem in that the EC has in the past often given too little thought to the dietary customs of the recipients in the developing countries and their facilities for hygiene. The deliveries of powdered milk invite special criticism in this respect.

Taking all things together, the EC should examine

- whether, with all its internal agricultural difficulties, it has really made the fullest use of the opportunities for easing the access of third countries – including in particular the developing countries – to its agricultural market, and
- whether easing the access to this market would not be a more efficacious aid to development than many another bi- or multilateral cooperation programme or project.

<sup>24</sup> D. K e b s c h u l l : Agrarpolitik und Entwicklungspolitik der EWG im Interessenkonflikt (Agricultural policy and development policy of the EEC in the conflict of interests), quoted from K. K ö h l e r , op. cit., p. 310.