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## European Agricultural Policy: Is There Really No Alternative?

by Eckart Guth, Brussels\*

**In the intense political debate on the reform of the Common Agricultural Policy there is a high degree of consensus that the present rates of production growth must be stopped and structural surpluses dismantled. On the other hand, there is broad agreement that the structural adjustment of agriculture must not lead to unacceptable social hardships. Is an alternative to the present CAP which meets these criteria conceivable?**

The realization is growing among Community agricultural policy-makers that continuation of present policy is neither desirable nor possible. For this reason the Commission recommended in 1981 that future decisions on the Common Agricultural Policy should have the following aims:

- ☐ a price policy based on a narrowing of the gap between Community prices and prices applied by its main competitors in the interest of competitiveness, and a hierarchy of prices designed to improve the balance of production;
- ☐ an active export policy which would honour the Community's international commitments;
- ☐ a modulation of guarantees in line with Community production targets;
- ☐ an active structures policy tailored to the needs of individual agricultural regions;
- ☐ the possibility of income support subsidies to certain producers in specific circumstances;
- ☐ improved quality control at Community level and tighter financial control by the Community in the management of EAGGF expenditure;
- ☐ stricter discipline in relation to national aids to avoid undermining Community policies.

Since the Stuttgart summit in June 1983, negotiations have been in progress on far-reaching changes to Community agricultural policy. The chief political objective has been that the Community's own resources

should not be exceeded. Principles such as "financial solidarity" and the "common agricultural market", which had long been regarded as fundamental, have declined in significance in the process and are even in danger of being abandoned. The conviction is gaining ground in Community agricultural policy that the only way to get surpluses under control and thus to ensure the survival of the Common Agricultural Policy is to impose administrative constraints in the form of quotas (wine, milk and sugar) and production thresholds. Is there really no alternative?

### Essence of the Problem

From the beginning the Common Agricultural Policy was faced with the difficult task of giving an economically and socially acceptable direction to the inevitable processes of adjustment in agriculture which, in terms of the numbers of persons employed, was declining in all the member states. This will continue to be a central objective of Community agricultural policy in future. The uneven age structure of the rural population and the small farms still typical of many member states on the one hand, and the potential for increasing production if even the technology available now were fully utilized coupled with the limited sales outlets for agricultural products on the other, are economic and social factors which will doom to failure any attempt to halt structural change in agriculture.

In order to achieve the objectives set out in Article 39 of the EEC Treaty, the Common Agricultural Policy initially relied mainly on the tools of market and price policy. It was only later, and then to a much lesser extent, that this policy was extended to include structural measures. At the same time the Common

\* Commission of the European Communities. This article expresses the author's personal opinion.

**Commission Farm Price Proposals and Council  
Farm Price Decisions from 1973/74-1984/85**

	73/74	74/75	75/76	76/77	77/78	78/79	79/80	80/81	81/82	82/83	83/84	84/85
Commission	+3	+11.7	+9.0	+7.5	+3.0	+2.0	0	+2.5	+7.7	+ 9	+4.2	+0.8
Council	+5.5	+14.5	+9.4	+7.5	+3.9	+2.1	+1.3	+4.8	+9.7	+10.4	+4.2	-0.6

Agricultural Policy was supplemented in the member states by a wide variety of aid and social, fiscal and training measures.

With the instruments of agricultural price policy at their disposal, the Commission and the Council of Agricultural Ministers had the task every spring of determining the "right" level of farm prices. Commission and Council arrived at the results shown in the above table.

In each negotiating round the objective of securing adequate agricultural incomes played a central role. In this context it was accepted that the price increases which were necessary for income reasons were not a reflection of the demand and supply conditions on the major agricultural markets. The result of these decisions today is an excessive farm price level, which is mainly responsible for the structural surpluses of practically all agricultural products. It is evident that the potential offered by technological progress was underestimated or neglected. Price increases of + 9.7 % (1981/82), 10.4 % (1982/83) and 4.2 % (1983/84) indicate that the art of fixing the "right" farm prices from the point of view of Commission and Council did not consist in reducing the nominal level of farm prices but in avoiding excessively high nominal increase rates.

To take milk as an example: it was assumed in the 1984/85 round of negotiations that a price reduction of 12 % would have been necessary in order to have the same effect on production as the establishment of quotas. In the light of a total increase of 23.7 % in farm prices in the period 1981/82 – 1984/85, however, it is necessary to ask why the milk price was raised by 12 % too much during this period. If mistakes are not recognized as such, there is of course little chance of learning from them in the future. Thus the nightmare alternative of a 12 % reduction in milk prices was decisive for the introduction of milk quotas. It was also argued that a milk quota system was the only way of preserving the 1 % VAT ceiling on Community finances and that it was the only way of keeping milk producers' incomes at the politically desirable level. It has meanwhile become clear as a result of the debate surrounding the financing of the 1984 and 1985 budget deficit and the political controversy in connection with

the milk quotas in Germany in particular that these objectives have not been reached. This example demonstrates that not even a supreme political effort can serve to correct years of misguided policy at one blow. Given the relatively long time-lag between the formation of political will and the reaction of agriculture to these signals, there is definitely a need for a medium-term concept. If, despite basically unchanged market, budget and income data, changes in farm prices ranging from 10.4 % to - 0.6 % are decided within four years, it tends to indicate a stop-go approach rather than any concept of agricultural policy.

Despite the warning signs, the Common Agricultural Policy was able to continue basically unchanged over a long period for several reasons. A decisive factor was that there were sufficient funds in the budget to finance the agricultural policy. Not even the faith and hope of some member states that the exhaustion of the Community's own resources would have a salutary effect proved to be realistic. Increases in Community spending on agriculture in 1983 of around 33 % and the overstepping of financial targets in 1984 and 1985 show that lack of funds alone is not sufficient incentive to modify policies in time.

As a result of painful experience in the post-war period, achieving security of supply remained an important political argument even when the level of self-sufficiency in many products was well above 100 %. The period in which the Community gained an increasing share of world markets for almost all major EEC farm products and became a net exporter coincided with a phase of rapidly expanding demand on the world market. Therefore the resistance of the competing trading partners to subsidized EC-agricultural exports was for a certain time rather limited.

### **CAP at a Turning-point**

The dilemma affecting Community agricultural policy is that a whole series of political, economic and financial factors have changed within a relatively short period.

The most patent problem of EEC agricultural policy is the growing accumulation of structural surpluses of the main farm products (milk, wine, cereals, beef and olive oil).

The development of agricultural expenditure mirrors the surplus situation. The political controversy surrounding the exhaustion (1983) and overstepping (1984 and 1985) of own resources and – in terms of the problems – the relatively small increase in own resources to 1.4 % of the basis for calculating VAT have shown that easy financing of the agricultural policy is a thing of the past.

EEC agricultural policy has already reacted to this situation in the last few years. In addition to the – as yet unsuccessful – measures to curb the development of expenditure, a number of trends have become particularly apparent. In the course of the numerous rounds of price negotiations it proved expedient for political reasons to grant specific aid to deal with many individual problems which could not be solved with the tools of price policy (e.g. aid for oilseeds, protein feed plants, beans, soya, olive oil). A whole collection of different aids has therefore come into being. If direct consumption aids to lower the prices of farm products are included, whose ultimate aim is likewise to support producer incomes, aids currently constitute the largest expenditure item with a share of over 40 % of the agricultural budget. In addition to these Community aids a whole range of sometimes spectacular national aid measures has been introduced.

It is clear that aids have become a necessary instrument in reaching and maintaining consensus at Community level. In the vast majority of cases, however, these aids have the fundamental defect that they are production-linked and thus tend, like price support, to stimulate output.

#### Recent Reforms

There has been some movement in agricultural policy since the Stuttgart summit in 1983. The outcome is reflected in the Council Decisions of 31 March 1984. The negotiations on the accession of Spain and Portugal provide a further incentive to reform agricultural policy.

Of the many individual decisions taken, the following are particularly significant:

- ☐ On average the prices in ECU of all products subject to an organized market were reduced for the period 1984/85 (by about 0.5 %). This is supplemented by adjustments to the market regulations aimed at diminishing the financial inducement to deliver surpluses into intervention.
- ☐ A new mechanism was created for dealing with positive monetary compensatory amounts. Five percentage points of the existing positive monetary

compensatory amounts are to be dismantled on 1 January 1985. Three percentage points were converted to negative MCAs and thus greater scope provided for price increases in the member states with negative MCAs. Furthermore, because of the introduction of the "green ECU", when a currency is revalued in future there will no longer be creation of positive MCAs in the revaluing country, but only the corresponding negative monetary compensation in the remaining member states which can then be used to increase farm prices in national currency.

☐ Guarantee thresholds were introduced into the market organizations for several products. When these thresholds are reached (absolute production level or growth rates of production), appropriate measures are to be taken (reduction in guarantee prices, application of a levy, etc.).

☐ A quota system has been introduced into the milk market organization at the 1981 production level (plus 1 %).

How are these "reforms", which have evolved in response to the most pressing agricultural market and budgetary problems, to be assessed?

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The introduction of milk production quotas is without doubt the most far-reaching change to EEC agricultural policy. The repeated attempts to curb milk production have thus culminated in an extreme form of market control such as previously only existed for sugar.

The example of the milk market is particularly interesting because it might become a model for other markets. The development of the market organization for milk confirms that planned intervention in a market has the inevitable consequence of making further intervention necessary. Thus the quota system developed with remarkable interventionist logic from the co-responsibility levy (first introduced in 1977) via the introduction of a guarantee threshold for milk production (1981). It is revealing that the guarantee threshold in the form of a levy on the milk price covering the costs of surplus production was superseded in its second year, when it could and should have begun to bite, by a still more rigid control system, i.e. production quotas. The concept appears plausible, for the quotas avoid the major disadvantage of increasing milk prices, which is stimulation of production. Political and administrative problems in the introductory phase could then be dismissed as unavoidable side effects which have to be borne until the advent of the golden age of milk market policy.

However, this optimism is based on the hope that in future the milk price can fully respond to the income support objective, but ignores the fact that even in a quota system market forces cannot be totally neglected. That holds true especially insofar as milk price increases will tend to weaken the competitive position of butter against margarine, of milk powder against other high protein feed and also of milk against soft drinks.

If we leave aside the numerous purely economic considerations which weigh against a quota system, there is nevertheless the political question as to whether the introduction of more and more controls into Community agricultural policy is an acceptable development in the long term and whether this development can be in the interests of the Community.

### **Dangers of Production Quotas**

From the Community point of view milk quotas represent a virtual freeze in production at present levels. This to a large extent excludes an essential feature of a common market, i.e. competition in production. The quota system places the Common Agricultural Policy on a completely new foundation. Whereas the guiding principle previously consisted in creating a uniform

basis by means of common price and market mechanisms which individual farmers were free to use to their best ability in keeping with their personal and business circumstances, the allocation of quotas now determines the production rights of the individual farmer. Thus quotas are not merely a tool to restrict expansion of production, but quite clearly have the much less publicised political aim of averting losses in production share to other member states or even to other regions within a member state during the process of adjusting production to market realities.

The potential long-term political and economic damage is likely to be very great. The Community would be departing from the previous principle of gradual harmonization of agricultural policy and wittingly or unwittingly preparing the ground for a return to separate national agricultural policies. The immense administrative and political problems in introducing the milk quota, which have their origin partly in Brussels and partly in the member states themselves, are an early indication that the unwieldiness of the whole system will prompt the member states to make a determined effort to broaden their scope for taking measures specially designed to solve national problems.

Production quotas are not a suitable means of solving the problems of Community agriculture, because they perpetuate a status quo in a sector which is still in a process of structural change. Consequently, holdings which have already advanced beyond small-scale farming receive an "economic rent" from their quota in line with their higher overall production, whereas small farms are abruptly deprived of any scope for development. This can only be remedied by state redistribution of quotas which will always be politically explosive because it would mean taking something away from a large number of farms which is nevertheless not enough to satisfy the few.

Much of the political dynamite in the quota system stems from the fact that a whole series of individual decisions on professional advancement which would normally be taken over the course of several years in many farming businesses, are in practice forestalled and telescoped into a limited period on the strength of a government decision. The need to create a set of criteria for a huge number of individual cases must be felt by those who are affected by it as the cold arrogance of a bureaucracy. It is therefore easy for those affected to blame the politicians and public administration for their situation. Thus a whole professional group is forced into adopting a hostile attitude to the Community, which can do nothing to promote the cause of Europe.

In view of the major economic, legal and administrative problems caused by the introduction of milk quotas and the resulting scarcely controllable potential for conflict, the question is bound to arise as to whether there is an alternative. If mistakes cannot be recognized in advance, at least it should be possible to learn from them once they have been made.

### **The Alternative**

In the intense political debate on the reform of the Common Agricultural Policy, there are at least two principles on which there is a high degree of consensus: the present rates of production growth must be stopped and structural surpluses dismantled, and the structural adjustment of agriculture must not lead to unacceptable social hardships. In addition, the fact that the Community's own resources were exceeded without encountering much political opposition and that the 1984/85 farm price decisions were topped up with national aids shows that the political will to support farmers' incomes still exists.

An effort is being made, however, to gain control of the development of expenditure and make it more predictable. Moreover, experience has shown that sudden changes of policy either with prices, or nowadays with quotas, stand little chance of political survival.

The following ideas take up the guidelines presented by the Commission in 1981 which constitute a viable approach to the future development of Community farm price policy. Unfortunately this approach seems to have been eclipsed by efforts to achieve quick successes in some problem areas, such as the cutting of milk production.

The Commission's view as expressed in 1981 that farm price policy should be geared to medium and long-term market conditions is indeed the only alternative to a policy of administrative controls on the supply of farm products. It is not a question of abandoning price policy completely to the free play of market forces but of shaping price policy so that the basic tools of Community agricultural market policy, which still serve a valid purpose – price support in the domestic market and corresponding protection against outside influences – can be kept functioning. The principles of Community preference, financial solidarity and free trade could be retained.

Compared with administrative controls, a cautious price policy could take account not only of the problem of inflated prices, but also of the unrealistic price relationships between competing farm products such as

margarine and butter, olive oil and other vegetable fats, skimmed-milk powder and high-protein feeds, cereals and cereal substitutes. Restrictive farm price decisions would have the advantage that domestic produce would gradually become more competitive vis-à-vis imports and that the costs of exporting agricultural products from the Community would be lower. Furthermore the permanent conflict with third countries over EC export policy for agricultural products could be reduced and the unpredictable dependence of the EC-budget upon the world market situation could be diminished.

A glance at the political realities shows that a price policy geared primarily to market conditions has little prospect of being implemented at Community level. Farm price policy needs to be supplemented by a mechanism which enables account to be taken of income, regional and environmental factors, which are no less important a part of Community agricultural policy. Moreover, member states which have derived benefit from the current agricultural price policy in the form of a net transfer of funds will be anxious not to lose this advantage completely in the event of current policy being discontinued.

### **Severing the Link with Production**

Direct aids to income are therefore an essential adjunct to any restrictive price policy. In this connection it is imperative to avoid as far as possible the fundamental error of almost all existing types of aid, i.e. their link with production, and to match the aids more closely to social, regional and environmental factors. The variety of aids and their importance in the Common Agricultural Policy demonstrate that agricultural aids are an essential element in finding consensus. To that extent, the long-lasting debate on the pros and cons of aids has been by-passed by reality. For farmers the principal choice is therefore no longer between being a free farmer on the one hand and the nightmare vision of a receiver of alms on the other. In view of the clear limits of price policy as a means of solving all agricultural problems, today the basic questions are the following: should the freedom of individual decision-making, which is still typical of agriculture, be further reduced by quotas and production constraints or should the considerable financial resources which are already deployed in the framework of aid policy not be directed more to the social, regional and environmental problems of agriculture?

The attempt to sever the link between aids and production has so far only been made in individual cases. Thus, in 1981 the Commission suggested

confining aids for durum wheat to farms with less than 10 hectares of this crop. This would have meant that 96 % of the beneficiaries would still have received the same aids. The stopping of aid to the relatively few large businesses, however, would have resulted in savings of 25 % in this aid category. This attempt failed in the Council, because the member state most affected was rightly able to show that a new element had been introduced into aid policy in an individual case, whereas in all other cases the link between aids and production was strictly honoured. Consequently, present practice in granting aids can only be successfully changed if the dissociation of aids from production volume is introduced as a fundamental principle for all aids.

On this basis it would be possible to adapt all existing aids in a similar way as suggested in the durum wheat example. In order to avoid abrupt transitions, the aid should be degressive. After the adaptation of the existing aids, the decoupling of aid from the level of production could be further developed by granting it as a flat rate aid per hectare. The objective of this aid would not be to grant a certain minimum income which would need to be more closely defined or to compensate precisely for the income losses brought about by a cautious policy on prices. The main objective would be to relieve price policy of income considerations in such a way that prices could be fixed in a more market-oriented way.

With this approach, the need for aids would not have to be proved by individual accounts, which do not exist on most farms. The basis for the aid would be the easiest available criterion, namely the surface area. Degressivity is necessary to avoid an abrupt division between recipient and non-recipient of aid.

Another important requirement is that the present piecemeal approach to aids should be replaced by a concept which will enable them to be brought into play as a quantitative counterweight to excessive price demands in the political process of the annual round of farm price negotiations. This has so far not been possible owing to the proliferation of ad hoc measures.

### **Social, Regional and Environmental Criteria**

An important reason for the opposition to a departure from the present policy of agricultural aids based on production towards an aids policy oriented towards social, regional and environmental criteria is that the political argument of global disparity of incomes between farming and the rest of industry would be greatly diminished in force. To this extent a reorganization of the present system involves potential political problems. These have to be weighed against the known political problems connected with the alternative, i.e. quotas. The fact that farmers adversely affected by quotas are already forming action groups is

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evidence that the solidarity of farmers as a group is at risk.

The political advantage of an aids policy based on social, regional and environmental criteria would be that individual farmers could produce what they liked and how much without restriction. The individual would remain responsible for his own future and could not pass the buck to politicians and administrations. In addition, in the context of a restrictive policy on farm prices, account could be taken of the increasingly articulated need for less intensive farming in some regions.

Since in the foreseeable future there will continue to be income disparities between farming and the rest of industry in the member states, and given the differences in respect of regional and environmental problems, the member states should have sufficient scope to determine the amount and nature of the aids. This possibility already exists in the case of some EEC aids, such as the Directive on mountain and hill farming and farming in less-favoured areas. Application of this rule to other types of aid could satisfy the political need for a measure of flexibility in supporting farmers' incomes in the member states without completely abandoning the Community framework and the principle of financial solidarity.

If aids policy is left to evolve from a collection of individual national measures, there is a danger that the Community aspect will be completely neglected and that aids policy will increasingly become a national preserve. In practice this would mean abandoning the principle of financial solidarity. This may well appear to be a desirable goal for short-term budgetary considerations from the point of view of a net contributor country. On the other hand it would jeopardize an important objective of aids policy, which is to divorce price policy from income considerations, for it is unlikely that member states benefitting from a financial contribution by the Community under the market and price policy would renounce this transfer of funds, so long as it was not certain that at least a partial substitute had been created elsewhere.

Finally, an agricultural aid policy based on social, regional and environmental criteria would have the advantage that the transfer of funds from the Community and national budgets would serve appropriate social and regional policy goals.

Whereas the transfers induced by farm price policy are mainly determined by the volume of agricultural production and hence predominantly flow to the good farming locations within the Community and the individual member states, an aid policy based on social,

regional and environmental criteria would tend to channel the resources into areas with a poor farming structure and unfavourable natural conditions. These are usually also the areas with particular regional and infrastructural problems and a disadvantageous population structure.

The most frequent objection to direct aids is that they cost too much. Certainly every aid policy designed to make up a shortfall in income resulting from a freeze on price increases by means of undifferentiated production-linked aids will quickly come up against financial constraints. On the other hand the increases in Community expenditure for aid (2,056 Mio ECU (1980) to 4,537 Mio ECU (1983)) and the readiness of the Council to exceed expenditure foreseen in the price proposals from the Commission (1982/83 +653 Mio ECU; 1983/84 +112 Mio ECU; 1984/85 +1,924 Mio ECU), show that lack of money is not the real reason for the failure to implement a restrictive price policy over a period of years and to switch to an aid policy based on social, regional and environmental criteria.

The more probable explanation is that existing agricultural policy and the political decision-making mechanisms at Community level have particularly favoured the promotion of the specific group interests of agriculture. Solidarity within agriculture was maintained above all because the income support achieved in the interests of low-income farmers benefitted all. The hope that this principle can continue to be effective in the case of milk quotas initially produced a basic willingness among farmers to accept the system. It has meanwhile become clear, however, that a quota system is primarily an instrument to preserve the status quo, which because of the uneven distribution of resources (i.e. quotas) needs to be coupled with a state redistribution mechanism (transfer of quotas). Since small milk producers, who are clearly in the majority, rightly or wrongly feel particularly hard hit by the milk quota system, solidarity among farmers is becoming more and more shaky.

The possibility of granting income aids not linked to production would provide the Commission and the Council with a tool enabling them to resolve the conflict between fixing prices appropriate to market conditions and the social, regional and environmental goals of agricultural policy. This change is a prerequisite if the Common Agricultural Policy is to respond with differentiated instruments to the objectives of Article 39 of the EEC Treaty, without abandoning such essential elements of the Common Agricultural Policy as financial solidarity and the common market in agricultural products.