THE FUTURE OF THE COMMON AGRICULTURAL POLICY*

By Ian Sturgess, University of Cambridge

INTRODUCTION

The objective of this paper is to highlight the constraints on and pressures for these in the Common Agricultural Policy (CAP) and to speculate whither these may lead over the next decade. Little attention is given to the economic efficiency and distributional effects of the (CAP) or the role of the European Community (EC) in negotiation on international agricultural trade. These are well understood in Australia; indeed some of the best and most accessible analysis of these issues has been done here.

The CAP is similar to the policies of most other industrialized market economies in several key respects. Amoung a number of stated and contradictory objectives, priority has been given to the level and stability of the incomes of farmers and the scarcity of food supplies. Income support has been pursued via price support and security by self suffiency – in both areas misguidedly. The main way of raising and stabilizing prices is by border intervention, in the form of restrictions on imports and the stimulation of exports. The first line of defence is a commitment to purchase from farmers for storage (or degradation) at predetermined intervention prices. The instruments of each regime are complex and almost every conceivable device for agricultural support is employed including deficiency payments, home consumption schemes, marketing quotas, land retirement, limitations on substitutes and food aid. However, the quintessential instruments of the CAP are the variable import levy and the variable export subsidy (coyly called restitution) which produce almost complete internal price stability at the cost of destabilizing world markets.

The more distinctive features of the CAP arise because it is not the policy of a nation state but the joint policy of 12 sovereign countries. This is not to suggest that the policy is a creature of the Community. On the contrary it derived from well established systems of protection in the six original member countries. Because of these agriculture could neither be ignored nor treated the same as manufacturing but rather was given a special status enshrined in the Treaty of Rome. In addition to this fundamental principle the three more commonly quoted principles of the CAP are the unity of the market, common financing and community preference. These have been observed in varying degree. Community preference has been enthusically espoused; indeed the gaps between minimum import and internal intervention prices have been progressively weakened. Common financing of price support though not of structural spending has been largely achieved. Indeed many of the problems of the CAP arise from the resultant 'restaurant table' effect. Market unity, that is common support prices at current exchange rates, was achieved only in the first three years of the operation of the policy. Community support prices are denominated in a unit of account which was originally tied to the US dollar and later varying baskets of particular community currencies. The original principle was that national support prices would be then derived from these at current exchange rates. However even before fixed exchange rates were abandoned in 1972 devaluing countries were unwilling to accept the inflationary effect on food prices nor revaluing countries the depression of farm prices. To allow support prices to remain unchanged in national currencies despite changes in currency parities but to prevent the intervention system being undermined by arbitraging exports into intervention in the countries of currency appreciation, a system of border taxes and subsidies was introduced in 1969. These so called monetary compensatory amounts (mca's) were intended to be temporary but like temporary buildings have persisted ever since. They have been the source of much discussion but three

---

* Paper presented to the 1991 annual meeting of the Australian Agricultural Economics Society.

consequences only will be briefly outlined here. First differences in prices between countries have often been greater and trading between them more complicated under the CAP than previously. Secondly production in the countries with strong currencies, notably Germany and the Netherlands, has been stimulated to grow faster than elsewere. In essence currency appreciation has reduced prices of inputs but not prices of outputs. Finally prices in terms of national currencies have moved more favourably for farmers than prices in Community units of account (see figure after p.2). This is basically because for most of the time of its operation the value of the unit of account has been closely tied to that of the appreciating Deutshchmark.

To provide a context for the future discussion of constraints and pressures some recent developments are not outlined.

RECENT DEVELOPMENTS

INTRODUCTION

The review of recent developments in the CAP is necessarily selective. Outlined first is the basic stimulus to policy development and debate, that is the switch of the Community from being a net importer to being a net exporter in many core commodities which has led to acute if intermittent budgetary pressure. Next discussed are four responses to this pressure, each of which could be precursors of further future change. These are the introduction of dairy quotas, threshold pricing related to standard quantities, tighter overall budgetary controls, and land set-aside.

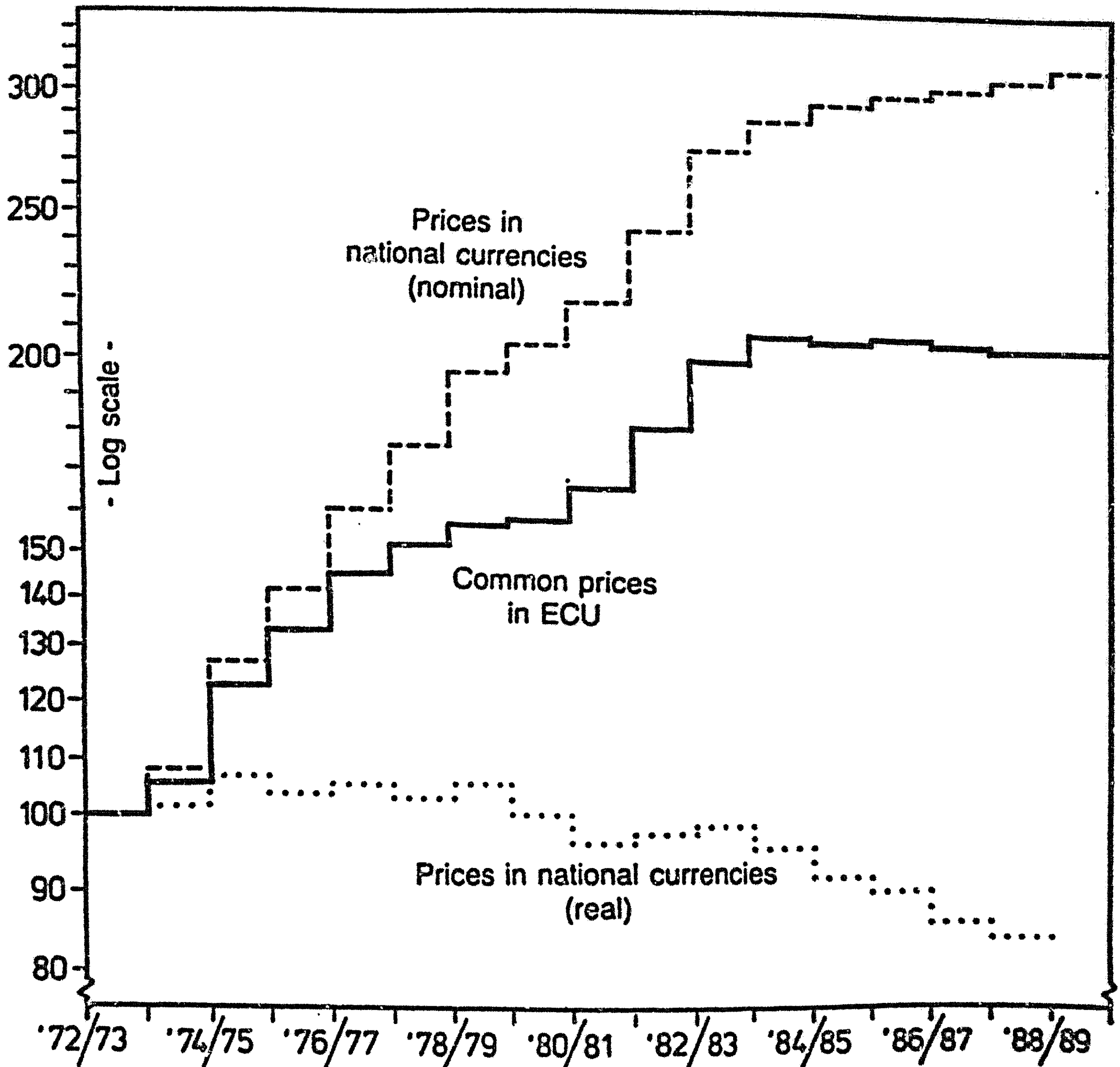
The conceptual framework of this description can be simply stated. The CAP was established with support prices above import parity. Concerns about security of supplies from volatile world markets meant support prices were maintained at a high level even though demand was virtually static while supply was moving out in response to technological advance and the stimulus to adoption of new techniques provided by guaranteed prices. Hence support prices led to rapidly diminishing import deficits and ultimately export surpluses. Gaps between support (intervention) prices and world prices had to be bridged by export subsidies. With world prices declining in real terms and the amount of exports ever increasing the exchequer cost of the policy rapidly increased. To contain costs the Community was faced with familiar alternatives: cut support prices, control production, either directly or by control of inputs, or put limits on budgetary payouts.

INCREASED EXPORTS

The consequences for internal trade of maintaining prices above world levels were only temporarily alleviated by the accession of the UK as a major food inporter in 1973. Denmark and Ireland, both large exporters of livestock products, joined at the same time. Moreover British farmers responded to higher prices with unexpected vigour. Hence, although when all products including tropical are considered the community remains a large net importer of agricultural products the value ratio of importers to exporters declined from over 3 in 1973 to under 2 in 1984 and has since roughly stayed there. Of more significance for the CAP, the community moved into increasing surplus on certain heavily supported products, cereals, sugar, dairy products and beef, up to the mid-eighties and subsequent more prudent pricing and supply controls have no more than held this situation (see charts following P.2). Smaller but troublesome surpluses of wine and intensive livestock products have also changed,while with the accession of Spain self-sufficiency in horticultural products has also increased. These changes in self-sufficiency levels have been the root cause of a budgetary problem. More has had to be paid out in export subsidies while fewer import levies have been granted. The most dramatic response to this problem has been the imposition of milk quotas.

Prices decided upon by the Agricultural Council

(indices, 1972/73 = 100)

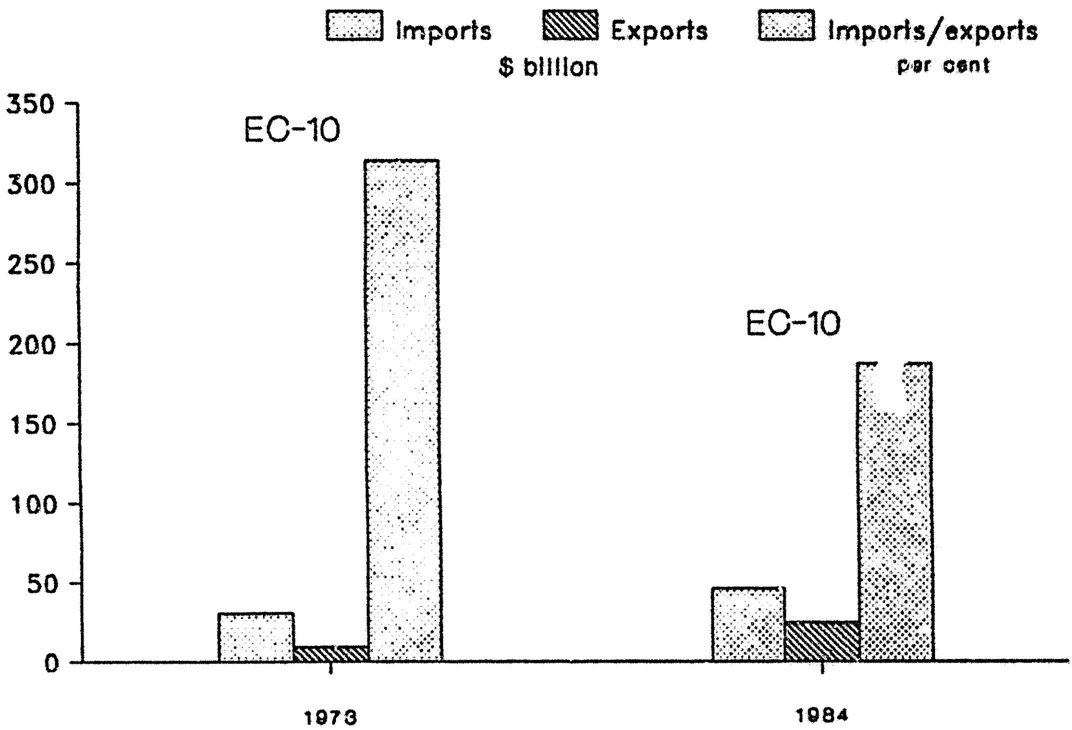


Notes:

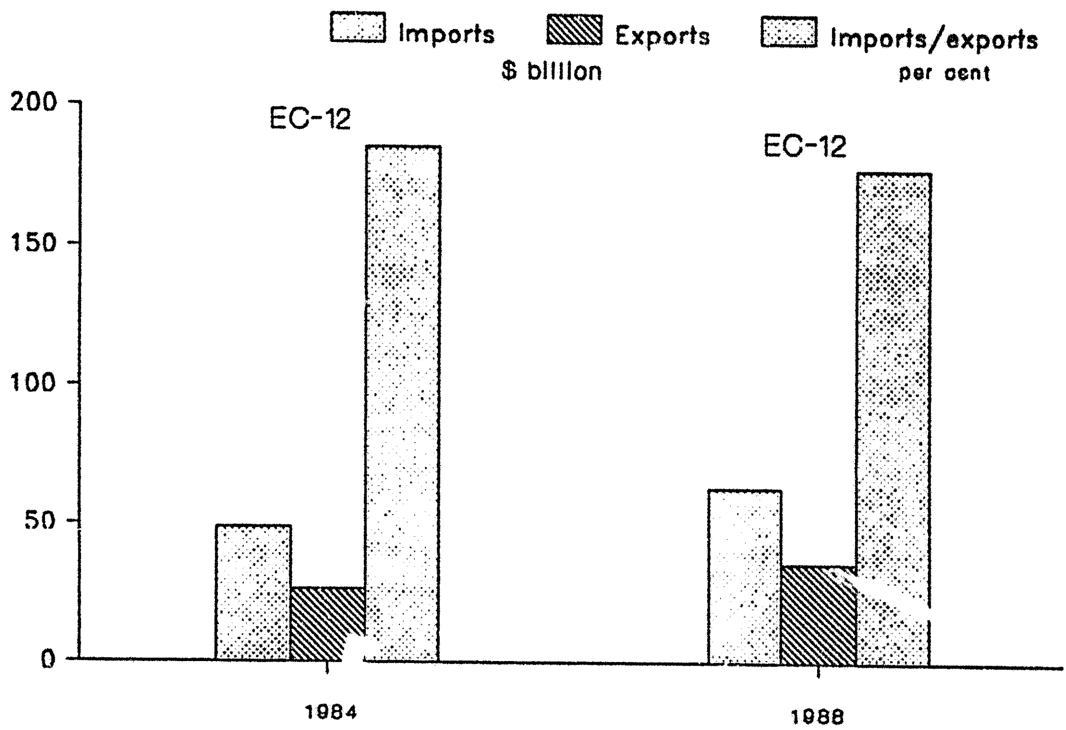
a) The data refer to intervention prices or the nearest equivalent according to product, and are averages for all products and all Member States, weighted according to the value of output of each product.

b) Data in UA or EUA have been converted into ECU equivalents.

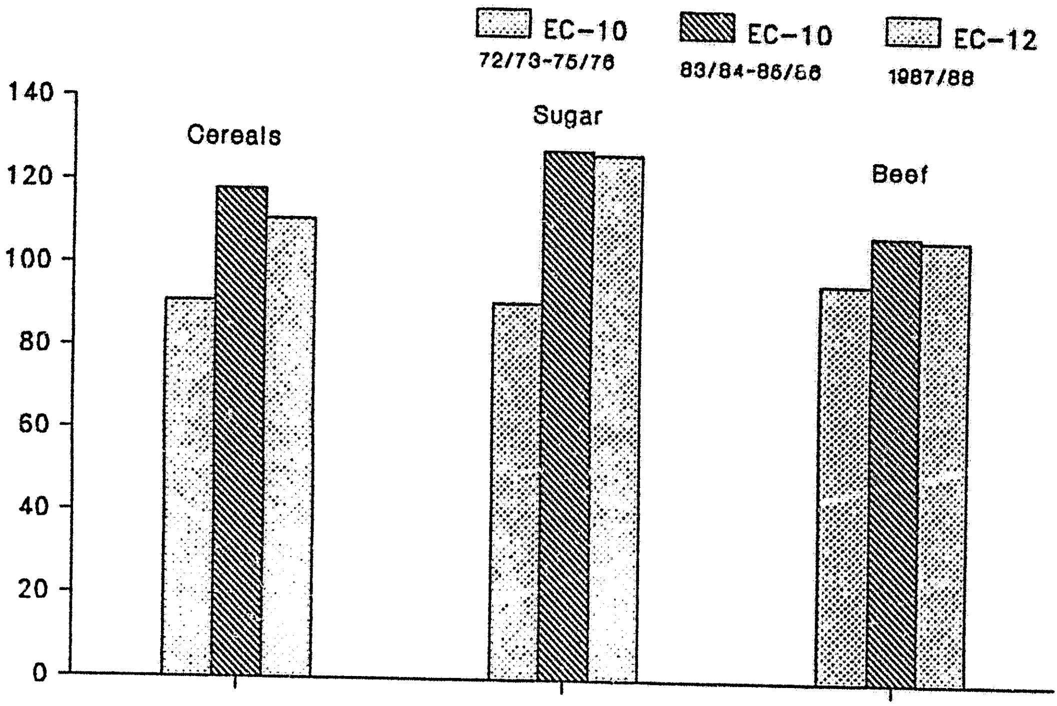
Trade in Agricultural Products



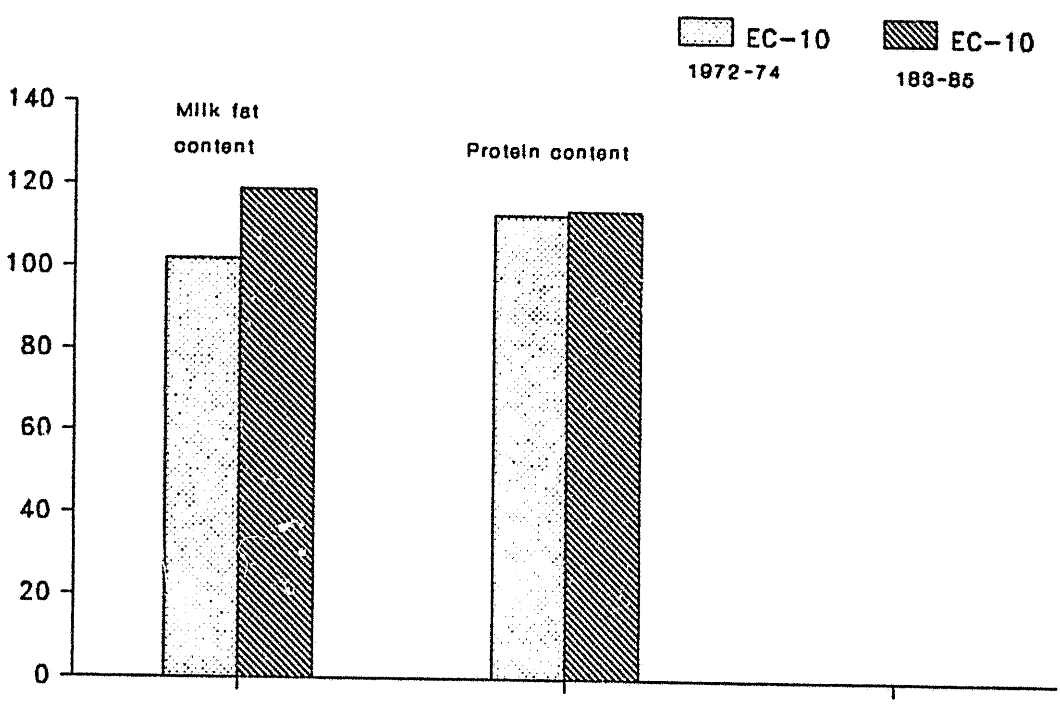
Trade in Agricultural Products



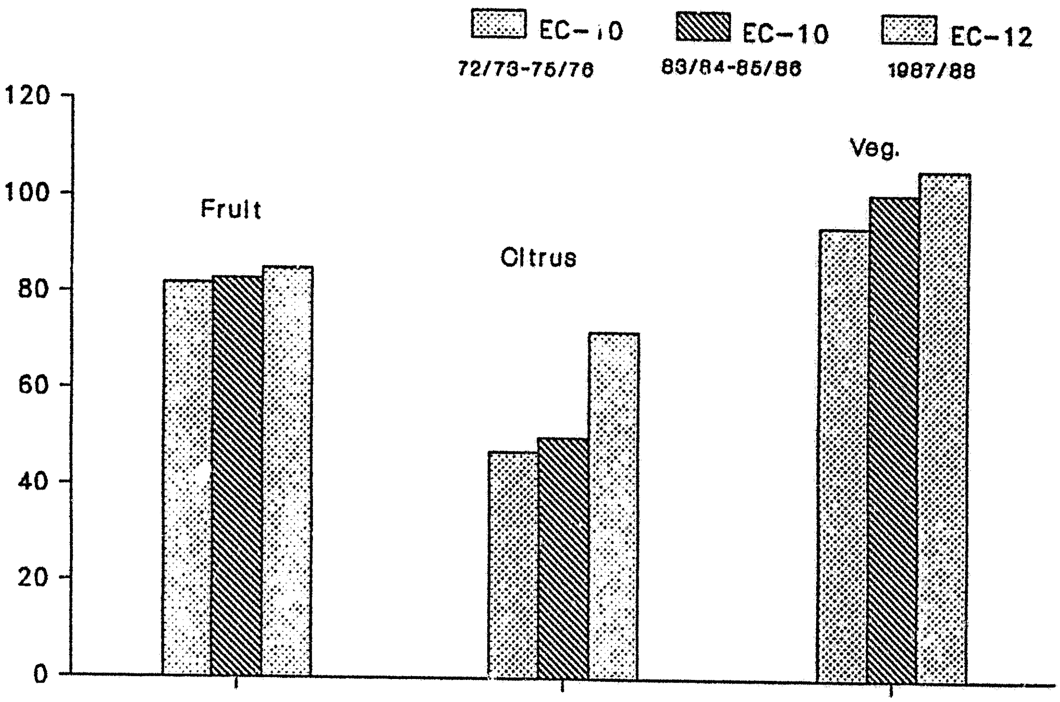
Self Sufficiency Ratios



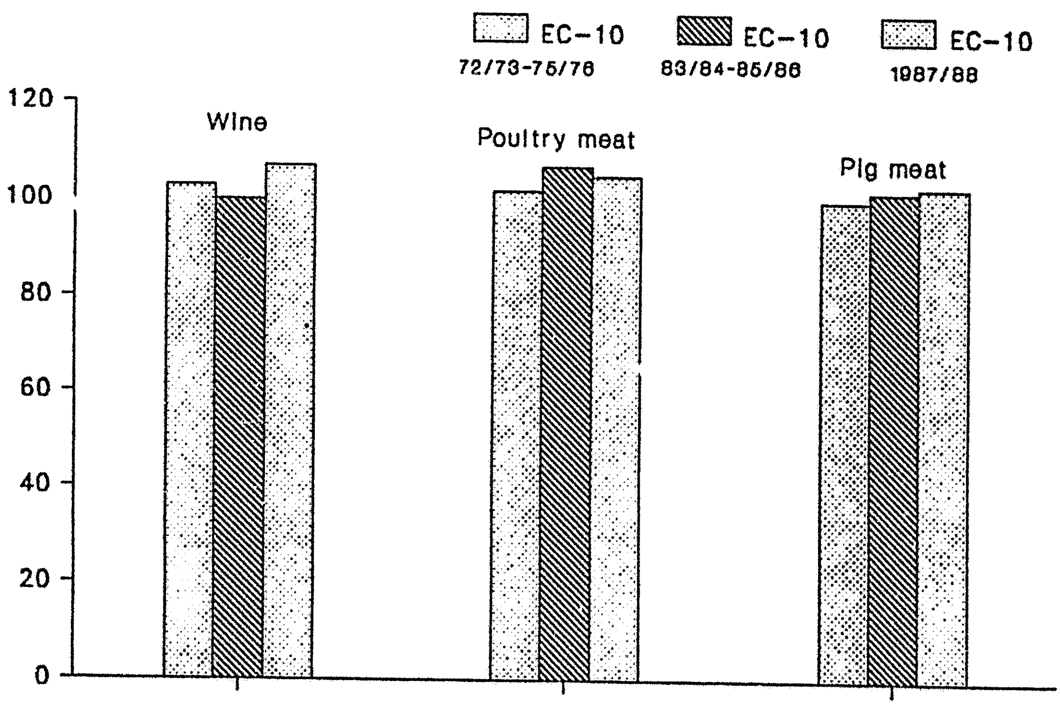
Self Sufficiency Ratios



Self Sufficiency Ratios



Self Sufficiency Ratios



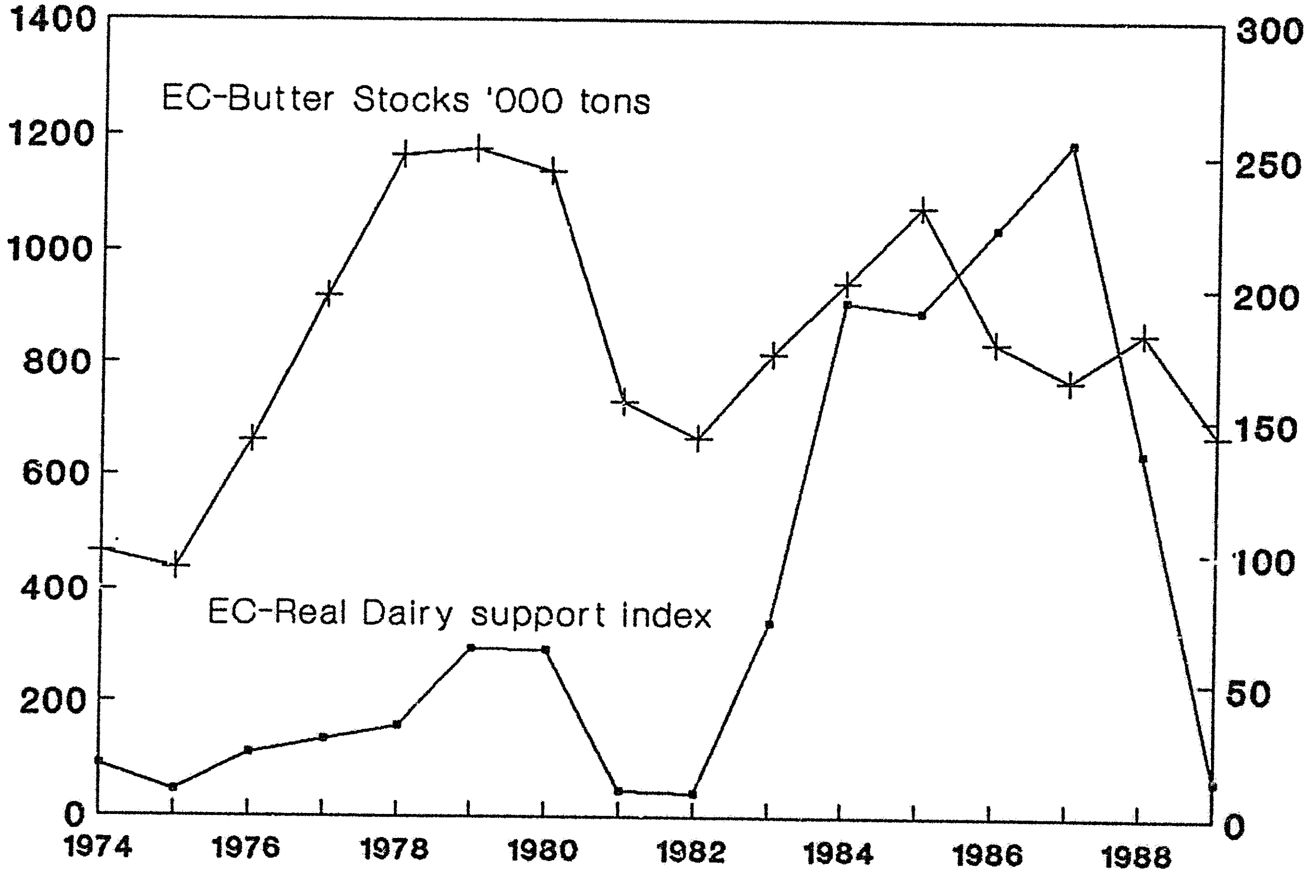
MILK QUOTAS

The wide dispersion of dairying both regionally and among farmers has induced generous support. Prices which gave a modest living with pygmy herds gave a strong incentive to expand production in larger, better managed herds. Supply curves were meanwhile being pushed outwards by a switch to better yielding breeds and feeding improvements. On the demand side consumer taste, spurred by concerns about the effect of butterfat on heart disease, turned against some of the main milk products, especially full fat milk and butter. Thus between 1973 and 1983 deliveries of milk in the EC-10 increased by 29% while consumption fell. Similar trends were taking place elsewhere in the world and unlike cereals there were fewer markets in the third world. By 1983 self-sufficiency in butterfat had risen to 127% and in solids not fat to 123%. The problem was exacerbated, though to a degree exaggerated by political debate, by the free access to the Community of oilseeds at world prices. The consumption of butter was thus further depressed by competition from margarine based on oils bought at world prices. For producers located to take advantage, the deterrent to concentrate feeding of highly supported cereal prices could be in part overcome by reformulation of feeds, using higher levels of oilseed meals and other feed ingredients with tariffs also bound under the GATT at low levels, e.g. manioc and maize gluten feed. The limited world market encouraged stockpiling of butter and skim milk which was inherently expensive because of the perishability of the products (see chart after P.3).

A number of measures had been tried to reduce the problem of surplus disposal. Subsidies had been put on skim milk powder for use in animal feeds, on butter for pensioners and on milk for schoolchildren. Incentives were paid for farmers to give up dairying and co-responsibility levies of from 0.5% to 3% applied to producer prices. These are essentially producer taxes which lower producer prices while leaving consumer prices unchanged. Such a policy has little to commend it on efficiency grounds but for the Commission provided extra funds for surplus disposal. The initial measures proved only palliatives and by the early 80s the Community was faced with the choice of cutting prices by 12% (the estimated cut required to restore fiscal solvency), allowing the CAP to crumble though lack of funds, or finding some new policy instrument. The Agriculture Council was unable to resolve this dilemma and unusually finance and prime ministers became involved in the decision. Though initially quotas were strongly supported only by Germany, the political process in the face of a mortal threat to the CAP came up with a package which enabled all countries to support the introduction of quotas. This package included a tighter system of budgetary controls, a rebate of budget contributions for the UK, a revaluation of the ECU and price decreases on other products.

Effects

The basic principles of the scheme were that a Community quota equal not to domestic consumption but to a level some 15% above this was distributed among countries, then among dairies, and finally among farms on the basis of production in 1981. Production above quota received only a small fraction of the normal price. Inevitably, being produced in some haste, there were loopholes which later had to be closed. Thus some producers initially weakened the effect of the quotas by increasing the butterfat content of the milk delivered or by over-producing in the hope that other producers' underfulfilled quota would be reallocated to them. By and large the quotas, which were further reduced slightly in both 1986 and 1988, were successful in containing both production and expenditure, if not initially stocks. Production was held to within 1% of the quota level each year and by 1988 production was 10% below that in 1983. The surplus of production over consumption which by 1988 would have been over 40% without quotas was held back to under 20%. Consequently exchequer expenditure, mainly on export subsidies and stockpiling, levelled off in the succeeding three years, remaining even in current terms below a peak less than a tenth above that of 1984.



EC-Butter Stocks '000 tons
EC-Real Dairy support index
1400
1200
1000
800
600
400
200
0
300
250
200
150
100
50
0
1974
1976
1978
1980
1982
1984
1986
1988

Farmers have overcome their initial fears to welcome the certainty which quotas provide. In contrast to the preceding decade, there has since been much more confidence in the dairying than in the arable sector. Beef production was initially stimulated by the culling of cows and then depressed by lower calf supplies from the dairy herd, but spill-over effects on other enterprises have been less than expected. Rather than diversify into sheep or cereals, producers have lowered stocking rates and reduced feeding of concentrates. No provision was made for transferability of quotas but in varying degrees (France being the main exception) they are traded within countries. This capitalisation makes it unlikely that quotas will remain for the foreseeable future. Thus in 1988 they were extended until 1992.

GUARANTEE THRESHOLDS

Understandably, given the unwanted radicalism of the change, many in the Community were inclined to feel dairy quotas had resolved the budgetary problem of the CAP. Soaring costs for the cereals and oilseeds régimes soon dispelled this illusion. The first reaction was to manipulate the intervention system (e.g. by deferring paym...s and reducing monthly increments). These somewhat reduced prices at the farm level but in some countries the effect was modified by monetary compensation.

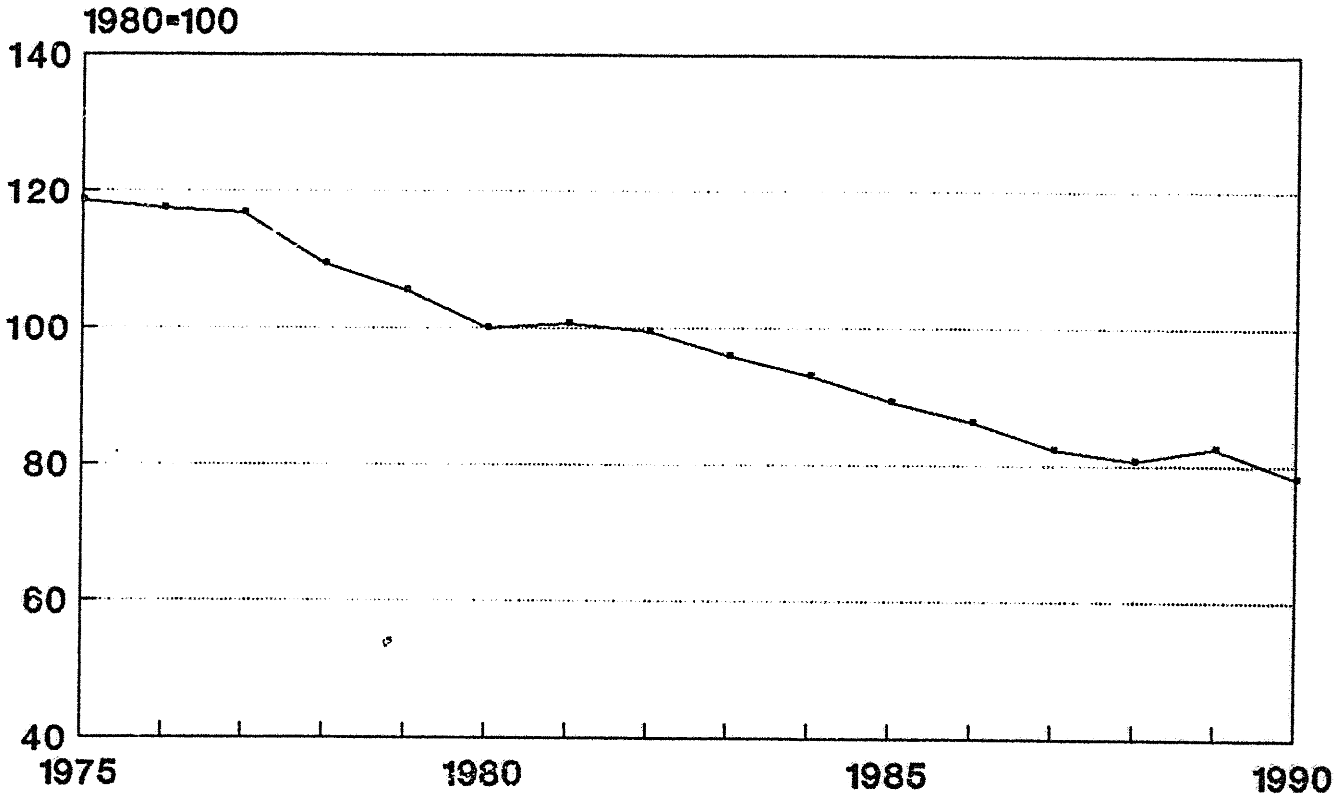
A more formal and permanent reform was made in 1988 with the introduction of guarantee thresholds. The intention was to introduce within an administered price system some of the discipline of a market, though paradoxically the concurrent effect was to make the market more regulated. These applied not only to cereals and oilseeds but also to protein crops, olive oil, sheepmeat, wine, tobacco and cotton. Provisions vary between commodities but the common principle is that if aggregate production exceeds a pre-set threshold level all producers suffer a price penalty. This may be via a cut in support level (e.g. in the intervention price or ewe premium), or by a co-responsibility levy, or by both. In some cases part of the penalty is exacted in the next season either cumulatively or not. The size of the price cuts are related to the degree of over-production but with scales and ceilings varying between commodities.

An earlier version of the threshold system had been brought in for cereals in 1982. The price cut however applied only in arrears. So it was easier for the Council of Ministers to offset its effect by increasing the basic determination. The system set up in 1988 and to apply for the following four seasons provided for a threshold level for total cereal production of 160 million tonnes. (This was above the harvests of 1986 and 1987 but well below the previous record crop of 173 m.t.) The price penalties for exceeding this level were as follows. For excesses of up to three per cent a co-responsibility lev. of an equal percentage of the intervention price was to be levied in the same season; there was to be no further levy for excesses of more than three per cent. Secondly any excess above the threshold, however great or small, would result in a cut of three per cent in the intervention price in the following season. This cut was cumulative if the excess were repeated; thus if an excess followed an excess in the previous season, the intervention price in the next season would be cut by six per cent.

For oilseeds and protein crops the threshold system is more severe than for cereals. The maximum guarantee quantities are lower in relation to recent crops. All cuts in intervention prices take place within the same marketing year as the production excess and there is no ceiling on cuts; each one per cent excess results in a price cut of one half of one per cent. (However cuts are not cumulative from year to year.) The effect has been to depress the prices of oilseeds and pulses in relation to cereals. This has reversed a long-standing policy of encouraging diversion from cereals to oilseeds and protein crops to increase self-sufficiency and farmers have responded predictably.

The threshold arrangements for these and other products have been accompanied by tighter pricing arrangements for other régimes. The guarantee thresholds and related revisions

Index of Producer Prices
EC-11



in intervention systems to make them safety nets rather than regular outlets represent a genuine switch to more severe pricing. The Agricultural Council can still offset their effects at the annual price fixing. However it is now constrained by tighter budgetary control and has so far opted not to do so. Inevitably there are loopholes. Thus on cereals the coresponsibility levy is not paid if used on farm of origin or produced on farms selling less than 25 tonnes a year. Also the effects on cuts in ECU terms at the Community level have been in part offset by devaluations of green currencies. Nevertheless the overall effect of these measures has been to constrain producer prices (see chart following P.5). This however has not generally reduced levels of protection because world prices have also fallen during this period.

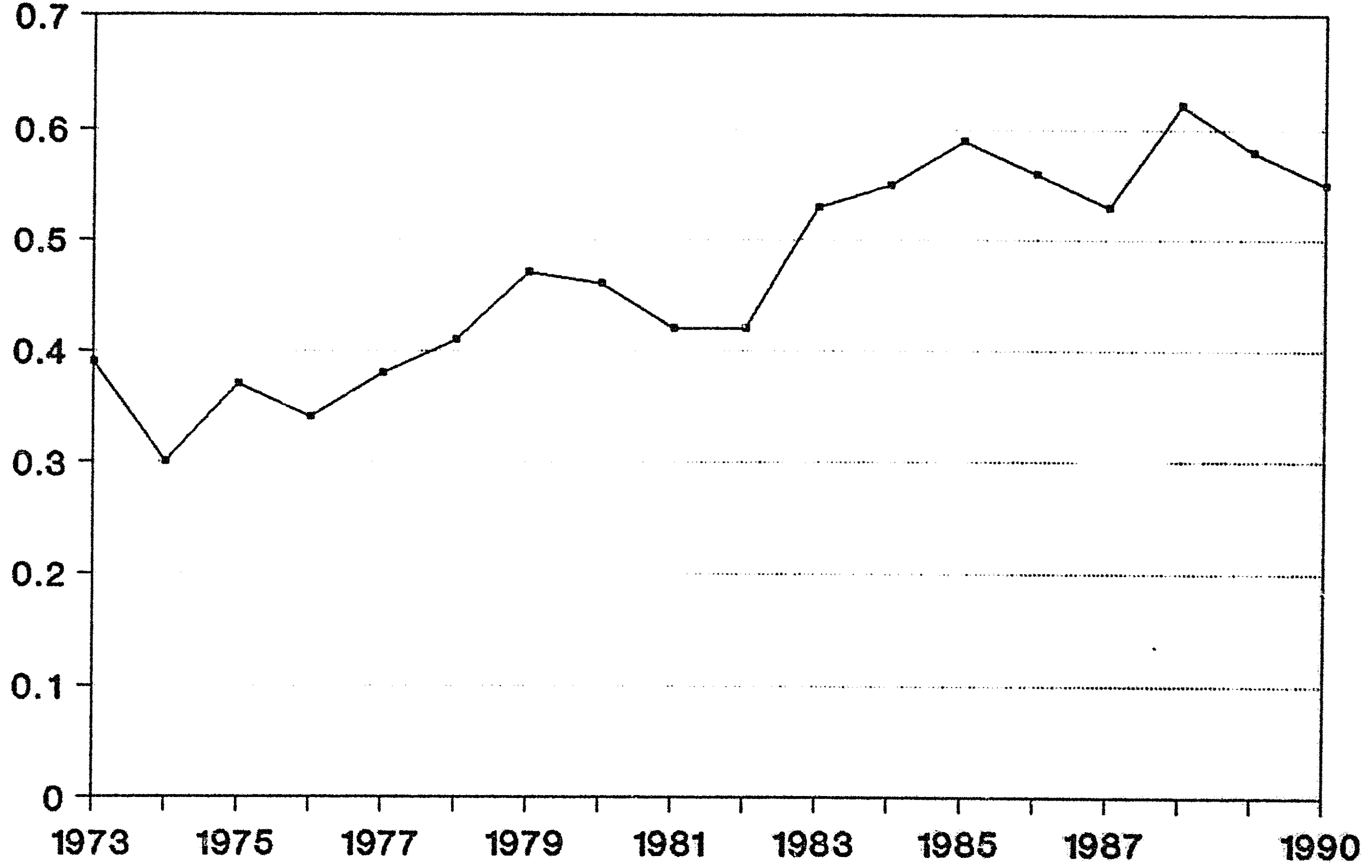
NEW BUDGETARY CONTROLS 1988

Like 1984, 1988 was a year when several important changes took place in the CAP. New rules on budgeting as well as pricing were introduced. In the broadest terms the recurrent budgetary problem of the CAP arises as follows. The Agriculture Council of Ministers (the ministers of agriculture in each member state), which is the main decision maker on matters of agricultural policy, is both encouraged and allowed to award generous price supports. These decisions are made at an annual price review with little opportunity for interim adjustment. On the revenue side however the system provides no flexibility. The Community exchequer (two thirds of the expenditure of which goes on the CAP) however can not run a deficit, borrow, or increase the money supply. In the resolution of the consequences of this conflict finance and prime ministers are involved only exceptionally and then at a late stage. The overall effect has been to encourage creative accounting and ad hoc firefighting rather than strategic planning and in the longer term to push up CAP expenditure as a proportion of Community income. Thus expenditure by FEOGA (the Community agricultural treasury) had been increasing annually at more than three times the rate of GDP (see chart after P.5).

The 1988 budgetary controls go further toward tackling these weaknesses than previous budgetary reforms such as that of the 1984 Fontainebleau summit. A clear aggregate expenditure ceiling will now be provided each year which constrains the growth in spending on price support from a base of 27.5 billion ECU in 1988 to 80 per cent of the rate of growth of GNP over the next few years. If the proposals of the Agricultural Council exceed this guideline (or a derived guideline for a particular sector) a resolution must be found by a joint council of Finance and Agriculture ministers. There are also caps for commodity sectors. If monthly monitoring by the Commission shows that the year on year growth is higher than the previous three-year average, the Commission must first take immediate action, e.g. by restricting intervention purchases, and then if necessary make appropriate proposals to the Council for policy change.

As might be expected there are some exceptional provisions. To cover the depreciation of support stocks 1.4 billion ECU per year is provided outside the limit. Then a monetary resource of one billion ECU can be called from the member states to cover the effects of any further depreciation of the US dollar. Finally there are possibilities within limits to transfer funds between commodity sectors and between years. Despite these qualifications the 1988 budgetary reform should be seen as a significant innovation which will both intensify budgetary pressures and allow them to be resolved more effectively. It should also materially reduce the growth of the guarantee expenditure on price supports in the period 1988 to 1992 as compared to the previous quadrennium. Between 1983 and 1987 expenditure rose by over 12 per cent; between 1988 and 1992 on the assumption of an average two per cent a year growth in GDP it should have risen by six per cent or less.

Net FEOGA Guarantee Expenditure as per cent of GDP



LAND SET-ASIDE

The third change of 1988 to be considered is the instalment of land set-aside. This is included not because its immediate impact on either the supply of cereals or the environment has been great, or for its general novelty as an instrument, but because it represents a first dipping of a toe into the pool of input restriction. The set-aside scheme is voluntary, leaves much discretion to national governments on its implementation and is only partly financed by the Community. The principle is that arable producers who undertake to retire from normal cropping 20% or more of their land for five years, either in a fixed segment or by rotation, receive a payment, fixed nationally by soil class, of between 100 and 600 ECU ($A175 - 1050) per hectare a year. Participants must maintain the land and prevent nitrate leaching and soil erosion. Depending on the country, they may use the land for extensive grazing, growing certain pulses, woodland, or nonagricultural purposes such as 'horticulture' but in some cases with reduced payment.

The response has been small in relation both to the arable area of the EC and to the areas retired in the USA under similar schemes. Only 550 thousand hectares have been signed up; of this 170 are in Germany, the only country to pay the maximum compensation. Variations of this scheme are however supported by environmental and farmer groups and in association with the related but even more inchoate instrument of extensification.

INSTITUTIONAL INHIBITIONS TO FURTHER CHANGE

INTRODUCTION

The recent developments in the CAP just outlined provide some pointers to both future pressures for change and some possible responses. Before proceeding to discuss these it will be salutary to review some of the institutional features of the formation of agricultural policy which make it unlikely that future changes will be rapid, radical or recurrent. They may be briefly stated as follows.

1. Decision making on policy remains mainly international rather than supranational. Despite some erosion of its power in relation to the Commission the Council of Ministers is the key body in policy formation.

2. Major changes require unanimous, or close to unanimous agreement between countries which differ greatly in their agricultural and political structures, levels of self sufficiency in food, the health of their economies, and their product mixes.

3. Decisions on agricultural policy are made in a compartmentalised way by parties who are receptive to the views of farmer organisations and farmer suppliers. This tendency has been a little modified but continues to be reinforced by the complexity of the policy.

4. People in general in the Community are inclined to see the costs of the CAP as a fair price to pay for a reliable supply of their preferred foods.

INTERNATIONAL NATURE OF DECISION MAKING

External observers of the EC might reasonably form the impression that it is the Commission, a body who are in principle first Europeans rather than European nationals, which is in the driving seat of the CAP. Such policy statements as the Community produces emanate from the Commission. It also is responsible for negotiating external trade arrangements and setting export restitutions. This view might well be reinforced by a study of the formal powers of the Commission. In addition to being the Community's executive the European Commission has political, regulatory and quasi–judicial powers which are surprising to those whose model of government is the Westminster system. The Commission can for example bring legal actions in the Court of Justice against countries not fulfilling their obligations under the Treaty of Rome. On points of detail it can issue directives to member states and decide regulations in its areas of competence (mainly agriculture, intra-Community trade and competition policy). Even at a more strategic level the Commission appears to have a key role in that it uniquely has the power to propose legislation to the Council of Ministers.

The Council is, for most practical purposes, the final point of decision. It is a committee of Ministers from the member states, with the membership determined by the subject in question. Thus on CAP matters it is a Council of agricultural ministers, or Agricultural Council. Since the Commission controls the agenda of the Council it might be supposed that it also has the policy initiative. This would be so if the member countries subscribed to a federal concept of the Community. In practice their perception is one of a Europe des Patries. Hence the Council is rarely inclined to rubber stamp proposals coming directly from the Commission. More commonly the Commission's role is to find a passage between the wishes of member states rather than to produce new initiatives. Draft legislation is crafted to be politically acceptable to the twelve member countries. This process is in part carried out through COREPER, a committee of permanent representatives of the member states, or in the case of agriculture, the Special Committee on Agriculture, a committee of ministerial deputies.

It should also be recognised that the Commission itself is not impervious to national influences. Commissioners (of whom there are 17, two each from the five largest states and one each from the smaller) are in practice appointed by governments of the member countries for terms of four years. To ensure either reappointment or a better job in their own country Commissioners are therefore likely to listen more readily to advice from their own countries. This bias is reinforced by considerations of contacts, culture and linguistic convenience. Many senior functionaries also are in practice seconded from national public services so that similar influences apply.

A more 'communautaire' input might be expected from the European Parliament, the members of which are directly elected. However its elections attract only low turnouts and are decided more on current national rather than European issues. More to the point, its roles are consultative and investigational rather than directly legislative. In general it acts as a well informed watchdog, an inquisitor of the Commission and Council and a sounding board for ideas. It has the power to sack (as well as censure) the Commission but it has no power to reappoint and in general the power is too devastating for it ever to be used. In legislation the role of the Parliament has been enhanced a little by the Single Europe Act. It can introduce and reintroduce amendments, in conjunction with the Commission, to the Council. This is not very relevant to agricultural policy, expenditure on which is compulsory and not therefore subject to Parliamentary amendment. In practice and in general a stronger legislative role has been played by the European Court through its judgements on food standards and the freedom of internal trade in food but not on the CAP more narrowly defined. In sum, despite outward appearances and the formal constitution of the EC, decision making on the CAP is international rather than supranational.

Unanimity Requirements

Within pluralist nation states in government policy it is hard to achieve compromises between interest groups with conflicting objectives. The difficulty is multiplied when the process is international as for the CAP. Delicate compromises must be found between member governments each attempting to use EC regulations to achieve its own ends. Because it lacks the ultimate sanction of force an international organisation like the Community is unlikely to be able to impose on a dissenting member country a decision which is seen as being seriously adverse to its national interests. This natural thrust toward unanimous decisions has been regularised but not legalised in the decisions of the Council by adherence to the so-called Luxembourg compromise.

The Treaty of Rome, reinforced by Court judgements, provides that decisions on the CAP can be taken by qualified majority. In 1966 however, following a dispute between France and the Community over the financial powers of the Commission and Parliamentary control over agricultural policy, an agreement was made at Luxembourg that if in the Council a country were to insist that a matter were of supreme national interest then a unanimous vote would be required. In other words each member country had a power of veto. This agreement made explicit what had previously been done implicitly. In the same vein it is uncertain that the extension of majority voting by the Single Europe Act has materially changed the practice of the Council. The Single Europe Act of 1987 provides for decision in Council by qualified majority* on any Commission proposal other than on taxation, the free movement of people or the rights of employees. However whatever the legal position the dictates of realpolitik are likely to require that a decision on a major matter such as a reform of the CAP will have to be taken unanimously.

This requirement for unanimity impairs the legal pre-eminence of Commission proposals. The Rome Treaty provided that the Council could adopt Commission proposals by qualified majority but amend them only by unanimity. As it is the Commission has to seek to find packages of proposals that will be broadly acceptable to all states and contain something for which each agricultural minister can take credit. It must seek at all costs to avoid putting forward proposals that will be seen as overriding a vital national interest.

In the Council itself and its preparatory committees, the policy making process is one of bargaining. Decisions tend not to be taken till the last possible moment with each country seeking to extract concessions by holding out the prospect of a veto. This does not encourage well-considered decisions. The need for unanimity also encourages expansion of expenditure, and thereby the pie to be divided, to avoid disputes over distribution. Above all that there is a strong tendency to preserve the status quo. Agriculture ministers are prone to see any action which visibly reduces the farm income of their country either absolutely or in relation to those of other member countries as being against the vital national interest. This ensures that any package which introduces new benefits or costs for particular countries - as is almost inevitable with any major change - will be rejected. By the same token general acceptability will be most readily achieved by policies which do not differ much from existing policies attained in previous bargaining. It is thus highly likely not only that new instruments will be rejected but also that old instruments will be retained after they are no longer appropriate.

DIFFERENCES IN PERCEIVED INTERESTS BETWEEN COUNTRIES

The tendency to policy inertia brought about by the need for unanimous international agreement is axacerbated because of the member countries in relation to the CAP differ for agricultural, economic and political reasons.

Agricultural structure

In agriculture as such the most often cited difference is in the level of concentration by farms. There is a widely spaced hierarchy with at the one end the UK, where farming is

---

* In the EEC-12 a qualified majority requires at least 54 of 76 votes, distributed into blocks as follows: France, Germany, Italy and UK, 10 each, Spain 8, Belgium, Greece, Netherlands and Portugal 5 each, Denmark and Ireland 3 each and Luxembourg 2.

dominated by middle-class employers of labour, and at the other Portugal and Greece, where most production is still in the hands of struggling peasants. Even within Northern Europe there are striking differences. Whereas in the UK 15% of holdings are over 100 hectares, in Germany these are under 1%. In the UK 80% of cereals production comes from farms growing more than 30 hectares, whereas the fraction in Germany is under 25%. France lies in between in structure. Mean farm size is about 50% greater than in Germany and approaching half of cereal output comes off farms of over 30 hectares. Agriculture in the Low Countries and Denmark, having been also more exposed to external competition, has a developed structure similar to that of Britain. These differences are reflected in income. On the (admittedly imperfect) measure of value added per labour unit, the Netherlands and Belgium approach double the Community average while Denmark and the UK are 50% above. France is about average and Italy and Spain about 10% below. Germany notably is below the average by as much as 20%. Since Germany is the richest country in the Community the farm problem in this sense is the most severe there. Socially and economically the position is qualified by off-farm earnings; almost half German farmers are classed as part-time. In political terms this is less so and in many respects Germany is the strongest supporter of agricultural protection among the countries of the Community.

Understandably then the UK, Netherlands and Denmark are is likely to oppose any measures which target support more toward smaller farmers. Germany, with an uncompetitive structure, favours production quotas and 'monetary' border interventions which limit competition from adjacent countries. The Southern countries favour structural policies more than the Northern.

Product mix

For reasons of topography and climate there are also differences in the product mix between countries. This affects the prospects for reform of particular régimes. France fights especially hard for its wheat and sugar beet producers while the UK has taken a particular interest in the beef and sheep meat régimes. For similar reasons Italy is inclined to veto any change which materially weakens the c.a.p. on olive oil and Greece that for tobacco.

A broader difference in this respect and one of increasing importance is between the Northern countries, Germany, the UK, the Netherlands, Ireland, Belgium and Denmark, and the Southern, Italy, Greece, Spain and Portugal. (France has a foot in both camps.) The Northern countries produce the bulk of tthe cereals, sugar and milk whereas wine, olive oil and many horticultural products are mainly produced in the South. These commodity differences are reinforced by those of structure and income. The Southern countries have three main grievances, the resolution of which they are likely to demand as the price of any major changes in the CAP. First they believe they have received too low a part of the budget expenditure. Second they feel that they have borne the main cost of recent enlargements. Thirdly they complain of being disadvantaged by the concessions in trade made to Mediterranean countries outside the EC, e.g. Israel. These problems have in part been self-inflicted through political disunity and administrative incompetence. Nevertheless the strength of feeling is such that attention will be often distracted in Council from more fundamental and permanent issues. Even if majority voting becomes more common the Southern countries are now in a position to form a blocking minority in the Council; they have together 28 votes compared to the 27 required.

Another broader difference is based on production practice in the feed:livestock complex. It lies between those countries who feed manufactured compounds with high import content and those who are more self-contained. At the one extreme there are those countries who import feedstuffs, now mainly oilseed meals and cereal substitutes, to produce intensive livestock products, possibly for export, and at the other those who feed livestock mainly on domestically produced feeds, both bulk and concentrated. This is broadly a difference between the countries with a North Sea littoral and therefore access to Rotterdam, which is by far the most efficient entry point for imports, and the others. The former, archetypically the Netherlands, are resistant to any policies which involve restricting the relatively free entry to the Community of oilseeds and cereal substitutes. The latter, and especially France, are eager to close the gaps in the EC's protective wall, which engenders a merry-go-round whereby imported substitutes force Community cereals into subsidised exports. These differences are reinforced by differing attitudes to margarine versus butter.

Exporters versus importers

Another difference likely to encourage different attitudes to policy reform is that between those countries who are net agricultural exporters and those who are in deficit. The CAP causes transfers from importers to exporters by two routes; its high external protection and its financing arrangements. Importing countries lose by having to buy at supported high prices imports which outside the CAP they would have the option of buying at world prices. Conversely exporters receive better prices for their exports. The further (and more visible) budgetary transfer arises because levies on agricultural imports are Community 'own resources' while most spending under the CAP is on the dumping and storage of surpluses.

The other sources of finance for the Community are the duties on manufacturing imports and a direct contribution from national exchequers, assessed as hypothetical yield of a standard value added tax. Consequently countries with small agricultural sectors, high import segments and higher incomes (or more precisely, consumption) are contributors to the Community via the CAP, whereas those with opposite characteristics are beneficiaries. This pattern, post 1984, has been modified by an arrangement whereby the UK receives a rebate of broadly two thirds of its exchequer contribution. Nevertheless the broad result is that Germany and the UK are contributors, Italy and France are approximately in balance (though gradually becoming contributors) while the other countries, especially the Netherlands, Ireland and Denmark, are beneficiaries.

It would be expected that the beneficiary exporting countries would oppose any policies which constrain production and would be less concerned to contain the budgetary cost of the CAP. This is indeed the case. Their attitude to pricing is less straightforward. They at times are concerned by the loss of EC market share through the stimulation of production in the exporting countries and the threat to the survival of the policy of the visible costs of surplus disposed. On the contributor side the UK has generally followed a predictable attitude and indeed made reduction of its contribution the core of its policy toward the CAP. In Germany however, other considerations have produced, in these terms, an irrational suppport of the CAP in general and of generous pricing in particular.

Currency strength

One consideration has been the secular strengthening of the mark in relation to other European currencies. Whereas countries with weakening currencies would have been able to present their farmers with increases in support prices, even if Community prices denominated in a unit of account based on a currency basket had been held constant, Germany needed rises in terms of ECU to avoid having to cut DM intervention prices. To do so was a political imperative for Germany. To explain this one has to look beyond purely economic factors.

Political differences

In addition to these variations in national attitudes to the CAP based on measurable contemporary differences in the agricultural and total economies, there are other political differences arising from, for example, historical events, ideologies, electoral systems and farmer political organisation.

Some of the political differences in stance between countries are continuations of policies developed in the 1870s in reaction to the influence of products from the lands of new European settlement. The UK as a large industrial exporter, with an interest in cheap food and competitive wages, and a naval and colonial power, and having a small agricultural segment, opted for continued free trade. In France and Germany however the reaction was to limit imports. Landowners and industrialists combined to introduce protection. Denmark and the Netherlands took a third path. Imports of cheap feed grain were permitted as a base for livestock exports and productivity stimulated by state programmes for input supply, education and marketing.

It is not within the compass of this paper to detail contemporary political features country by country but something may usefully be said about Germany. Contrary to common belief, it is Germany rather than France which has been the most stalwart and consistent defender of the CAP. Also in Germany more than any other member country political pressures have induced attitudes to the CAP which conflict with the country's economic self-interest. Finally, as the main paymaster of the Community, Germany is in a particularly strong position either to encourage or frustrate radical change in agricultural policy. In addition to a tradition of protectionist economic thinking an especially vigorous form of agricultural fundamentalism has conditioned German beliefs and actions. This was most starkly encapsulated in the Nazi slogan 'Blut und Berden' (Blood and Soil) but the ideology was older and is still influential. There are a number of strands. One is a belief that the German tribes were settlers rather than nomadic and that this folk tradition must be maintained. A second is that self–sufficiency is necessary for national independence. This view was strongly reinforced by the food deprivation experienced during and immediately after the second world war. A third thread is that a large agricultural population is necessary to the moral life of the nation. This is associated with a particular reverence for family farms. These are seen as best fitted to guarantee a reliable food supply, care for rural resources, keep the ownership of property dispersed and to provide employment. Finally there is great concern for stability as a goal. Indeed the view that it is the role of the government to protect agriculture against the vagaries of the market is enshrined in German law. This ideology was reflected in policies in the century or so preceding the formation of the EC that were more highly and consistently interventionist than in other partner countries. Thus in the pre-CAP period one government agency controlled all imports of cereals. In 1962 the minimum import price for wheat in Germany was 27% higher than in France and 32% higher than in the Netherlands. The reluctance of Germany to reduce support prices delayed the fixing of the original common prices for cereals for four years (from 1963 to 1967), initiated a theme in price negotiations which has persisted to this day.

Then, as now however, it was political rather than economic factors which encouraged high price support. Favourable anatomical features of the German constitution are that the constitution is federal and bicameral. This means rural interests are over-represented, and elections are frequent. Radical changes in agricultural policies are almost certain to lose votes in rural areas but are unlikely to win votes in urban constituencies. Hence policy reform is unlikely when elections are imminent. Election by proportional representation furthermore means that coalition government is the norm. Often in German politics the pivotal third party has been one especially supported by farmers, thus giving the agricultural interest a particular leverage. In addition to the consequent political power of the Ministry of Agriculture and the importance attached to agriculture by government for ideological reasons, two other features of German politics give agricultural pressure groups an unusually high influence. First farmer political groups are highly cohesive, so that one organisation speaks for all farmers. Secondly there is a strong functional relation between this organisation and the Ministry of Agriculture. Only in Germany among the partner countries are all these four conditions met. (In Italy none of them are met!) There is finally a more general consideration. Because of its immediate previous history Germany has believed that the only way it could have influence in the world was through the EC. The CAP was further seen as an integral feature of the EC. Hence even non-agricultural interests in Germany have been prepared to underwrite the CAP as a necessary price to pay for this political international legitimacy - and also of course for access to a wider market for manufacturers.

COMPARTMENTALISATION OF DECISIONS ON AGRICULTURAL POLICY

The argument thus far is that radical or regular reform of agricultural policy in the EC is inhibited because decisions are made internationally rather than supranationally by a process which requires unanimous agreement between member countries whose attitudes to agriculture and its support differ widely according to farming structure, product mix, and political factors. This assessment is reinforced because at almost all stages of the decision-making process the process is dominated by parties with close sympathy for agricultural interests.

Underlying this argument is a general presumption that both ministers of agriculture and public servants in agricultural departments are more likely to give particular attention to the special interests of farmers (and their suppliers) than to other interests in society such as consumers. This is readily observable in most democracies and the proposition can be reached by a number of theoretical routes. Public choice theory would suggest that to satisfy their needs for advancement, security and prestige, bureacrats and politicians concerned with agriculture require information of a type most readily obtainable from farmer groups. To establish such a relationship they must go some way to helping such groups achieve their own objectives. At the national level such corporatist relations are strengthened by the common financing of the CAP. This reduces the political cost domestically of high agricultural spending and allows ministers, public servants and farmer organisations to align themselves in obtaining maximum support benefits from the policy.

The corporatist relation between agriculture ministries and farmer organisations is of particular significance in the CAP because ministers and officials with other responsibilities are little involved at any stage of making decisions. Because Community political institutions are little integrated there is no regular mechanism whereby central policy can be co-ordinated. Except at exceptional times of crisis therefore the Agricultural Council, of the final authority on questions of agricultural policy. Only at times of revenue exhaustion do finance and possibly prime ministers become involved. Hence in forming the CAP agriculture ministers are less constrained by considerations of costs to other sectors and consequences abroad than in most national systems.

Involvement tends to be confined to agricultural specialists also at the stages of initiation and consultation. In the Commission proposals are formulated in practice by the Agricultural Commission and DG VI, the agricultural directorate, which operates for the most part independently of other directorates. True the proposals have finally to be approved by the full Commission but the Commissioners, except in times of revenue exhaustion, are unlikely to have the will or expertise to make changes. In framing proposals for particular commodities DG VI typically consults the management committees of officials from national ministries of agriculture and possibly also the advisory committees. The advisory committees do contain a minority (about one tenth) of consumer representatives but the bulk of the advisory committees are either from farmer organisations or interests who will align themselves with farmers on most issues, i.e. co-operatives, merchants, processors and agricultural and food employees. The Parliamentary input, though ultimately toothless, to the extent it is influential, comes via the Agricultural Committee, most members of which represent agricultural constituencies. Service on this committee is one of the few ways such members can influence the benefits accruing to their constituents. However, in the consultation phase the key role is played by the Special

Committee on Agriculture, composed of civil servants from agricultural ministries. In sum then most regulations and directives are agreed by agricultural ministers sitting in Council, on the advice largely of specialist committees of unelected public servants also from agricultural ministries. The final phases of decision are also conducted in great secrecy and beyond the scrutiny of the Parliament.

The compartmentalisation of decision making is reinforced by the special legal position of agriculture within the Community. Agriculture (defined to include first stage processing) is given a separate Title in the Treaty of Rome. The Treaty requires the establishment of the CAP and it thus has a status equivalent to the basic principles of the Community. The Commission is given unusual control over agricultural spending by member governments. Thus agricultural expenditure is compulsory and can not be amended by the Parliament. The Community has also been permitted to impose border taxes (mca's) on agricultural products in apparent conflict with the basic principles of the free movement of goods. This privileged legal position is reflected in common political parlance. The CAP is variously described as the cement and the marriage band of the Community. To criticise the CAP is to criticise the Community. This special position is clearly less justified than it was 30 years ago, as agriculture has become more industrialised, international and integrated with the marketing chain. It is also no longer true that the CAP is the only collective achievement of the Community, with recent moves toward a single market and monetary co-operation. Nevertheless, as has been argued throughout this section of the paper, the institutions of the Community favour the retention of anachronisms.

The compartmentalisation of decision making in the CAP is further reinforced by its international nature and the complexity of the policy. Agriculture ministers can thus fashion deals mainly with reference to farmer interests but then apologise to taxpayers and consumers that price rises were forced on them by other ministers. The complexity strengthens the institutional tendency for actors who know most about agricultural issues to play the central role in decisions on the CAP.

The consequences of this setting apart of the making of agricultural policy are two fold. First it makes it unlikely that any policy seriously adverse to established agricultural interests will be adopted. Second the unusually high involvement of public servants inclines the system toward at best incremental change. Bureaucrats are understandably concerned that any change involving new ideas will further complicate their administrative task and possibly reduce their relative power. Their strong preference is to retain standard operating procedures. In general it may be said that the process of making decisions on the CAP is characterised by bargaining among very disparate national agricultural interests with an unusually high input from bureaucrats and for the most part an unusually low input from groups concerned with fiscal or foreign or consumer affairs.

Concern with security

The lack of involvement of non-agricultural groups in decision making reflects in large part a lack of concern rather than a conspiratorial exclusion by producer interests. One view which I sense is common in Australia and to which I long subscribed is that consumers and taxpayers are unaware of the costs involved. The plethora of recent studies from a wide variety of institutions, academic, national and international, on the deadweight costs and the transfers involved in agricultural protection makes this view now, untenable. A more likely explanation is that the general public believe that the transfers are a reasonable price to pay to avoid a repetition of earlier food shortages in Western Europe or those in Eastern Europe today.

Deadweight costs, despite their fascination for economists, do not cut much ice politicially, and perhaps never will. They are hidden, hard to explain (not that economists have tried very hard), sensitive in their estimation to assumptions about elasticities, and rarely compared with the costs of protection in other sectors. Moreover a half or even one per cent once and for all increase in GNP may well not seem a very great prize. The better understood transfer costs however are seen as the premium required to ensure a regular supply of preferred foods. This is not exactly a fear of starvation but rather a strong desire to avoid the hardships of an unpalatable diet, restricted choice, and the high costs of search in an undersupplied market. Folk memories in Europe of food shortages during and immediately after the second world war have an influence which is hard for those in more sparsely settled countries to appreciate. It is salutary to recall that in the winter of 1946/47 in West Germany the official food ration was only 1,400 calories per person per day. For younger people who may be disinclined to heed their parents or grandparents, the well-publicised miseries of food shortages in the countries immediately to the East provide a more contemporary admonition. A recent large-scale opinion poll in the Community found that most citizens believed on balance that the CAP had been good for consumers. Concerns about food security appear to make the general public tolerate and even support a policy which it is not difficult to show is ineffective, inefficient and inequitable.

This view is prevalent in many government circles as well as among the general public. Even in the UK degree of self-sufficiency remains a widely used measure of the success of government policy. In earlier days, of course, this argument was reinforced (though unwarrantedly) by considerations of balance of payments and, in many countries, government revenue. The equation of security with self-sufficiency is probably illfounded. A seriously thought out security policy would likely involve some combination of a food policy to identify priority foods and to increase consumer flexibility, a policy to make farming less dependent on purchased and especially imported inputs, contracts with overseas suppliers, and stockpiling of both food and resources. However as far as I am aware little attention has been given by economic researchers to this question and it is therefore perhaps not surprising that farmer pressure groups and ministries of agriculture are able to persuade both government and electorate that food security and self-sufficiency go hand in hand. True the margin of export surplus might now be considered excessive for several commodities but the strength of this policy militates against changes which would involve any cuts in agricultural production.

Several powerful inhibitors to change have been identified. The force of each has withered over time a little - but only a little. Hence I would suggest again that future changes are likely to be both incremental and irregular.

PRESSURES FOR CHANGE

Having identified the main constraints to change it behoves me now to assess the pressures toward change which will press upon these limits. The context of the CAP over the next decade or so will change. First there will be macro-economic and possibly macro-political changes in the Community. The movements toward a single European market with no hindrances to trade and toward a common monetary policy are now firmly in train. How fast and how far these will progress is uncertain but their impacts will be considerable for all sectors including, though not especially, agriculture. It is possible, though even less certain, that these moves may be accompanied by greater political integration. Also to be considered are the enlargements of the Community both recent and potential. Spain and Portugal have been in the Community since 1986 but because of the long harmonisation period for agriculture the impact has yet to be felt. The reunification of Germany has brought a sudden and unexpected extension of the Community eastward. Movements in neighbouring countries toward more liberal political and economic institutions make further enlargements in this direction possible. Even if this does not happen the disappearance of the 'Iron Curtain' must affect the development of Community institutions not excluding the CAP. Finally the budgetary pressure which has largely driven the CAP in recent years is unlikely to disappear and environmental pressures, though less clearly focused and measureable, are likely to intensify rather than diminish.

SINGLE EUROPEAN MARKET AND MONETARY UNION

The developments in the Community which are now exciting most interest in business circles are the moves toward a Single European Market (SEM) and European Monetary Union. For agriculture the direct effects are less than for other sectors. This is especially so if the industry is narrowly defined distinctly from food processing and distribution. There may however be significant indirect effects, not least via the effect on the general stance of the Community toward the outside world and through possible federalist moves inspired by greater economic integration.

The ideal of the SEM is to complete the four freedoms enunciated in the Treaty of Rome, the free movement of goods, services, workers and capital. The process, which was supported especially strongly by the UK, began with a White Paper in 1985 and was enacted in the Single Europe Act. To the economic theorist it is surprising that legislation is required to bring about what it would be in the interests of countries to do unilaterally. However because trade policies arise from vested interests rather than rational action, these interests need to be persuaded that if they open up their markets they will in reciprocity obtain equal access to larger, more numerous markets abroad. The general aim is that by the beginning of 1993 all non-tariff barriers to trade within the Community will have been eliminated. These barriers are conventionally classified as physical, e.g. health regulations, technical, e.g. labelling requirements and fiscal. Important elements are the abolition of frontier documentation, the harmonisation of industrial standards, free competition in financial services, and the opening of government contracts to all comers within the Community. One valuable change, of particular significance to the food industry, is on product quality standards. The liberal principle of mutual recognition replaces the bureaucratic ideal of total harmonisation. The Community seeks only to establish broad criteria on safety, health and environmental protection within which national standards must fall. The Community now takes the minimalist approach that what can legally be sold in one country can be sold throughout the Community as long as it is properly and comprehensively labelled.

The indirect effects of the Single European Market on agricultural policy may be more important than the direct. First there is likely to be some effect through high Community GNP. How much this last will be is a matter of debate. The officially commissioned Cechini report suggests a boost to real GNP of about a tenth. A healthier economy by lowering input prices and improving off-farm opportunities should moderate the pressures for agricultural support but not so much so that it is necessary to consider at length its likely extent. A more serious issue is whether the SEM will lead to an extension of its liberal precepts to the external relations of the Community, or rather encourage a retreat to a Fortress Europe to prevent the benefits being captured by foreigners. The latter political climate would clearly be much less favourable to the reform of the CAP.

The 1985 Act makes little specific mention of agriculture. The requirements on removal of physical barriers to trade and the harmonisation of health and hygiene regulations clearly apply to agriculture but these are not specific to agriculture. The Commission has taken advantage of the Act to emphasise additional objectives for agricultural policy, including the stabilisation of production and expenditure, a closer link between agriculture and other sectors, the preservation of the family farm, and international co-operation. These shifts in emphasis, though interesting in themselves, do not seem inherently related to the Act. The issues which stem more directly from the move to an SEM are the harmonisation of plant and animal health regulations, the future of mca's and the position of quotas, national aids and taxes. The harmonisation of regulations has run into difficulties both for technical reasons, in particular a dearth of expertise, and because of differing impacts between countries.

On mca's the original expectation was that without border controls these would no longer be able to be administered. However it now appears that to allow for differences in indirect taxes, which contrary to original intentions are to be permitted, provision will be made to collect and redistribute among countries the revenue from such taxes at the final point of consumption. This mechanism could also be used for mca's some other respects also the Single Market may paradoxically lead to some loss in efficiency of the CAP. Thus in anticipation of the Single Market the exceptional provisions whereby the UK has been allowed to support beef and sheep production by deficiency payments are being withdrawn. A corollary of this system is that the deficiency payments had to be clawed back when beef or sheep meat was exported to other countries to avoid the de facto payment of an export subsidy. This will no longer be possible with a single market.

The philosophy of European economic integration is a mixture of liberal and protectionist elements. A core liberal element is the elimination of barriers to trade among member states. Complementary to this however is the belief that some of the pains of social adjustments to competition should be alleviated by increasing the demand for Community products through a common level of external protection against imported supplies. A third prong was the Europeanisation of decisions on especially protected sectors such as coal and steel, textiles and agriculture. The hope of liberal Europeans was that this would expose the folly of these policies, a hope as yet unfulfilled. These strands are intertwined in the Single Market movement. So far the liberal elements have been most prominent. It should be noted however that the Single Europe Act qualifies its otherwise pro-Market stance by a commitment toward harmonisation on rules governing the health and safety of workers. Apparently mutual recognition is not to apply here. Labour and environmental laws are to be approximated upward. Such distortions of labour markets like most price distortions would encourage protectionism both through covert subsidy and in relation to the outside world. A resurgence of socialism through the Community back door in this way is a possibility rather than a probability. A more likely scenario is that internal liberalisation will be accompanied by some weakening of the commitment of the Community to external free trade. Certainly the Commission is eager to promote large European firms to match those of Japan and the USA. What is clear is that it can not be assumed that the development of the Single Market will necessarily make the Community either more liberal in its trade policy or more intolerant of such distortions of factor markets as the Common Agricultural Policy.

Monetary union and possible federal moves

The Delors report which aims to chart the future path of integration of the Community declares that closer economic union must be accompanied by closer monetary union. Some progress has already been made. The Exchange Rate Mechanism which in the early years after its introduction in 1979, when parity revisions were frequent, was little more than a floating peg, has since 1983 been more nearly a system of permanently fixed exchange rates. This has been strengthened by the recent accession of the UK. For the future the Delors report sets target dates of 1994 for the setting up of a European Central Bank and 1997 for that of a common currency. This programme is accepted by most countries except the UK and there should be considerable economic benefits a more critical question is whether monetary integration will lead to greater political integration. Certainly the establishment of a European central bank must involve some loss of sovereignty. There could no longer be independent monetary or exchange rate policies and some fiscal autonomy might also have to be ceded. Monetary union does not require political union. After all the Gold Standard operated without a supranational authority. Nevertheless monetary union makes political union more likely.

Political union has received less attention than economic union but there is considerable enthusiasm in Germany and Italy for such a move. This is seen as necessary if the Community is effectively to consolidate its freedom of movement, enlarge to include countries in EFTA and Eastern Europe, and to collaborate on defence, security and environmental improvement. France and the United Kingdom however are reluctant to have the sovereignty of their national parliaments compromised. On balance further political integration seems more likely than not. It is not difficult to envisage a federal model which would encourage greater economic intervention, more power to pressure groups, and a greater role for bureaucrats - in short one which would even more firmly entrench the existing CAP. In this model the need to take collective action on such issues as external trade or defence leads to most political direction coming from the centre. There are indeed influential elements within the Community who support such a federal structure. However the overall political climate is very much against it. There is now little faith in a benevolent and omniscient state and great scepticism about the workings of political agents and institutions. This makes it likely that any future federation would have strong constitutional guarantees that would limit the control and regulatory functions of Community institutions. National parliaments would be more directly involved in decisions and thus the influence of pressure groups would be limited by cross-national competition. Among these constitutional constraints would be rules against the abuse of power, policed perhaps by the European Parliament, strict monetary rules, and a limit on the size of the budget. The Commission would be made strictly non-political. The European Council would remain the primary decision maker but would derive its authority from national parliaments. Individual countries might retain powers of veto and withdrawal, thus preserving separate national jurisdictions, even though there would be some loss of efficiency from the free rider problem. In such a federation producer biased policies such as the CAP would be less likely to thrive. Intensity would less readily overwhelm numbers.

Our discussions have thus produced two slightly paradoxical conclusions. First one can not be confident that a Single European Market will make reform of the CAP in a liberal direction more likely. On the other hand future moves toward greater European political integration by reducing the power of both bureaucrats and pressure groups, may enhance the political possibilities of developing a more rational agricultural policy.

ENLARGEMENT OF THE COMMUNITY

For the present further integration of the Community has taken precedence over expansion. The view that the Community should mark time until other new democracies in Eastern Europe have been absorbed has been rejected. On the contrary, there has been a move to accelerate integration in order to bind an enlarged Germany firmly into the Community and prevent any danger of a rival central European alliance. Thus we are reminded once again that the ultimate raison d'être of the Community is political rather than economic. Nevertheless before the end of the century it is likely that some Eastern European countries will have joined the Community. If, as is likely, though now by no means certain, that as the role of the Community as an instrument of security is lessened, then the EFTA countries, in particular the neutrals Sweden, Switzerland and Austria, might also have joined by then. There could also have been further extension on the Southern flank with the accession of Turkey. However rather than speculate on the consequences of hypothetical changes it is more fruitful to consider the effects of actual recent enlargements to include Spain, Portugal and, through the unification of Germany, East Germany.

Iberian Accession

Spain and Portugal joined the Community in 1986 following six years of hard negotiation and the earlier Mediterranean enlargement of 1981 to include Greece. A long transitional period of seven to ten years, during which production is restricted by lower prices and trade by quotas, was agreed so that the main impact has yet to be felt. The main impacts are likely to arise through increased budgetary pressure, on both the total and agricultural budgets, a greater political thrust toward support for Southern products and an increased role for structured policy. These arise from the key features of the Spanish general and agricultural economies. Unemployment is high, around double the Community level, while incomes are low. Over 15% of the Spanish labour force work in agriculture so that the number of farmers in the Community has been raised by some 40% (and the agricultural area by over 30%). However they contribute only about seven per cent of national output in reflection of a weak farming structure. Fruit and vegetables, olive oil and wine feature prominently in the production mix in relation to cereals and milk. Thus whereas the accession of Spain has increased total Community agricultural output only by about 15%, output of vegetables has been increased by a quarter, fruit by a half and olive oil by almost 60%.

Though Spain may be a particular beneficiary of freer trade in manufactures under the 1992 programme she will no doubt continue to press for regional aid from her richer partners. There is also a spill-over effect. Other Mediterranean countries seek compensation for accepting greater competition from Spain. Hence Integrated Mediterranean Programmes which seek to link agricultural development with the building of new roads, water supplies and tourist facilities, will continue to be a drain on the general budget. In the agricultural section some budgetary savings are arising for example through no longer having to subsidise dairy exports to the acceding countries. The net effect however is adverse because policy alignment is either reducing consumption or increasing production of products already in surplus and for which support comes from transfers from taxpayers. Consumption of olive oil is being discouraged not only by higher prices but also by the abandonment of quotas on competing vegetable oils. Yields of table wines are being encouraged upwards with better EC prices. In addition the Community is losing the import levies on Spanish exports of fruit and vegetables, 90% of which went to the Community even before accession.

In political terms the accession of Spain is adding to the pressure to support products like wine, fruit, olive oil and soyabeans more generously in relation to the Northern products of milk and cereals. This pressure from Spain is being increased as the country switches resources more toward Mediterranean and away from Northern products. With now a blocking minority of votes in the Council the Southern countries are now in a better position to prosecute their common interests. Having small fragmented farms in the North and latifundia with absentee landlords in the South, as well as a general farm problem of low relative incomes, Spain by joining the Community has materially increased its structural problems and the case for giving more attention to guidance in relation to guarantee expenditure accordingly strengthened.

In sum then the full adoption by Spain of the CAP will intensify budgetary pressures and strengthen the case for diversion of support spending on dairy products and cereals toward horticultural produce, wine and possibly olive oil and toward greater expenditure on structural policies.

Addition of East Germany

In contrast to the accession of Spain and Portugal the absorption of East Germany by West Germany has been hastily prepared and not subject to a transition period. As already mentioned the main immediate impact on the Community has been to accelerate the timetable of moves toward monetary and political union. This reaction has been strongly urged by France but in no way resisted by Germany. Chancellor Kohl appears eager to embed Germany firmly in the Community to avoid any fears that Germany will break free of its Western moorings and has promised his French allies that he will join them in aiming for political and monetary union by 1997. The unification of Germany also now seems unlikely to be seriously disruptive to the Community on the economic front, despite earlier fears. Simple but salient facts to bear in mind here are that East Germany is little more than a quarter the size of West Germany in population

(16m cf 61m) and at best are sixth in national income. True, to prevent a further politically destabilising refflux of people from East and West the German government is having to mount a colossal new programme of public expenditure to improve social services, renew infrastructure and clear up pollution. The effects on inflation are however being cushioned by large savings and international payment surpluses and by the commitment of the Bundesbank to sound money and a strong currency.

On the more narrowly agricultural front there has been some disruption of Community livestock markets through East Germany being used as a conduit for stock from other countries in Eastern Europe. This should however be corrected by tighter frontier controls. The immediate effect of East German agriculture per se on the CAP is less dramatic since the country is a small net importer of many products and much of its production is not of exportable quality. Thus for cereals in relation to a production of 11 million tonnes 1.5 are imported. There is potential for increased production. Despite soil and climatic advantages crop yields are about 20 per cent lower than in West Germany. There are serious legal and ownership problems yet to be overcome in dismantling the large co-operative farms but in the longer term a structure superior to that in many parts of West Germany. In sum then the unification of Germany seems unlikely to disrupt the Community either economically or politically. It may eventually increase surplus pressures but in the medium rather than the short term.

Other pressures from Eastern Europe

The potential for increased agricultural production is even greater in other parts of Eastern Europe. For example in Romania yields of wheat are little more than half those in East Germany. These countries, to satisfy their thirst for foreign exchange (not least to pay hard currency for oil imports from the USSR) and because their manufacturing plant is antiquated, are likely to seek to increase their exports of farm products. Fearful of a flow of economic refugees and seeking to avoid the political isolation of Eastern Europe, the Community is likely to become more open to such imports than in the past. One can not be sure however that the Community will follow GATT principles in making itself more open to agricultural imports from all origins. It is more likely that, as for the associated ACP (African, Caribbean and Pacific) and Mediterranean countries, special arrangements will be made.

BROADER INTERNATIONAL PRESSURES

From countries more distant than Eastern Europe pressures may arise indirectly through the effects of world prices on budgetary costs but direct political influence is likely to be small. As in other developed countries decisions on agricultural policy will continue to be concerned almost exclusively with domestic interests. There is no way for foreign countries to take part in domestic bargaining and there is little incentive for policy makers to take heed of advice from foreigners since they are not part of their constituency. Bureaucrats for their part are understandably reluctant to complicate further the process of policy making to introduce foreign concerns.

For the foreseeable future budgetary rather than external pressures will be the main driving force in diverting agricultural policy from exclusive concern with farm incomes and self-sufficiency. Also influential however will be a more broadly based pressure in concern over the external effects on the environment of a specialised, capital intensive agriculture. To this question we turn first.

ENVIRONMENTAL PRESSURES

Over the past five to ten years there has been revived concern about environmental pollution. There has also been an increased willingness to consider correction by routes other than by direct regulation, i.e. by taxes, subsidies, pollution permits and the redefinition of property rights. This is one reason why environmental concern and agricultural policy are more closely linked than in the past. The other reason is that only recently in Europe (and even now not universally) has agriculture been seen to be environmentally damaging. This is surprising when it is considered that agriculture is the main user of around 80% of the land area. Until about twenty years ago farming was seen as being almost wholly good for the environment and the main imperative that of shielding farmed areas from urban encroachment. With changes in agricultural technology and greater capital intensity that view has changed rather dramatically. Even now however the hostility is not by and large to farming as such but rather against particular farming practices. Thus the Community's opinion poll discovered that most people thought the CAP provided the economic conditions necessary for preservation of the environment but they were nevertheless concerned about the quality and safety of food and what they saw as the excessive use of pesticides and inorganic fertilisers.

Contemporary European concerns about agriculture and the environment relate broadly to conservation of natural resources, wildlife, pollution and scenic amenity and countryside access. These concerns are sometimes in conflict. Thus improved access may conflict with the preservation of wildlife. There can also be differences of opinion on for example which species to encourage or the qualities of different landscapes. Environmental pressure groups are many and their positions are not well brokered in the way that agricultural interests often are. There are narrow differences in emphasis between countries. Germany and its neighbours the Netherlands are especially concerned about pollution, whereas in Britain anxieties about wildlife and landscape are more to the fore. The Southern countries apart from being generally less exercised are especially interested in soil conservation. Though not politically well focused the range and depth of these environmental concerns is increasing.

Some ten per cent of the land area of the Community is officially accepted to be threatened by soil erosion and green groups claim that this is a substantial understatement. Through loss of habitat and the use of pesticides the range of species of flora and fauna has been reduced over the past generation at an unprecedented rate. In West Germany, where three quarters of the losses are attributed to agriculture, over a quarter of the species of flowering plants and ferns have become extinct or endangered. Over the past thirty years in the United Kingdom 10 out of 55 butterfly species became endangered, 6 out of 43 dragonflies, 4 out of 12 reptiles and amphibians and 4 out of 15 bats. Pollution concerns relate especially to water, an understandably emotive area. Though the dangers are not well proven there is little doubt that levels of nitrate pollution in groundwater have increased and that the main culprit has been agriculture. In the Paris area for example the level of nitrates in drinking water has doubled over the past 20 years. Contamination of water by run-offs from slurry and silage are also increasing problems. Another powerful if not necessarily well-founded fear is of pesticide residues in foods.

Concerns about scenic amenity and access relate to such changes as increased specialisation and larger field sizes, the ploughing, fencing and improvement of permanent pasture, the filling in of ponds and removal of hedges, and the erection of modern industrial type buildings. It is recognised by the more thoughtful environmentalists that many of these external costs are attributable to technological change and higher relative labour costs rather than to agricultural policy. Nevertheless they see rightly the raising and stabilisation of prices as an important contributor to these external costs (and in any case look to government to reduce them). Price supports have led to more intensive use of land. In arable farming there has been a great increase in the use of both fertilisers and pesticides with a consequent reduction in species and (more debatably) problems of contamination. Higher stocking rates and in particular more intensive housing of livestock have led to problems of dung and slurry disposal as well as air pollution. More certain prices have encouraged mechanisation and thereby field consolidation, with grubbing of trees and hedgerows and also a shortage of labour to manage hedges andwoods. Specialisation has been encouraged both within farms and regionally, thus reducing the diversity of both landscapes and wildlife. By increasing land values price supports have led to higher land values thus increasing the opportunity cost of other uses of land and encouraging land improvement by drainage, irrigation and pasture reseeding. Hence ponds, ancient lowland woods and hedges have been taken out. Grazing marshes have been drained and other wetlands dried out by irrigation schemes. This has had particularly savage effects on the numbers of birds, amphibians and wetland plants. Improvement of lowland heaths and upland grassland has destroyed natural vegetation and wildlife habitats. Fencing and mechanisation have reduced the access to the countryside of an urban population with greater leisure, mobility and inclination to enjoy it.

One general consequence of this concern is to increase the interest of the general population in agricultural policy. While concern about food prices on the one hand may be diminishing with increased incomes and with security, on the other as export surpluses rise the concern that policies should protect the environment is burgeoning. One particular result is to reinforce feelings about the inequities of present production based systems of support. The smaller, more traditional labour-intensive and diversified type of farm is seen as more likely to produce the desired environmental goods. Beyond this there is considerable diversity of opinion on the best instruments to use. Some environmentalists would advocate stricter regulations; for example more planning controls, compulsory retirement of land, or restrictions on pesticides. Others, more friendly to farmers, would prefer a redirection of subsidies away from food toward environmental goods. In sum then environmental concern is increasing, well-founded but diverse in both its ranking of problems and its favoured solutions.

BUDGETARY PRESSURES

Though environmental pressures will become increasingly powerful it is likely that in the future as in the past the strongest force for change will be pressure on the Community exchequer. Some institutional features of the CAP and its formation already discussed 1) predispose it to budgetary crisis and 2) make budgetary problems a particularly potent force for change.

Any policy of supporting prices of commodities mostly in export surplus at prices well above levels of parity which are themselves trending downwards is likely to cause increases in government expenditure which strain political acceptability. The problem is unusually acute for the Community because its institutions encourage profligacy in expenditure but give little leeway on the revenue side. Agricultural policy is internationally determined but collectively financed. This produces a restaurant table effect. Because member countries pay not the full costs of surplus disposal of extra production but only a share broadly equal to their fraction of Community GNP, they support policies which increase their production more enthusiastically than if they were nationally responsible. This effect is particularly strong for those countries, the majority, who are net beneficiaries. Furthermore agreement by bargaining, which arises from the need for unanimity, is most readily achieved by policy changes which increase the size of the pie to be divided. Profligacy is further encouraged because the EC has no regular mechanism for balancing the funding claims of policies, and decision making at all levels is largely by agricultural specialists. Again control is not by the parliaments of the member states but by the European Parliament and only then in a very attenuated way. Agricultural expenditure is compulsory and not subject to line by line review. The Parliament can reject the budget in toto but cannot deny supply completely.

On the revenue side the own resources of the Community (for all its needs, agricultural and non-agricultural) are closely limited. All levies and duties on imports go to the Community exchequer and beyond that it can call on contributions from member contries but only within severe limits. The basic ceiling, since 1986, is the hypothetical yield of a 1.4% applied in standard fashion. If account is taken of the UK rebate this in practice is equivalent to a 1.25%. There is moreover since 1988 conditional provision for further contributions but only to a limit of 1.3% of GNP. The overall system makes it highly likely that sooner or later expenditure will bump against the revenue ceiling. When such collisions occur they are, especially if sustained, an unusually strong impetus to policy reform. The reasons for this have been well put by Josling and Moyer. Other actors are brought into the policy process, certainly finance agencies and probably also prime ministers. Additionally Commissioners responsible for other programmes will become involved to protect their financial means. Hence policy making becomes less compartmentalised and decisions less a process of partisan mutual adjustment. The actors who are normally most centrally involved are also affected. Bureaucrats who usually prefer to avoid uncertainty by moving incrementally when faced with threats to jobs, programmes and the autonomy of their organisations, become much more ready to take the risk of more far-reaching changes. Legislators, for similar reasons, are less impelled to posture and more likely to think strategically. With a zero sum game in the Council it becomes more difficult for Ministers to reach the usual package deals and more uncomfortable measures have to be contemplated. Pressure groups, faced with a threat to the existence of the policies they support, become more receptive to reform. Finally, and more generally, revenue exhaustion creates a political incentive to pay more attention to the efficiency of pricing, stronger programmes and export subsidies.

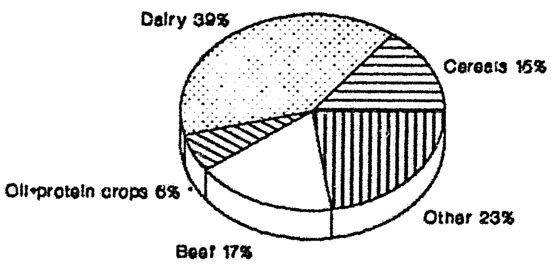
These features are well exemplified by the genesis of some of the changes mentioned earlier in the paper. Budgetary pressure has been a recurrent problem throughout the Eighties. For a time it has been possible to shelve the problem by creative accounting (such as transferring commitments from the short to the long term, or obtaining reimbursable advances, or adjusting the timing of financial years), and by grasping the temporary relief provided by blips in world markets arising from droughts or fortuitous appreciation of the dollar. Eventually however the crisis has to be faced. Finance and prime ministers become involved and a more radical change such as dairy quotas or maximum guarantee quotas for cereals arises. This has been especially the case when, as in 1988, assertive characters have been in key positions.

The problem was manifest by the end of the Seventies but several factors conspired to delay a solution. The Commission was timidly led by Gaston Thorn; 1981 saw both a recovery in dairy prices and a strengthening of the dollar; discussion was confused by British pressure for a rebate and the uncertain costs of Iberian accessions. Hence not till 1984 was the sea change of milk quotas introduced. This brought relief on the livestock side but did nothing to stop the ballooning costs of support for cereals and oilseeds. (See chart after P.22) Budgetary disciplines introduced then proved ineffective. Expenditure which should have been constrained to a growth of two per cent per annum over the four succeeding years instead rose by 78% per annum in response to falling world commodity prices and a radical weakening of the dollar. (The dollar fell from a peak level of 1.32 ECU in 1985 to .81 in April 1988.) By 1987 an accumulated liability of 17 billion ECU had arisen. Faced with a threat to the CAP as an institution a powerful combination of an assertive President, a resolute Agricultural Commissioner and an active Budget Commissioner overcame the normal inertia of the system to introduce along with threshold pricing adjustments the improved budgetary control earlier described.

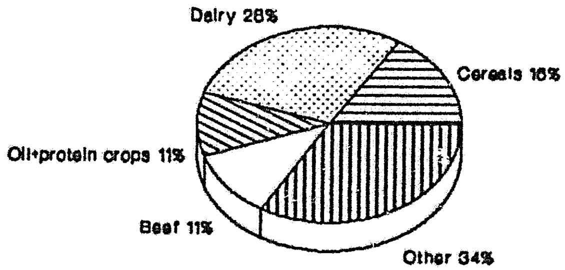
These new controls mean that finance ministers will become involved at an earlier stage as budgetary problems arise. This could of course mean that solutions are more likely to be found within existing régimes without radical change. Also one price of the 1988 reform was that the own resources of the Community were materially extended. So over the past three years, with world prices relatively firm, the budget has been underspent and some funds transferred forward. However this year, with prices on world markets tumbling, especially for cereals, the provisional budget has been fixed 13% higher and is unlikely to be underspent.

EC-Composition of Expenditure on Commodity Regimes

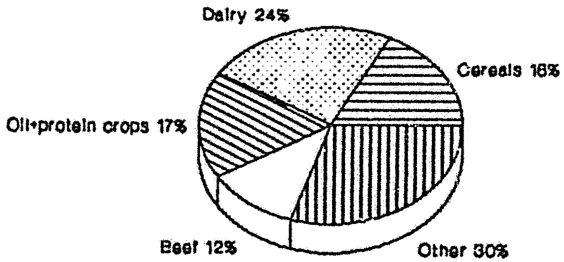
1974-76



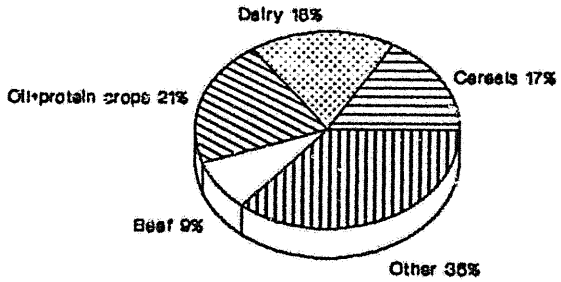
1981-83



1986-88



1989-91



In the longer term there are several reasons to expect budgetary problems to return. First there will be increasing pressure to spend more on Community programmes other than agriculture, especially from the social and regional fund. Greece, Spain and Portugal made a commitment to this a condition of their agreement to the 1988 package. There is also a more general understanding that this will be a corollary of the opening of markets under the Single European Market initiative. Furthermore there seems no reason to predict that either the downward march of world prices or the onward march of technology will be arrested. Finally, enlargements of the Community, recent and prospective, will on balance increase its surplus problems.

POSSIBLE RESPONSES

The discussion of possible responses to the pressures indentified will be couched in terms of what might happen rather than what ought to happen. What is called the economists' ideal solution, in essence decoupling, is discussed first not because it is most likely; rather will it serve as a landmark to which other less efficient but more politically feasible changes can be related. For example, a greater use of non-price instruments through more guidance as opposed to guarantee expenditure could improve economic efficiency in some respects. Hence structural policies are considered next. Within the realm of price policy both efficiency and equity could be enhanced by use of the ingenious approach of producer entitlement guarantees (PEGs). However dairy quotas and to a much less degree, land set-aside, provide better beacons for supply control as a response and one that might be favoured by finance ministers more concerned with expenditure control than economic growth. Finally to be considered is the approach of diversification. Diversion of crops to non-food uses, though understandably popular with agricultural interests, seems to be a non-starter on budgetary grounds. A more plausible approach, which would marry supply control with a response to green political pressures, would be to divert support from the production of food to production of environmental goods.

PRICE CUTS AND DIRECT INCOME SUPPORTS

To make support prices closer and more sensitive to world levels and to support incomes by direct transfer. That is the solution to the pressures outlined which would be favoured by most economists within the Community, and even more so outside it, and by not a few public servants outside agriculture ministries. Such a move would increase efficiency by releasing resources from agriculture that could be used to greater social return elsewhere, and reduce general unemployment by lifting what is in effect a tax on manufacturing exports. It would be more equitable because there would be less burden on low income consumers who spend much of their income on food, and less income transferred to already wealthy landowners. Income transfers would be better targeted to those in need rather than as a reward for surplus production. Reduced and more variable prices would encourage some return to mixed farming and check mechanisation and the use of agrochemicals, and thereby reduce the external costs of agriculture.

The merits of this solution from the perspective of a rational actor are so great and obvious that it would seem otiose to consider others. However, if one combines a frame of reasoning based more on the concepts of public choice with a consideration of the institutional features of the CAP outlined above, one is unlikely to conclude that it is probable. Previous analysis has suggested that the policy responses most likely to be adopted are those which

1. do not involve great costs of adjustment or markedly increase administrative complexity;

2. are not very far from the status quo (otherwise the bargaining costs would be impossibly high); and

3. safeguard the intense interests of those most strongly affected rather than the diffuse interests of the majority of people.

The final feature has two aspects. The first, that policies will continue to give priority to the interests of farmers in general in relation to taxpayers and consumers, is widely accepted and indeed implicit in this policy alternative. The second and more debatable aspect is that policies are unlikely to be adopted which switch benefits from larger landowning farmers to small farmers whose main input is their own labour. The reasoning here is that it is larger farmers with big fixed investments and who therefore cannot readily exit from the industry and who receive the largest rents from the existing policy, that have the strongest incentive to mobilise their political voice. Individual farmers are prepared to accept the responsibility of safeguarding and enhancing the benefits for all farmers because there is more solidarity of feeling amongst farmers than most producer groups. Large farmers in turn co-opt the support of smaller farmers by providing benefits such as insurance and information on farm programmes. This model does not apply peculiarly to the EC but its institutions, especially the combination of international finance with international and compartmentalised decision, ensure that the political voice of larger farmers is especially well headed.

These criteria militate strongly against direct income support. Budgetary pressures, possibly reinforced by pressure from nonagricultural interests to limit protection for agriculture to gain trade advantages in other sectors, are likely to lead to some further reductions in price support but not the comprehensive and abrupt changes implied by this policy change. Direct income supports however per se face serious political and administrative obstacles. Larger, more politically influential farmers recognise that however the transfers were initially labelled and distributed, they would swiftly be seen as welfare payments and therefore likely to be distributed according to need. This is in marked contrast to price supports, which in the main and in principle are founded on equal treatment of all farmers, and therefore go mostly to large producers. There is also a more general, if perhaps overstated aversion to the welfare stigma and a reluctance to see transfers made more transparent.

Direct income supports conflict even more strongly with the first two criteria. They involve a rejection of the fundamental feature of the policy that incomes are supported by supporting prices and politically at least would mean a marked redistribution of benefits between countries. They also raise severe administrative problems. First the statistical base is weak. In most countries of the Community farmers pay tax on a notional income based on the inputs they command. Hence any income compensation would have to be either unacceptably crude or very expensive to administer. There would also be motley problems of how to allow for income from non-farming activities and off-farm investments. If these were to be fully taken into account the point of a separate agricultural income transfer would be called into question. It would also have to be decided how entitlements should vary according to differences in incomes between countries. In sum it is difficult to envisage a scheme that would be both administratively feasible and politically acceptable.

Conceivably limited schemes of income support might be introduced for specific purpose. Thus recent Commission proposals have suggested that they could be used to help debt servicing during reconstruction or smoothing a transition to a non-agricultural activity. The line of course between such supports and investment aids is a fine one and touches on a more general difficulty of preventing income aids being used to fund additional investment. National governments are likely also to use income aids for such purposes as flood relief. However a comprehensive Community financed scheme of decoupling support seems a non-starter.

STRUCTURAL POLICIES

Direct income payments with restrictions on their use overlap another broad area of possible responses under the head of structural policies. For our purposes these may be defined as public expenditure for the benefit of agriculture and surrounding rural areas by means other than commodity price support, but intended to bring about specific reallocations of resources.

It is suggested that when account is taken of the institutional and political constraints this route will be preferred to direct income support as an accompaniment to restraint of price support, for several reasons. First it will be seen as preferable in budget terms. Whereas income supports would be seen as alarmingly open-ended, structural policies can be directed to limited purposes and in part hold out the promise of reducing the future need to support agriculture by making it more internationally competitive. Moreover insofar as support prices are set to give marginal farms a living, an increase in their productivity allows prices to be cut across the board. These were very much the intentions of the Mansholt plan of the early 70s. They were not however fulfilled, mainly because the security fears aroused by the subsequent commodity boom meant support prices were not cut as productivity rose, thus creating a surplus problem. Furthermore much of the support for restructuring was captured by farms who were well established rather than marginal.

Structural policies also respond better to environmental pressure, basically because they affect resource allocation. Grants can be made conditional on particular environmentally friendly practices being followed. This also makes them more politically acceptable to the general public. While high food prices are paid fairly cheerfully as the perceived cost of security, there is a growing feeling that in return for this transfer to farmers the public should have a larger say in countryside management. Pressure groups and international politics also favour structural policies over income supports. Though often billed by the Commission as policies to help the 80 per cent of farms which produce only 20 per cent of production, large politically active farmers are well aware that at least some of the benefits will be captured by them. Internationally the increasingly influential Southern countries of the Community favour structural policies because they can more readily be directed to help the very small farmers and landless labourers in which their countries abound. Indeed as part of the 1988 reform package the Southern countries, supported by Ireland, secured a commitment that structural spending should increase by two thirds by 1992 above a 1987 base of 7.8 billion ECU.

A final argument for expecting some expansion of structural policies is that this would not involve a leap away from the status quo. On the contrary so-called guidance expenditures are an established part of the CAP. Indeed the Treaty of Rome envisaged that the objective of a fair standard of living for farmers would be obtained by structural changes and that guidance expenditure should broadly match guarantee expenditure. This was very much the expectation of Mansholt, the first Agricultural Commissioner, but one never realised because product guarantees have virtually exhausted the FEOGA budget, and national governments have preferred to retain structural policies as national instruments.

One difficulty in discussing structural policies is that they are a somewhat amorphous group. They could however be broadly categorised according to intention into those designed

a) to make factor markets work better;
b) to reduce regional inequalities; and
c) to promote rural rather than agricultural development.

Economists imbued with the Schultzian perception of the farm problem see structural policy very much as improving resource mobility. This too was the intention of the Mansholt plan. It was envisaged that the work force in agriculture of the EC-6 would be reduced by half by 5 million over the decade and that 5 million hectares of land would be retired. This would be encouraged by retirement and retraining grants and land consolidation. The scheme was however implemented in a very emasculated form and with the main emphasis on capital grants. Structural intervention of these types has since become if anything even more unfashionable, particularly in relation to labour markets. Policies for moving labour out of agriculture have become less attractive to politicians as structural unemployment has replaced overfull employment in the non-farm economy. Demography, greater mobility and the dispersion of industry have combined to make overpopulation per se less clearly a long term problem in agriculture. Thus about half the farmers in the EC are over 55 and more than half of these have no successor. In some countries the imminent decline is even greater. (In France for example the mean age of farmers is well over 50 and 30 per cent are over 60.) Around a third of farmers have some off-farm source of income and one which usually yields more than farming. In Germany more than 40% of farmers are classified as spare time, with a further 10% classed as part-time.

The emphasis of capital grants has meanwhile changed from correction of capital rationing toward environmental improvement. Following the rationalisation of structural policy in 1985 the Community now provides support (usually at 25%) for national schemes for management compensations in environmentally sensitive areas, planting of woodland, extensification and diversion of land to new specified uses.

A pre-pension scheme for retirement of farmers was introduced in 1988 but with only part funding and at a puny level. It was planned to spend 294 million ECU over a four year period whereas guarantee spending in that year alone was 26.4 billion ECU. It is likely that policies for removing labour from agriculture will remain similarly tokenist. Future expansion is more likely to be in regional programmes which will on balance draw resources into farming.

Programmes to reduce variations in prosperity between regions will build on the 1975 initiative which introduced special aids for less favoured areas. These are defined as either mountainous, areas in danger of depopulation or 'small areas affected by specific handicaps'. In area about half the farmland of the Community is so classified, though of course much of this is rough grazing land of very low productivity. The aids take the form mainly of livestock headage payments and improvement grants. There are also regional infrastructure projects such as for irrigation in Greece and drainage in Ireland. Support for local food processing and marketing plant has been especially prominent, absorbing over a third of total expenditure. Such projects are designed not only to improve the position of farmers in particular rural areas but also to increase general employment in them. This broader approach of rural rather than simply agricultural development was explicitly reaffirmed in connection with both the 1985 rationalisation and the 1988 budgetary agreement.

It seems likely that structural policies will increasingly take the form of such broader schemes as the development of rural roads or electricity systems and also integrated schemes for regional development such as the Integrated Mediterranean Programmes, which are partly funded from regional and social funds. This will be so because the impetus will not be simply to protect the weakest regions from the effects of reduced price support provoked by budgetary pressures but also to compensate regions more broadly affected by the freeing of trade.

PRODUCER ENTITLEMENT GUARANTIES

Price reduction, income support less related to production and improvement of factor markets are likely to be elements in the future development of the CAP. However political and administrative factors will cause both the extent and form of these to fall far short of what most economists would advocate. An approach which seeks to recognise these factors while achieving many of the gains in efficiency and international acceptability of more purist economists' solutions is that of production entitlement guarantees.

The key principle of such schemes is that producers of a particular commodity are entitled to a deficiency payment on a given amount of production which is related to previous production but subject to a common and relatively low maximum. For example producers of wheat might be entitled to receive as a direct payment from the Community the difference between a pre-fixed guaranteed price and a freely determined average market price on an output of 400 tonnes. Production above the entitlement would be marketable at the trade parity price. The total entitlement would be set at a level somewhat less than what production would be under a totally free market. (This might be obtained by the Community initially introducing a higher total entitlement and then bringing back to proportion of them. Similarly import levies, export subsidies and intervention purchases might be phased out gradually.) The eligibility certicates would ideally be issued to farmers but could be issued to farms. They could be transferable, at least within countries. This would avoid the support of production that would not occur under a free market and would allow relocation of production as comparative advantage changed. New producers could either buy entitlements or produce entirely at world prices.

The economic merits of such schemes are clear. Benefits would be directed to farmers rather than determined by production. Deadweight losses in both producer and consumption would be avoided. The distortion to trade would be minimal.

For administrators producer entitlement guarantees have the advantage that they would achieve all the objectives of the CAP both stated and implicit. Thus the incomes of poorer lower producing farmers would be boosted but without raising the incomes and wealth of those already well off by most standards. A minimal level of supply would be guarantied irrespective of external disruption Such schemes would also give fair prices to consumers and not inhibit the improvement of productivity. Furthermore they cater to the desire of member governments to retain more people in agriculture and more family farms than would result from market forces.

The budgetary influences moreover are less fearsome than the mention of deficiency payments might suggest. By setting entitlement limits well below levels of production on larger farms much of their production would no longer be supported. This saving could offset the extra excequer costs of shifting the burden of support away from consumers. Thus it has been calculated that under 1990 conditions PEG scheme for cereals with a 'peg' of 400 tonnes per farmer would have allowed 85 per cent of farmers to have been given the same level of support with no increase in overall exchequer spending. PEG schemes would also make the commitment of FEOGA (the EC agricultural treasury) less open–ended. Whilst there would still be uncertainty about the level of the unit deficiency payment the quantity to be supported would be fixed and there would be a mechanism for further limitation. In the particular case of CAP for cereals there would be a further indirect saving. If livestock producers could buy cereals at world prices they would be less in need of support. Finally in terms of control, the cashing of certificates would require less supervision and entail less fraud then schemes which require control of the actual marketing of products.

This feature is a political as well as an administrative advantage insofar as producers would be left greater freedom of action. PEG schemes would also attract some support from interests other than producers. Consumers would be advantaged by lower prices and might also feel that the continued support of some production might safeguard scarcity of supply well enough. Taxpayers would not be worse off and of course would profit as consumers. Overseas interests would welcome the recoupling of intra–EC to world prices. Those concerned about the environmental effects fo agriculture could welcome PEG schemes for several reasons. Being less favourable to larger producers, they would check field consolidation and mechanisation. Lower production would mean less use of chemical fertilizer and pesticides. Also they would lower the price of marginal agricultural land and thus allow more to be used for environmental purposes. The critical political reaction however, is likely to be that of producers. Producers in general (and agricultural supply industries) are likely to prefer PEGs not only to supply controls but also to direct income payments. Both the stigma and the political hazard of a welfare connotation would be avoided. PEG schemes also give a measure of income stability. The recoupling involved would also make world prices more stable. EC users and stockholding would take part in adjustments to external stocks and the effects of stocks within the EC would no longer be wholly exported abroad.

Among producers, the main political opposition to PEG's would come from larger farmers. Among countries it would come mainly from those with few farmers who are small by EC standards, notably the UK, Netherlands and Denmark. It is large producers who are active in agricultural politics and who in the EC as elsewhere have ensured that whatever their announced rationale, farm programmes have mainly benefited them. The opposing countries form close to a blocking minority. These are formidable obstacles to the introduction of PEG's despite their undoubted general merits. They nevertheless more likely to be adopted than direct income payments although if so probably in a very attenuated form. EC institutions favour incremental change whereas the PEG principle in its pure form is a radical change.

Proponents of PEG's argue that they are an evolution from present policies. This is true insofar as some link is retained between support and production. It is manifestly untrue insofar as the main burden of support is taken from consumers and there is discrimination in support between producers according to size. These are both fundamentally new principles. The sugar regime provides a precedent inasmuch as production beyond domestic use and a fixed level of exports receives only the world price. However at the producer level the effect is often masked by price pooling. The regime differs from PEG schemes in more basic respects. Support comes from consumers rather than taxpayers and production is encouraged well beyond that of a free market. Quotas for sugar, and more especially milk, are seen rather as precedents for direct supply control. In producer and government circles such control whether of output as such or of inputs has received more attention than PEG's.

SUPPLY CONTROL

Administrators are attracted to marketing quotas because they work quickly and predictably. However many recognize, along with economists, that productive inefficiency is likely to be a resultant cost of this convenience. This is especially so if quotas are not negotiable and political pressures will work in this direction. In any event the rents created by quotas will be captured by the first holders through capitalisation into the value of the associated land if not the quotas themselves. For the commodities in which the EC is in surplus and for which there are not already established the market share is too small to create a case on grounds of terms of trade for supply restriction. If might be argued that such restrictions will reduce tension in agricultural trade but any form of market sharing is unlikely now under GATT and would be ineffective in the long run. On top of and perhaps even more so than these economic objectives administrators are aware of the extreme difficulties of controlling marketing off farms of products which, unlike milk and sugar beet, are not inescapably funnelled through a few processing points. Control is especially difficult for cereals which can be not only sold on to other farmers but also marketed indirectly after conversion to livestock or their products.

Our discussion of marketing quotas could well end there, were it not that they have some political support, albeit sectoral and occasional. Producer organisations, though in general opposed to quotas as constraints on both managerial freedom and revenue, may on occasion press for them when faced with the alternative of sharp price cuts. This attitude has been encouraged by the experience of milk quotas, which are held to have greatly reduced certainly in dairy farming. In addition some non farm interests favour quotas as means of obtaining certain regional, or environmental objectives. Such a dirigiste approach however is unlikely to be adopted in the present general political climate. More straightforward quotas allocated according to past production are improbable not only because of the general economic and administrative objections outlined above but also through more particular circumstances. Firstly, any further extension of quotas to other commodities is likely to be resisted by some influential member countries. The UK and Netherlands are likely to oppose them in principle as restraints on market forces while France would be inclined to reject them as limits on its exporting ambitions. Secondly, it is unlikely that any scheme quotas which might be adopted would allow international transfer. Yet if it did not do so it would seem inconsistent certainly with the spirit, and conceivably the letter also of the single European Act.

Land set aside

The economic objections to marketing quotas are fairly well recognised. More to the point any further extension would be both administratively impracticable and politically unacceptable. The limitation of land inputs though even more objectionable on economic grounds have more political support and are administratively easier to operate. Quotas on other inputs notably nitrogen have been mooted by both producer and environmental organisations but thus far have been very low on the political agenda.

Farmer organisations tend to favour measures which are feasible toward the maintenance of land values. It can measurably be argued that the main effect of the CAP has been to buoy values of land and that the main impetus for its retention is to prevent them falling. Though there is some public objection to paying farmers for doing nothing with land, this is not politically well articulated or focussed. Of more political significance is the support of some environmental groups who hope that land set aside may be diverted into environmentally friendly areas. Administrators like the relative simplicity of checking compliance with land restriction and questions of transferability do not usually arise. Enforcing compliance nevertheless may not be absolutely simple where, as is common in continental Europe, as a result of the Napoleonic code, farms are fragmented.

About totally voluntary schemes, however, such as that already in place on a small scale, the more serious concern of administrators is on the budgetary effects. Limitations of production and thereby savings on export subsidies, may be expensive to obtain for several reasons. First participating farmers will naturally retire lower yielding fields and those who participate are likely to be those with some particularly unproductive marginal land. Secondly with less land to cultivate farmers may achieve, through more timely operations, better yields on their unretired land. (However since prices received by farmers are not affected by set aside, there is, contary to a common assertion, no reason to expect more intensive use of inputs). Finally on land brought back into production after fallowing yields are likely to be temporarily boosted.

Where, as in the USA, set aside is made a condition of receiving support payments, the budgetary arithmetic is likely to be more favourable. This is an element in the very latest commision proposal for reform prepared only within the last month. To receive per hectare payments, which compensate for cuts in support prices of around 40%, producers of cereals, oilseeds and protein crops, to a degree dependent on their size, would have to set aside up to 35% of their land under these crops. It is to be remembered however that it is the Council of Ministers which decides. The chances of such a proposal being approved by the Council of Agricultural Ministers as such are slim indeed. France will oppose any measure which limits exploitation of its 'green oil' while the UK, Netherlands and Denmark will oppose one which diverts support toward small farmers. Its only chance of success is that non-agricultural ministers may press their colleagues to comply to unlock the gains from liberalization under GATT of such areas as financial services and intellectual property. This and other pressures outlined above will bring reforms of broadly this nature but probably not immediately and with a greater slant towards environmental benefits.

DIVERSIFICATION FROM FOOD PRODUCTION

Radical reform of the CAP will require the involvement of political interests which are not narrowly agricultural. These are unlikely to be satisfied by the simple sterilisation of land. There will continue to be an interest in the production of physical goods other than food such as ethanol. Such moves, for example the use of land set aside for non food crops, are popular with both farmers and their suppliers but with present technology and fuel prices would be too expensive to interest the commission. Of more immediate importance is likely to be diversification into non-food services. This would reinforce the diversification already brought about by market forces. Responding to the higher income elasticities of demand farmers where suitably located have for example converted land to use for houses or golf and buildings to holiday or even permanent residences with complementary diversion of their labour and management. The clearest role for government policy in this area is to encourage the provision of these goods with a strong public element such as scenic amenity, habitat for wildlife, and water improvement. In Europe, unlike more recently settled areas, this generally means inducing particular types of farming rather than withdrawal from farming. A further advantage of extensification over set aside is that rural population is maintained.

The Community has already made moves in this direction by both pilot schemes and policy statements. In 1985 member countries were permitted by directive to start schemes for environmental improvement and from, 1987 financial aid has been provided. The Single Europe Act added environmental protection to the objectives of the community and the 1988 policy statement Monde Rurale emphasised rural rather than more narrowly agricultural targets. The most likely model for further development is that of compensation by management agreement for such practices as grazing rather than draining marshes, deferring the time of mowing grass, or limiting the use of nitrogen and irrigation or levels of stocking.

Producers have become increasingly receptive to the transfer of subsidy from the production of food to that of environmental goods. The more thoughtful however recognise that to be acceptable on exchequer grounds a reduction in the level of protection must accompany this switch of burden from consumer to taxpayer. They further recognise that the incidence of such subsidies between regions and farm types could be very different from that of existing support. Such programmes require more careful and specific planning than blanket measures such as indiscrimate set aside or protective compensation. Nevertheless their appeal to a broader political constituency make them a more likely path of development in the longer term.

CONCLUSIONS

1 Because public decisions on agricultural matters in the EC are made internationally rather than supranationally and in a compartmentalized way and because consumers, misguidedly, believe that agricultural protection is the necessary price of food security, change in the CAP is likely to be incremental and gradual rather than radical or sudden.

2 The policy will be driven by budgetary and environmental rather than international pressures.

3 Budgetary pressures will on balance be increased by other Community initiatives on enlargement, the Single Market , and monetary integration.

4 The primary response to these pressures will be price reduction rather than the extension of marketing quotas or the set-aside of land.

5 Complementary programmes, though inevitably a mish–mash, will incline more toward rural structural grants and compensation for environmental improvement rather than direct income supports.

6 The benefits of the CAP may be redirected toward smaller farmers but political pressures, both internal and international, will prevent a radical switch to producer entitlement guarantees.

7 The most liked alternative scenario that would overturn the above conclusions though one not developed in an already over long paper, is that non–agricultural interests force a more radical and rapid reform of the CAP to obtain the benefits of liberalization by agreement of international trade in sectors other than agriculture.

BIBLIOGRAPHY

ABARE, The 1988 EC Budget and Production Stabilisers: A Means of Containing the Common Agricultural Policy? Discussion Paper 89.3. Australian Bureau of Agricultural and Resource Economics, Canberra, 1989.

Baldock, D. The Common Agricultural Policy and the Environment: from the CAP Structures Policy series, CAP Discussion Paper Number 2, World Wildlife Fund International, Switzerland, 1989.

Brown, C. Price Policies of the CAP: Retrospect and Prospect. Statens Jordbrugsokonomiske Institute, Rapport nr. 41, Copenhagen, 1988.

Harvey, D.R. Decoupling and the European Common Agricultural Policy, Proceedings of the International Agricultural Trade Research Consortium Symposium, Conrell University, March, 1988.

IEA Europe's Constitution Future, IEA Readings. Contributions by J.M. Buchanan, K.O. Pohl, V.C. Price and F. Vibert; introduced by G. Magther. Institute of Economic Affairs, London, 1990.

Moyer H.W. and T.E. Josling Agricultural Policy Refore: Politics and Process in the EC and USA. Harvester Wheatsheaf, 1990.

Petit, M. et al Agricultural Policy Formation in the European Community: The Birth of Milk Quotas and EEC Refore. Elsevier 1987.

Phillips, P.W.B. Wheat, Europe and the GATT: A Political Economy Analysis. Pinter, 1990.

Snyder, F. New Directions in European Community Law. Weindenfeld and Nicolson, London, 1990.

Tracy, M.A. Government and Agriculture in Western Europe: Challenge and Response, 1880–1988. Harvester Wheatsheaf, 1989.