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The failures of CAP

The CAP must be modified …the present system is a manifest absurdity …it is time to grasp the nettle of reform

Tony Blair, the Prime Minister, speech in The Hague, 20th January, 1998

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Objectives of the Common Agricultural Policy

Original objectives in Rome Treaty 1957, similar to those of the UK and other developed countries:

- To increase agricultural productivity
- To ensure a fair standard of living for the agricultural community
- To stabilise markets
- To assure availability of supplies
- To ensure reasonable prices to consumers

Additional objectives in the 1990s:

- To maintain the maximum number of farmers on the land and preserve rural communities
- To preserve the countryside and the environment
- To avoid the build-up of food mountains
- To maintain good international trading relations
- To fulfil the 1993 GATT agreement
- To "decouple" farm income support from production

Economic Consequences

Increased agricultural protection. To get political agreement on common prices meant pitching them towards the highest in the Six founding countries, ie German prices way above international free-market levels. Ever since, CAP has been a high price policy, with most EU countries enjoying higher tax support than would ever have been voted without CAP.

Level of protection. The Nominal Tariff Equivalent (NTE) for the EU countries' agricultural products as a whole rose from 16% in 1956 (prior to CAP) to 108% in 1986, when world prices were very low, dropping to 96% in 1990. In 1997 the EU NTE was still 72%, compared with 23% for the USA and 3% for New Zealand. The OECD average was 52%.

Budgetary problems. For most of its life CAP spending, mainly on support-buying and export subsidies, absorbed two-thirds or more of the EU's budget. It has recently accounted for just under one-half, due to increases in such items as Regional and Social Funds. CAP expenditure has risen inexorably from £1.3bn per annum in 1968, to £20bn in 1990 and currently some £30bn. The Berlin Summit reform (25th March 1999) agreed to still higher spending over the period 2000-2006.

Burden on consumers and taxpayers. For

Principles and Mechanisms

The CAP has mainly employed a single policy instrument – regulated prices (with compensation per acre if they are reduced) - to meet a host of objectives. This contravenes the maxim for successful public policy that at least as many instruments as objectives be used. Moreover, it has been applied to 15 countries with agricultures ranging from the frozen wastes of Sweden and Finland to the Mediterranean climes of Italy, Greece, Spain and Portugal, producing a huge diversity of temperate to sub-tropical products, on holdings varying from several thousand acres in East Anglia to the minute smallholdings of Bavaria. Soon it may have to apply to the enormous and highly productive former co-operative and state farms of Hungary and Poland.

The main principles and mechanisms of CAP emerged in the 1960s and continue to be:

- A quasi-free internal agricultural market with no internal tariffs, quotas (except for milk) or other protective devices;
- Common farm prices: fixed annually by the Council of Ministers and maintained by intervention (support-buying) and export subsidies;
- Protection of community farmers by variable import levies (and now tariffs) to prevent the target price for Community farmers from being undercut;
- Central top-down funding from the EU Budget administered from Brussels by the Commission.

most of its life, CAP farm prices have been supported at roughly twice world market levels. Families in the EU suffer the double burden of higher taxes and higher food prices. Typically, the cost has been of the order of £250 per person per year for every man, woman and child, split roughly equally between taxes and food prices.

International discord. By the early 1980s the EU was the world's largest subsidised exporter of butter and beef and the second largest (after the USA) of cereals. These trading practices depressed and destabilised world market prices of farm products, damaging traditional commercial exporters in the USA, Australia, New Zealand, Canada, and numerous Third World countries. Consequently, the CAP became a principal issue in the Uruguay round of GATT which dragged on from 1986 to 1993, mainly through EU intransigence, and which led to limited reductions in agricultural support.

Farmers' incomes falling. The CAP has failed to give reasonable prices to consumers, to preserve the environment, to maintain rural communities and, above all, to raise farmers' incomes. In Britain, 1997 total farm income plunged by 45% to the level (in real terms) of 1989, which itself was less than half that of 1970. In 1998 it fell a further 29%. Despite this, the cost of UK farm support has risen from £1bn in 1980 to £1.9bn in 1990 and £4.3bn in 1996.

Reasons for Failure

The CAP is one of the prime and persistent examples of costly, yet totally unsuccessful, attempts by government to circumvent the

However, external pressures - EU enlargement and the next WTO negotiations2, for example - may yet force reform, even on France.

laws of supply and demand.

Demand for food is virtually static, while supply tends to grow more rapidly, spurred by high prices and the adoption of new technology.

Downward pressure on market prices increases the cost of supporting them.

The CAP is very inefficient at transferring income to farmers. The annual cost to consumers and taxpayers has typically been more than double the gain in gross income to farmers, with about 60% being spent on payments to administrators, storage agencies, financing stocks, and export subsidies.

Of the 40% which adds to farmers' gross incomes only a tiny amount ends up as net income. About 50% of the extra revenue from higher prices is spent on additional inputs to increase output, some 45% on higher rents (or inflated land values), and only around 5% in net income to the farmer.

All these payments have been subject to prodigious and largely untackled fraud, amounting to at least 10% of the CAP budget1.

CAP reform from within unlikely

In the last thirty years, changes to CAP have consisted mainly of tinkering with the price support mechanism, with ever-increasing regulation. The most recent attempt at even modest reform, the Commission's Agenda 2000 package, covering the period 2000-2006, was scuppered by the French. The CAP budget even without EU enlargement will continue to rise albeit with some shift from price support to compensation payments.

Consequently, the CAP will continue to pour money into the pockets of the wealthiest farmers; to penalise the poorest consumers, who spend the biggest proportion of their incomes on food; vastly to raise the level of farm support in countries like Britain,

The Solution

New Zealand rejected subsidised, government-administered agriculture in 1986 and adopted a free-market system. It took about seven years for the reforms to work through to product, factor and labour markets. The success of the experiment suggests a way out of the CAP impasse for the UK: repatriation.

A free-market agriculture, preferably including an EU-wide free internal market for farm products with no external protection, would be perfectly feasible for British farmers. It would return to British consumers the freedom to purchase their food from the most efficient sources all over the globe. But it could not be introduced overnight, since the present level of support under the CAP is about twice as high as in pre-reform New Zealand. The shocks to factor and land markets and the rural economy would be too severe. After repatriation, there would have to be direct income support for farmers in disadvantaged areas (not linked to output), special pension schemes for older farmers, retraining grants for younger farmers, and transitional payments to ease the pain of change over, say, five years.

The New Zealand experience suggests that the disruption and hardship of transition would not be as severe as British farmers fear. At lower land costs and using inputs less intensively, the bigger farms would be internationally competitive. The concentration of production on a small number of large holdings would continue. The proportion (about half) of farmers who are part-time, (mostly hobby farmers), would increase more quickly. Diversification into speciality products, tourism, leisure and sporting enterprises, into processing and adding value to farm products, and other activities such as rural crafts and timber products, would accelerate. Families whose main activity is farming could expect to earn more than the present 40% they now derive

Holland, Denmark and Ireland, which would now have little or no support if they were free to pursue their own farm polices; to cause friction and dispute with our trading partners in the USA, Canada, Australia and New Zealand; and yet completely to fail in the basic objective of raising farmers' incomes overall.

from other sources.

Such a reform would attract wide support in the UK. As the House of Lords Select Committee on the European Communities observed in its May 1999 report A Reformed CAP? The Outcome of Agenda 2000: "This Committee has long urged that European agriculture should become more market-orientated. … production-support regimes … have ceased to perform any useful purpose".

Source:

1 - Since most EU Budget fraud arises in CAP, its reform would mean lower taxation EU-wide and remove the pretext for new costly anti-fraud bureaucracies such as Corpus Juris.

2 - "The CAP is responsible for 85% of the world's agricultural export subsidies, which may well qualify as the largest distortion of any sort of trade", Charlene Barshefsky, the US trade representative. Speaking before the House agricultural committee, Ms Barshefsky said the focus of the next round of multilateral trade negotiations would be reform of the CAP and its subsidies. Quote in *Financial Times*, 24th June 1999.