1-1-1990

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The agricultural implications of Europe 1992

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Most farmers know only too well that the policies of national and international governments affect the prices they receive for their produce. The Europe 1992 policy is a new policy with potential to benefit Australian agriculture.

The origins of the Europe 1992 policy

The uninspiring nature of economic trends for most member countries of the EC in the late 1970s and early 1980s gave rise to the term Eurosclerosis.

The unemployment rate in the EC had risen from 2.9 per cent in 1975 to 10.6 per cent in 1985. Total employment fell by 1 million in the EC from 1975 to 1985 while strong employment growth was recorded in other major OECD countries. In the USA, for example, total employment grew by 21 million over the same period.

Historically low birth rates in the EC bode ill for its economic and demographic future (Kelch, 1989) and rates of economic growth were superior in Asian countries.

The economic stagnation and poor prospects for member countries of the EC eventually were translated into political pressures for reform. These pressures arose from various sources and levels in the EC.

Many politicians in the governments of the EC member nations were seeking policy options to improve the economic performance of their national economies. Some governments (for example, Thatcher's Conservatives in Britain)
were dissatisfied with the economic benefits they received from membership of the EC relative to its costs.

Also, many EC politicians and bureaucrats were sensitive to criticism of the economic performance of the EC, and saw the tendency of member countries to renationalize EC policies (especially in agriculture) as contributing to the economic malaise of the EC.

Consumer groups and many taxpayers expressed growing dissatisfaction with the economic benefits of EC policies relative to their costs, particularly regarding the Common Agricultural Policy (CAP). International pressures were mounting against the protectionist nature of many EC trade policies, again especially regarding the CAP.

Many large corporations trading in Europe saw great financial advantage in the economic revitalization of the EC.

In response to these pressures the EC Commission in 1985 released a blueprint for a barrier-free EC market. In 1985 this blueprint became an EC Commission White Paper comprising 279 directives. However, it was not until February 1987 that there was final agreement among EC members committing them legally and financially to complete the internal market by the end of 1992.

The 1985 White Paper, entitled “Completing the Internal Market”, outlined a policy to remove obstacles to a truly integrated EC market by the end of 1992.

Barriers to the movement of goods, services, capital and people within the EC were to be dismantled. The economic benefits associated with removal of these barriers were predicted to be large. Industries could relocate to areas of comparative advantage. Easier market access would encourage firms to adopt technologies based on economies of scale. Removing impediments to capital and labour mobility would encourage their more efficient use. Efficiency gains would result in lower costs of production and lower prices to consumers.

Cecchini (1988) estimates that forming the single market would result in the EC achieving an additional average GDP growth of 4.5 per cent ($300 billion), a 6 per cent decline in consumer prices and creation of an additional 1.8 million jobs.

Favourable responses to the 1992 policy by consumer groups, taxpayers and corporate firms has made it easier for EC member countries to adopt the 1992 policy. In recent years the potential benefits to businesses of the formation of a single market has spawned a flurry of corporate mergers and takeovers in Europe and given further impetus to implementation of the 1992 policy.

1992 policy and EC agriculture

In the 1985 White Paper on completing the internal market, 100 of the total 279 directives involved agriculture and the food industry. The directives outlined the abolition of major impediments to free trade of agricultural and food products within the EC.

Even though the 1985 White Paper with all its directives clearly would affect EC agriculture, initially the 1992 policy drew a phlegmatic response from European agriculture and food industries.

Many farmer organisations thought that the Common Agricultural Policy (CAP) introduced in the 1960s meant there was already an integrated market in agriculture, so therefore agriculture could remain largely untouched by implementation of the 1992 policy. However, what is becoming increasingly clear to these organisations is that the deregulation principles of the 1992 policy threaten the type and level of support that farmers extract from their national governments and from the CAP.
National agricultural aid

National aids to agriculture, in the form of rebates, tax incentives and other subsidies, are a significant form of assistance to agriculture. From 1981 to 1986 national aids represented 31 to 42 per cent of total aid to EC agriculture.

There are also a host of border and import regulations that protect national food industries. More than 200 non-tariff barriers exist to protect national food industries against competition from other EC countries. However, as part of the implementation of the 1992 policy, these non-tariff barriers are being removed, by choice of national governments, by force of law in the EC Court of Justice and through financial incentives.

The financial incentives for removing national agricultural protection come from funds for structural adjustment, set-aside programmes and direct payments to disadvantaged farmers.

The 1987 Single European Act and 1988 Brussels agreements provide mechanisms and funds for the re-structuring of national agriculture such that farmer incomes rather than their price levels can be protected. This opportunity to decouple agricultural support (that is, not tie supports to price levels) is a major policy change for the EC.

The Common Agricultural Policy

Besides national protection, EC farmers also have relied on protection of the Common Agricultural Policy (CAP). Under the tariff and price support protection of the CAP, agricultural production in the EC has increased to record levels such that France, the United Kingdom, West Germany and the Netherlands now each earn more agricultural export income than Australia. Even the small EC nations, Belgium and Luxembourg, together generate the same agricultural export income as Australia. However, the protection of EC agriculture is costly to EC consumers and other export competitors such as Australia.

In the early 1980s the effectiveness of the CAP came under scrutiny. Originally the CAP was to help small ‘traditional’ farmers, yet in reality mainly large farms were beneficiaries (Agra Europe, 1989d). By maintaining high levels of output large farms captured most of the benefits associated with price support. The failure of the CAP to protect small farmers has heightened pressures for its reform.

The cost to taxpayers of maintaining the CAP began to concern governments and consumer groups. The International Organization of Consumers Unions (Agra Europe, 1989c) estimates that an average family of four in the...
EC pays about $1,200 each year in direct taxes to subsidize EC agriculture.

The continued subsidization of EC agricultural exports also drew criticism from the Cairns Group of countries and other members of the General Agreement on Trade and Tariffs (GATT).

Concerns about the CAP, when combined with political and economic pressures on other EC sectors, have hastened the adoption of many ingredients of the 1992 policy that directly relate to food and agriculture. Of the 100 directives affecting agriculture and food industries in the 1985 White Paper, only 18 remain to be adopted.

**Main effects of the 1992 policy on EC agriculture**

So far, implementation of the 1992 policy has succeeded in reducing many barriers to internal EC agricultural trade. In anticipation of fewer barriers to internal trade the EC has experienced a flurry of merger and takeover activity in the food processing industry. This activity will benefit EC consumers and encourage relocation of agricultural production in areas with comparative advantage.

The restructuring of the transport and capital markets will also significantly affect the food and agriculture industries. Transportation costs will be less when border controls are minimized and cabotage is eliminated. (Cabotage is the practice in some countries of requiring non-national trucks to return empty.) Farmers will benefit from reductions in the cost of transporting both their produce and farm inputs.

The free movement of farm labour could also affect production patterns and farm profitability. Hired labour is important in EC agriculture. In 1985, non-family members provided 16 per cent of farm labour in the EC.

The 1992 policy and Australian agriculture

Australian agricultural exporters will enjoy significant benefits should the 1992 policy generate genuine reform of the Common Agricultural Policy (CAP) leading to reductions in EC food surpluses. Fewer EC stocks will overhang international markets to depress prices. Competition from EC subsidized agricultural exports will be less. Higher levels of employment and disposable income in the EC (BAE & CIE, 1987) should result in increased demand for wool, meat and horticultural products.

The 1992 policy seeks to establish a single market among EC members. How open that market is to forces of external competition is not mentioned in 1992 policy documents. However, the EC policy stance at the 1989 Uruguay Round of GATT (General Agreement on Trade and Tariffs) shows that the EC favours a very gradual reduction in its tariffs. Nonetheless, EC members are being forced by their allegiance to GATT and by some EC pressure groups to reduce tariffs and partly reform the Common Agricultural Policy (CAP).

There are features of the 1992 policy that will exert continual pressure for reform of the Common Agricultural Policy (CAP). Given the spate of takeovers and mergers in the food processing sector, this sector increasingly will look beyond national and EC borders for least-cost sources of food inputs and therefore should be less aligned with particular national or EC farm lobbies.

The 1992 policy provides funds to farmers for adjustment and compensation purposes. The net effect of these funds should be to facilitate movement of resources out of agriculture and for agricultural surpluses to be smaller.

The 1992 policy allows for farmers to be compensated for production foregone because of environmental concerns. As environmental and animal welfare issues increasingly attract voter interest, EC agriculture will increasingly face pressures to be more extensive (Agra Europe, 1989b) and to depend less on chemicals whose use may cause environmental damage or raise animal welfare concerns.

The 1992 policy allows direct income payments to farmers, thereby avoiding the need for the CAP to rely solely on inappropriate price support policies.

If other more effective policy instruments replace sole dependence on price policy then incentives to create massive EC agricultural surpluses should diminish. Australian competitors in export markets should benefit as perhaps will Australian suppliers to the EC.
The principal effect of the 1992 policy is to encourage an EC agriculture based on comparative advantage. The structural adjustments accompanying the 1992 policy are predicted (Agra Europe, 1989a; Kelch, 1989) to be:

- a strengthening of French agriculture,
- a concentration of quality grain production in France, northern Italy and possibly Spain,
- promotion of dairying in France and the Netherlands and
- general reductions in food prices. Lower food prices should lead to less unemployment and, for farmers with marginally profitable businesses, more off-farm employment opportunities.

The extent of the success of the 1992 policy in reorganising EC agriculture depends on how whole-hearted is the support that the policy receives from EC members, particularly West Germany, France and the United Kingdom.

EC members may use national policies to counteract the effect of the 1992 policy on their food and agriculture sectors. If these national policies are direct income supports rather than subsidy measures, then the economic distortion of national aids will be lessened and agricultural reorganisation still would be possible.

However, major aspects of 1992 reform can be prevented by the failure of a key EC member to offer its support, such as the United Kingdom's often stated refusal to accept the need for monetary union.

Will the 1992 policy succeed?
The EC member most pivotal to the success of the 1992 policy is West Germany because:

- it is the main net contributor to the CAP,
- it stands to gain the most economically from the 1992 policy,
- it has the strongest economy in Europe, although France is challenging,
- it has a poorly structured farm sector requiring high CAP support prices,
- its coalition government is vulnerable to a consolidated farm vote,
- it has a powerful 'green' lobby.

A major policy question in West Germany appears to be the political feasibility of replacing agricultural price supports with direct income supports, thereby reducing agricultural inputs and production - all under the guise of environmental concern and support. A more basic question is will farmers give up the pricing system that has served them so well for over 20 years?

References
Agra Europe (1989b). Recognition of need for more extensive farming in UK. No 1345, N/1, July 7.


Glossary
Common Agricultural Policy (CAP)
The CAP was introduced in the 1960s to promote a common market for EC agriculture through a system of export subsidies, import tariffs and direct production subsidies. The CAP takes up almost two-thirds of the EC budget.

European Community (EC)
The EC originally comprised six members - France, the Federal Republic of Germany, Italy, the Netherlands, Belgium and Luxembourg. Later to join were the United Kingdom, Denmark, the Republic of Ireland, Greece, Spain and Portugal; making a current full membership of 12 nations.

EC Commission
The Commission of the European Community is the main executive body. It creates and forwards policy proposals to the EC Council of Ministers and executes and administers decisions taken by the Council. The Commission has 17 EC Commissioners - two each from France, the Federal Republic of Germany, Italy, Spain and the United Kingdom; and one each from other members. The Commissioners are expected to act independently of national interest. There are about 16,000 Commission staff.

EC Court of Justice
It comprises 13 judges, each appointed for six years by mutual consent of EC members. It interprets EC law for national courts and rules on matters pertaining to EC treaties. EC bodies, EC members and individuals may bring cases before the Court and its judgements are binding.