

Issues in Agricultural Trade: The European Union

IPC Member Rolf Moehler led a seminar on February 12, 2004 for members of the Washington, DC agricultural trade community. Moehler discussed three topics: CAP Reform, Enlargement and European agricultural policy and how Europe sees the Doha Round of WTO negotiations.

CAP Reform

The European Union's Common Agricultural Policy (CAP) was built on the idea that the European Union was to be a common market and therefore, there needed to be a common market for agricultural products. There were varying agricultural support policies in all European countries and these needed to be consolidated through the creation of common European agricultural policies. The CAP was comprised of market price support above a set intervention price level; border protection through high and sometimes prohibitive tariffs and variable limits; and export subsidies.

Problems began to appear in the early 1980s. The European Union began to accumulate large commodity surpluses and was spending a great deal of money on export subsidies. In 1992 the CAP was reformed under the MacSharry Plan. The Plan reduced the market price support for cereals and beef and replaced the income loss through direct payments linked to historical production levels. The MacSharry reform took place during the Uruguay Round, but MacSharry was careful to argue that the reform was not taken because of the Uruguay Round negotiations (although it certainly played a role).

In 1999 the next reform program, Agenda 2000, was put in place to prepare for an enlarged European Union. Agenda 2000 was a continuation of the MacSharry reforms. It further lowered the market support price and added dairy to the program. Agenda 2000 also added what European Union Commissioner for Agriculture, Franz Fischler termed the "second pillar" of the CAP - rural development measures. These rural development measures aim to increase competitiveness of farmers but even more so to enhance the protection of the environment and the well-being of rural areas. More than half of the rural development funds go to maintaining and improving the environment and rural areas.

Fischler thought that the CAP was still too focused on product support after the Agenda 2000 reform. In 2002 he began the so-called Mid-Term Review of the CAP. In June 2003, another reform of the European Union's Common Agricultural Policy (CAP) was realized. In a major breakthrough, Commissioner Fischler persuaded the Council of Ministers to accept the idea of transferring payments into a single, direct payment. To receive the single payment, farmers must keep the land in good agricultural and environmental condition. To make the payments more palatable to taxpayers, Fischler's plan required farmers to comply with several hygienic, animal welfare and environmental standards in exchange for receiving the payment. The single payment was implemented to eliminate the artificial incentives to produce and to make European Union farm payments consistent with the notion that European agriculture does not exist solely to produce agricultural products, but also to provide a public good. Farming in Europe today is less about production; farmers are stewards of the environment.

Fischler was successful to some extent in cutting the link between production and support. He launched the idea for this reform a year after he became commissioner in 1996 and did not succeed until 2003. It is a measure of the difficulty in realizing this reform that it took Fischler nine years to do so. The fact that this accomplishment is not always appreciated discourages further reform. Reforms in tobacco and olive oil will be implemented soon and in June, Fischler will issue a White Paper on sugar reform. Reform of the sugar program is inevitable, but will be on the agenda of the next European Commission.

Enlargement

On May 1st of this year, the European Union will become larger by ten members: The Czech Republic, Cyprus, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, the Slovak Republic, and

Slovenia. In most of the new member states the contribution of agriculture to GDP and the percentage of total employment in the agricultural sector is greater than the current European Union average.

There are currently 6.7 million farmers in the European Union. On May 1st that will increase to thirty million by some estimates. (That number is likely to be overstated; the number of commercial farmers is far less.) If the number of farmers increases to thirty million the average farm size will fall to 5.7 hectares.

Regardless of what the actual increase in the number of farmers will be, it is a dramatic increase and will be a significant challenge. The European Union has never grown by such a large number or such a diverse group of countries in its history. There are still questions on how best to integrate the ten new member states into the European agricultural system. Critics have claimed that enlargement will destroy the CAP, but that is wrong. A mechanism to cut payments to farmers if there is not enough money available to meet expenditures was agreed on last year. It is unclear how the institutions of the enlarged Union will work. It will likely not affect decision-making significantly. It will be difficult to make decisions, but that is already the case.

The Uruguay Round had a significant influence on the CAP. At the same time, the MacSharry reforms affected the outcome of the Uruguay Round. The Uruguay Round Agreement on Agriculture also influenced the creation of the second pillar of the CAP in the Agenda 2000 reform as well as many of the measures that are included in the most recent reform, including the Single Farm Payment, which fits into the Green Box. Fischler indicated that preparing the EU's agricultural policies for WTO negotiations was not his main concern in the June 2003 reform, but it could certainly help the Doha Round.

The Doha Round

Enlargement will not change the European Union's position in the WTO negotiations. All of the new members are members of the WTO and will not want to change the European Union's position immediately. However, they may decide in the future that the Union's position as it stands would require too much reform too quickly for them. Contrary to popular belief, the European Union is not a closed shop. The Union has many commitments to imports beyond those that the new member states already have. Furthermore, the new member states will have to implement the European Union's general system of preferences (GSP), which applies to Former Soviet Union countries. This will be difficult for newly acceded states, since former Soviet Union countries have historically been significant trading partners for them and they will be forced to provide them non-reciprocal tariff reductions under the GSP.

A brief illustration of the initial European position on the three pillars of agricultural negotiations in the WTO follows.

Market Access: European Union leaders are attached to the Uruguay Round formula for cutting tariffs.

Export Subsidies: The European Union can only commit to reducing export subsidies, not phasing them out entirely.

Domestic Support: The Union could agree to substantial reductions in trade-distorting domestic support, but will insist on keeping the Amber, Blue and Green boxes and the Peace Clause.

The European Union's position moved significantly in the EU-US joint paper that was issued before Cancun, but other WTO members did not appreciate this. In the proposal, the European Union moved on market access by accepting the blended formula – one part Uruguay Round Formula and one part Swiss Formula; the Union agreed to phase out export subsidies on products of interest to developing countries; and the Union accepted the idea of capping the Blue Box category of domestic support.

Unfortunately the EU-US paper was not well-received. Critics have said that the United States should have joined with the Cairns Group rather than the European Union. However, had the United States not paired with the European Union, the Union's position would not have moved at all and there would have been deadlock between the United States and Cairns Group on one side and the European Union and Japan on the other.

At a recent farmers' meeting, an official from the Office of the United States Trade Representative said that the United States' main goal in the WTO negotiations is to open markets for United States agricultural products and decrease protection in the European Union. When United States Trade Representative, Robert Zoellick issued letters in an attempt to restart the Doha Round, he noted the importance of eliminating export subsidies. These are not useful positions because they impose reform on the European Union rather than propose reform for the United States. It is highly unlikely that the European Union will commit to date-certain elimination of export subsidies. In order to completely eliminate export subsidies in the European Union, there would have to be further CAP reform and this has not even been considered yet. The three boxes that define domestic support work well and the CAP fits within them. There is a chance that WTO members will come to an agreement, but it will probably not be this year.

Discussion

...on CAP reform

IPC Chairman, Robert Thompson asked Moehler about the flexibility countries have on decoupling payments. Member states have a minimum percentage of payments that must be decoupled from production, but may decouple their payments beyond the minimum level. Is there momentum toward the more decoupled payments that Fischler originally pushed for? Moehler answered that not all member states of the European Union have decided whether or not they will take advantage of the option to decouple payments beyond the minimum level. Germany has said it will; France has said it will not. Germany wants to go even further and transfer all payments to area payments – even those for dairy and beef. There is definitely strong momentum toward providing 75-100% of payments as direct payments.

...on European Union accession

A participant asked Moehler about the expenditure ceiling on CAP spending from the most recent reform in view of accession. Moehler answered that with the new member states agricultural area in the European Union will increase by 30%, but the amount of money available will only increase by about 10%, so there will definitely be budget pressure. The most recent CAP reform established a mechanism to cut payments to farmers in case the money available is not sufficient to keep expenditure up. If there are not sufficient resources, the single payment will be cut, so cereal farmers would effectively be paying sugar farmers.

The European Union agreed last October that the amount of money that will be available for agriculture should be announced seven years in advance in line with the EU's seven-year planning framework. EU member states have agreed to keep the amount of money in the CAP level as a percentage of the European Union's overall budget. Farmers in new member states are not immediately eligible for the full payment upon accession, but receive proportionately more until 2013. That means less money for individual farmers as the newly acceded countries become eligible for more of the CAP payments.

A few weeks ago, six European Union governments expressed concern that there are not sufficient funds in the current budget if were enlargement to take place today. In view of this, it is possible that the entire agricultural budget could have to be reviewed and eventually cut. However, if the European Union has less money, it does not mean the it will change its position in the WTO.

...on the WTO negotiations

Another participant noted that it increasingly looks as if there will be a tradeoff between domestic support and market access in the Doha Round agricultural negotiations. The United States and European Union tiptoed around the issue of tariff-rate quotas (TRQs) in its proposal. Is Europe willing to loosen TRQs?

Moehler answered that the EU-US paper said if it was politically difficult to apply the Swiss Formula, countries could expand TRQs in combination with the Uruguay Round approach to increase access. Therefore there could be more TRQs, but they would be larger.

Another participant asked if the EU-US proposal was still in effect and still binds the United States and European Union together. Moehler was unsure to what extent the two parties are bound to the proposal. He noted that the proposal says that export subsidies are still under negotiation, but United States Trade Representative Zoellick recently stated that the United States will work for date certain elimination of export subsidies. The two parties will certainly continue to work together.

Another participant asked about the future of the Peace Clause. There are many observers that think Brazil has a good chance of winning its sugar case. Moehler said that the Peace Clause is more at stake in Brazil's cotton case against the United States than in the European Union sugar case because the EU's dual pricing system makes the situation more complicated. When asked whether he thought the Peace Clause expired at the end of individual commodity marketing years, he said he believed it expired on January 1, 2004.

However, he said that there is a need for the Peace Clause because the Agreement on Agriculture and the Agreement on Subsidies and Countervailing Measures are not compatible. For example, some policies allowed under that Green Box are actionable under the Agreement on Subsidies and Countervailing measures. There needs to be an agreement on how countries can apply trade remedies on agricultural support. The Peace Clause came at the end of the Uruguay Round and it will probably be the same case at the end of the Doha Round.

Another participant asked how to go forward with special and differential treatment that will be agreed by developing countries but will not hurt their potential for economic growth. Moehler replied that special and differential treatment was established to give developing countries more time to reform and to give them better access to developed country markets than developed country WTO members.

It seems that developing countries have now determined that special and differential treatment also means they do not have to liberalize and can increase protection. This is why ideas like the Special Product designation have gained significant ground. This kind of special and differential treatment will ensure that developing countries stay where they are economically rather than improving their development.

A participant from a developing country asserted that many developing countries do not believe that the developed countries met their reform commitments from the Uruguay Round. Moehler answered that developed countries will not agree to open markets completely and some degree of protection will remain. However, developed countries can accept the Uruguay Round's classification of domestic support, they can agree to decrease trade distorting support. But if countries pursue claims that Green Box are trade-distorting, they will not get anywhere.

Robert Thompson asked when Moehler referred to developing countries if he meant countries that were truly developing or whether he was referring to countries that have designated themselves as such in the WTO. Moehler said that if countries can continue to self-designate as developing countries, the GSP does not mean that much. There have been efforts to change this, but they have not been successful. The EBA initiative is a beginning to do this, but it will be difficult to find a solution in the Doha Round.

...on the Everything but Arms initiative

Another participant asked about the commodity protocol for least-developed countries under the Everything But Arms (EBA) initiative. Moehler answered that it will continue, but it is not yet implemented on sugar, bananas and rice. There are still quotas for those products, but they are enlarged and will be phased out. The EBA initiative is partially driving the sugar reform.

...on export subsidies

Another participant said that Western Hemisphere FTA negotiations are trying to eliminate export subsidies. He asked if there is any chance that the European Union would agree not to use subsidized exports to the Western Hemisphere. Moehler answered that the only way he could foresee that would be in the context of an EU-MERCOSUR FTA.

...on reform of the European Union sugar program

IPC Chief Executive, Ann Tutwiler said that Commissioner Fischler's White Paper on sugar reform is rumored to have two extreme options for reform and one more moderate proposal. She noted that France seems to have realized that it could be the most competitive sugar producer within the European Union is therefore becoming more progressive when it comes to sugar reform.

Moehler answered that the middle of the road sugar reform proposal is likely to be something similar to what is currently in place for other crops – a lower price support for sugar, with more direct payments. The treatment of C Sugar quotas (sugar produced above domestic production quotas that cannot be sold internally during the year) will depend on the results of WTO dispute brought by Brazil. If prices are lowered sufficiently there could be an elimination of the sugar quota. French producers are not opposed to the abolition of the sugar quotas, but Germany is.

...on developed country import standards

Another participant asked if there had been any suggestions to harmonize developed country import requirements like rules of origin and sanitary and phyto-sanitary (SPS) standards to help LDCs be more successful in exporting to developed country markets? So far the only product from Africa that has made it through the United States SPS standards are peas from Senegal.

Moehler answered that it would probably be nice to have harmonized import standards for developing countries, but it is not likely. SPS rules and rules of origin are complicated everywhere. The United States and European Union can hardly agree with each other on these.