

# Agriculture and agricultural policy in the European Union

## *Zemědělství a zemědělská politika v EU*

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**Abstract:** The paper deals with the particular stages of development of the EU Common Agricultural Policy (CAP) in the last forty years. The process and impacts of CAP reforms are analyzed for the particular production industries of agriculture. The paper also presents a detailed description of Agenda 2000 and mid-term review of the Common Agricultural Policy in 2002 that brought about many proposals for the future working of CAP after accession of Central and Eastern European countries.

**Key words:** Common Agricultural Policy (CAP), EU, Agenda 2000, Mid-Term Review of CAP

**Abstrakt:** Příspěvek se zabývá jednotlivými etapami historického vývoje Společné zemědělské politiky (SZP) EU v posledních 40 letech. Analyzuje průběh a dopady reforem SZP z hlediska jednotlivých výrobních odvětví zemědělství. Podrobněji pojednává o Agendě 2000 a o poločasovém hodnocení Společné zemědělské politiky v roce 2002, které přineslo řadu návrhů pro budoucí fungování SZP se zřetelem k rozšíření EU o země střední a východní Evropy.

**Klíčová slova:** Společná zemědělská politika (SZP), EU, Agenda 2000, hodnocení reformy SZP

### **FOUR DECADES OF COMMON AGRICULTURAL POLICY (CAP)**

For four decades, the CAP has constituted the main policy framework for the development of the EU's agricultural economy. It was put in place to ensure stability and continuity. But it does not prevent change. During the last 40 years, agricultural employment in the EU has been more than halved. There have been sometimes quite spectacular increases in productivity and production. On the downstream side, a modern and highly efficient food industry has emerged which today buys and adds value to more than 70% of the EU's agricultural output and employs more than two and a half million people. Both agriculture and the food industry have become increasingly trade oriented. The EU is the largest importer and the second largest exporter of farm and food products in the world. Again there have been quite important changes over time. The most remarkable development is probably the strong growth in trade of high value added processed products.

Structural change will continue to take place over the years and decades to come and new challenges will appear. Although it is difficult to establish clear cut causalities, it is certainly not wrong to say that the relatively stable support framework offered by the CAP to farmers in the EU has contributed to the developments of the past 40 years. It has also helped in a number of rural regions to avoid economically and socially disruptive effects that would otherwise have occurred. However, in order to achieve its objectives and to respond to new challenges,

the CAP itself has to adapt to the changing environment, inside the EU and internationally. Indeed, the CAP has evolved considerably, in particular over the last decade.

### **THE CAP REFORM PROCESS**

Until the early 1990s, CAP market policy relied almost exclusively on price support systems combined in a few cases with strict quantitative production controls. Price support was generated through the combination of border protection, export subsidisation and intervention buying at guaranteed prices.

In many respects, even today, most of these support systems are still in place. But their importance has diminished. The 1992 reform introduced for a few key agricultural sectors partial, but significant, shifts from price support to direct payments and these direct payments were based on to historical references. With the Agenda 2000 reform, decided in 1999, the shift from price support to direct support continued and in the future, it could well become the dominant form of agricultural support in the EU. This development has the double advantage of making support to agriculture less distorting and more transparent.

As regards the structural policy for agriculture and rural areas, a first attempt to develop a common policy framework was decided in the 1970s with the so-called socio-structural directives. Their main aim was to improve agricultural production, processing and marketing structures and to support farmers in less favoured areas.

During the 1980s, the first integrated development programmes were launched, some of them specifically targeted at rural regions. They were multi-sectoral programmes with the combined intervention of different Community funds and carried out in close partnership between the EU, Member States and regions. This approach was further developed into the reform of the structural funds in 1988 and still remains the basic philosophy and orientation after the Agenda 2000 reform.

During the first two and a half decades of its existence, environmental questions played no major role in the CAP. This has changed. Increasing environmental problems have drawn public attention to the role, whether negative or positive, agriculture plays or at least could play in this context as the biggest land user in the EU. After some optional measures in the second half of the 1980s, a more comprehensive agri-environmental policy was introduced under the 1992 reform and its implementation was made compulsory for Member States. Together with other measures, it forms today an integral part of the EU's agricultural and rural policy and its importance is increasing, in political as well as in financial terms.

## **THE AGENDA 2000 REFORM**

With Agenda 2000, a new and important step was made in the CAP reform process. Most of this has now been implemented. As far as market policy is concerned, the Agenda 2000 reform basically represents a deepening and an extension of the 1992 reform. Price support has been reduced further for cereals and beef and direct payments in these sectors have been increased and re-organised to compensate farmers, at least partially, for the price cuts. In addition, direct payments for oilseeds have been phased down to the cereals' aid level and the specific support for oilseeds has been abolished. A similar reform with support price cuts and the introduction of direct payments is foreseen for the milk sector, but only from 2005 onwards.

Member states have the possibility to introduce environmental cross-compliance requirements. Thus, direct payments can be reduced if farmers do not respect statutory environmental standards or other specific environmental requirements that form part of good agricultural practice. Member states can also introduce modulation mechanisms reducing direct payments by up to 20%. Savings, obtained through cross compliance or modulation, can be used by the member states concerned for additional measures in their rural development programmes.

As far as rural development is concerned, the Agenda 2000 reform implies a considerable overhauling, streamlining and consolidation of the existing policy. All relevant measures have been brought into one policy framework and are in principle applicable in all rural areas of the EU. Rural development is presented as "the second pillar" of the CAP. This sounds ambitious and critics rightly say that in terms of resource endowment, we

are still far away from a real second pillar. But the structures to get there have been put in place, the foundations have been laid down and if there is a political will to build on these foundations in the future, it can be done.

## **THE MID-TERM REVIEW OF THE CAP**

### **Background**

When the final decisions concerning the Agenda 2000 reform were adopted in spring 1999, it was also decided to undertake a number of mid-term reviews around 2002/2003, re-examining market developments as well as the situation of the agricultural budget.

Since then, a lot has happened. The BSE crisis has triggered off a process of growing public concerns about both the way in which food is produced and the way in which agriculture is supported. And these concerns are not only linked to food safety and food quality, but also to the consequences of agricultural production for the environment and for animal welfare.

The integration of environmental concerns into EU policies and their contribution to the achievement of a sustainable development are explicitly required by the Treaty of Amsterdam, in force since May 1999. It also lays out new ground rules for the actions of the EU on animal health and welfare in a special "Protocol on the Protection and Welfare of Animals".

In June 2001, the European Council in Göteborg agreed on the basis of a communication from the Commission on a strategy for sustainable development. It made once more clear that sustainable development – to meet the needs of the present generation without compromising those of future generations – is a fundamental objective under the Treaties. Economic, social and environmental effects of all policies should be examined in a coordinated way and taken into account in decision making.

In its submission to the European Council, the Commission had stressed that all EU policies should have sustainable development as their core concern and that the forthcoming reviews of common policies should look at how they can contribute more positively to this objective. Thus, the mid-term review of the common agricultural policy should reward quality rather than quantity by, for example, encouraging environmentally-friendly farming methods and a further shift of resources from market support to rural development.

### **The Commission's proposals for the future**

It is against the background of all these developments, that the policy orientations the Commission proposed in its mid-term review of the CAP in July 2002 have to be seen.

The mid-term review is presented in the form of a Communication to the Council and the Parliament. It is meant to open the debate on the future development of the

CAP and to allow a broad consultation of the other EU institutions, of national and regional authorities and of the civil society at large. Detailed legal proposals will follow later.

It is not possible here to enter into a detailed description and analysis of the measures proposed by the Commission. I will therefore just try to give an overview and highlight a few aspects.

The Commission proposes adjustments to common market organisations for a number of agricultural commodities together with major changes in the system of direct payments. They should to a very large extent become decoupled income payments. Another key proposal is the strengthening of rural development as the second pillar of the CAP. More funds should be made available for this purpose by shifting money from the first to the second pillar through a mechanism of dynamic modulation. The measures for which this money can be used in the second pillar are extended. Food safety and food quality, environmental objectives and animal and welfare concerns are addressed through cross compliance as well as through the encouragement of farmers to participate in voluntary schemes under rural development programmes.

As regards market policy, the Commission sees a need for adjustment in order to reinforce the role of intervention as a safety net and not as a systematic outlet for surplus production. Agricultural production should be more oriented to the products and the services that the public wants and not to artificially created price incentives or product-specific aids. The proposals also respond in part to criticism from the European Court of auditors and take account of the Commission's own evaluation work.

In the cereals sector, it is proposed to reduce price support further, with partial compensation through increased direct payments, to abolish the intervention of rye, where the market situation is particularly unbalanced, to reduce the specific aid for durum wheat and to introduce a quality premium for this cereal. Compulsory set-aside would be maintained. But in order to enhance its environmental benefits, the Commission proposes to transform the current scheme into fixed long-term set-aside. The existing arrangements for non-food production on set-aside land would be replaced with an aid for the production of energy crops.

A major reform is foreseen for the rice sector, with a reduction of price support down to the level of expected world market prices and a safety net intervention below this level. Again there will be partial compensation in the form of increased direct payments for the farmers concerned. Without such a reform, the situation would become unsustainable in the second half of this decade when imports from least developed countries will get totally free market access to the EU market.

In order to be complete, let me still mention that the Commission also suggests some major adjustments to the common market organisation for dried fodder and proposes to continue the support scheme for nuts and almonds, again with some adjustments. Finally, the oilseeds sec-

tor has been examined as part of the mid-term review, but no specific new measures are judged necessary here.

The beef and the dairy sectors, too, were on the agenda of the mid-term review. As the beef market is progressively recovering from the second BSE-crisis, no specific new measures of market intervention are deemed necessary at this stage. However, the Commission proposes to include the current headage payments in a single decoupled income payment per farm, to which I will come in a moment. This should reduce pressures towards intensive production and help to achieve a more balanced market situation in the longer run.

As regards the dairy sector, the Commission refers to a technical report dealing with the current quota system and with the advantages and disadvantages of several options for the EU's dairy policy post 2006. The options analysed range from a continuation of the status quo after implementation of the Agenda 2000 reform to a complete abolishment of the quota regime post 2008. The Commission thus wants to open the debate on the future of the EU's dairy policy without prejudging its outcome. No proposals are made at this stage.

A core element of the Commission's proposals is the introduction of a single decoupled payment per farm. It would be based mainly on historical references and should cover as many sectors as possible. In a first stage beef, sheep, cereals, oilseeds and some smaller crops would be covered which together represent a large part of the existing direct payments. Farms under the scheme will have a far-reaching flexibility in their production decisions.

This new approach is seen as the logical final step in the shift of support from production to the producer, a process which started with the 1992 reform. Decoupling should improve the overall market orientation of agriculture and allow farmers to adjust their production mix in line with market opportunities. The transfer efficiency of direct payments as an income aid should increase and support would become simpler and more transparent. Last, but not least, such a scheme would be compatible with the WTO Green Box requirements.

The full granting of the decoupled farm income payment, but also of other direct payments will be conditional on a certain number of statutory environmental, food safety, animal health and welfare standards, as well as occupational safety requirements for farmers. This cross compliance will be applied as a whole farm approach with conditions attached to both used and unused agricultural land.

A system of farm auditing will be mandatory as a part of cross-compliance requirements for producers receiving more than 5000 € per year in direct payments. The main objective is to help farmers to become aware of material flows and on-farm processes relating to the standards they have to respect. Support to cover the costs of participation in audits will be available under new rural development measures.

In order to achieve a better balance between market and income support on one side and rural development on

the other, the Commission proposes introducing a system of dynamic modulation on a compulsory basis for all member states. This is another core element of the mid-term review proposals. The new system would replace the current optional arrangements from 2004 onwards. All direct payments would be reduced progressively in arithmetic steps of 3% per year to reach 20%.

This reduction of direct payments would be combined with a franchise dependent on employment on each farm. For up to 2 full time annual work units, the franchise would be 5 000 €. This would ensure that a large majority of smaller farms would not be subject to modulation. For each additionally employed annual work unit an additional 3 000 € may be granted on an optional basis by member states.

After the application of modulation, the maximum sum paid to a farm should not exceed 300 000 € plus the franchise. Direct aids beyond this amount would be capped and made available for transfer to the second pillar in the member state concerned.

The amounts saved by modulation itself would be redistributed to member states on the basis of agricultural area, agricultural employment and a prosperity criterion. Member states may use the additional funding from modulation and capping to reinforce their rural development programmes.

In order to strengthen the second pillar of the CAP, the Commission not only proposes to shift funds from the first to the second pillar. It also foresees the extension the scope of the so called accompanying measures in the second pillar to better address concerns about food safety and quality as well as animal health and welfare.

Currently, there are four accompanying measures. They comprise actions in favour of agri-environmental protection, farming in less favoured areas, afforestation of agricultural land and early retirement. For the future, the Commission proposes to add two new measures.

The first one concerns food quality and is meant to encourage farmers to participate in quality assurance and certification schemes. A farmer who enters such a scheme can receive a flat rate payment for a period of maximum five years. In addition, producer groups can get help for the promotion of quality products covered by these schemes.

The second new measure is called "Meeting Standards". It offers the possibility to help farmers financially during five years to adapt to the introduction of new standards based on the EU legislation in the fields of environment, food safety, animal health and welfare and occupational safety. In addition, all farmers participating in farm audits can receive a flat-rate payment to help them meet the costs of such audits.

In addition to these two new accompanying measures, the Commission proposes to introduce into the agri-environment chapter the possibility to offer specific animal welfare payments for efforts that go beyond the mandatory reference level. And the EU co-financing rate for agri-environment and animal welfare measures would be increased by an additional 10%.

## First assessment

These are the main policy orientations the Commission proposed in its mid-term review. They go further than the minimum programme for the mid-term review that was foreseen when the Agenda 2000 reform was decided in spring 1999. But the Commission could not simply ignore developments, which have taken place since then. And although the mid-term review goes further, it remains clearly in the logic of the CAP reform process that started in 1992. It stays below the budget ceiling set for agricultural expenditure by the Berlin European Council. And it continues to pursue – and is meant to better achieve – the objectives of Agenda 2000.

These objectives involve more market orientation and improved competitiveness; food safety and quality; stabilisation of agricultural incomes; integration of environmental concerns and sustainable rural development; simplification of the policy and its administration and a better sharing of responsibilities through increased decentralisation.

With respect to all these objectives, the Commission expects benefits from the proposed policy orientations. Decoupling should allow farmers in the sectors concerned to focus on products, which give them the best return from the market, reflecting their skills and initiative as well as local agronomic conditions. It should also improve in a number of cases the efficiency of transfers to farmers and should help them to improve their income situation. First impact analyses, which have been carried out with the help of policy simulation models, would tend to confirm this expectation.

Dynamic modulation will provide the means to increase spending in favour of rural development programmes and the range of measures that can be included in these programmes has been extended. In combination with the proposed changes to common market organisations, this should improve the potential for long-term sustainability of the sector. Moreover, once it is fully implemented, the proposed decoupled income payment should represent a major simplification of current arrangements. The majority of income support would be made in one single payment.

For consumers, too, the proposals represent a step forward. The inclusion of food safety, animal health and welfare and protection of the environment in cross-compliance and their systematic monitoring through farm audits should improve transparency and help to rebuild confidence.

Although the Commission has made its proposals mainly to meet internal needs and expectations, it is convinced that they will also help the EU to respond to external challenges. Thus, the integration of new member states into the CAP should be facilitated. The proposed changes in common market organisations address problems in EU-15 before enlargement. Decoupling should help farmers in the new member states to improve market orientation from the very beginning, rather than focusing production mainly on policy incentives. The farm in-

come payment should offer a relatively simple solution compared to existing arrangements. Dynamic modulation would not be applied to farmers in the new member states before they had reached the normal level of EU direct payments. In addition, it has already been proposed to increase their rural development allocation compared to the normal EU level. Last, not least, the proposed change changes and additions to rural development measures should help farmers in the new member states to implement the EU standards for food safety and quality, environmental protection and animal health and welfare.

## Outlook

All these aspects deserve further consideration. But once again, we are now in a phase of consultation and discussion. As I said before, we expect detailed legal proposals to be presented and we hope that decisions can be taken in the first half of next year.

Already now, a number of other sectors are scheduled for reform in 2003: Olive oil, sugar, tobacco, wine, hops and perhaps also cotton. The Commission will propose

policy orientations for these sectors in line with the mid-term review and in the light of the debate it generates during the coming months. In 2003, we will probably also know more about the modalities and the possible outcome for agriculture of the new WTO-Round. Towards the end of next year, the Commission is expected to present first orientations for the EU's structural policy. In this context, more fundamental questions concerning rural development and its future architecture may also be raised. Finally, in spring 2004, we expect the debate on the next financial perspective for the period 2007–2013 to start.

## CONCLUSION

As regards agricultural and rural development policies, we have an important work programme in front of us for the months and the years to come. It represents a unique opportunity to make our policies fit for the next decade and to establish a stable framework for farmers in all member states, the old and the new ones. And this is what they need. We therefore should not miss this opportunity.

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