THE COMMON AGRICULTURAL POLICY OF THE EEC -
A Review of Recent Developments

D.C. SPROTT and I.C. DICKIE

Occasional Paper No. 41

Australian Government Publishing Service
Canberra 1976
CONTENTS

Introduction

The Organisation and Regulation of the EEC's Major Agricultural Markets

Cereals

Sugar

Beef and Veal

Dairy Products

The Impact of Major Economic Problems on European Agriculture

Monetary Adjustments and Intra-Community Farm Trade

National Aid Measures in Individual Member Countries

Consumer Interests and Cost of the CAP

Structural Adjustment in EEC Agriculture

Proposals for Reform

Implications of Recent EEC Developments for Australia

Conclusions

TABLES

Table No.  

1  Self-sufficiency Levels for Major Agricultural Products in the EEC  

2  Economic Indicators in Major EEC Countries  

3  EEC Expenditure Patterns
TABLES (continued)

Table No.                                                                                   Page
4   Labour Mobility in EEC Agriculture                                                      27
5   Changes in the Number and Size of Community Farms: EEC-9                                28
6   Australia: Gross Value of Exports of Rural Commodities to the United Kingdom: 1970-71 to 1974-75 33
7   Australia: Gross Value of Exports of Rural Commodities to the Enlarged Community: 1972-73 to 1974-75 34

GRAPHS

Graph                                                                                       Page
I    Prices of Certain Agricultural Products in the EEC in Relation to World Prices          6
II   Exchange Rate Adjustments of Selected EEC Currencies                                    15
III  Adjustments in EEC Representative Exchange Rates and in Monetary Compensatory Amounts 19
THE COMMON AGRICULTURAL POLICY OF THE EEC
A REVIEW OF RECENT DEVELOPMENTS

Introduction

Since its introduction in 1962 the Common Agricultural Policy (CAP) has, through providing extensive assistance and protection to the EEC's agricultural sector, influenced the levels of agricultural output and resources utilised in agriculture. At present over 80% of the Community's agricultural production is covered by the system which involves the provision of internal support for market prices, the abolition of barriers to intra-Community trade and the establishment of common border regulations for both imports and exports.

The major elements of the CAP mechanism and the overall objectives of the system were described in some detail in an earlier Bureau study(1) and also in the recent OECD report on agricultural policy in the EEC.(2) Essentially, however, the system ensures that for most agricultural commodities, intervention agencies support market prices for producers by buying at predetermined levels which, for most of the period since 1962, have been well above world market prices. This has been made possible by insulating the domestic EEC market from the world market through the operation of variable import levies and threshold prices. The existence of relatively high support prices, often in conjunction with climatically induced increases in output, has periodically generated surpluses which have often been exported with the aid of export restitutions. Alternatively, however, when world prices are above EEC support levels, as they were in 1973 and 1974 for grains and sugar, and there is at the same time the possibility of insufficient domestic supplies, export levies and controls are sometimes used to discourage Community exports and subsidies are used to encourage imports.

During the past fourteen years the principles and the basic mechanism of the CAP have remained essentially unchanged. However, within this broad framework there have been continuing adjustments in the regulations of the CAP and some relatively minor shifts in the emphasis given to the various objectives of EEC agricultural policy. The period 1962 to 1968 can be viewed as a transitional phase during which the original six member countries adapted their agricultural systems to the major principles of the CAP such as the harmonisation of farm prices, Community preference and centralised financial management. By July 1968 the CAP's provisions were fully operative on the EEC's production of cereals, dairy products, eggs, and beef and veal, accounting for over 50% of the gross value of EEC agricultural output.(3)


(3) The major horticultural industries in the Community and its mutton and lamb industry are protected through the Common External Tariff (CET). Neither the CAP nor the CET are applicable on raw wool and oilseeds, imports of both commodities being admitted duty free.
The major emphasis of EEC agricultural policy during the 1960s and early 1970s was on the implementation of a system of common prices in order to support market prices and farm income levels. There was much less attention given to consumer interests and to measures to improve the structure and to promote the productivity of the EEC agricultural sector. As a result there were marked increases in farm support prices, especially in France, the largest agricultural producer, and in levels of agricultural self-sufficiency within the Community. There was also an increase in the propensity of the EEC to generate surplus supplies, particularly of soft wheat and butter, and in total Community expenditure on agricultural support. During this period the CAP played a relatively minor role in the implementation of programs designed to improve the productivity and structure of EEC agriculture. Thus, although there was an especially large outflow of labour from the rural sector between 1962 and 1971 and consequently an impressive growth in labour productivity, these developments were largely autonomous and were not a result of the implementation of Community agricultural policy. In fact the high levels of support under the CAP have tended to constrain the movement of labour from agriculture.

Since 1971 there have been several important developments which have influenced the evolution of the CAP. In this respect the enlargement of the Community from six to nine members at the beginning of 1973 was of fundamental importance. This had the effect of altering the export/import balance and self-sufficiency levels for some of the main agricultural products in the EEC. In particular the accession of the United Kingdom, a major agricultural importing country, to the EEC has had important implications for the direction of international commodity trade(4) and for the exports of countries such as Australia that were major suppliers to this market in the past. Internally the enlargement of the EEC, in conjunction with other factors, e.g. inflation and the spread of consumerism, helped to focus greater attention on issues such as consumer food prices, the cost of agricultural support and structural reform. However, crises in various agricultural markets and the continuing dominance of producer interests have subsequently diminished the importance of these issues to a considerable extent.

Another major factor which has affected Community agriculture over recent years has been an increase in economic and monetary instability. In particular there was a serious deterioration in the economic environment in all member countries in 1974 and 1975, especially in Italy and the U.K. This deterioration was manifest in high rates of inflation, depressed levels of economic activity and, in some countries, severe balance of payments problems. Also, the economic costs associated with the CAP became much more burdensome in this period of economic depression.

One of the effects of this economic malaise has been an increasing incidence of unilateral agricultural action by member countries. This has taken various forms, including the imposition of import controls by Italy and of domestic livestock producer subsidies by France and Belgium. In some cases the measures have apparently been in

contravention of CAP regulations. Another important aspect of recent economic developments has been the large number of exchange rate variations amongst member countries. This has created problems in maintaining common price levels and has made the operation of the CAP more complex. The system of compensatory measures introduced to offset the effects of these exchange rate variations has, to some extent, fragmented Community agricultural markets.

Since 1973 EEC agricultural policy has also had to respond to rapid and significant changes in the world supply/demand situation for important agricultural commodities. In 1973 and 1974, world prices for cereals and sugar rose to extremely high levels and were at times well above EEC support levels. This necessitated the introduction by the Community of unprecedented measures such as levies on exports of cereals and sugar and subsidies on sugar imports. After a long period of buoyant demand there was also a severe downturn in world meat trade and prices in 1974, largely as a result of lower levels of consumption and greatly increased supplies in major producing regions, including the EEC. In this situation the EEC intensified its efforts to protect its domestic beef producers by several means including the closure of the market to non-member sources of supply such as Australia.

The period 1971 to 1976 has thus been one in which the foundations of EEC agricultural policy have been subject to considerable and diverse pressures. Internal and external developments have encouraged a more critical assessment by the EEC Commission and by member countries of the direction and operation of agricultural policy in the Community. Several proposals for reform of the CAP have been produced since 1973, the most recent and probably the most important being the Commission's 'Stocktaking of the Common Agricultural Policy' which was released in March 1975. However, in spite of these pressures, the pace of change has been slow and there have not as yet been any significant alterations brought about to the basic principles and framework of the CAP. It has often been necessary instead to concentrate on resolving short-term problems that have arisen, at the expense of working towards achieving longer-term objectives.

The purpose of this report is to review major developments in the organisation and regulation of agricultural markets and in agricultural policy in the EEC over the last five years and to make some assessment of the effects of these developments on EEC agriculture and agricultural trade. The report also describes the recent proposals to reform the CAP and attempts to identify possible longer-term changes in Community agricultural policy and their implications for Australian farm trade.

The Organisation and Regulation of the EEC's Major Agricultural Markets

The enlargement of the EEC and the magnitude of the fluctuations in world commodity prices over recent years necessitated important adjustments in the Community's regulations regarding the production and trade of several agricultural commodities.

For many major agricultural products the accession of the United Kingdom to the EEC initially reduced the Community's level of self-sufficiency (see Table No. 1). Community enlargement resulted in a sharp fall in self-sufficiency levels for wheat, dairy products and sugar. In fact, in the case of sugar the EEC moved, at least in the short term, from being a sizable exporter to being a sizable net importer. Enlargement had little immediate impact on self-sufficiency levels for the major meat products (although since 1974 the enlarged Community has experienced surplus beef supplies).

Table No. 1

<table>
<thead>
<tr>
<th>Product</th>
<th>EEC - 6</th>
<th>EEC - 9</th>
</tr>
</thead>
<tbody>
<tr>
<td>Common wheat</td>
<td>102 %</td>
<td>115 %</td>
</tr>
<tr>
<td>Oats</td>
<td>88 %</td>
<td>100 %</td>
</tr>
<tr>
<td>Barley</td>
<td>91 %</td>
<td>110 %</td>
</tr>
<tr>
<td>Beef and veal</td>
<td>88 %</td>
<td>86 %</td>
</tr>
<tr>
<td>Maize</td>
<td>66 %</td>
<td>68 %</td>
</tr>
<tr>
<td>Pigmeat</td>
<td>101 %</td>
<td>100 %</td>
</tr>
<tr>
<td>Poultry meat</td>
<td>101 %</td>
<td>100 %</td>
</tr>
<tr>
<td>Butter</td>
<td>105 %</td>
<td>116 %</td>
</tr>
<tr>
<td>Cheese</td>
<td>102 %</td>
<td>103 %</td>
</tr>
<tr>
<td>Sugar</td>
<td>106 %</td>
<td>122 %</td>
</tr>
</tbody>
</table>

(a) Including durum wheat.


The organisation of the EEC agricultural markets has not only been influenced by internal structural changes such as enlargement but also by external commodity price developments. World prices of many agricultural commodities registered massive and in most cases unprecedented increases between 1972 and the end of 1974, largely as a result of production shortfalls in several major producing countries. During this period world wheat and coarse grain prices more than doubled while there was practically a tenfold increase in world sugar prices. The price of these commodities has eased during 1975 and 1976. Nevertheless, the increase in world cereal and sugar prices from 1972 through 1974 was of such magnitude as to alter the traditional relationship for these commodities between world and Community price levels. For the first time
since the inception of the CAP, world prices of these commodities at mid-1973 were above EEC threshold levels (Graph I).

World meat prices, which had been on a strong upward trend throughout most of the 1960s and until 1973, weakened sharply in 1974 and have remained weak into 1976 as a direct result of lower world demand and a substantial build-up in world cattle numbers. A substantial supply/demand imbalance in world dairy product markets has also recently developed in 1975 and 1976, and has been particularly marked in the skim milk powder (SMP) sector. This has been reflected in the EEC by the accumulation of large surplus stocks of SMP. These recent disruptions in the world dairy products and meat markets and the earlier market buoyancy and abnormally high prices for cereals and sugar have led to the introduction of new agricultural market regulations and tested the flexibility of the CAP. The new regulations introduced for major agricultural sectors in response to these changed circumstances and pressures are reviewed in the following sections.

Cereals

Until 1973 the usual external trade regulations applicable to the EEC grain market were import levies and export restitutions. However, as a result of the upward movement of world cereal prices the EEC Commission, in May 1973, cancelled export restitutions on all cereals, flour, fine meal and semolina. This was followed by a decision in July of that year to apply levies on grain exports in the event of the c.i.f. price exceeding threshold prices by more than 2%. After a short period in which the Commission suspended wheat exports a system of variable export levies was introduced in August 1973 to cover not only wheat but also barley and maize shipments. The purpose of these levies was to safeguard Community supplies.(6) Their method of operation was similar to that of import levies in reverse, and they were made equal to the difference between world market prices and target prices in order to discourage cereal exports.

The above measures represented a significant departure in EEC regulations governing cereal trade, and remained operative in the case of wheat for the remainder of 1973 and for most of 1974. Export levies on barley and maize were applicable for shorter periods because world prices of these commodities periodically dipped below EEC threshold levels in 1973 and 1974.(7) Significant weakening in world cereal prices during the first half of 1975 resulted in the re-introduction of import levies which have been in operation again over most of the ensuing period. However, the strong recovery in world grain trade in the second half of 1975, which came about largely as a result of substantial USSR imports, led to the re-introduction of EEC export levies in August for a short period.

(6) The EEC attempted to ensure that exports to traditional markets were not disrupted, through the use of tendering procedures. Under this system EEC exporters were invited to tender for the export levy on the supply of a given quantity of grain to specified markets.

(7) In comparison to levies on soft wheat, export levies on maize and barley were not only of shorter duration but were also not as great. For example, at the beginning of 1974 export levies on soft wheat were the equivalent of about $A80 per tonne whilst levies on barley and maize at their highest, were, only about $A30 per tonne.
GRAPH I
PRICES OF CERTAIN AGRICULTURAL PRODUCTS IN THE EEC IN RELATION TO WORLD PRICES
(EEC threshold prices as percentage of world prices)

Source: Commission of the European Communities, The Agricultural Situation in the Community, 1974 and 1975 Reports, Part I.
In addition to the EEC frontier adjustments for cereals over the last three years there have been other measures designed to influence internal consumption and production. On the consumption side, the run-down in the Community's wheat supplies resulted in the denaturing premium being discontinued in early 1974. The main objective of discontinuing this premium was to increase domestic food wheat supplies by allowing a considerable quantity of soft wheat, which had been used previously for animal food, to be available for human consumption.

Cereal production has not been particularly encouraged by the annual increases in support price levels, which have tended to be about the same as the average increases accorded most other agricultural products covered by the CAP. A new device designed to improve price relativities between the various cereals was adopted in early 1976 to encourage the use of poor quality wheat as feed and to avoid the need for denaturing premiums. To this end, a lower intervention price for non-baking quality wheat has been established for the 1976-77 season onwards.

Sugar

In many respects, developments in the world sugar market over the last four years have been similar to those in the world cereals market and to a large extent Community responses have also been similar. After rising steadily during 1972 and 1973, world sugar prices in 1974 soared to record levels mainly as a result of poor harvests in some major producing countries.

The enlarged Community was affected by supply shortages caused by disappointing beet harvests, an unexpectedly large growth in consumption levels in 1973-74 and by deliveries from some developing Commonwealth countries being below supply commitments. At the end of 1974 the price of white sugar on the world market was about three times the EEC threshold level.

It is against this background that the EEC Commission adopted a series of trade and production measures to ensure adequate supplies to the domestic market. Consequently, for the first time since the introduction of the common organisation of the EEC sugar market in 1968, export levies on unprocessed sugar were introduced at the end of 1973 and import levies were discontinued. In addition, in February 1974 the Commission also introduced a special export levy on syrups and other sugars to avoid possible exports of Community sugar in this form, and in December of that year an export tax was introduced on sugar contained in processed products. The system of export levies was maintained throughout 1974 and for most of the first half of 1975. Nevertheless, world sugar prices declined sharply during early 1975 and in June of that year import levies were re-introduced.

Broadly speaking, the trade measures adopted by the Community with respect to sugar were parallel to those introduced for cereals.

(8) This applied initially only to quota sugar production. However, it was extended during 1974 so that sugar produced over and above the maximum quota was subject to 80% of the export levy. Community exports of 'over quota' sugar (sometimes called 'C' quota) have at times been substantial, for example 665 000 tonnes in 1973-74.

(9) In 1973-74 about 225 000 tonnes of sugar were exported by the EEC in the form of manufactured goods.
However, an important difference was that in the case of sugar the Community undertook specific action to encourage imports. For example, in October 1974 the Community decided to subsidise sugar imports in order to compensate for supply deficiencies, particularly in the U.K. and Italy. These were brought about mainly by shortfalls in deliveries by other Commonwealth countries. Under this arrangement some 500 000 tonnes of sugar were imported and the total cost of the import subsidies was about 140 million units of account (1 unit of account is approximately equivalent to $1). A further significant development regarding EEC sugar imports occurred at the beginning of 1975 with the negotiation of preferential sugar trade arrangements with the EEC's associated countries in Asia, the Caribbean and the Pacific (the ACP countries).(10) Under these arrangements the ACP countries are guaranteed an annual market in the EEC of 1.3 million tonnes of sugar, at prices determined annually by negotiation.

Sugar production over recent years in the enlarged EEC has not shown any significant change and has generally been below self-sufficiency levels. Consequently, important steps were taken to encourage sugar production in 1975-76. As with cereals, however, these steps involved adjustments to the existing regulatory mechanism and did not involve the adoption of new measures. Community sugar production in 1975-76 was encouraged both through an expansion of production quotas and through a substantial lift in the minimum price for sugar beet. Production quotas were increased in 1975-76 by 25% to 13.2 million tonnes(11) while the minimum (guaranteed) price for quota sugar beet production was increased by 15% (compared with an increase of 7.5% in 1974-75).

Prior to the establishment of 1976-77 season prices, the Commission anticipated a turnaround in the supply position for the EEC leading to a possible exportable surplus in 1976. Therefore, no further measures were considered necessary to encourage increased community sugar production, and the minimum beet price for 1976-77 was increased by only 8% in line with the overall increase for other farm products. There was also a reduction again in 'B' quota sugar beet from 145% to 135% of the basic, or 'A', quota which was not increased. In addition, the price differential between 'A' and 'B' quota beet was re-introduced.

(10) The ACP countries are all developing countries and have in the past been colonies of the present EEC member countries. They include several countries of the British Commonwealth. To a large degree the ACP preferential sugar arrangements replace the Commonwealth Sugar Agreement (C.S.A.) which expired at the end of 1974. Australia was a member of the C.S.A. which involved the supply of sugar to the U.K. but is not included in these new sugar arrangements.

(11) Sugar production in the EEC is largely regulated by production quotas which are allocated to factories and hence to sugar beet producers. There are two classes of quota, namely 'A' and 'B'. Prior to 1975-76 'A' quota production received a price premium above 'B' quota. For 1975-76, however, the minimum price for production under both quotas was made identical. Nevertheless the system still differentiated between the two quota types. For 1975-76, 'A' quota was increased from 7.82 million tonnes to 9.136 million tonnes and 'B' quota was increased from 35% to 45% of 'A' quota.
Beef and Veal

Tight world supplies and rising demand in conjunction with increases in the volume of international trade resulted in prices for beef and veal reaching historically high levels in 1973. However, unlike the situation in the cereals and sugar markets, these high world prices were not sustained in 1974 and in fact prices and trade turned sharply downward to extremely depressed levels. This was caused initially by a slowing of world demand growth and significantly increased world supplies. Within the Community, cattle slaughterings in 1974 increased by about 21%, partly as a result of greatly increased feed costs, while consumption rose only marginally. (12) There was a further increase in slaughterings of about 3% in 1975 with only a slight increase again in per capita consumption. Declining beef market prices and increasing farm costs adversely affected producers' incomes while at the same time there was a substantial increase in EEC intervention stocks which had previously been at negligible levels. In response to this situation the Community introduced a variety of trade and production measures designed to maintain the domestic market and to support market prices. However, apart from a few important exceptions most of these measures have been of an administrative nature taken within the framework of the existing beef and veal regime. (13)

While several measures were adopted in 1974, the two most important were the suspension of import licences for beef from non-EEC countries and the introduction of slaughter premiums for beef producers. The suspension of EEC beef and veal import quotas in July 1974 has meant that, apart from small quantities of beef and veal entering the EEC under the levy-free quotas of GATT (14), the Community beef market is effectively closed to major beef exporters such as Australia. This virtual embargo on beef imports by the EEC has continued into 1976 although as a result of steps approved during 1975 there has been some slight relaxation in the restrictions. A limited and relatively small number of store cattle from Yugoslavia, Poland and Austria were allowed entry to the EEC during the northern summer of 1975 and a small quantity of boned beef from four of the ACP countries is also permitted entry on a continuing basis in accordance with predetermined quotas. In addition, a special export-import scheme was introduced as from June 1975, allowing the importation of up to 50 000 tonnes of beef into the Community by September. (15) The scheme was then relaxed slightly to allow the import


(14) Within the framework of GATT the EEC has granted countries which are exporters of frozen beef an annual export quota which is not subject to the common customs tariff. This quota, which is 38,500 tonnes in 1976, falls into two parts: a consolidated duty-free quota, and a quota which is duty free yet liable to compensatory taxes if the offering price is inadequate.

(15) From June to September 1975, import licences were issued for a total of 15,344 tonnes of meat under this scheme.
of two tonnes for each one tonne previously exported, until finally, at the end of December, the Commission decided to abolish it. It was replaced by a more usual linking system which had been used previously by the Community and which is still currently operating. Under this system the purchase of one tonne of intervention meat confers the right, in principle, to import an equivalent quantity. Although these schemes have permitted the entry of certain qualities of beef not readily available in the EEC, they have nevertheless been essentially cosmetic and have had an insignificant effect on Community beef trade.

Overall, despite the partial easing of import controls during 1975 and 1976, it is apparent that in future the EEC beef import regime is likely to be more protective than it was prior to the imposition of the import embargo in 1974. The Commission has proposed that the import levy system should be more restrictive when the embargo is eventually lifted.

This will be achieved by tightening up the import levy procedures. For example, when the internal market price (reference price) is at a level between 98% and 100% of guide price (the price that the authorities would like to be achieved) then the basic import levy is charged, equal to the full amount between c.i.f. import price and guide price. However, only when reference price reaches 112% of guide price is the import levy reduced to zero. Under the previous arrangements this occurred when reference price was 106% of guide price. At the other extreme the levy to be charged under the new arrangements could rise to as high as 130% of the basic levy (the previous maximum was 100%) when reference price falls below 90% of guide price.

The slaughter premium system which was introduced in August 1974 represented an attempt by the EEC to encourage cattle producers to temporarily withhold their cattle from the market and to encourage the orderly marketing of cattle through the autumn and winter. The system involved a flat rate payment per head on finished cattle rising from the equivalent of about $A20 in August 1974 to about $A80 in April 1975. This was in addition to the return obtained through the supported market price. The provision of direct assistance of this type was a departure from the more traditional Community approach which has relied primarily on high support prices to maintain producer returns. The above arrangements were replaced in May 1975 by a system of variable slaughter premiums. The aim of this system, which was introduced on the initiative of the U.K. and was optional to member countries, was to provide beef producers with a predetermined guaranteed return. Under this system the difference between the market price and the guaranteed unit return was made up by a premium, the cost of which was met partly from Community funds and partly by the member country concerned. The premiums paid to producers varied according to the state of the beef market. An essential feature of the scheme was that the premium could not be paid on beef sold into intervention. This scheme, which ran until April 1976, was similar in concept to the U.K.

deficiency payments scheme which was in effect prior to that country's accession to the EEC. (17) As a concession to the U.K., that country has been permitted to continue operating the premium system in the 1976-77 marketing year but in a modified form involving lower payments.

From 1974 through 1976 the EEC has been confronted for the first time with major problems in the beef sector. In response, a large number of ad hoc and temporary measures have been adopted in an effort to protect the domestic EEC market, to support producers' incomes and to reduce intervention purchases. Most of these have been taken within the framework of existing EEC beef policy, although measures such as the variable slaughter premium represent an alternative form of support to intervention and hence a significant development in terms of Community beef market regulations. However, it now appears that these may be phased out completely after the 1976-77 marketing season as moves have been made already in this direction. A further important development was the unilateral action taken by some member countries to support their domestic beef industries even though such action contravened the rules and the spirit of CAP. This is discussed in detail in a later section. Such developments indicate the problems and difficulties involved in reconciling, in a situation of severe market strain, the interests of various countries by means of a single all encompassing regional policy.

Dairy Products

Since the current Common Market arrangements for milk and milk products were introduced in 1968, the EEC dairy sector has been characterised by very high support for market prices relative to world prices (Graph I) and a consequent tendency for the sector to periodically accumulate large intervention stocks, particularly of butter. In fact, the Commission has described the EEC milk sector as having a 'persistent structural production surplus in relation to possible outlets' (18) and at various times during the past five years the EEC has amassed huge stocks of both butter (450 000 tonnes in July 1973) and of skimmed milk powder (1.3 million tonnes in May 1976).

Despite this tendency towards excess production, the EEC has introduced only limited measures to change the structure of its dairy industry and to make it more responsive to domestic and world market developments. Traditionally the EEC has sought to regulate domestic dairy production by manipulating support price levels and to dispose of a major portion of its accumulated surpluses on export markets by means of substantial export subsidies. In 1973, for example, some 200 000 tonnes of butter were shipped to the USSR with an export subsidy at a level in excess of $A1200 per tonne. At the same time, the intervention price for butter was reduced while support for other dairy products was increased and this tended to make butter production less attractive. The Community also introduced some special butter disposal measures in 1973 including sales at concessional prices to manufacturers and to various institutions.

While these measures resulted in a significant reduction in butter stocks, other EEC measures, in conjunction with market forces, have

(17) Under this scheme U.K. cattle producers received direct payments from the government on the difference between the market price of cattle and a predetermined guaranteed price which was fixed annually.

(18) Commission of the European Communities, op. cit., p. 47.
subsequently encouraged increased production and stocks of SMP. For example, there was a 22% rise in the intervention price for SMP in 1973-74 and in excess of 25% in 1974-75. While there was an overall increase in Community production, consumption declined in both 1974 and 1975. This came about mainly as the result of a decline in SMP utilisation in livestock feedstuffs. In addition, the situation on the world market did not allow the disposal of the bulk of surplus production as exports. Consequently, there was a build-up in Community SMP stocks in 1974 and 1975, particularly in the latter year. The EEC's approach to this was to re-introduce export restitutions, to raise subsidies on the use of SMP for stockfeed and to increase SMP food aid shipments. Also, the intervention price for SMP was increased by only 7% for 1975-76 compared with a 14% increase for butter.

In March 1976 despite EEC SMP stocks of over 1.2 million tonnes the Council again rejected more radical reform measures proposed by the Commission and opted for the reinforcement of existing policies. Thus, in the 1976-77 price package the intervention price for SMP was again increased by a lesser amount than for butter. A scheme was agreed upon to enforce the incorporation of SMP in compound animal feeds and it was decided to increase shipments of SMP as food aid. The subsidy for feeding SMP to calves was also increased.

The above measures taken by the Community are all of a short-term nature and designed to alleviate an excess supply problem confronting one or more of the dairy products. The only attempt in recent years to make basic long-term changes to the dairy sector as a whole was the dairy-to-beef conversion scheme which was re-introduced in 1973 after being suspended in 1971. The major objective of this scheme was to encourage producers, through subsidies, to switch from dairy to beef production. The scheme appears to have had little impact on dairy industry adjustment, the conversion premium being granted on only about 1% of the Community's dairy cow population, and in view of the depressed beef market it was discontinued at the beginning of 1975.

Another recent development for the EEC dairy industry has been the increasing use of consumer subsidies within the Community to encourage the consumption of dairy products. Subsidies on dairy consumption are common throughout the EEC and are particularly large in the U.K. (current consumer subsidies on butter of about $A225 per tonne). A part of the U.K. butter subsidy is met from Community funds. While consumer subsidies have helped to expand dairy consumption in the Community the cost of such subsidies has been immense (for example, in 1974 EEC expenditure on price subsidies for dairy products amounted to the equivalent of about $A650 million) and they have not significantly reduced the tendency of the EEC to produce periodic dairy surpluses.

The Impact of Major Economic Problems on European Agriculture

Largely as a result of changes in supply/demand balances there have been numerous regulatory and other adjustments to the common

---

organisation of the EEC's major agricultural commodity markets over the past five years. In addition, this period has been one of great economic and monetary instability and these developments have had a significant effect on the operation of the CAP. Of fundamental importance in this respect was the severe economic downturn in EEC economies (and in other industrial economies) during 1974 and 1975 and the evidence of increasing economic disparities between member countries. The economic indicators shown in Table No. 2 highlight the economic instability in recent years and also the serious deterioration in economic circumstances, particularly the widespread negative GDP growth that occurred in 1975. The high degree of monetary instability is reflected in the number and extent of exchange rate variations amongst member countries (Graph II).

These economic and monetary developments have had a major and pervasive impact on European agriculture. There has been a steep rise in the price of EEC farm inputs, particularly in 1974 when they rose by over 18%. This placed great pressure on the incomes of many European producers, especially beef producers. In fact, the squeeze on beef producers' margins was such that some EEC countries have taken independent action to protect their beef industries. Furthermore, the high cost of support in times of economic recession, accompanied by widespread inflation and the spread of consumerism, fostered increasing criticism of the cost of the CAP, especially amongst the major food importing member countries which bear a disproportionate share of the cost of farm support. The exchange rate fluctuations have resulted in the introduction of a system of compensatory measures which have complicated the operation of the CAP and threatened the unity of the Community's agricultural markets.

Monetary Adjustments and Intra-Community Farm Trade

One of the basic principles of the CAP is the harmonisation of prices of agricultural products throughout the EEC. These common prices are fixed in terms of the Community's unit of account (UA) by agreement between the Ministers of Agriculture of the member countries. The UA which has its value fixed in relation to gold (1UA = 0.8887 grams of fine gold) is the basis of the management of the common organisation of markets.(20) The currency of each member country has an official parity relationship to gold and hence to the unit of account. During the past five years there have been several official parity changes but more important has been the decision of individual member countries to allow their exchange rates to float. As a result of floating, the market values of individual member currencies differ from the official parities used in determining domestic agricultural prices. This has necessitated the introduction of border compensatory measures to prevent the intra Community movement of agricultural commodities based solely on this monetary aberration.

Changes in the official gold parity of an EEC currency have a more or less automatic effect on domestic agricultural prices. In the case of a devaluation the prices expressed in local currency rise, while in the case of a revaluation they fall. A fall in agricultural prices

(20) The unit of account in the Community has a twofold objective, namely to prevent financial contributions agreed jointly from being affected by unilateral decisions and to enable authorities to establish common prices.
Table No. 2
ECONOMIC INDICATORS IN MAJOR EEC COUNTRIES

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Growth of Real GDP(b)</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>France</td>
<td>5.5</td>
<td>5.5</td>
<td>6.5</td>
<td>3.9</td>
<td>-2.4</td>
<td>6.3</td>
</tr>
<tr>
<td>Germany (GNP)</td>
<td>2.7</td>
<td>2.9</td>
<td>5.3</td>
<td>0.4</td>
<td>-3.4</td>
<td>5.5</td>
</tr>
<tr>
<td>Italy</td>
<td>1.6</td>
<td>3.4</td>
<td>6.3</td>
<td>3.4</td>
<td>-3.7</td>
<td>1.5</td>
</tr>
<tr>
<td>U.K.</td>
<td>1.7</td>
<td>3.4</td>
<td>5.2</td>
<td>-0.1</td>
<td>-1.6</td>
<td>2.3</td>
</tr>
<tr>
<td>Netherlands</td>
<td>4.5</td>
<td>4.5</td>
<td>4.2</td>
<td>3.3</td>
<td>-1.0</td>
<td>4.0</td>
</tr>
<tr>
<td><strong>Inflation(b)</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>France</td>
<td>5.5</td>
<td>5.9</td>
<td>7.3</td>
<td>13.7</td>
<td>11.7</td>
<td>10.5</td>
</tr>
<tr>
<td>Germany</td>
<td>5.2</td>
<td>5.8</td>
<td>6.9</td>
<td>7.0</td>
<td>6.0</td>
<td>4.8(c)</td>
</tr>
<tr>
<td>Italy</td>
<td>4.8</td>
<td>5.7</td>
<td>10.8</td>
<td>19.1</td>
<td>17.0</td>
<td>20.0</td>
</tr>
<tr>
<td>U.K.</td>
<td>9.4</td>
<td>7.1</td>
<td>9.2</td>
<td>16.0</td>
<td>24.2</td>
<td>16.0(c)</td>
</tr>
<tr>
<td>Netherlands</td>
<td>7.6</td>
<td>7.8</td>
<td>8.0</td>
<td>9.6</td>
<td>10.2</td>
<td>8.5</td>
</tr>
<tr>
<td><strong>Unemployment(d)</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>France</td>
<td>2.1</td>
<td>2.3</td>
<td>2.1</td>
<td>2.3</td>
<td>3.8</td>
<td>4.2</td>
</tr>
<tr>
<td>Germany</td>
<td>0.7</td>
<td>1.0</td>
<td>1.3</td>
<td>2.7</td>
<td>4.9</td>
<td>5.2</td>
</tr>
<tr>
<td>Italy</td>
<td>3.1</td>
<td>3.6</td>
<td>3.5</td>
<td>2.9</td>
<td>3.3</td>
<td>3.5</td>
</tr>
<tr>
<td>U.K.</td>
<td>3.0</td>
<td>3.4</td>
<td>2.6</td>
<td>2.5</td>
<td>3.9</td>
<td>5.2</td>
</tr>
<tr>
<td>Netherlands</td>
<td>1.8</td>
<td>3.0</td>
<td>2.3</td>
<td>2.8</td>
<td>4.1</td>
<td>4.4</td>
</tr>
<tr>
<td><strong>Balance of Payments</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>France</td>
<td>0.53</td>
<td>0.27</td>
<td>-0.69</td>
<td>-6.00</td>
<td>0.30</td>
<td>-2.75</td>
</tr>
<tr>
<td>Germany</td>
<td>0.17</td>
<td>0.41</td>
<td>4.31</td>
<td>9.70</td>
<td>3.70</td>
<td>2.00</td>
</tr>
<tr>
<td>Italy</td>
<td>2.03</td>
<td>2.57</td>
<td>2.67</td>
<td>-8.00</td>
<td>-0.60</td>
<td>-2.00</td>
</tr>
<tr>
<td>U.K.</td>
<td>2.56</td>
<td>0.07</td>
<td>-2.88</td>
<td>-8.70</td>
<td>-3.80</td>
<td>-2.50</td>
</tr>
<tr>
<td>Netherlands</td>
<td>0.17</td>
<td>1.05</td>
<td>1.77</td>
<td>2.00</td>
<td>1.60</td>
<td>2.50</td>
</tr>
<tr>
<td>EEC</td>
<td>4.94</td>
<td>5.47</td>
<td>0.50</td>
<td>-12.00</td>
<td>1.25</td>
<td>-5.25</td>
</tr>
</tbody>
</table>

**Index Numbers**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>France</td>
<td>115.9</td>
<td>132.8</td>
<td>149.1</td>
<td>119.5</td>
<td>na</td>
<td>na</td>
</tr>
<tr>
<td>Germany</td>
<td>103.9</td>
<td>115.7</td>
<td>109.5</td>
<td>98.0</td>
<td>na</td>
<td>na</td>
</tr>
<tr>
<td>Italy</td>
<td>115.5</td>
<td>117.5</td>
<td>150.1</td>
<td>148.7</td>
<td>na</td>
<td>na</td>
</tr>
<tr>
<td>U.K.</td>
<td>104.7</td>
<td>114.0</td>
<td>124.5</td>
<td>113.5</td>
<td>na</td>
<td>na</td>
</tr>
<tr>
<td>Netherlands</td>
<td>105.6</td>
<td>114.2</td>
<td>117.9</td>
<td>102.2</td>
<td>na</td>
<td>na</td>
</tr>
</tbody>
</table>

(a) Forecasts. (b) In consumer prices. (c) National Accounts implicit consumption deflator. (d) 1976 figures are for the first quarter only. (e) "Wages of farm workers' plus 'other income' = net value added at factor cost less 'rents' and 'interest payments'. (f) Adjusted for the trend of the GNP deflator. na, not available.

Sources: OECD, Economic Outlook (various issues); Commission of the European Communities, The Agricultural Situation in the Community, Report 1975, Part III.
GRAPH II

EXCHANGE RATE ADJUSTMENTS OF SELECTED EEC CURRENCIES

(Percentage change against the U.S. dollar between 1971 and 1976)

Source: OECD, Main Economic Indicators (various issues)
that is explicit in an official currency revaluation disadvantages domestic agricultural producers and, consequently, countries that have revalued, such as Germany and the Netherlands, have cushioned this impact by granting special national producer subsidies or compensation. For example, between 1970 and 1974 German farmers received revaluation compensation equivalent to about $A2000 million and this assistance will not be finally phased out until the end of 1978. A significant part of this has come from Community sources.

With floating exchange rates there are no corresponding automatic adjustments made to support prices in terms of units of account which therefore continue to be converted into national currency at the official parity. However, the official parity no longer corresponds to the value of a member's currency as determined by foreign exchange markets. In terms of market exchange rates for currencies, this leads to a disparity between the agricultural price levels guaranteed in the various member countries and tends to disrupt the organisation of Community markets. For example, producers in a member country whose currency has floated downwards would be inclined to direct their products towards an intervention centre in a member country with an appreciating exchange rate as this would give them a higher return in terms of their country's currency. Since 1971 most of the EEC currencies have been floating either jointly or individually and this has necessitated a system of frontier compensatory payments (referred to as monetary compensatory amounts, or MCAs).

The purpose of these compensatory payments as applied to intra-Community trade is to offset the difference between the official exchange rates applied under CAP and the value of the currencies as determined primarily by market forces. When a currency is revalued on foreign exchange markets without a corresponding change to its official parity, compensatory payments are charged on agricultural imports and granted for agricultural exports to offset the difference between the market and official parities. Alternately when a currency is devalued, payments are charged on exports and granted on imports. Compensatory payments are also applied in a similar manner to EEC trade with non-member countries and are either added to or, as the case may be, deducted from import levies and restitutions.

The operation of the frontier compensatory payments systems has become increasingly complicated as a result of the enlargement of the EEC and more importantly by the frequent differences between the official and market parities of member currencies since 1973.(21) Farm support price levels, in terms of national currencies, have lost their comparability between member countries and the free flow of agricultural products throughout the Community has been impeded by the imposition of border taxes and subsidies. Frequent alterations in the levels of compensatory payments have also increased the uncertainty of intra-Community farm trade.

(21) The three new member countries, the U.K., Ireland and Denmark, apply accession compensatory amounts which will be eliminated in six stages. For those member countries that are floating in isolation, France, Italy, the U.K. and Ireland, the EEC Commission fixes the frontier compensatory amounts each week. For those countries that are floating together in the so-called 'snake', Germany, Denmark and the Benelux countries, compensatory amounts do not change during the marketing year.
In fact it has become clear that while this mechanism has enabled the CAP to function, despite frequent exchange rate fluctuations, important costs have also been involved. In the first place, the direct financial burden of monetary compensatory measures is considerable and in the first six months of 1975 alone, for example, Community expenditure for this purpose was estimated by the Commission to have been about 299 million UA.\(^{(22)}\) In addition, compensatory payments have also caused severe distortions to resource allocation in Community agriculture and to agricultural trade flows within the Community.

The result of compensatory payments has been that agricultural production and consumption within member countries of the Community have been shielded from the full effects of currency changes. Normally a revaluing country will benefit from a relative decline in the unit cost of its imports (in terms of its currency) while at the same time it will be disadvantaged by a relative decline in the unit value of its exports (again in terms of its currency). Consequently, in broad terms, a revaluation will tend to benefit consumers through cheaper imports and disadvantage exporters through reduced export returns. The reverse is applicable in the case of a country with a depreciating currency. In the Community, however, the normal economic consequence of currency adjustment have not been allowed to occur. For example, in countries with relatively strong currencies, such as Germany and the Netherlands, the monetary compensatory mechanism has tended to benefit producers, penalise consumers and ensure the continuance of the strong balance of payments position of these countries. Thus the direct result of the imposition of direct charges on agricultural imports and subsidies on agricultural exports is to partly offset the expected impact of an appreciating currency.

Furthermore, monetary compensatory payments have also influenced the allocation of resources within the agricultural sector and between agriculture and other sectors. For example, in Italy in mid-1974 border compensatory payments of about 28% of market price were being levied. This represented the extent to which Italian farm prices trailed behind the general level of prices in that country. The result was a corresponding price distortion between the farming sector and the rest of the economy.

The difficulties involved in attempting to maintain common price levels have encouraged the Community to adopt measures to improve the functioning of internal agricultural markets during monetary instability. A major objective has been to reduce the size and importance of compensatory payments. This has been achieved, at least partially, by moving from a system whereby agricultural prices (in national currencies) are based on the official gold parity to one where farm prices are derived from so-called representative exchange rates which are more in line with actual conditions on the exchange markets. The representative, or 'green' rates, indicate the relationship between the unit of account and national currencies.\(^{(23)}\)


\(^{(23)}\) Representative rates were first set for the currencies of the three new member countries. Rates were subsequently set for the Italian lira and the Dutch guilder. In February 1975 the Council set representative rates for the currencies of all member countries.
Representative rates in the EEC have been primarily used to reduce the compensatory payments applicable on those currencies that have undergone a significant depreciation such as the lira and the pound (see Graph III). Since the effect of adjusting the representative rates is similar to a change in a currency's gold parity, common farm prices expressed in national currency have risen in those countries with relatively weaker currencies.

The Community's attention has also been focused on the composition and application of the unit of account. The unit of account defined in terms of gold and entailing a conversion procedure, based on currency parities, raised no major problems for as long as fixed exchange relationships prevailed in the international monetary system. However, the floating of exchange rates away from the official gold parities has meant that the conversion operations provided for in Community regulations have lost the foundation upon which they were based. There is clearly a need to devise a more flexible unit of account enabling the present disparities between all the Community currencies to be reconciled, whether they are floating jointly or separately. Consequently, to modify the undesirable effects of floating currencies the Commission proposed, in December 1974, a new type of unit of account based on a 'currency basket' of members' currencies. Under this system sudden variations in the unit of account would be absorbed. A change in the exchange rate of a currency affects the value of the unit of account only in terms of its relative weight in the basket. The Commission believes that a 'currency basket' type unit of account would constitute a step towards the establishment of a Community monetary identity. While there are clear advantages with the currency basket concept there are no plans at present for its introduction to the CAP. This is likely to require lengthy bargaining by member countries and complex administrative adjustment of EEC agricultural trade arrangements.

However, despite the difficulties and costs involved in the administration of the current CAP monetary arrangements, particularly those arising from the MCA system, the Community is apparently unable to agree on any permanent solution to these problems. The Commission is in favour of complete abolition of MCAs and has suggested that the system be phased out in stages to avoid excessive disruption. But, on recent indications, the many inter-country compromises which are an essential part of the CAP decision making process will make this objective very difficult to attain. For example, in line with its policy, the Commission put forward as part of its 1976-77 price proposals that the Dutch and Belgian MCAs be eliminated altogether and that those of other members be cut by varying amounts by the adjustment of representative rates. However, the Benelux countries were unwilling to have the price increases for their farmers reduced to the extent implied by these proposed adjustments and the U.K. successfully resisted devaluation of its

(24) A fore-runner in this respect was the first unit of account, the EURCO, which was introduced in 1973 by the European Investment Bank. Several loans denominated in this unit of account have been issued by the Bank. In addition the Special Drawing Right (SDR) of the IMF is also based on a basket of currencies concept.

GRAPH III
ADJUSTMENTS IN EEC REPRESENTATIVE EXCHANGE RATES AND IN MONETARY COMPENSATORY AMOUNTS


mca: monetary compensatory amounts
er: exchange rates
rp: representative 'green' rates
representative rate as this would have added to the consumer food price increases brought about by the annual prices agreement. Therefore, the Commission's moves towards phasing out the MCAs were considerably diluted.

The rapidly escalating cost of the MCAs in early 1976 brought about another attempt to solve the problems arising from use of the system. The Commission estimated that the cost to the EEC's 1976 budget would rise from the 248 million UAs originally provided for to 800 million UAs as a result of depreciation of the pound and the lira. A special meeting of the Council of Agriculture Ministers was held in April, therefore, to consider how to alleviate the situation. Once again no fundamental solutions were reached and it was decided instead to devalue the representative rate of the lira by about 6% and to transfer to the exporting country the payment of MCAs on intra-Community sales of agricultural products to Italy and the U.K. This latter measure is basically an accounting device which will have the effect of reducing the apparent cost of the MCAs as expressed in the Community budget i.e. making the system appear cheaper. (26)

The MCA system continues to operate, therefore, despite the considerably increased cost in 1976 and the Commission's policy in favour of its abolition and the restoration of unity of agricultural markets in the Community.

National Aid Measures in Individual Member Countries

An important new feature affecting European agriculture over the past three years has been the extent to which individual member countries have taken unilateral action with respect to policies affecting their agricultural production and trade. These actions which have been taken outside the provisions of the CAP and without Council endorsement have stemmed from either a serious deterioration in the economy of a particular country or in the economic circumstances confronting an individual industry.

The chief example of the former was the import restrictions imposed by Italy in May 1974 on a wide range of products including agricultural products. The aim of these measures was to curb domestic demand and to improve the country's serious balance of payments situation caused largely by the greatly increased cost of oil imports. These import restrictions, as applied to agricultural products, involved the deposit by importers of 50% of the c.i.f. value of the imports for six months in the Bank of Italy, interest free.

(26) This apparent reduction in the cost of MCAs occurs because the Community's budget is drawn up in units of account different to those used for the CAP. Exchange rates used for budget purposes are still derived from pre-1971 (Smithsonian agreement) parities while the 'representative' rates used in agriculture are in fact closer to actual market exchange rates. Therefore, the stronger currencies of recent years (e.g. the Deutsche Mark) are now undervalued in budget terms and the weaker currencies (the pound and the lira) are now overvalued. Because of these anomalous conversion rates, the EEC farm budget appears to cost less if more operations are conducted in the strong currencies e.g. by paying MCAs in Germany rather than in the U.K. or Italy.
In view of the threat to the unity of EEC agricultural markets posed by these restrictions, the Commission reached a compromise agreement with the Italian Government for a lifting of the deposits for all agricultural products except beef, on which it remained at a level of 25%, in return for a number of concessions. These included a 12.5% depreciation of the 'green' lira (the representative rate) and the temporary suspension of compensatory payments on beef and veal imports for a period of three months together with a reduction of compensatory payments on other Italian agricultural imports. The import deposit for beef was not lifted until March 1975.(27)

Although the Italian restrictions on agricultural imports were almost entirely removed shortly after they were first imposed they provided a good example of a member country being obliged by domestic economic conditions to take independent action regardless of the disruptive effects of such action on the free flow of agricultural commodities within the Community.

An example of unilateral action to support a particular industry or industries occurred in 1974 when France and Belgium introduced national subsidies to support their ailing livestock sectors. In July 1974, the French Government announced a group of farm income subsidies valued at about 2000 million francs ($A282 million) designed to assist livestock and horticultural producers. In the beef industry the measures included a premium of 200 francs per head (about $A28) payable for the first fifteen breeding cows on a farm and in the pig industry a premium of 100 francs per sow, also payable on the first fifteen sows per farm. At the end of July the Belgium Government announced a number of direct, once and for all, subsidies to beef producers and a slaughter premium for pig producers. For beef producers the subsidy was the equivalent of $A32 per head for the first ten animals and the equivalent of $A24 per head for the next ten.

These national income support measures contravened the regulations and the spirit of the Common Agricultural Policy and met severe criticism from other Community members and the Commission. Nevertheless, the impact of large increases in farm costs and the worsening income position of many EEC farmers, especially in the livestock sector, was widely recognised and resulted in the EEC Council agreeing in September 1974 to an increase of 5% in Community farm prices. At the same time, Germany, through its threat to veto the farm price increases, extracted an agreement from other countries to phase out national aids and an acceptance in principle to review the entire operation of the CAP, which resulted in the 'Stocktaking' exercise.

Despite this agreement and earlier criticism it appears that the Council subsequently adopted a more accommodating attitude towards national measures to assist domestic beef producers. This was exemplified in France being authorised by the Council in May 1975 to pay a breeding cow subsidy, similar to its 1974 scheme, in lieu of slaughter premium payments.

(27) A similar import deposit scheme was re-introduced by Italy for a period of three months from May 1976 onwards, but on this occasion the action was taken with the agreement of the other EEC members.
More recently, the Council has been embroiled in a dispute between France and Italy over wine trade. This originated when France, in response to pressure from domestic producers, imposed a unilateral ban on imports of Italian wine in April 1975. The Commission informed the French Government that this action was illegal and, with the Italian Government, proposed court action against France under the Treaty of Rome articles guaranteeing free trade throughout the Community and under the common wine market regulation banning the operation of quantitative restrictions on produce from other member countries. France lifted the import ban following a special meeting of the Council at which a number of concessions, aimed at alleviating the wine surplus situation, were adopted. However, France did not consider these adequate and in September 1975 imposed an import tax of up to 15% on Italian wine. The Commission informed France that this action was also a violation of the EEC free trade rules but the tax was not removed again until April 1976 following a reduction in Italian exports of wine to France and Council moves to reform EEC wine market regulations.

The above developments have highlighted the fragile nature of Community rules governing agricultural production and trade in the face of determined action by individual member countries to protect their economies and their agricultural producers. On the other hand, the CAP has at the same time demonstrated a considerable resilience in its ability to withstand the internal strains caused by these actions. Member states have also shown a willingness to compromise and to make adjustments to the rules, thus preventing the structure breaking apart.

**Consumer Interests and Cost of the CAP**

One of the objectives of the Common Agricultural Policy as specified in the Treaty of Rome is to ensure that supplies reach consumers at reasonable prices. The Treaty does not, however, define what is reasonable. Despite this objective the operation of the CAP has reflected a strong producer bias. This has been due in part to the strength of the influence of agricultural interests within the Community, in conjunction with the continuing attempt to maintain producers' incomes at reasonable levels in relation to those earned in other economic sectors. As a result, for much of the time since the inception of the CAP, producer prices have been maintained at levels which have been in some cases well above world prices. Developments in recent years such as EEC enlargement, double digit inflation and the economic recession, however, have resulted in increasing attention by EEC consumers and member governments to issues such as the cost of food and the cost of agricultural support.

Prior to 1973, retail food prices within the Community, although relatively high, were also relatively stable showing only moderate annual increases. The increases since 1973 have been much greater largely as a result of sharp rises in the cost of agricultural production and subsequent increases in farm support prices. However, to some extent the CAP successfully insulated the EEC from the unprecedented increases in the prices of many agricultural commodities on world markets. In fact in 1974 the increase in consumer prices for foodstuffs was 10.4% in the original six countries of the Community compared with 14.6% in the United States and 29.0% in Japan. In Australia the consumer food price index rose by 10.0% in 1974.
Within the enlarged Community the impact of rising commodity prices has been particularly important in the United Kingdom. Prior to EEC accession, food prices in the U.K. were relatively low compared to those in the original Community, partly as a result of the U.K.'s open import policy and its system of deficiency payments to local producers. Following the adoption, at the beginning of 1973, of the transitional arrangements of the CAP, the United Kingdom has experienced a rapid increase in retail food prices of 15% in 1973, 18% in 1974, and 26% in 1975. Imports by the U.K. of foodstuffs and beverages also increased from £2200 million in 1972 to £4200 million in 1975.

These developments were instrumental in the U.K.'s renegotiation, during much of 1974 and early 1975, of its terms of accession to the EEC. Important British objectives in the renegotiations were to make the CAP more flexible in regulating the production and marketing of agricultural commodities, to ensure that greater priority be given to the interests of consumers and to introduce 'new and fairer methods' of financing the Community budget. (28)

In the event, the U.K. obtained Community approval for a number of special arrangements designed to protect U.K. consumers from the full effects of producer price increases, in support for market prices. These measures include consumer subsidies for butter and a system of variable slaughter premiums on beef cattle. These slaughter premiums, which were referred to earlier, represent an alternative to intervention buying since they allow consumers to buy beef at lower market prices while direct subsidies are paid to producers to bring their returns from the market up to a predetermined level. The cost of the butter and the beef subsidies are borne jointly by the U.K. and the EEC.

However, despite these indications of a partial shift in emphasis towards consumer interests in recent years, progress in this direction has been only slight or has proved to be temporary. For example, the beef slaughter premium system was weakened for the 1976-77 season by Council agreement and in its modified form it involves lower payments. In addition, the Commission issued a report on the slaughter premium system in April 1976 which criticised the system on the grounds of cost and suggested that it should not become a permanent part of the EEC beef market support regime. Furthermore, consumer interests appear to have less influence on the CAP decision making process than do the agricultural producers. Unlike the farmers' lobby group, COPA, which is now virtually a part of the institutional structure, consumer groups are not yet closely involved in the consultations held prior to the annual price fixing process. In general the CAP has remained basically producer oriented.

The second and associated reason for the increasing challenge to the longstanding producer bias of the CAP is the high cost of agricultural support and the assertion that importing countries bear a disproportionate share of the cost of this support. The bulk of the EEC budget expenditure is channelled into the EEC farm sector, mainly to support agricultural producer prices through the Guarantee Section of the European Agricultural

Guidance and Guarantee Fund (EAGGF). In 1974 and 1975, for example, the EAGGF accounted for 66% and 81% respectively of total Community budget expenditure (see Table No.3). The Guarantee Section accounted for over 90% of the amount directed to agriculture in these two years. The balance of expenditure on agriculture was spent by the Guidance Section which is involved essentially in financing measures to achieve structural reform in EEC agriculture.

Table No. 3

EEC EXPENDITURE PATTERNS

<table>
<thead>
<tr>
<th>Year</th>
<th>Total Community Expenditure</th>
<th>Expenditure of EAGGF</th>
<th>Expenditure of the 'Guarantee' Section</th>
<th>Expenditure of the 'Guidance' Section</th>
<th>Total EAGGF as a share of GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>1970 (EEC-6)</td>
<td>3531 million UA</td>
<td>2804 million UA</td>
<td>2603 million UA</td>
<td>202 million UA</td>
<td>0.58</td>
</tr>
<tr>
<td>1971 &quot;</td>
<td>2357 million UA</td>
<td>1814 million UA</td>
<td>1571 million UA</td>
<td>242 million UA</td>
<td>0.34</td>
</tr>
<tr>
<td>1972 &quot;</td>
<td>3292 million UA</td>
<td>2425 million UA</td>
<td>2258 million UA</td>
<td>167 million UA</td>
<td>0.40</td>
</tr>
<tr>
<td>1973 (EEC-9)</td>
<td>4653 million UA</td>
<td>4004 million UA</td>
<td>3815 million UA</td>
<td>189 million UA</td>
<td>0.48</td>
</tr>
<tr>
<td>1974 &quot;</td>
<td>5133 million UA</td>
<td>3366 million UA</td>
<td>3107 million UA</td>
<td>259 million UA</td>
<td>0.37</td>
</tr>
<tr>
<td>1975(e) &quot;</td>
<td>6062 million UA</td>
<td>4897 million UA</td>
<td>4572 million UA</td>
<td>325 million UA</td>
<td>0.46</td>
</tr>
<tr>
<td>1976(e) &quot;</td>
<td>7577 million UA</td>
<td>5485 million UA</td>
<td>5160 million UA</td>
<td>325 million UA</td>
<td>0.50</td>
</tr>
</tbody>
</table>

(e) Estimated.


Between January 1971 and January 1975 expenditure by the EAGGF was covered from three main sources namely:

- levies and charges instituted under the CAP on trade with non-member countries,
- a progressive proportion of the Common Customs Tariff, and
- financial contributions from member countries in order to ensure a balanced budget.

As from the beginning of 1975 the third of these sources was to have been abolished and replaced by the revenue from a rate of Value Added Tax (VAT) not exceeding 1%, applicable in each member state on a uniform basis. However, the introduction of this has been delayed by an inability to agree on a uniform basis for assessment of the VAT. In the meantime the third source of revenue consists of financial contributions based on members' shares of total Community GNP.
EAGGF expenditure is not high in relation to total Community GNP, having been well below 1% in every year between 1971 and 1975. Expenditure also sometimes falls from one year to the next, as happened in 1974, for example, when it was in fact lower in real terms than expenditure in 1970. This came about largely as a result of higher world commodity prices and relatively low EEC commodity surpluses. Nevertheless, the cost of support is a contentious issue, especially among the major food importing member countries such as Germany, since in effect it involves a transfer of financial resources from these countries to major agricultural exporting countries. These countries have expressed concern at the possibility that Community farm expenditure could rise steeply if surpluses appear over a wide range of commodities. In fact this has already partly occurred in 1975 and 1976 with the build-up of EEC surpluses of beef, dairy products and wine. Estimated expenditure by the guarantee section of EAGGF in 1975 was 4572 million units of account compared with actual expenditure of 3107 million units of account in 1974. It is estimated that the budget for the guarantee section in 1976 could exceed 5100 million units of account.

As a result of the U.K./EEC renegotiations the U.K. managed at the beginning of 1975 to achieve some moderate reduction in its budget commitments. The EEC Commission has also recently acknowledged that the cost of the CAP is a major problem and in its 'Stocktaking' document it submitted various proposals directed at limiting EEC farm expenditure. These are discussed in a later section.

Despite these relatively minor developments, however, the cost of EAGGF Guarantee Section expenditure is likely to be a continuing source of problems for the Community budget. The system of agricultural support in the Community continues to generate substantial commodity surpluses which are a direct and major charge against the EAGGF. Similarly, monetary developments such as the depreciation of the pound and the lira in early 1976 also result in substantial and largely unpredictable additional expenditure while the MCA system remains in operation. Finally, although the EAGGF represents only a small fraction of total Community GNP, it is the major EEC budget item and the uneven distribution of the cost can and does cause friction within the Community.

Structural Adjustment in EEC Agriculture

Under the Treaty of Rome a priority objective of the CAP is to increase agricultural productivity and to improve the utilisation of labour and other resources in EEC agriculture.(29) It is difficult, however, to reconcile this objective with the structural imbalances in many of the EEC's commodity markets caused by the CAP mechanism. Community farmers are largely insulated from the effect of market forces

(29) Article 39(1)(a) of the Treaty of Rome states that the first objective of the Common Agricultural Policy is 'to increase agricultural productivity by promoting technical progress and by ensuring the national development of agricultural production and the optimum utilisation of the factors of production, in particular labour'.


through an elaborate system of high price supports and trade barriers which, as described earlier, have led to periodic production surpluses of several agricultural products. It is apparent that support for farm incomes through the pricing mechanism has become the main feature of the CAP system and has in practice taken precedence over the objective of efficient resource use. Community expenditure on structural reform programs, therefore, has been relatively small compared with expenditure on price support arrangements (see Table No. 3).

Nevertheless, expenditure by individual countries on structural programs is substantial. For example, in 1974 such expenditure by member countries was an estimated 3146 million units of account, which was slightly greater than the amount spent by the Community on price support under the Guarantee section of the EAGGF. The major role of the Community in the field of agricultural structural policy has been to provide some financial assistance and to co-ordinate the structural measures taken by member countries. In this respect it participates on a joint basis with member countries (with funds provided by both national and Community budgets) in projects to assist persons wishing to leave agriculture (through retraining programs and retirement premiums), in projects to assist those persons remaining in agriculture (farm enlargement programs and low interest loans) and in projects to promote development of information services and vocational training of farmers.(30)

Undoubtedly the impact of Community and national structural reform programs on resource movement and agricultural productivity has been reduced by the Community's price support arrangements which have tended to discourage and slow down the adjustment process. Nevertheless there has been a relatively high percentage movement (about 4% per annum in the original Community members) of labour out of EEC agriculture. Between 1961 and 1971, 5.5 million farmers moved out of agriculture in the EEC, while total agricultural production rose by about 20%. The average annual percentage reduction in the rural labour force in each of the member countries is shown in Table No. 4. This high level of labour outflow from the EEC farm sector has been largely responsible for the favourable levels of growth achieved in terms of labour productivity. In the ten years to 1971 the labour productivity index for agriculture in the EEC rose from 100 to 188 and for industry from 100 to 166.

Despite this favourable trend there are still important structural weaknesses in EEC agriculture. The great number of relatively small farms (in terms of area) is at least a partial indicator of this weakness. Approximately 78% of EEC farms are less than twenty hectares and these farms constitute only 30% of the total utilised agricultural area in the enlarged Community. Furthermore, the average size of farms has increased by only three hectares since 1958, bringing the average area

(30) For a detailed discussion of structural programs in member countries see OECD, Structural Reform Measures in Agriculture, Paris, 1972.
### Table No. 4

**LABOUR MOBILITY AND PRODUCTIVITY IN EEC AGRICULTURE**

<table>
<thead>
<tr>
<th>Member States</th>
<th>Average Annual Change in the Number of Persons Engaged in Agriculture</th>
<th>Growth in Labour Productivity between 1968 and 1973</th>
</tr>
</thead>
<tbody>
<tr>
<td>Germany</td>
<td>-5%</td>
<td>-5%</td>
</tr>
<tr>
<td>France</td>
<td>-4%</td>
<td>-4%</td>
</tr>
<tr>
<td>Italy</td>
<td>-4%</td>
<td>-5%</td>
</tr>
<tr>
<td>Netherlands</td>
<td>-3%</td>
<td>-2%</td>
</tr>
<tr>
<td>Belgium</td>
<td>-6%</td>
<td>-6%</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>-6%</td>
<td>-9%</td>
</tr>
<tr>
<td>EEC - 6</td>
<td>-4%</td>
<td>-4%</td>
</tr>
<tr>
<td>U.K.</td>
<td>-2%</td>
<td>-1%</td>
</tr>
<tr>
<td>Ireland</td>
<td>-3%</td>
<td>-3%</td>
</tr>
<tr>
<td>Denmark</td>
<td>na</td>
<td>-4%</td>
</tr>
<tr>
<td>EEC - 9</td>
<td>na</td>
<td>-4%</td>
</tr>
</tbody>
</table>

to 13.5 hectares in 1973. Changes in the average size of Community farms and in the total farm area within various size categories are shown in Table No. 5.

Table No. 5

CHANGES IN THE NUMBER AND SIZE OF COMMUNITY FARMS: EEC-9

<table>
<thead>
<tr>
<th>Farm Size</th>
<th>Farms in 1973</th>
<th>Annual Rate of Change 1960 to 1967</th>
<th>Annual Rate of Change 1973 to 1973</th>
<th>Utilised Agricultural Area in 1973 '000 ha</th>
<th>Annual Rate of Change 1960 to 1967</th>
<th>Annual Rate of Change 1973 to 1973</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 and under 5</td>
<td>2 296 879</td>
<td>-2.9</td>
<td>-3.7</td>
<td>5 791</td>
<td>-3.0</td>
<td>-3.8</td>
</tr>
<tr>
<td>5 &quot; &quot;</td>
<td>10</td>
<td>967 713</td>
<td>-3.5</td>
<td>-4.4</td>
<td>6 914</td>
<td>-3.5</td>
</tr>
<tr>
<td>10 &quot; &quot;</td>
<td>20</td>
<td>968 377</td>
<td>-2.2</td>
<td>-3.5</td>
<td>13 542</td>
<td>-2.2</td>
</tr>
<tr>
<td>20 &quot; &quot;</td>
<td>50</td>
<td>853 645</td>
<td>0.3</td>
<td>0.3</td>
<td>25 837</td>
<td>0.5</td>
</tr>
<tr>
<td>Over 50</td>
<td>317 539</td>
<td>1.5</td>
<td>2.6</td>
<td>36 229</td>
<td>na</td>
<td>na</td>
</tr>
<tr>
<td>Total</td>
<td>5 404 153</td>
<td>-2.3</td>
<td>-2.9</td>
<td>88 313</td>
<td>na</td>
<td>na</td>
</tr>
</tbody>
</table>


Since 1972 the Community, through the CAP, has taken a more active and concerted role in attempting to direct change in EEC agricultural structures. On the basis of Community criteria and some Community financial assistance, member countries have adopted several new structural measures. A key element in the Community's structural objectives is the concept of 'farms suitable for development'. With investment and other assistance it is proposed that such farms should be able to attain a return to labour comparable to that obtained in non-agricultural activities in the regions concerned, allowance being made for an adequate return on invested capital.

In April 1972 the EEC Council adopted three directives designed to improve farm structures. (31) The first directive focuses on the

(31) For a more detailed discussion of these directives see OECD, Agricultural Policy of the European Economic Community, op. cit., pp. 89-92.
modernisation of farms and requires member countries to introduce a selective system of aid to those farms which submit development plans and are potentially able to attain a level of income comparable to that received in the non-farm sector. The second directive concerns a system of aid to those persons wishing to discontinue agricultural activity and takes the form of an annuity for elderly farmers or a premium to other farmers to encourage them to move to alternative occupations. Land that becomes vacant as a result of these measures is allocated to farms in the process of modernisation. The third directive aims to improve the vocational guidance and training of persons engaged in agriculture, through the provision of information, advisory and counselling facilities. Under the present arrangements member countries are refunded, from the EAGGF Guidance Section, 25% of the costs incurred in the implementation of the above directives although this refund is as high as 65% for the so-called 'disadvantaged' agricultural areas, which have a higher percentage of the agricultural labour force than the Community average.

In April 1975, the Council adopted another directive which provides special assistance, through direct annual payments, to farmers in difficult farming areas, especially in hilly areas. The objective of this directive is to maintain the incomes of farmers in regions with natural disadvantages. Total expenditure over the three years of operation of the scheme is expected to be about 340 million units of account. Of this, the amount available from the EAGGF will be 25% initially, with provision for an increase in this rate in subsequent years.

The above directives indicate that the CAP is being increasingly recognised and used as a vehicle for structural adjustment in EEC agriculture. However, recent developments also highlight the problem of reconciling the productivity and income objectives of the Community's structural policy. For example, while a major purpose of present structural measures is to increase agricultural productivity through the enlargement and modernisation of farms, another aim is to reduce farm income disparities through direct income subsidies to farms in less favoured areas. More generally there is an important and fundamental conflict between the Community's measures to increase agricultural productivity and its price support activities. Under the latter, many marginal high cost farms have been assisted and supported by the influence on income levels of the high support price regimes maintained by the CAP. This consequently slows the flow of resources out of agriculture and within agriculture and has a detrimental effect on levels of productivity.

Proposals for Reform

The various economic and farm problems that the Community has encountered in recent years have been outlined in the previous sections. The major ones have been: the widespread economic depression following boom conditions which has affected the EEC and other developed nations; the periodic accumulation of commodity surpluses; the slow progress towards solving structural problems which is partly the result of the continuing need to devote the bulk of EEC budget expenditure to agricultural price support; relatively low and unevenly distributed incomes in agriculture; and monetary complications brought about by exchange rate instability and differing economic performance amongst the member countries. Although these factors have prompted a more critical examination of the CAP within the Community this has had a limited effect so far on its basic structure.
Two major reform documents have been prepared by the Commission. The Commission's 'Memorandum' on the reorganisation of the CAP was submitted to the Council in October 1973 and its 'Stocktaking' of the CAP was completed in February 1975. The first was prepared at the initiative of the Commission but the second was due largely to the instigation of the German Government, which insisted on a comprehensive review of the CAP in return for its approval of the proposed increase in EEC farm prices in September 1974.

The two documents have a great deal in common and both canvass ways and means of improving the operation of the CAP. Both documents contain various recommendations and proposals for the consideration of the Council of Ministers.

The 'Memorandum' which presents a reform program for the period 1973 to 1978 has three main objectives; namely to reduce the disequilibria on certain agricultural markets, particularly the butter market, to simplify the machinery of the common organisation of markets and to reduce expenditure under the Guarantee Section of the EAGGF. To achieve these objectives the Memorandum submitted a number of proposals including:

- That farmers should assume some degree of financial responsibility for structural surpluses, especially in the dairy sector (to be achieved for example through a variable levy on surplus production).

- That a better price relationship be established between agricultural products (based on so-called objective criteria such as the level of costs on 'modern' farms).

- That the monetary compensatory payments system be phased out by 31 December 1977.

The 'Memorandum' also called for a reduction in the number of CAP regulations, the introduction of a common organisation of the mutton and lamb market, a storage policy for cereals and, somewhat ironically, improved incentives for meat production.

Although the implementation of these proposals is not mandatory, some of the recommendations have been introduced. As explained earlier, monetary compensatory payments which are a disruptive influence on intra-Community farm trade have been reduced below what they would otherwise have been by the increasing use of representative or 'green' rates. They are still a continuing problem however. Secondly, in presenting its price proposals for the 1976-77 season, the Commission stated explicitly that in preparing its price proposals in recent years it had increasingly related them to 'modernised farms' as well as taking into

---


account the supply and demand position for individual markets. This implies that the Commission is seeking to reduce Community support through prices policy for the less efficient rural producers. Thirdly, for the 1976-77 season onwards, an attempt is being made to improve the price relativities between various cereals, as has been described earlier. Finally, the Commission agreed in September 1975 for the CAP regulation of the EEC sheepmeats sector. However, at the time of writing, the scheme had not yet been agreed upon by the Council. Basically the Commission proposals for sheepmeats would, if introduced, only affect domestic production and intra-Community trade. If in the longer term, however, the proposed regime was extended to include mechanisms to protect Community producers from non-EEC suppliers, as has been the case for other agricultural products covered by the CAP, this would have important implications for sheepmeat exporters such as Australia.

The 'Stocktaking' is complementary to the 'Memorandum' and examines how effectively the mechanism and regulations of the CAP have achieved CAP objectives and further suggests ways of improving the system. The 'Stocktaking' is critical of certain aspects of the CAP and refers to short-term and structural imbalances in certain agricultural markets, to the lack of specialisation within the Community, to the high disparity of incomes between regions, to the lack of unity within the Community market as a result of monetary instability and to the high budgetary cost of current agricultural policies. While its proposals and recommendations are similar to those of the 'Memorandum', the 'Stocktaking' does introduce some new and important initiatives including:

- That Community consumers should be able to obtain more benefit from the occurrence of agricultural surpluses and that priority be given to disposing of these surpluses on internal rather than external markets through the use, for example, of consumer subsidies.
- That Community exporters be encouraged to enter into long-term contracts for the supply of certain agricultural products to non-member countries.
- That direct income subsidies be more widely used in EEC farm policy.

The 'Stocktaking' and the earlier 'Memorandum' are evidence of the ongoing review and debate within the Community of the CAP and its policy instruments. In broad terms, probably the most significant aspect of these documents is the increased emphasis they give to consumer interests both in relation to food prices and to the overall cost of the CAP. This is highlighted through proposals for consumer subsidies, producer co-responsibility for commodity surpluses and a more 'objective' basis for the setting of support price levels. At the same time, however, the basic and explicitly stated CAP principle of support for agricultural producers' incomes which has been pursued through the maintenance of high guaranteed prices and the use of variable levies on imports has been subject to less scrutiny and critical evaluation.

While the 'Stocktaking' recommends the use of direct income subsidies, such measures are seen by the Commission primarily as a means of reducing farm income disparities within the EEC rather than as an alternative to price support arrangements. The 'Stocktaking' does not recommend the widespread introduction within the Community of deficiency payments schemes similar to those previously in use in the U.K. This is largely because it is considered that the adoption of such schemes by the Community in place of traditional market and price policy measures would be likely to greatly increase the budget cost of EEC farm policy (although consumer prices would be lower and there would be little change in the 'real' cost of farm support). In addition, the financing of deficiency payments type schemes from national budget revenues would almost certainly create more problems than current support measures which are mainly financed directly from Community sources.

There has been little progress to date on the implementation of the major reform proposals contained in the 'Stocktaking'. For example, there has been no extension of the use of direct income subsidies or of consumer subsidies. At the main Council meeting to consider the proposals held in November 1975 there was some agreement on general principles (e.g. that in the milk sector, the aim is to restore market balance and prevent an excessive build-up of stocks). On the other hand, there were no recommendations made for any action on specific proposals.

However, the two reform documents are of some importance insofar as the Commission does include recommendations from them in its annual price proposals to the Council. In some instances these recommendations are wholly or partially accepted (e.g. the reduction in MCAs and adjustments in the cereals sector for the 1976-77 season). Nevertheless, the prospects of significant changes to the CAP arising from these initiatives are strictly longer term and there are no indications of a radical new farm policy emerging in the EEC in the near future. Indeed the complex bargaining and the political nature of decision making in the Community farm sector makes any significant short-term departure from existing policy both difficult and unlikely.

Implications of Recent EEC Developments for Australia

The accession of the U.K. to the EEC in 1973 and the build-up of Community beef stocks in 1974 and 1975 have had a major impact on Australian trade. As a result of the former, Australia has lost its preferential access to the U.K. market while the latter has meant the virtual closure of the EEC market to beef imports. The severity and suddenness of the loss of agricultural export sales to the U.K. and to the enlarged Community are clearly illustrated in Tables No. 6 and No. 7. Australian rural exports to the U.K. slumped from $283 million in 1970-71 to $100 million in 1975-76. Australian exports of wheat and butter to the U.K. were particularly affected, falling from 1.7 million tonnes to 73 thousand tonnes for wheat and from 55.6 thousand tonnes to negligible levels for butter between 1970-71 and 1975-76.

The Australian beef and veal industry has been very seriously affected by developments in the EEC beef sector. The value of Australian beef and veal exports to the enlarged Community plummeted from $108 million in 1972-73 to only $11.5 million in 1975-76. Since the suspension of EEC beef and veal import licences in July 1974 almost all of
Table No. 6
AUSTRALIA: GROSS VALUE OF EXPORTS OF RURAL COMMODITIES TO THE UNITED KINGDOM: 1970-71 TO 1974-75
(Million Dollars)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Wheat</td>
<td>81.5</td>
<td>27.5</td>
<td>28.7</td>
<td>-</td>
<td>(a)</td>
<td>6.9</td>
</tr>
<tr>
<td>Barley</td>
<td>10.6</td>
<td>10.4</td>
<td>2.2</td>
<td>3.4</td>
<td>1.5</td>
<td>3.1</td>
</tr>
<tr>
<td>Other coarse grains</td>
<td>1.1</td>
<td>0.9</td>
<td>0.7</td>
<td>1.9</td>
<td>1.2</td>
<td>1.2</td>
</tr>
<tr>
<td>Rice</td>
<td>1.6</td>
<td>1.9</td>
<td>4.0</td>
<td>4.2</td>
<td>3.6</td>
<td>2.3</td>
</tr>
<tr>
<td>Sugar</td>
<td>40.4</td>
<td>43.6</td>
<td>39.2</td>
<td>28.0</td>
<td>33.8</td>
<td>15.1</td>
</tr>
<tr>
<td>Butter</td>
<td>29.1</td>
<td>9.9</td>
<td>27.7</td>
<td>(a)</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Cheese</td>
<td>3.6</td>
<td>2.7</td>
<td>0.8</td>
<td>(a)</td>
<td>-</td>
<td>0.1</td>
</tr>
<tr>
<td>Processed milk</td>
<td>0.8</td>
<td>(a)</td>
<td>(a)</td>
<td>(a)</td>
<td>(a)</td>
<td>(a)</td>
</tr>
<tr>
<td>products</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Eggs</td>
<td>2.2</td>
<td>1.5</td>
<td>3.7</td>
<td>0.2</td>
<td>-</td>
<td>(a)</td>
</tr>
<tr>
<td>Beef and veal</td>
<td>21.0</td>
<td>34.4</td>
<td>101.0</td>
<td>48.1</td>
<td>13.5</td>
<td>7.0</td>
</tr>
<tr>
<td>Apples and pears</td>
<td>11.7</td>
<td>10.2</td>
<td>7.0</td>
<td>10.4</td>
<td>6.7</td>
<td>5.4</td>
</tr>
<tr>
<td>Dried vine fruits</td>
<td>7.1</td>
<td>6.6</td>
<td>6.4</td>
<td>5.4</td>
<td>3.5</td>
<td>7.4</td>
</tr>
<tr>
<td>Canned fruit</td>
<td>27.7</td>
<td>19.7</td>
<td>23.7</td>
<td>21.7</td>
<td>17.8</td>
<td>12.7</td>
</tr>
<tr>
<td>Mutton and lamb</td>
<td>14.4</td>
<td>12.7</td>
<td>15.2</td>
<td>13.1</td>
<td>5.9</td>
<td>5.0</td>
</tr>
<tr>
<td>Wool</td>
<td>30.1</td>
<td>32.5</td>
<td>55.5</td>
<td>43.1</td>
<td>24.6</td>
<td>32.8</td>
</tr>
<tr>
<td>Oilseeds</td>
<td>0.2</td>
<td>(a)</td>
<td>0.7</td>
<td>0.2</td>
<td>0.5</td>
<td>1.1</td>
</tr>
<tr>
<td>Total</td>
<td>283.1</td>
<td>214.4</td>
<td>316.5</td>
<td>179.5</td>
<td>112.6</td>
<td>100.1</td>
</tr>
</tbody>
</table>

(a) Negligible.

Source: ABS, Overseas Trade (various issues).
Table No. 7
AUSTRALIA : GROSS VALUE OF EXPORTS OF RURAL COMMODITIES
TO THE ENLARGED COMMUNITY : 1972-73 TO 1974-75
(Million Dollars)

<table>
<thead>
<tr>
<th>Item</th>
<th>1972-73</th>
<th>1973-74</th>
<th>1974-75</th>
<th>1975-76</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wheat</td>
<td>29.5</td>
<td>-</td>
<td>1.8</td>
<td>6.9</td>
</tr>
<tr>
<td>Barley</td>
<td>8.4</td>
<td>5.0</td>
<td>9.2</td>
<td>24.6</td>
</tr>
<tr>
<td>Other coarse grains</td>
<td>0.8</td>
<td>3.7</td>
<td>5.7</td>
<td>7.4</td>
</tr>
<tr>
<td>Rice</td>
<td>4.5</td>
<td>4.4</td>
<td>3.6</td>
<td>2.6</td>
</tr>
<tr>
<td>Sugar</td>
<td>40.4</td>
<td>28.0</td>
<td>33.8</td>
<td>15.2</td>
</tr>
<tr>
<td>Butter</td>
<td>27.7</td>
<td>(a)</td>
<td>-</td>
<td>15.7</td>
</tr>
<tr>
<td>Cheese</td>
<td>0.8</td>
<td>(a)</td>
<td>-</td>
<td>0.2</td>
</tr>
<tr>
<td>Processed milk products</td>
<td>(a)</td>
<td>(a)</td>
<td>-</td>
<td>(a)</td>
</tr>
<tr>
<td>Eggs</td>
<td>3.8</td>
<td>0.2</td>
<td>-</td>
<td>(a)</td>
</tr>
<tr>
<td>Beef and veal</td>
<td>108.4</td>
<td>53.2</td>
<td>16.1</td>
<td>11.5</td>
</tr>
<tr>
<td>Apples and pears</td>
<td>15.2</td>
<td>16.9</td>
<td>13.0</td>
<td>10.6</td>
</tr>
<tr>
<td>Dried vine fruits</td>
<td>11.2</td>
<td>7.6</td>
<td>6.5</td>
<td>12.4</td>
</tr>
<tr>
<td>Canned fruits</td>
<td>32.9</td>
<td>30.8</td>
<td>20.4</td>
<td>17.5</td>
</tr>
<tr>
<td>Mutton and lamb</td>
<td>16.9</td>
<td>13.8</td>
<td>6.3</td>
<td>6.0</td>
</tr>
<tr>
<td>Wool</td>
<td>319.4</td>
<td>309.0</td>
<td>237.5</td>
<td>300.8</td>
</tr>
<tr>
<td>Oilseeds</td>
<td>1.4</td>
<td>0.2</td>
<td>7.3</td>
<td>8.0</td>
</tr>
<tr>
<td>Total</td>
<td>621.3</td>
<td>472.8</td>
<td>361.2</td>
<td>439.4</td>
</tr>
</tbody>
</table>

(a) Negligible.

Source: ABS, Overseas Trade (various issues).
Australia's beef shipments to the enlarged Community have been a share of the EEC's levy free quota under GATT and have been between 10 000 and 15 000 tonnes. There is not likely to be any marked improvements in this situation in the near future as the enlarged EEC is expected to have little requirement for imports of beef until at least 1977, and even then the situation does not appear particularly favourable if the new beef import levy arrangements, discussed earlier, are introduced.

The enlargement of the Community has also meant the effective closure of the sizable U.K. market to Australian exports of cereals and dairy products. In the case of cereals this has had little impact on the Australian industry as alternative outlets have been readily available since 1973, notably the USSR.

The entry of the U.K. into the EEC has excluded Australian dairy supplies from this major market. The adverse effect of this development on the Australian industry was initially offset to some extent in 1973 and 1974 by increased exports of butter and cheese to other countries, notably Japan, Canada and the United States. There was also a boom in Australian exports of skim milk powder which almost doubled from 48 000 tonnes in 1972-73 to 94 000 tonnes in 1975-76. However, many of these improvements in other markets were only temporary. During 1975 and 1976 there has been a marked decline in the level of world trade and prices of most dairy products largely as a result of increased supplies in major producing regions, especially the enlarged EEC. In this situation the Australian dairy industry has now felt the full impact of the loss of the U.K. market and the increased competition on other world markets.

The Australian dried vine fruit and canning fruit industries were, until the end of 1974, largely cushioned from the full effects of the progressive imposition by the U.K. of the EEC's common external tariff through a generally buoyant world market situation. However, world market prices for these products declined in 1975 and have remained low. This has led to a significant decline in the value of Australian exports to the U.K. Australian apple shipments to the U.K. have fallen sharply since 1973 although this reduction has resulted to some extent from reduced Australian export availabilities. The export market for Australian apples has been declining since about the mid-1960s and the market outlook has deteriorated further as a result of the U.K. entry to the EEC.

As a result of tight world supplies and high prices the detrimental effects on the Australian sugar industry of the termination of the Commonwealth Sugar Agreement at the end of 1974 have been cushioned to some extent. This agreement gave Australia an assured market at stable prices for a minimum of 340 000 tonnes of raw sugar each year. Therefore, for the sugar industry, the need to replace this guaranteed market with others has obviously increased the degree of uncertainty involved in exporting. Although the U.K. proposed that there should be continued access for sugar from efficient producers such as Australia as part of its renegotiation discussions this objective was not achieved.

Some Australian rural exports, particularly beef and dairy products, have already suffered the consequences from either the accession of the U.K. or recent changes in the organisation of EEC commodity markets. On the other hand the Australian sugar industry has had some degree of success in diversifying its export markets. Overall, the most important effect of the diversion of rural exports from the U.K. market
has probably been the increased uncertainty facing Australian rural exporters in new and alternative markets. (35)

Some Australian rural industries have also benefited, although only marginally, from the special compensation provided by the EEC under the GATT in respect of tariff concessions lost by Australia on the U.K. market. The compensatory tariff concessions include:

- Bound duty reductions on products such as dried vine fruit, apples and pears, and oranges.

- An increase in the EEC’s levy-free beef import quota, from 22,000 tonnes to 38,500 tonnes. This increase is shared by Australia and other GATT members.

- A binding of the EEC duty at present levels on mutton and lamb, honey, canned fruit, hides and skins and greasy wool.

The above concessions have been applied to EEC imports since the beginning of January 1975. The value of these concessions to Australian exports is relatively small and it is relevant that although exports of dried vine fruit, apples and pears, and canned pears to the Community now face lower duties than previously, the new rates are in fact much higher than the old duty rates which applied on exports to the U.K.

While the U.K. accession has had an immediate and direct impact on the direction and level of exports of some Australian rural commodities, this factor in conjunction with other developments within the Community is also likely to have a continuing effect on Australian farm trade. However, in the longer term the importance of the Community is more likely to be as a competitor in third country agricultural markets rather than as a large potential export market for Australia as it has generally been considered in the past. This is because there seems to be little prospect at present of any fundamental change of emphasis and direction for the CAP.

The various pressures to which the CAP has been subjected in recent years and the Community’s responses to these pressures have been discussed in earlier sections. As a result there emerged a more critical attitude to agricultural policy within the EEC and the possibility of some basic policy changes. The main manifestations of this new attitude were the Commission’s 'Memorandum' and 'Stocktaking', containing a number of important reform recommendations which if implemented would have had important implications for levels of EEC agricultural production, consumption and trade. However, on present indications any substantial adoption of the more important proposals will be difficult to achieve, as long-term rationalisation is continually being hampered by short-term and often political considerations. For example, the Council has been unable to agree to basic reform of the dairy industry despite the periodic recurrence of structural surpluses in this sector.

Although there have also been indications in recent years of more attention being paid to Community-wide structural reform programs

this aspect of the CAP still plays a relatively minor role and the Guidance Section of the EAGGF which finances such programs continues to receive only a very small fraction of the total funds allocated to agriculture through the Community budget. Structural reform on a scale sufficient to significantly reduce the periodic production and accumulation of surplus commodity stocks is certain to occur only slowly.

On the demand side, the CAP continues to maintain Community prices for most major agricultural products at levels higher than world market prices (with the exception of a period in which world prices for cereals and sugar were very high). In addition, because of a range of difficulties, there are no indications of an extension of the use of consumer subsidies or of deficiency payment type schemes in the EEC, both of which have a dampening influence on consumer prices. These factors constrain domestic consumption growth and increase the need for export subsidies which have had a depressing and destabilising effect on world trade.

The major implications of recent developments for Australian rural trade are, therefore, that the U.K. has now ceased to be a major market for Australian rural exports since its accession to the EEC and its increasing absorption into the CAP. In the absence of any indications of the Community's import regime becoming more flexible or liberal, there is no reason to expect any significant increase in the level of the Community's agricultural imports. Finally, it is evident that reform of the CAP in any meaningful way is going to be a very slow process. This suggests the continuing appearance of periodic commodity surpluses while at the same time moves to significantly increase domestic consumption have apparently stagnated. The disposal of the EEC's surplus agricultural production on overseas markets will, therefore, be a continuing and perhaps increasing problem for other agricultural exporters such as Australia, although a return to greater stability on world agricultural markets could reduce the impact of the problem.

Conclusions

During the past five years, agriculture in the EEC has had to cope with several new and major developments. Some of these, such as the enlargement of the Community and the problems associated with depressed and unstable economic and monetary conditions, have been external to the agricultural sector but have nevertheless been important in shaping agricultural policy. Others, such as the extreme fluctuations in world commodity prices, have necessitated major adjustments in the organisation of Community markets.

The performance during this period of the Common Agricultural Policy in dealing with the growing number and complexity of problems confronting the farm sector has been increasingly questioned. While it is clear that the CAP mechanism has, during times of high world commodity prices since 1973, ensured lower and more stable domestic consumer prices for some agricultural commodities such as cereals and sugar than would otherwise have occurred, it is also apparent that in other important respects its actual performance has fallen short of its own objectives.

The price support policies of the CAP have insulated many Community producers from the influence of international market forces and have in several cases encouraged excess production and contributed to the
accumulation of large costly surpluses. At the same time measures to improve the structure and the efficiency of the European agricultural sector have only received relatively modest support from the Community farm budget. A large part of EEC agriculture is still characterised by relatively low levels of labour productivity and small farms. In fact some so-called structural measures such as the special assistance to hill farmers in the Community are not likely to improve levels of agricultural productivity and may instead aggravate problems of surplus supplies.

Furthermore the unity of EEC agricultural markets, a basic principle of the CAP, has been seriously undermined by the exchange rate fluctuations since 1971. These currency fluctuations have been partially offset by monetary compensatory payments which have in effect introduced different price levels within the Community. The CAP system has also been strained by the increasing willingness of member countries, in the face of serious economic and industry problems, to adopt independent agricultural and trade policies, sometimes in direct contravention of CAP regulations.

The past five years have been a particularly difficult period for the operation of the CAP and several weaknesses of the system have been highlighted. Nevertheless the system has shown considerable flexibility and has proved amenable to change in the use of various policy instruments. The need to find quick and effective solutions to immediate problems has led to the introduction of many ad hoc measures. These have often been influenced more by perceived economic needs of a short-term nature than by the need sometimes for more fundamental changes which would have longer-term effects. However, there has also been a considerable willingness amongst members to compromise on difficult issues and a determination to maintain the CAP at all costs despite its weaknesses.

Although the Commission's agricultural reform documents were indicative of a more critical approach to Community farm policy, few of the documents' recommendations have been implemented. Furthermore it seems unlikely that in the near future there will be any significant movement in Community agricultural policy away from a dependence on high producer support prices and stringent import barriers. It is these elements of the CAP that have been primarily responsible for the production surpluses that characterise most areas of EEC agriculture. They have also made the objective of structural adjustment through improved resource use more difficult to achieve.

While there have been some signs over recent years of a shift in the emphasis of the CAP towards more consumer oriented policies it is apparent that by the first half of 1976 the more traditional producer bias had been reasserted with a run-down of the slaughter premium system and the rejection of the use of consumer subsidies.

In conclusion, moves to implement structural reforms, to improve efficiency and resource allocation in the Community's agricultural sector and to reduce the tendency to generate commodity surpluses have received more emphasis in recent years, but progress has continued to be very slow. The Community's unpredictability as an agricultural trading group seems likely to continue therefore, with little prospect of any significant reduction in the disruptive influence of traditional CAP measures on world agricultural trade.