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The Contribution of 14 European Think Tanks to the Spanish, Belgian and Hungarian Trio Presidency of the European Union

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Reforming the CAP Budget – A Perfect Test for the EU

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Reforming the CAP Budget – A Perfect Test for the EU

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"EU money for jobs, not cows". Who can forget Tony Blair's 2005 speech when he asserted before the European Parliament that a "modern budget is not a budget which, in 10 years, will still dedicate 40% (of EU spending) to the Common Agriculture Policy (CAP)"? At that time, the British Prime Minister was formulating a concept that has since become widely accepted – namely, that any sort of budget that devotes most of its spending to agriculture, food and rural development should be viewed as obsolete. Tony Blair's criticism would have been justified if the EU budget was that of a federation, but rather it is one of a heterogeneous political integration process. As the only common economic policy to be endowed with an EU budget, the agricultural and rural policy is also the only one almost entirely funded by Brussels. This particular Community status has earned the reputation of being an ever-recurrent topic of contention in budgetary negotiations since 1979. Viewed as being costly, as compared to cumulated European public spending (member states and EU spending) broken down by sector, agricultural policy ranks only 11th, with 1.1% of total public spending (Bertoncini, 2009).

Spain, Belgium, and then Hungary, will share the challenging task of initiating debate within the European Council on budget revision followed by the post-2013 Financial Perspectives. These negotiations will be a perfect test for assessing the EU's ability to venture beyond the 'budget rebate' approaches which have impeded the latest budgetary discussions since then. By demonstrating its ability – or inability – to reform the CAP, along with the agriculture budget, the Council will prove that it is capable of formulating a renovated agricultural common project. But the context bodes difficult negotiations: 27 member states share a budget nearly identical to that of the EU-15 and the EU is facing new climate and energy – as well as economic and social – challenges. Failure to seize this opportunity would deprive the EU of one of its most effective tools for protecting its environment, cause a definitive destabilisation of the sector and of European campaigns, and threaten the EU's food production capacities. Leading this debate goes to the Trio Presidency.

Agriculture in the 21st century: a key for food and natural resources management

Global agricultural markets are increasingly unsettled

In a context of rising volatility in commodity prices, bolstered by the interconnection of global markets, farmers will be facing additional uncertainties in the next few years on top of the long list of natural vagaries that periodically destabilise their sector. The horizon is becoming more complex due to a combination of several phenomena, with uncertain consequences for European agricultural markets. As developing countries become richer, consumption patterns are changing to include more meat products, leading to an expansion of agricultural demand (one animal protein requires, on average, seven plant proteins in order to be produced). World population is currently increasing at a rate of 80 million people annually (a population equal to that of Germany), and is expected to reach 9 billion people by 2050. To these developments may be added an increased demand for energy production (biofuels) which increases the volatility of some commodity prices now linked to petrol prices. In order to deal with this growing challenge, and after having spent more than 20 years backing policies aimed at liberalising the agricultural sector, international institutions (World Bank, OECD) are calling for massive investments in Least Developed Countries' (LDCs) agriculture. In rich countries these changes remind us of the elementary role of agriculture and of the need to be cautious when reforming market regulation instruments, which are needed when prices are uncertain.

The environmental challenge

Protecting natural resources and biodiversity has become a primary concern, in view of accelerating environmental damage. At the same time, given the increase of agricultural demand in the medium-term, an intensification of production will be necessary. And yet farming activity has a considerable impact on natural resources. On the one hand, agriculture can pollute and overexploitation often leads to the irreversible destruction of an ecosystem. Rich countries' agricultural policies, inspired by green revolution principles such as those of the CAP, are still helping to foster the intensive use of exhaustible natural resources, particularly water. On the other hand, agriculture can enhance the preservation of biodiversity and natural spaces. In that case abandoning the practice of farming can lead to very serious environmental problems. Fragile zones (such as mountains and the Mediterranean region) are still experiencing soil erosion and depopulation phenomena.

The uncertain fight against global warming

The inclusion on the global and EU agenda of the fight against climate change issue has recently generated new expectations with regard to the agricultural sector, which produces 13.5% of the world's Greenhouse Gases (GHGs). However, beyond statements about the necessary participation of agriculture in the fight against global warming, no clear and precise implementation plan has yet been formulated. Moreover, research findings – still highly experimental at this stage – have yet to identify any promising options for farms with carbon-neutral environments. In addition, agriculture's contribution to the reduction of GHGs is bound to be offset by the extensive reshaping of the global agricultural map which should result from the rise in the average temperature. This uncertainty is compounded by considerable doubt as to whether populations in the newly productive areas will be able to attain productivity levels equal to, or higher than, what they are today. Will they reserve sufficiently fertile land for farming? Will they invest in the sector in order to equip themselves with the necessary means of production? Will they secure the manpower and know-how needed?

Reforming the CAP in order to meet 21st century challenges

Agriculture, the environment and European rural areas would ultimately suffer as much from a dismantling of the CAP as from a lack of reform. The very likely reduction in the agriculture budget anticipated in the next financial perspectives should usher in a new policy approach – one which offers answers to future challenges and serves the medium-term strategy of the EU. A flawed policy, despite past reforms.

Reformed since 1992, the CAP has been constantly revised in order to improve its regulations. The Single Payment Scheme nonetheless plays a particularly noteworthy role as a price-fluctuation shock absorber; eco-conditionality has begun to have positive results for natural resources as has the increased expenditure in favour of the environment and rural development. The merits of the improvements made and of budgetary discipline should not mask the current system's limitations. The primary criticisms concern the efficiency of support for 1st pillar income; the efficiency of the transfer of income linked to aid distributed under the 2nd pillar; management costs; the leakage of aid towards unintended beneficiaries; the concentration of payments; and the unequal exposure of sectors to price volatility. In environmental and rural matters, criticisms deal with water pollution incentives and the limited impact of agri-environmental and eco-conditionality aid programmes. Next, agricultural crises are continuing despite the market instruments available. Lastly, the CAP has not yet been made consistent with other EU policies: it is still a more agricultural than food policy; the EU competition policy sanctions some organised groups of producers, while it tolerates certain excessive concentrations within the agro-food industry; 1st pillar financial aid is sometimes deployed in a way that conflicts with the cohesion principle because of its inequitable distribution.

Reforms should not be made for the wrong reasons

In 2008, the CAP represented 44% of the EU budget, or €52.3 billion. Many protesters have denounced this situation, even though Eurobarometer survey has shown in March

2008 that 58% of EU citizens believed that the CAP's budget should either stay the same or increase. The recurring criticisms of the CAP are sometimes surprising inasmuch as it ranks eleventh in the cumulated national and EU public expenditures with 1.1% – far behind the leading trio, which are social protection and active policies in the labour market (41.4%), health (14.2%) and education / training (11.3%) (Bertoncini, 2009). Also, a brief worldwide comparison shows that Europeans rank among an average of developed countries in terms of the relative share of GDP devoted to this sector with 0.5%, compared to 0.2% in the United States, 0.4% in Canada and 2.4% in Japan. Similarly, while the pre-reform CAP may have had a negative impact by allowing for unfair competition against LDCs agricultures, that is no longer the case. In view of the current CAP's flaws, particularly its inequitable way of distributing aid by sector – few realise that a majority of European farmers and breeders are not benefiting from the CAP – it appears possible to regulate more effectively with equivalent financial resources by formulating new rules and using a new method of allocating funds.

A distinctive economic sector which calls for cautious CAP reforms

The 27 member states could thus decide not to improve the regulation of their agricultures, considering the strongest farm businesses should, as in other sectors, be able to compete and food supplies could be secured through international trade. Nonetheless, some economic foundations dictate that the regulation of the agricultural sector should differ from that of the industrial and service sectors. Indeed, the 'health check' (adopted in 2008) and the informal Agricultural Councils' discussions led by the last Trio Presidency on the CAP's post-2013 objectives have all confirmed unanimous agreement on this issue. Several points of consensus emerged from these discussions between the 27 member states on the need for a common agricultural policy in order to avoid competitiveness distortions to the greatest extent possible. The question of the potential dismantling of this common policy is raised outside of non-specialist circles which are unaware of the sector's economic specificities. All agricultural economy analyses point at least to the following conclusion: agricultural markets must be regulated, for three reasons. First, the limited elasticity of agricultural demand (once consumers are satisfied, they no longer buy agricultural commodities) is facing an extremely variable supply that is not closely linked to price level (attributable, for example, to unpredictable weather conditions). Second, supply and demand adjustment mechanisms do not operate properly and take too long to be implemented (for example, crop growing time). Lastly, these markets include major entry barriers because of investment level, land capital, necessary know-how and time necessary to become competitive in the marketplace.

A budgetary and political intolerable situation

For the first time in its history, the EU will institute a budgetary negotiation involving 27 voices whose tone will translate highly heterogeneous economic and agricultural backgrounds, amplified by the crisis. The positions in the future negotiation and alliances which may formed are still uncertain. However, the member states who joined the EU in 2004 and in 2007 are expected to be opposed to the current allocation of funds. Indeed, the Copenhagen European Council (2002) which completed negotiations for the accession of ten new member states anticipated that the latter would receive 2nd pillar aid and benefit from market measures, but would only gradually be entitled to receive direct assistance. Therefore, since 2004 and 2007, the allocation of CAP support has been following a discriminatory principle with respect to the 12 newest EU members. This situation, which has allowed the CAP budget to remain stable, has confirmed an inequitable situation that the 12 States expect to see eliminated after 2013. This claim is all the stronger in that since 2008, the crisis has curtailed the granting of loans to farms and, in some cases, deprived the States of resources needed in order to co-finance the aid planned by the EU. It is against this background, in which wide gaps in agricultural competitiveness subsist between older and newer member states, that the negotiations will take place.

Good ways to reduce the CAP budget

Debating issues in the right order

The way in which the price regulation system derailed in the 1980s tarnished the CAP's image. Various reforms have corrected these problematic mechanisms but they were never accompanied by a revision of the fundamental CAP principles. Today, this multi-layered policy suffers from a lack of legibility that is eroding its legitimacy. Therefore, before debating the budget, the EU should assess medium-term challenges, in order to define new agricultural policy objectives. J.C. Bureau and L.P. Mahé (2008) stressed that "any serious effort to undertake a long-term analysis of the CAP objectives for this 21st century must begin with two questions: what types of market failures require an agricultural policy? What policies should lie within the EU's competence and funding?" Discussions could then logically focus on the toolbox needed to attain those objectives, and lastly on the funding level.

Avoiding unproductive debates on CAP funding

Due to the exceptional nature of the CAP's governance which, unlike the other sectors, is common and to the fact that 72% of the expenditure is incurred by the common budget, this minority spending within the European public expenditure is automatically more closely scrutinised. In a primarily urban Europe which has witnessed a decline in the number of its farmers and in the share of European GDP produced by the economic sector, it is an easy mistake to view that trend as a Community money reserve from which it can draw to fund other projects or to meet new challenges.

Even though the CAP's budget has not been extensively changed in terms of its allocations between the two 'pillars,' the aid modulation mechanism – which transfers part of the aid from the 1st pillar towards the 2nd – provides some more flexibility to States which co-finance 2nd pillar measures. Moreover, the recent milk crisis allowed the States to raise the national aid ceiling. This rampant renationalisation of the CAP is exposing farmers to differentiated amounts of aid from one country to the other. The consequence of this could be the return of competitiveness between national agricultural policies in a distorted market.

Calling for an overhaul of European public support for agriculture

Setting aside the CAP's normative achievements, which are very positive (in health security, for example) to consider measures which have had a budgetary impact, three objectives can be assigned to the post-2013 CAP: the environment (preservation of natural resources and the fight against global warming); the regulation of agricultural markets (inherently unstable); and rural public goods (i.e. landscapes, recreational areas). The directions to be taken call for the creation of objective-specific instruments so as to better identify and measure their effectiveness. European public funds must finance European public goods and the payments must be designed as incentives rather than as 'rights'. Indeed funds must be allocated according to a contractual principle that compels the Community to remunerate farmers who provide a service (such as farming lands in rural regions according to strict environmental rules; compensation associated with natural handicaps; services in environmentally sensitive or high nature-value areas). Finally the CAP helps to ensure agricultural competitiveness, rather than income, but it must also anticipate the safety nets and guaranties which will enable agricultural markets to withstand price volatility.