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PART I

The Common Agriculture Policy: key to Europe's farm productivity

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As this year's round of European Community farm-policy negotiations open, European agriculture is being held hostage to the deteriorating world economy. The European Community (EC) is plunging into a paralyzing political crisis as French President Mitterrand and British Prime Minister Thatcher battle each other and undercut West German Chancellor Schmidt's hope that the EC can provide a unified voice for world economic recovery and political stabilization.

Since its controversial entry into the EC in 1973, Britain has led an attack on the Community's Common Agricultural Policy (CAP) as a wasteful and unnecessary "giveaway" program. Lately, the situation has been exacerbated by attacks against the CAP by U.S. free-marketeers echoing Britain and adding their own charge that the CAP which is stealing U.S. markets, particularly for grain, and is responsible for the bankruptcy facing American producers.

In reality, neither the CAP nor its programs are wasteful of European tax money, or unfair to American farmers. Anyone clinging to this excuse is ignoring the usurious interest rates that are both crippling farmers' ability to produce and constricting the world markets' ability to consume expanded farm-food exports from both the United States and Europe.

How CAP works

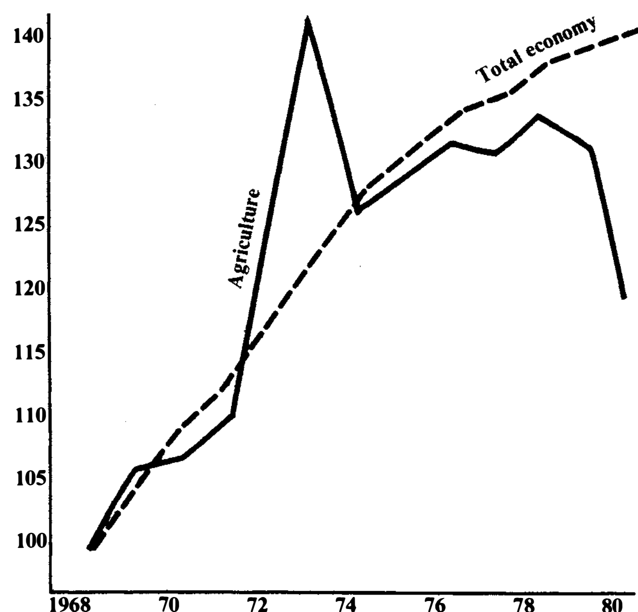
The CAP came into being in 1963, developed out of the 1957 Treaty of Rome. The treaty was to create a unified Europe for economic recovery some ten years after the war that devastated Europe's agriculture and left consumption levels below those of many Third World countries.

The six founding nations were expanded to include the United Kingdom, Ireland, and Denmark in 1973, and Greece in 1981. At the insistence of French President de Gaulle, upholding the CAP was made a prerequisite for EC membership to guarantee the coordinated growth of European agriculture and restore food self-sufficiency as rapidly as possible.

Thus the CAP, coordinating and meshing the national policies of farm-sector support of all its members, is the vehicle through which agricultural production and trade has developed in Europe. Through its guidelines the CAP has built the EC into a self-sufficient food producer and the second most important grain exporter after the United States. These guidelines—to increase agricultural productivity, stabilize markets, ensure a fair standard of living in the farm sector, and secure supplies—have been responsible for the modernization and expansion of European cereals, dairy, fruit, and vegetable production.

Following guidelines, a price-support program was established similar to the parity system in effect in the United States during the 1940s. Parity—the policy of

Figure 1
Agriculture and total economy in the European Community, an index of per capita real income
(percent of 1968)



Source: The Agriculture Situation in the Community, 1980 Report, January 1981

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government action to guarantee orderly marketing at prices sufficient to assure producers cost of production plus a profit adequate to finance future production—laid the basis for the colossal gains American agriculture made during the past three decades.

CAP works as follows for the major grains, the core of the farm economy:

There is a system of three basic price support levels:

The target price, which serves as the reference point to establish the intervention price, and represents the price the farmer believes he should get for his grain. Each year a single target price is calculated for each major grain, plus monthly increments for storage and insurance. **The threshold price,** the central mechanism for protecting the internal market. This price determines the price at which grain can be imported into the EC. It is normally substantially above the international "free-market" price, because of the "import levy," but it averages about 2 percent below the target price level. **The intervention price,** a kind of "floor price." In order to safeguard farm incomes, the EC guarantees a market for Community-produced grain at intervention prices. Through its many intervention centers, the EC will purchase all grain offered in minimum 80-ton quantities. A single intervention price is formulated for each type of grain and is applicable throughout the Community. Since the French market center of Ormes traditionally has the most extensive surplus, it is taken as the standard for all price calculations.

The consequences

What this means for European farm producers can be seen from the following comparison of European and U.S. wheat prices. In 1981, the EC wheat target price was $6.38 per bushel, the wheat threshold price was $6.22 per bushel, and the wheat intervention price was $4.55 per bushel. Compared to this, the U.S. target price for wheat—roughly comparable to the combined EC threshold and target price—was $3.81 per bushel, and the U.S. price support loan rate, comparable to the EC intervention price, was $3.20.

Taking the U.S. Department of Agriculture's own cost-of-production estimates as a standard, it is apparent that European producers, unlike most American farmers, have a chance to break even. According to USDA, 1981 wheat production costs per bushel, including land charges, were $6.77—close to the European target price and nearly twice the U.S. target price levels!

The grain "surpluses" Europe has been producing are testimony to the success of the CAP pricing system. To stimulate exports of the surpluses at world market prices (kept below cost of production levels by the major grain companies), a program of export subsidies has been developed. Under CAP there is thus no control of the market by the large grain companies as in the United States marketing situation.

Figure 2

Shifts in world wheat trade

(national exports in million metric tons)

	1970-71	1975-76	1981-82
United States	19.9	31.7	48.3
European Community	3.4	8.6	14.5
Canada	11.5	12.1	17.0
Australia	9.5	7.9	12.0
Argentina	1.6	3.2	5.0
Other	9.1	3.2	4.0
Total	55.0	66.7	100.8

From 1970 to 1980, European grain production increased by 50 percent, with yields more than doubling. U.S. wheat yields are approximately 3 metric tons per hectare, while average yields in Europe are 4.6. Labor-productivity gains have kept pace with production increases. The total small-peasant population has been halved over the past 15 years; in Italy, the reduction has been even greater. Tractorization has increased 40 percent over 15 years, and the number of holdings under 20 hectares has been reduced by nearly half. Livestock production, while making definite but slow progress, is the weakest production area. In all areas, France, bolstered by its own national agricultural program, has made the best progress.

Complementing the CAP price-support system is the guidance program. Funds from CAP for the Feoga, or farm fund, which pay for intervention purchases, and storage, also provide farmers with funds for modernization and improvements.

For the European farmer who is prepared to change with the times, the CAP has been key to his progress. Unfortunately, since 1979, the tight credit situation worldwide has caused the EC as a whole to tighten its belt. This has lowered rates of production increase, pinched price support levels, and decidedly cut back imports.

1982 negotiations

Two issues are on the table: 1) setting new price-support levels for 1982-83; and 2) deciding on a proposed revision of the CAP guidelines. The outcome will determine whether or not the European farm sector is thrown irrevocably into the kind of spiral of equity bleeding and debt-mushrooming that has put U.S. farm producers into the worst crisis since the Great Depression.

The CAP Commission has drafted a proposal to implement a 9 percent price increase—the largest in any

recent year, yet still far below the 12 percent average European inflation rate—combined with a proposal to further revise the guidelines in the direction of setting production limits which producers are taxed for exceeding.

The French government has already declared that it favors a 12 percent price-support increase, while the European Farmers Union has stated that nothing less than 16 percent is acceptable. Only the Thatcher government claims that 9 percent is too much, ignoring the farmer demonstration in the United Kingdom demanding 16 percent. Even the European Parliament, whose clout is considered weak, endorsed a 14 percent increase.

Even though CAP remains a critical defense for European farm production, it has been seriously compromised. As Figure 1 shows, European farm income in real per-capita terms has taken a beating since 1973. But especially in the past several years, when price support levels were held below the rate of inflation (in 1980 the price increase was 4.8 percent and in 1981, 11 percent), real farm income has taken a nosedive.

Already, capital investment has been hit. In Britain investment in machinery in 1981 was down 18 percent from 1980, and in France investment plummetted by 26 percent during the 1974 to 1979 period. Fully 100,000 farms are reportedly on the verge of bankruptcy in France.

This pressure on the CAP comes after a succession of political and monetary assaults. Starting in 1969, just two years after common EC price-support levels had been established for cereals, the French franc fell under attack and was forced to devalue. Later in the same year the deutschemark was revalued upward. To maintain common price-support levels, France would have had to increase prices by the full extent of the devaluation, and West Germany would have had to lower farm support prices—both unacceptable propositions.

As a result, a set of border taxes and subsidies to account for the new discrepancies now known as monetary compensatory accounts (MCAs) were adopted to bolster the CAP. As the Bretton Woods monetary system further unraveled with the successive dollar crisis and the adoption of "floating" exchange rates, the CAP has been under consistent pressure.

Today there is in fact not one farm price zone within the EC, but seven, and farm prices have diverged by as much as 40 percent between Germany at the top and the United Kingdom at the bottom. Currently the farm-price spreads in Europe are about 10 percent.

The extent to which the CAP has been undermined over the years has been masked in countries like France, Italy, and the Netherlands because those governments have adopted, independently of CAP, supplemental price-support programs. The effects of undermining CAP have also been masked by Europe's relatively recent adoption of hybrid seed varieties, which expanded output and yields without major capital investments in land and equipment.

Also contributing to the CAP's erosion have been the British gentleman farmers—the largely anti-Europe titleholders whose land is worked by tenants in the United Kingdom. Those gentleman farmers have stated their conviction that farm prices should be fixed "by markets, not by ministers," adding that that is the best way to eliminate so-called surplus production. The British want to replace the CAP's parity system with a system of feudal grants issued directly to farmers, as Part II of this report will elaborate.

Western Europe has benefited from an approximation of a parity system.