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How to reform the Common Agricultural Policy

Jack Thurston
with an introduction by **Chris Haskins**

The Foreign Policy Centre



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How to reform the Common Agricultural Policy

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Jack Thurston
September 2002

Foreword

The Foreign Policy Centre is an independent think tank launched by the British Prime Minister Tony Blair (Patron) and the then foreign secretary Robin Cook (President) to broaden debates about foreign policy in the UK and internationally. The Centre seeks to develop innovative approaches to policy which help foster a global community committed to democracy, human rights and social justice. Integral to this agenda is research and analysis into the effectiveness and legitimacy of international systems and institutions.

We are delighted to publish this report by Jack Thurston and its fellows in the 'Future of Rural Communities' project. Agriculture is set to become a key battleground for global politics. Commitments to liberalise agricultural trade are at the centre of creating a fairer and more equal the relationship between North and the South – as well as putting renewed pressure on the transatlantic alliance. But successive attempts at reform have been blocked by the ability of well-organised lobbies to dominate the policy agenda at a national level. This report sets out an innovative approach to the problem – looking at the practical steps Europe can take to put its house in order and 'reform the unreformable'.

Tom Arbuthnott and Mark Leonard

The Foreign Policy Centre
September 2002

Introduction by Chris Haskins

Two great challenges face Europe in the next few months – the opening up of the EU to the East with the admission of 11 new and poorer members, and the opening up of European markets to the poorer countries of the world at the Doha trade talks. Most people agree with the objectives – but there are great problems in getting there.

The 30 year old European Common Agricultural Policy, based on protectionism and market-distorting subsidies, must be radically reformed to allow for a successful enlargement of the EU. If fairer trade with poorer countries is a goal, then the CAP's protectionist barriers to trade in food and its destructive dumping of food surpluses on world markets will have to be eliminated.

The purpose of this project has been threefold. First, we have sought to see the problem through the eyes of European taxpayers, consumers, environmentalists, policy makers and, particularly, farmers in order to mobilise European opinion towards an agreed reform agenda. Second, we have attempted to point out why the time has never been more propitious for tackling reform. And finally we have drawn up a political route-map showing how these reforms should be achieved to allow for a successful enlargement of the EU.

In order to do this we have held seminars in Berlin, Warsaw and Paris. One of our researchers is Danish, and we have had contributions from several other member states, as well as the Commission. In the past British advocates of CAP reform have concentrated too much on their own national priorities and taken little heed of concerns elsewhere.

The report in this volume is the first of a set of papers which address the most important questions which must be answered if the CAP is to be reformed.

First, we address how reform might actually happen. In this first report, Jack Thurston, former special adviser in the Ministry for Agriculture Fisheries and Food, dissects the politics of CAP reform. He identifies winners and losers and analyses what the political momentum for change is, why there are different views amongst member states and where the real power lies. This report presents a route-map for reform, and sets out practical steps towards that end.

Second, we examine what form a revised CAP should take. The second paper, written by Vicki Swales, Head of Agricultural Policy at the Royal Society for the Protection of Birds, makes practical suggestions about the implementation of reform policies which will promote rural development consistent with enlargement, fairer trade and a sustainable environment. This paper particularly questions whether the main plank for the Fischler reforms, the so-called second pillar of the CAP, can be effective in its current form, and suggests ways of making it so.

Third, we look at the 'what next'. I have written a paper which examines whether, in the light of discussions about CAP reform, there is a future for farming in Western Europe. The paper points to the continuing, but changed subsidies under a revised CAP, the extraordinary scientific and technological developments in farming, the growth in farm sizes, the stability of asset values even at a time of declining income and the resourcefulness of the farming community in arguing that, whatever happens to the CAP, farming will continue to have a viable future in Western Europe.

We have also addressed the 'why' of reform, alongside the 'how', the 'what' and the 'what next.' A fourth paper, written by Jonny Trapp Steffensen, CAP specialist and Conservative party candidate in Denmark, will be published on the Internet alongside the three printed papers. This paper contrasts the effectiveness of the small, highly motivated farming interest which is against reform, with the inertia of a wide number of interests who would benefit from reform –

taxpayers, shoppers, business, environmentalists, the new EU members and the developing countries.

In our discussions across Europe we have found considerable dissatisfaction with existing policies. Taxpayers feel they are getting poor value for their money, consumers believe they are paying too much for their food, environmentalists are convinced that the CAP is encouraging bad farming practices, businesses complain that they cannot achieve more trade liberalisation because of protectionist farm policies, and many farmers recognise that the policies are not addressing their real concerns.

In July this year the Agriculture Commissioner, Franz Fischler published a radical programme which would make Europe's farm policies compatible with enlargement and more free trade. As is the way with European policy-making, member states all expressed reservations. Large beneficiaries such as France, Ireland and Portugal argued that there should be no reassessment at all until the previously agreed date of 2006. Mediterranean countries complained that their interests were not being taken into account. Environmentally minded countries felt that the changes did not go far enough. Britain and Germany, with a disproportionate number of very large farms, rejected the proposals to put a limit on individual payments.

We feel that the Fischler proposals are a positive step in the right direction and, to a remarkable extent, meet the Principles which we developed last year as a matrix for evaluating options for CAP reform.

We suggest that good European agricultural policies should satisfy the following criteria:

1. Farmers in Europe should continue to be supported but the present system of market subsidies and protectionist barriers must be phased out.

2. Policies should encourage a culture of enterprise among European farmers with state support being earned rather than given as a right.
3. Policies should ensure an ample supply of safe, affordable, nutritious food.
4. European support for farming should be directed towards policies that preserve the environment, contribute to thriving rural economies and meet other social objectives, recognizing the particular needs of rural communities which, for reasons of location, climate or soil cannot compete effectively in a free market.
5. European policies should give national and regional governments flexibility to address local environmental and social needs whilst ensuring that local interventions do not distort the effectiveness of the European single market.
6. In developing policies the EU institutions and national and regional governments should involve all aspects of government – environmental, trade, consumer, social and foreign affairs, tourism and finance as well as agriculture – and ensure that discussion reflects the interests of all stakeholders. Reform should form an integral part of the post-Nice agenda.
7. Agricultural reform should be compatible with the interests of the new EU members.
8. The EU should pursue an international approach to the regulation of scientific innovation in agricultural and food production.
9. Pursuing agricultural reform on the basis of the above principles should enable the EU to adopt a proactive and positive approach to further trade liberalization in the WTO. This will involve the

abolition of export subsidies, the lowering of tariff barriers and the opening up of European food markets to fairer competition from elsewhere.

We believe that the Fischler proposals, in meeting these criteria, offer benefits to all stakeholders. Taxpayers will be required to pay less in the future, and the considerable levels of support which remain will produce tangible benefits to all those who are committed to a pleasant and viable countryside. Consumers would expect to pay rather less for their food. Environmentalists would welcome a massive switch in public funding from market subsidies to environmental support programmes. Businesses recognize that the reforms will enable trade liberalisation to be extended, giving them wider marketing opportunities. The new members of the EU will see the Fischler approach as being fairer and more tailored to their needs than the existing proposals being offered.

We also believe that, whilst many farmers will be apprehensive of change and therefore resist it, their best interests would be served by accepting the Fischler approach rather than rejecting it. The amount of money available to farmers will decrease by a relatively small amount (20% over 7 years), but much of this can be recovered by denying 'middlemen' the opportunity to exploit the present system. It is estimated that only two-thirds of the money currently made available ends up in the farmers' pockets. Larger farmers would receive less support, but they will be able to offset this by expanding their business as production quotas and restraints are reduced. Smaller farmers should receive more support, although in return they will be expected to adopt environmentally friendly practices. Organic farmers would benefit at the expense of those who damage the environment. The vast number of small farmers in, for example, Poland, will find that the Fischler approach is much more appropriate to their needs and expectations than the existing proposals. Enterprising farmers, keen to diversify, will be encouraged to do so. Elderly farmers will be given more incentives to retire. The growing importance of part-time

farming, as an essential means of maintaining a vigorous rural society, will be recognised.

Some will question why it is necessary to pay farmers anything to pursue responsible farming practices, arguing that regulation is a much more effective way. The state is much better at restraining people from behaving badly than it is at encouraging them to become more responsible. But the state, through incentives, can persuade farmers that it is in their own interests to improve their practices.

There is a danger that payments for good environmental practices will generate even more costly and potentially corrupting bureaucracy. A common sense approach to enforcement is essential, using a mixture of self-regulation and light-touch inspection but with severe penalties for failing to comply.

Germany would like to see much of the financing of agricultural policies handed back to member states in order to reduce its own contributions to the EU budget, but the poorer, new members argue that this would be unfair, because they would not be able to provide the levels of support affordable by the richer countries. There needs to be a compromise here. The poorer countries must continue to get the benefits of fiscal transfers, but regions and nations should have the right to address their own rural problems as long as, in doing so, they do not distort the single market.

Whilst many of the proposals can be implemented unilaterally across the European Union, any initiatives to reduce trade barriers will require reciprocal action from other countries. The US and Canada in particular must tackle their own protectionist practices. There will have to be basic standards of food safety if markets are going to be opened up. The monitoring of scientific developments such as genetically modified plants and hormone treatment of livestock must be consistent and agreed internationally.

But poorer countries cannot be expected, in their domestic markets, to meet the standards of food safety, environmental and animal welfare regulation which richer countries can afford. And national and regional diversity must be tolerated, even if North European animal lovers are understandably shocked by the bull fighters of Spain.

Older farmers remember the horrors of rural poverty in the pre-war years, and fear that if reformers win the day, they will revert to the misery of Steinbeck's *Grapes of Wrath*. But they need not be fearful. There is no plan to eliminate all support. Levels of aid will remain at 80% of existing levels. Furthermore the state offers its citizens, including its farmers, a range of social provision which were miniscule in those days – high standards of health care, extensive social security safety nets and acceptable support for the old. A generation ago many farmers in remote areas could not compete against those who lived close to lucrative urban markets. Now, thanks to the motorway revolution, most farmers can access and compete in these markets.

The competitive gap between European and North American agriculture has narrowed as European farmers have improved their outputs and reduced their costs through amalgamation and investment in scientific and technological innovation. Although, as a result, there are far fewer farmers, the industry still experiences severe labour shortages, because farmers' sons and daughters much prefer the opportunities available to them in the towns, compared with the physically demanding nature of farmwork. Ironically, if Western Europe's labour intensive farming of livestock and produce is to survive, it will increasingly have to rely on migrant labour from the new members. If labour is not available, it would be logical for Polish farmers to supply these markets, rather than the Danish, Dutch and Lincolnshire ones.

This project argues that the reform of agricultural policies offers real benefits to Europe's citizens, including most farmers. We believe that

the commitment to enlarge the EU and liberalise global trade in food can only be achieved after radical agricultural reform. If the EU's political leaders fail to meet the challenge of reform, they will jeopardise enlargement and global trade agreements, thereby undermining social stability and economic prosperity. And if they fail to reform the most anomalous and inappropriate of the EU's policies and institutions, they will do untold damage to the credibility of the EU itself.

Executive Summary

European farmers receive 40% of their total revenue from the Common Agricultural Policy, at an annual cost of around €95 billion to European taxpayers and shoppers. Spiralling costs, growing food surpluses, concern about the environment and pressure from international trade agreements have increased the pressure on the European Union to reform the CAP.

A broad model of CAP reform has emerged among agriculture policy circles over recent years, elements of which have been implemented in the reform rounds of the 1990s. Yet the CAP remains expensive, inefficient and out-dated. The purpose of this report is not to describe what a reformed CAP should look like, but to address the vexed political question of *how to get there*. This requires a better understanding of the distinctive politics of European agriculture and practical steps to help policy entrepreneurs tip the balance in favour of reform.

Over the years the CAP has generated a political dynamic whereby the potential costs of reform are highly *concentrated* among a clearly defined and relatively small group of farmers while the potential benefits are *dispersed* throughout the whole of European society. Agricultural interests dominate a complex and opaque decision-making process that has many veto points for opponents of change. Most changes to the CAP have been small, incremental and focused more on addressing short-term problems than working towards a clear long-term vision.

Variation in farm structures and diverse social and political attitudes to farming and the countryside give rise to different approaches among national governments to the CAP. Traditionally the UK, Sweden, Denmark and the Netherlands have been the most pro-reform countries. France, Spain, Ireland, Greece and Portugal have been the strongest

opponents of change. But crucially, the ever-increasing burden of EU contributions on German taxpayers and shockwaves from the recent BSE crisis have combined to make Germany much more favourable to reform.

The European Commission's proposals for the 2002/03 Mid-Term Review have the potential to be the most radical in CAP history. The proposed reforms could reduce food prices for shoppers, make it easier for farmers to read market signals, remove incentives for farmers to over-produce and make the countryside a better place to live and work. Bureaucracy would be reduced and freer markets would increase opportunities for entrepreneurial farmers to get better returns on their businesses. The CAP would be made more compatible with the enlargement of the EU into central and eastern Europe and the EU would be able to assume a strong position in the current round of WTO negotiations. Farmers would no longer enjoy artificially inflated prices and farm support payments would be made conditional upon observing good farm practice. Agricultural land values may fall, eroding the wealth of landowners although reducing rents for tenant farmers. Although there would be long-term benefits from a freer, less constrained agricultural marketplace, many farms would have to make significant and difficult adjustments to this new business environment.

While farm unions strongly opposed to CAP reform have traditionally dominated the debate at national and EU level, their position is under challenge from a diverse constellation of NGOs and lobby groups in favour of reform. Despite food safety scares and a "rural crisis" in some regions, agriculture policy does not appear to be a salient issue in day-to-day politics. There is little evidence of a groundswell of public support for CAP reform. Yet opinion surveys show that many European citizens back the core policy objectives of CAP reform.

Longstanding political obstacles to CAP reform can only be overcome through policy entrepreneurship. This takes many forms, including the following:

- 1. Policy proposals for a reformed CAP should pay attention to political viability as well as economic efficiency.** The CAP has created entrenched interests that benefit from the status quo. Reform is bound to create some losers. Compensating losers helps reduce political opposition to reform. Providing special help to the large number of small farmers is a relatively inexpensive way to diffuse a significant obstacle to reform. Converting existing subsidies into tradable bonds helps to offset the negative effect of a gradual phasing out of subsidies. Other ways to increase political viability through policy design include: Implementing reform gradually; minimising redistribution between countries; increasing national discretion; encouraging private sector farm safety nets; and ensuring that farm support payments underpin farm incomes rather than land values.
- 2. A broad, inclusive coalition reflecting the many benefits of CAP reform will increase the political pressure for reform.** Farming interests opposed to reform dominate the debate on the CAP. But ever more NGOs and other groups are taking an interest in CAP reform. Building a coalition from diverse interests means establishing common ground and maximising the mobilisation of all potential winners. The issue of CAP reform has many dimensions. The way reformers frame the debate will vary depending upon the audience.
- 3. Changing the CAP decision-making process could increase the chances of achieving reform.** Current decision-making structures are secretive, dominated by agriculture interests and provide many veto points for opponents of reform. Opening up the Council of Ministers to public scrutiny and increasing the role of finance, trade and environment ministers will increase the chances of reform.
- 4. Reformers should anticipate and take advantage of the limited windows of opportunity when CAP reform is possible.** Factors

that determine windows of opportunity for CAP reform include WTO negotiations, the timetable for enlargement of the EU, national election cycles, EU budget timelines and the rotating EU Presidency.

1 Introduction: a route-map for reform

Throughout the developed world, agricultural subsidies have proved notoriously resistant to reform. While economic sectors such as energy, heavy engineering, manufacturing, transport and telecommunications have been subject to deregulation, privatisation and trade liberalisation initiatives, farming continues to be subject to complex systems of state intervention and trade protection.

The Common Agricultural Policy of the European Union is no exception. Reforms during the 1990s made some improvements to the CAP but fell short of the radical change sought by most reformers. European agriculture remains among the most heavily subsidised in the world.

The need for reform has never been greater – and the opportunity for reform has never been better. The CAP has done little to address the social and economic consequences of structural economic changes in Europe's remote and deprived rural areas. In some cases it has made matters worse. Farm incomes have fallen to historically low levels. Public confidence in some modern farming methods has been shaken by food safety scares. And as it stands, the CAP is endangering Europe's ambitions for further agreements on world trade liberalisation and enlargement into Central and Eastern Europe.

Europe has an unprecedented window of opportunity to create a new agricultural and rural policy framework to address the needs of today and meet the challenges of the future. While setting budgets until 2006, the Agenda 2000 agreement provided for a Mid-Term Review (MTR) process in 2002-03. The Commission has made radical proposals for the MTR and started a debate that will intensify over the next six months.

There is no shortage of scholarly critiques of the shortcomings of the CAP and there are many imaginative blueprints for what a reformed CAP should look like.¹ This report is not meant to add to this literature. The intention is rather to understand, in political terms, *how to get there*.

The report describes the political landscape of CAP reform and outlines a political route-map for reform. The analysis focuses on likely winners and losers from CAP reform, public attitudes to farm and rural policy, variation in the approaches of EU member states to the CAP and the role of public institutions and interest groups at EU, national and regional levels. The upcoming Mid-Term Review is examined, both in terms of the political rationale of the Commission's radical proposals and the emerging groupings of pro- and anti-reform member states. As a political process CAP reform does not exist in isolation. It influences and is influenced by other highly politicised processes including WTO negotiations and development and enlargement of the European Union itself. These important linkages are of central importance to the political dynamics of European agriculture policy.

The report concludes with ideas about how policy entrepreneurs can increase the chances of achieving CAP reform. Political viability of reform proposals can be increased through smart policy design. A broad, inclusive and vocal coalition for reform will increase the pressure on politicians to deliver reform and challenge the dominant position of farming interests opposed to reform. The rules of the CAP decision-making process can be changed to correct the current bias against reform. CAP reformers must anticipate and make the most of limited windows of opportunity where an agreement on radical reform is feasible.

2 The direction of reform

The evolution of European agriculture policy

A founding element of the European Economic Community, the CAP was constructed along the lines of existing French and German agricultural subsidy arrangements. Its aims reflected post-war concerns: the prevention of food shortages, the stabilisation of food prices and the guarantee of reasonable incomes to European farmers. Until the 1980s the CAP operated through a combination of agricultural prices fixed above prevailing world prices, tariff and quota barriers on imports into the Community and subsidies for EU exporters. In this form, the CAP was largely a transfer of income from shoppers to farmers through an invisible food tax. This kept the high level of support concealed and the role of government obscured.²

Increases in agricultural productivity and the maintenance of Community prices above market clearing levels led to large surpluses in many commodities and expensive budgetary measures to dispose of them. An attempt to address the surplus problem was made in the 1980s with the introduction of quotas to limit production in some sectors. Even after quotas were introduced, ever greater intervention buying and export subsidies increased costs to taxpayers.

The CAP has contributed to dramatic increases in the productivity of European agriculture and the increased wealth of many agricultural landowners. The downsides are higher food prices for shoppers, a heavy burden on taxpayers, the destabilisation of world markets, environmental damage and increased bureaucracy.

The MacSharry reforms of 1992 brought about reductions in support prices, with farmers being compensated by new direct payments linked to historic yields. In some cases direct payments were structured to

Table 1: Evolution of the CAP: conceptual differences

	Original CAP	Current CAP	"Emerging model" for future of CAP
Type of support	Price supports	Direct payments	Direct payments
	Linked to production	Linked to production	Decoupled from production
Environmental and rural economy aspects	No environmental conditions	Some environmental conditions	Many environmental conditions
	No rural development & environmental measures	Some rural development measures	More rural development & environmental measures
Trade aspects	Export subsidies	Export subsidies	No export subsidies
	Import barriers	Import barriers	Reduced import barriers
Administration	Centrally run	Centrally run, with some national and regional discretion	More national and regional discretion
	Less bureaucratic	More bureaucratic	More bureaucratic
Who pays?	Shoppers	Shoppers and taxpayers	Taxpayers
Visibility of support levels	Low	Medium	High
Objectives	Increase food production; ensure stable prices; boost farm incomes	Boost farm incomes; encourage environmental protection	Develop rural economies; protect rural environment; reward good farming practices
Economic distortion	High	Medium to High	Low
WTO green box compatible	No	Partially	Yes
EU food prices	Above world prices	Above world prices	Closer to world prices
Budgetary cost	Low to medium	High	Medium to high
Financial Commitment	Open-ended	Budget ceilings	Budget ceilings

encourage less intensive production methods. This was an attempt to break the link between production levels and subsidy levels and thereby reduce incentives to over-produce. The Agenda 2000 reforms agreed in 1999 continued the MacSharry approach of price cuts compensated by direct payments. Together, the reforms of the 1990s started to transform the CAP from a farm subsidy system paid for by shoppers into a farm subsidy system paid for by taxpayers. Direct payments have increased the visibility of farm subsidies (both to farmers and to the general public) and have required that farmers apply to the government to receive a growing proportion of their support. The reforms have reduced the overall level of transfers from European society to its farmers by around 30%.³ However, the CAP still represents around half of the total EU budget.

The new “second pillar”

The most innovative element of the Agenda 2000 agriculture package was the creation of a “second pillar” of the CAP known as the Rural Development Regulation (RDR). Pillar II enshrines at EU level a number of environmental and broader rural development schemes designed to recognise the environmental, social and cultural aspects of farming (known as “multifunctionality”).⁴

By and large Pillar II supports are decoupled from production levels and so cause much less economic distortion than the direct market interventions of Pillar I. For this reason Pillar II measures are exempt from commitments to reduce trade-distorting farm subsidies made by the EU in free trade agreements.

According to the World Trade Organisation (WTO) *Agreement on Agriculture*, to qualify for the “green box” exemption, a subsidy must not distort trade, or must cause minimal distortion. The subsidy must be government-funded (i.e. not funded by charging consumers higher prices) and must not involve price support. They tend to be programmes that are not directed at particular products, and include direct income supports for farmers that are not related to production.

Although widely welcomed by many long-time CAP reform advocates the Pillar II currently represents just 10-15% of the total CAP budget. Agenda 2000 gave member states the option of transferring up to 20% of Pillar I expenditure into the Pillar II but only the UK has opted to do so.⁵ Expenditure in Rural Development Programmes varies greatly between member states reflecting historically different levels of commitment to rural development and conservation objectives.

The development and future of Pillar II is the subject of a forthcoming Foreign Policy Centre policy brief.

An emerging reform model

Changes to the CAP over the past 15 years suggest an emerging model for reform, towards which the CAP is slowly moving.⁶ Table 1 shows the key conceptual differences between the old-style CAP, the current CAP and an emerging model for a reformed CAP. Although the emerging model is quite different from the original CAP in both its objectives and policy instruments it does not represent a challenge to the underlying policy paradigm that European farmers are entitled to large transfers of money from the rest of society.⁷

3 The politics of previous CAP reform attempts

Analysis of previous reform attempts gives important lessons on the political challenges of CAP reform today.

Mid-1980s

The reforms of the 1980s were driven by the twin problems of rising budgetary costs and food surpluses. The reforms did not solve the root causes of the problems; rather they worked to reduce some of the symptoms. Among member states, the UK and the Netherlands were the strongest proponents of reform. France and Germany were opposed to major changes. Farmers opposed the reforms, and there was little involvement of other groups such as taxpayer and consumer groups or environmentalists.⁸

1992: MacSharry Reforms

The 1992 reforms were driven by the continuing problem of structural surpluses combined with the need to find an accommodation on agriculture within the ongoing Uruguay round of GATT negotiations. The CAP was coming under heavy diplomatic pressure from the United States and the Cairns Group of agricultural exporting countries. It was possible that the CAP would become a major obstruction to a wider agreement on trade liberalisation that would bring real benefits to the EU economy.

The original proposal by Commissioner MacSharry was more far-reaching than the final agreement. The UK, the Netherlands, Belgium and Denmark advocated radical reform. France was a strong opponent of any reform although in the end it did not veto the final, weakened reform package. It has been suggested that on this occasion the desire of the French business sector for success in the GATT round prevailed over the political power of French farmers strongly opposed to reform.

The need to deliver CAP reform to ensure success in the GATT round is what tipped the balance in 1992.⁹

The MacSharry reforms are the most significant in the history of the CAP. They represent the beginning of a real change in emphasis from price support to direct payments and signal the future direction of reform. Farmers strongly opposed the idea of direct payments, arguing that it was undignified to receive government handouts. It is possible that their fears were well founded. Direct payments have created important political feedbacks that further undermine the CAP. First, they have revealed how much Europe spends on its farmers and how reliant European farmers are on public subsidy. Second, they have required the imposition of significant new bureaucratic burdens on farm businesses. Both of these (unintended) effects have generated new impetus for further CAP reform.¹⁰

1999: Agenda 2000

The Agenda 2000 agreement was driven by the need to ready the CAP for the eastward enlargement of the EU and the new round of WTO negotiations. There was also a desire to address the problem of the ever-increasing CAP budget. For the first time there was an important environmental driver as it became increasingly evident that intensive agriculture was having a damaging effect on the environment.

During the Agenda 2000 negotiations the UK, Sweden, Denmark and Italy joined together as the pro-reform “gang of four”. France, Spain, Portugal, Greece and Ireland were the strongest opponents of reform, with Germany also opposing many of the gang of four’s proposals. In March 1999 Agriculture Ministers agreed a package of measures that, although less radical than the Commission had originally proposed, represented real progress towards reform. Yet Heads of Government further watered down the reforms at the Berlin Summit in July 1999, an outcome seen as a victory for French President Jacques Chirac.¹¹

The Agenda 2000 reforms did nothing to reduce the *budgetary* cost of

the CAP since compensation for cuts in support prices actually increased burdens on taxpayers. Even so, it is estimated that once fully implemented in 2008 the package will bring annual net economic welfare benefits of €7.5 billion to the EU economy (not including dynamic gains through reduced economic distortion).¹² Environmentalists and countryside groups welcomed the creation of a second pillar but recognised that in terms of funding, the RDR would be dwarfed by old-style production subsidies. Agenda 2000 put off most of the difficult questions relating to enlargement and the WTO for another day.

Common Themes

Common themes emerge from the history of CAP reform:

First, the reform process tends to move at the pace of the slowest. Reform proposals are drawn up by the Commission, which in the interests of the wider project of European integration, places a strong emphasis on accommodating the needs of each member state. The Commission and the Agriculture Council try to achieve consensus and avoid conflict wherever possible. Many veto points in the EU decision-making process provide opportunities for opponents to obstruct reform. As former French Agriculture Minister Jean Glavany has remarked: “The CAP is a heavy cruise ship that can’t make a U-turn like an inflatable dinghy... all it takes is for one country to oppose it, for the rules not to change.”¹³

Second, farmers and their representative organisations have strongly opposed reform and have succeeded in preventing radical change. The benefits of the CAP are *concentrated* among the EU’s 7 million farmers; the costs of the CAP are *dispersed* among 375 million EU citizens. This means farmers have always been much more strongly motivated to lobby governments to preserve the CAP than the rest of society is motivated to campaign for reform.¹⁴ It has been estimated that EU farmers’ stake in preserving agricultural support is, on average, 9.5 times higher than consumers’ and taxpayers’ stake in eliminating it.¹⁵

Third, the pre-eminence of agriculture ministries in CAP decision-making militates against reform. Politicians and officials in these ministries usually have close links to farming representatives and tend to see their role as serving farm interests. Sometimes this can be at the expense of other parts of society. Finance and environment ministries have a legitimate interest in the workings of the CAP, but have rarely had much of a look-in. The freedom of agriculture ministers to advance the sectional interests of a national farm lobby will usually be greater in a coalition governments. In multiparty systems where coalition governments are the norm a small rural or farming party may only agree to join the governing coalition if it is awarded the agriculture portfolio. Coalition governments tend to have lower levels of collective responsibility and this allows a greater degree of autonomy for individual Ministers.¹⁶

Fourth, the higher the costs of no agreement, the more likely it is that a significant reform will take place. CAP reform has tended to come about as a direct reaction to acute problems, rather than as a carefully planned evolution of agriculture policy.¹⁷ Of these acute problems, external issues have been more powerful drivers for reform than internal problems. The need to find an accommodation between the CAP and the Uruguay round of the GATT was the single largest driver of the MacSharry reforms. Enlargement of the EU was a major driver for Agenda 2000. Internal drivers like budgetary pressure, high food prices, low farm incomes, food surpluses, market distortions and negative environmental effects have not created sufficient political momentum to bring about significant reform. These types of drivers have been ignored, sidestepped or resulted in modest and incremental changes and adjustments.¹⁸

Fifth, there has been a powerful Franco-German axis in CAP decision-making. As with the European integration project, Franco-German bilateralism is central to the history of the CAP. When France and Germany oppose one another, the result has usually been deadlock. When they agree, their common position tends to the position accepted

by other member states. France has often adopted a leadership role with respect to southern countries. Many northern countries have looked to Germany.¹⁹ Two recent challenges to Franco-German hegemony are the formation of pro-reform groupings in 1992 and 1999, evolving into the CAPRI group in 2000 and the recent changes in the agricultural policy of the German government following the BSE crisis.

Sixth, reform to date can be characterised as “tinkering rather than tackling”. Even after the changes of the 1990s the CAP is still largely unreformed. 85-90% of agricultural supports are market distorting; export subsidies have a dramatic and destabilising effect on world markets; tariff barriers continue to disadvantage imports into the EU. Existing policy arrangements tend to condition the range of alternative responses to problems that arise. Faced with complexity and uncertainty, policy makers tend to prefer incremental changes to existing policies over radical reforms unless the total failure of the existing policy becomes apparent.²⁰ Furthermore, the EU-wide network of agriculture and rural policy experts remains strongly committed to an interventionist policy paradigm and so favours moderate change over fundamental reform.²¹

4 Winners and losers from CAP reform

A careful assessment of who wins and who loses from reform is central to understanding the politics of the CAP. By providing large subsidies to farmers the CAP has created many beneficiaries. But this has meant burdens for those taxpayers and shoppers who foot the bill, for the wider European economy and for countries outside the EU.

The current CAP

Where does the money go?

Farmers are the major recipients of CAP subsidies. The OECD's calculation of Producer Support Estimates indicates that in 2000 subsidies accounted for around 40% of gross farm revenues in the EU. This is the equivalent of €14,462 per person employed in farming, or €751 per hectare.²² Subsidies are not evenly distributed across agricultural sectors. The most heavily subsidised sectors are arable crops, dairy, sugar, beef, sheep, tobacco, cotton and olive oil. By comparison horticulture, poultry, egg and pig farmers receive very few subsidies. Farms in remote and marginal areas tend to be more heavily reliant on state support than farms in prime agricultural land.

The close link between output level and subsidy means that large farms receive a large proportion of CAP support. The largest 2% of farms receive 24% of all direct payments while the smallest 60% of farms receive just 10%.²³

While farmers are the primary recipients of CAP subsidies there are “upstream” beneficiaries, primarily landowners, suppliers of farm inputs and commodity traders. An OECD study estimates that in the absence of agricultural subsidies land prices could fall by 30-40% across the EU.²⁴ In the years just after the UK joined the EEC agricultural land prices increased by 50% in real terms as the value of

future CAP payments were capitalised into land values.²⁵ When New Zealand abolished its agricultural subsidies in the mid-1980s land prices fell by 60%. They have recovered since then, but remain 25% lower in real terms.²⁶

By encouraging high productivity, the CAP stimulates demand for farm inputs such as agrochemicals and farm machinery. As production subsidies are reduced, it can be expected that revenues and profits to firms supplying these inputs would fall.²⁷

The high level of intervention in agricultural markets has created a whole new sector of commodity traders and storage agencies. Most estimates put the cost of this at around 10-15% of the total CAP budget.

Who pays?

Taxpayers and shoppers pay for the CAP through EU budget contributions and higher food prices respectively. The CAP budget for 2002 is €45 billion.²⁸ The total annual cost to EU shoppers of artificially high food prices is estimated to be in the region of €50 billion.²⁹ Together this works out at over €250 a year for each EU citizen.

Insofar as the CAP encourages a more intensive form of agriculture than would prevail in a freer market, there are additional costs to society in the form of avoidable environmental damage. It is very difficult to quantify environmental damage in monetary terms. One estimate is that intensive farming in the EU causes avoidable environmental damage costing around €9 billion a year.³⁰ A detailed study estimated the value of negative environmental impact of agriculture to be £2.3 billion a year in the UK alone.³¹ Not all of this can be directly attributed to the CAP, although it is a contributory factor. It is also argued that sustainable agriculture brings important environmental benefits in terms of landscape and biodiversity.

Countries outside the EU also pay a price for the CAP. Subsidised exports of food from the EU destabilise world markets and depress

prices. Barriers to imports into the EU disadvantage competitive non-EU farmers. Developing countries are estimated to face annual welfare losses of \$20bn a year as a result of the developed world's agricultural policies.³² Part of that is due to the policies of the US and other developed countries but the CAP is the single largest culprit. Even the EU's recent initiative to give the very poorest developing countries free access to its markets for 'everything but arms' contained significant exemptions and delays for three key developing world agricultural exports (rice, sugar and bananas).³³

A reformed CAP

Who gains from reform?

Reform of the CAP would bring a wide range of benefits. Shoppers would enjoy some reduction in food prices. A more economically rational agricultural and rural policy would deliver savings for taxpayers. Additional spending on rural development and agri-environment schemes will make the countryside a better place to live and work. Food manufacturers and retailers, although seldom ready to put their heads above the parapet, are opposed to trade protection and artificially high EU farm prices. Developing countries would benefit from freer access to EU markets and reduced dumping. Enlargement of the EU would be less problematic. The EU negotiating position in the Doha round of WTO talks would be strengthened.

The emerging model of reform set out in Section 2 does not mean the abolition of all state support for agriculture. Considerable sums of taxpayers' money will continue to be transferred to farmers and rural areas. Entrepreneurial farmers will benefit from less constrained and distorted agriculture markets. Enterprising and environmentally aware farmers will stand to benefit from a greater emphasis on Pillar II support measures.

Although inflated land prices increase asset values for landowners, they can increase farm operating costs substantially, thereby reducing competitiveness and creating incentives for farmers to be landowners

before being efficient farmers. High land prices and rents stifle innovation, business growth and the ability of the farm sector to adjust to a changing marketplace. Artificially inflated land prices make it more difficult for successful farmers to grow their businesses and increase the debt burden of farmers buying new land.

Higher land prices mean higher rents for tenant farmers. 39% of EU farm area is tenanted. The greater the extent to which production subsidies have become capitalised into land values and rents, the smaller the benefits of the CAP to tenant farmers. Reducing land values ought to have the effect of reducing the rents that tenant farmers pay.

The CAP encourages the overproduction of supported commodities, driving down prices and profit margins. State intervention in production decisions partially disconnects farmers from market signals. Decoupling support from production will reconnect farmers with the changing needs of their customers, and ensure that it is consumer demand that determines what farmers produce.

A fall in the EU price of animal feeds will be a benefit to intensive, non-grazing livestock farms and poultry and egg farms, as animal feeds are a significant input cost.

Who loses from reform?

Despite many potential winners, it is the potential losers that dominate the politics of CAP reform. Potential losers are almost always the most vocal in debates over policy change. Decision-makers often shy away from making policy improvements because they expect the political backlash from the losers will outweigh the political rewards from the winners. Understanding the needs of potential losers and incorporating them into reform proposals is central to increasing the political viability of reform.³⁴

Although there are many benefits to farming from the replacement of a distorting subsidy system with a broader rural development and agri-

environment policy the fact is that CAP supports currently provide 40% of the gross revenue of European farming. Phasing out these supports, even if new supports are made available through Pillar II, will have a profound impact on most farm businesses. In the short-term the impact on many farm businesses will be negative.

Some uncompetitive farm businesses have been kept afloat by subsidies. These businesses will have to make significant adjustments to prosper under a reformed CAP. Not all farmers have the business know-how to manage this change successfully. Long-term structural changes will continue and even accelerate. Some farmers will choose to exit the industry.

As Table 2 shows many farm households already have income from non-farming activities. For 35% of European farmers farm income represents less than half of total household income.³⁵ This diversification into non-farming activities will be further encouraged by CAP reform.

The farms that lose most from a shift from Pillar I supports to Pillar II supports are those most reliant on current production subsidies and those which have the least opportunity for diversification and qualification for expanded rural development and agri-environment measures. Although it is very difficult to generalise across diverse farm sectors, farms at greatest risk include the least competitive arable, sugar beet, intensive beef and dairy operations.

Landowners may experience a fall in the value of their assets and thus an increase in their debt/equity ratios, which could reduce their ability to borrow money. The position would be worse for individuals who had bought land relatively recently. Significant falls in land prices could lead to a negative equity problem for farmers carrying a high level of debt.

Even within a single farm sector, debt levels vary enormously, reflecting the history and past business decisions of the farm. On

average, debt levels are highest in the most capital-intensive farm types like intensive livestock, dairy and horticulture.³⁶ Of these, intensive livestock and dairy farmers appear to be at greatest risk from the effect of a decrease in land values on debt levels. Although fairly highly indebted, pig, poultry and egg producers are relatively lightly aided under the CAP, so have far fewer subsidies to lose.

Table 2: Farm diversification by member state, 2000

	Percentage of farmers for whom farming accounts for half or less of total income
Denmark	65
Greece	55
Sweden	55
Austria	48
UK	47
Ireland	44
Belgium	39
Germany	38
Finland	37
EU-15	35
Portugal	35
France	33
Spain	30
Italy	29
Netherlands	27
Luxembourg	24

Source: Eurobarometer Flash Survey No 86 (Sept-Oct 2000)

Table 3 shows that the more commercial and capital-intensive farm sectors of northern Europe have the greatest ratio of debt to gross value added. Farm debt is a less significant problem for farmers in southern Europe and the Mediterranean.

Table 3: Farm debt to gross value added ratios

	Average debt per farm/euros	Average gross value added per farm/euros	Ratio of debt to gross value added
Denmark	345,029	55,962	6.2
Sweden	109,240	18,698	5.8
Finland	51,804	12,992	4.0
Netherlands	320,692	81,190	3.9
Belgium	114,231	39,804	2.9
Austria	31,445	11,575	2.7
Germany	92,432	35,514	2.6
UK	101,524	45,872	2.2
Luxembourg	94,026	43,960	2.1
France	96,227	46,658	2.1
Ireland	13,864	18,278	0.8
Portugal	1,775	6,511	0.3
Spain	4,704	18,758	0.3
Italy	2,613	12,241	0.2
Greece	531	10,003	0.1

Source: Eurostat, own calculations

The long-term shedding of manual labour by the farming sector is likely to continue, and may be accelerated by CAP reform. However

rural employment would benefit if Pillar II measures are designed to encourage labour-intensive rather than capital-intensive activities. Enterprises focussed on environmental stewardship, tourism and leisure and food processing would clearly require more labour than a modern, mechanised farm.

5 Attitudes of European society to reform

Public opinion

Public opinion surveys reveal that agriculture policy is rarely a salient issue in European public discourse and that the European public is fairly uninformed about how the CAP works. Despite this, there is evidence that the objectives of CAP reform could be expected to win the support of European citizens.

Aims and objectives

When asked about the rationale for agriculture policy, the two most popular objectives are consumer-related: 'ensuring that agricultural products are healthy and safe' (90% approval) and 'promoting respect for the environment' (89% approval). This compares to 'providing farmers with stable, adequate incomes' (77% approval) and 'reducing development gaps between regions' (74% approval).

The policy objective of 'protecting small and medium sized farms' has an approval rating of 82% among all Europeans. Approval of this objective is strongest in member states with large rural populations and many small farms (Spain, Greece and Portugal), and weakest in member states where the population is predominantly urban and farms are larger and more commercially oriented (Denmark and the Netherlands).

80% of European citizens agree that the EU should intervene through agriculture policy to 'favour and improve life in the countryside'. Again, the highest approval ratings are obtained in Spain, Greece and Portugal. Countries where support for this objective is weakest are Denmark and the Netherlands, just behind Belgium and France.³⁷

In 2000, another survey showed that there was strong support for the CAP within the EU public. 46% felt that agricultural support was

insufficient and 28% said it was sufficient. Only 15 per cent said that it was too high.³⁸

In the same survey, a majority of Europeans thought the move from Pillar I to Pillar II was a good thing (65%) or a very good thing (10%). Only 15% felt it was a bad thing. Table 4 shows that support was strongest in Ireland, Greece, France and Spain and weakest in Sweden and Denmark. This is a rather surprising finding, contradicting the respective positions of the governments of these member states.

Table 4: Attitudes to switching support from Pillar I to Pillar II

	Approval rating	
	General public	Farmers
Ireland	44	36
Greece	44	40
France	42	11
Spain	41	18
Germany	39	12
Belgium	38	6
EU-15	37	22
Luxembourg	37	5
UK	36	15
Italy	35	27
Portugal	33	29
Finland	32	-5
Austria	31	5
Netherlands	31	15
Sweden	15	-9
Denmark	9	2

Source: Eurobarometer Flash Survey, 11/2000

As would be expected, farmers are less favourable than the general public towards the idea of shifting resources from Pillar I to Pillar II. Interestingly, there is a much closer correlation between farmers and the general public on this issue in Greece, Ireland, Italy and Portugal than in the other eleven member states, perhaps reflecting the large number of farmers in these countries and closer social links between farmers and the rest of society.

Performance

Asked whether the CAP is delivering on its policy objectives, respondents to the Eurobarometer survey were fairly evenly divided between those who think the CAP performs “rather well”, those who think it performs “rather badly” and those who don’t know.

In 2000, 52% of Europeans thought the CAP was able to ensure healthy and safe food. Eight months later and following the news of a growing BSE problem on the continent only 37% remained satisfied. The Commission described the drop in confidence as “alarming.”³⁹

Four out of ten Europeans think that the European Union’s agricultural policy at present fulfils its role in promoting respect for the environment. 34% think that it fulfils its role in this regard “rather badly”. Approval is strongest in Germany (54% approval) and Netherlands (52% approval). Disapproval is strongest in Denmark (54% disapproval), Sweden and France (46% disapproval each).

Only 28% of Europeans think that the CAP fulfils its role “rather well” in protecting small and medium-sized farms, whereas 44% think that it fulfils its role “rather badly”. Germany (45% approval) and the Netherlands (36% approval) compare to Finland (65% disapproval), Denmark (64%), France (58%) and Sweden (54%).

This data shows that despite near unanimity among economists and agricultural policy experts on the failings of the CAP a large proportion of the European public are reasonably favourable about the policy.

There certainly cannot be said to be a significant groundswell of public opinion in favour of radical CAP reform.

Non-Governmental Organisations

NGOs and other interest groups play an important role in mediating between the public and policy-makers. The power and diversity of interest groups affect policy outcomes. It is easier for policy-makers to achieve CAP reform when the issue attracts a large array of diverse interests. There is less room for manoeuvre when a focussed, powerful and united lobby dominates the debate.⁴⁰

One study estimates that roughly £100 million is spent annually on the salaries alone of agricultural NGO lobbyists in Brussels.⁴¹ Farming representatives are still dominant, but other groups are challenging this supremacy.

Farming unions

At EU and member state level farming organisations are committed to preserving the policy paradigm of large transfers of public money to their members, preferably in the form of production-linked subsidies. During the MacSharry reform negotiations farm unions were opposed to moving from price supports to direct payments, arguing that such payments are demeaning to farmers. With the emergence of Pillar II as a possible alternative to production subsidies there is widespread opposition among farm unions to the idea of farmers as “countryside stewards” receiving payment for the delivery of environmental goods. At the EU level, COPA and COGECA – the two largest European farmers’ federations are firmly opposed to any consideration of CAP reform before 2006.

Membership-based farm unions are easily the most influential interest groups in determining European agriculture policy. Within each country farming organisations tend to be monolithic, well organised, well resourced and carefully focussed on a relatively small number of issues that are of great importance to their members.

In northern countries there tends to be a single dominant farm union while in southern countries there are often several organisations representing slightly different farm interests. Table 5 shows that membership densities of farm unions are high compared to other comparable organisations such as trade unions.⁴² High membership density increases the campaigning power of farm unions as well as enhancing their authority and legitimacy as representative organisations.

Table 5: Membership density of farm and trade unions

Proportion of potential members that are actual members

	Largest farm union %	All trade unions %
France	54.5	23
Germany	90	40
Italy	76	50
UK	80	36.5

Source: Keeler (1996)

Close, mutually reinforcing relationships between politicians, bureaucrats and farm unions are typical. These “iron triangles” have formed over time in response to the technical complexity and interventionist character of the CAP and the power and influence of farm unions within the political process, particularly at member state level.

The dominant position of traditional farming unions is not only being challenged by other parts of society, but by other rural voices. In France in recent years the left-leaning Confédération Paysanne has enjoyed a renaissance as an alternative voice for many smallholders who have traditionally been represented by the much larger, right-leaning Fédération Nationale des Syndicats d’Exploitants (FNSEA).⁴³ In the UK the dominant position of the National Farmers Union has come under pressure from organisations that claim to speak for smaller and family farms and wider countryside interests.⁴⁴

Despite being the main beneficiaries of the CAP and despite the support of farm unions for the CAP, public opinion surveys have found that in just two countries (Denmark and Ireland) where the majority of farmers think that the CAP is favourable to them personally.⁴⁵

Table 6: Farmer attitudes to the CAP

"For you personally, would you say that the agricultural policy of the European Union is..."

	Favourable	Unfavourable	Neither	Don't know
Denmark	67	26	5	3
Ireland	65	26	7	3
Spain	34	51	12	4
Sweden	33	53	10	5
Luxembourg	32	42	22	4
Italy	27	65	8	0
EU-15	26	64	9	2
Belgium	26	65	8	0
Netherlands	24	57	8	12
France	21	69	9	3
Austria	20	69	9	1
Finland	19	69	9	3
Greece	19	66	10	5
UK	17	77	3	3
Portugal	14	62	20	4
Germany	12	83	3	2

Source: Eurobarometer Flash Survey, No 86 (Sept-Oct 2000)

Other NGOs

Whereas agriculture policy was once the exclusive preserve of governments, farm unions and agricultural economists, there is an increasingly diverse array of NGOs that are devoting policy development and campaigning resources to agriculture issues.

Membership of the eight largest European environmental NGOs stands at over 20 million members. In some countries the membership of environmental groups as a proportion of the total population is much higher. Environment groups have strengthened their influence in Brussels and are particularly strong in northern member states such as Germany, Sweden, Italy, Denmark, the Netherlands and the UK. Many environmental groups consider agriculture policy to be a central part of their work. BirdLife International, Friends of the Earth, Greenpeace and WWF are devoting significant resources to agriculture policy development and strongly favour the emerging model of CAP reform.

Consumer organisations are stronger in some member states than others, but are a less powerful lobby on the CAP than farmers or environmentalists. A survey in 1999 found that 4% of Europeans are members of a consumers association. The most significant memberships were recorded in Luxembourg (29%), the Netherlands (25%) and Sweden (22%) with membership not exceeding 10% in any other member state.⁴⁶ The gains to consumers through cheaper food and better value for taxpayers' money provide strong motivations for consumer organisations to lobby for CAP reform. The relationship between CAP reform and food safety is less clear, although it could be argued that the emphasis of Pillar II on promoting quality over productivity would lead to improvements in safety standards.

The principal European consumers' organisation is BEUC (Bureau Européen des Unions de Consommateurs). BEUC submits opinions on agricultural and food policy, and has representatives on all committees that deal with consumer issues, including the advisory committees on foodstuffs, agricultural products and customs.

In the UK the two largest consumer organisations consider the CAP and food production policy more widely to be a major policy development and campaigning issue.⁴⁷ In 2000, as a response to the BSE crisis, the German government replaced its federal agriculture ministry with a new Ministry for Consumer Protection, Nutrition and

Agriculture. This change in name has been followed by a major change in policy establishing consumer protection and sustainable agriculture as the top priorities.

Another important lobby with an interest in the CAP is the array of rural development advocacy groups. While sharing many of the objectives of environmental and conservation NGOs, rural development advocates have a broader agenda with poverty, unemployment, infrastructure and public services in rural areas as key issues of concern.

The increasing importance of trade issues to overseas development policy and the adverse impact of the CAP on many developing countries means that development NGOs are more interested in CAP reform than ever before. The abolition of export subsidies and increasing market access for developing countries' agricultural exports are central components of many campaigns for "fair trade".⁴⁸ The WTO Doha Declaration, which places special emphasis on the needs of developing countries, and the success of recent initiatives on debt forgiveness reflect the increasing influence of development NGOs on high-level policy agendas.

While it certainly helps to have environmental, consumer, rural development, taxpayer and international development NGOs in favour of CAP reform it is important to realise that it is just one of many issues of concern for these groups. By contrast, the future of the CAP is probably the single most important issue for farm unions. It can be expected that farm unions will choose to devote more political resources and will be better able to mobilise their members on CAP reform than other NGOs.

6 Member states' approaches to CAP reform

For most of the life of the CAP there has been little appetite among European governments for reform. This is beginning to change. Awareness of the shortcomings of the CAP is growing but there are great differences over how the EU should respond. The high degree of variation in attitudes towards agriculture policy among EU member states is the central feature of the politics of CAP reform.

Understanding general approaches

In recent years the member states most consistently in favour of CAP reform have been the UK, Sweden and Denmark. Recently Germany and the Netherlands have shown an interest in reform. France and Ireland have come out strongly against CAP reform.⁴⁹ Austria, Belgium, Luxembourg and Greece generally fall in behind the French position.⁵⁰

The positions of Italy, Spain and Portugal have been more difficult to discern. They have each advanced their own distinctive reform proposals over the past few years, often concentrating on food quality issues or attempting to reorient the CAP towards "southern" agricultural products. Italy was a member of the "London Club" of reform-minded countries during the Agenda 2000 negotiations. Yet there is little common ground between these countries and the northern European reform bloc.

What explains why some countries are pro-reform and others are not? There are many factors involved, but the three most important are:

- The size of the agricultural sector relative to the rest of the economy.
- Farm structures.

- Prevailing political and social attitudes towards farming and the countryside.

The characteristics of agriculture sectors in the EU

Countries with a relatively large farm sector such as France and Ireland get more net benefits from the CAP than countries with a relatively small farm sector such as Germany, and the UK. Member states that perceive the CAP as a net benefit can be expected to favour the status quo. Countries with large farm sectors are also more inclined to equate farmers' sectional interests with the national interest.

Table 7: Agriculture in GDP by member state

	Share of agriculture in GDP (%)
Greece	6.8
Spain	3.7
Ireland	2.6
Italy	2.4
Portugal	2.4
France	2.3
Netherlands	2.2
Denmark	2.0
EU-15	1.7
Austria	1.2
Belgium	1.1
Germany	0.9
Finland	0.9
United Kingdom	0.7
Sweden	0.7
Luxembourg	0.6

The CAP is biased towards supporting commodities produced in northern Europe, reflecting the agricultures of the six founding members. Since the CAP rewards the most productive and efficient farms, smaller and less efficient farms tend to get fewer benefits. Southern countries with a large number of small farms (e.g. Portugal, Italy and Greece) do less well out of the CAP than countries with larger, more commercial farms.

Table 8: Total support by commodity, 2000

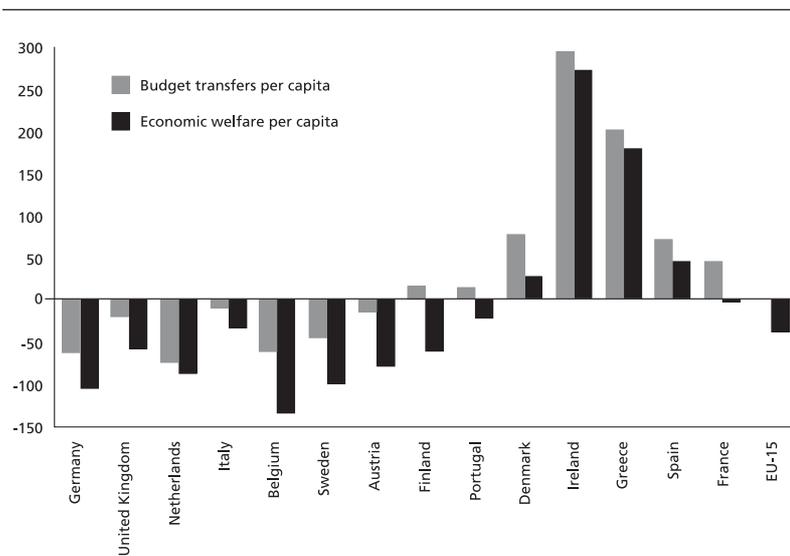
Commodity	PSE* (million euros)	% Gross Revenue
Wheat	8,570	43
Maize	2,335	36
Other grains	5,196	46
Rice	71	8
Oilseeds	1,261	30
Sugar	2,559	49
Milk	15,481	43
Beef and veal	19,856	75
Eggs	398	9
Poultry	4,695	57
Pigmeat	5,749	25
Sheepmeat	3,383	52
Other	28,334	28
Total	97,907	38

* The OECD defines the Producer Support Estimate as "an indicator of the annual monetary value of gross transfers from consumers and taxpayers to agricultural producers, measured at the farm-gate level, arising from policy measures that support agriculture".

Source: OECD (2001)

The benefits of the CAP vary between member states, both in terms of budget transfers and overall economic welfare effects. In terms of budgetary transfers, Ireland, Greece, Spain, France, Denmark, Finland and Portugal gain, while the remaining eight member states are net losers. In terms of overall economic welfare, only Ireland, Greece, Spain and Denmark gain from the CAP. For the other eleven member states the CAP represents a net drain on GDP. The four countries that lose the most from the CAP are Belgium, Germany, the Netherlands and Sweden.⁵¹ Losses to the UK are partially mitigated by its budget rebate mechanism.⁵²

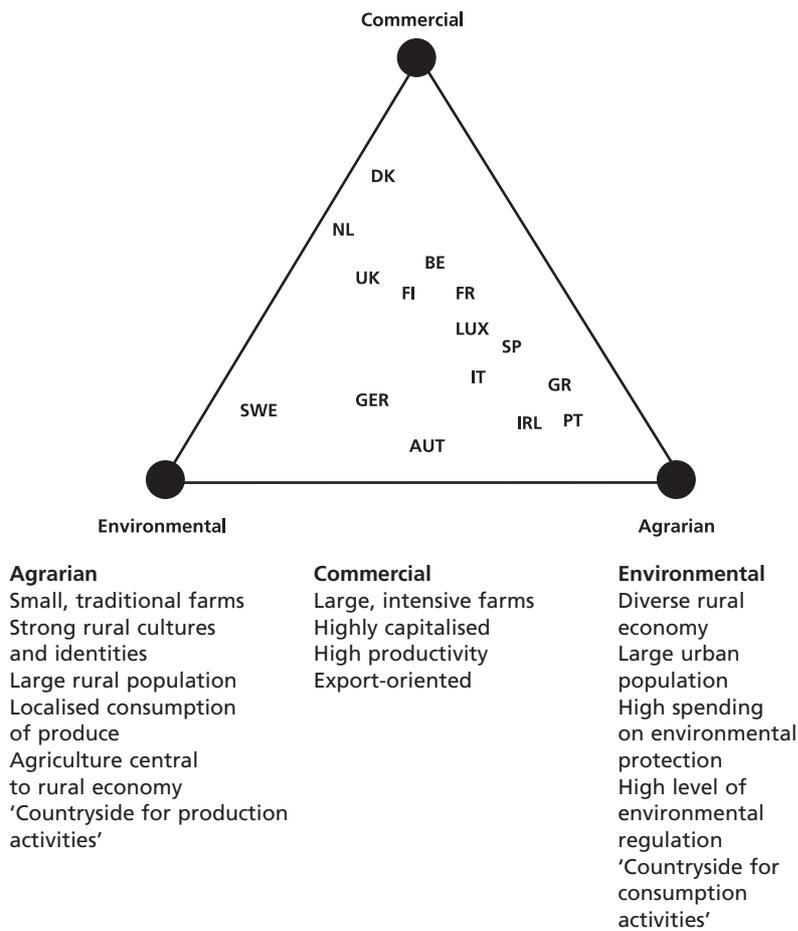
Figure 1: Net budgetary transfers and net economic welfare benefit of the CAP, 1998 (€ per head)



Source: DEFRA

Variation in farming structures and in social attitudes to agriculture and rural areas can be better understood using a three-pole typology illustrated in Figure 2.

Figure 2: A typology of European agriculture



Political factors

In some member states CAP reform is a contentious political issue; in others there is a measure of consensus among the main political parties' attitudes to the CAP. In some countries there are political parties that have strong connections to rural areas and to farming constituencies.

These small parties are likely to do best under proportional representation electoral systems.

The size and importance of the “farm vote” varies by more than just the number of farmers in a society. The level of social solidarity between the general population and farmers varies greatly. Rural votes are particularly important in France. In the early 1990s, active farmers only made 4% of the electorate but 17% of the electorate possessed a “strong agricultural attribute”.⁵³ By contrast, in fewer than a dozen UK parliamentary constituencies does a majority of voters live in rural areas.⁵⁴

Table 9: Rural population by member state, 2000

	% Population	
	Urban	Rural
Portugal	38	62
Ireland	59	42
Greece	60	40
Austria	65	35
Finland	65	35
Italy	67	33
France	76	24
Spain	78	23
Sweden	83	17
Denmark	86	14
Germany	88	13
Netherlands	89	11
UK	90	11
Luxembourg	92	8
Belgium	97	3

Source: Euromonitor

Commitment to sustainable development

One of the core features of CAP reform is a move from a purely productivist agriculture policy towards broader sustainable development goals. Some member states have done more than others to promote sustainable development policies in their domestic policies. Across the EU, Pillar II accounts for just 10-15% of total CAP spending. However, as Table 10 shows, spending on rural development and agri-environment measures varies greatly between member states, reflecting at least in part the underlying commitment to sustainable development objectives.

Table 10: Spending on rural development measures, by member state, 2001

	% on market support	% on rural development
Austria	56.5	43.5
Finland	58.4	41.6
Luxembourg	61.9	38.1
Portugal	70.8	29.2
Ireland	79.1	20.9
Italy	79.8	20.2
Sweden	79.8	20.2
Germany	82.7	17.3
Spain	82.9	17.1
EU-15	85.1	14.9
Greece	87.9	12.1
France	92.1	7.9
Netherlands	93.1	6.9
United Kingdom	94.3	5.7
Denmark	95.2	4.8
Belgium	95.8	4.2

Source: Figures presented at informal Agricultural Council, 30/04/2002

Overall, just 3% of land in the EU is farmed organically. But Sweden (12.5%), Austria (7.9%) and Italy (6.8%) are far ahead of France (1.2%) Ireland (0.7%) and Greece (0.6%), reflecting differences in government support for organic farming and differences in consumer preferences.

A strong commitment to sustainable agriculture is likely to be reflected in a positive approach to the development of Pillar II as the future of European agriculture policy.

7 The Commission's reform proposals

The Agenda 2000 agreement set the parameters of the CAP up to 2006/07, but contained provision for a Mid-Term Review (MTR) of most aspects of the CAP to take place in 2002/3. Pro-reform interests have sought to use the MTR as an opportunity for significant reform to make up for the shortcomings of the Agenda 2000 agreement. Interests that favour the status quo argue that the MTR should be a purely technical exercise in which small adjustments are made to existing policies.

An overview

The Commission announced its proposals for the MTR in July 2002. Their radical nature has surprised many. The centrepiece is the transformation of existing direct payments to farmers into a new payment decoupled from production levels. Initially these decoupled payments would be based on entitlements over a recent reference period. This would be expressed as an aid entitlement at a given number of euros per hectare, and would be subject to the farmer observing good farming practices (known as 'cross-compliance'). No farm would be allowed to receive more than €300,000 a year in direct payments.

The Commission is also proposing that payments under Pillar I be gradually redirected to Pillar II, up to a maximum of 20% in 2011 (this is known as modulation). Farmers receiving direct payments less than €5,000 a year would be exempted from modulation.⁵⁵

Pillar II would be expanded both in financial terms and in the range of schemes that it contains. New programmes would be introduced to encourage improvements in animal welfare and encourage farmers to join farm assurance schemes and producer groups.

Further reductions in support prices and export refunds for a number of commodities are proposed. This would bring EU prices closer to world prices and reduce the volumes of surplus EU produce dumped on world markets. Farmers would be partially compensated for price cuts by increased direct payments.

The political rationale

The proposals share much with the emerging model of CAP reform described in Section 2. If implemented, they would deliver a significantly more economically efficient CAP with an increased emphasis on rural development, environmental conservation and food quality objectives. The proposals have been crafted to give the EU a strong position in WTO negotiations and to accommodate the accession of new member states in central and eastern Europe.

Taken together the Commission's proposals are the most radical in the history of the CAP. It is possible that the Commission has deliberately aimed high expecting that its proposals will be watered down by the Council of Ministers.

The Commission has worked hard to increase the political viability of its proposals by offering "something for everyone". Inevitably, just as there is something for every member state to support, there is also something that every member state will want to oppose.

Traditionally pro-reform countries are expected to welcome the unexpectedly radical nature of the shift away from production subsidies. The emphasis on environmental issues is designed to win the favour of conservation-minded northern countries. Increased expenditure on Pillar II, greater emphasis on food quality and regional distinctiveness and favourable treatment of some Mediterranean commodities are intended to win support among traditionally anti-reform southern member states. The interests of small farmers are protected by the exemption of the smallest 60% of farmers from reductions in direct payments. The bias of the current CAP in favour of very large farms is

corrected through the €300,000 ceiling on direct payments.

Negotiations will continue into the autumn under the Danish Presidency, with the hope that some agreement can be reached in November, partly to avoid the issue being held over until the Heads of Government meeting in December. It is difficult to say whether the Commission will be able to maintain this timetable, but those opposed to reform are likely to favour delay. French President Chirac was successful in watering down the Agenda 2000 CAP reform agreement at the Berlin Summit of 1999. Pro-reform member states will be keen not to allow the same to happen to the Mid-Term Review.

External pressures for reform

Analyses of previous reform attempts reveal that CAP reform has been driven by pressures external to agriculture policy. For the MTR, the key external pressures are the need to make the CAP compatible with the accession to the EU of central and east European countries (CEECs) and the current WTO round of international trade negotiations.

Enlargement

The terms and conditions under which the CAP is applied to new member states is the most important unresolved aspect of EU enlargement. Enlargement with full entitlement to CAP benefits and no phase-in period would dramatically increase the burdens on contributor member states and would break the ceilings on CAP expenditure set by Heads of Government in 1999.

The current Danish EU Presidency is strongly committed to achieving a final agreement on the terms of enlargement at the Copenhagen Summit in December 2002. Even though many have worked hard to keep negotiations on EU enlargement separate from CAP reform, the fact is that the two processes are closely linked.

To keep within budgetary ceilings the Commission has proposed that accession farmers in new member states initially receive 25% of direct

payments, rising to 100% over 10 years. Poland and other CEECs have strongly objected to this, arguing for direct payments to start at 40% and for a shorter phase-in period. There are also concerns about the size of quota entitlements for farmers in accession countries. Poland has a large agricultural sector and it is feared that a bad deal for Polish farmers in the accession treaty could jeopardise a “yes” vote in the referendum on EU membership.

The current lack of agreement on the shape of the CAP beyond 2006 makes accession negotiations even more difficult. However, the Commission’s proposals for the MTR give accession countries a clear idea of the CAP beyond 2006.

The overriding political commitment of accession countries and of most EU member states to enlargement is such that at the very least an outline agreement on agriculture is likely to be reached by the end of 2002, with the fine details to be worked out once the MTR is completed in 2003. Enlargement is of such strategic importance to the EU and to accession countries that failure to reach an outline agreement on agriculture is unlikely to delay final accession agreements for very long.

Insofar as accession states see themselves as likely beneficiaries of the CAP they can be expected to argue against reform. On the other hand, there are important ways in which a reformed CAP may be better suited to the agriculture for CEECs.

CEEC farms are small by EU standards so they will stand to benefit from reforms that correct the existing bias in favour of the largest farms. CEEC farms tend to use much less fertiliser and pesticide than EU farms. This puts them at an advantage in terms of qualifying for new payments that reward low environmental impact and organic farming. Another advantage of the proposed system is that it will not require that accession countries create the complex and expensive bureaucracy needed to manage markets and administer complex commodity support schemes.

Enlargement will have a significant effect on the distributive profile of EU structural funds. After enlargement many deprived areas in northern and western Europe will no longer qualify for large transfers of structural funds. The accession of poorer countries in central and eastern Europe will thus transform EU structural policy from a transfer from prosperous *regions* to poorer *regions* into a transfer from wealthier (northern and western) *countries* to poorer (southern and eastern) *countries*. This will increase the divide between net contributors and net beneficiaries, potentially undermining the consent of net contributors to redistributive EU policies including the CAP.

WTO negotiations

The United States and the Cairns Group of agricultural exporting countries have long opposed the CAP and sought to apply pressure on the EU to reform its agriculture policies.⁵⁶ For these countries, export subsidies are the most unpopular element of the CAP.

The Doha Declaration agreed by members of the WTO in November 2001 sets the broad agenda for a new round of trade negotiations. It contains explicit promises to address the trade needs of developing countries. Their key demands are greater access to agricultural markets in the EU and the US and an end to subsidised dumping of agricultural products on world markets.

The US Farm Act of 2002 has dramatically increased subsidy levels for American farmers, in many cases to similar levels in the EU. The Act reverses all the progress towards reform made by the 1996 FAIR Act. Although it is not absolutely clear whether the 2002 Act breaks the letter of WTO rules, it is certainly against the spirit of the Doha Declaration. The Act certainly undermines the moral authority of the US to press other countries to reduce their levels of agricultural support, as well as undermining the confidence of developing countries that developed countries will keep the promises they have made. If the US is entering a new era of trade protectionism, marking a clear break from the Clinton administration's free trade orientation,

it will be much harder politically for Europe to proceed with CAP reform.⁵⁷

The Cairns Group of agricultural exporting countries continues to argue for agricultural trade liberalisation. The pressure from these countries in the WTO will remain strong, particularly in sectors where these countries stand to gain, e.g. North America on grain and protein crops Brazil on sugar and soya, Australia and New Zealand on livestock and dairy products.

A key question is whether the Doha round of the WTO will provide the same kind of pressure for CAP reform during this decade as the Uruguay round of the GATT did during the 1990s. There are a number of reasons why it is difficult to be optimistic. The Doha agenda has not won the support of the business community in the same way as the very large Uruguay round. Financial services stand to make gains from Doha, but these are not perceived as crucial. Doha has a seven-year phase-in period even after agreements are made. This lengthy timescale goes beyond many medium-term planning horizons. Moreover, many businesses in richer countries are concerned that Doha will undermine the highly favourable terms of trade achieved in the Uruguay round.⁵⁸

In addition, the anti-globalisation movement has created a climate of at best controversy and at worst public hostility to the WTO. Many businesses and politicians are unwilling to put their heads above the parapet by openly campaigning for a successful Doha round.

The Doha round of WTO negotiations has a number of decision-points with implications for the CAP reform process. March 2003 is the deadline for agreeing the modalities of the round. A midway meeting will take place in Mexico in September 2003. At either of these meetings developing countries could withdraw support for the round if they consider that the explicit promises to them in the Doha Declaration are not being delivered. This would fundamentally

undermine the viability of the round, and thereby weaken one of the key external drivers of CAP reform.

The final summit to seal agreements is scheduled for Paris in January 2005. This is a tight deadline and it is conceivable that it could slip. A delay in the WTO round could allow the agreement to take place at the same time as discussion of the post-2006/07 EU financial perspective.

Reaction to the proposals

The Commission's proposals for the Mid-Term Review of the CAP have brought a wide range of reactions from member states and NGOs. Although there are 15 member states in reality the range of likely Mid-Term Review outcomes is drawn by the approaches of the large member states, particularly Germany and France. As it currently stands the anti-reform group has greater voting strength in the Council of Ministers, although the pro-reform group does command a blocking minority.

Broadly anti-reform: France, Italy, Spain, Ireland, Greece, Austria, Belgium, Portugal and Luxembourg (52 votes out of 87)

France is the most powerful supporter of the status quo. In a recent response to the Commission's proposals for the Mid-Term Review, France not only proposes no reform before 2006, it actually calls for increases in the levels of market intervention.⁵⁹ However France does have an ambitious and distinctive approach to rural development that emphasises territorial and environmental objectives and a whole-farm approach to agriculture policy.⁶⁰ The principal innovation of the French Rural Development Programme is the new farm-level individual land management agreement (CTE). This suggests that while the French still see market supports as central to agriculture policy, they can be expected to make a positive contribution to the development of Pillar II.⁶¹ However much of the innovation in French rural policy took place under the socialist government of Lionel Jospin. The electoral success of Chirac's centre-right in 2002 could

mean a return to more traditional and more conservative French agricultural policy.

Broadly pro-reform: UK, Germany, Netherlands, Sweden, Denmark and Finland (35 votes out of 87)

As the largest financial contributor to the CAP, Germany occupies a pivotal position in CAP reform negotiations. A serious determination by the German government to reduce the net financial contribution it makes to European agriculture (or to the EU more generally) would significantly increase the prospects for CAP reform.

Germany may seek to redress the financial imbalances of the CAP through a greater degree of co-financing of CAP expenditure. This would require that member states pay for a greater proportion of the support that their own farmers receive. The effect would be to reduce the imbalances between net beneficiaries from and net contributors to the CAP. It would also sharpen incentives for all member states not to propose purely self-interested expenditure, providing an additional brake on spending. However, greater co-financing would be seen as unfair to poorer EU member states and to accession countries which would find it difficult to match the high expenditure of wealthy member states.

Despite recent changes in approach brought about by the BSE crisis, Germany cannot be seen as a natural ally of traditionally reform-minded member states. Germany has a tradition of interventionist farm policy and a strong commitment to supporting the income of its farmers (particularly in the southern Länder). This sets it aside from the more free-market approach favoured by the UK, Sweden and Denmark. Under a Green Party farm minister, Germany has become a strong advocate of environmental protection, organic farming and animal welfare. It is conceivable that Germany might favour a highly interventionist (and even protectionist) CAP based around Pillar II measures and a high level of consumer protection and environmental regulation.

The UK is a long-term advocate of CAP reform. Its priorities are to increase market orientation of farming and reduce the cost of the CAP through cuts to support prices and year-on-year reductions in direct payments.⁶² As the only member state to have used the option of modulation to shift resources from Pillar I to Pillar II, the UK can be expected to back further shifts.

The UK and Germany have some of the largest farms in Europe and have traditionally defended their interests against attempts to favour smaller farms by introducing upper limits on CAP entitlements. This suggests they may oppose the Commission's plan to limit the size of payments to very large farms.⁶³ The dairy sector remains one of the most highly distorted farm sectors, and the UK is keen to abolish quotas that constrain its competitive dairy farms. The UK farm lobby is well matched by strong environment, rural development and animal welfare lobbies that expect the Government to deliver in these areas.

Farm Unions

At the EU level COPA and COGECA – the two largest European farmers' federations – have strongly criticised the Commission's proposals for the Mid-Term Review.⁶⁴ Within member states the reaction of farm unions has been similar. The main farm unions in France and Germany (FNSEA and DBV respectively) issued a joint statement in opposition to the proposals.⁶⁵ The President of the Irish Farmers Association described the proposals as a "breach of faith" by the Commission. Coldiretti, Italy's largest farmers union, is less critical, seeing the proposals as offering the chance to re-distribute CAP funds in favour of Italian farmers. The President of the UK National Farmers' Union recognised that the CAP is "long overdue for substantial change" and supported in principle the idea of decoupling of supports from production levels. But the NFU is "fundamentally opposed" to modulation of support payments.⁶⁶

8 The EU decision-making process

The preceding chapters have set out the array of interests likely to play a part in the CAP reform process. This section analyses the political process within the EU through which decisions on the future of the CAP are made.

The Council of Ministers

The Agriculture Council is made up of the agriculture ministers from the 15 member states. The Council makes key decisions on the CAP on the basis of proposals made by the European Commission's Agriculture Directorate-General. Only the Commission has the right to make proposals and its approach can be critical, although it will always have an eye to the chances of acceptance by the Council of Ministers. Major reforms are sometimes subject to a final round of negotiation by Heads of Government at the European Council.

Although decisions in the Council are made according to qualified majority, the Commission and Presidency work hard to achieve compromises that each member state can accept. Furthermore, a single member state can still invoke the Luxembourg compromise to veto a proposal it considers to be against its vital national interest. This increases the blocking power of a minority or even a single member state. Since the Council meets in private, the negotiation process is characterised by secrecy and lack of transparency.

Votes in the Council of Ministers are as follows: France, Germany, Italy and UK (10 each); Spain (8); Belgium, Greece, Holland and Portugal (5 each); Austria and Sweden (4 each); Denmark, Finland and Ireland (3 each); Luxembourg (2).

Agricultural interests occupy a dominant position within the Council of

Ministers at the expense of other equally legitimate interests (consumers, taxpayers, industry, environment, etc).

The Council of Ministers is assisted by the Special Committee on Agriculture and by Management Committees for each commodity group. These are made up of civil servants from national agriculture ministries and member state Permanent Representations in Brussels.

Formal stakeholder involvement is via the Advisory Committees for each commodity group. These committees include the full range of stakeholders but are dominated by farmers and agricultural co-operatives.

The European Commission

As the civil service of the European Union, the Treaty of Rome gives the Commission an important agenda-shaping power in the right of initiative. It is the task of the Commission to draft proposals for consideration by the Council of Ministers. The Commission is also responsible for the implementation and enforcement of EU policies.

While DG Agriculture has the most dealings with the Council of Agriculture Ministers formal proposals by the Commission are endorsed by the full Commission. This provides the opportunity for interaction and co-operation with DG Trade, DG Environment and DG SANCO. This gives the Commission an advantage in terms of agenda setting for complex linked policy issues such as CAP reform. For example, DG Trade can work towards a particular EU negotiating position for WTO talks and in doing so shape the range of potential decisions that can be made on the CAP.⁶⁷

As with any bureaucracy, the Commission has its own policy preferences. Agriculture Commissioner Fischler has been keen to reduce the economic distortions of the CAP and deliver better value for taxpayers and consumers. While many of the Commission's policy objectives reflect the views of member states, there is an important set

of concerns that the Commission has of its own. The Commission is a sponsor of the whole European integration project. European integration, maintenance of the single European market and the promotion of a distinctly European structural policy are high priorities. This leads the Commission to be instinctively resistant to proposals that might lead to the re-nationalisation of EU policy programmes including the CAP.⁶⁸

The European Parliament

The European Parliament is largely excluded from executive and legislative decision-making on the CAP. This is anomalous since co-decision-making between the Council and the Parliament applies in every economic sector except agriculture.

In theory it is possible for the Parliament to block the CAP budget although this is something of a “nuclear option”. Practically speaking, the role of the European Parliament with regard to the CAP is limited to scrutiny, facilitating public debate and raising issues of concern with the Commission or the Council.

The European Parliament has consistently shown itself to be among most conservative of bodies when it comes to CAP reform. Increasing the role of the European Parliament in the CAP (for example, through co-decision mechanisms) is unlikely to increase chances of achieving reform.

9 Policy entrepreneurship

CAP reform is disadvantaged by a political dynamic in which the costs of reform are concentrated while the potential benefits are dispersed. Policy entrepreneurship is needed to overcome this political dynamic.⁶⁹ There are many dimensions of policy entrepreneurship including: ensuring policy design reflects political realities; strengthening the coalition for reform; changing decision-making processes; and making the most of windows of opportunity. This section describes practical steps that policy entrepreneurs can take to increase their chances of success.

Using policy design to increase political viability

CAP reform campaigners often focus on policy design purely from an economist's perspective: what are the desired policy outcomes and which instruments will deliver them in the most efficient way? Policy design must start with the efficient delivery of public interest objectives. Yet issues of political viability must be considered if policy design is to be more than an academic exercise. Political viability of CAP reform proposals can be increased if special attention is paid to compensating losers, increasing national discretion, avoiding the capitalisation of payments into land values, avoiding significant redistribution between member states, implementing changes gradually, and developing private sector alternatives to state safety nets.

Compensating losers: a small farms scheme

Most policy changes create winners and losers. The number of losers, the size of their losses and effectiveness at mobilising opposition determine the political costs of policy change. A strategy of minimising the number and scale of losses increases political viability. However, compensating losers costs money.

In the case of CAP reform, a policy to exempt small farmers from

subsidy cuts would achieve the twin objectives of buying off the largest amount of potential opposition for the least amount of expenditure and directing compensation to those with the greatest ability to win the sympathy of wider society.

The smallest 60% of farms receives just 10% of all CAP direct payments (less than €5,000 a year). This means it would be relatively inexpensive to ensure that CAP reform does not reduce the level of payments received by these farmers – at least not in the short term. The recent CAP small farms scheme provides a suitable vehicle for treating small farms separately from the rest of the industry, as does the Commission's proposal for exempting small farms from modulation of direct payments.

It is unlikely that the largest 2% of farms that currently receive 24% of all CAP payments – over €50,000 a year per farm – will generate anywhere near as much public sympathy as small farmers.

Compensating losers: a bond scheme

A radical approach to CAP reform involves decoupling future CAP entitlements from production and converting them into a tradable bond. In terms of political viability this offers many advantages over year-on-year reductions in direct payments.

The bond would be a tradable financial instrument and farmers could choose to keep the bond and receive annual payments for its lifetime or sell the bond and enjoy a large one-off windfall.⁷⁰ For farmers wishing to stay in the industry the windfall could be used for investment purposes; for farmers wishing to exit the industry it could serve as an early retirement package.

Table 11 shows how current entitlements to direct payments could be transformed into windfall gains under a bond scheme. For a bond with a lifetime of 20 years and subject to 5% annual degressivity a farmer currently receiving €10,000 in direct payments a year would receive a bond worth €85,000.

Table 11: Sale value of bonds under various scenarios

Indicative sale value of bonds issued in respect of current entitlements to CAP direct payments

		Current annual entitlement to direct payments				
		€5,000	€10,000	€15,000	€20,000	€30,000
Rate of degressivity	Duration of bond	Sale value of bond*				
zero	10 years	€38,000	€76,000	€114,000	€152,000	€228,000
5%	10 years	€31,000	€62,000	€93,000	€124,000	€186,000
zero	20 years	€61,000	€122,000	€183,000	€244,000	€366,000
5%	20 years	€42,500	€85,000	€127,500	€170,000	€255,000

* assumes 5% annual discount rate

The bond proposal was first made by the German agricultural economist Stefan Tangermann in 1990 and was proposed by Denmark during the MacSharry reforms in the early 1990s.⁷¹ The UK gave a qualified backing to the proposal, but it failed to win the support of other member states or the Commission.⁷² The EU is currently funding a multidisciplinary research programme into how a CAP bond scheme might work.⁷³

Increasing national discretion

Many countries – particularly those in southern Europe – express dissatisfaction with the “fit” between the CAP and their agriculture sector. A greater degree of national discretion would allow each member state to tailor agriculture policies to its own needs and circumstances within the constraints of single market and other commonly agreed rules. This would reduce many of the problems associated with a one-size-fits-all CAP: a problem that can only get worse with enlargement of the EU to include 22 member states.

Pillar II schemes allow much more discretion at national and regional level than Pillar I, where flexibility would undermine the single market.

Redirection of funds to Pillar II will necessarily increase the extent of member state discretion in the CAP, thus increasing the political acceptability of reform. Similarly, a degree of flexibility can be granted to member states in the precise application of the compulsory modulation of funds from Pillar I to Pillar II.

Additional flexibility in the application of the CAP will allow Agriculture Ministers to argue that CAP reform has delivered tangible benefits to domestic client groups.

Ring-fencing expenditure by member state

Unsurprisingly, any CAP reform proposal that involves significant redistribution of funds between member states will be opposed by member states that stand to lose. Considerations of political viability would suggest that the shift of funds from Pillar I to Pillar II take place at the member state level, rather than the EU level.

Modulation was introduced as an optional measure under the Agenda 2000 reforms, with member states being required to match modulated funds with new national expenditure. Member states were given some discretion in the way funds were to be skimmed from Pillar I, for example they could choose to discriminate on the basis of farm size, farm labour force or other factors. Compulsory modulation that ring-fences resources at the member state level stands a greater chance of being accepted than the “dynamic” modulation in the Commission’s Mid-Term Review proposals, although it has the countervailing disadvantage of perpetuating existing inequalities.

As former Portuguese Agriculture Minister Arlindo Cunha MEP argues, “the decision-making system of the CAP will never allow for such a thing as a radical reform because of the redistributive effects which it implies... The most likely scenario would be for the Agriculture Council to approve a shift from the first to the second pillar on condition that the savings thus obtained are kept and re-utilised inside each Member State.”⁷⁴

Gradual, locked-in change

Where far-reaching changes are proposed, it is sensible that they be implemented gradually in order to allow those affected to make adjustments. Abrupt changes in policy can cause unnecessary and damaging shocks. Incremental changes may be small, but as long as the change is locked-in, the desired effect will be achieved over time. Gradual, locked-in change has a political advantage because even though the full effect is known, it will not actually happen until some time in the future. The political costs of the change are partially deferred to the future and are diffused over time. The classic example of gradual, locked-in change is to freeze an entitlement at its nominal value (i.e. not to make increases in line with inflation). Over time inflation reduces the real value of the benefit, and GDP growth further reduces the cost of the benefit relative to overall government expenditure.

Introducing private sector price safety nets

The system of EU prices and market supports provides guaranteed minimum prices for European farmers even when the world market prices are low. This means taxpayers and shoppers are the primary insurers of farmers against the adverse effect of world market price fluctuations. CAP reform involves the gradual reduction of EU prices to world levels and the phasing out of market supports. With no safety nets EU farmers will be exposed to the full effect of fluctuations in world prices.⁷⁵ This prospect is a major source of the anxiety many farmers feel about CAP reform. To address this legitimate concern, attention should be paid to how to fill the place of current publicly financed price safety nets.

Futures markets and private-sector insurance schemes can be used to smooth out cyclical variations in prices. North America has well-developed agricultural commodity futures markets and private agricultural insurance schemes. The EU and the OECD have explored frameworks through which farmers can insure themselves against risks.⁷⁶ The European single currency eliminates exchange rate variation

within the Eurozone thus removing a significant impediment to European agricultural futures markets. Further development and implementation of private sector insurance schemes and commodity futures markets will not only make agriculture policy more rational and equitable, they will help to reduce the culture of state dependency in farming. Similarly, there is no reason why farmers cannot insure themselves against animal and crop disease outbreaks. The additional costs of insurance will be passed on to shoppers through higher prices. It might be worthwhile for the EU to subsidise insurance schemes, at least in the form of initial pump priming.

Supporting farm incomes rather than inflating land values

The capitalisation of agricultural supports into land and quota values is a major weakness of the current CAP. Since CAP supports are diverted into asset values, farmers remain income poor while being asset rich. Furthermore, artificially inflated land values are bad for tenant farmers and impede the ability of the farm sector to adjust to economic change. Many European farmers suffering from low incomes will welcome supports directed at farm income rather than land values.

If entitlement to direct payments is conditional upon the ownership of land the value of the entitlement will become capitalised into the value of the land. This will happen even if direct payments are decoupled from production levels. Evidence from Environmentally Sensitive Areas schemes in the UK suggests that broad, unspecific agri-environment agreements inflate land values.⁷⁷

The capitalisation effect can be minimised if support payments take on more of the characteristics of public procurement and less of the characteristics of welfare entitlements. In theory, payments should be linked to outputs that can be specified and measured. Many Pillar II schemes are supposed to work in this way by rewarding farmers for conservation activities. Yet real practical problems with the specification and measurement of environmental public goods need to be overcome.⁷⁸

Building a broad, inclusive coalition

Bringing together a diverse set of interests

More NGOs are taking an interest in CAP reform than ever before. Although it is not sufficient alone to secure reform, a broad and inclusive NGO coalition for reform does increase the pressure for reform. Bringing this coalition together requires a common policy platform with which each member can agree. CAP reform is backed by consumer and taxpayer representatives, environmentalists, rural development advocates, trade unions, animal welfare campaigners, developing countries and some farmers; but for a wide variety of reasons. The emerging model reflects much of the common ground between these diverse interests but there may be areas where niche interests can be further accommodated, for example, by widening the range of schemes in Pillar II.

Mobilising the support of potential winners

Greater mobilisation of potential winners in the campaign for reform will increase the chances of success. This is a difficult task for two reasons. Firstly, there are collective action problems because most of the gains from CAP reform are very small at the level of the individual. Secondly, many potential winners from reforms that shift resources to Pillar II may not be readily identifiable.

Providing more information to the public about how the CAP operates, who pays for it and how it is slowly changing is bound to increase public mobilisation in support of further reform. In the United States following a freedom of information lawsuit filed by the Washington Post in 1996 the Environmental Working Group has set up a website containing detailed information on how much each farm receives in federal subsidies (www.ewg.org/farm). In the EU this kind of information is kept secret on grounds of commercial confidentiality.

Providing public information about the positive effects of environmental and rural development measures and establishing visitor

programmes so that people can see their money at work are important ways of bolstering support for a CAP based around Pillar II.

Probably the single greatest benefit of CAP reform to European society would be cheaper food. Analysis of retail behaviour shows that price is a key determinant of food purchasing choices, suggesting the public is aware of and sensitive to the price of food. However, for most people the price of food does not seem to register as a distinctly political issue. By contrast, the effect of government policies on petrol prices has recently become high profile political issue in some northern European countries.

There is no doubt that many farmers and their representative organisations will remain opposed to the “emerging model” of CAP reform and will fight hard against any major attempt at reform. Nevertheless, reformers should work hard to present a positive vision for the future of European farming. This might take the form of a new “contract” between society and farmers under which farmers are freer to earn their way as businesses in the marketplace while the state provides supports that explicitly recognise the multifunctional character of agricultural production. At a practical level, demonstration projects show the benefits to farmers of new kinds of support measures that might form part of a reformed CAP.

Framing the issue

Agriculture and agriculture policy mean different things to different people. There are important variations within and between member states and so the way in which the issue of CAP reform is “framed” varies greatly across the EU.

Theories of public policy agenda setting suggest that policy innovation rarely reaches the agenda of high level decision-makers unless there is a widely recognised problem to which the proposal can be presented as a solution.⁷⁹ Presenting CAP reform as a single solution to a wide range of problems is central to the policy entrepreneurship required of CAP reformers. Linking unexpected but relevant events to the need for CAP

reform can strengthen the broader reform argument. Two recent examples are the BSE crisis in Germany and the FMD outbreak in the UK.

Drawing on the public opinion data presented in Section 5 and the analysis of variation in European agriculture presented in Section 6, there are many issue dimensions in which the debate on CAP reform can be framed, depending upon local circumstances:

- *Food prices* – especially important in countries where food represents a large proportion of household expenditure, e.g. Greece (23%) and Portugal (21%).⁸⁰
- *The future of small and family farms* – a key issue in France, southern Europe and in accession countries.
- *Food safety* – of all the issues related to agriculture policy, food safety has the greatest political salience amongst the general European population, particularly in countries that have recently experienced food safety crises such as BSE.⁸¹
- *Reducing taxes* – of greatest relevance to the net contributor countries such as Germany, Netherlands, UK and Belgium.
- *Food quality and distinctiveness* – especially important in countries where food is central to conceptions of national and regional culture and identity.⁸²
- *Environmental protection* – most relevant in the northern European and Scandinavian countries where there is the highest level of environmental activism. Environmental issues encompass conservation of landscape features, water, soil and air quality and protection of wildlife.
- *Rural crisis* – in regions where rural depopulation and rural poverty is a problem.

- *Tourism* – in areas where rural economies are heavily dependent on tourism, or where tourism is seen as a potential engine of economic growth.
- *Animal health and welfare* – UK, Finland and Sweden have well-established animal welfare movements.

Changing decision-making processes

Changing the “rules of the game” by which CAP decisions are made can be expected to have an impact on the content of those decisions.

For reform advocates the principle objectives must be to weaken the monopoly that agricultural interests still enjoy, to reduce the number of veto points and to increase transparency and accountability. There are many institutional changes that could achieve this.

Academic and former EU Commissioner Lord Dahrendorf described the CAP as “little more than an instrument for Ministers of Agriculture to get for their farmers in Brussels and in the name of Europe what they would not get at their national Cabinet tables.”⁸³ It is certainly the case that at the national level agriculture ministers are subjected to far greater financial control and oversight by national finance ministries than applies to the EU Agriculture Council. This is a general weakness of EU machinery that suggests the EU is institutionally ill equipped to control big spending programmes, and perhaps should restrict itself to a largely regulatory role.

Transparency and accountability of CAP decision-making would be improved if Agriculture Council meetings were held in public. The creation of a “jumbo” council to negotiate CAP reform (including finance, environment, trade and consumer ministers) could increase the chances of achieving reform, although past experience of “jumbo” councils has been mixed.

The UK Consumers’ Association has proposed a radical shake-up of agriculture decision-making processes including:

- Abolition of the Special Committee on Agriculture (SCA) and replacing it with a Food and Rural Policy Committee to be managed by the normal COREPER mechanisms.
- Greater integration of other DGs (Finance, Trade, Industry, Development, Environment and SANCO) into the Commission's development of agriculture policy.
- Greater openness on policy development and more consultation with a wide range of interests.⁸⁴

Windows of opportunity

Even where there are obvious problems that need to be solved, and a policy proposal that fits the bill, there will only be a limited number of moments where the political will ever be sufficient for an agreement to be reached. With the Commission proposing radical changes to the CAP, now is a rare window of opportunity to achieve reform.

The history of CAP reform shows that shortcomings in agriculture policy have not been sufficient to bring about reform. External drivers are critical. The urgency of the current Mid-Term Review is heightened by the need to make the CAP compatible with the Doha Round of WTO international trade negotiations and the accession of CEEC countries to the EU.

Growing concerns about pesticides and genetically modified crops and a spate of animal diseases and food safety scares is causing the European public to think more deeply about how food is produced. Depressed farm incomes mean many farmers are concerned for the future.

The timing of elections in key member states has an impact on windows of opportunity for CAP reform. In the run-up to elections governments are less willing to consider radical reforms, as to do so would risk generating an electoral backlash among vocal farming and

rural interests. General elections in France and Germany in June and September 2002 respectively mean that neither government will have to face the polls for several years.

A further factor that affects the timing of reform attempts is the rotating Presidency of the European Union. When a pro-reform member state holds the Presidency, CAP reform is likely to rise up the decision agenda. A Presidency favouring the status quo may attempt to delay the process of reform. Yet this tendency is not universal. The Presidency will often work hard towards securing agreement, even if this requires putting aside its own national policy objectives. This is particularly the case for smaller member states, many of which attach considerable prestige to a successful Presidency. Larger member states may be more inclined to use the Presidency to advance their own national interests.

Denmark holds the Presidency for the remainder of 2002. In 2003 it passes to Greece (January-June) and Italy (June-December). In 2004 the Presidency is held by Ireland (January-June) and the Netherlands (June-December). Denmark has prioritised enlargement over all other issues for the remainder of 2003. This suggests that the approach of the Greek Presidency will be significant in determining the outcome of the Mid-Term Review of the CAP.

10 Conclusions

There is nothing new about reforming the CAP. Since its creation people have been coming up with more appropriate objectives for agriculture and rural policy and better ways of delivering them. Yet the political barriers to reform have rarely been overcome. A complex and obscure policy has disbursed massive subsidies and protection, creating entrenched supporters. Potential beneficiaries of reform have not been motivated to mount a campaign necessary to overcome entrenched supporters of the status quo. The decision-making process lacks transparency and is dominated by farm interests. Policy failures have led to tinkering rather than tackling. Where important issues external to the CAP have required reform, as in 1992, a measure of progress has been made.

The current Doha round of WTO negotiations and the accession of new countries to the EU are the two most powerful drivers of the current reform debate. In addition there are growing public concerns about food safety, the nature of food production and about the plight of struggling farmers and some rural communities. All of this turns up the heat on the Mid-Term Review of the CAP that is currently underway. The Commission has been bullish in proposing radical reform. The response of member states has been mixed, but the pro-reform group is stronger than ever before.

This is more than an auspicious opportunity for achieving CAP reform. Issues of strategic importance beyond agriculture depend upon achieving radical reform of the CAP. External drivers have their own timetables: this is not a moment that can be revisited. Another fudge will have serious consequences: for farming; for rural communities; for the accession of new EU members; for trade liberalisation; for the world's least developed countries and poorest communities; and for the

very reputation of the Europe as a mature polity able to reform its institutions and recast its policies to meet the challenges of a changing world. At such a defining moment for Europe, agriculture policy is too important to be left to farming ministers.

Notes

- ¹ See for example Packer (2001), Oxfam (2002), National Consumers' Council (1998), European Commission Expert Group (1997), Consumers' Association (2002), Borrell and Hubbard (2000), Hill (2000).
- ² Daugbjerg (2001).
- ³ DEFRA (2002).
- ⁴ The term 'multifunctional' refers to an economic activity that has multiple outputs and therefore may contribute to several societal objectives at once. OECD (2001b).
- ⁵ The French modulation scheme, which would have redistributed money from large arable farmers to small family farms, was shelved by the centre-right administration elected in 2002. Germany has recently signalled that it plans to implement modulation to increase funding for agri-environment programmes.
- ⁶ European Commission Expert Group (1997) is an influential exposition of the emerging model.
- ⁷ A radical proposal that challenges the policy paradigm underlying the emerging model is Packer (2002).
- ⁸ Howarth (2000), Swann (1995).
- ⁹ Fouilleux (2001), Coleman and Tangermann (1999), Patterson (1997), Mahé and Roe (1996), Keeler (1996).
- ¹⁰ Daugbjerg (2001).
- ¹¹ Ackrill (2000).
- ¹² MAFF (1999).
- ¹³ *Les Echos*, 8 March 2001.
- ¹⁴ Weaver (1986).
- ¹⁵ Thomson (1989).
- ¹⁶ Recent examples are the distinctive approaches of the Italian Minister Alfonso Pecoraro Scanio and the Austrian Minister Wilhelm Volterer.
- ¹⁷ Patterson (1997).
- ¹⁸ In order to avoid a significant reform of the CAP financial over-runs in the mid 1980s were addressed by increasing Germany's contribution to the CAP budget.
- ¹⁹ Webber (1999).
- ²⁰ Pierson (1993).
- ²¹ Daugbjerg (1999).
- ²² OECD (2001a).
- ²³ Eurostat data, DEFRA calculations.
- ²⁴ Martin et al (1990).
- ²⁵ MAFF (1999).
- ²⁶ OECD (1997).
- ²⁷ MAFF (1999); Chemical Market Reporter (2001).
- ²⁸ European Commission (2002b). CAP expenditure is in addition to around €14 billion spent annually by EU member states on agriculture. This includes some farm support measures but also spending on food safety, animal health and scientific research.
- ²⁹ OECD (2001a). It is notoriously difficult to measure precisely the additional costs to consumers of higher food prices in the EU because the prevailing world price of many

foods is a *residual* price, and can be expected to increase in the absence of agricultural price supports in the EU and elsewhere.

- ³⁰ Trapp Steffensen (forthcoming).
- ³¹ Pretty et al (2000).
- ³² World Bank (2001).
- ³³ Oxfam (2002).
- ³⁴ Weaver (1986).
- ³⁵ European Commission (2000b).
- ³⁶ DEFRA analysis of Eurostat data (1999).
- ³⁷ European Commission (2001a).
- ³⁸ European Commission (2000b).
- ³⁹ Agra Europe (2001).
- ⁴⁰ Patterson (1997).
- ⁴¹ Egdell and Thomson (1999).
- ⁴² Keeleer (1996).
- ⁴³ The decision by the Jospin government to modulate funds from large arable farmers to small farmers is an example of this dynamic, as is the decision of the new centre-right government to drop modulation.
- ⁴⁴ The 2001 foot and mouth disease outbreak exacerbated divisions within farming and rural communities with many objecting to the NFU's support for the Government's mass slaughter policy. The Countryside Alliance was established to defend fox hunting, but it could find itself seeking a new role as the voice of farming and rural communities, at the expense of the NFU.
- ⁴⁵ European Commission (2000).
- ⁴⁶ European Commission (1999).
- ⁴⁷ Consumers' Association (2001), National Consumer Council (1998).
- ⁴⁸ Oxfam (2002).
- ⁴⁹ Ministère de l'agriculture de l'alimentation de la pêche et des affaires rurales (2002) <http://www.agriculture.gouv.fr/actu/PACberlin.htm>
- ⁵⁰ Agra-Europe (2002c).
- ⁵¹ DEFRA (2001).
- ⁵² It can be argued that the rebate represents a cost to the UK as it must be regularly renegotiated and EU partners can expect to extract a price for agreeing to renew the rebate.
- ⁵³ Keeler (1996).
- ⁵⁴ MORI (2000).
- ⁵⁵ European Commission (2002c).
- ⁵⁶ The 18 current members of the Cairns Group are Argentina, Australia, Bolivia, Brazil, Canada, Chile, Colombia, Costa Rica, Fiji, Guatemala, Indonesia, Malaysia, New Zealand, Paraguay, the Philippines, South Africa, Thailand and Uruguay.
- ⁵⁷ The protectionist charter of the new US Farm Act means the expiry of the WTO "peace clause" at the end of 2003 loses some of its significance as a driver for CAP reform.
- ⁵⁸ Oxfam (2002).
- ⁵⁹ Ministère de l'agriculture (2002).
- ⁶⁰ This is set out in the *Loi d'Orientation Agricole* adopted in 1999.
- ⁶¹ Lowe et al (2001).

- ⁶² A policy of gradually reducing in CAP support levels is known in the CAP reform lexicon as “degressivity”. This concept has long been central to reform proposals advanced by the UK, and was put forward by France during Agenda 2000 negotiations as an alternative to Germany’s proposal for co-financing.
- ⁶³ The UK NFU estimates that there are approximately 500 large arable farms that receive more than €300,000 per annum in direct payments.
- ⁶⁴ COPA (2002).
- ⁶⁵ FNSEA (2002).
- ⁶⁶ Agra Europe (2002).
- ⁶⁷ Coleman and Tangermann (1999), Patterson (1997), Putnam (1988).
- ⁶⁸ Grant (1995), Keeler (1996).
- ⁶⁹ Baron (1987).
- ⁷⁰ The size of the windfall gain will be the market price of the bond, that is to say the net present value of the future payments to which the bondholder is entitled.
- ⁷¹ Tangermann (1991).
- ⁷² Daugbjerg (2001).
- ⁷³ Details of this research are at <http://www.rdg.ac.uk/AgriStrat/bondscheme/>
- ⁷⁴ Cunha (2002).
- ⁷⁵ A countervailing factor is that reducing EU prices to world prices will reduce the size of cyclical price variations because prices will be established in a much larger market and so will be less sensitive to changes in output.
- ⁷⁶ European Commission (2001b), OECD (2000).
- ⁷⁷ Roberts, D., Macdonald, D., Kampas T., Shannon, P., Potts, J. and Barroclough, F. (2002): *Nature Conservation Designations and Land Values*. Edinburgh: Scottish Executive Central Research Unit.
- ⁷⁸ Latacz-Lohmann (2000).
- ⁷⁹ Kingdon (1995).
- ⁸⁰ European Commission (2002b).
- ⁸¹ European Commission (2002a).
- ⁸² France, Italy, Portugal and Spain account for two thirds of all food and drink products with EU registered protected designations.
- ⁸³ Hallett (1981).
- ⁸⁴ Consumers’ Association (2001).

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