DEVELOPMENT POLICY VERSUS COMMON AGRICULTURAL POLICY OF THE EU

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"Aid without trade is a lullaby—a song you sing to children to get them to sleep."

Yoweri Kaguta Museveni

INTRODUCTION

The last enlargement of the EU in May 2004 has brought an incentive for the EU to realise important reforms and changes to the existing EU structures. The aim of this paper is to bring attention to one of the EU policies, one which is not working well in its current shape and whose reform should belong among the main priorities of the European community. It is the Common Agricultural Policy (CAP), which negatively affects the economic development of developing countries[1], and thus causes a huge disharmony in development efforts of the EU. This paper will also try to find an optimal solution to how CAP should be reformed to meet the basic domestic social and environmental goals of the EU without harming economic development in the Third World.

DEVELOPMENT AID POLICY OF THE EU

The EU claims to be actively engaged in development. Article 177 of the Treaty on the European Community states that the EU should foster sustainable economic and social development in developing countries, that it should integrate these countries into world economy and campaign against poverty.[2] How successful and coherent is the EU in this effort?

The EU belongs among the world's greatest donors. The commitment of the EU to development has first of all historical and moral grounds. During the colonization era, Europe enriched itself enormously at the expense of its colonies, leaving them in an impoverished state from which they have not yet fully recovered. However, it is not just moral responsibility which leads the

EU to perform such an active role in development aid policy. Maybe an even more important incentive is an effort to establish a close co-operation with the countries of the Third World, because these countries represent potentially very lucrative growing markets in the future. Therefore, the EU Member States use development aid as a means to promote their national political and economic interests.

Nevertheless, the EU is aware of the fact that it is impossible to financially boost economic growth in its former colonies by development aid alone. Therefore, it has often declared its commitment to use trade as a development tool. There is a growing recognition of the theory that trade is the best tool for fostering economic growth. In general, countries with higher international trade participation tend to show higher growth rates.[3] As EU Trade Commissioner, Pascal Lamy, stated: "Our objective is clear: development is our objective, trade the instrument".[4]

The most logical sector in which developing countries could succeed on the world markets would be agriculture. Why? Some 96 % of the world's farmers live in developing countries.[5] These people not only rely on agriculture for a key part of their livelihoods; agriculture represents almost the only sector where they can successfully compete on international markets, since it is a sector where they possess the greatest comparative advantage[6]. Unfortunately the trade rules of the WTO and the agricultural policies of rich countries and trading blocks such as the EU, have made it far more difficult for farmers from developing countries to succeed in the world trade structures than those from developed ones.

THE COMMON AGRICULTURAL POLICY (CAP)

Economic and political reasons for CAP

EU trade with agricultural products has been highly regulated by CAP since 1968.[7] There are many economic and especially political reasons for that. Among the most important is the desire to preserve national heritage, cultural diversity, and to prevent rural unemployment and subsequent depopulation of the countryside and land degradation. Another important factor is the strength of the agricultural lobby. Despite the decreasing percentage of people engaged in agriculture on the EU level, farmers still have strong organizations to represent their interests. They are very well organised, which enables them to exert enormous political pressure.[8]

Negative effects of CAP on the EU

CAP has had negative effects not only on the economic development in developing countries, but also on the EU itself. CAP is run by a complicated price- setting mechanism. This mechanism should set prices of agricultural products in such a way as to provide EU farmers with a "fair" income and thus to keep them in production. To fulfil this objective, the prices for agricultural products are set artificially high.[9] What are the negative consequences of such a policy on the EU?

First of all, it is a huge burden on the EU budget to finance this policy, which consumes more than half of the EU budget.[10] Secondly, higher prices naturally stimulate agricultural overproduction, which creates problems with their disposal. The EU has to intervene to buy excess supply to keep the prices high. Surpluses are then stored, dumped on international markets, donated as food aid for humanitarian purposes or converted to animal foodstuff.[11] In any case, the management of the surpluses represents another burden on the EU budget. Moreover, high prices provide an incentive for inefficient farmers to stay in production, which causes ineffective distribution of human and economic capital and thus brings economic loss. Furthermore, the EU consumers are forced to pay 44% higher food prices than they would pay without CAP.[12] And finally, the EU is facing international criticism because of continuous distortions of the world trade in agricultural products and because of the negative impacts of CAP on developing countries.

Negative effects of CAP on developing countries

Agricultural subsidies

The EU provides its farmers with trade distorting subsidies to ensure that farmers cover not only costs, but also get a "reasonable" profit. In comparison with huge amounts of EU agricultural subsidies, EU development aid to developing countries is negligible. The EU is the world's biggest user of export subsidies, accounting for 90% of the world subsidies in 1994-1997. The EU supports its farmers twice more than is the amount of the combined aid budget of the EU and all EU Member States together.[13] As a result of this policy, inefficient EU farmers are encouraged to stay in production, while more efficient farmers from developing countries are unable to compete.

Dumping

Price setting mechanism of the CAP encourages overproduction. The EU buys the surpluses produced by its farmers and often dumps[14] them on the international markets. As a result, world food prices fall and do not reflect the real costs of production. Farmers from developing countries are then unable to compete under these low prices and they are pushed out of production.

Low market access

The main philosophy of the external mechanisms of CAP is to give preference and price advantage to EU agricultural products over imported ones. There are various external mechanisms, which are used to protect EU farmers from competition of cheaper imports. It uses classical means such as tariffs, which reach on average 20% but peak to as high as 250%. Moreover, it uses a quota system and non-tariff barriers such as health and safety standards.

Nevertheless, these protection mechanisms do not apply to all imports from all countries equally. Many countries have special access to EU markets, so called "trade preferences", at least for some agricultural products. Trade preference usually takes the form of a regional trade agreement, which is composed of lower tariffs, higher quotas or other kinds of relaxations of trade restrictions. The least favoured countries are normally subjected to the rules of the WTO.[15]

However, despite various trade preferences offered to developing countries (e.g.: the Everything But Arms Initiative[16]), almost the only agricultural products allowed to enter the EU market freely are tropical or temperate ones not grown in Europe, which thus cannot endanger EU farmers. How is this possible? The EU is under continuous international pressure to remove its trade barriers on agricultural products. As a result, the EU often pretends liberalisation of agriculture by shifting protection into more covered non-tariff barriers. The Centre for European Policy Studies has published a report concluding that only one third of the imports eligible for tariff preferences actually enter the EU market, since they fail to meet some technical criteria. The Centre admitted that some EU health and safety standards are legitimate, but emphasizes that many are simply protectionist. For example, the smaller Indian farmers complain about the EU requirement that cows have to be machine-milked, which makes them unreasonably disadvantaged.[17] As a result, in spite of some limited trade preferences, developing countries face great difficulties while trying to export to the EU market.

Case study about the negative effects of CAP

Let's take an example of sugar production to demonstrate the negative effects of CAP on developing countries. Although the EU produced beet sugar at more than double the cost of developing countries, the EU is the second world sugar exporter. For example, in the year 2001 the EU covered 40% of world sugar exports. How is this possible? The EU supports its sugar industry up to $1.7bn in subsidies every year.[18] This results in artificial overproduction of sugar, which is then dumped on international markets at below-cost prices. EU "exporters" then compensate their losses by receiving export refunds from the EU budget. For example, the EU gave six leading sugar-processing companies €819m in subsidies just for the year 2003 to compensate them for lower prices, for which they had to sell in external markets.[19] Dumping gradually decreases world prices and causes effective sugar producers from developing countries to be pushed out not only from the international but also from their local markets. Moreover, apart from high agricultural subsidies and dumping, the EU restricts access of sugar producers from developing countries to its lucrative home market.[20] The EU imposes high import tariffs and quotas on this crop. Even though some developing countries, such as African, Caribbean and Pacific countries, have preferential treatment and receive limited quota access to the EU market; they are allowed to export only raw sugar there. The control over much more profitable refining still remains in the hands of EU companies.[21] As a consequence of such trade barriers, it is estimated that, for example, Malawi has lost about $32m in possible foreign exchange with the EU.[22]

Double Standards League

The EU presents itself as highly committed to the liberalisation process; however, there is a great gulf between the declared principles and the practices. In 2002, Oxfam International compared free trade rhetoric of the world's richest countries with their protectionist practices against the imports from developing countries. Especially due to CAP, the EU was placed at the head of the Double Standards league.[23]

PROBLEMATIC SITUATION

As we can see, the negative consequences of CAP are causing a disharmony in development efforts of the EU. To come to a conclusion that CAP needs to be reformed is not difficult. The problem starts when one tries to find an agreement on what such a reform should look like, and what rules of global trade with agricultural products the international community should set to help developing countries out of poverty.

LIBERALISATION OF AGRICULTURE?

The key international organizations such as the WTO, IMF or WB tend to be biased toward liberalisation of trade, including trade in agriculture. However, is it always wise to follow blindly the liberalisation doctrine? What effects would liberalisation of agriculture have on the EU and on developing countries?

Effects of liberalisation of CAP on the EU

Liberalisation of CAP would have many positive effects on the EU. First of all, it would provide a possibility to allocate half of the EU budget currently spent on CAP for much more effective fields such as research or science. Secondly, it would bring economic benefits due to the more efficient allocation of economic resources. For example, Borrel and Hubbard calculated that the country undergoing the process of liberalisation bears the biggest benefits. Their

[1] Developing countries are countries in the process of becoming industrialized, in which average annual income is low, most of the population is engaged in agriculture and the majority live near the subsistence level.

[2] Neill Nugent, Government and Politics of the European Union, 4th ed. Palgrave: England, 1999.

economic model takes the sugar trade as an example. They came to a conclusion that liberalisation of trade with just this one commodity would benefit the EU by $2.5bn.[24] Furthermore, liberalisation of CAP would decrease expenditures on food for consumers and also for the producers using food as an input for further production. And finally, it would silence the international criticism for hindering international trade and harming the economic development in the Third World, thereby strengthening the negotiating position of the EU within the WTO.

Unfortunately, liberalisation of CAP would also have some negative effects on the EU. It would be undesirable from the point of view of nature conservation and rural culture. There would be continuous pressure on EU farms to enlarge, specialise, industrialise and to cut costs. This would cause agricultural production in some marginal areas to disappear and many traditional systems of farming would be lost. The negative effects would also spill over to other sectors. It would bring social problems due to growing unemployment in rural areas followed by their depopulation, and environmental problems connected to the land degradation of the fields and meadows left uncultivated.

Effects of liberalisation of agriculture on developing countries

A free market only benefits those who are able to sustain competitive pressures; therefore, developing countries would probably be unable to benefit from a complete liberalisation of world trade in agriculture. It is always dangerous to open up the fragile agricultural sectors of developing countries to very competitive producers from developed ones, since increased competition tends to favour large and established producers. Moreover, developing countries usually lack financial and technical capabilities to meet the technical standards

[3] European Commission, Trade and Development: Assisting developing countries to benefit from trade (2002), <http://europa.eu.int/comm/trade/issues/global/development/docs/comdev_170902.pdf>.

[4] Ibid

[5] Oxfam International, The Rural Poverty Trap: Why agricultural trade rules need to change and what UNCTAD XI could do abut it (2004), <http://www.oxfam.org.uk/what_we_do/issues/trade/downloads/bp59_unctad.pdf >.

[6] A comparative advantage is the ability to produce goods at lower cost, relative to other goods, compared to another country.

of developed countries. As a result, local producers would probably be pushed out even from their home markets. The Food and Agriculture Organization carried out research in 14 countries undergoing the process of liberalisation, and concluded that all these countries exhibited rising imports and displacement of local producers.[25] Given the absence of any safety net or possibility to create alternative livelihoods in developing countries, such a development could result in a severe social and economic crisis. Moreover, in comparison with the already developed countries, developing ones are forced to liberalize at an incredible speed. They have no time to adapt to changes, which causes them much harm. The weakness of this policy was visible, for example, in the case of Haiti. It had to reduce its rice tariffs from 35% to 3% in the course of just one year under an IMF adjustment programme. The result was an influx of rice from the USA, which forced tens of thousands of small local producers out of business.[26]

A POSSIBLE SOLUTION?

The EU should accept its moral debt to poverty in developing countries and primarily take their concerns into account. Therefore, it should liberalize its agriculture, while not requiring the same from developing countries. This would be the most effective way how to help developing countries to succeed in world trade, and thus to boost their economic development. They need to maintain some degree of protection so as to become developed. The East Asian Tigers[27] would never have become industrialized so successfully, if they had blindly followed free trade principles.

The liberalisation of CAP should proceed in three steps:

1) Abolishment of subsidies to EU farmers

If subsidies to EU farmers were abolished, only efficient farmers would remain in production. It would have two positive consequences and two negative

[7] Ian and Pamela Barnes, The Enlarged European Union. Longman: New York, 1995.

[8] As early as in 1963, Community-wide agricultural groups also began to be formed. Most important is the Committee of Agricultural Organizations in the EU, which serves as an umbrella organization for the farmers. See: N. Nugent.

[9] Steve Margetts, The Common Agricultural Policy (2004), <http://www.revisionguru.co.uk/economics/cap.htm>.

[10] N. Nugent.

ones. Among the positive belong economic benefits coming from the shift of saved resources into more effective sectors and obviously significant relief for developing countries.

The biggest negative effect would be growing unemployment and depopulation of rural areas. However, this malaise would have a treatment. Saved money from the EU budget could be allocated for rural development. For example, farmers would be encouraged to diversify their enterprise mix into other sectors than agriculture (such as tourism). Development spending would generate new employment opportunities in the countryside and thus prevent depopulation.

The second negative aspect would be a land degradation and from that subsequent environmental problems. However, even this problem would have a solution. Special agencies established in each Member State would buy land from unsuccessful farmers, in the event of their not being able to find other reasonable use for it or being unable to sell their land themselves on a free market for a "fair" price. These agencies would then plant the unused land with trees. This policy would serve many purposes. It would not only prevent soil degradation but in fact would be a long term investment, which would create new sources of employment without producing unusable surpluses of food; and it would improve the quality of air and decrease flood problems in Europe. Nevertheless, the most important incentive behind this policy should be that it would be a morally correct decision in relation to developing countries. European and other developed countries have sacrificed the great majority of their forests during the process of industrialization. Now the same countries are exerting pressure on developing countries to protect their environment and to save the last forests remaining on our planet to provide oxygen into the atmosphere. By doing that, we are denying developing countries their right to become industrialized, in the

[11] S. Margetts

[12] Faizel Ismail—Trade Law Centre for Southern Africa, Part II of the Road to Cancun: A development perspective on EU trade policies (2003), <http://www.tralac.org/scripts/content.php?id=1870>.

[13] Oxfam International, Europe's Double Standards: How the EU should reform its trade policies with the developing world (2002), <http://www.oxfam.org.uk/what_we_do/issues/trade/downloads/bp22_eutrade.pdf>.

same way that we did two centuries ago. Developed countries such as the EU are those which should be paying for preserving the last forests, since they are those which have destroyed them the most.

2) Abolishment of protectionist tariff and non-tariff barriers

The abolishment of protectionist practices would make it even more complicated for EU farmers to sustain competitive pressures. It would force them to become really effective to be able to survive. On the other hand, the subsequent fall of food prices would represent a huge relief for the budgets of EU consumers and all industries using food products as inputs. Moreover, so far disadvantaged developing countries would finally obtain access to the lucrative EU market. This should increase their share of world trade and thus boost their economic development.

Position of the EU on further liberalisation of CAP

Unfortunately, liberalisation of agriculture within the EU is a very sensitive question. It is very unlikely that the EU itself would push for a radical liberalisation of CAP. As former Agriculture Commissioner Franz Fischler said there was a clear bottom line in liberalisation of agriculture, up to where the EU was willing to go. He explained that agriculture required support from governments, since it served many more functions than mere food production which are not provided by the market mechanism. He expressed his conviction that the EU has already made enough concessions, that the EU is a long way ahead of most other developed countries in reforming its agricultural policy, and that this effort should be recognized and rewarded. In his personal opinion, reform of CAP has gone far enough in liberalisation and there is no need to go any further.[28]

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[14] Export dumping is exporting at prices below the costs of production.

[15] I. and P. Barnes

[16] The Everything But Arms Initiative is offered through the General System of Preferences to increase market access for Least Developed Countries. It provides duty-free and quota-free market access for all products originating from 49 Least Developed Countries except from arms. See: Speech by Pascal Lamy at 2nd LDC's Ministerial Conference in Dhaka (2003), <europa.eu.int/comm/commissioners/lamy/speeches_articles/spla171_en.htm>.

CONCLUSION

The Member States of the EU have significant moral debts to developing countries, particularly from the colonization era. If the EU wants to gain credibility as a trading block sincerely devoted to their development, it has to reform its CAP so as to meet basic domestic social and environmental goals but not to hinder their integration into world trading structure and thus their development.

[17] Oxfam International, Europe's Double Standards

[18] International Trade Centre UNCTAD/WTO, The Status of the Pre-Cancun Negotiations: A brief accounting of the Montreal ministerial meeting, World Trade Net Newsletter Vol. 4, No 7 (July 2003), <http://www.intracen.org/worldtradenet/welcome.htm?http&&&www.intracen.org/worldtradenet/docs/whatsnew/newsletters_2003/newslettervol4no7.htm>.

[19] Oxfam International, The Rural Poverty Trap

[20] Ibid

[21] International Trade Centre

[22] Oxfam International, The Rural Poverty Trap

[23] Oxfam International, Europe's Double Standards