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## What Future for the Common Agricultural Policy?

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# What Future for the Common Agricultural Policy?

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## 1. Changing agricultural world markets

International agricultural policy-making is faced with new trends on agricultural world markets. The recent price boom for cereals and, for some time, also for milk products is certainly due to specific short-term factors: bad weather conditions in major production regions, historically low storage levels for cereals, and speculation. But the rising price trend on agricultural world markets also reflects structural factors, and the trend is expected to continue over the next decade.

Basically, five structural factors drive the evolution on agricultural world markets. First, this is the increasing demand for food and feed in emerging economies, particularly in South Asia and South-East Asia. Second, this demand increase is confronted with limited productivity increases on the supply side. We have observed in the recent 10-15 years that agricultural productivity still goes up in major production regions of the world, but with a decreasing trend, also reflecting a neglect of research and investment in agriculture on a global scale. Third, rising energy prices lead to rising food and agricultural prices. This is due to increasing costs for intensive agriculture on the supply side and the increasing demand for bioenergy on the demand side. This effect is certainly enhanced by the current bioenergy policy in many industrialized regions in the world, notably in the European Union (EU), but also in the United States. The last factor to be mentioned though less measurable is climate change which is expected to lead to productivity decreases in major production regions of the world. The more important impact of climate change, however, might be a higher volatility on agricultural world markets due to increasing extreme weather conditions.

What are the responses to these challenges for agricultural policy-making in the EU and its neighbour countries?

## 2. Changing paradigms for the Common Agricultural Policy

From its very beginning the history of the EU's Common Agricultural Policy (CAP) is a history of reforms. Today, the EU's agricultural policy is a complex policy field which might better be characterized by "three" agricultural policies than just by one. Let us call them: The "old" agricultural policy, the "new" agricultural policy, and the "future" agricultural policy.

The "old" agricultural policy is characterized by market and price policies and protectionism trying to solve income problems of farmers. Today, the topics of this policy field are liberalisation and WTO negotiations and the future of direct payments. These direct payments have been introduced into the CAP since the MacSharry reform in 1992 accompanying liberalisation of agricultural markets and cutting down protection. Since the Luxembourg reform in 2003 most of

these direct payments have been “decoupled” avoiding production and trade distortions and bringing the CAP in line with WTO requirements. This “old” agricultural policy field is still relevant for the CAP and it is dominant for the EU budget, but time for this policy is running out. The question is how change can be designed. The topics are: further liberalisation of EU agricultural markets, full integration in world agriculture, and phasing out of direct payments.

The “new” agricultural policy has a broader perspective and is policy-making for rural areas. The question in this policy area is the supply of public goods and policy-making beyond markets. During the last decade the EU has forced agricultural policy-making into this direction. The question in this policy field is how such a policy for rural areas can actually be designed and what would be the role of old agricultural policy instruments in the new context. The “new” agricultural policy will certainly play an important role in the future, but still several problems have to be solved.

The “future” agricultural policy might be characterized by policy-making in times of new scarcity. Facing the global trends on agricultural markets new and other problems may become relevant for agricultural policy-makers. The problem may no longer be to think about price support but to deal with price fluctuations, production and market risks, and to reflect upon price stabilization policies. The policy perspective would be food security, and this will be less a problem for farmers, but for consumers, notably for low-income population groups and less developed countries. Generally, determining the path between food security and bioenergy production will become a key issue. There is no need to say that rich countries in Europe and other regions of the world should not endanger food security in less developed countries by imprudent bioenergy policies. Such topics of the agricultural policy of the future are emerging in the agricultural policy debate, but to a less extent yet as they should. We are still inclined to look on the old agricultural policy problems. Our view on agricultural policy-making is still affected by cheap food prices, surpluses, and farmer protection.

### **3. Open questions for the Common Agricultural Policy**

#### **3.1 The future of direct payments**

There is a growing debate on the future of direct payments in the CAP. Basically, three arguments are used to justify direct payments in the current and future policy framework. First, direct payments are considered as a major element of a stable policy framework in the adjustment process following the Luxembourg reform of 2003. But what is the time horizon for this adjustment process, and what is the adjustment need in times of stable and rising agricultural prices? Second, direct payments may be considered as a basic premium for providing public goods. However, 300 €/ha will certainly not be necessary to provide such goods, and a differentiated and more direct incentive policy to achieve the objectives pursued will be the better approach. Third, direct payments are said to compensate for higher standards and costs in EU agricultural production. This is a weak argument with respect to product quality standards, but may be a relevant argument with respect to processing standards. Calculations have shown that EU processing standards may in fact result in higher costs e.g. in pork production as compared to major global competitors, but the differences are rather small. Again,

differentiated and more direct incentive policies will be the better approach to deal with processing standards.

In view of these arguments the justification for future direct payments is rather weak. It is time to think about a future CAP without direct payments, and farmers should get a clear view on what they have to expect in this respect.

### **3.2 The future policy for rural areas**

The policy for rural areas is an acknowledged new policy field in the EU agricultural policy context. From the farmers' point of view this new 2. pillar of agricultural policy will certainly not replace the financial support of the historical 1. pillar. From a society's point of view the new direction is welcome, but there is criticism, too.

It is criticized that the new policy for rural areas is still very much sector-oriented and several instruments rather support farmers instead of achieving objectives properly. It is also criticized that important topics are missing on the EU's rural policy agenda: demographical change, climate change adaptation measures, and the focus on regional development potentials. Other questions relate to an integrated view of rural and structural policies and subsidiarity. There is a widespread opinion that the policy for rural areas has been shifted too much on the supranational level and should be decentralized.

Hence, the perspective for the EU's future policy for rural areas is not so clear as often claimed. It is an open secret that this policy field tends to be directed rather by financial funds instead of objectives and instruments. The key problem, despite all rhetoric is that the concept for rural areas still has to be sharpened. The new ideas under the current "health check" of the CAP do not yet solve the problem. New funds for the 2. pillar "modulated" from direct payments are to be used for new challenges: climate protection, renewable energy, water resources, and biodiversity. This may sound convincing, but it is not. The overall concept of which objectives should be pursued by the EU at the supranational level and which not, is not clear; and there is no reflection on priorities of measures. "More is better than less" is not yet a convincing policy concept.

### **3.3 The future bioenergy policy**

The EU continues to enforce bioenergy and biofuel production though the implications for agricultural price increases have become visible and may become drastic in the future. This may be positive from the farmers' point of view, but the question is how meaningful and sustainable this policy is.

In a recent study the German Scientific Council for Agricultural Policy has criticized the EU's and Germany's bioenergy policy suggesting thorough reflection and change. The basic argument is that CO<sub>2</sub> emission reduction costs of bioenergy production lines tend to be very high. The "benchmark" for avoiding CO<sub>2</sub> is the "price" of ca. 20-30 €/t CO<sub>2</sub> that has to be paid for a better isolation of buildings. A similar low price for CO<sub>2</sub> emission reduction can only be achieved for bioenergy production lines in few cases, e.g. burning wood and straw. In many cases CO<sub>2</sub> emission reduction costs for bioenergy lines are substantially higher, in particular for some biogas production lines and biofuel.

One need not be an economist to interpret such figures. Obviously the current bioenergy policy is rather inefficient: With the same financial resources much more climate protection could be achieved instead of using measures with little impact and high costs. Even more important is the fact that a continuation of this policy will have tremendous effects on agricultural prices with all negative implications for food security worldwide. It is not understandable that, despite all warnings, this oncoming and policy-induced problem is practically denied in many policy debates.

#### **4. Perspectives for the European Union and neighbour countries**

The agenda for future agricultural policy-making in the EU is quite obvious. The old concept has come to an end and the old instruments should be phased out. The new policy concept for rural areas must be further developed and sharpened. New ideas have to be developed to shape up an agricultural policy framework in times of fluctuating markets and new scarcity. And, the EU should definitely reflect and change its blue-eyed bioenergy policy.

From the EU farmers' point of view the future will not be to trust in old subsidies. Farmers already do and may benefit from new subsidies for bioenergy production in the future, but this new policy framework is hardly sustainable. In any case, the future for EU agriculture will be on markets and not only on EU markets, but on global markets under competitive conditions. There will certainly be new risks, but also chances and prospects.

From the point of view of new EU member countries it should be clear that the EU's CAP is in transition, maybe more than ever before. It is somewhat paradoxical that these countries had to adjust to and are on the way to fully adopt the instruments of the old agricultural policy which will be phasing out. On the other hand, these countries have certainly benefited from the policy concept for rural areas, but they have to notice that this concept is not "sacrosanct", but will have to be adjusted in the future or may even lose its importance as compared to today.

The same ideas will have to be reflected in countries on the way to joining the EU. The "acquis communautaire" is not a fixed, but a changing target, and this is, in particular, true for the CAP.

Current and future neighbour countries of the EU might benefit from the intensive agricultural policy debate in the EU: They might understand that the original protectionist agricultural policy approach does not fit into globalised agricultural markets and is not a model for future challenges. On the other hand, neighbour countries may benefit on the extensive EU experiences on broadening agriculture policy towards a policy for rural areas.

The basis for the EU's future cooperation with neighbour and third countries would be fair trade with market access opportunities on both sides. This will encourage countries with a comparative advantage for specific commodities to increase exports to the EU. On the other hand, those countries benefiting from preferential trade arrangements with the EU today might be hit by preference erosion. This may be a particular point for discussion and adjustment in the EU's southern and south-eastern neighbour countries.

All countries will have to face considerable consequences on agricultural markets if the EU and other countries continue and extend their current bioenergy support policy. Consequences may be more drastic than the implications of the old EU agricultural policy for the rest of the world.

Ambitious objectives and isolated approaches in the EU's bioenergy policy have to be questioned. There is a need for joint international actions and an integrated global view on food and energy security.

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