The Common Agricultural Policy and Trade

The Common Agricultural Policy [CAP], which started after the Second World War to ensure that Europe's farmers would always be able to feed Europe, has had an enormous effect on the trade in agricultural goods worldwide. Under the CAP, payments are given to farmers according to different criteria.

Subsidies work to artificially force down the price at which agricultural products can be sold, ie below the cost of production. This means that it is possible for European farmers to export their crops to countries and areas where the cost of production is actually much lower than that within the EU thereby undercutting the local producers [a process known as dumping]. This can have massive effects on the livelihoods of the world's farmers who are overwhelmingly among the world's poorest.

Types of Domestic Support

Given the way that subsidies have almost the same effect upon trade as tariffs and duties, they have been a part of the WTO and previously GATT negotiations, under the Agreement on Agriculture. Here they are subject to commitments to their reduction. Domestic support has been divided into three kinds, called boxes, based upon their likelihood to affect world markets:

Amber Box

These are the most trade distorting kinds of support such as those that increase the level of production, ie those that guarantee a minimum price and so encourage the production of a surplus at below the cost of production.

Green Box

These are called the "minimally trade-distorting support measures". They should not include price support or be linked to the quantity of production. They can include payments for research or food security stocks, direct payments to farmers decoupled from price or quantity, safety net payments and environmental or structural adjustment payments.

Blue Box

Blue Box payments include payments that do not increase the production of crops below the cost of production, ie payments for leaving fields fallow or reducing animal numbers subject to keeping production below a specified quota.

Reductions Required:

Amber Box: A negotiated level of reduction is included in the schedules that are negotiated. Subsidies that fall below de minimis levels are exempt from the total that is used to indicate the reductions required.

Blue Box: No reduction is required.

Green Box: No reduction is required.

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The Lastest EU CAP Reform: When is a Subisdy not a Subsidy?

In June 2003 the Council of the European Union agreed to a reform of the CAP. It would largely although not completely, de-couple payments from production, ie follow the American path of moving payments to the green and blue boxes under the WTO agreement where they are not subject to elimination over time. Although their impact is more subtle and harder to measure, many argue that de-coupling in and of itself does not reduce production and so therefore does not reduce the tendency for agricultural products to be dumped on third country markets.

Whilst CAP spending makes up around 50% of all EU budget expenditure, and billions of euros are spent annually on supporting European farmers, the price that European farmers can sell at does not reflect the real cost of production. Additionally, it appears that some of the direct payments that are made to farmers will be based upon their production levels during a set base period, a period in the past where their production level is measured. In the past and in similar situations in the US, the base periods have been moved, which means that farmers have an interest in maintaining production at high levels so as to benefit from future payments where the base period might be changed.

The time frame for the reduction of payments under the CAP has been set at being due for completion by 2013. This enables the EU to negotiate at the WTO on the basis of reforms that it is undertaking very slowly. The EU will thus be able to argue many times over that the developing world needs to open access to their markets to agricultural imports as well as expanding the negotiations into many other issues such as investment and competition. These are widely perceived as being of benefit to the large corporations at the expense of development amongst the world's poorest in return for their reform of the CAP.

Quantity of Subsidy:

A major issue for developing countries is the quantity of subsidy. No matter how the subsidies are arranged they still 'subsidise' agricultural production. Whereas the average cow in the EU earns $1.5 / day, there are 1.1 billion people in the world surviving on less than $1/day. Given the billions that are poured into European agriculture, it remains almost inevitable that European farmers can export at a level that undercuts what would otherwise be competitive farmers in the developing world.

Given the importance of agricultural production for many of the world's poorest people, subsidies have a massive detrimental effect on the likelihood that the world's poorest countries will successfully be able to enter the area, agriculture, where they should have, according to free-trade economics, the greatest comparative advantage.

Multifuctionality

At present there is an ongoing debate within WTO agricultural negotiations about the multifunctionality of agricultural subsidies. Under Green Box payments direct payments can be made for purposes that do not influence production such as animal welfare, environmental concerns and rural development. However many trade analysts question whether paying farmers to pursue this end is justified, especially as it can influence agricultural production through the volume of subsidies given. Some developing countries want to see tighter control over green box payments.

It is argued that the need for Europe to be able to use direct payments [payments made to each farm] as a means of maintaining Europe's countryside and safeguarding animal welfare and environmental issues justifies the subsidies. Many others remain doubtful as to whether they are truly directed towards these aims.