FAO AGRICULTURE AND TRADE POLICY

BACKGROUND NOTE

THE EUROPEAN UNION

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INTRODUCTION

Agriculture and agri-food sector play a vital role in the European Union (EU) and Common Agricultural Policy (CAP) of the EU shapes the policies applied in agriculture, food, and rural development in the union. This brief addresses main issues related to the overview of agricultural sector, domestic support, trade policy, recent reforms and developments in the EU.

OVERVIEW OF AGRICULTURAL SECTOR

The overview of Agricultural sector is summarized in Table 1. As can be seen, the share of agricultural population in the total population is low (5.13 %) and the share of agriculture in the GDP is 1.42 %. However, total agricultural value added is quite high (US$ 250 billion).

Table 1. Overview of Agricultural Sector in the EU

Total Population	503.680.116
Agricultural Population	25.883.000
Share of Agricultural Population, %	5.13
Total Land Area, ha.	418.173.000
Agricultural Land Area, ha.	188.405.000
Share of Agricultural Land Area, %	45.05
GDP, current US$ (1000000)	17.552.216
Agricultural value added, current US$ (1000000)	250.434
Share of Agriculture, % of GDP	1.42

Source: FAOSTAT, 2012; WDI, 2012.

Production

The EU is major producer of milk, pigs, cattle, and cereals in the world. Table 2 presents major commodities produced in the EU.

Table 2. Major Items Produced at Basic Prices, Euro Million, 2009

Product	Value
Milk	41.782
Pigs	29.987
Cattle	28.665
Fresh vegetables	28.620
Plants and flowers	19.302
Other forage plants	17.830
Wheat	17.019
Poultry	16.312
Wine	16.065

Source: WTO, 2011.

Trade

Major export items of the EU are cereals (mainly wheat), meat, fruits, and milk products, while the main import items are soya cake and beans, cereals (mainly coarse grains), fruits and vegetables, and sugar (Tables 3-4).

Table 3. Major Export Items of the EU, 1000 Tonne, 2009

Product	Quantity
Cereals	26779
Meat (beef and poultry)	2886
Fruits	2871
Soya cake and beans	2787
Fruit and Vegetable Preparations	1925
Milk and Milk Products	1539
Vegetables	1505
Wine	1654
Sugar	1488
Potatoes	1132

Source: EU, 2011.

Table 4. Major Import Items of the EU, 1000 Tonne, 2009

Product	Quantity
Soya Cake and Beans	37 826
Cereals	9319
Fruits	6740
Seed Oil	3449
Sugar	3056
Vegetables	1769
Rice	1477
Meat (Beef and Poultry)	1405
Wine	1315
Tobacco	613

Source: EU, 2011.

AGRICULTURAL SUPPORT

The total support estimate of the EU is approximately € 86 billion in 2011 (OECD, 2012a-b). This value consists of producer support estimate PSE (€ 74.2 billion), consumer support estimate (CSE) (€ -6.9 billion), and general service support estimate (GSSE) (€ 10.7 billion). The European Union has gradually reduced its support to agriculture, from production and trade distorting forms to the forms of area and income support. The level of price distortions has been significantly reduced as reflected by changes in the NPCs, ratio of domestic prices to world prices (Table 5). As a result of reform process, in 2011 the share of PSE in total gross farm receipts (percentage PSE) decreased to 18 % from 39 % and CSE decreased to 2 % from 36 % compared to the 1986-88 level. On the other hand, the share of general service support estimate increased to 12.5 % from 8.3 % in the same period.

Table 5. Estimates of Support to Agriculture, Euro Million, 1986-2011

	1986-88	**2011**
Total Value of Production	211 380	357 632
Total Value of Consumption	188 226	347 532
Producer Support Estimate (PSE)	**88 005**	**74 203**
Supports Based on Output	79 853	9 583
Payments Based on Input Use	4 565	11 262
Payments Based on Area and Income	3 195	13 893
Payments Based on Non commodity Criteria	428	1 515
Percentage PSE	**39**	**18**
Producer NPC	1.71	1.03
Producer NAC	1.65	1.21
General Service Support Estimate (GSSE)	**8 391**	**10 749**
GSSE as a share of TSE	**8.3**	**12.5**
Consumer Support Estimate (CSE)	**-65 589**	**-6 957**
Transfer to Producers from Consumers	-75 427	-8 297
Other Transfer From Consumers	-1 501	-1
Transfer to Consumers from Taxpayers	4 442	1 340
Excess Feed Cost	6 897	0
Percentage CSE	**-36**	**-2**
Consumer NPC	1.70	1.02
Consumer NAC	1.56	1.02
Total Support Estimate	**100 838**	**86 292**
Transfer From Consumers	76 928	8 297
Transfer From Taxpayers	25 411	77 995
Budget Revenue	-1 501	-1
Percentage TSE , GDP	**2.56**	**0.68**

Source: OECD, 2012b.

Producer single commodity transfers, which show the ratio of commodity specific transfers to the value of receipts from the production of that commodity, are presented in Figure 1. As can be seen rice, beef and veal, sheep meat, and poultry receive relatively higher supports in terms of transfers compared to other commodities. These values also reflect relative weights of producer groups in the union.

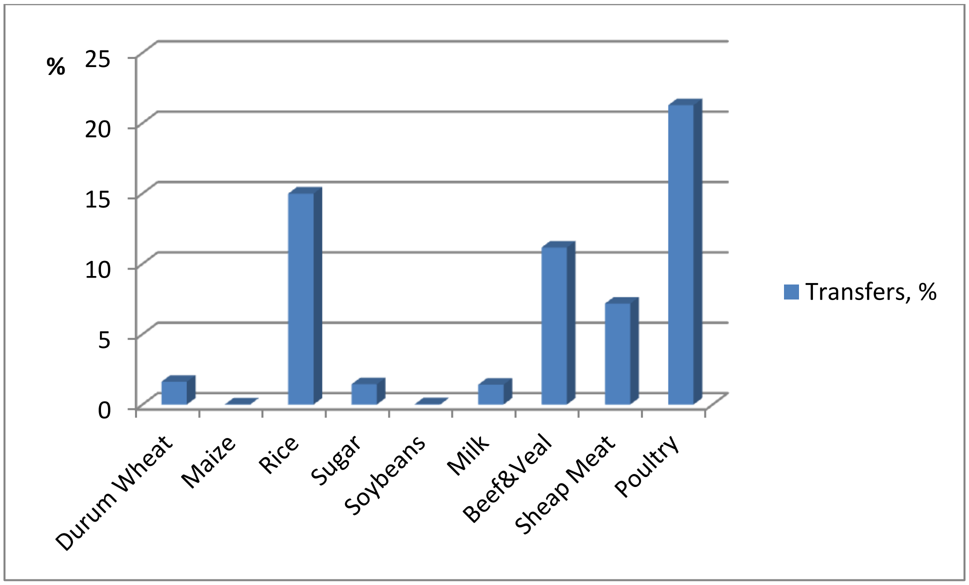

Figure 1. EU Producer Single Commodity Transfers (Ratio of Transfer to Value of Receipts) in Selected Commodities, %, 2011
Source: OECD, 2012a

Common Agricultural Policy (CAP)

The agricultural policy in the EU is shaped by the CAP, and is composed of two pillars. Pillar I regulates support measures under the Common Market Organization, and includes the Single Payment Scheme (SPS), and the Single Area Payment Scheme (SAPS). The SPS replaces various subsidies and decouples supports based on compliance with a set of environmental, food safety and animal and plant health standards. The SAPS is a transitional income support scheme offered to new members in order to facilitate the implementation of direct payments. This program is funded by the European Agricultural Guarantee Fund (EAGF). Pillar II includes various measures co-financed by EU member states, such as agri-environmental programs, payments to less favored areas, investment assistance, and is funded by the European

Agricultural Fund for Rural Development (EAFRD). The CAP has undergone various reforms since early 1990s. The major reform programs are summarized below (EC, 2012; OECD, 2011).

1-1992 MacSharry Reforms*:* The intervention prices in cereals were cut 30% and compensatory payments were introduced. The premiums for livestock were increased.

2-1995 Uruguay Round Agreement on Agriculture: Tariffication of border measures were introduced such that variable import levies were replaced by specific tariffs and tariff rate quotas, and the ceilings of export subsidies were reduced.

3-Agenda 2000: The Agenda 2000 reforms aimed more market orientation and increased competitiveness. The intervention prices were reduced further for cereals and beef, and rural development agenda is extended.

4-2003 Reform: The 2003 reforms made drastic changes such as decoupling of support payments. It introduced the concept of cross-compliance such that farmers need to obey certain rules (good agricultural practices, environmental standards) to be qualified for support. The modulation system aimed progressive reduction of direct payments allowing a transfer of funds from Pillar 1 (European Agricultural Guarantee Fund) to Pillar 2 (European Agricultural Fund for Rural Development).

5-2008 Health Check: The intervention price mechanism was reformed substantially. For instance, the intervention is abolished for pork, is limited for cereals, milk quotas were reorganized and will be eliminated in 2015, set-aside program (temporary removal of land from production) was abolished, all payments were integrated into SPS.

Current Supports

Decoupled Payments:

Most of the Pillar I payments are implemented as a single payment that does not require production. Under the SPS (applied in EU15, Malta and Slovenia) payment entitlements are based on historical references, either at individual farm level (historical model), at regional level (regional model) or as a combination of the two (hybrid model). Under the SAPS, each hectare in a member state receives the same payment rate. However, payments relating to the reform of the sugar regime and the fruit and vegetable regime may be paid on a historical basis. In EU15 countries, most payments for specific commodities are integrated into the single payment as of 2012. However, member states can introduce commodity-specific payments as part of the *Health Check* Regulation. This program gives them the option to use 10% of their national budget ceilings under EAGF for specific purposes. During the ten-year phase-in period, new member states may complement EU funds with Complementary National Direct payments (CNDPs) from national funds based on a defined ceiling.

Commodity Specific Supports

Cereals: The cereals in the EU are supported through a decoupled payments system, which means that payments are independent of production. The direct payment system provides flexibility to producers to switch to production of different crops according to the market signals. The intervention purchases are used only in real necessity. The imports and exports of cereals are subject to licensing. There are fixed and variable tariffs depending on the cereal types. The EU did not subsidize its cereal exports since 2006.

Sugar: The sugar policy includes quota management, reference price, and trade measures. The total quota of production is 13.3 million tonnes (EC, 2012) and divided between member states. Sugar factories are required to pay farmers a minimum price (Euro 26.29 per tonne), but out of quota production is not qualified for the payment. The reference price is fixed at Euro 404.4 per tonne. If the EU market price falls under the 85 % of reference price, private storage aid is activated. The EU became a net importer of sugar since the implementation of reform process. Thus, a safeguard mechanism is used for imports that exceed 3.5 million tonnes a year. In addition the EU implements a number of reduced duty import quotas (1 million tonne a year).

Milk and Milk Products: The EU designed a program called *Milk Package* for the support mechanism of milk and milk products. This program aims to support producers in the supply chain and favors market orientation. The package provides for written contracts and negotiation process between producers and processors. Farmers together with producer organizations can negotiate contract terms such as price of raw milk. The quota applied in the milk production is aimed to be ended in 2015.

Beef and Veal: The livestock sector is diversified in the member states. Thus the EU utilizes various support tools for the sector. Cattle farmers benefit from the decoupled single payment and, in addition, some countries support specialist beef production in marginal farming areas through coupled payments. The export subsidies are used for the beef and veal sector.

Pork and Poultry: For the pork, market management now occurs through aids for private storage. Support policies for poultry are usually related to the marketing standards, import and export licenses, common customs tariffs, and export refunds.

Cotton: Cotton is produced in Spain, Greece, and Portugal. Under the single payment scheme, national base areas are specified to be qualified for coupled payments (Greece: 370 000 ha, Spain: 70 000 ha, Portugal: 360 ha).

The summary of commodity specific supports tools can be seen in Table 6.

Table 6. Market Support Measures in the EU, 2009/2010

	Wheat	**Other Cereals**	**Rice**	**Sugar**	**Fruits and Veget.**	**Milk and Dairy Products**	**Beef and Veal**	**Lamb**	**Pork**	**Poultry**
Import Tariffs	x	x	x	x	x	x	x	x	x	x
Tariff Rate Quotas	x	x	x	x	x	x	x	x	x	x
Export Subsidies	xo	xo	xo	xo		x	x		x	x
Production Quotas				x		x				
Public Intervention	x	x	x	e		xo	x			
Private Storage				xo		xo	xo	xo	xo	
Market Withdrawals				xo	x	x				
Commodity Specific Consumer Subsidies					x	x				

Source: Adapted from OECD, 2011. Explanations: x: exist, xo: not currently used, e: ends in marketing year 2009/10.

Trade Policy Instruments

The EU applies common tariffs for imports. The MFN Tariff profile is presented in Table 7. In general, tariffs are higher for dairy products, sugar, and animal products. The agricultural tariff levels are considerably higher compared to non-agricultural sectors. In recent years the EU imposed import bans for sanitary reasons (meat products). In addition the EU made use of WTO's special safeguard provisions for poultry, eggs, and sugar (price based) and for fruits and vegetables (volume based). Export licenses are required to export products. Products eligible for export subsidies include wheat and wheat flour, coarse grains, rice, rapeseed, olive oil, sugar, dairy products, beef, pig meat and poultry meat, eggs, raw tobacco, alcohol and some processed products. In addition, export credits, insurance, and guarantees are granted at member level.

Table 7. Tariffs and Imports by Product Groups, the EU, 2011

Product Groups	*MFN Applied Duties*			*Imports*	
	Average	*Share of Duty Free*	*Maximum*	*Share in %*	*Duty-Free in %*
Animal Products	23.0	23.8	140	0.4	8.3
Dairy Products	55.2	0	205	0.0	0
Fruits, Vegetables	11.5	18.8	170	1.5	12.5
Coffee, Tea	6.2	27.1	25	0.9	77.1
Cereals&Prep	16.3	12.0	167	0.4	2.3
Oilseeds, Fats, Oils	7.1	43.5	171	1.4	72.7
Sugar	29.1	0	131	0.1	0
Beverages&Tobacco	19.2	19.8	162	0.6	16.8
Cotton	0	100.0	0	0.0	100.0
Other Agricultural Prod.	4.8	65.1	131	0.4	68.0
Fish&Fish Prod.	10.3	16.4	26	1.3	6.3
Minerals&Metals	2.0	49.9	12	16.6	72.3
Petrolium,	2.7	29.7	5	20.3	87.4
Chemicals	4.6	21.7	17	9.5	46.5
Wood, Paper	0.9	81.2	10	2.8	86.3
Textiles	6.6	2.1	12	2.2	2.3
Clothing	11.5	0	12	4.4	0
Leather, Footwear	4.2	22.7	17	2.4	17.8
Non-Electrical Machinery	1.9	21.4	10	10.9	56.4
Electrical Machinery	2.8	20.4	14	12.3	59.8
Transport Equipment	4.3	12.7	22	5.1	27.1
Manufactures	2.7	20.5	14	6.4	52.6

Source: WTO, 2012.

DISCUSSION OF POLICY CHANGES

WTO classifies domestic supports as Green box (minimal trade distorting policies such as government service programs, direct payments), Amber box (trade distorting programs such as price supports, deficiency payments) and Blue box (production limiting programs). Green and Blue box commitments are exempted from the WTO reduction commitments while the Amber box policies are subject to reduction commitments. The value of support in Amber box is calculated as Total Aggregate Measurement of Support (Total AMS). As mentioned above, the structure of support has changed significantly over the years. For instance since the marketing year 2000, Green Box support has almost tripled amounting to € 62.6 billion, Blue and Amber Box support have declined by 75 %, to about € 5.2 billion and € 12.4 billion respectively (WTO, 2011). Agricultural supports provided by Amber box decreased substantially because of the replacement of intervention purchases and payments by the SPS in the sectors of livestock and crops. Blue box supports covering the direct payments to farmers based on animal number and crop area declined as well. The decline is expected to continue because of the 2008 Health Check reforms. On the other hand, support provided for general services has remained constant over the past ten years, but in 2007/08 a quite significant increase was observed in spending on extension and advisory services (amounting to € 1.1 billion from € 347 million in the previous year).

Although recent reforms of the CAP shifted forms of support from intervention prices to direct payments, market price supports still have important role in total supports for some commodities such as beef and veal, poultry (OECD, 2012; WTO, 2011). The export subsidies were also reduced significantly, but are still applied for some sectors such as dairy and livestock. On the other hand, the relatively high MFN tariff rates were not influenced by the reforms.

The PSE values indicate that (OECD, 2012b) support based on output decreased significantly in 2011 compared to the base year of 1986, while the payments based on inputs and area increased significantly. In addition, the ratio of GSSE (research and development, training, infrastructure, marketing and promotion support) in total support increased to 12.5 % from the 8.3 %. As a result of the reforms, transfers from consumers decreased substantially, while those from taxpayers increased, and this contributed to the overall budget savings.

According to the OECD study (2011) the reform process improved the market orientation of farmers. The reforms allowed farmers to benefit from market opportunities caused by higher prices. However, the drawback is that an increasing proportion of support is transferred to non farming landowners and large farms. As a major player in world agricultural trade, The EU agricultural policies need to address some global problems in the future such as food security, climate change, and price volatility. Therefore future policies should consider risk management tools for farmers, agri-environmental programs should be designed to address global issues, and impacts on developing countries should be evaluated.

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