

European Network of Agricultural and Rural Policy Research Institutes (ENARPRI)
Seminar

*“The Interactions of Agricultural Trade Agreements: Scenarios on Multifunctionality
Impacts and EU-Policy Reactions”*

Andros, Greece, 2 October 2004

Agricultural Multifunctionality and EU Policies: Some Cautious Remarks

Kenneth J Thomson

University of Aberdeen, United Kingdom¹

Abstract

Multifunctionality has been suggested as a “new paradigm” for European agriculture and rural development, requiring “a fundamental rethinking of the position of agriculture within society”, and “a complete rethinking of the institutional system surrounding agriculture”. If this is true, neither the European Union nor the World Trade Organisation (WTO) has yet gone far in this direction, i.e. in actually making the “impacts” suggested by this Seminar’s title, or in forcing “policy reactions” to the new pressures and concerns involved in multifunctionality. However, the new Single Farm Payments of the Common Agricultural Policy, along with their “cross-compliance” conditions, do begin to emphasise new attitudes to farming’s contributions and responsibilities to various rural and societal demands. Moreover, agreement within the WTO Doha Round may both consolidate and accelerate this shift in the still-major costs of agricultural support. However, “integrated” and “territorial” policy approaches to rural development still pose some problems. The paper will explore these themes in a way intended to be relevant to local, regional and national decision-makers.

¹ Contact details: Emeritus Professor, Department of Land Economy, University of Aberdeen, St Mary’s, Elphinstone Road, Aberdeen AB15 8SJ, Scotland, United Kingdom. Tel. ++44(0)1224 274138, email k.j.thomson@abdn.ac.uk.

Agricultural Multifunctionality and EU Policies: Some Cautious Remarks

Kenneth J. Thomson, University of Aberdeen, Scotland, UK

Introduction: Some "External" Aspects

First, a few words about "external" developments that influence the above topic. The "July package" agreed for the WTO Doha Development Agenda (or Round) (WTO, 2004) determined a number of "modalities" for future negotiations, which are due to be completed by December 2005 but may take longer (and, if concluded, will certainly involve a substantial transitional adjustment period such as 5 or 6 years, like the Uruguay Round Agreement). Failure in July would have meant a severe and possibly fatal blow to Doha and perhaps the whole WTO trade dispute system. However, the July package only decided "what to talk about" - i.e. what will not be talked about, at least explicitly - in future negotiations. Agreed topics - within "*three pillars*", i.e. domestic support, export competition and market access, all of which "*form an interconnected whole and must be approached in a balanced and equitable manner*" - include:

- A 20 per cent cut in overall domestic support ceilings, to apply in the first year of the agreement as a "down payment". Even though the ceiling includes the CAP's "Blue Box" of payments linked to production limits, and 'de minimis' subsidies less than 5% of production value for any product, the EU is not expected to find this difficult after the recent CAP reforms. The total eventual percentage cut is still to be negotiated.
- Re-evaluated criteria for the "Green Box" of non-trade-distorting supports, such as income and environmental payments. Nevertheless, the EU expects the new Single Farm Payments to be included in the Green (rather than the Blue) Box.
- All export subsidies - including subsidy elements in the US export credit and food aid schemes, at the insistence of the EU and others - are to be phased out by the end of the implementing period, and monopoly export agencies such as the Canadian Wheat Board are to have their selling powers examined.
- Import tariffs are to be reduced according to a 'tiered' formula, with the highest tariffs subject to the largest cuts, and with a possible maximum tariff "cap".

These are all welcome items, especially the clear guidance on the expensive and trade-disruptive export subsidies. However, numbers - other than the initial 20% cut in aggregate domestic support, and the "zero" for export subsidies - have still to be negotiated: certainly, "free trade" completely unencumbered by direct and indirect barriers and supports is not to be expected. Moreover, countries may propose a number of products as "sensitive", for which tariff cuts may be less severe, although some expansion of tariff quotas must be permitted even for these. Special arrangements will apply for developing and least developing countries, and to cotton, and the issue of geographical indications (GIs) will be addressed.

Items not agreed in part or in full in the July package include "non-trade concerns", such as food security, rural development, environmental concerns and social aspects (e.g. minimum worker practices). These "*will be taken into account*", but are

effectively ruled out as matters which WTO members can raise for substantive negotiation.

A further “external” development of interest to the present paper is the expansion and changing nature of the European Union itself. Recently, 8 countries in Central Europe, along with Malta and Cyprus, have acceded to the EU, with transitional periods of up to 8 years, e.g. for CAP payments. Bulgaria, Romania and now Croatia are awaiting similar treatment in the next 2-3 years (European Commission, 2004a). A Commission opinion on beginning negotiations with Turkey is imminent (European Commission, 2004b), and other possible candidate countries include other parts of the former Republic of Yugoslavia. All these countries pose interesting but difficult questions as regards agriculture and agricultural trade, e.g. additional surpluses of sugar and dairy products in several Central European countries, relations with non-member countries in Central and Eastern Europe (and further afield), quite apart from the domestic problems of direct farm payments and standards in food processing plants for which perhaps only temporary solutions have been found.

More generally, the operation of the EU-25 has yet to settle down, with new and more Commissioners in their posts, and Councils of Ministers with a new voting system. They have a fairly clear but not easy agenda before them. In the economic sphere, this primarily comprises: maintaining the monetary disciplines of the Eurozone, promoting the “Lisbon agenda” of greater EU competitiveness, and agreeing the budgetary “framework” beyond 2006. This last point is overshadowed by disagreement over the overall size of the EU budget, with Britain, Sweden and others suggesting a limit of 1% of EU GDP, while the Commission proposes 1.17%. An additional complication is the proposed extension of the UK budget rebate formula to all member states. Given the 2002-agreed budget for most CAP spending until 2013, any cuts from the Commission’s proposals would fall mainly on “development”, both “regional” (or cohesion), and “rural”, i.e. within Pillar 2 of the CAP.

Finally, one cannot discount the constitutional uncertainties of the EU, both as regards the formal adoption (or rejection) by parliaments and/or popular referendums of the document proposed by Giscard d’Estaing and others, and the more informal acceptance of EU involvement in domestic affairs, ranging from taxation, workers’ rights, environmental regulation, etc. The EU cannot work by legislation alone, but needs the willingness of officials and citizens of its member states. Both in “old” members battered by past arguments, and in “new” ones only recently released from socialist domination, this willingness cannot be taken for granted but needs constant discussion, argument and persuasion, to gain acceptance both in the “recipient” country, and in its partners who must provide most of the necessary EU funds or are attempting to impose a commonality of rule.

Concepts of Agricultural Multifunctionality and Policy

Multifunctionality has been suggested (Van Huylenbroeck and Durand, 2004) has been suggested as a “new paradigm” for European agriculture and rural development, requiring “a fundamental rethinking of the position of agriculture within society”, and “a complete rethinking of the institutional system surrounding agriculture. Whether

this be true or not, it is a concept which has attracted increasing interest and attention - within the EU and beyond.

Formally, multifunctionality is the joint production of commodities and non-commodities (goods and services). However, as analysed first in detail for agriculture by the OECD (2001), the concept has a somewhat more restricted meaning, and policy intervention - such as ensuring the “European Model of Agriculture” via the CAP (European Commission, 2004c; Cardwell, 2004) - requires justification. Three questions have to be answered positively:

- Is there jointness, i.e. does the same farming activity produce more than one output?
- Is there market failure, i.e. is at least one of these products sold and bought on the market inefficiently (e.g. too little or too much, or in the wrong way), or not at all? - the latter include the cases of “public goods” such as attractive landscape and “public bads” such as water scarcity or pollution
- Have non-governmental solutions, such as privatisation, or market creation such as carbon credits, or consumer pressure via product labelling, been sought without success?

Only if the answer to all three questions is "yes" may direct policy interventions - which may conflict with trade liberalisation; see below - be the most efficient solution. Note the double use of the word “may” here: Policy intervention involves “transaction costs” - initial information gathering to assess the extent, severity and location of any “problem”, administration of payments, subsidies, taxes and charges, and of regulations, and enforcement costs such as inspection, law court cases, etc. Given these, and in a “second best” world where other inefficiencies may have distorted market prices such as those for farm and official labour, or for land, policy intervention should not automatically be invoked; it may be better to “leave well alone”, or at least to operate in other ways, such as demonstration and exhortation by governments and ministers, or by encouraging voluntary groups.

As mentioned above, policy interventions such as payments to farmers for environmental management may be held to conflict with trade liberalisation. It may be (and is) argued that monetary rewards to farmers adds to output, and thus “distorts” international trade. Once the effect is admitted, it becomes a matter of determining whether the trade effects are “minimal” (i.e. WTO-admissible) or significant. In turn, this requires definition of what is the “product” (all dairy products? bovine milk? cheese made from such milk? a particular kind of cheese?), and perhaps what the effects actually are, so that compensation can be offered. With (as is likely) a multiplicity of policy interventions, several interested parties inside and outside the EU, significant lags in agricultural restructuring, and the normal volatility in agricultural trade, one begins to see the complexities of the WTO negotiation and disputes procedures.

The Common Agricultural Policy and its Reform

For perhaps the first time since its inception, the CAP can be said to have undergone “fundamental reform”. There has not been complete reform, let alone abolition, of the

CAP, but the overwhelming bulk of production-linked - and hence production-incentivising - subsidies has been partly replaced by the Single Farm Payments (SFPs) which do not require specific farm outputs or even specific farm input use (such as headage payments or arable area payments). Recent work within the ESPON research programme (Shucksmith *et al.*, 2004) has demonstrated that direct payments to farmers are somewhat more consistent with territorial cohesion across Europe than the older Pillar 1 (and 2) payments. Of course, some governments have made full use of the options in the 2003 reform agreement to maintain some “coupled” or production-linked measures, or at least to minimise the geographical effects by adopting the “historical basis” for the new SFPs (see Shucksmith *et al.*, 2004, p.56). And import barriers - as well as the sugar and some other commodity regimes - were left largely unaffected.

However, the “new CAP” is more explicitly justified than ever in terms of agriculture’s social and environmental responsibilities rather than those related to food security and supplies. So far, the “cross-compliance” requirements attached to the SFPs have been limited, and have been mainly attached - at least in the UK and some other countries - to the conservation of soil, grazing and water. The many other actual and potential joint products of farming have not yet been recognised, even in crude “good practice” regulations.

In the future, more explicit consideration and recognition of agricultural multifunctionality, to be required as a condition of SFP receipts, may be expected. It remains to be seen whether the balances of SFP payment rates and conditions will be determined more by the Commission - which is mainly concerned with fair competition and minimal environmental standards - or by national and regional authorities - who may value certain public goods and bads quite differently, in accordance with local attitudes and political systems. However, the basic vehicle for multifunctionality policy, in the shape of the SFP, is now in place.

National and local differences can of course be expressed through the CAP’s Pillar 2, with its greater flexibility reflected by Rural Development Plans which cover agri-environmental measures as well as “development” proper (Kasimis and Stathakis, 2004). Unfortunately, the budgetary scope of Pillar 2 is still severely limited, both by the restricted extent of modulation, and by the pressures of national co-financing. Even under the Commission’s proposals (European Commission, 2004d), rural development spending does not rise greatly over the period 2007-2013, and, as mentioned above, any cutback of the overall EU budget by Finance Ministers would mean further pressure on Pillar 2 funds. Modulation funds, especially in the new member states, may well be devoted to the agrifood chain in the form of grants for farm modernisation and food processing and marketing, rather than to environmental or social purposes.

Partly to avoid the above danger (if it is so perceived), the Commission has proposed a new rural development policy, to be funded from a single European Agricultural Fund for Rural Development (EAFRD), and involving 3 “priority axes”:

- improving competitiveness
- land management, i.e. agri-environmental schemes
- diversification and quality of life

plus a multi-sectoral LEADER-type axis. Annual spend between 2007 and 2013 would average some €14 billion (at 2004 prices). This compares with some €43 billion per year on market and direct aids (the SFPs and remaining Pillar 1 payments), to which should be added the even larger economic effects of market protection via import tariffs and other barriers. Savings within the Rural Fund may be made by reducing the extent of the long-established and much-expanded Less Favoured Area scheme, but maintaining spend within the Objective 1 zones has been promised.

Thus CAP reform has some way to go before agricultural multifunctionality, alongside support for rural economic and social development, becomes the basis for EU intervention. However, the elements of a Common Rural Policy are in sight.

Research Issues

From a research point of view, optimal or at least less inefficient policy analysis for multifunctionality should address further and rather different issues. For example, what are the (monetary) “social” valuations of non-marketed goods and services, so that appropriate budgetary or other costs can be assessed? Do these valuations change over time (highly likely) as incomes increase, travel and leisure patterns change, or citizen concerns (e.g. over animal welfare, or rare wildlife species) alter? Jointness in production is unlikely to be fixed, e.g. in a 2:1 ratio, or even unidirectional, regardless of agricultural intensity; several researchers (e.g. Latacz-Lohmann and Hodge, 2001) have found a negative link between farming and environment if agriculture is introduced into wilderness areas, a positive link if farming is carried out at relatively low intensities (e.g. open and “interesting” landscapes) but a negative one (pollution, dull landscapes) at high farming intensities.

Other research - or at least public - issues concern governance: what level of administration is most appropriate for determining and administering multifunctionality? The EU principle of subsidiarity obviously applies here (Rabinowicz *et al.*, 2001), but then involves awkward questions of the relative roles of the EU, national and regional budgets (alongside private contributions) in covering necessary expenditures. An associated issue concerns risk management, if irreversible changes in natural resources (extinction of species, loss of traditional landscape features or local skills) are possible.

Further, farmers in Europe have been subjected over several decades to a substantial degree of both positive and negative policy interventions. The former include CAP subsidies and border protection, and tax concessions; the latter might cover the withdrawal (or non-provision) of some public services from rural areas, and increasing food and environmental regulation, often justified - at least rhetorically, if not always in practice - in terms of the Producer Pays Principle (PPP). In this complex context, introducing or modifying policy instruments for multifunctionality poses severe political as well as “technical” problems; the question of “entitlements” e.g. to compensation is bound to be raised (Buller, 2000).

One (partial) solution to these apparently hopeless problems is to limit interventions severely in territorial terms - the principle of *geographical specificity* - so as to be less likely to attract adverse attention in international trade negotiations. Of course, this

omits some widespread or even global public goods such as limiting climatic change, or protecting migratory species.

A further policy suggestion is to modify the application of policy as it affects “farmers” or, more generally, land owners and managers. The CAP was set up to support the “*agricultural community*” (Neville-Rolfe, 1984); but with 80% of EU output now produced from about 20% of its farms, there is a widespread imbalance (echoed in budgetary receipts) between farm output and farm households. Moreover, more and more farmland in Europe is being bought and sometimes managed for non-agricultural purposes - primarily for whole- or part-time residence, e.g. retirement and holiday homes. Such “privatisation” of the countryside is likely to have implications (some negative, some positive) for public interest, whether this be public access across the countryside on foot, cycle or horse, or the preservation of rare species or cultural or archaeological heritage. In this context, “agricultural multifunctionality” is only part of “rural multifunctionality”, and the CAP is ill-equipped - legally or politically - to address the difficult new problems which arise.

Conclusions

This paper has attempted a brief and summarised review of recent developments in agricultural policy (and perhaps, more widely, in the agri-food markets and sectors) as regards the concept of “multifunctionality” in farming, especially insofar as this links with policy actions (or inactions) by governments. This has been done largely at EU and international level, so that readers can compare their own national, regional and local experiences.

References

- Buller, H. (2000) *Actors, Institutions and Attitudes to Rural Development: the French National Report*. Research report to World-Wide Fund for Nature and the Statutory Countryside Agencies of Great Britain.
- Cardwell, M. (2004) *The European Model of Agriculture*, Oxford University Press.
- European Commission (2004a) *Enlargement website*:
http://europa.eu.int/comm/enlargement/index_en.html
- European Commission (2004b) *Regular Report on Turkey's progress towards accession*, COM(2004)656. Brussels.
http://europa.eu.int/comm/enlargement/report_2004/pdf/rr_tr_2004_en.pdf.
- European Commission (2004c) *What is the European Model of Agriculture?* In *Agriculture: Frequently Asked Questions*. Brussels.
http://europa.eu.int/comm/agriculture/faq/q1/index_en.htm.
- European Commission (2004d) *Proposal for a Council Regulation on support for rural development by the European Agricultural Fund for Rural Development (EAFRD)*, COM(2004)490 final. Brussels.

- Kasimis, C. and Stathakis, G. (eds.) (2004) *The Reform of the CAP and Rural Development in Southern Europe*. Aldershot: Ashgate.
- Latacz-Lohmann, U. and Hodge, I. (2001) Multifunctionality and Free Trade: Conflict or Harmony? *EuroChoices*, Premier Issue Spring 2001, 42-47.
- Neville-Rolfe, E. (1984) *The Politics of Agriculture in the European Community*, Policy Studies Institute (PSI), London.
- Organisation for Economic Cooperation and Development (2001) *Multifunctionality: Towards an Analytical Framework*. Paris.
- Rabinowicz E., Thomson K. J. and Nalin, E. (2001) *Subsidiarity, the CAP and EU Enlargement*, Swedish Institute for Food and Agricultural Economics (SLI) report 2001:3, Lund, Sweden.
- Shucksmith M. *et al.* (2004) *The Territorial Impact of CAP and Rural Development Policy*. ESPON Project 2.1.3 final report, August 2004, Luxembourg. www.espon.lu.
- Van Huylenbroeck G. and Durand G. (eds.) (2004) *Multifunctional Agriculture: a New Paradigm for European Agriculture and Rural Development*. Ashgate, Aldershot.
- World Trade Organisation (WTO) (2004) *Doha Work Programme: Draft General Council Decision of 31 July 2004*, General Council paper WT/GC/W/535. http://www.wto.org/english/tratop_e/dda_e/draft_text_gc_dg_31july04_e.htm