The Challenges of CAP Reform

Speech delivered by RISE Vice Chairman Corrado Pirzio-Birolli, to the Scottish Rural Property and Business Association

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Agriculture has an effect on and/or is affected by ten major world challenges: population growth, growing demand for crops, promotion of renewable energies, globalization, urbanization, climate change; growing public interest in agricultural public services, such as food and feed, rural landscapes maintenance, and animal welfare; social problems such as aging of farmers, farm successions and competition for land; increasing market volatility, and the timing and application of innovations such as biotechnology (GMOs, Nanotechnology), precision farming, carbon sequestration, and information technology.

Land managers are directly affected by, and impact on, all of these challenges, which are changing their industry quite radically, but don't enjoy the hearing that their key role warrants. This public neglect of their predicament is one of the reasons farmers still tend to opt for a status-quo that is not a realistic option for society.

The demands of society on Europe’s land managers are mind-boggling. In times of looming climate change, the production of eco-systems by farmers has become as important as that of food. They are asked not only to provide more and healthy food at stable and affordable prices, but also to supply fibre and renewable energy, apply more sustainable land management methods with diminished production intensity, reduce air, water and soil pollution, and improve the landscape. They are expected to do all this whilst preserving their economic and social sustainability and their cultural heritage, despite the uncertainties that are connected with more open markets and growing public demands to revoke the CAP. Few people sense that if the performance of land managers is found wanting, it is in good part due to an inappropriate legal and regulatory framework.

Ignoring that farming remains a key to Europe’s and the world's future would be a gross blunder. While climate change will make most of Europe an even more secure production location in comparison to other world regions, the EU net-agricultural-trade position is likely to deteriorate, over the next forty years, reducing EU capacity to help fight world starvation. Between now and 2050, EU demand for grains and oil seeds is expected to increase. Together with agro-energy production, it risks to make the EU a net importer of wheat at a time when food production may well decline in those countries that already record
increasing food deficits.\textsuperscript{1} We have recently witnessed fights for food in many countries, and seen many signs of international scramble for food, and for land to produce it. Some people say: “Don’t worry, markets always balance”, and FAO says the world is expected to produce enough food to feed itself by 2050. But there are three inescapable questions to the future of food: a) what will be its price, b) how many will not be able to afford it, and c) can more be produced sustainably?

The challenge is to devise a CAP that allows Europe to preserve its capacity to sustainably produce the food it needs and satisfy a growing world demand. This challenge is of a high order because today’s agriculture has become a net polluter. Unfortunately, EU budget talks are actually likely to overlook the Union’s role in world food security, as well the vital role of a reformed CAP in meeting the ten challenges I mentioned.

The Agenda 2020\textsuperscript{2} just published by the Commission betrays a lack of awareness of such a vital role. The Commission does of course admit the obvious that “it is necessary to harness the contribution of agricultural and rural development policies to address climate change and achieve biodiversity targets through adaptation measures based on a more efficient use of resources”. And it does also appropriately indicate that improving global food security is an EU objective. But when it advocates a decoupling of economic growth from resource use, is devotes less than one line to agriculture. The Commission seems oblivious of the countless interconnections of land management with most elements of the 2020 strategy.\textsuperscript{3} The biggest proof of such a mind-set is that the Commission’s “Consultation on the Future ‘EU 2020’ Strategy” of last November, even in its chapter 3. ‘Creating a competitive, connected and greener economy’, makes no reference at all to agriculture and rural development. No wonder then that virtually no respondents to that document made any reference to Europe’s foremost common policy.

The Commission urgently needs a wake up call. One can only hope that the Communication on the CAP post 2013 later this year will do more than simply “mirror” the objectives of the Agenda 2020, and propose to strengthen the CAP with the measures necessary and include them in an overall fully-fledged Agenda 2020 strategy, and that the relevant means will be set aside for that purpose in the New Financial Perspectives to be tabled next year.

A comprehensive and thorough study published in Nature Geoscience compiling the first comprehensive greenhouse balance of Europe shows that “emissions of

\textsuperscript{1} Particularly in sub-Saharan Africa and East Asia. Climate change is expected to have a minor impact additional hungry people compared to biofuels: 1-35m compared to 25-135m by 2030 (Fischer – 2009)
\textsuperscript{2} Communication from the Commission “2020, A strategy for smart, sustainable and inclusive growth”, 3 March 2010
\textsuperscript{3} See se insert “Flagship Initiative: Resource efficient Europe”, page 14
methane and nitrous oxide tip the balance and eliminate Europe's terrestrial sink of greenhouse-gases”. While European forests and grasslands embrace a strong 305m tons carbon sink every year, potentially offsetting 19% of the emissions from fossil fuel burning, Europe's agricultural lands are also emitting CO₂, which cancels part of this sink. They also release other GHG such as methane and nitrous dioxide as by-products from land management. The study concludes, “Stimulating the free service of aquatic and terrestrial ecosystems is considered one of the main, immediately available ways of reducing climate change”.

**CAP Reform post-2013**

The next reform will have to respond to questions about the objectives of the CAP in light of the challenges it faces. EU budget foes demand new justifications in order to accept to allocate a substantial share of future EU budgets to the CAP. But European farmers, like other entrepreneurs demand better policies, more stable regulatory frameworks, and positive incentives to meet society's goals.

Logically, the first reform question to be raised regards the **objective of the Single Farm Payment (SFP)**, whether it is or should be social/income support, and/or income stabilization, compensation for higher EU standards, or an environmental payment. From the answer(s) will depend any future adjustment in the SFP, and its distribution. Any such answer will prove hard to come by. But if, as it is widely believed, the purpose of the CAP will be further redefined away from production (“farming”) towards multifunctionality (“agriculture”), the current distribution of CAP resources will have to change.

Commissioner Dacian Ciolos has rightly told the EP that current inequities make a redistribution of the historical SFP necessary, particularly since it was “decoupled” from production. However, a readjustment in SFP allocation will raise its own problems of equity due to differences in national incomes, the productivity and value-added of farms, and increased price volatility. If these differences cannot be addressed via the EU budget, they may require an understanding as to the introduction and limits of national top ups to bridge them.

The second major reform question is how best foster a further “greening” of the CAP. This objective cannot be reached just through environmental regulations, which entail costs for producers without proper remuneration. How can land entrepreneurs be blamed for responding to market signals by producing more of what pays than what doesn’t? As farm prices rise, the opportunity cost of reducing farming intensity and using land to produce biodiversity and habitats rises as well. In order to encourage farmers to deliver those services one has to pay them enough to do so. Regulations must not be simply a certificate of good conscience. They must produce effects. Beyond a certain limit, farmers cannot merely be asked to pay penalties if they do not
implement environmental rules and objectives. They must also have, or be given the means to respect such rules and objectives, in full compliance with WTO rules. To that effect, direct CAP payments must cater for the environmental goals adopted by society.

When crop and meat prices are on average high, a greater shift from Pillar 1 to Pillar 2 via additional modulation becomes possible, using the money under Axis 2. But the weight of agriculture and downstream production services in Pillar 2 is currently too high. More of Pillar 2 should go to the non-agricultural population (which includes members of farmer families) and benefit the rural economy as a whole.

The tendency of the CAP to support public goods and services that are not paid for by the market will develop regardless of the evolution of farm incomes. These services notably concern resource protection in defence of the ecosystem: water management, carbon sequestration, biodiversity, the preservation of landscapes, notably in less favoured areas and the protection of the cultural heritage. There seems to be growing interest in the delivery of public goods through the CAP, which would require a commensurate budget to achieve that goal. The focus is therefore shifting to a better definition of public goods produced by farmers, and to how to pay for true environmental benefits.

This is no easy matter. Per hectare, probably regionalized payments may become more appropriate to reward agricultural management systems under clear conditions. Some of these could be targeted payments. Whether these will, or can be coupled payments or not won’t depend on whether they take place under Pillar 1 or Pillar 2, but will have to be compatible with WTO principles and negotiations. One should not make too much of a difference between the 1st and the 2nd Pillar of the CAP. They are man-made and we should not make icons of these structures, which are amenable to change. The purpose of policy is more important than the instrument used to reach it. But the preservation of the SFP, which provides a basic farm income, is essential to ensure farm income stability from below average incomes. Public goods production in agriculture depends on both pillars of the CAP. Less SFP means less public goods. Without economically viable farms there is no sustainable agriculture. The expenditure flexibility provided by Art. 68 must in future be confined to rural development actions, excluding additional production support.

Apart from SFP redistribution through regional and hybrid payment models, and a shift of CAP support for public goods by land managers, what other changes can we actually expect with the next CAP reform?

The abolition of obligatory set-aside is permanent. Agricultural export subsidies, while reduced, will not be abolished as long as there is no Doha Round agreement, and I doubt there will be one before CAP reform is settled. The commitment to abolish dairy quotas will stick, regardless of farm protests, but
concerns about the potential increase in diary production without quotas will have to lead to some sort of European Dairy Strategy. There will be no reintroduction of the classic market intervention, as against safety nets. Decoupling will become total. Something will be done to reduce the impact of market volatility.

Above all, there will be a stronger rural development policy. This may mean one or more of the following: stronger modulation of aid, a closer link between level of payments and service provisions, strengthening of Axis-2 and Leader-type programmes, more support for the place of the farmer in the food chain, via producer organizations, cooperatives and anti-trust policy (with exemptions where necessary), and the strengthening of cross compliance. Ideally, the reform should include a catalogue of defined measures that farmers could select and combine on the basis of a checklist.

Separately, one can only hope that subsidies for bio-fuels and on-shore wind energy, which pollutes the landscape, will stop, and that agriculture will have a much higher profile in the next R&D Framework Programme. R&D is a recently neglected key to the future of food and agriculture.

The speed of technological adaptation notably depends on the developments of biotechnology. A certain potential environmental risk with GMO crops remains. There is no zero risk. Do we take that risk or not? It depends on the objective. If we do take the risk in order to tackle climate change, then we should. In the context of accelerated climate change, ultimately, the risk of not using GMOs is probably greater than that of using them. But producers of GMOs should accept to be liable for environmental damages if any ever occur, as is the case in Germany. Subsidiarity will apply to domestic GMO regimes.

To sum up, we face a future of food scarcity, with high, albeit very volatile prices both for inputs and outputs. Farm subsidies, possibly not distorting trade, will have to stay if food scarcity is not to worsen. Southern hemisphere countries will have to introduce land reforms allowing the poor to accede to the land, and adopt more appropriate food pricing policies. But this will not suffice, because we also face a future of global warming.

Farming is one of the economic sectors that can do much for, but also against it. European society is rightly concerned that land managers are doing too little to counter biodiversity loss, pollution and environmental degradation. Why is this so? Because the conditions under which land managers operate are unfavourable.

In order to enhance its positive role on the climate, it is necessary to establish a better structure of incentives for farm delivery of eco-systems and other public services. If this cannot be done by creating the necessary markets, as is done with the Emission Trading Scheme, it will have to be achieved via targeted public
payments. Such payments exist already in other sectors, for instance to promote renewable energies. Moreover, agriculture and forestry must be included in a European Emission Trading Scheme for all GHG, including methane, as well as in any post-Kyoto deal in Mexico.