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The World Trade Organization and the Common Agricultural Policy:

Is the Common Agricultural Policy of the European Union Changing?

BA thesis in Philosophy, Politics & Economics

Supervised by Guðmundur Ólafsson

April 2011

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Abstract

This paper presents the World Trade Organization, and analyzes how ongoing international trade negotiations (the Doha Round), if completed, will significantly limit the protection provided to farmers in the European Union. Export subsidies will be eliminated and import tariffs lowered by 60%. Yet, deadlines for the agreement have been violated several times, and it is unclear when a Doha Round agreement will be struck.

Agricultural subsidies are widely supported in most European Union's member countries, both in the political sphere and amongst the public. The role and the budget of the Common Agricultural Policy (CAP) after 2013 is currently under revision. Although the system is controversial, the majority of political actors do not suggest any major changes. However, in the absence of a Doha Round agreement, a slight decrease in budget size and a reassessment of payments, leading to more equal distribution between farmers, can be expected.

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Abbreviations

bn	Billion(s)
CAP	Common Agricultural Policy of the European Union
DSB	Dispute Settlement Body
EEC	European Economic Community
ESCS	European Coal and Steel Community
EU	European Union
GDP	Gross Domestic Product
IMF	International Monetary Fund
GATT	The General Agreement on Tariffs and Trade
OECD	Organization for Economic Cooperation and Development
SPS	Single Payment Scheme
UK	The United Kingdom
USA	The Unites States of America
WTO	World Trade Organization

Introduction

Farmers in Europe and elsewhere have long held strong positions in society, and are often seen as fundamental to national (food) security and the conservation of particular traditions. Agriculture is generally subsidized heavily in richer countries and farm products face higher import tariffs, on average, than other products.

Since 1947, The General Agreement on Trade and Tariffs (GATT) and, since 1994, the World Trade Organization (WTO) have provided framework for world's governments to discuss and regulate trade. The main objectives have been lowering barriers and making trade more transparent. Open trade is believed to enhance economic growth and reduce the risk of war. Industrial tariffs have been reduced substantially since the foundation of the GATT, nevertheless negotiations have only recently started to involve agricultural trade. As a result, agricultural support is now on the decline worldwide.

In the European Union (EU), the Common Agricultural Policy (CAP) provides financial support to farmers, while it protects them from competition by common import barriers, such as tariffs and quotas. The system's estimated cost is a total of €87bn a year, or €187 per citizen of the Union.

Currently underway is the work to define the budget of the European Union for the period 2014-2020. The role and limits of the Union's most expensive program, the CAP, are being re-evaluated. The outcome could, in theory, lead to substantial reform of the system. I will scrutinize the main factors likely to influence the decision-making process, which has been defined as a "three-level game". It firstly takes place on a national-level through local governments, next, national governments and representatives negotiate within EU institutions. Finally, and possibly most importantly, states agree on limiting regulations through the WTO.

It is clear that WTO negotiations have for the last two decades influenced and even dictated reforms of the CAP. Therefore, the first chapter of this paper entails a detailed analysis of the WTO and an insight to the international reality of the CAP.

Methods and approach to subject

The aim of this paper is to identify and shed light on the politics and forces that will influence the current reform process of the CAP, and try to predict likely outcomes. The paper aims at answering the question: “Is the CAP Changing?”

Ideological and historical background of the WTO and the CAP will be examined to gain understanding and an overview of the two systems. Forces and arguments for and against the current system reform of the CAP will be analyzed. The rhetorics within both the EU and the WTO on the future of agricultural markets is an interesting and often fascinating subject. Yet, I will not judge whether one group or other has a more valid argument. My aim is rather to focus on analyzing neutrally the cirucumstances of the CAP, and the characteristics of each interest group and their claims. With this information gathered, I intend to predict, based on facts and with a realist perspective, which force will win in future reforms. As we know, it is not necessarily true that the most sensible ideas come out on top in political processes.

Sources of information are mainly academic papers and books on the subject. However, I made my own research and used primary sources as time and access allowed.

Assumptions

I assume all information published by the WTO and the European Commission to be accurate and not skewed on purpose. Nevertheless, I have done my best to compare all information to other reliable sources.

Limitations

The Common Agricultural Policy for 27 countries is a complex system. This paper only provides an overview of parameters used to measure the system as a whole, but does not represent the experience of particular programs and countries.

1. The Context of Agriculture: Organization of World Trade

A starting point is to understand the motivation of governments trade policy preferences, and the setting in which decisions are made. The framework of agriculture in the European Union is formed not only through European institutions, but largely by cooperation through international organizations as well as world markets. Before zooming in on the CAP it is important to be aware of deciding factors from outside the Union. The WTO holds a special status as "a regulator of the regulatory actions of governments".

1.1 Theory of Trade

There exists a generally accepted theory in social sciences called *comparative advantage*, introduced by the economist David Ricardo in 1817 (Mankiw & Taylor, 2006, p. 52). Comparative advantage is a fundamental law of economics. According to the theory, goods should be produced by those who can produce them in the cheapest manner, considering their opportunity cost. Countries, areas and individuals specialize in producing a certain kind of goods or services, and then trade with others, benefitting everyone concerned. Each party only produces what it has comparative advantage in producing and then trades with others. With specialization, production becomes more efficient, which then rewards everyone in a higher standard of living, as purchasing power and the overall economy grows. The law of comparative advantage proves with logic that there are mutual economical gains from trade. Simply put: we should not try to make everything at home because trade makes us better off.

The law of comparative advantage however leaves out an important factor; it does not take *trade costs* into account. Costs of trading can cancel out the gains of following comparative advantage. Trade costs can include transport cost, transaction cost, border and customs procedures, tariffs, taxes and more. Some of those costs are natural, such as transport and some minimal transaction cost, but others are government-made and are called *trade barriers* (Financial Times). With some goods, the costs can be trivial or insignificant. However in other cases trade costs can prevent trade from happening and thus hinder gains from trade (Krugman, 2010).[1] Trade facilitation and/or liberalization aims at minimizing trade

[1] For instance: trade costs are often trivial in the trade of crude oil; prices of crude oil are generally very similar in different markets. At the same time, prices of products such as fresh fruits or livestock animals can vary, transporting them in the right condition has a proportionally higher cost.

costs, for example by removing barriers such as tariffs (The World Bank). Getting rid of trade costs allows more trade and thus more benefits.

Though, the most obvious trade costs are tariffs, trade barriers can take number of forms, one is subsidies. Subsidies *distort* the market and an individual or a party might therefore have a “fictitious” comparative advantage. He specializes in producing something he is not best at producing, benefitting personally but laying costs on the whole society. This is often stated to be the case of the ineffective but highly protected sugar industry in the EU (The Economist, 2005). The subsidies are an expensive deal for European taxpayers while they keep other areas more suitable for producing sugar from developing as they might (Thurow & Winestock, 2005). Other trade barriers include production quotas, complicated or unreasonable laws on standards and general lack of transparency. Where there is will, there seems to be a way to impose trade barriers.

More harmful than trade barriers are unpredictable trade barriers. “Sudden” trade barriers have been put up for political reasons, and for protecting the interests of certain groups of people. *Trade wars* take place as countries try to punish each other for imposing barriers by setting up their own trade barriers (BBC News, 1999b). Instability caused by sudden changes in the trade system, raises prices and damages the world economy as a whole. Confidence, and thereby willingness to invest decreases when businesses are frequently caught by surprise. Unpredictability of an unstable environment makes businesses and individuals worse off, as planning becomes more difficult; operating costs increase. Those who get hit the worst by rising prices are repeatedly the poorest of poor.

1.2 Reality of Trade

Experience gives the theory of comparative advantage more authority; a correlation has been found between countries’ amount of trade with the outside world and their economic growth.[2] Governors tend to recognize the economical gains of trade with the outside world, or in another way of seeing it: they tend to recognize the cost of not trading. Governments generally would like other countries to embrace free trade. They want goods and services from their country to be exported fairly and sold to the highest bidder, for their country to make the most of its comparative advantages. Still, most governments are somehow involved in maintaining barriers, through some kind of market-distorting activities. This contradiction

[2] See for example: (Gylfason, 1999), (Yanikkaya, 2002) or (Mankiw G. , 2006).

has a number of explanations, although very commonly, they are justified by protection provided for certain domestic producers (Perdikis & Read, 2005, p. 3).

There are endless number of modern examples of proactive market distortions. In August 2010, one of the World's main wheat exporters, Russia, introduced a ban on all exports of wheat and other similar cereals. Although, curbing domestic inflation, the move harmed Russian farmers and contributed to the already high world market prices (Ghanem, 2010). Russia's main export markets, Egypt and other Middle Eastern countries, were particularly hit (BBC News, 2010a). Two closer examples of market distortion is when the Organization of Petroleum Exporting Countries, the 'OPEC Cartel', deliberately and openly, tries to coordinate the future world supply of oil (OPEC, 2008) and the way the EU protects its milk producers by upholding a value-added import tariffs of 49,5% on average on dairy products (UNCTAD/WTO, 2010). In the year 2011, the United States uphold active official bans on trade, *embargos*, with a number of countries for political reasons, some of which have been maintained for decades (U.S. Department of the Treasury, 2011).

Governments are constantly intervening in markets both temporally and in the long term with different reasoning, frequently favoring narrow interests at public cost. In the meanwhile, the world economy, according to the theory of comparative advantage, fails to fulfill its potentials. If more countries get drawn to imposing trade barriers, the risk of trade war increases. In the 1930s, countries all around the world, one after another increased trade barriers. They managed to punish each other but caused tensions and a collapse in world trade at the same time. The rise of trade barriers is blamed for contributing to the Great Depression (Noland, 2007).

It is argued that some countries (especially big economies) can benefit from market distortion policies if used appropriately (Hoekman & Kostecki, 1995, p. 56). Still most governors and experts agree that the best solution for even bigger countries would be: open, transparent and stable trade policies upheld by everyone (Mankiw & Taylor, 2006, p. 517). The difficulty is that only few countries seem ready to engage when they have no proof others will. There is a coordination problem, a kind of multiplayer prisoner's dilemma. 'I won't open my market unless you'll open yours'. Countries "defect" from free trade as they fear others will do the same.

1.3 The World Trade Organization (WTO)

WTO is intended to be a forum where governments can settle and commit in a credible way to multilateral agreements on world trade. WTO is an international organization that operates a system of trade rules that come out of negotiations between member states. The organization is meant to be a place to resolve and to avoid international trade disputes. According to a statement on the organization's website: "the most harmonious way to settle these differences is through some neutral procedure based on an agreed legal foundation." (WTO.a)

In the coordination problem of world trade, the larger task is to establish common non-discriminative trading rules to be fixed in the right way for everyone to benefit. That is the ideological background of the WTO. Nation's representatives come together and (seek to) agree and compromise on the future of world trade by creating a system of trade rules. "The WTO provides mechanism to induce countries to adopt non-discriminatory trade policies and reduce their barrires to trade, thereby enhancing efficiency and economic growth" (Hoekman & Kostecki, 1995, p. 51). The WTO gives disciplines to which government trade-policies should comply with for the sake of their own, as well as the greater good. Even if WTO cannot punish countries directly, bad reputation resulting from defecting from WTO regulations can prove costly in future international negotiations (Davis, 2003, p. 52). WTO is "a regulator of the regulatory actions of governments" (Hoekman & Kostecki, 1995, p. 12).

The establishment declaration of WTO, signed in 1994 by foreign ministers of 40 member countries, affirms:

> *The establishment of the World Trade Organization (WTO) ushers in a new era of global economic cooperation, reflecting the widespread desire to operate in a fairer and more open multilateral trading system for the benefit and welfare of their peoples. Ministers express their determination to resist protectionist pressures of all kinds* (WTO, 1994b).

The WTO operates from Geneva, Switzerland, it took over and updated an inter-governmental treaty called the General Agreement on Tariffs and Trade (GATT). GATT had the same purpose as the younger WTO: to facilitate the reduction of barriers and discriminating trade policies. The WTO was established by the conclusion of the eighth negotiation round under GATT: the *Uruguay Round*. The World Trade Organization could therefore be seen as a modern name rather than a new entity. However, with the change of names, the issues concerning the forum became of a wider range, by including trade in services such as telecommunications, banking, and intellectual property rights (Noland, 2007,

p. 214). The Uruguay Round also took up areas that previous negotiations had practically avoided: textile trade and the politically sensitive subject of agriculture. WTO has the status of an international organization while GATT was an inter-governmental treaty that was in 1994 modified and embodied in the WTO (Hoekman & Kostecki, 1995).

GATT came to exist in 1947, as the end result of tariff negotiations between 23 countries.[3] Although the incentives behind the GATT were clearly economic gains, it was at the same time, the belief that by ensuring more interdependence between countries the risk of war would be reduced (Hoekman & Kostecki, 1995).

1.4 Status of the World Trade Organization

The main aim of all negotiations since the appearance of GATT, has undoubtedly been trade facilitation. There seems to be a consensus amongst specialists that this development should continue, although it is not the answer to every problem of the world (Moore, 2004, p. vii). Markets failures do exist, and already in some circumstances WTO has been used to maintain trade barriers, to prevent spread of diseases and in some cases to protect consumers (WTO.a). WTO has been harshly criticized for overlooking issues such as protection of the environment, workers rights and transparency (BBC News, 2011a). Future agreements might well come to include *trade obligations*, concerned with ethics and issues of fairness, such as sustainability, as well as environmental and labor standards. An evidence of this possibility is that WTO regulations already allow states to ban imports of goods produced by prison labor, as well as market-distorting measures “necessary to protect human, animal or plant life or health” (WTO, 1994a). However, as the founding director of the Institute for European Environmental Policy reminded:

> *It is important to recognize that WTO negotiations do not aim at solving specific policy problems, such as the protection of the rural environment. They revolve around issues raised by member states and ultimately involve a process of bargaining that tends to exclude any item not represented at the table* (Moltke, 2004, p. 11).

Regulations of the WTO are in fact written by nobody but member states, and they do not pass without the signature of representatives of every member country, which since 2010 are

[3] The 23 countries were the following: Australia, Belgium, Brazil, Burma, Canada, Ceylon, Chile, China, Cuba, the Czechoslovak Republic, France, India, Lebanon, Luxemburg, the Netherlands, New Zealand, Norway, Pakistan, Southern Rhodesia, Syria, South Africa, the United Kingdom, and the United States.

153, making up more than 97% of international trade (UNCTAD/WTO, 2010, p. 2). The adoption of WTO labor standards has been resisted strongly by many developing countries, fulfilling such standards would be costly for underdeveloped countries and some leaders argue they might be used for protectionism and unfair sanctions against their countries (Baldwin, 2004, p. 55).

The highest authority of the WTO is a gathering of ministers of member countries, that reunite usually every two years in *Ministerial Conferences*.[4] While on day to day basis, the organization is run by the *General Council* which works on the behalf of the ministerial conferences. The Council is made up by ambassadors of all member state. One of the tasks of the General Council is to run the *Dispute Settlement Body* (DSB), a neutral body helping states to reach conclusions on conflicts that arise on the practice of trade and the interpretation of WTO agreements. Disputes often end with *early concession*; by the disputing parties simply sitting down to discuss the case. If early concession is not reached, a panel of experts is put together to report on the case. The experts are chosen, if possible, in accordance with the disputing parties. Next, the General Council accepts or rejects the judgment of the experts by a consensus of all representatives. Finally, either side can decide to appeal the ruling to the *Appellate Body*, which works much like the panel of experts, except it is filled up by permanent members, sitting four years each. After the Appellate Body sends out its report, the General Council makes the final verdict. Although DSB or the General Council has no direct power of enforcement, more than 300 cases have been brought to the body since the establishment of the WTO. This provides evidence of the legitimacy of the DSB and is "a strong indication that legalism influences state behavior" (Davis, 2003, p. 49).

Another important part of the WTO is the *Secretariat*, a body of 629 full-time employees. The Secretariat organizes and coordinates meetings and provides technical support to member governments in carrying out activities related to the Organization. The Secretariat chairs negotiations but is also meant to help poorer and smaller countries with limited capacity to deal with complication involved with international law making and compliance.

The WTO has often been portrayed in a negative way; it is criticized for serving the interests of corporations, while it lacks democratic accountability, and violates states sovereignty.[5] A country might through international pressure decide to accept an agreement

[4] Generally foreign ministers or ministers of commerce.

[5] See for example (Þorsteinsson, 2005), (Wallach & Sforza, 1999) or (Preston, 1999)

highly unpopular at home. Many respond to such criticism by highlighting that the WTO does not take decisions independently but rather are agreements made by member states, many of which are run by democratically voted governments. Others point to the importance of increased economic prosperity, and world order that would not be possible without the WTO.

Cristina Davis, a professor at Princeton University, argues with the support of statistical analysis of negotiations rounds, that the legal framing provided by a formal institution such as the WTO has allowed greater liberalization, than otherwise could have been realized. WTO helps to bypass political obstacles (Davis, 2003, pp. 69-70). The study also shows that linking together various subjects in trade rounds, in *package negotiations,* boosts the likelihood of major liberalization, especially in the field of agriculture, one of the most difficult to negotiate. When more fields are interconnected it is easier for all parties to identify benefits of a negotiation round. Although a government meets political obstacles at home for liberalizing trade in one field, it might receive strong support by achieving liberalization for other products.

Oxfam, a major international charity organization, has stated that the current regulations and agreements of the WTO are unfair and greatly favor richer nations. However, according to the organization: WTO is still a better ground than bilateral agreements for developing nations and more trade can benefit everyone (Oxfam International). Assuming that liberalizing and standardizing trade is a worthy task, it can be said the GATT/WTO project has been a very successful project, although there is still work to be done.

The fact is that, since 1947, major trade liberalization has been achieved, industrial tariffs have come down by 90%, and other areas are being worked on (Dadush, 2006). The world has seen tremendous growth in international trade and economic output.

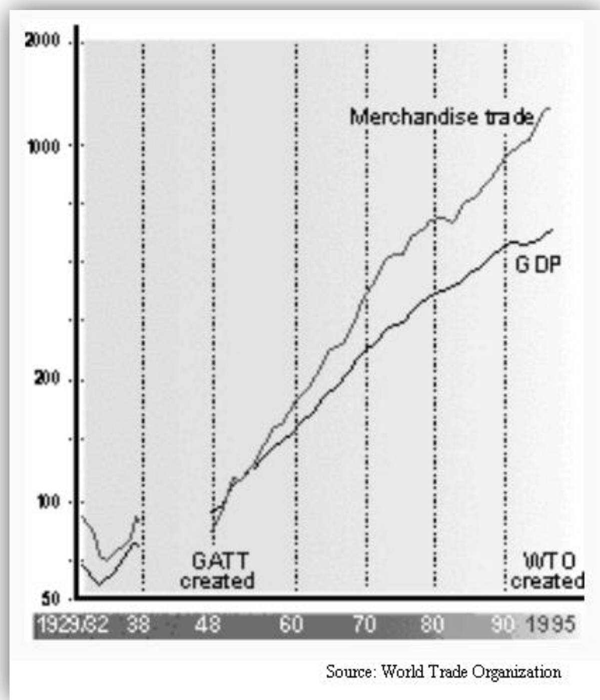


Chart 1: Growth in economic output (GDP) and trade in goods from 1929 until 1995. 1950 = 100.

1.5 Agriculture and the Doha Round

The current regulations of the WTO are the result of the Uruguay Round negotiations which started in 1986 and were concluded with an agreement of 123 nations in 1994. ”Most probably the largest negotiation of any kind in history” (WTO.b) and the first WTO agreement to take agriculture into account. Included in the agreement was also a commitment to continue further reforms regarding agriculture, services and intellectual property rights in near future. It furthermore set up a framework and definitions that future negotiations could be based upon. Agricultural support was categorized into three “pillars”: (1) market access, (2) export subsidies, and (3) domestic support. As of market access, non-tariff barriers had to be replaced by tariffs that could not exceed a specific upper limit. Export subsidies were also bound to certain limits. Finally, domestic support programs or subsidies were categorized into three “boxes”, according to their degree of “trade distortion”: (1) green box, (2) blue box, and (3) amber box. The programs of the first two boxes were not limited in any way while amber box programs, considered the most market distorting, were bound to a limit with reference to historical subsidies (Hart & Beghin, 2006, p. 221).

Typical amber box trade distortions are subsidies encouraging or rewarding production. An example is when the EU buys produce from farmers above market price and possibly also above production cost at a ‘guaranteed minimum price’ (Le Monde diplomatique, 2005).

A fruitless ministerial conference, in Seattle 1999, failed to lunch a new round of negotiations, and was rather remembered for ‘out of control’ protests that created almost unbearable working conditions for ministers. Demonstrators fought the “Battle of Seattle” amongst other things for a fairer treatment of poorer countries, as well as labor and environmental standards (BBC News, 1999a). It was a ministerial meeting in Doha, Qatar two years later, where a new round of negotiations was finally lunched, with a declaration called the ‘Doha Development Agenda’. Ministers recognized that the WTO has contributed positively to the world economy and stated determination to continue “the process of reform and liberalization of trade policies”, especially in order to help developing countries, while they vowed “to reject the use of protectionism“ (WTO, 2001). The agenda, amongst other things, repeated calls for further commitment in agriculture. Experience shows that when a negotiation agenda has been formalized, anyone arguing for a change must present a very strong case in order to achieve amendments (Davis, 2003, p. 43).

In the spring 2011, after almost ten years of continuous discussions and three full ministerial conferences, no final agreement has been reached in the negotiations.[6] The World Bank has stated that a serious reduction in trade barriers would far exceed benefits from current development assistance (The World Bank, 2004, p. 105). Furthermore that barriers to trade in agricultural products are the biggest obstacle to development (Jonquieres, 2003). However, there are many concerns and not much progress has been made. The Doha round has been characterized by “insoluble conflict over agricultural subsidies by developed nations, an issue threatening to undermine the WTO” (Goldstein, 2007, p. 272).

Whether different in nature or not, liberalizing trade of agricultural products has been a more difficult than trade in other areas. In a 12 year-old study done for the OECD, it is stated that agricultural tariffs in developed countries are tenfold industrial tariffs. In developing countries the difference is smaller but still notable (Josling, 1998). Agricultural tariffs have increased while industrial tariffs have come down by 90% since the beginning of GATT (Dadush, 2006). Although the Uruguay round agreement (1994) was a breakthrough, as it managed to reverse the development of agricultural tariffs.

There seems to be a general consensus about the benefits of liberalizing the system to some extent, but farm lobbies tend to hold great power, especially in richer countries. Also

[6] Ministerial conferences were held in Mexico in 2003, Hong Kong in 2005 and Geneva in 2009.

arguments related to regional policies, food security, maintenance of cultural heritage and concerns about unsustainability come forward in defense of protectionism. However, the reason for the current system might be simpler, one expert explains straight out: "states intervene in agricultural markets because farmers are an important political constituency whose role in society rallies the sympathy of the general population." (Davis, 2003, p. 37). Taking that into account, a study done for the World Bank points to the fact that farming population and farm political representation in the countries where probably the hardest opposition to liberalization is found (EU and USA) farmers are ageing quickly and are only being very slowly replaced. Therefore, their strength should gradually decline (Hart & Beghin, 2006, p. 237).

Doubts on the fairness of the trade rules are growing and agricultural regulations are at the center of that criticism. The fact that certain developing countries are gaining strength in international diplomacy means they will be able to put more pressure on the old rich world to liberalize. On the other hand experts writing for the World Bank (Hart & Beghin, 2006) are probably right when they say "it is foolish to hope that vested agricultural interests in some of the high- and middle-income countries would give up huge and concentrated rents without virulent and long fights" (p. 237). They remind that it took many decades and eight negotiations rounds to lower industrial tariffs to the current level. With information gathered: considering the long term prospects of agricultural regulations - a major liberalization in agriculture is most definitely to be expected, eventually. For the next years, it is harder to expect anything, each year of failure to reach a Doha agreement seems to lower expectations.

The Doha agenda had in 2001 set a deadline for the conclusion of the negotiation round at January, 2005. Although some progress was seen, the deadline was moved to 2006. 'Last chance' talks held in 2008, collapsed. A rise has been seen in bilateral agreements, which are believed to benefit stronger countries, while developing countries suffer (Matthews, 2010b). The government office of sciences in the UK concludes a study:

> *Were there to be a substantial breakdown in world trade negotiations followed by countries adopting the maximum levels of intervention allowed under the Uruguay trade round, there would be a major risk of a recession in the agricultural sector of many middle- and low-income countries. Decreased global production would raise prices and threaten food security, risking a large increase in the numbers of people suffering hunger.*
> (The Government Office for Science, 2011)

Governments are under pressure, but disputes on agriculture remain the main obstacles in the way of a final agreement; developing countries feel that they should be permitted more flexibility and developed countries find hard to accept making “sacrifices” alone. It seems that developed countries want to make sure they can take advantage of this big play card, by ensuring market access in other areas. **As things look: a Doha agreement would mean gradual elimination of all export subsidies for agricultural goods, as well as a commitment to limit amber box domestic support and improve market access through lowered tariffs.** Currently the main disagreements are on cotton subsidies and details of the *special safeguard measure* (SSM) (Bhagwati & Sutherland, 2011). SSM “would allow developing countries to raise tariffs temporarily to deal with import surges and price falls“ (WTO, 2008), what has not been agreed upon is exactly how much and for how long such measures could last.

Analysts and negotiators may have grown tired, yet, governments are at the present encouraging each other to compromise and focus to conclude the Doha Round (BBC News, 2011b). A group of experts (put together by the governments of Germany, Great Britain, Indonesia and Turkey, to report on what actions are missing for a successful Doha negotiations) state that a great bulk of the work is already done and only minor gaps remain to be closed. The experts demand an “absolute deadline” by the end of 2011 for a Doha agreement to be concluded (Bhagwati & Sutherland, 2011).

2. The Common Agricultural Policy

The Common Agricultural Policy of the European Union (CAP) is a system of controlling the production and sale of farm produce. Government money is paid to farmers throughout the Union, while they are also protected from competition by common import barriers, such as tariffs and quotas. In the past, the amount of money paid to farmers was related directly (coupled) to what and how much farmers produced, since 1992 the CAP payments increasingly rely on other references, such as fulfillment of environmental standards. The role and budget size of the CAP, for the years beyond 2013, is currently under revision, the outcome could lead to a substantial reform of the system. The decision process is initiated and supported by the European Commission, but the final decision will be taken in cooperation between the European Parliament and Council of Ministers (Zahrnt, 2011a).

The following chapter and subchapters present an overview of the CAP. The system is very extensive and complex; the analysis can therefore not cover the entire program. I will give details of the more important features while analysis of others is sacrificed, in order to not lose focus of the big picture. The chapter is divided into four parts: The first part provides a brief overview of the background of the system, while the second explains the system as it functions today. The third focuses on different perspectives and rhetorics concerning the reform debate in the last years. Finally, in the last subchapter I attempt to forecast CAPs future, in a realistic and fact based way.

2.1 History of the CAP

Although the EU did not come to exist until 1992, with the Maastricht agreement, the first steps towards cooperation were taken in 1951, when France, West Germany, and four other countries founded the European Coal and Steel Community (ESCS). A further step was taken in 1957, with the Treaty of Rome, that transformed the ESCS into the European Economic Community (EEC), and established one common market for goods throughout member states. The common market came to include agricultural products, that were defined as “products of the soil, of stockfarming and of fisheries and products of first-stage processing directly related to these products” (The Treaty, 1957). At the same time, governments agreed that the common market for agricultural products had to be accompanied by a common agricultural policy.

All countries had intervened heavily in their own markets before, and so it continued to be under the CAP. National barriers and interventions were abolished and replaced by the common system. During the negotiations of the treaty, France especially insisted on a system of agricultural subsidies (BBC News, 2010b). Objectives of the new system were defined by fear of food supply shortage; by the hunger experienced in the continent in relation to the World Wars (Chaffin, 2010). Food production was to be increased and stabilized and at the same time agricultural communities were to be ensured "a fair standard of living", while providing goods at a reasonable price to the consumer (The Treaty, 1957). In 1958 at the Stresa conference, more detailed talks on the future system took place, and four main principles of the CAP were laid out (Blanc, 2002, p. 47).

1) Free movement of goods within the community.

2) Community preference. A common market protected by tariffs on imports, from outside the community, valued below a certain price: *threshold price*.

3) Common intervention. Produce bought from farmers at a guaranteed minimum price: *intervention price*.

4) Financial Solidarity. Each country contributes to the common fund used for interventions.

Based on these four principles, the CAP began gradually to come into force in 1962. In less than a decade, it had transformed the European Community from a net importer of agricultural products into a major exporter (Davis, 2003, p. 10). Over time, other elements have been added to the system, including: import quotas, production quotas (1984), set-aside payments (1988), private storage aid, less favored areas aid, rural development measures (2000), export refunds and more.

The CAP budget for a long time represented over two-thirds of the community's common expenses (European Commission, 2007), today the number is down to less than 50%. The total expenditure of the system in 2009 was €55 billions, or around €110 per citizen of the EU (Chaffin, 2010). At the same time the average import tariffs on agricultural goods averaged around 13.5% (UNCTAD/WTO, 2010). Tariffs were higher in the past, but between 1994 and 2000, as a part of the Uruguay agreement, the EU committed to an average reduction of 36% (USEU).

Until the "Mac Sharry reform" in 1992, almost CAP's entire budget was spent on common interventions and market support through export subsidies (BBC News, 2008). In the

1980s, the common intervention policy had become very unpopular for leading to over-production, by guaranteeing farmers a minimum price for certain products, which was often far above world market price. Farmers had always an incentive to produce, although sometimes there was no demand for their products. Mountains of butter and other produce built up and were stored for later, destroyed or dumped on international markets. The market interventions came at high cost to taxpayers in the EU, and farmers outside the Union suffered from a drop in prices when European mountains of food were dumped on the market (European Commission, 2007). In 1992, the guaranteed price started to be lowered, and support to producers moved to other forms. Particularly, annual direct payments, subventions related to production levels, but also included set-aside payments that rewarded farmers for leaving proportions of their land not in cultivation.

As guaranteed prices were lowered further in 2000, a new program was started called rural development. The program consists of providing money for various development projects, and support to farmers with objectives such as: training farmers, helping them to diversify rural income, assisting modernization of farms, and to generally increase quality of life in rural areas (Moussis, 2009). The program also includes less favored areas payments, providing additional subsidies to farmers in less fertile areas.

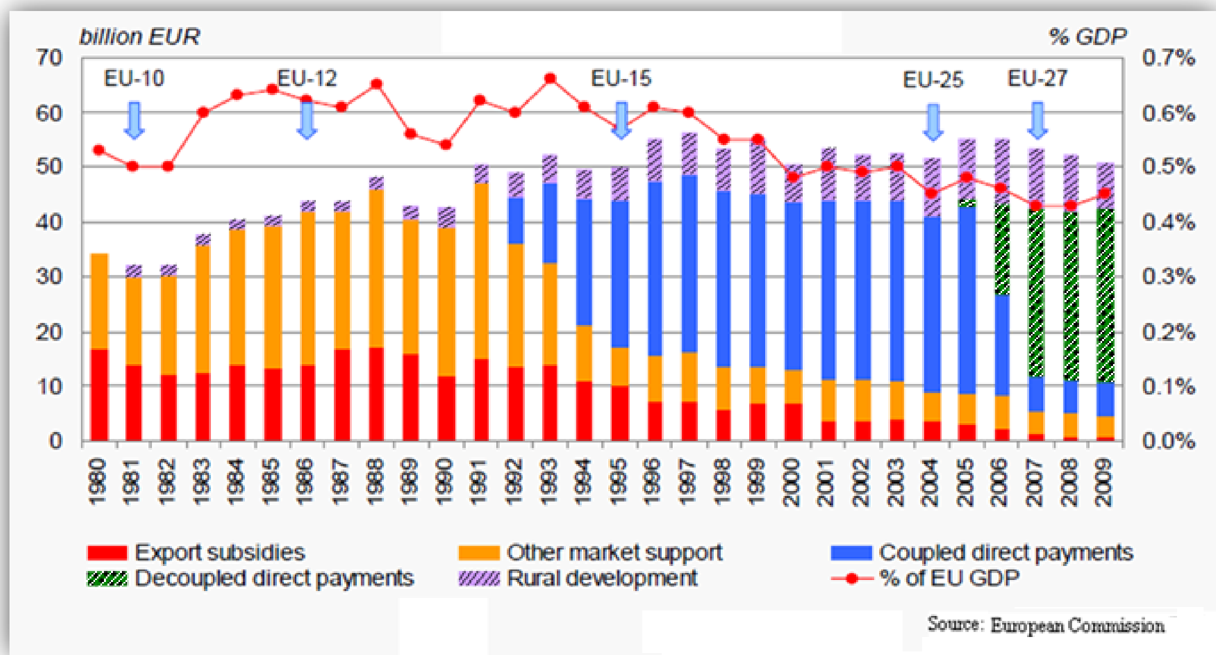


Chart 2: CAP expenditures 1980-2009 (2007 constant price). The chart most importantly shows CAP expenditure as a whole and as a % of GDP. Also how market support (interventions, including export subsidies), and later production related payments (couple direct payments) gives way to other WTO friendlier programs.

The CAP was last reformed in 2003, when it was decided to lower intervention prices once more over time. However, as seen in chart 2, CAP expenditures would not decrease. A new program was started: the Single Payment Scheme (SPS).[7] SPS offers farmers direct payments that are not linked (coupled) with the level or the type of production, but with historical production of the land between 2000 and 2002, and *cross compliance* to certain standards that include: fulfillment of environmental standards, and animal welfare. SPS are subsidies, even though they are *decoupled* from production. Through SPS farmers receive money independently from how much they produce or if they produce anything at all, which stabilizes their income. The decision of 'what and how much to produce' is now more up to farmers' estimation of the market. It should be noted that the decrease in market interventions in 2003 was not optional. It was necessary for the CAP to comply with the Uruguay round agricultural trade agreement (Chaffin, 2010). The SPS does not fall into WTOs most trade distorting category, the amber box, along with common interventions (Swinbank & Tranter, 2005). A new reform defining the role of CAP until 2020 is currently being prepared. The depth of the reform will depend on EU (now composed of 27 states) internal politics, which will be constrained by conflicts of interests within the Union as well as the Doha Development round.

2.2 Active protectionism: the CAP today

CAP activities are categorized into two types, called *Pillar 1* and *Pillar 2*. Pillar 1 covers direct payments to farmers and market measures (intervention price mechanism and import barriers). Pillar 2, which was founded in 1999, covers rural development measures. The two pillars are financed by two different funds, the second pillar is also co-financed by concerning member countries, with a contribution of around one third (House of Lords, 2005). Expenses for each fund in 2011 are outlined €42.9bn for Pillar 1 and €15.7bn for Pillar 2 (European Commission, 2010b).

The total expenditures of the CAP, in 2009, were €55bn. However, that number ignores the cost that import tariffs on agricultural products lay on consumers. The Organisation for Economic Cooperation and Development (OECD) calculates yearly the *producer support estimate*; the total monetary loss of (1) taxpayers in the form of subsidies and (2) consumers in the form of higher prices because of trade barriers. The results for EU citizens in 2009 was €87bn, making the average cost per person for upholding the CAP, in the

[7] The Single Payment Scheme is also known as Single Farm Payments.

year 2009, €187 (OECD, 2011). The total cost has been rather stable in the last years, but considering economic growth and the enlargement of the Union, the number has been falling quickly as a percentage of gross domestic products (chart 3). To put the numbers in context, the EU producer support estimate is very close to what is found in OECD countries on average, yet, some countries have shown greater falls in producer support estimate since the conclusion of the Uruguay Round Agreement (OECD, 2011).

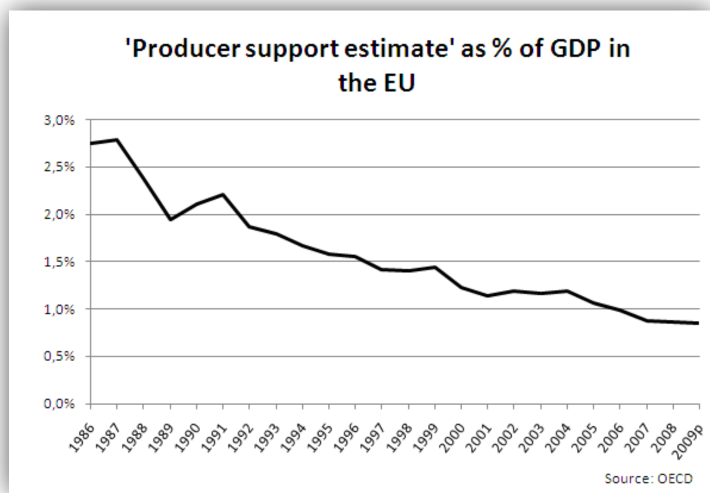


Chart 3: The OECD agriculture producer support estimate in the European Union has been declining when measured against GDP.

In 2009, CAPs main expenditures were: market interventions of €3.4bn, direct payments of €37.8bn, and rural development of €13.6bn (EUR-lex, 2009a). The average tariff on actual imports of agricultural goods in the EU were in 2004 22.9% (Jean, Josling, & Laborde, 2008). This number might however not be completely realistic, as it is based on what was actually imported, level of tariffs for agricultural products vary greatly, some even surpass 100%. A more recent number, for the year 2009, covering an average of all agricultural products is 13.5%, just as is allowed under the current regulations of the WTO. However animal products were tariffed on average by 23.2%, dairy products by 49.4%, and sugar and confectioneries by 27.5% (UNCTAD/WTO, 2010).

A simple overview can be obtained by organizing CAP activities using the WTO categorization system (explained in chapter 1.5). Agricultural support categorization is in three pillars: (1) market access, (2) export subsidies, and (3) domestic support.

1) The EU upholds 13.5% average value added tariffs on imports of agricultural products, matching the maximum limit allowed by the WTO (UNCTAD/WTO, 2010).

2) Total market interventions in 2009 were €3.4bn, of which €0.65bn went to export subsides (European Commission, 2010).

3) Domestic support takes what seems infinite forms, under different names and programs. Luckily, WTO categorizes domestic support into the three well defined “boxes”: The green box, the blue and the amber. Any kind of direct market intervention falls under the amber box, production-related direct payments are accepted in the blue box as they are associated with limits on production, while rural development and decoupled direct payments fall mostly under the green box. The chart below shows domestic support categorized by WTO boxes.

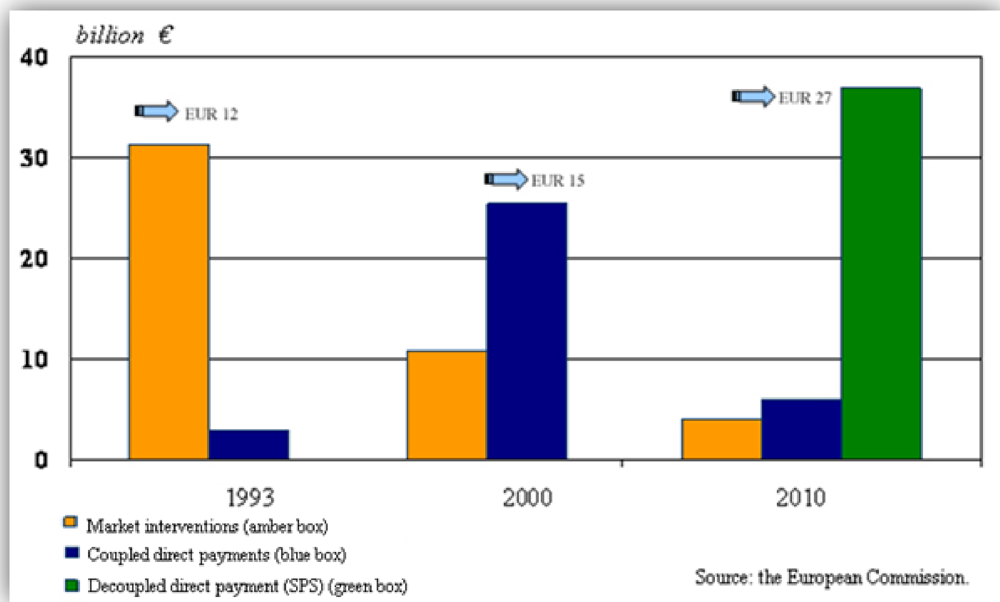


Chart 4: Cap money paid to producers in 2010 and earlier. The chart shows the movement of payments towards WTOs blue and green box. Coupled direct payments generally fall under blue box, and decoupled under green, while market measures are amber, most trade distorting.

A new issue concerning the CAP, although not directly, is the production of biofuels and the enthusiasm for them in the EU. In 2008, the European Parliament and Council agreed on the “Renewable Energy Directive”, which mandates that 10% of energy used for transport will be from renewable sources before the year 2020 in every member state (EUR-Lex, 2009b). The implementation is in the hands of each government, and they are obliged to find their own way to meet the goal. As a result, an increase in biofuel usage is to be expected, and crops used to produce them. In many member countries, tax exemption and special subsidies have already been seen, while imported biofuel from outside the Union faces tariffs. The move is thus likely to increase farmers’ income, and as well as and land prices (Josling, Blandford, & Earley, 2010).

2.3 Praise and criticism of the CAP

This subchapter will concentrate on presenting different opinions, from supporters, critics, academics and most importantly, political actors relevant to CAPs decision making. As for public view, it is worth bearing in mind that, according to public surveys done for the European Commission in 2009, a majority of EU citizens is in favor of “giving payments to farmers to help stabilize their income”, 39% answered to be "totally in favor” and 44% “somewhat in favor” (TNS Opinion & Social, 2010). It is still debatable how much weight public opinion carries, although direct elections to the European Parliament are held regularly in every member country, decision making process seems to stay mostly within Brussels and is somewhat isolated from the public. In 2007, only 9% of EU citizens reported knowing what the CAP was (see chart below). In 2009, the number was up to 13% from that we can draw the, scandalous or not, conclusion that 87% of Europeans do not know what the CAP is, although it represents almost a half of the European common budget.

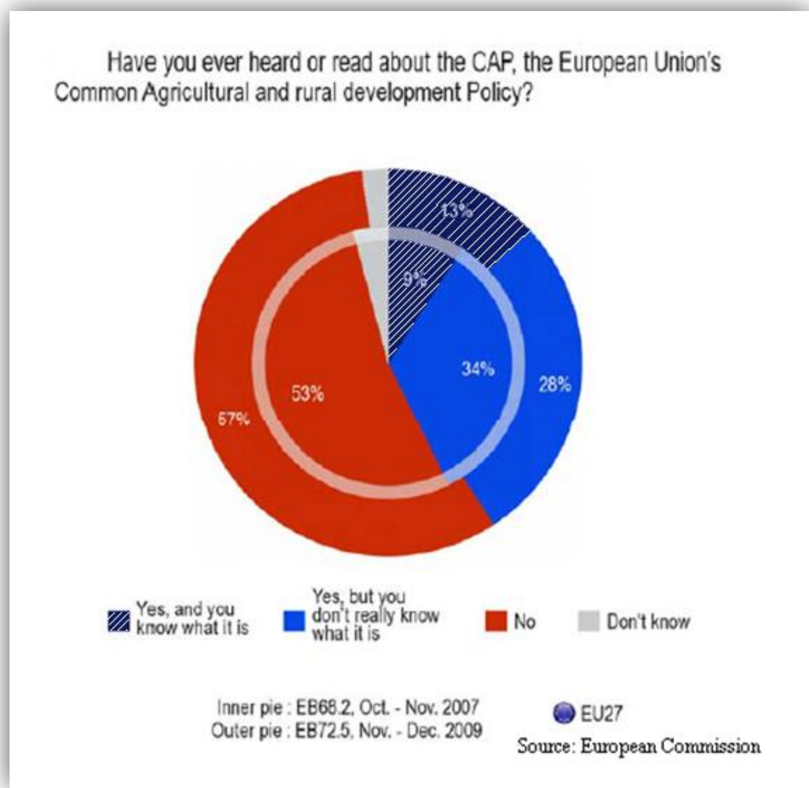


Chart 5: According to a recent survey, more than two thirds of EU citizens have never heard about the CAP, while only 13% know what it is.

In 2007, the government of Sweden was the first member country to suggest a complete elimination of farm protection and subsidies, except those related to the environment (The Local, 2007). All political parties in the Swedish Parliament are reported to support reform over the status quo, and generally argue that the environment should be the fundamental policy driver while based on a transparent and deregulated agricultural policy (CAP2020, 2008). A new Conservative-Liberal coalition government in the UK has been asking for cuts in the European Common Budget, where CAP represents almost a half. The government has been making painful government-budget cuts at home and believes EU funds should take similar cuts. Still, even before the change of governments, Britain had adopted a similar position to the Swedes, calling for a phase-out of all market price support and all direct payments to farmers by 2020 (Hall & Parker, 2009). Governments of the Netherlands, Denmark and Malta have positioned close to Sweden and UK, yet, out of the 27 states, a majority favors retaining the status quo (Zahrnt, 2011a). France historically has been the loudest guardian of the system, standing by the "keepers of the countryside", and trying to avoid a decline in production (Gordon, 2005).

Europe biggest farmers' organization Copa-Cogeca, in a communication on the future of CAP, asks for a simplification of the CAP and CAP requirements. They furthermore demand increased support due to price volatility, including export subsidies, at least at the time other countries are using export subsidies (Copa-Cogeca, 2010). There is no doubt few farmers would like there support to be cut, yet "what is good for farmers is not necessarily good for society as a whole" (Mankiw & Taylor, 2006, p. 102) The European Consumers' Organization (BEUC) raise the question why "common consumer rights" are missing, while producers are protected (EurActiv, 2011). They complain about high prices and tax burdens of the system and have stated that support should be slashed, so recent enlargement and international trade negotiations can be taken better advantage of (BEUC, 2002). Furthermore they demand that "the policy should be consumer-focused and not producer-driven" (BEUC, 2010).

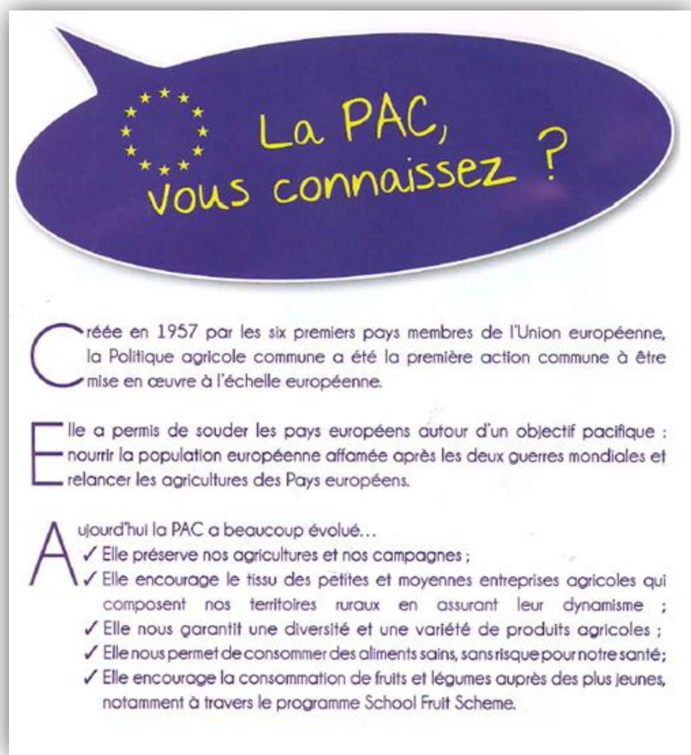
As we saw in last subchapter, the total costs of the CAP can be measured by adding up (1) the money paid out of the EU budget to uphold the program and (2) the cost of consumer due to higher food prices. According to OECD calculations, the cost in 2009 was €187 per capita, or a total of €87bn. Such monetary costs are relatively easy to measure and can be considered as a matter of fact. On the other hand, measuring the benefits and more subtle costs incurred by the CAP can be up to subjective judgment and is not always as clear-cut. People might have different premises of what the CAP should stand for. It is common to hear that the CAP is a successful policy but almost as common is to hear it is a straightforward waste of money. Is the CAP delivering public goods that otherwise would be lost? What are those public goods? Opinions differ.

A trained economist can easily understand the misallocation of resources and the deadweight loss caused by the CAP system. However, he would be radical if he did not consider government interventions a possibility under some circumstances. Some believe agriculture is not like other industries, and we have a duty to keep the cultural heritage inherent in traditional farming alive, even though it might mean inefficiency and higher costs. "Family farms—not industrial combines—are a public service: they produce quality food, unobtainable elsewhere. If these farms are allowed to disappear, so will this food" (King, 2005). Agricultural markets are believed by some to be different from other markets because farmers are more defenseless against price volatility "You can't just turn off a cow" (Chaffin, 2010). It is also argued that farmers are defenseless only because they are used to being protected in forms of guaranteed prices, but will learn to adapt in the long-run, like their counterparts in New Zealand did 30 years ago (BBC News, 2004). Brussels agricultural commissioner Dacian Ciolos, believes European farmers need to be compensated as they face higher quality standards than other industries in Europe, as well as their competitors in other parts of the world. The cross compliance standards are a burden for farmers for which they should be remunerated (Ciolos, 2011). Another view is that cooperation of CAP symbolically unites Europe which has an enormous value in itself. A CAP supporter seldom fails to highlight the food security it provides. A French economist accepts that there are certain gains from liberalization, nonetheless he argues that differences in comparative advantage between countries in most food production is hardly any. The gains of trade would therefore not be very high, while the cost to culture and security might be substantial (Boussard, 2002, p. 247).

The idea of *food security*, the availability and access to food, clearly seems to come out as the main driver behind expenditure on the CAP system and is central in every argument for a strong CAP. Strong CAP and agricultural tariffs guarantee production, which is good because it leads to food security. The European Commission along with many states has proposed food security to be the main theme of the post-2013 CAP reforms. In December 2009, 22 states signed the *Paris declaration* on the future of CAP, the countries included all EU member states except the five reform-minded: Sweden, UK, Netherlands, Denmark and Malta, that were not invited according to some sources but did not wish to join according to others. The declaration refers to food security:

"In the face of climate change, global political and food insecurity, the volatility of global market prices and the resurgence of health crises, only an ambitious, continent-wide policy with adequate resources can safeguard Europe's independence." (Paris declaration, 2009)

Researchers have found the argument of protecting EU agriculture for security reasons to be weak. There is not any foreseeable major decrease in production in Europe even though support would be gradually eliminated. They however remind that food in-security is a constant problem in many third world countries (BBC News, 2009). A study argues that the CAP might rather be contributing to long-term food insecurity in Europe by encouraging 'intensive farming' which damages the land. The bulk of food production is anyway dependant on imports of fossil fuels and therefore CAP could rather encourage real security by engaging in more international cooperation and encouraging open and stable trade systems (Zahrnt, 2011b). Yet, there is no reason to believe the idea will not continue to carry the CAP in the near future. The argument for food security somehow seems to surpass mere private interests. Possibly the importance put on food security has psychological roots. For instance, it might be a source of national pride to be self-sufficient when it comes to food.



Picture 1: The European Commission publicity for the CAP published in a Commission-financed brochure promoting healthy eating in France. "The CAP, do you know it?": "it preserves our agriculture and our countryside"; **"**it guarantees a diversity and variety of agricultural products". Not everyone would agree.

A declaration signed by a number of European agricultural economists (A Common Agricultural Policy for European Public Goods, 2009) and another one (For an Ambitious Reform of the Common Agricultural Policy, 2010) signed by over 40 agricultural economists (through the webpage reformthecap.com), both present a fairly similar idea of reform as presented by the government of Sweden. Think tanks and researchers have also come forth with comparable views.[8] The general view presented is that: Pillar 1 should be gradually abolished and politics of the second pillar should be seriously reassessed, and focused effectively on what are clearly public goods. All this will focus on greater market orientation, while sustainable land use must become the central objective of the CAP. More attention should be put on research to enhance productivity. Subsidies could still be considered if there is a clearly defined public-good purpose. However, for clearer accountability and more effective use, subsidies should be co-financed by member-countries and common funds. Rural poverty alleviation should hear under social policies rather than agricultural policies.

Although Sweden has been forthcoming and has received wide support, their view is still on the margin. The European Commission along with most countries stand firm in support of the current system although there is some criticism that has not been disregarded: unfair distribution of payments and lack of transparency are generally accepted problems. A project named *Farmsubsidy.org* aims at gathering and sharing information on exactly where each Euro is going out of the common funds, but in many countries the information is hard to get. A rule of the European Court of Justice made things harder, reaching the conclusion that providing such personal information is illegal (BBC News, 2010c).

Direct payments took more than two thirds of the CAP budget in 2009. As things are today, there is no upper limit on direct payments to farmers nor amounts received through the guaranteed price scheme. The CAP has been criticized for this, as an 80% of the direct payments go to 20% of farms (Thurston, 2005). Some of those farms are owned by big corporations and very rich individuals such as the Queen of England, which is estimated to have received over €8 millions in CAP payments (Farmsubsidy.org). Furthermore, it has been argued that subsidies often improve incomes of landowners more than the income of the actual farmers working the land. It has also been experienced that subsidies have been taken out of farms to fund other businesses (Grant, 2011). Another criticism of the payments, has been unequal distribution, depending on the states in which farmers lived. In 2010, farmers

[8] See for instance a study by the Social and Economic Council in the Netherlands (Sociaal-Economische Raad, 2008).

were reported to receive €560 per hectare in Greece to just €90 in Latvia (Financial Times, 2010). It is argued that the production within the Union can therefore not work according to comparative advantage.

A flat rate over Europe has been proposed but has been opposed due to different environments and unequal cost of living. Others have suggested a roof on CAP payments, but a reform in that direction was vetoed by ministers of Britain, where over 300 persons have been receiving over €300,000 on an annual basis. The argument against the roof is that big farms are equally important, as they provide jobs and efficiency and should thus not be discriminated (King, 2005). The negative publicity, with a number of newspapers quoting *Farmsubsidy.org*, has ensured that the issue has not been ignored: the man in charge; the current agricultural commissioner of the EU, Dacian Ciolos, has repeatedly proven he is aware: ”There will be a process of redistributing direct payments on the basis of objective criteria. Of course, a transition period will be needed to ensure that the changes do not fundamentally affect the balance that is currently in place in some agricultural sectors.” (Ciolos, 2010a).

Criticism towards the CAP has also been originated outside the Union; third world countries especially suitable for agriculture are losing out, having to deal with export subsidies and tariffs on import to the EU, the world’s biggest economy. It has also been stated that the CAP, by hurting the world economy, and especially poorer countries, are contributing to hunger (CAFOD, 2004). Studies have found tariffs and other market access barriers to be far more harmful to the world economy than subsidies, accounting to even more than 75% of welfare costs induced by agricultural market distortions (Anderson, Martin, & Valenzuela, 2006). Those are still not likely to be lowered unless for pressure from outside, as governors don’t have to pay it out of their own funds. Political actors such as the French farm minister Michel Barnier have said other areas in the world should build their own CAP to ensure food safety. Food markets should not be left to the mercy of market forces and France would be willing to share their positive experience of CAP (Hall, 2008).

Different negotiators have different views and interests. However it is clear that the CAP is an expensive deal, it is a huge state intervention in an otherwise liberalized market. The governments of both Sweden and the UK have come clearly forth with the view that interventionist policies should be left behind. While most other countries, especially countries such as France, Ireland and Poland have come in defense of the current system, highlighting food security concerns and that farmers should receive remunerations they deserve for giving public goods to society. Arguments of both sides for their case have been presented.

Interestingly, by simply comparing the numbers going in and out of the common funds, one sees that governments' viewpoints for or against the status quo generally coincides with their net-contribution to the common funds. France, the strongest defender of CAP is also one of the five biggest net-beneficiaries along with Spain, Poland, Greece and Romania. Governments criticizing the CAP generally depend much less on agriculture and are often net-contributors to the system. The biggest net-contributors in 2009 were: Germany, Belgium, Netherlands and the UK. The political debate might up to some degree be based on private interests rather than different perceptions of the common European good. The following chart shows what countries receive from the funds in proportion their contribution.

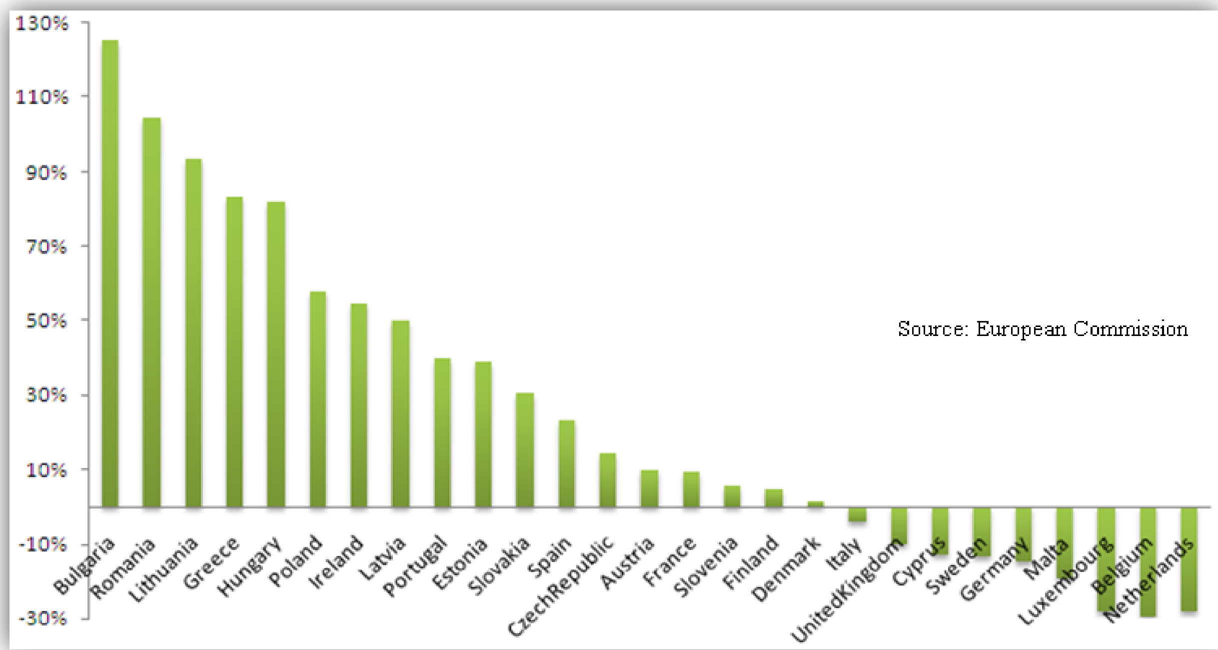


Chart 6: Countries CAP net-receipts in proportion to CAP contributions in 2009.[9]

[9] Calculated by deducting each country's CAP receipts from its CAP contribution, which is assumed to be the same percentage of its total payments to the EU budget as the CAP is of the total budget EU budget. The percentage in 2009 was 45,3%. The final number is calculated with the following formula: $\boldsymbol{{}^{receipts\,-\,contribution}\!/_{contribution}} \times \mathbf{100}$.

2.4 Future Reforms of the CAP

Currently underway is the work to define next multi-annual budget framework of the EU for the period 2014-2020. The role and limits of the EU's most expensive program, CAP, are being re-evaluated, along with other programs. The final decision making is up to a "three-level game" of governments that will take their stands firstly on national-level. Next they will have to negotiate with other national governments on a European-level, while past and future WTO agreements will limit their possibilities (Davis, 2003, p. 20). As things look, in the absence of a Doha agreement, an increase in subsidies is technically possible under the current WTO agreement (Josling, 2007). A major reform is nevertheless unlikely; countries are dealing with fiscal problems, making it hard to legitimize a budget increase. Still, there are not many signs of political will to make big cuts to the budget either. At the same time, probabilities are that the current CAP reform will be finished before the conclusion of a new WTO agreement (Bhagwati & Sutherland, 2011).

The European Commission, led by *commissioners* and a president from every member country, is the "designer and manager" of EU policies and is responsible for preparing a proposal for the future of the CAP (Peterson & Shackelton, 2006, p. 82). A final version of the proposal is expected to be presented in summer 2011 to the Council of Ministers and the European Parliament. The Commissioner for Agriculture and Rural Development since 2009 is Dacian Ciolos from Romania, a country highly dependant on agriculture; 47% of the population lives in rural areas and agriculture makes up 10.5% of GDP against an average of 2% in Europe (Earth Trends, 2007). Ciolos is responsible for defining a facilitating the reform process, and probably is the single person that is going to influence the CAP reform the most. His task, in consultations with Member States and stakeholders, is to develop a proposal for the future CAP.

An official beginning of the reform process took place in 2008, with a debate conference (*Reforming the Budget, Changing Europe*) organized by the European Commission, that brought together over 500 participants from across Europe (European Commission, 2008). In November 2010, The Commission published a communication on its vision of the CAP after 2013. The paper is considered a draft for a CAP legislative proposal that will be presented in summer 2011 to the European Parliament and the Council of Ministers, that are then responsible for carrying out the final deal. The communication, to a certain degree, defines and limits the scope of the post-2013 reform. The communication is not binding, but when already years of work have been done, a U-turn is unlikely (Zahrnt, 2011a). Apart from international pressure through WTO, the CAP has received criticism from wide sources and at least certain minimal reforms can be expected, Dacian Ciolos, has stated that CAP has to respond better to the expectations of the community or either the policy will lose its credibility (Ciolos, 2010b).

The consultation document argues for a strong agricultural policy and states that "goods provided by the agricultural sector cannot be adequately remunerated and regulated through the normal functioning of markets" (European Commission, 2010a). It defines the primarily role of European agriculture as supplying food. Judging from the paper it seems, the Commission wants to make sure that production will not decline and is maintained across the whole Union, however, without challenging international trade commitments. Secondary roles are defined as sustainable management of natural resources and development of rural communities. Furthermore the CAP should be there to address food security. The following reforms are proposed as "Option 1": with other things equal, it "should be considered" to give decoupled direct payments an upper ceiling. The distribution of direct payments between member states should be balanced and the cross compliance standards, needed to receive the payments, should be simplified. To make things more egalitarian, a price floor should also be put for payments per hectare, while the idea to pay all farmers across the Union an equal amount per hectare is rejected. The system should be simplified and payments have to focus more on active farmers, although a definition for an "active farmer" is not suggested.

Option 1 generally stands for a very mild reform. Options "2" and "3" are also presented. Option 2 would introduce slightly more reforms: reduce direct payments and increase focus on sustainability. The third represents the "radical" view associated with British liberalism and the government of Sweden: all market intervention should be abolished except those related to environmental management. However with the introduction and the objectives defined, it is clear that the Commission is siding with the first option.

On December 18, 2010, in a public letter addressed to José Barroso, the president of the European Commission, the heads of state of France, Germany, the UK, the Netherlands and Finland insist on budget discipline. They wrote that "payment appropriations should increase, at most, by no more than inflation over the next financial perspectives" (Letter to Barosso, 2010). The move is significant as France and Germany are the main contributors the Common budget. Especially as France traditionally has been the strongest defender of a big CAP, the fact that without much negotiations its government has accepted to not ask for an increased overall budget might come as surprise. France, not adopting an initial position with a bigger CAP, will make it harder for pro-CAP countries to defend from demands of a reduced budget.

In March 2011, an open letter to the Presidents of the European Commission and the European Council, was signed by nine prime ministers of the more reform orientated European countries: Britain, Netherlands, and the Scandinavian states, along with Poland, and the Baltic states. In the light of slow growth in the continent, the letter urged European leadership as well as other nations to commit to the Doha round for more liberalization of trade (Getting Europe Growing, 2011).

There is no doubt that the EU recognizes the primacy of international law, including those generated by the WTO, over European law (Davis, 2003, p. 63). When EU former trade commissioner Pascal Lamy addressed the European Parliament Agriculture Committee in 2000, he repeatedly referred to the need for the EU to bring policies into conformity with WTO rules from the Uruguay round agreement, at the time the EU had violated certain rules regarding trade of bananas. The demands of following WTO rules were not contradicted and about this time the largest reform of the CAP so far took place (Davis, 2003, p. 75). Last November's Commission communication states: "it is essential that EU agriculture maintains its production capacity and improves it while respecting EU commitments in international trade and Policy Coherence for Development.“ (European Commission, 2010a).

A Doha agreement might upset the way in which post-2013 is going. As a part of the Doha Round, the EU has offered to cut farm tariffs by close to 60%, and an altogether elimination of export subsidies, while the most trade distorting, "amber box", farm subsidies could be limited by 80% (European Commission, 2011). However, a study shows that the lowering of upper limits of the amber box won't affect CAPs domestic support, as it is has already been lowered far below the limits (ICTSD, 2011). Although some cast doubt on the "greenness" of the decoupled direct payments, and believe the EU will be challenged within the Dispute Settlement Body.[10]

Yet, a Doha round agreement would make the 2003 reforms of the EU irreversible (Bhagwati & Sutherland, 2011), moreover export subsidies would be eliminated and import tariffs will have to be lowered substantially. This will be a popular change with European consumers as well as non-European farmers. Offers are naturally set forward provisionally; they come with demand that for example US and Canada liberalize their agriculture to similar extent, and market access in other fields (Jean, Josling, & Laborde, 2008). None of the offers are likely to be realized without the conclusion of an overall Doha round agreement.

[10] See for example: (Grey, Clark, Shih and Associates, 2006) or (Matthews, 2010b).

Back to Europe: an economic crisis is shaking the boat. Still, as politics have been happening in Europe, an absence of progress in the Doha round, an evolution of CAP might be expected instead of a revolution. Anyway, it is widely believed that "the WTO remains the only place where agricultural subsidies can realistically be tackled" (Dadush & Nielson, 2007). In the international arena of the WTO, agricultural interests are harder to protect. It is thus possible, that even though defenders of the CAP might manage to ignore what is happening in the Doha round for now and keep a strong CAP for the next period, that in the revision for the post-2020 period, WTO agreements will force European politicians to listen more closely to Swedish proposals.

In Europe there have been five countries speaking out against the CAP but the other twenty-two, along with the European Commission generally support it. The Paris Declaration of 2009 clearly confirmed the support of the 22 countries (Paris declaration, 2009). There are until now no signs of weakness in support from beneficiaries countries such Ireland or any of the Eastern-European countries. Changes in governments might, of course, affect the pictures but the main elections in France and Spain are due in 2012 – ensuring in the meantime, along with great net-benefits, that these two important countries will stick to their defense of the CAP.

With continuing stagnation in international trade discussions of the Doha round a slight decrease in the budget of the CAP along with certain small reforms are to be expected.

Conclusion

The process of defining the CAP for the period 2014-2020 is most definitely going to change the CAP, at least in a minimal way. If a Doha Round agreement will be concluded in the next years, a profound change is to be expected.

Although agricultural subsidies have been on the decline in the EU, they are widely supported in most member-countries, both, in the political sphere and amongst the public. It is worth taking into account that the countries with the most net-benefits from the agricultural and rural development funds, are the strongest supporters of the system. However, an increase in subsidies is unlikely for the next period. Five member-countries have taken a stand against the protection of farmers provided by the CAP, while criticism from both inside and outside the EU is strong. At the same time, most European nations are going through times of an economic downturn and austerity measures. A common declaration of the three biggest economies of the EU (UK, Germany and France), states that the common EU budget should not be increased for the period 2014-2020. CAP represents close to half of the EU budget.

The European Commission is responsible, for preparing a legislative proposal on the post-2013 CAP. A final version is expected to be presented in summer 2011 for the European Parliament and the Council of Ministers, that then will takeover the responsibility of the reform-process. As the Commission has cooperated with EU institutions and relevant politicians from member-countries in the preparation, the proposal is not expected to undergo big changes. A draft version of the proposal was published by the Commission in the end of 2010. It recommends a few changes to the CAP, including: more even distribution between farmers in different member states. An upper and lower limit to payments is also suggested, at the benefit of smaller farms and the expense of the biggest. Payments and standards should be simplified and focused on the environment. Finally, the Commission articulates that strong protection is important to protect rural areas and avoid decreased production. The Paris declaration in 2009 confirmed the support of 22 out of 27 EU countries for the maintainance of a strong CAP. It is thus clear that the majority of political actors do not suggest any major changes. The future CAP can be expected to be very close to the actual system, with a slightly lower budget - unless the process will be upset by a new WTO agreement.

The International Organization WTO holds authority as the regulator of the regulatory actions of government policies. The Organization has 153 members, making up 97% of international trade. Member-countries are since 2001 negotiating a new agreement (in the Doha Round) on trade rules, covering a wide range of subjects. When the round is completed, the protection provided to farmers in the European Union will have to be decreased in several ways. Export subsidies will be eliminated and import tariffs lowered by 60%, while domestic subsidies might have to be lowered. Although generally EU governments are against cutting farm subsidies, they see other opportunities in the negotiations, such as decreased subsidies elsewhere and better market access for their exports. Most EU governments seem eager to conclude the deal. Yet, the negotiations have taken longer time than expected, and deadlines for the agreement have been violated several times. It is still unclear when a Doha Round agreement will be struck, though negotiations are reported to be advancing and an agreement might be reached in 2011 or 2012. A deal that soon, would completely upset the current reform process, and force most European politicians to reevaluate their ideas on the future of CAP.

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