

SEBASTIAN STĘPIEŃ  
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## Quo vadis Common Agricultural Policy of the European Union?<sup>1</sup>

### 1. Introduction

Agriculture generates too weak internal forces so that they can trigger the growth process and keep it in a state of dynamic equilibrium, so its development requires impulses from the outside, and otherwise exogenous stimuli. This means citing after Y. Hayami and V. W. Ruttan (1985) the need for the development induced in the sector. Agricultural policy plays the role of such a stimulator. The need to implement such a policy results from the fact that market participants do not fully flexibly adapt their activities to external conditions (legal, political, or economic), thus they do not achieve the maximization of their usefulness. Therefore, it is necessary to launch interventions at the state level, affecting the direction of the sector's development, in accordance with social and economic needs. According to O.E. Williamson and K.J Arrow freedom and independence, as well as customs and social habits are determined by institutions

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that direct behavior, imposing certain limitations on people (Williamson, 1991; Arrow, 1970). D. C. North by institutions, understands both customs and informal and formal habits that define the rules of behavior occurring in society, specify restrictions and shape the mutual interactions of entities on themselves, creating social, political and legal reality (North, 1990). In this context, the policy implemented through the institutions is associated with the setting of goals and desirable directions of development, which then, through specific instruments, enable achieving the desired result. In the European Union, such an institution is the Common Agricultural Policy (CAP) together with its instruments that create the development of agriculture in a socially desirable direction. The evolution of the CAP and changes in its instruments are a flagship example of the exemplification of the operation of institutions in the agricultural sector.

The aim of the study is to indicate the directions of reforms of the Common Agricultural Policy during its sixty-year functioning, the reasons for these changes and the consequences they have had for the agricultural sector in EU countries. These outcomes were supplemented by outlining the perspectives for the development of the EU agricultural policy in the coming years. The authors focused on the basic instruments for supporting the CAP with an income-generating, environmental and rural-related character.

## **2. Reorientation of support in the process of the evolution of the Common Agricultural Policy**

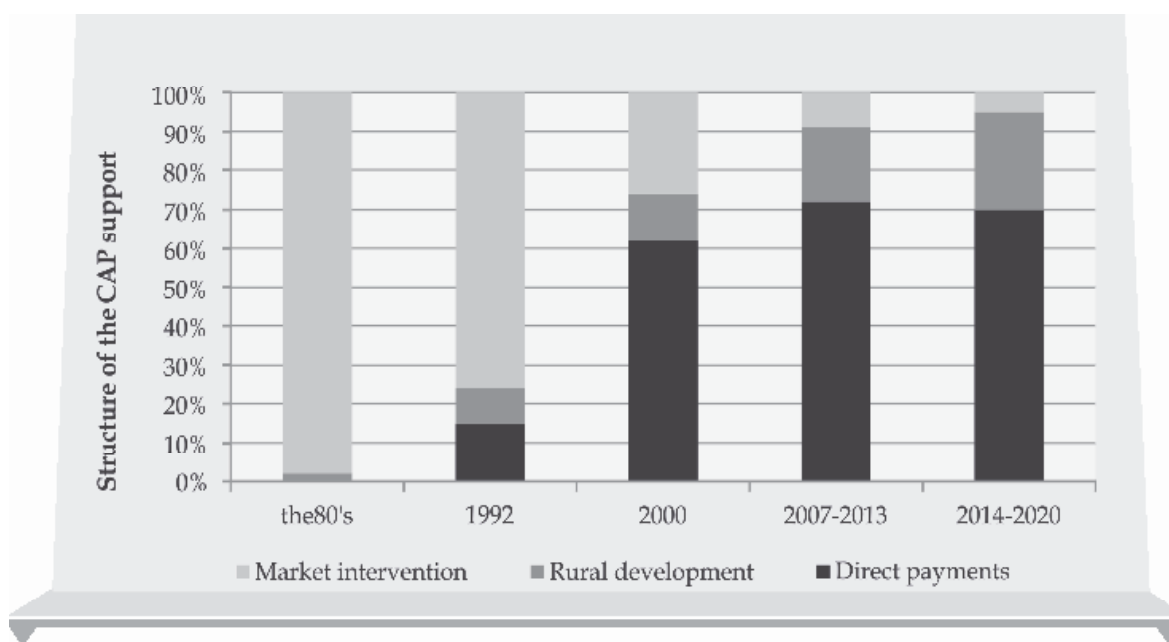
The Common Agricultural Policy of the European Union was introduced in the 1960s as the first sectoral policy. After the entry into force of the Treaty of Rome in 1957, individual agricultural policies of the Member States had to be replaced by intervention mechanisms at Community level. In the formal sense, the existing solutions taking into account domestic policies were inconsistent with the principle of free movement of goods and services in the area of six members of the European Economic Community of that time. At the same time, for strategic reasons, attempts were made to maintain public interventionism in the area of agriculture, which was the premise for creating a new system (Massot, 2019). It was based on the specificity of the agricultural sector, as strongly dependent on unpredictable weather conditions, characterized by low price and income elasticity of food demand, limited mobility of assets (including primarily land), relative long payback period and high risk, which leads to the inefficiency of the market mechanism (Czyżewski, 2007). An additional argument of the intervention was the reconstruction of the production potential after the

destruction caused by the Second World War in this period (Jambor and Harvey, 2010) and the creation of a balance of power between industrial Germany and agricultural France (Tangermann and von Cramon-Taubadel, 2013; European Commission, 2012). As a result, 5 CAP objectives were defined, which were to be the basis for its functioning (Burrell, 2009):

1. Increasing the productivity of agriculture through technical progress and optimal use of production factors, mainly work.
2. As a result, ensure a fair standard of living for the agricultural population, in particular by increasing wages (income).
3. Stabilization of agricultural markets.
4. Guaranteeing regular food supplies.
5. Ensuring rational food prices for consumers.

These objectives ~~have been~~ were confirmed in Article 33 of the Treaty on the Functioning of the European Union (2012), signed in Lisbon in 2007, although the internal and external conditions of the Community have changed significantly and despite the fact that they have been incoherent from the outset. The success in just a few years of improving the agriculture production output and increasing the supply of food (objectives 1 and 4) was a success, with growing farm incomes (objective 2). The alternative cost of the intervention measures, mainly involving the regulated purchase of agricultural raw materials at a fixed price, was the relatively high price of food and excess supply in the sectors covered by support (milk, butter, cereals), with a large import of other products. Two of the above-mentioned objectives (3 and 5) were therefore not achieved. This was the reason for the reforms that were undertaken in subsequent periods.

The external effects of interventions and growing integration within the European Union as well as with the global economy have changed the point of view of the role of the Common Agricultural Policy. The initial idea of a self-sufficient region for the diversification of supplies within the global market has become outdated. The preferences of Europeans regarding the consumption of food, also from outside the Member States, have changed (Boulangier and Messerlin, 2010). Bilateral trade exchanges provided greater guarantees of stabilization of supply than the internal market, exposed to shocks. The new direction was also marked by negotiations on tariffs and trade at the WTO forum (General Agreement on Tariffs and Trade - GATT). Keeping relatively high prices of agricultural products and restrictions on trade could no longer be sanctioned. The answer to the incorrectly designed policy was to change the mechanisms of the CAP and adapt them to new conditions. After the first 30 years of operation, there was a reorientation of the policy with the market-price policy



**Figure 1. Evolution of support system of the Common Agricultural Policy**

Source: European Commission 2013

towards income and structural policy, and later also environmental. Introduced in 1992, EU Commissioner MacSharry reform abolished import tariffs, lowered price support and withdrew production quotas, and in their place introduced direct payments (originally defined as compensatory and related to the size and structure of agricultural production) and instruments focused on rural development (compare figure 1). Further two reforms - Agenda 2000 from 1999 and Fischler from 2003 - continued the reduction of market support, increasing the share of the budget for direct payments (attributed to the first pillar of the CAP, from 2005 increasingly decoupled from production<sup>2</sup>) and rural areas (Pillar II of the CAP). There were also activities for the natural environment (e.g. afforestation, agri-environmental payments, organic farms) (Marcinkowska et al., 2011; Greer, 2013; OECD, 2011). The solutions adopted for 2014-2020 support most of the earlier mechanisms, putting even more emphasis on environmental

2 The abandonment of linking support under direct payments with the volume and structure of production was aimed at increasing the flexibility of an agricultural holding in terms of choosing the type of production and following market signals. It was also the result of excessive production of those agricultural goods for which the highest support was granted.

goals. Today's priorities can be divided into three areas - income (see goals 1-3, table 1), environment (goals 4-6), rural population (goal 7). In conclusion, the current shape of the CAP exposes the multifunctionality of the agricultural sector - in addition to food production, it contributes to the attainment of social goals and provides environmental public goods (Matthews, 2013). There has been a reorientation of budget expenditures from those aimed at a continuous increase in productivity of production factors through high food prices to those that directly form the farmer's income, while at the same time taking care of the development of rural areas and nature. Thus, the scope of impact of today's EU agricultural policy is wider than assumed in the treaty objectives, hence it is necessary to revise these assumptions and adapt them to the current conditions and expectations.

**Table 1. Reorientation of the objectives of the Common Agricultural Policy**

Primary objectives	Current objectives
1. Increase in the agriculture productivity through technical progress and optimal use of production factors, mainly labor	1. Maintaining the stability of agricultural markets and risk management
2. As a result, ensure a fair standard of living for the agricultural population, in particular by increasing wages (income)	2. Strengthening agricultural income
3. Stabilization of agricultural markets	3. Increasing the competitiveness and innovation of agriculture
4. Guaranteeing regular food supplies	4. Provision of environmental public goods
5. Ensuring rational food prices for consumers	5. Mitigation of the effects of climate change
	6. Preservation of biodiversity
	7. Promotion of economic and social development of rural areas

**Source:** own performance on the basis of Traktat o funkcjonowaniu Unii Europejskiej 2012

Looking at the original objectives of the common agricultural policy in retrospect, it can be assumed that some of them were implemented. The productivity of EU agriculture has increased, the situation on agricultural markets is relatively stable, and food is available at lower real prices. In this context, almost 60 years of CAP functioning can be assessed positively. However, although the directions and instruments of support have changed, the analyzed policy still remains ineffective in solving certain important structural problems. First of all, it mainly supports big, large-area farms. About 80% of direct payments go to less than 20% of entities, which deepens the income gap

between small and large producers (Bournaris and Manos, 2012; Matthews, 2019). In this way, the concentration of land is promoted in the hands of a small group of beneficiaries of subsidies. Meanwhile, money should flow more to small and medium-sized farms, in accordance with the assumption of fair distribution and in line with the idea of maintaining the traditional character of food production. Secondly, the problem of agriculture income deprivation in relation to its surroundings is still present, especially visible for small-scale farms (Czyżewski and Poczta-Wajda, 2016). Despite transfers under the CAP, the distance of agricultural income to wages and salaries in the national economy remains high. On average, in the years 2005-2015, the ratio was 62% for the EU-28 countries<sup>3</sup>. The source of this deprivation is the inefficient allocation of value added in the food supply chain. It is partially intercepted by buyers, processors, sellers and, ultimately, consumers themselves. The farmer himself, to an inadequate degree, participates in the process of shaping the intermediate and final demand due to the lack of internalisation, i.e. taking into account many costs (e.g. maintaining the natural environment's well-being) and the lack of payment for public goods (Czyżewski and Stępień, 2017). Thirdly, existing environmental instruments do not guarantee the implementation of ecological goals that have been set for agriculture. Particularly strong criticism is subjected to the so-called "greening"<sup>4</sup> existing within the system of direct payments. The European Court of Auditors (2017) in a special report states that this element has no measurable impact on the environment, its assumptions are not ambitious, and thus the expenses for this purpose are unjustified. In fact, the requirements of the "green" component cover only approx. 5% of farms, above a certain area of arable land, for others they are the same form of income support as basic payments. Similar conclusions includes the development of the German Ministry of Agriculture (Wissenschaftlicher Beirat für Agrarpolitik, 2018) and BirdLife Europe organization (Pe'er et al., 2017). It is stated that the adopted solutions are obligatory for beneficiaries of support and do not go beyond the accepted standards, thus they do not motivate to take additional actions for the

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3 Authors calculations based on the FADN agricultural accounting database (2019) and the Eurostat database (2019).

4 The greening of direct payments means that the farm must meet certain environmental requirements as a condition for obtaining a part (30%) of the payment per hectare. These requirements are related to the exclusion of part of agricultural land from cultivation, crop diversification and maintenance of permanent grassland. Greening is a mandatory component of the new direct payment system that has been implemented since 2015.

benefit of the natural environment. It can be assumed that from a political point of view their implementation was supposed to be a kind of alibi for transfers of budgetary funds for agriculture. Finally, fourthly, EU agricultural policy has not solved the problem of the aging EU farmers' population. The functioning aid mechanisms have proved to be ineffective and do not encourage young agricultural producers to remain in the countryside. As a result, 56% of farmers are people over 55 (including 31% over 65), and only 21% under the age of 45 (including 6% below 35 years of age) (European Commission, 2017a).

### 3. Beyond 2020 - the future of the EU agricultural policy

On June 1, 2018, the European Commission (2018) presented a package of legislative solutions for the common agricultural policy after 2020. The overall message was to make the CAP more sensitive to current and future challenges related to climate change, care for food quality and safety, rural vitality, generational renewal, while maintaining support for competitiveness and sustainability of agriculture. The document presented by the Commission was the result of months of negotiations based on the formula of open public debate. In total, over 320,000 observations, opinions and comments have been collected that reflect the positions of various social groups (European Commission, 2017b). Due to diverging interests, it is impossible to indicate one direction of change preferred by all participants in the discussion. There are different priorities of farms - increasing income support, rather than all EU citizens or social organizations - environmentally sustainable agriculture, quality and food safety. There are also different visions of agricultural policy among individual Member States, depending on the level of economic development and financing of the EU budget - the beneficiary of support vs the net payer<sup>5</sup>. Therefore, the final result is the result of a broad compromise, developed by most countries (European Commission, 2018) and is a response to the challenges and objections posed to the current CAP<sup>6</sup>. The previous 2013 reform has also been taken into account, where the starting point was the establishment of a common budgetary framework. The approach "first budget, then solutions" stiffened the negotiation

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5 In 2017, the largest beneficiaries of the CAP were: Poland, Spain, Romania, Greece and Hungary, and the largest net contributors - Germany, the United Kingdom, the Netherlands, Italy and Belgium (European Commission - Directorate-General for Budget, 2017).

6 57% of all persons participating in public consultations said that the current CAP mechanisms operate only to a limited extent.

parties and contributed to maintaining the status quo or minimizing changes for a large part of the mechanisms (regarding, for example, environmental requirements) (Heinemann<sup>2017</sup>). Meanwhile, the conditions for the functioning of the common agricultural policy have changed. Nominal and real prices of agricultural products fell<sup>7</sup>, the EU undertook new international commitments in the field of climate change mitigation (e.g. as part of the United Nations Conference of Paris 2015 - COP21), there was a need to shift to fully sustainable agriculture and rural areas, guaranteeing environmental and social public goods and opportunities for social inclusion have increased the importance of new technologies and areas such as the bio-economy, renewable energy, the circular economy and the digital economy.

Taking the above into consideration, the proposed reform of the common agricultural policy after 2020 can be assessed. According to the assumptions, it is supposed to be a more effective and equitable policy for the redistribution of funds (especially under direct payments), more ambitious in the use of natural resources, environmentally friendly and climate, aimed at the problems of generational change and socio-economic development of rural areas, emphasizing the importance of research and innovation, especially in the context of agricultural competitiveness and risk management. For greater efficiency and simplification, it is postulated to strengthen the principle of subsidiarity and responsibility for Member States at the level of setting specific objectives and solutions (European Commission, 2017a).

The main profit-making instrument of the future CAP is to remain direct payments. Therefore, the need to continue them should be well justified, especially since the system costs are relatively high. In 2014-2020, their budget amounts to over EUR 40 billion per year, i.e. about 70% of the expenditure of the common agricultural policy and almost 30% of the total expenditure of the European Union (Heinemann, 2017). In the 2021-2027 perspective, annual average is to be almost EUR 38 billion. The data also shows that in 21 EU countries farm incomes, after taking into account the subsidies, exceed the so-called low level of wages in the national economy<sup>8</sup>. This means that supporting farms through the national social welfare system to the threshold of low wages for 21 countries

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7 In nominal terms, the FAO food price index decreased in 2011-2018 from 230 to 168, at constant prices from 170 to 135 (FAO, 2019).

8 According to the OECD methodology, low wages are below the 2/3 limit of median average wages in the national economy and should form the basis for determining the threshold for social assistance (OECD, 2019).



would be cheaper than subsidizing them under the direct payments system. Such data may be a weapon for supporters of liquidation of income support, their re-nationalization or co-financing. This would be particularly disadvantageous for less affluent countries, mainly new Member States, which have never reached the level of agricultural financing in Western Europe and have not made up the gap in the productivity and profitability of the agricultural sector. Hence, the proposal to increase the redistribution of support towards small and medium-sized farms, as well as the introduction of degressivity and an upper limit on payments for large entities, as well as the orientation of transfers to "active" farmers, can be welcomed. The argument about the interception of money by large-scale agricultural entrepreneurs (or even only land tenants) is precipitated by opponents of direct payments. In addition, such targeting of support for the needs of small family farms can contribute to maintaining jobs throughout the area, and thus to strengthening the socio-economic structure of the country. It is a pity, however, that in the new period there will be no offsetting of subsidies between countries, even in the case of the part which is to be related to environmental actions. While the differentiation of the basic rate related to running agricultural activity can be justified by the costs of production (or life) in a given region, the maintenance of other rates for the implementation of the same nature functions seems unfair.

The weakness of previous solutions in the field of direct payments was the lack of motivation of the farmer to undertake actions for the benefit of the natural environment, climate or animal welfare that went beyond the general requirements adopted at EU level. Hence the creation of obligatory special eco-programs by Member States at the level of their strategic plans, as part of a special fund from the first pillar of the CAP. This is to be a voluntary payment for a farmer in the form of an incentive, received for providing defined public goods through the use of environmentally friendly agricultural practices or for refraining from negative nature-related activities (in this sense treated as compensation for the costs of lost profits). Each country would be able to flexibly set its priorities, adapted to local conditions. It is also assumed to leave separate support for agri-environmental-climate programs in the second pillar of the CAP. In total, a minimum of 40% of the national envelope is to be allocated for the aforementioned goals, ie by 10% more than in 2014-2020 (Hogan, 2018). If this money is spent on ambitious goals, without increasing administrative burdens for the farmers, and the actions will break through to public opinion, the legitimization of budget expenditures on the common agricultural policy will increase.

In the framework of rural development programs, the European Commission offers even greater flexibility in planning specific objectives and tasks, but with a higher than before level of national co-financing of some programs, which is the result of CAP budget reduction in the next financial perspective - about 5% from 408 billion in the period 2014-2020 to EUR 365 billion in 2021-2027 (in current prices). The use of external financing mechanisms does not seem to be a good solution considering the farmers' aversion to this type of commitments, and in recent years growing debt, also resulting from the need to participate in the costs of previous investment programs. Therefore, within the lower budget, the most important goals should be defined and specific solutions should be adapted to them. In addition to the mandatory allocation for environmental activities, one of the most important tasks is to determine the priorities for the direction of investment. It seems that the current financing for the purchase of machinery, equipment and farm modernization should be orientated to those activities that use innovations related to computer-assisted precision agriculture, digital technology, clean energy. In addition, measures that increase the farmer's bargaining power in the food supply chain should be supported through the development of short supply chains, local and direct sales, industry organizations and producer groups. With the increasing volatility of prices on the global market and the increase in the frequency and intensity of extreme weather events, it is legitimate (and not optional) to finance risk management mechanisms, for example mutual fund investments. Finally, from the point of view of generational change in rural areas, it will be crucial to create programs for young farmers, eg motivating to launch start-ups in innovative fields. An interesting idea is to include agricultural producers in Erasmus international exchange.

#### **4. Conclusions**

The Treaty on European Union (formerly EEC) has been changed many times since 1957, but the objectives of the common agricultural policy are as it was six decades earlier. Meanwhile, agriculture and its surroundings have changed, priorities and social expectations have changed, and the paradigm of economic development has changed. If budget expenditure on agricultural policy is to be legitimized, the Treaty objectives should be revised first. They must be supplemented above all with those activities that are currently addressed to agriculture. It is about more responsibility for the natural environment and climate, while maintaining the traditional role of farms, acting as a food supplier

and a wide range of public goods. In the latter case, it is necessary to evaluate this type of goods and create a payment catalog for various types of practices. Guarantee of supply of agricultural products at reasonable prices has long been realized, it is time to replace it with a guarantee of fair distribution of added value in the supply chain, which means including agriculture in the process of distributing economic surplus (e.g. through the development of industry and production organizations, creating a local sales system, facilitating direct sales). Maintaining farm income support should be a priority under the conditions of specific features of the agricultural sector and be treated as a kind of remuneration for the implementation of non-standard activities related to nature conservation. Fair and decent standard of living of agricultural producers, included in the treaty objectives, can be achieved not only through the increase in productivity, but also through the implementation of these tasks. At the same time, "fair" means a progressive redistribution of payments to small and medium-sized entities, both at the level of an individual country and between countries. Although the direction of the next reform is coincident with this approach, the dependence between the size of the farm and its support will still be visible. From the point of view of rural areas, special attention should be paid to the issue of depopulation and lower economic development than in urban areas. The programs intended for young farmers, support for small-scale farms or entrepreneurial activities, especially in innovative areas of the food economy, should serve this purpose. The above-mentioned goals are to be implemented in a flexible way for EU countries, which should be evaluated favorably. Different regional conditions (geographical, natural, institutional, etc.) and various expectations of the local community are the premise for designing and implementing tasks at the lower level, but within one, shared and fairly divided EU budget. The European Commission should also guarantee compliance with the principles of fair competition and respect for the law.

Finally, it is worth adding that the role of the agricultural sector will in the future evolve towards the implementation of new, wider than before functions, in accordance with the concept of sustainable development. In addition to the environmental activities described above, the production of clean energy and bio-economy products, the contribution of agriculture to the sustainable food supply chain related to food safety and quality will be important. Agriculture can also play a significant role in promoting healthier nutrition and reducing obesity and wastefulness on the one hand and malnutrition on the other. In this context, it may be worth considering renaming the Common Agricultural Policy to a *Common Food and Environmental Policy*.

## Summary

### **Quo vadis Common Agricultural Policy of the European Union?**

The agricultural policy of the European Union - Common Agricultural Policy (CAP) - was introduced in the 1960s as the first EU policy. Over the next decades it constituted the largest share in the expenditure of the EU budget. Today, although cohesion policy has replaced it in the first place, it is still being prioritized by the countries of the Community. Observation of the next financial perspectives, however, allows to conclude that the nature of the CAP is changing, which is a manifestation of the evolution of views on the role of the food sector in the economic development of the European Union. The aim of the study is to indicate the directions of reforms of the Common Agricultural Policy during its sixty-year functioning, the reasons for these changes and the consequences they have had for the agricultural sector in EU countries. These outcomes were supplemented by outlining the perspectives for the development of the EU agricultural policy in the coming years. The authors focused on the basic instruments of the CAP including income-generating, environmental and rural development-related. On the basis of the analysis of objectives and instruments of the CAP, it was stated that it departed from traditional market support to create more sophisticated intervention related to the changing macroeconomic conditions and expectations of the society. The paper is a review, with elements of meta-analysis, deduction and inductive reasoning.

**Key words:** *agricultural policy, sustainable development, reforms, European Union.*

## Streszczenie

### **Dokąd zmierzasz wspólna polityka rolna Unii Europejskiej?**

Polityka rolna Unii Europejskiej - wspólna polityka rolna (WPR) - została wprowadzona w latach 60. XX wieku i była pierwszą wspólnotową polityką UE. Przez kolejne dekady stanowiła największy udział w wydatkach budżetu unijnego. Dzisiaj, choć ustąpiła miejsce polityce spójności, jest nadal traktowana priorytetowo przez kraje Wspólnoty. Obserwacja kolejnych perspektyw finansowych pozwala jednak wnioskować, iż zmienia się charakter WPR, co jest przejawem ewolucji poglądów

na temat roli sektora żywnościowego w rozwoju gospodarczym Unii Europejskiej. Celem opracowania jest wskazanie kierunków reform wspólnej polityki rolnej w okresie jej sześćdziesięcioletniego funkcjonowania, przyczyn tych zmian i konsekwencji, jakie niosły dla sektora rolnego w krajach UE. Wywody te zostały uzupełnione nakreśleniem perspektyw rozwoju unijnej polityki rolnej w kolejnych latach. Autorzy skupili się na podstawowych instrumentach wsparcia WPR o charakterze dochodotwórczym, środowiskowym i związanych z rozwojem obszarów wiejskich. Na podstawie analizy celów i instrumentów unijnej polityki rolnej stwierdzono, iż odchodzi ona od tradycyjnego wsparcia rynkowego na rzecz tworzenia bardziej wysublimowanych narzędzi interwencji, powiązanych ze zmieniającymi się uwarunkowaniami makroekonomicznymi i oczekiwaniami społeczeństwa. Referat ma charakter przeglądowy, z elementami metaanalizy, wnioskowania dedukcyjnego i indukcyjnego.

#### Słowa

**kluczowe:** *polityka rolna, rozwój zrównoważony, reformy, Unia Europejska.*

#### JEL

**classification:** Q10, Q18, Q01, Q5

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