Research on the EU Direct payment schemes
2003 CAP reform:
Key findings and Research Issues

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ERS Workshop on “Modelling Decoupling”

Washington October 4-5, 2004

European Commission - Agriculture Directorate-General
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Main objectives of CAP reform

- More competitive agricultural sector through reformed market organisations (notably dairy, cereals, rice sectors)
- More sustainable, market-oriented agriculture through introduction of single farm payments combined with cross-compliance and good agricultural and environmental practices
- Reinforced Rural Development policy (broader scope and additional financial support)
- Financial discipline (ceiling on farm budget)
Methodological approach

Models

• Recursive dynamic partial equilibrium models

Main assumptions

• Uruguay Round Agreement on Agriculture maintained constant
• Favourable, though moderate world agricultural market outlook
• Modest EU economic and population growth
• $/euro Exchange rate stable at 1.1 over the medium-term
Modelling of decoupling

- Decoupling – key element in CAP reform to move towards more market oriented policy and less production & trade distortion
- Effect of policy measures: Static effect, Dynamic effect, Risk-related effect (insurance and wealth effect)
- DG AGRI analyses based on assumption on static effect - decoupled payments are lump sum transfers with no impact on production decisions (vs. FAPRI 30 % of previous DP and OECD 0.06-0.1)
- Cross compliance and good agricultural conditions – producer risk aversion could influence degree of decoupling
- Implementation of decoupling option: 66 % of animal premia and 90 % of arable crop payments decoupled over the medium-term (EU-15) and 90% decoupling EU-25
Enlargement – general situation in the EU-10

– Economic growth stimulated by structural change supported by structural funds, rural development

– Sustaining high growth rates through flexible labour markets, strong FDI and domestic consumption should reduce the income gap with EU-15;

– Agricultural sector abundant of labour, scarce capital, and low productivity
  • 14.4% labour employment (4.2% EU-15) but similar GDP contribution
  • duality of agriculture (subsistence vs. market-oriented)
  • structural change and competitiveness depends largely on developments outside agriculture
Restructuring of agriculture in the EU-10 facilitated by EU funds:

– economic growth will contribute to create alternative income outside agriculture;

– more investment in agriculture due to

  • improving market and income situation (single market, decoupled direct payments)
  • improving rural infrastructure and banking systems
  • specific instruments facilitating restructuring in rural development programmes available
Driving factors of EU-25 agricultural markets

- EU-10: High income growth leads to growing markets for meat, fruits and vegetables as well as fresh milk products and cheese in the EU-10

- EU-15: High consumer income, limited expansion of quantities, strong demand for quality and niche products

- World markets developments will become an increasingly decisive factor for market outlook

- Restructuring of agriculture and the food industries in order to better address demand
CAP reform: more pronounced increase in land set-aside and slight further decline in EU-15 arable crops area

Changes in arable crop allocation in 2010 (in % deviation from Agenda 2000)

- Cereals: -0.9%
- Oilseeds: -1.0%
- Voluntary set-aside: 19.7%
- Rice: -10.2%
- Silage: -5.5%
- Common wheat: 0.4%
- Durum wheat: -5.5%

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CAP reform: slight decline in EU-15 arable crop area

Arable crop allocation, 2002 - 2010 (mio ha)

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CAP reform: limited build up in EU-15 cereal stocks

Total public stocks, 2002 - 2010 (mio t)

Public stocks

Agenda 2000

CAP Reform

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CAP reform: rapid improvement for EU-15 rice market

Production, consumption and total stocks, 1990 - 2010 (mio t)

- CAP reform
- Agenda 2000

Consumption and production

Total stocks

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CAP reform leads to reduction in EU-15 beef production potential

Changes in cow number, 2003 – 2010
(in % deviation from Agenda 2000)

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EU-15 beef demand to exceed production over the medium-term
Impact of CAP reform dependent from the degree of decoupling

Changes in production and prices/stocks for beef and cereals, in 2010 (in % deviation from Agenda 2000)

- Minimum decoupling
- Central assumption
- Maximum decoupling

- Beef
- Cereals

Production
Prices
Production
Stocks

-0.8%  -1.9%  -3.0%  2.8%  6.0%  8.9%
-0.4%  -0.6%  -0.9%  0.6%  -9.5%  -15.7%
CAP reform: favourable impact on EU-15 pork and poultry sectors

Pork and poultry production & price changes, 2010
(in % deviation from Agenda 2000)

- Pork: 2.30%
- Poultry: 0.60%
CAP reform would secure income gains for new Member States

Income in 2010, real terms (2002 = 100)

EU-25
New Member States

Agenda 2000
CAP reform
• Improvement in the balance of agricultural markets through the reduction in EU production without jeopardising production potential
  – Notably for sectors influenced before by high support and more coupled instruments (beef, sheep)
  – the balance of agricultural markets in an enlarged EU would improve significantly
  – significant improvement in the structural balance of the rice and rye sectors

• Agricultural income little affected
### Enlargement

- Competitiveness (cost, quality) will increasingly allocate production
  - Old MS competitive in pork, high-value dairy products, certain fruit & vegetables, food industries
  - New MS competitive in poultry, (feed) cereals, certain fruit & vegetables
  - Dynamic concept (market orientation, production standards, investment)

### Adjustment

- Rural development (EU-25) and structural funds (EU-10) help facilitate adjustments to policy changes
More information available at ...

- http://europa.eu.int/comm/agriculture/publi/index_en.htm
Research issues 1/6

• Treatment of decoupled direct payments based on assumptions
  – DG AGRI lump sum, no effect of decoupled part
  – OECD 6% effect
  – FAPRI 30% effect on production

• Analyses largely with traditional PE models
Research issues 2/6

Future issues

- Understanding the dynamics on factor markets (Land, Labour, Capital)
  - Land markets should be included in PE models
    - Institutional settings (rules very different across EU)
    - Active farmers depend on renting land (high rents throughout EU)
Future issues

• Other dynamic effects on EU agriculture
  – Increasing risks on markets vs. better income transfer efficiency of decoupled direct payments;
  – Rural development measures in the new Member States
  – Future policy development:
    • What happens if direct payments are nominally decreased through financial discipline measures?
    • Future CAP developments regarding direct payments?
  – Does the amount of direct payments matter and if, how much?
Research issues 4/6

EC funded research projects

• IDEMA
  – The impact of Decoupling and Modulation in the Enlarged Union: A sectoral and farm level assessment

http://www.sli.lu.se/eng/idema/

Farm surveys, dynamic farm based regional modelling, sector analyses including factor markets
EC funded research projects

Research issues 5/6

- GENEDEC
  - Farm level analyses
  http://www.grignon.inra.fr/economie-publique/genedec/eng/
Analyses of institutional settings for factors markets across the EU