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DOCUMENT ON U.S. VIEWS OF CAP

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Several high-level meetings have taken place over the last few months between the United States and the European Community. As the EC knows from discussions at those meetings the U.S. continues to be concerned about the problems created by the European Community in its implementation of the Common Agricultural Policy.

We recognize the policy prerogatives of the European Community to pursue the satisfaction of internal objectives for its agricultural sector. However, when the implementation of EC governmental policy in pursuit of those objectives becomes detrimental to the well being of U.S. farmers, it becomes imperative that the U.S. government act to protect the interests of U.S. agriculture. Such has become the case.

The economist, Adam Smith, in the late 18th century documented the advantages of free and unfettered markets and the merit of a laissez-faire approach to those markets by governments. And David Ricardo, in the early 19th century, argued for free trade and against the British Corn Laws, a trade restrictive measure not unlike the modern variable levy mechanism of the CAP.

Over the last 1 1/2 decades the U.S. has made great strides in moving Government Agricultural policy away from interference with the market. Today our domestic prices and world market prices are the same for most major agriculture commodities. For the most part our agricultural sector adjusts fully and freely to the international market. The EC, as the other major agricultural trader in the world today, is fully insulated from the international market. And that causes the U.S. severe problems.

The following evidence has been compiled showing how EC policy actions have been harmful to the agricultural producers of the U.S. and those of a number of other countries around the globe. We also suggest some remedial actions we believe necessary by the EC to show good faith in proceeding toward an acceptable solution to our problems.

Our concerns about the effects of the way the CAP has been implemented center in three areas -

1. the stifling of EC internal demand for food products.

2. EC subsidized competition with us and other exporters in third markets, and

3. the added instability that the EC transmits into the world markets by maintaining rigidly stable internal prices and thus insulating member countries from the adjustments signaled by the international market.

Internal Demand. Several analyses are available that show the effects of the CAP on EC food demand. For example:

-- A 1968 USDA study covering the grains, livestock, dairy and sugar products estimates the EC consumer cost of the CAP in that year to be $6.4 billion.

-- A partial update of that study for 1978 shows the EC consumer cost of the CAP for just 4 grains (soft wheat, durum, barley, rice) and sugar to be $3.7 billion dollars.

-- A recent World Bank study shows the net social loss from misallocation of resources due to CAP price distortions in wheat, corn, barley, sugar and beef in France, Germany, and the UK to total as high as $1.4 billion. The welfare transfers from consumers to producers was estimated as high as $6.7 billion.

-- Per capita consumption levels of various food products are enlightening. In 1978 the U.S. per capita consumption of meat was 29.5 kilograms greater, than that in the EC; of dairy products 10 kilograms greater and of cereal products 19 kilograms less. Per capita beef consumption in the EC at 25 kilograms is 1 kilogram less than in the USSR. The average U.S. consumer spent 16% of income on food while the EC consumer spent from a low of 22% of income on food in the Netherlands to a high of 45% in Ireland.

The point is that the high agricultural prices within the EC have stifled consumer demand for food. We estimate that if EC agricultural prices were at world market levels the EC would be importing an additional 6.5 million metric tons of feed grains, an additional 1 million tons of bread wheat and perhaps 1.5 million tons less of soybeans.

Subsidized third market competition. We maintain that the EC has become a major world exporter of agricultural products largely through the use of export subsidies provided through the CAP.

Since its inception, the Common Agricultural Policy has been operated to maintain high and stable internal prices without any mechanism to limit the extra production elicited by those high and riskless price support measures. This excess and growing production has first displaced EC imports and, then as it grew larger has been disposed largely through subsidized prices into the international markets, thus further displacing our and other countries more efficient exports.

During the period of the operation of the CAP the EC has moved from a substantial importer to a significant exporter of a large number of major agricultural products. EC exports as a percentage of world trade in food products have increased from 9.3 percent in 1973 to 11.4 percent in 1980. We stress that this increase has been achieved largely through the application of export subsidies. During the same period, the EC's share of world imports declined from 24.7 percent to 19.5 percent. Thus EC net imports of food products dropped from 15.4 percent in 1973 to 8.2 percent in 1980. These are not our numbers, they are statistics published by the GATT.

Clearly the Community has moved beyond self-sufficiency through its pricing policies. One measure of the effectiveness of the CAP levy system in protecting EC producers from imports is the difference in the rate of growth in EC imports of levy versus non-levy products. U.S. exports of levy items increased in value terms by 2.6 times between 1970 and 1979 while exports of non-levy items increased by 4.1 times. As a percent of total agricultural exports by the U.S. to the EC, variable levy items decreased from 31% in 1970 to 22% in 1979.

The move to self-sufficiency on the basis of high support prices reduced the EC market opportunities for traditional exporters. The move beyond self-sufficency has spilled over into the international market through subsidized EC exports that compete unfairly with traditional exporters in third markets.

--In grains, last year for the first time since the inception of the CAP the EC became a net grain exporter. The Community is now challenging Australia as the third largest wheat exporter with 15.5% of total world wheat exports. This has occurred because of subsidies and increased levels of import protection. The import levies on corn and wheat during the last 15 years have risen. The target price for corn, for example, has been increased nearly three times as fast as the intervention price during this period. This slowly but surely shuts out imports and contravenes both the spirit and intent of GATT.

Domestic grain consumption in the EC-10 increased by nearly 9 million metric tons from 1970/71 to 1979/80 (to 122.2 million mt), but the community reduced its net imports from 22.3 million mt in 1970/71 to 2.5 million mt in 1979/80. In the 1980/81 the EC became a net exporter of 3.8 million mt and net exports are also anticipated for 1981/82. For coarse grains, net imports declined from 15.8 million mt in 1970/71 to 9.3 million mt in 1979/80, in spite of an increase in domestic consumption of 8 million mmt during the same years. In 1980/81 there was a further decline in net imports to 6.8 million tons.

--In sugar, EC exports have soared from 2.1 million mt in 1976/77 to 4.5 million mt in 1980/81. This has had a tremendous impact on the world and the U.S. markets and has affected sugar exports from Australia, Brazil, and the Philippines. The U.S. sugar industry estimates that EC export subsidies, which are responsible for world sugar market price levels, have cost U.S. industries $2.1 billion in lost revenue. We would not have the type of sugar support program that was passed by the U.S. Congress if it were not for the price depressing effects of EC sugar export subsidies.

--In poultry, the EC has moved from the worlds largest importer to surpassing the U.S. in 1970 to become the world's largest exporter. The Community now accounts for 35 percent of the world broiler market.

--In beef and veal, for many years the EC was a net importer. In 1973/74, however, the EC reached self-sufficiency. Thereafter production continued to increase while consumption remained stable. This has resulted in the EC moving from a net importer position to the second largest exporter of beef in the world for the last two years, behind only Australia.

--In fruit, the EC processing subsidies pose a serious threat to U.S. producers. The recently introduced subsidies for Greek raisin producers have virtually stopped U.S. raisin exports to the EC. This policy which also applies to canned fruits impairs bindings given in good faith by the Community during GATT negotiations.

Transmission of instability. EC policies also contribute to increased world market instability. By maintaining a rigid internal price structure under the CAP and insulating the EC agricultural sector from the international market, the EC forces other countries to bear the brunt of international market instability. Although some of the less developed countries are least able to cope with these distortions, the U.S. also must adjust both production and consumption to accommodate EC market distorting practices. As one indicator of increased market instability, USDA analysts estimate that present U.S. export volume projections are subject to a forecast error of $\pm$ 12 percent or 16 million metric tons, up substantially from a forecast error of $\pm$ 8 percent or 5.5 million metric tons in 1950.

While the EC is not accountable for all of this growing instability, as a major agricultural trader it must accept responsibility for its fair share. And we fully expect the E.C. to share the burden with the U.S.

Thus as we step back and look at the CAP as it has developed over the last 20 years, we see a policy that has resulted in high and rigid internal support prices that have increased production and slowed consumption to such an extent that the Community is now a major exporter of most major food products. This was achieved because product surpluses to the domestic market were pushed into export through the aid of export subsidies, further exacerbating the instability of world markets.

The cost for these policies has soared enormously, to the point where the EC budget for direct market support in 1982 is projected to exceed $14 billion with about 50 percent of those expenditures going to export subsidies. In addition, some $20 billion will be spent by the Member States on agricultural support programs.

Quite frankly we feel that this approach has gotten out of hand. The sharp increase in EC exports is imposing a serious burden on U.S. farmers who have become increasingly dependent during the past 20 years on export markets. Today nearly 40 percent of U.S. cropland is devoted to export production. Unfair competition by foreign competitors in the form of export subsidies threaten our export markets and the livelihood of U.S. producers. An unfolding political difficulty for this Administration is the 40 percent decline in net U.S. farm income in 1981 that in real terms constitutes the lowest level of net farm income since the Depression. Because of low grain prices, we expect have to make deficiency payments to farmers totaling more than $500 million in FY 1982. Further, we are now projecting the value of our exports this year will fall below last years level. This will be the first downturn in exports since 1969.

In this environment USDA has had to abandon its position against production controls and announce set aside programs. If we achieve producer participation in the wheat set aside program for the 1982/83 crop year of about 10 percent, it will result in a decrease in U.S. wheat production of about 7.5 million mt. That is nearly the amount by which the EC has increased its wheat exports to world markets over the past three seasons.

USDA analysts have estimated the effects on the U.S. and other suppliers if in 1981 the EC would have exported only 7 million metric tons of wheat (a more historical level) rather than the 14.5 million metric tons that were shipped. The U.S. would have exported 4.1 million tons more, Canada 1 million tons more, Australia 200 thousand tons more and Argentina 100 thousand tons more.

The U.S. producer price for wheat (and thus the world price) would have been 50 cents per bushel higher resulting in an increase in net farm income for U.S. producers of 1.7 billion dollars.

Even if the EC would have substituted 6 of the 7 million tons of EC wheat for imported corn, the price of corn would have decreased only 13 cents per bushel and the net farm income gain to U.S. producers would still have been 800 million dollars.

The point is that EC subsidized exports are hurting the U.S. High internal EC prices stifle food demand by consumers, some of which would be satisfied by imports. Subsidized exports add supplies into the world market. Both of these actions depress world market prices and thus our domestic producer prices. This results in higher farm program costs for both the EC and the U.S. EC consumers bear the burden. U.S. producers bear the burden. And taxpayers on both sides of the Atlantic bear the burden.

If we cannot resolve our differences, we are on a collision course. Last November when EC officials were here they spoke of reform of the CAP. The U.S. applauds the internal EC discussions now underway on the need for CAP reform. The proposal to phase EC prices to world market levels is most welcome. But we must ask how this convergence will take place when the Commission is proposing an average increase in prices for 1982/83 of about 6.6 percent. And again target prices would be increased more (7%) than intervention prices, increasing further the levels of EC protection for grains.

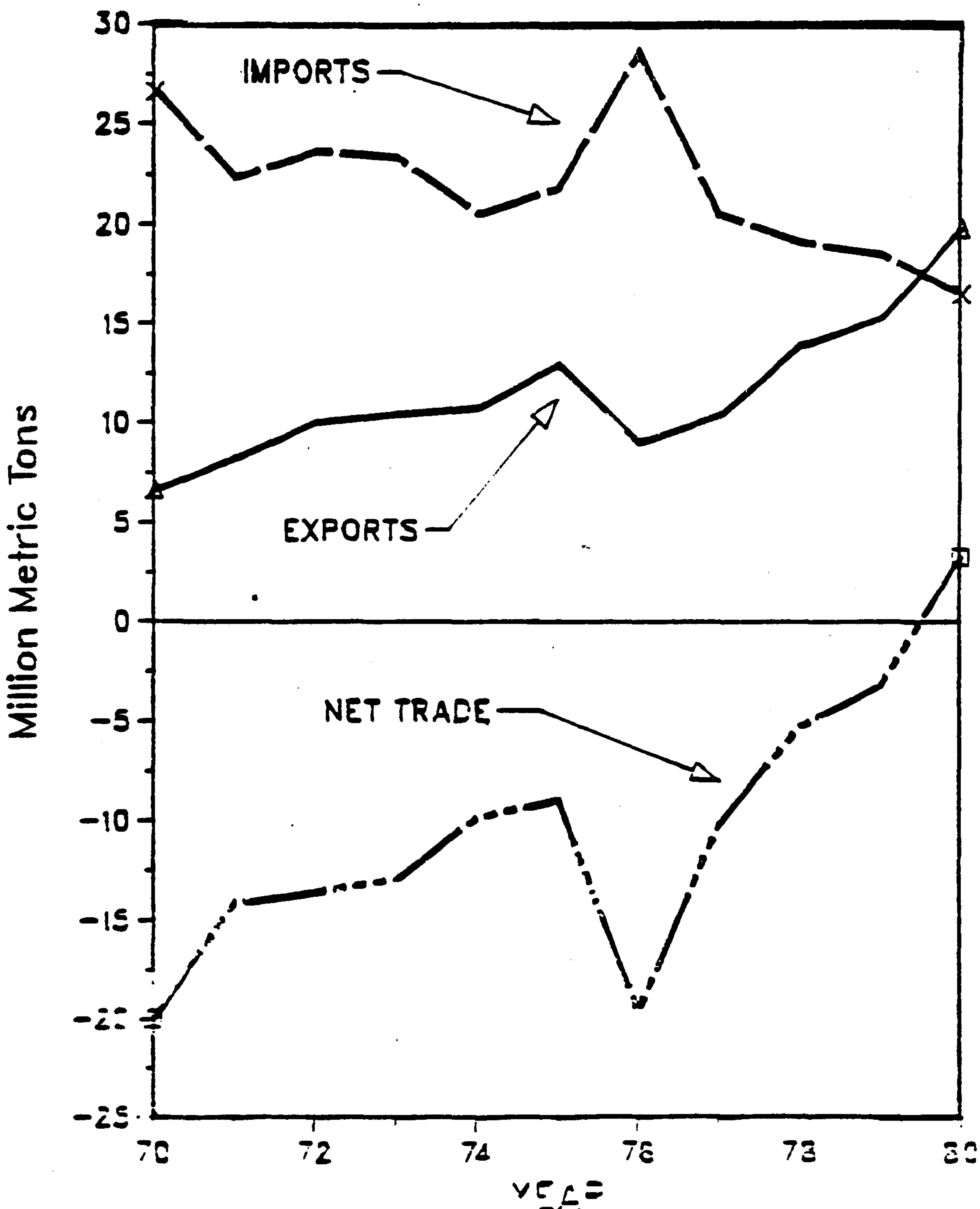
The U.S. cannot tolerate the evolution of the CAP to a Common Export Policy as the proposals imply. The proposals are silent on the subject of export subsidies. As we have indicated, EC export subsidies are the single most harmful of EC policies. The U.S. must see an acceptable plan and timetable for their elimination.

The proposals indicate a target volume of grain production of 130 million mt excluding durum by 1988. To achieve that target would take an annual rate of production increase of 1.7%, significantly lower than the EC historical rate of yield increase. The proposed reduction of 1% in the intervention price in the following year for each million tons of production over the target volume seems to be a rather mild price penalty. Is the EC prepared to impose production controls if necessary? And what level of export do the volume targets imply?

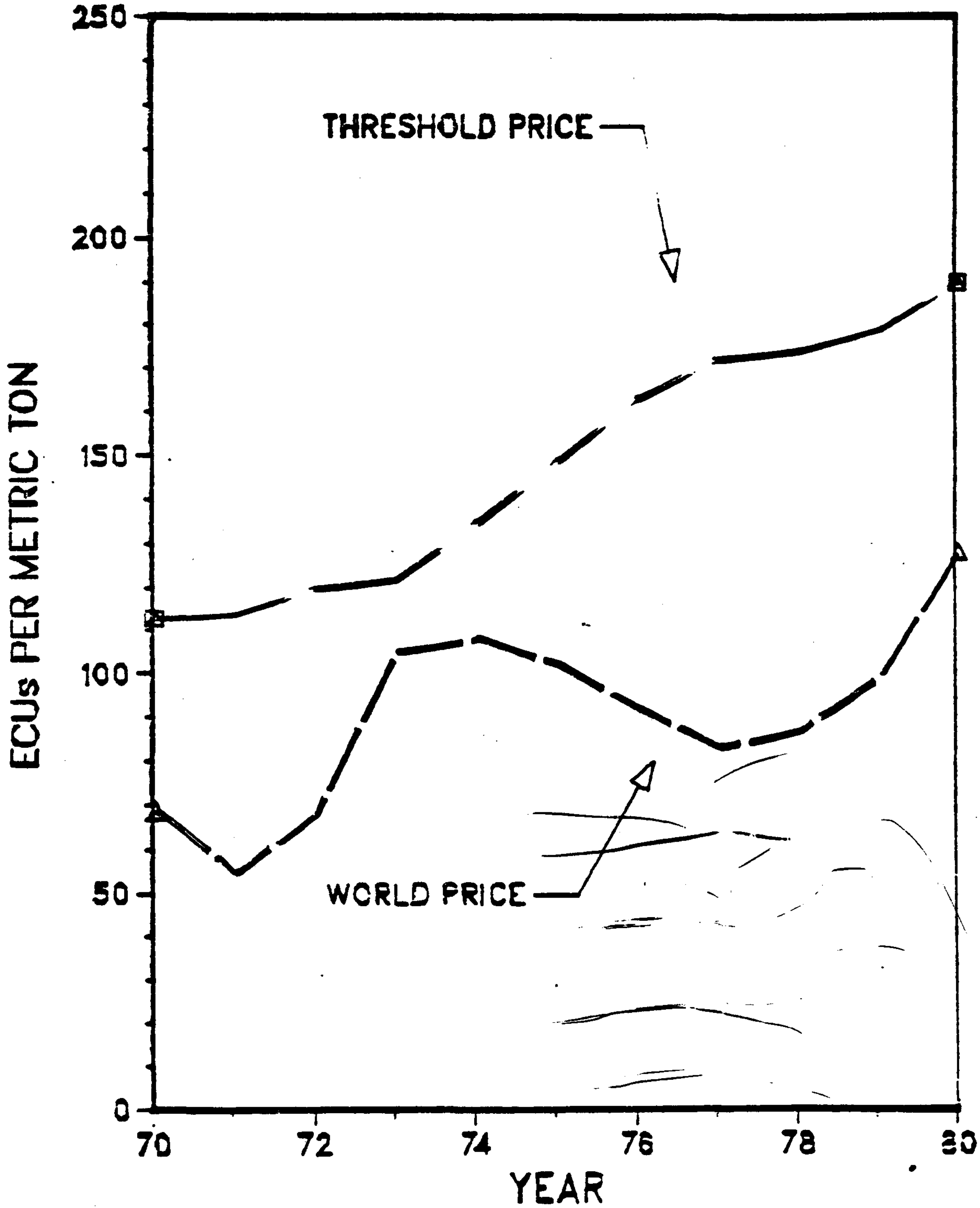
While the EC proposes phasing internal prices to world levels by 1988. Nothing is said about the level of threshold prices at that point. To share in the international market instability, it is important that EC border protection be keyed to world price movements in such a way that EC production and consumption will adjust on the basis of world market conditions. Such adjustment would also require increased stocking levels in the EC.

To summarize, we do not question the European Community's right to export agricultural products. Our concern is that net exports from the Community not be allowed to rise as long as world prices are below EC prices. Until this principle is allowed to prevail, we must regard EC trade policies as a major problem that will continue to erode the overall relations between our countries.

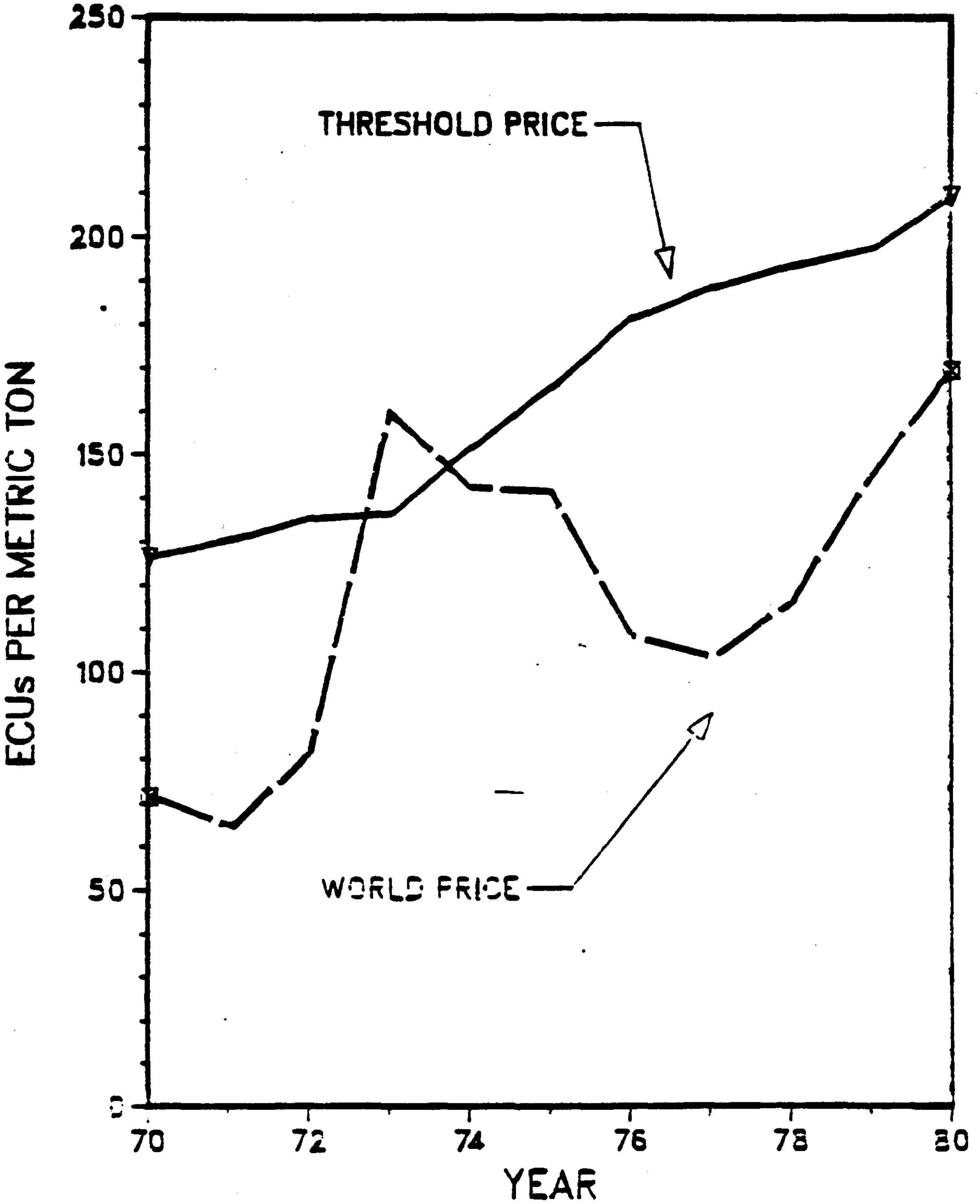
EC TRADE IN WHEAT & FEED GRAINS



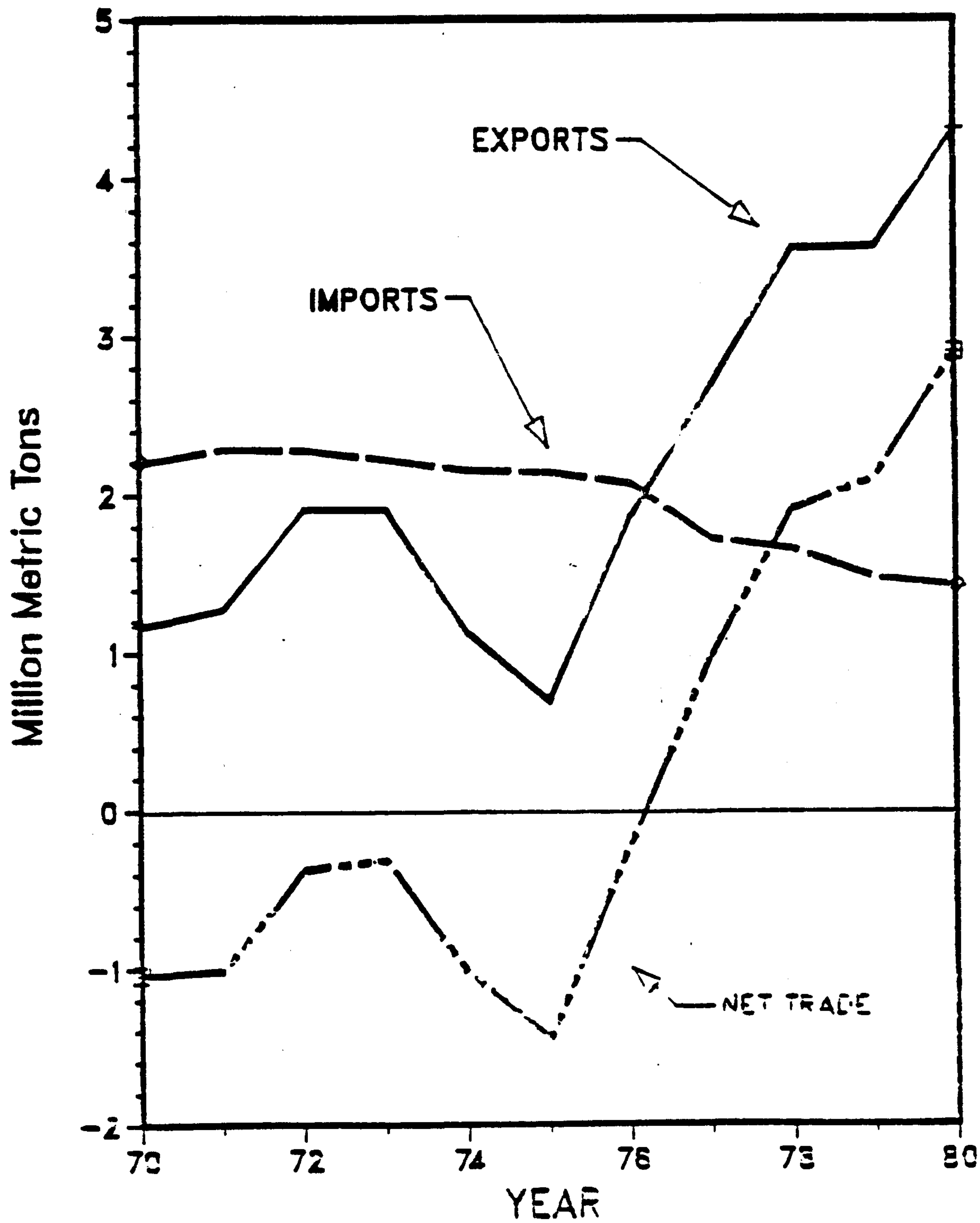
EC AND WORLD CORN PRICES



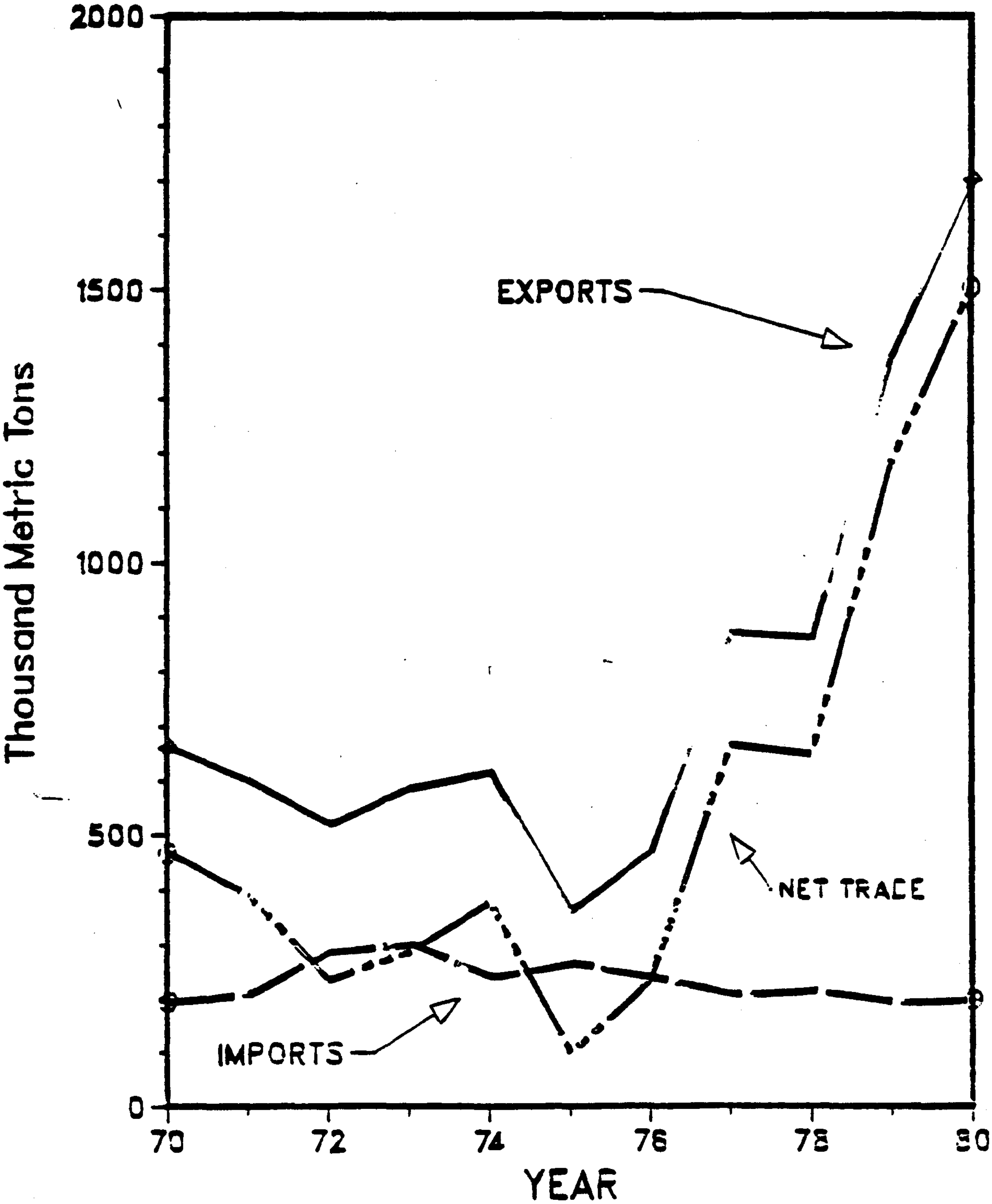
EC AND WORLD WHEAT PRICES



EC TRADE IN SUGAR



EC TRADE IN DAIRY PRODUCTS
(butter, cheese, and nonfat dry milk)



EC TRADE IN MEAT