



Report on Wilton Park Conference WP828

AGRICULTURE IN EUROPE: WHAT IS THE FUTURE?

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Summary

1. There is the potential for a brighter outlook for Europe's agriculture sector and for European farmers over the next 15 years, however many challenges lie ahead. Agriculture remains a strategic asset; this is likely to increase in the coming years given the contribution agriculture can make to reducing climate change, both in terms of providing new sources of energy and contributing positively to the carbon cycle. Ensuring safe, nutritious and reliable food supplies for EU citizens and a growing global market will also provide European agriculture with opportunities.

2. The diversity of Europe's agriculture will increase over the coming 15-20 years ranging from more intensive large-scale producers, increasing their economies of scale to smaller holdings, some creating niche products, selling locally. Organic farming will continue to play an increasing role within EU agriculture; as will the production of non-food crops including biofuels which will provide significant opportunities as an alternative market for crops. Overall, production might be predicted to fall since the decoupling of CAP payments (for example beef and durum wheat), or shift to the production of other commodities. In the longer term production is likely to increase due to the growing global demand for food and non-food crops, including energy crops.

3. The EU model, whereby agriculture is multi-functional, producing high quality, safe food with high environmental and welfare standards, is likely to remain intact. The key question for Europe, however, is how farm enterprises can provide food to the standards expected under the EU model whilst doing so competitively, not least given the challenges of the international market. How can agriculture deliver public goods, in terms of environmental and landscape benefits, and how much will this cost?

4. Farming which is more connected to consumer demand will be key, as will entrepreneurship and diversification. Farmers also want a level playing field. But policy makers will continue to need to provide a variety of financial and non-financial tools to support Europe's agriculture. Research and development for the agricultural sector is critical and the EU is encouraged to catch up with US and Latin American competitors in research both for core agricultural developments and renewable crops. Policy makers also need to ensure a well-functioning food chain, appropriate regulation and policy simplification, monitoring of retailing competition and ensuring a fair global playing field. Governments can also help to develop appropriate risk management tools for farmers; the question of EU support for such risk management tools remains open.

5. Whilst it is still too early to assess the longer-term implications of the 2003 reforms to the Common Agricultural Policy (CAP), the proposed "health-check" of the CAP in 2008 provides an opportunity for both review and simplification. Some believe that the health-check should provide the opportunity for further reform. This could be driven, politically, by the pressures from the 2008-9 EU Budget Review, which provides an important opportunity for the EU to undertake a full and wide-ranging review on all aspects of EU spending, including the CAP. There are calls for Member States to take this opportunity to consider ways towards achieving a restructured budget for the EU 27 in the 21st Century. Debate will intensify about what the CAP is now for and whether and how financial support should be distributed to support Europe's model of agriculture.

6. Looking to the future there seems to be a clear need for a longer term policy outlook, to prepare for and respond to growing external (globalisation) and internal (societal, financial, enlargement) pressures and environmental demands, and to give farmers the certainty they need to run their businesses competitively. To respond to these pressures while providing the appropriate public support to the farming sector, it is likely that the mechanisms of the CAP, such as Pillar 1, will need to be adjusted. Such reform needs to ensure simplification, be manageable and appropriately phased. A CAP of the future also needs to reflect the demands and expectations of society if public money is to be spent on public goods.

Introduction

7. The sheer diversity of agriculture across EU will increase over the next 15 years to 2020, operating in diverse conditions from the frozen north to near desert south, from hill-farming to small island plots. Farming styles range from more subsistence-based farming to large-scale intensive production with many varied operations in between; agriculture employs almost one in six people in Greece or Lithuania yet less than one in fifty in some others.

8. The EU remains a large importer of raw food products and the largest exporter of processed food. Overall the EU's trade balance is almost €20,000 million in deficit in raw materials, with a surplus of about €15,000 million in processed products.

9. The opportunities for Europe's farmers and growers are increasing. The EU's population of 450 million provides a ready local market with richer consumers wanting quality food. Changes in population structure will mean that by 2030 almost half the EU's population will be over 50; flexi-living, increased use of convenience food, eating out, functional food, ethno food, and changing palates will all affect consumption patterns and thus demand for products providing opportunities for farmers operating in a more sophisticated food processing and distribution system.

10. There is also increased demand for food, generally and for better quality food, from urbanising populations of China and India, and the growing populations of Africa and the Middle East¹. International trade continues to grow at about twice the rate of production and consumption. There are now more obese people in the world than starving. Crop production growth, especially oilseeds, is expected in Latin America and expansion in livestock, particularly poultry expected in Asia.

11. Europe's relatively benign climate is likely to provide some longer-term stability in production. But climate change generally will continue to have a significant effect on production patterns; with the Mediterranean region expected to be dryer and northern Europe wetter with increased risks of storms and droughts threatening levels of annual production. Globally, climate change will also affect levels and patterns of production.

A vision of Agriculture in Europe

How do farmers see the future?

12. Across Europe farmers want the freedom to produce goods for the market place; they do not want to be merely park-keepers, or landscape managers. For many, farming is a way of life, but also a career choice and business opportunity. To farm they need access to markets and a fair market price, recognising that the majority of most farmers' income comes from the market place; in the UK the market share is estimated by the National Farmers' Union to be 84%; direct payments made to farmers under the CAP make up only 16% of their market returns (although market prices in some sectors are heavily influenced by the CAP). In an ideal world farmers do not want financial support, which many see as equating

¹ Annual global population growth is estimated at 9%.

to social security payments or charity. They want to be rewarded by the market as in other sectors of the economy. But for some European farmers the direct payments they currently receive stand for the difference between profitability and loss². European farmers are under pressure from, amongst other things:

- rising energy costs (affecting input costs);
- the power of supermarkets, squeezing prices to below the cost of production;
- national governments in relation to the way policies are implemented (and changes to policies and regulations are implemented); farmers see themselves as policy takers not makers;
- cheap imports and further prospects of trade liberalisation as a result of negotiations in the WTO;
- the changing weather patterns resulting from climate change.

Farmers also need proportionate and simple regulation to ensure that their competitiveness is not harmed.

13. The priority of farmers is to ensure that they can earn a living from their production. Increasing **competitiveness** is critical to their success – either through volume, or through adding value but, crucially, by being connected to consumer demand. For many farmers the key question is how can they adapt to be as efficient and competitive as possible whilst ensuring quality products. Many farmers are entrepreneurial, using their initiative. They are keen to embrace new technologies – but need access to this both through research and development (R and D) or new technologies for example, including Genetically Modified Organisms (GMOs) or practices based on the better use of the bio-functioning of soils.

14. Farmers are also increasingly **managing risk**, and will need to do so further in future. This they can achieve to some extent through commodity futures and options (with large scale production such as cereals), mutual funds or private sector insurance. They can also diversify and exploit new markets (e.g. tourism) and non-food crops (see below) and this is likely to increase.

15. Farmers need access to **markets** and the ability to negotiate with processors and retailers for a fair price. This is hugely challenging, for example where large supermarket chains are responsible for the majority of food supply³. Farmers need close partnerships with producers and retailers to produce what the market needs, but also to ensure a fair price

² This is roughly the case for 80% of farmers.

³ In Germany and the UK four main retailers in each country are responsible for about 90% of direct food sales.

above the cost of production; this may be best achieved by farmers organising themselves into groups.

16. For many farmers across Europe developing speciality **niche products** and direct selling can be a successful approach. Branding is critical; linking the product to the farm or locality can ensure its “added-value” and saleability. Clear labelling is also important, indicating geographical origin alongside the assurance of quality. Italy is an excellent example where production of a wide range of high-quality food is sold to a loyal customer base. Branding, based on locality is increasingly popular such as in the Po Valley. Farmers’ markets are also increasing in popularity in the UK and providing outlets for products, as are farm shops.

17. Farmers who have turned, or are turning to, **organic** production methods are also working closely with their markets. Consumption of organic food in Europe has increased over the last 20 years and this trend is likely to continue. The challenge for farmers choosing organic methods is to maintain their market without too high a price differential.

18. Organic methods of farming can also contribute to the reduction in greenhouse gases through the reduced use of nitrate fertilizers, which create CO₂ during their production and increased nitrous oxide when applied (which is estimated to be 300 times as strong a greenhouse gas as CO₂). Agriculture also produces methane (mostly “emissions” from animals). As debate around climate change intensifies the role of agriculture in tackling this could increase with farming acting as a reservoir for carbon for instance. This is particularly so for organic farming which can increase the carbon-rich organic matter in the soil⁴. Permanent pastures, lower stocking rates, systems encouraging deep rooted plants, or not grazing drylands could provide other agricultural solutions to climate change; also the sequestration of forest timber in building construction. The increased cost of nitrates, due to higher energy costs in production, could lead to less intensive farming, benefiting the carbon levels.

19. Niche market and organic production will be important aspects of European agriculture; but volume production of foodstuffs will remain an important segment of the European farm sector. Certain products need to be produced in large quantities, for

⁴ According to the Soil Association the carbon loss from soil through intensive methods of agriculture can be 30-40 tonnes per hectare. Over intensification of European agriculture, with increased use of chemicals and fertilizers, has left many soils depleted. Estimating the real value to society of carbon is difficult but the Soil Association believe the rational price to be about \$200 per tonne of carbon emissions (the actual price for carbon in 2006 being just \$20/tonne). They estimate that organic farming, if applied globally, could halve agriculture’s estimated 2 billion tonnes of carbon; (an organic farm uses 6 calories of fossil fuel to produce 1 calorie of food; an industrial farm uses 12 calories).

example cereals; adding value at a local level is difficult for such basic foodstuffs needed in quantity.

Are biofuels an answer for the future of Europe's agriculture?

20. Europe's agriculture is already producing a wide range of renewable products from crops for industrial use including chemicals, pharmaceuticals and fibres. The big potential market increase, however, is in producing biofuels from crops. The EU Biofuel Directive states that 5.75% of transport fuel used in Europe should be made from biofuels by 2010⁵. Currently 5.8% of the EU's total energy consumption comes from renewables, of which biomass is about 3.75%; The EU Energy White paper seeks to increase the renewable output to 12% by 2010. 75% of this growth is likely to come from biomass sources. To achieve this level of biomass/biofuel, without the need for imports, varied estimates suggest that between 11 and 38% of Europe's current total cropland would be needed, matched by a 60% increase in production capacity. The EU is expected to produce more biodiesel (from rapeseeds) than bioethanol (from grain) at the outset, although the latter is more efficient in terms of production yield per hectare of land used⁶. Whilst there is sufficient surplus of cereals produced within the EU for about 6 Mt of bioethanol, much more will be needed to meet the 2010 targets. The potential cereal demand for bioethanol in 2010 is about 24 Mt. (maize, wheat, triticale, barley and rye).

21. This therefore provides many European farmers with a significant new market for their crops. The implications mean that farmers: have new markets for their cereals and oilseeds; the potential for long-term contracts; price certainty through fixed contracts, with prices being set higher than the cost of production, allowing cash-flow forecasts for farmers and thus the opportunity for them to invest in infrastructure etc; a risk management tool; the opportunity to grow crops for a local market. The by-product of high-protein animal feed supports the livestock industry also reduces the need for production of some cereals being grown for animal feeds topped up by EU imports. There are opportunities across the EU, and especially for new member states once their yields increase through higher investments etc.

22. The price of oil, and its volatility, is a critical factor in the profitability of biofuels. Brazil, where bioethanol production is mostly from sugar cane, witnessed the world sugar price doubling, when oil rose to more than \$50 per barrel, and then dropping back 40% in

⁵ The target for 2006 is 2.75%.

⁶ If only 75% of the 5.75% biofuel target is to be "home-grown" estimates suggest a further 45 new plants are needed, producing 200 million litres (Mlit) of biofuel each. 200 Mlit equates to 500,000 tonnes of cereal. To date production facilities produce c 1,260 Mlit with capacity led by Spain, Germany, France, Poland and Sweden. It takes about 2 years to design and build a new plant.

just two weeks after a fall in oil price. It is also noted that the production costs for oilseeds in France, for bio-diesel, for example, is significantly higher than in Canada or Argentina, particularly if GMO crops are used. Some EU countries can achieve greener energy through existing means (for instance forestry plays a large part in the renewable energy for Sweden and Finland).

23. There are some major issues for Europe in relation to developing the agricultural production of biofuels. If more land is taken into biofuel production will it lead to increased intensity of production? Will it increase food prices generally, thus giving farmers' more return on other products? Or will it increase dependency on food imports? Will the best land be used? Can set-aside land be used to provide for the increased land needed and if so what will be the consequences for the environment? If crops are used for biofuels their interchangeability can provide for both food and fuel, although cereals with a higher starch content are better for ethanol production than those with a high protein content. Care is needed if dedicated ligno-cellulosic crops are to be used as they cannot feed humans or livestock. In the US, where the biofuel market is growing rapidly, demand for maize for ethanol has increased but has not led to a fall in exports; increased demand has encouraged additional planting and has not caused food price inflation. Second generation ligno-cellulose products are due to come on the market in the relatively near future.

24. Will Europe therefore see increased crop production over the coming years? There is early anecdotal evidence, for example in the UK, that the introduction of the Single Farm Payment (SFP) under the 2003 CAP Reforms has led to decreased planting of crops and more extensive stocking rates – likely to reduce production overall. However, a significant and sustained increase in wheat prices, and/or a significant market for bio-fuels could lead to a sharp increase in production.

25. Farmers would be looking to increase yields from existing land use, and would depend on scientific and technological developments to increase yields from the same area planted. There could, therefore, be growing pressure to introduce GMOs in Europe and some believe that farmers should be able to choose whether to grow GM crop varieties if they want to reduce production costs and increase competitiveness. Others suggest that it should not be a question of organic versus GMOs; in the long term genetically modified organic products may be developed. And new farming practices taking more advantage of the bio-functioning of soils may be developed.

Providing a public good in rural areas

26. In addition to providing food and non-food products Europe's farmers will continue to provide a public good through their protection and development of biodiversity and the local environment and their management of the landscape. Rural areas cover 80-90% of European landscape (between 40-60% of this is farmed in each country); the landscape is seen as natural heritage with agriculture playing a crucial link for rural areas between the natural environment, economy, society and culture. Maintaining this link is, to many in Europe, a key role of agriculture. The vast majority of farmers look after their patch of the countryside as part of their farming job. The belief that highly efficient production methods are bad for conservation is not necessarily an accurate one - intensive farm enterprises can also produce conservation; it is not necessarily an "either/or". But if farming is not profitable there is no funding for farmers to look after the landscape as they would want to. Funding to support the environmental and land management role, whether the funding is public or private money, means that farmers can do more.

27. Agriculture will also remain a critical part of lively rural communities. There are many examples of successful developments of rural areas as tourist attractions, linking agriculture, local food production (marketed as such) and the environmental benefits of the area and encouraging tourists and such examples are likely to increase. Nevertheless, the viability of rural areas depends on much more than just agriculture (eg services, infrastructure, diverse employment opportunities) and holistic rural development strategies are needed.

The changing nature of farming

28. In the coming years there is likely to be further change in farm structures across Europe. Some fear that pressures to remain competitive will lead to larger farm enterprises and the reduction in family-run farms which would be to the detriment of the viability of rural areas. In new EU countries continued consolidation of land (whether owned or rented) is likely. Slovakian agriculture already has the advantage of big farms and cheap labour. Poland, on the other hand has small units. There are also very different patterns of ownership across the EU, and land markets have become more complex given entitlements and quota attached (or not). With the variations of implementation of the SFP across Europe, the capitalisation of some payments, and different tenancy legislation, expansion or structural change of farm units may be less feasible. This may however be a good thing, some argue, allowing the traditional family farm to be preserved in many areas.

29. In many countries only large specialised farms currently operate profitably. In Germany only 8% of farms have more than 100 hectares, covering 50% of the land with 10%

of the units producing 50% of total production; whilst in the Czech Republic about 12% of farms have more than 100 hectares, accounting for more than 88% of total land. In Poland less than 8% of farms have more than 20 hectares. Change is happening, but slowly; in Germany the number of farms decreased by just 3% between 1991 and 2003; with a similar decline in the total labour input. It is likely that agricultural labour will continue to diminish and become “Europeanised” with more workers from new member states working in old member states for instance, and north Africans crossing the Mediterranean for seasonal work. In Poland 17.6% of the population still works in agriculture (producing 2% of GNP); in Germany it is 2.4%. More telling is the average age of farmers which remains high (50s and 60s) across Europe. In many parts of Europe farming is done part-time on small parcels of land.

30. Significant structural change is also difficult given the scarcity of land in some parts of the EU coming onto the sale or rental markets due to ownership or tenancy legislation for instance, taxation or farm profitability. This can make it difficult to expand if farmers want to, particularly in their neighbourhood. The scarcity of available land may restrict the number of farms which have the opportunity to expand and exploit economies of scale. High land prices because of inelasticity of supply and demand from housing and other activities also make growth expensive. Some are looking for land elsewhere in Europe; and this trend may continue with for instance Dutch farmers operating in Hungary, or Germans in Poland. The combination of an aging population of farmers and land being a scarce asset means there is little opportunity for new entrants. The long-term future of agriculture will depend on younger people becoming involved.

31. Agriculture also remains a highly capital intensive sector. Investment in infrastructure, buildings and machinery is continuously needed, and especially so in most new member states.

32. The long-term success of European agriculture also depends to some extent on the importance Europe places on home-grown supplies as against imported food. Local food miles is becoming part of the debate about food production patterns, but is also a feature of the debate about overall food security. Is there a need for self-sufficiency and if so, in what commodities, and at what level; EU wide, member state or region? Is food security measurable in term of self-sufficiency, and if so what are the appropriate levels of self-sufficiency? Some argue that food security is enhanced by encouraging diversity in supply sources. To ensure long-term food security for Europe there is a requirement to:

- keep land in good agricultural order and to maintain agricultural structure and skills if this land is to be brought back into food production when required;
- ensure there is not over reliance on too narrow a range of food-producing regions, crops and animals (especially with a narrow genetic base) to avoid vulnerability to potentially catastrophic attacks from virulent pests and diseases;
- encourage the interchangeability of crops for energy and food rather than the conversion of too much land into woody, short rotation coppice which is difficult to reconvert for food production;
- maintenance of a viable food chain and distribution system. The UK fuel crisis highlighted the vulnerability of complex “just-in-time” distribution networks and the limited number of processors and distributors in the food supply chain. An influenza pandemic could pose a similar threat;
- build and maintain trading relationships with other food-supplying countries.

If there is a deteriorating global food supply it is the poorer people in both the EU and developing countries who are likely to be hit hardest through the increase in food prices.

33. In summary, in a vision of agriculture in the years to 2020, there is likely to be an increased diversity of farm enterprises and their products – food and non-food. A range of different “models” and types of farming across Europe are likely to emerge, it is suggested, including:

- farmers who are commodity producers (including renewables), much on a larger scale commercial basis, many using more contract farming;
- farmers adding value through niche-production, perhaps including on-farm processing, and/or direct marketing;
- farmers as a service provider (both to the public and private), as environmentalist, nature protector and landscape producer. This latter may include more farms in more marginal areas.

Many farming enterprises are likely to be involved in more than one, if not all, of these so-called “models”.

Supporting an EU vision: What policies are appropriate?

34. European policy makers are challenged to consider what policies are most appropriate to support an increasingly diverse model of agriculture and how such policies are best delivered. The starting point is to what extent the farming sector can be profitable without the need for subsidy. What can governments do to encourage the market place to provide a viable income? What levers can policy makers provide? More debate is needed about what policies and tools can be provided ensuring that farmers can maximise their

returns from the market before focusing specifically on the CAP as a policy mechanism. It is noted that certain areas of agriculture in Europe are succeeding without financial support (pigs/poultry etc); in the Netherlands two thirds of agricultural production is unsupported. Some believe that CAP Pillar 1 support is poorly targeted and think that it has inhibited farm competitiveness.

35. A range of policy measures can be considered at the local, national and EU level over and above straight financial measures. These can include policies which:

- *encourage competitiveness and entrepreneurship.* Whilst the farming industry does much to help itself, government-supported training can play a critical role in this, both on and off farm, and including online, whether in seeking improvements in farming methods, updating technology, process and marketing skills etc; also government backed farm advisory schemes, or IT software to provide a “whole farm approach”. Other support to manage retirement for some farmers can open opportunities for new, younger entrants or expansion of existing units to increase competitiveness;
- *increase spending on R and D* which is critical for the long-term success of the agricultural industry. Governments are encouraged to play a larger role in research; this can include supporting research into biofuel development (both main and by-products); reconciling the intensiveness of production methods with the environmental objectives; the microbiology and genomics of soils; GMOs etc. Some argue that more research should be funded at an EU level;
- *reduce paperwork and bureaucracy;* whilst it is necessary to regulate this should be balanced to allow farmers to farm rather than filling in excessive forms or meeting unnecessarily onerous standards;
- *regulate retailers,* particularly where there is a monopoly of retailers, and given the imperfect competition amongst some aspects in the food chain and strength of some retailers in their sheer purchasing power. Governments can play a critical role through competition authorities;
- *support farmers working together* to negotiate fair prices for their products;
- *encourage younger and newer farmers* into the industry; supporting managed retirement policies if necessary;
- *educate consumers* both in terms of quality food, and encouraging consumers to buy locally produced goods.
- *ensure clear labelling* of products and contents, and their provenance; in the UK the Farm Assurance scheme uses the Red Tractor logo.

36. There is widespread debate about how to encourage farmers to manage the risks associated with price volatility, and thus incomes, in agriculture. But what risk management tools are appropriate and what role should governments play? Increased use of the futures and options markets for some products is an option; but such measures are easier for large-scale cereals than smaller-scale producers and the livestock sector. If futures and options are to be used more the financial markets would look to the European Commission for a clear signal as to the sequencing of reform to support future increased commodity and futures markets. Insurance schemes are also an option; the question is whether these are best provided by government or the private sector? The question of the support for such schemes, through a new tool within the CAP, remains a matter for debate. In Spain government-sponsored insurance system has been running successfully for 25 years to provide compensation for climatological events such as drought or hail⁷. In 2005 Spain used its experience of this scheme to set up an income insurance scheme to provide protection for fluctuations in both volume of production and price fluctuations, but this has proved difficult to operate.

37. Governments also need to consider appropriate intervention policies where markets fail, for example because of price volatility in the cereal market dependent on annual global production levels. Is support appropriate to maintain minimum prices? Some call for the regulation of imported goods into Europe; there is a strongly argued case for competitors trading in EU markets to comply with the same requirements on food safety, environment and animal welfare as EU farmers. What is the role of the EU or national governments in the regard?

38. If agriculture is to provide the majority of biofuels needed by the EU there is a need for a significant increase in production. The EU will need to address the issue of how to meet this demand. If biofuels are to be produced within the EU what is the appropriateness of keeping 8% of land out of production through “set aside” policies (on which some energy crops can already be grown without support)?⁸ What incentives will be necessary for investments to be made in production capacity? Governments are encouraged to provide a steer to the biofuels industry with long-term policies and tax incentives in order for processors to invest in plant and infrastructure. Some suggest that to ensure fairness with oil an environmental statement is needed on all forms of fuel to determine whether they should qualify for tax breaks; with biofuels being assessed to be more environmentally friendly. Governments, with the support of the EU, could also: provide a steer on which biofuels are

⁷ This is included as a measure in the Rural Development Programme.

⁸ The total area of land set-aside across the EU in 2007, including the 2 new member states, will be 8 million hectares.

appropriate; encourage more efficient use of technology to maximise the output from the raw materials used and the residues; encourage greater use of biofuels in their transport fleets.

39. Ensuring the positive net balance in biofuel production is important in the fight against climate change. If agriculture is to contribute further in reversing climate change additional policies should be considered; its inclusion in the Emissions Trading System for example. Assessing the value of carbon in soil in different farming methods is also a possibility with support given for such a public benefit. Policies towards long-term sustainability of agricultural production also need to be considered.

40. Whilst European agriculture provides a public good through supporting the environment and maintaining the landscape there are major questions about how policy can best support this. What is the “value” of these public goods to society, how have these changed since the CAP was established and how can the value be measured? What level of support is appropriate for public goods which farmers provide? Who sets the environmental agenda? Does the NGO lobby hold too much influence on policy makers?⁹ Key questions remain about how best to look after landscapes, how governments can establish what society wants and how much society is willing to pay for this. (Will policies that offer incentives to farmers to produce public goods have a negative impact on farmers as they will serve as a distraction from the market? Or should the term “market” be considered more broadly?)

41. In ascertaining appropriate policy instruments to improve biodiversity on agricultural land careful consideration is needed as to what should be compulsory for the agricultural sector and what optional? Existing Directives, such as the Birds and Habitats Directive (Natura 2000) and the Water Framework Directive, may be satisfactory in their objectives but are under-resourced if they are to encourage biodiversity and prevent water pollution¹⁰. Whilst site protection under the Birds and Habitats directive is a positive tool, it is not necessarily a fully efficient conservation tool because of lack of funds. Conservation of high nature farmland depends currently on a range of instruments, such as support for Least Favoured Areas or agri-environment schemes (for instance the previously run Countryside Stewardship scheme, or Entry Level System and Higher level schemes currently being brought into England). Key to their success is commitment from farmers, and financial backing to provide some financial compensation. Some question whether the agri-environmental schemes are currently being targeted on the right areas in Europe in order to achieve the biodiversity required; there being no statistically significant relationship between

⁹ There are more members of the Royal Society for Protection of Birds than a UK political party.

¹⁰ WWF estimate that 15-25% of EU land is now covered by Natura 2000 areas.

regions with a high share of targeted Natura 2000 habitats (ie recognised for their biodiversity) and those areas receiving funding for agri-environmental schemes or having a share of organic farming to improve biodiversity. At a pan-European level it is recommended that there should be sound comparative and analytical research into the effectiveness of individual agri-environmental schemes, and similar analysis of the data of non-EU countries where there is farmland of a high-nature value and policy measures.

42. There is concern in some countries, such as Hungary where land is given a Natura 2000 status because of its biodiversity, that land value subsequently decreases. Such an unintended consequence needs to be recognised when the aim is to increase the value of biodiversity, and encourage farmers to preserve it. Targeting nature conservation by focusing on “honey-pots” is also challenged because it could exclude support for the environment in areas with less high natural value, or beauty. Ironically a lot of private money is raised successfully through NGOs to support the environment; but it is not necessarily directed to the agricultural sector where they are responsible for the environment.

43. In identifying appropriate ways to support rural communities, and particularly those away from large centres of population, or in marginal areas policy makers have traditionally used agricultural instruments. Many argue that family farms are the way to keep rural areas viable, given all the ancillary industries that support agriculture, and that they should be supported within a broader rural policy.

44. The LEADER programme, which will be funded under the Rural Development programme of the CAP, has been one instrument developed more recently by the European Commission, encouraging local communities in rural areas to work together to strengthen their viability. LEADER operates on small-scale projects and this can be complex for national governments to administer. Some argue, however, that successful though this “bottom-up” integrated approach has been in some areas, wider rural development policy depends on much more than agricultural measures.

45. Governments can play a role in encouraging rural areas through other policies, including support for infrastructure and encouraging private sector investment, for instance in tourism, and attracting people into an area. Tourism cannot be the answer, however, for all rural areas. Other ideas include creating “landbanks” of green areas around cities and encouraging forests for example.

Supporting an EU vision: setting the EU policy response in its global context

46. In considering a European policy response to support its vision for agriculture a global perspective is needed. It is still hoped that agreement will be reached to conclude the WTO Doha round during 2007, given the relatively close positions of the EU and US as two of the larger players in the negotiations. If a deal is struck this could, however, have a substantial effect on the EU. For example, increased imports of beef into the EU market are anticipated paralleled by reduced EU exports, impacting on the profitability of the EU beef sector. With or without a global deal, WTO business will continue with the WTO focusing on policies that distort markets and trade. Further trade rounds are anticipated and the trends to eliminate export subsidies and reduce tariffs expected to continue. This will allow less scope for price support through domestic subsidies. Support with minimal trade effects (green box) are likely to remain although the criteria could be tightened. Measures to protect health are also likely to remain if based on scientific evidence. The question for the EU is whether further tariff reductions, and in particular challenges to production linked support and the "blue box" will create major difficulties for the CAP?¹¹

Supporting an EU vision: Is the CAP "fit for purpose"?

47. The 2003 CAP Fischler reforms brought in the partial decoupling of direct payments to improve the transfer efficiency of direct payments and reinforce the farmers' market orientation and entrepreneurial role paralleled by cross-compliance to enforce standards (environment, food safety and animal welfare). The reforms also strengthened rural development policy and introduced modulation, redirecting CAP funding for specific rural development schemes. Payments under Pillar 1 are now virtually fully decoupled (90%). There is now, however, a complex array of degrees of decoupling across the EU: from partially decoupled historic based payments (France, Scotland); decoupled historic based payments (Wales); and transition to regional average payments (Germany and England). Meanwhile in the new member states, eight countries have applied the Single Area Payment Scheme (SAPS)¹². There are widely differing support levels per hectare across the EU. When Bulgaria and Romania join the EU in 2007 direct payments under the SAPS scheme will be phased in over ten years to reach 100% of the then applicable EU 15 level in 2016¹³.

¹¹ The Blue box, in WTO terminology, refers to a particular category of agricultural subsidy; Blue box being defined as the "amber box with conditions". The amber box refers to those domestic support measures considered to distort production and trade conditions. If subsidies are placed in the Blue box they are deemed to be support which would normally be placed in the Amber box, but are placed in the blue box if the support requires farmers to limit production (ie quotas, set aside etc).

¹² The changes to the CAP are still being implemented; five "old" member states are applying the SFP this year (the other 10 applied this in 2005) and Slovenia and Malta will apply this in 2007; the other 8 new member states having applied the SAPS.

¹³ In Bulgaria there are expected to be about 160,000 beneficiaries; 1.4 million in Romania. The average agricultural holding in Bulgaria is 16.7 hectares; but a large part of the 2.6m hectares is under large farms. In Romania the average holding is 8.8 hectares – over a total area of 10.6m hectares.

48. The question now asked is what the true objectives of Pillar 1 payments really are since they range from: compensation for reductions in price support; income support; stability for farmers; environmental payments; compensation for higher environmental and animal welfare standards etc; to ensuring food security by maintaining land in good agricultural order. Some question how well Pillar 1 payments are now structured and whether they are effectively targeted to achieve these different aims, and highlight the apparent conflict between two objectives; to increase competitiveness whilst improving the environment. By continuing Pillar 1 payments, which are essentially payment for a public good, are they not in danger of becoming “re-coupled” some argue.

49. The cross-compliance farmers need to achieve in order to receive Pillar 1 payments adds to the complexity¹⁴. One aim of cross-compliance is to ensure a distinction is drawn between fallow land which is kept in good agricultural order (and thus could revert to agricultural production) and land abandonment. However, in reality cross-compliance can be expensive for farmers, who risk losing payment if they fail one small aspect under inspection. That has been likened to someone receiving social security payment riding through a red traffic light on their bicycle and their payments being stopped. Is this appropriate?

50. Payments under the second Pillar of the CAP (essentially rural development funding) are for non-market services and recognise the so-called multi-functionality of agriculture. A reduction of about 8% in expenditure on rural development for 2007-13 was agreed at the December 2005 Council meeting. Support is allocated across three areas: to support the competitiveness of farming and forestry aiming to improve quality, marketing and productivity and restructuring; environmental land management (biodiversity and cultural landscape), and wider rural development and economic diversification. The main factors determining the extent of rural development are broader economic and social ones and cannot be solved by EU rural development policies under the CAP per se. Many argue that there is a public value in maintaining agriculture to ensure the viability of rural areas, particularly in marginal and LFAs rather than losing the last remaining agriculture from parts of Europe. Others argue that indefinitely supporting uneconomic activity cannot be justified and that more targeted employment schemes should be developed. Other CAP mechanisms can also be deemed to be supporting LFAs, for instance milk quotas which help slow down the relocation of dairy production away from LFAs – but these areas may also need Structural Fund support.

¹⁴ 18 sets of regulations were introduced under cross-compliance mechanisms, pulling together a range of earlier EC environmental and welfare standard Directives.

51. The practical implementation of rural development support by member states in the 2007-13 timeframe is likely to be delayed given the financial restraints. This is leading to uncertainty about future rural development and environmental policies in many areas. The future of LEADER projects is also in question. Whilst these have generally been successful given their bottom-up rather than top-down approach, they involve time-consuming bureaucracy for relatively small sums of money.

52. The “**health check**” of the CAP, expected during 2008, is to ensure that the CAP is working as it should. The European Commission stress that it is to be a health-check, not major surgery. The aim is to take the principles of the 2003 reform to its logical conclusion and achieve a simplified, fully decoupled system for all farmers within the EU, whilst assuring that agricultural support is in line with the needs and expectations of EU citizens. The Review clauses cover a variety of issues, and with varied deadlines, including direct payments per farm, market measures (including fruit and vegetables, cotton and dried fodder) and other measures such as the statutory management requirements of cross-compliance and farm advisory systems. The EC sees the “health-check” as an opportunity for simplification both technically, for example reducing Common Market Organisations from the existing 21 to just one encompassing them all, and with regards to policy. Greater simplification is also expected in relation to the current reforms on fruit and vegetables (fresh and processed), wine regulations, and in relation to cereal interventions and the simplification of the dairy sector.

53. The health-check needs to take into account the effects of decoupling which will start to become more apparent in the next few years; for instance has there been more land abandonment or reduced production where more extensive systems are being used? Will market forces, such as the increased development of biofuels from agricultural products, reverse this?

54. Many see the health-check as an opportunity to address distortions, whether real or perceived. Discrepancies have already developed whereby all land is eligible for the single payment in new member states, including woodland and forestry; in England, on the other hand, it is only related to some land, not woodland, orchards or vineyards. Other differences between member states include voluntary modulation.

55. In a fully decoupled CAP the retention of Set Aside land and Dairy Quotas also begs questions. Should these continue for another decade or be eliminated (as in the case of Set Aside) or phased out from 2008? The discussions over the future of set-aside are not

straightforward; particularly balancing the perceived environmental benefits of set-aside as advocated by NGOs, with allowing farmers the freedom to farm and convert this land to crops. This debate is particularly difficult to square if more land is needed to satisfy the demand for energy crops, whilst recognising that set aside land is not necessarily the most productive. What is the net advantage to biodiversity of set-aside, how detrimental to the environment and biodiversity would its removal be, and are there alternatives (such as agri-environment schemes) which could adequately compensate?

56. Some believe that to achieve a more uniform, simplified CAP deeper reform will be needed and that the “health-check” can and should achieve more. It is noted that the 2003 Mid-Term Review turned into more than a review leading to the most significant CAP reform to date. It may be hard to simplify what is now a very complex set of instruments with varying objectives.

57. European discussions around the CAP health-check will need to be set in the wider EU context of the 2008/9 review of all areas of EU spending; the review allows the European Council to take decisions on all subjects covered by the review and will be taken into account in the preparatory work of the Financial Perspectives from 2013-20 – thus covering CAP spending up to 2020. In the agreed 2007-13 Financial Perspective CAP funding is expected to be 34% of the overall EU budget¹⁵.

The future of the CAP - the ongoing debates

58. Looking to the 2013-20 period there are likely to be significant changes to the CAP, whether driven by financial or practical realities. There are a wide range of opinions about the future of the CAP and possible timescales for change. Some argue that the EU's model delivers a wider benefit to society that must be supported if agriculture is to have a future in the face of fierce global competition. Others counter that growing global demand will provide a secure future for European farming and competitiveness will not improve if the EU continues to provide some form of direct payment; that if any form of support is needed it should be more targeted to pay for the appearance of the countryside, improving diversity or environmental benefits. Some would argue that the EU should aim to move away from price support as an ineffective means of providing farm income support or supporting the multi-functionality of agriculture; and work towards more “Green box” support.

59. One option, recommended by some, is to phase out Pillar 1 payments, and transfer some of that support to Pillar 2. However, there is concern that by shifting environmental

¹⁵ €293.1 billion for agriculture under Pillar 1 and €69.75 billion for Rural development under Pillar 2.

payments to Pillar 2 the environmental and other welfare benefits currently secured through Pillar 1 and cross-compliance measures will be lost, particularly in larger-scale high-intensive agriculture. Many criticise this option of phasing out Pillar 1, believing that direct payments through such a mechanism are critical to ensure wider public benefits and enable European farming to meet high environmental and welfare standards across Europe. Land use is also likely to become more rather than less intensive under such an approach it is suggested. (However, intensive farming methods can also have good conservation practices). A proposed “exit strategy” from Pillar 1 payments is the development of a Bond scheme, capitalising ongoing historic payments. However, some think that such a scheme would impede any influence in favour of conservation and good farming practices as it would disconnect payments and the land and soil.

60. If Pillar 1 payments are to be retained in the medium or longer term how should this be organised? Are area payments the way forward for all EU member states as under the SAPS? If so, which land should be covered and what differentiations used? Some believe that capping levels of support in Pillar 1 should be the route to reduce overall CAP funding, though others argue that would add further market distortion. Others suggest that member states should co-finance Pillar 1 support as well as Pillar 2, or that more compulsory or voluntary modulation should be introduced to Pillar 1 (to date voluntary modulation has only been included in the UK).

61. Questions are asked about how common the EU policy can be in an EU of 27. As the major common policy for the European Union (alongside fisheries) there is likely to be strong political resistance to “renationalise” major aspects of agricultural policy. Co-financing, and regional payments could be a step towards re-nationalisation in another name, and some believe the CAP should continue in this direction. However, others question how equity can be ensured in policy support across a Europe of already diverging agriculture without defining common policies from Brussels.

62. Ultimately decisions on EU resource allocation will be taken by national politicians based on political imperatives, and whether they are net payers to the EU budget overall. This is not necessarily the best way forward for Europe’s agriculture. New member states are likely to play an important role in shaping the future policies. Although they currently account for only 10.6% of EU allocations they will have a greater voice in ongoing discussions.

Conclusions

63. Farmers will continue to become increasingly entrepreneurial, identifying niche markets, whether in specific added-value products, organic or larger scale production of commodities or in renewables. They are keen to be authors of their future. The key for them will be how they can ensure they are competitive whilst also delivering the “public goods” demanded in terms of landscape protection, environmental support or protectors of the natural habitat. Partnerships and contracts between farmers and the government, backed by the EU on behalf of taxpayers and society, will play an important role. However these need to allow farmers space to be entrepreneurs as well as stewards of the land.

64. It is suggested that the EU needs to distinguish clearly between policies supporting agriculture with those supporting rural development, the environment and land management. Changes to policies need to be carefully managed and appropriately timed and paced.

65. A common EU policy framework remains the ideal, but greater national or local focus to a range of policies and support mechanisms may become more appropriate in an EU of 27. Despite the challenges faced, the longer-term future looks brighter for Europe’s farmers and for agriculture given its strategic role. For many farmers now it is a question of surviving until that brighter outlook is achieved.

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