RELATIONS BETWEEN THE EUROPEAN UNION AND THE CENTRAL AND EASTERN EUROPEAN COUNTRIES IN MATTERS CONCERNING AGRICULTURE AND FOOD PRODUCTION

REPORT TO THE EUROPEAN COMMISSION

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SUMMARY AND CONCLUSIONS

At the end of several months of work we are in a position to propose, as a basis for further reflection by the EU authorities, a series of approaches which could become the broad lines of a policy for the Union in its relations with the CEEC on matters concerning agriculture and food production. Our general conclusions are as follows:

1) The steadily declining situation of agriculture in the CEEC cannot continue without some reaction by the EU. It is too dangerous for the stability of the CEEC and for the EU's relations with the various countries.

2) We are obliged to view the problem in macroeconomic terms. Without a globally healthy system of farm production, i.e. a system potentially capable of providing an income for the producers, all the different forms of aid and assistance will be merely palliative, and microeconomic decisions, however intelligent, will be doomed to fail.

3) We are convinced that the only effective way of improving the situation rapidly is to set up a system of price stabilization for agricultural commodities. Although such a system cannot be put in place immediately and in full, the legal and institutional infrastructure for it must be set up.

4) Without delay, the EU must set itself the objective of helping each of the CEEC - according to its level of development - to lay the foundations of an agricultural policy compatible with the reformed CAP.

5) To accomplish this work in preparation for the accession negotiations, the EU must define its doctrine rapidly and announce it; it must also provide itself with the necessary human and institutional resources.

The following report presents the analysis which led us to the above conclusions and proposes some concrete measures. The implementation of some of these can be decided by the Union itself.

The more concrete recommendations are as follows:

1) Measures are required to give assurances to agricultural producers that they will be recompensed for the inputs, such as fuel, machinery, fertilizers, seeds, herbicides/insecticides, which they must buy for normal production, along with a marginal compensation for their labour.

   It is suggested that these assurances can be given through a system of price supports at a low level. Emanating from this, a simplified system of EU levies and refunds for the CEEC, based on these price support levels, could be instituted. By making the EU levies equal to refunds, a form of common agricultural market would be formed which would recognize the differences in cost prices only through these levies and refunds.

2) Measures are required to liquefy the agricultural economy and to create markets in agricultural land in order to advance the gradual restructuring of agricultural production once it becomes potentially profitable. It is suggested that land can be used as collateral for loans through a "land bank". This "land bank" could also own land for resale, in order to regulate land prices and to promote the creation of viable production units. Such "land banks" could be created in cooperation with CEEC governments, the EBRD and the World Bank.

3) Measures are required to accompany a process of gradual convergence between agriculture in the EU and in the CEEC. These measures would aim, via the promotion of regular contacts between officials and professionals from both sides, to make effective use of trade opportunities and to eliminate unnecessary friction in areas such as veterinary and plant health matters. They would also encompass regular exchanges of views on market trends, on the working of the CAP and agricultural policies in the CEEC. Ways to enforce the contribution of the agricultural components of the PHARE programme to the process of gradual convergence should also be explored under this heading.

INTRODUCTION

Since the collapse of the controlled economies of Central and Eastern Europe the question of the EU's relations, now and in the future, with the former communist countries has become a focus of attention among the people and leaders of the EU and CEEC. The EU reacted rapidly to the situation in that, in the early stages, association agreements and aid programmes were proposed and launched, after which the prospect of the future participation of the CEEC in the EU was clearly stated. On 21 and 22 June 1993 the Heads of State and of Government meeting in Copenhagen issued the following statement:

> *"The European Council today agreed that the associated countries in Central and Eastern Europe[1] that so desire shall become members of the European Union. Accession will take place as soon as an associated country is able to assume the obligations of membership by satisfying the economic and political conditions required."*

This political objective was well received in the CEEC and has since constituted the main - in some cases the sole - plank of their foreign policies[2]. And there is no doubt that the prospect of the enlargement of the EU to several countries of Central and Eastern Europe which form an unquestionable and profound part of our common history offers great promise and hope for the future progress of our common enterprise.

For the executive authorities of the EU it is necessary to begin preparing now for this further enlargement of the Union to countries which are in transition between an administratively centralized economic system and a market economy, at a particularly difficult time for the system of international economic relations. The situation has no precedent from which to draw inspiration, and there is no theory to provide guidance for those actively involved. Automatic and dogmatic transposition of adjustment strategies has already shown its limitations and a pragmatic approach seems to be the only way. Step by step we must evolve practical responses to unforeseen or surprising developments. In the context of this approach, diagnosis is an important part of the reasoning process.

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1 *Bulgaria, Hungary, Poland, Romania, Czechoslovakia (today the Czech Republic and Slovak Republic)*

2 Hungary and Poland applied for membership on 1 April 1994 and 5 April 1994 respectively.

The following analysis of the present situation of farming in the CEEC is based on information collated from several souces: documents from international organizations (OECD, World Bank, European Union), numerous contacts with political and administrative authorities and researchers in the CEEC, conversations with specialists in DG I and DG VI and certain Member States, and, lastly, fact-finding tours in all the countries concerned.

I. SITUATION AND OUTLOOK

A. Some prejudices...

Whenever the subject of EU/CEEC relations in matters concerning farming and agricultural processing is raised it is quite clear that certain political leaders and most prominent representatives of the agricultural sector view the CEEC primarily as dangerous competitors for the protected farming sectors of the EU. This confused response springs first and foremost from past experience, when the countries referred to as the East-bloc countries regularly exported a few specific products[3] to the countries of the EU, and more recent memories when the beef herds in Poland and former East Germany were run down, giving rise to severe disturbances on the beef market of the EU, which is always in surplus and always fragile[4]. This standard attitude is reinforced by the widely held belief that the CEEC will keep trying indefinitely to supply the market with primary farm products and fairly simply produced food products for which they enjoy a comparatively advantageous position by virtue, in particular, of low labour costs[5].

This opinion, which naturally does nothing to dispel a somewhat cool attitude to the CEEC, can readily find justification in more scientific geographical and agronomic arguments: the EU and CEEC belong to the same large geographical area, where geological and climatological similarities are sufficiently numerous and pronounced as to give rise to identical, i.e. potentially competitive, agricultural enterprises. Cereals, milk, all types of meat, fruit, vegetables and wine, which are already produced abundantly or over-abundantly in the EU, are also the principal farm enterprises of the CEEC. The logical corollary of this is that complementary enterprises are few or non-existent. There can be no illusions in this respect : it is not the CEEC which will

3 cured meats, foie gras, certain fruits

4 This phenomenon, due to sudden partial destruction of beef herds, is no longer producing effects.

5 Article by Ulrich Koestler concerning the potentialities and handicaps of agricultural trade with the CEEC countries (Agrarwirtschaft 42 (1993), vol. 12, pp 429-436).

supply the EU with the plant protein it needs for its livestock sector. The agricultural industries of Western and Eastern Europe could therefore find themselves in competition on the already glutted markets for the main farm products. This hypothesis is all the more conceivable since the productive potential of Poland, Hungary, Bulgaria and Romania could make the area "one of the greatest exporters of the world"6. But potential can take a long time before it is realized: for instance, for more than a century, all the treatises on rural economics have cited Argentina as the great farming power of the future, given its exceptional "potential"7, but it is still not realized; cereals production has still not increased.

Realization of potential is not a technical matter as the agronomists and production engineers imagine, nor is it the result of an optimal mix of inputs as the economists make out; it is the outcome of a long and complex social process in which relations between the farming sector and the rest of society play a predominant role in raising agricultural production and productivity. The history of farming in Western Europe is a good illustration in this respect: the periods of growth of farm productivity coincide with the periods of industrialization, urbanization and capital accumulation in society as a whole.

From this point of view, the conditions for the realization of agricultural potential in the CEEC are not fulfilled, and there is every indication that it will be a slow process. The available figures, whose reliability depends on the quality of the data gathering systems concerned, show that agricultural production declined by at least 30%8 in all the relevant countries between 1988 and 1992. This decline is obviously linked to the comparable decline in consumption. The collapse of production is confirmed by certain realities observed at field level and we think that the considerable capacities for farm and food production in Poland, Hungary and Bulgaria in particular are lastingly impaired and that, for a fairly long time to come, it will be the farm and food products from the EU countries which may seriously disturb farming in the CEEC rather than the reverse.

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6 Ulrich Koestler, op.cit.

7 For instance, in "Agriculture dans l'évolution de la crise mondiale" (Paris Alcan 1933), it is pointed out "that Argentina can extract from its soil, whenever it so wishes, all the products of both tropical and temperate regions. It is a country with exceptional future potential".

8 OECD and EU series show that the average drop in production is 20-25% for cereals, but 40-45% for milk and meat.

B. Agriculture and agro-industries in deep crisis

The following analysis seems broadly valid for all six countries studied. There are nonetheless some very real differences in the history of agriculture, the structures of production and processing and the characteristics of the labour force in the various countries. The variable mix of these factors explains why the scale and form of the farming crisis is not the same in Poland as it is in Bulgaria. For instance, the agricultural markets and the way they operate will not be the same in a country with a large number of individual farmers who own their inputs as in a country where most production is in the hands of large-sized centralized production units. But despite these differences, which can only be examined systematically by individual monographs, the farming crisis shows common traits which can be identified in all the countries. The following phenomena are the main constant components of the crisis.

1. Trend towards farmland privatization

It is easy to understand the political obligation facing the CEEC leaders after the collapse of the communist regimes to declare their will to privatize State farms and cooperatives. This "agrarian reform" in reverse is being implemented differently in the various countries: extremely strictly in the Czech Republic, where former landowners can claim their full rights, with the result that a party of landowners has been formed and is represented in Parliament; in a disorderly fashion in Bulgaria, where, because of the lack of any recent land registry, the former cooperative members are sharing out land, infrastructure and livestock in an *ad hoc* way, and, when sharing cannot be organized easily, equipment is destroyed (irrigation systems) or abandoned (glasshouses); in a very complex fashion in Poland, where the State Agency responsible for privatizing State farms is marketing farm property very cautiously (10 000 ha a year) while a good number of cooperatives are transforming themselves into private companies with their old leaders still in managerial positions.

The process of land privatization, in its legal and practical aspects, is at different stages of advancement in the various countries, but it shows common traits throughout: the legal insecurity in which farm owners or tenants find themselves in the absence of almost any of the instruments needed for the management and recreation of private ownership; the lack of cash required for the transfer of a significant portion of the land, and the consequent lack of a land market; the extreme reluctance of the traditional managers of agriculture, government officials, researchers or farm managers, to destroy vast production units, some of which were far from bereft of technical rationality. For the time being, the only formula whereby State farms can be brought rapidly back into production is to rent them out, and some political and administrative leaders are wondering if this is not a suitable formula for the future. At all events, the hesitations and discussions suggest that land privatization will, for a fairly long time to come, cause instability and disorganization of production. There is no doubt that it is partly responsible for the general fall in production.

2. Disorganization and contraction of internal agricultural markets and breakdown of supply systems

The systems which used to supply the farm production sector with various types of inputs and those which placed farm products at the disposal of the population are all seriously impaired. Although the large production units still manage to obtain fertilizer and seed, admittedly in quantities far inferior to their requirements, and "commandeer" machinery and vehicles in the areas surrounding their place of operation, the individual farmers are all experiencing immense difficulties in obtaining the inputs they need, and in most cases cannot pay for in any case. Although the old systems of food distribution, often organized around the production units, were rigid and full of flaws, they still managed to provide the population as a whole with food rations of adequate quality and satisfactory quantity. Today they are in total disarray and have not yet been replaced by proper markets or modern methods of distribution.

This widespread disorganization of the upstream and downstream links of agricultural production is apparent in the least advanced countries of Central and Eastern Europe, but, even in the more advanced countries where the organization of supply used to be more or less satisfactory, the breakdown of the old system is so total that the networks are extremely disorganized.

And they too are affected by the market recession: the withdrawal of subsidies, the decline in the purchasing power of wage-earning urban populations[9], the rising prices of inputs combine to cause price increases in farm products, a contraction of demand which causes both a drop in production and a drop - sometimes very steep - in consumption[10]. For instance, it is estimated that per capita milk consumption in Slovakia has dropped by half since 1991.

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9 It is estimated that in the CEEC actual average national income per head has fallen by 20-25% from the maximum levels attained at the end of the 80s (cf "Le courrier des Pays de l'Est", No 383, October 1993).

10 Since 1989 the drop in per capita consumption is reported as between 40% in Romania and 10% in Poland (cf "Courrier des Pays de l'Est"). These figures are approximate and concern total consumption and standard of living.

The lack of any effective system for stabilizing farmgate prices - despite the existence of public or semi-public market support authorities in most of the countries - means that farm producers are unable to earn sufficient extra income to improve their methods of production[11]. We therefore witness a decline in production, a deterioration of quality and irregularities of supply on a patchwork of markets. In several countries and many regions the consumption of meat is a luxury no longer within everyone's reach. Finally, the arrival of processed farm products from EU countries on the markets of major cities has elbowed out local products: in Sofia there is more French cheese, Danish pork, Dutch tomato concentrate and Greek pasta than there is of equivalent Bulgarian products. In the Czech Republic, Hungary and Poland, the disorganization has facilitated the installation of foreign distributor chains, which naturally purvey products of EU origin. Two market situations are paradoxically superimposed on each other: the arrival of growing quantities of "western" goods to satisfy the demand of the better-off sections of the population, the decline of national production and the fall in food consumption by the sections of the population with falling incomes. This makes it more tempting for EU producers to export their surpluses at artificially low prices[12] to the depressed eastern markets. This shows how the EU could contribute "from the top" and "from the bottom" towards the deterioration of agricultural markets and the decline in production in the CEEC. This risk seems to be more than hypothetical and we therefore maintain that if it proves impossible to secure better market protection and growth of production by individual farmers or groups by ensuring price levels which permit investment as well as an adequate reward for labour, nothing will prevent a worsening of the crisis. There have already been drops in production in the order of 20-50%.

3. Loss of main external market

The former USSR was the main customer for the agricultural producers of the CEEC. The relations existing in the COMECON enabled Poland, Hungary and Bulgaria to supply farm products and processed products to their large neighbour in the East, often under a swap system whereby they received power, industrial products and capital goods in return. These flows have now been sharply and substantially reduced, and those that remain are organized through hidden channels or under conditions which destabilize the

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11 see below.

12 In January 1994 French pork producers called for another 100 000 t of production to be channelled to Eastern European countries with export subsidies (cf. Le Monde, 16-17 January 1994).

CEEC production systems still further. Poland, for instance, is regularly obliged to protect itself against the arrival of livestock products from Ukraine, sold at low prices to the great anger of Polish farmers' organizations.

As a result of the disorganization of the main external market for CEEC farmers, the almost mythical prospect of EU markets has assumed greater proportions in the eyes of the leaders and farm producers of the CEEC countries. It is true that exports of agricultural and processed farm products from the CEEC to the EU rose from ECU 1.65 billion in 1988 to ECU 2.51 billion in 1991, representing a 52% increase. But at the same time Community exports to the CEEC rose from ECU 0.71 billion to ECU 1.8 billion, which represents a growth of 167%. The EU therefore improved its trade balance from - ECU 0.95 billion in 1988 to - ECU 0.7 billion in 1991. In 1992 and 1993 the growth of EU exports continued, whereas CEEC exports fell, with the result that in 1993 the trade balance was positive for the EU13. These figures belie many prejudices and common assumptions. Contrary to the impressions of western agricultural leaders, the EU is improving its performance vis-à-vis the CEEC and "profiting" from the new situation. Similarly, and contrary to what is claimed by political and agricultural leaders in the CEEC, producers in the CEEC are selling more farm products in the EU than they did in the past. But it is equally true that the increase is far from offsetting the loss of the old Soviet market. Whence the dissatisfaction, or even anger, of CEEC leaders in the face of the difficulties they experience in increasing their exports to the EU and the bitterness they express as they realize that western outlets are not "drawing up" their production levels. This external factor, which is not likely to change significantly in the near future, combines with the disarray of the domestic markets to drag down production. Is there any way of helping the CEEC to regain at least some of the outlets that the former USSR once offered? This is a difficult question because of its monetary aspects, but it needs to be looked at.

4. Random process of modernization

We are convinced, like most specialists and observers, that the potential agronomic, geographical, technical and human capacities of the main farming countries of the area is significant. But they must be blended in an effective and productive way, in a process of modernization comparable to that which farming in the EU countries went through in the years following the second world war. The fact is, however, that the dramatic lack of cash, the disarray of industry, the shutdown of many undertakings supplying the inputs and equipment needed for modern farm production are combining to, at best, block production at its pre-1989 level, and, at worst, pull it into a downward spiral.

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13 Eurostat figures, cf. Annex 4.

This situation is clearly reflected in the declining level of mechanization of the old production structures. With the exception of a few cases, which seem mainly due to the installation of agribusinesses from EU countries having a spillover effect, in technical terms, on their productive environment, the global productivity of labour and management is at a standstill, or even declining.

The conditions for the beneficial knock-on effects of modernization, namely an expanding market, remunerative prices, growth of employment in non-agricultural sectors and cheap capital, are not met and there seem to be no immediate prospects of any notable improvement in productivity.

5. Inflation and agrimonetary problems

Inflation rates are generally high in the CEEC relative to the EU, with the current exception of the Czech Republic, but are quite different between the different countries. At some stage, a higher inflation rate in country A as compared to country B will lead to a depreciation of the currency of country A relative to the currency of country B. Such a depreciation or currency devaluation becomes necessary when the overvaluation of the local currency to other currencies cheapens import prices and increases export prices to an extent that the economy of country A becomes uncompetitive and its balance of payments deficit mounts.

Subsequent to a devaluation of its currency, the government of the country in question will try to keep down domestic wages and prices of domestic production. Otherwise the positive economic effect of the devaluation will be lost quickly. This applies especially to the prices of foods which can be considered as essentials. As far as cereals and oilseeds are concerned price ceilings below certain levels can be counterproductive in that production can thereby be decreased below required levels.

Cost prices of cereals consist of a number of cost categories. These cost categories include land, labour, taxes, machinery, seed, fertilizer, insecticide, herbicide and fuel. All this adds up to a cost price in the order of 140–200 dollars per ton of grain in the EU, depending on the scale of production. In this cost price there is a "hard core" of expenses which must be covered in order for a farmer to continue production[14]. This "hard core" of expenses includes "bought" inputs of fuel, some machinery, fertilizers, herbicides and pesticides, as well as the labour cost per man, on the basis of the minimum effective wage cost applicable locally.

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14 "Hard core" production costs do not include: return on capital cost of land rent, return and depreciation on capital employed in buildings, machinery, and stocks, the difference between "normal" labour cost and the "minimum" labour cost calculated in the "hard core" production costs. An estimate of these additional costs, expressed on the basis of the production of one ton of cereals, would be 50-75 dollars in the EU and 30-40 dollars in the CEEC(PECO).

"Bought" inputs are largely priced internationally and consequently have very similar costs everywhere. Assuming relatively normal inputs and input costs with relatively normal yields, the "hard core" costs based on small scale production in the CEEC would split up into 25 dollars per ton of cereals for labour and 50-60 dollars per ton for "bought" inputs, giving a total of 75-85 dollars per ton. For small scale production on average in the EU, "hard core" costs would be in the order of 60-70 dollars per ton for labour and 60 dollars per ton for "bought" inputs, giving a total of 120-130 dollars per ton. (On a scale of production of 100-150 hectares, "hard core" costs in the EU would decline to 20-25 dollars per ton for labour and 60 dollars per ton for "bought" inputs or 80-85 dollars per ton in total).

In the EU, because of the complicated agrimonetary system invented in the framework of the CAP, a devaluation of a currency of a member country relative to the "strong" currency almost immediately results in an increase in agricultural prices in the devaluing country to the extent of the devaluation. This process leads to windfall profits for producers in devaluing member countries who are compensated for non–occurring increases in a number of costs such as land, labour, and machinery. Even if some of these costs increased, they would be increased with a time-lag and certainly not prior to the subsequent crop year.

However, in the case of the CEEC, actual prices are mainly already at, or below, "hard core" cost prices which must be expressed in dollars or ecu. If prices in local currencies are not increased by the percentage of the devaluation, they will not cover "hard core" costs and production will decline subsequently. With all renewable resources, such as cereals, producers are at the mercy of the markets once crops are planted. Producers consequently usually consider replacement prices relative to actual cost at the time of the start of production. If a devaluation occurs during a crop year, it may not be necessary to compensate producers provided it is certain that compensation will be made for devaluations affecting the crop to be harvested in the subsequent crop year.

It must be recognized that prices for agricultural products in the CEEC generally are at present at levels which induce reduction of production. Further reductions in these prices in dollar or ecu terms (due to currency devaluations) may cause situations as in Argentina after 1955 where producers turned to a survival strategy of the lowest production at the lowest cost. Once producers lose confidence and turn to such a strategy, it becomes extremely difficult to restore confidence and to induce a return to normal agricultural production.

C. Priority: to end the crisis

In view of the foregoing, there is nothing in the general economic situation of the CEEC or in the particular situation of the agricultural industry to indicate that their production and export capacities will improve to any significant degree in the near future. On the contrary, a steady deterioration in production systems and a deepening of the agricultural crisis, with all its attendant economic, social and political consequences, are to be feared.

It is true that the picture is not uniform for all countries: Poland and Hungary are in relatively better positions than Slovakia and, above all, Bulgaria and Romania, but the syndrome is the same throughout: not only do the agricultural and food processing industries fail to contribute, as might be hoped, to overall economic growth, but, on the contrary, their disarray could drag several countries in the area into unpredictable and dramatic social upheavals. This prospect is neither morally acceptable nor compatible with the political interests of the European Union. The EU must face this major crisis with lucidity and take what steps it can, without delay, to prevent its aggravation, even if the eventual consequences of such a courageous policy are sharper competition and increased tension within the framework of the CAP.

This conviction is founded on straightforward historical and geopolitical realities. The farming and food processing sectors are decisively important for all the CEEC, with the exception perhaps of the Czech Republic. They provide jobs for large numbers of workers who are unable to find other work and their contribution to national wealth is three to four times greater than that of western agricultural industries. There can be no transition to a balanced market economy capable of association with the EU economies without an agricultural and farm processing economy which is also associated with the farming sectors of the EU in a wider context, whatever the nature and degree of integration. The corollary of this reasoning is that, with a view to enlargement, the EU must make it a priority to help the CEEC agricultural industries to recover. As regards the competition which these industries will one day present for the protected farming industries of the EU, it is relevant to point out that all the agricultural industries of the EU countries made prodigious progress in terms of productivity as soon as they were brought into ... competition with each other!

It would naturally be unrealistic to nourish the illusion, either inside or outside the EU, that the Union could itself organize such a recovery, for instance by opening up its markets, as if the causes of the crisis in the CEEC were essentially external. In particular, it is clear that as long as the production of basic farm products fails to pay for the inputs, any policy of recovery is doomed. But the EU can contribute powerfully to the success of a recovery policy by refraining from any action which would be counter to the major objective of stabilizing production, and by taking a series of initiatives which could provide some of the means of stabilization which are lacking at present.

II. AGRICULTURAL POLICY RECOMMENDATIONS

A. Stabilization of prices of agricultural production

The total volume of consumption of food depends on the evolution of purchasing power. The sharp reduction of purchasing power of the populations in the CEEC has caused surprisingly large reductions in food consumption during the last three years. Production has also gone down, in some cases to an extent that prices for certain food products in certain CEEC have become extremely unstable. Examples are the price of pork in Slovakia, which more than doubled between June and October 1993 and the price of wheat in Hungary which doubled between August and October 1993.

In both cases the prices from which the price advances started were very unremunerative to producers, but the higher October prices were far above cost prices. In the case of the wheat price evolution in Hungary, most producers could not hold back their wheat to wait for remunerative prices and the price rise served to benefit mostly others than producers.

In the present situation, prices for agricultural products in the CEEC are generally so low and unstable that producers cannot count on being remunerated for their cost of production. As indicated earlier, this will lead to further reductions in production and to a loss of confidence in the profit potential of normal agricultural production which will be difficult to reverse.

It seems evident that CEEC agricultural producers must be given the firm prospect of potentially remunerative production in order to induce them to continue, or return to, normal economic production. The only practical way to achieve this would be some form of stabilization of agricultural prices above the level of the "hard core" of production costs.

1. Free market approaches

Ideally, agricultural production should always be conducted competitively, allowing comparative advantage to determine the pattern of this production. In such circumstances, the CEEC could have a structural advantage for primary agricultural production relative to developed countries such as those in the EU. This approach would have the advantage not only of lightening the CEEC public spending budgets considerably, as they would not be obliged to finance support systems, but also of making it easier for the CEEC to find international outlets at world market prices.

However, the CEEC currently have substantial disadvantages in their own economic structures and in relation to competition from subsidized primary agricultural exports by the EU, the USA, and other developed agricultural producers.

Internal agricultural market structures in the CEEC

While the CEEC can produce primary agricultural products at prices comparable to the subsidized prices of exports from the EU and the USA, their storage, logistics, and marketing capacity are extremely deficient. In the former political configuration, products were basically continuously dispatched to the former Soviet Union. State trading organizations which might have provided marketing and logistic capacity have largely been dismantled. It will take time, incentives and money to create a viable trading and distribution system for export as well as for internal marketing.

Meantime, several CEEC governments (Poland, Slovakia, Romania) have already established price supports for cereals and milk production. In some cases, the levels of these price supports are higher than required for this purpose. The excessively high price levels could however easily be corrected through depreciation of most CEEC currencies. But it will be difficult to dissuade CEEC governments from using price support systems in view of their desire to emulate Western agricultural systems. It has to be borne in mind that with the exception of New Zealand no other developed country in the world does without some form of direct or indirect price support mechanisms.

The reflections on a liberal system of primary agricultural production should also take account of the following: since it is probable in the foreseeable future that, in one or all categories of agricultural production in the CEEC, production will decline to below the level of local demand during a crop year, prices should normally respond upward for the agricultural production so affected. This might be true to some extent but the fact is that producers are short of money and will sell their production quickly after harvest. In an illiquid economy, this will push prices down. Shortages of production will be recognized later and consequent price increases will probably only benefit a few producers who have held on to their production. Governments will probably encourage imports if prices rise, in order to push prices down. Under normal circumstances, a typical response to temporary oversupply of grain at harvest time would be to stimulate exports in some form. But given the particular conditions of the countries concerned, this would not give any certainty of selling product at the required time. In fact, the situation is that at harvest time (July/August) export possibilities tend to be limited and prices are usually rather depressed. Moreover, if there is an overall production shortfall, later in the year such a policy could require more costly imports.

There is a risk, therefore, that a free market approach would fail to provide an adequate response to the basic question of getting farm production started again in the CEEC.

Competition with primary agricultural products on world markets.

Potential exploitation of their basic comparative advantage in the production of primary agricultural products by the CEEC has to be evaluated bearing in mind both the economic and the political feasibility of such an approach.

As far as the former is concerned, the observations relating the internal structures in the CEEC are of course relevant. Another, external, factor has to be mentioned. The major exporting powers like the USA and the EU, apart from subsidizing primary agricultural products on world markets, employ credits, tied food grants and food aid to promote their exports.

These latter secondary sales devices are not, and will not be, available to the CEEC. The absence of appropriate marketing structures and the lack of capacity to use sophisticated marketing devices will severely handicap, at least initially, the CEEC's ability to exploit their basic comparative advantage in the production of primary agricultural products.

Another important point must be made in this respect. A system founded on the free play of market forces, within the context of the prospective accession of the CEEC to the EU, is conceivable only if it is accompanied by the dismantling, on the EU side, of export refunds, and the renunciation, on the CEEC side, of external protection for their markets and internal support for their farming industries. Such an approach would risk incurring a virulent reaction in the farming world in the EU, but also in the CEEC, and could jeopardize the accession of the CEEC.

2. Price support approach

Only if a government can state at planting time that the price of the grain or other agriculture product at harvest time will be guaranteed to be somewhat (barely) remunerative, is it likely that sufficient producer confidence can be generated to continue normal production at currently foreseeable price levels. This would mean a system of price supports for primary agricultural production, namely cereals, probably milk and sugar, possibly meat and oilseeds.

The EU has ample experience with such programmes (and the mistakes which can be made in their design and execution). Consequently, it could contribute knowhow/personnel to stabilization efforts, if required.

The levels of the price supports will be important. If too low (below the "hard core" production costs) price supports could be close to useless; if too high, they might create a situation similar to the one encountered in the EU where production is geared to intervention rather than markets.

The level at which CEEC price supports are started is of vital importance since it will form the base from which the supports will evolve.

At the outset of the PAC, for reasons of political expediency, Dr Mansholt accepted agricultural price levels which were much too high economically. He hoped and expected that these price levels would be reduced by market forces in a relatively short time span. Instead, it took 30 years of price distortion in agriculture before a start was made with such downward price adjustments.

Since the "hard core" production costs are mainly in materials that are traded internationally, the price support levels at the start of a crop year would best be denominated in dollars or ecu and subsequently in the local currency equivalent of the dollar price support. The cost prices of agricultural products in the CEEC are remarkably similar in dollar/ecu terms. After the start of a crop year, it would be possible to leave the intervention prices in local currencies unchanged for the course of the crop year, provided the new intervention prices for the following crop year were announced in a timely fashion based on cost prices in dollars/ecu.

Import and export systems are a natural complement to internal price support systems. They should be coordinated between the EU and the CEEC so as to prevent further distortions.

The current agreement between the CEEC and the EU has not had the positive effect on exports to the EU from the CEEC that these countries had hoped for. Exports of agricultural products to the EU have increased a little while (subsidized) exports from the EU to the CEEC have increased sharply. The general sentiment in the CEEC is that the agreement is unfavourable for them. This has created a great deal of bitterness in CEEC circles, whether justified or not, as indicated above.

As from now, efforts should be made to evolve the export–import relationship in agricultural products between EU and CEEC towards a constructive partnership with the aim of restoring CEEC agriculture to a healthy footing by supporting attempts to stabilize agricultural prices in the CEEC.

Levy-free quotas for imports into the EU from CEEC and credits granted by the EU for export of agriculture products from CEEC to the former Soviet Union, or to other importers, do not bring structural solutions for CEEC agricultural marketing problems. Moreover, these "facilities" are extremely difficult to administer in the absence of a central marketing agency in each CEEC. The question as to who will benefit from these "facilities" in the CEEC (and in the EU) cannot be decided objectively. Consequently, substantial economic/financial benefits inherent in these "facilities" are allocated in an arbitrary fashion.

Quotas with preferential treatment of tariffs or levies on imports into the EU are economically inefficient. There is a tendency to fill these quotas regardless of the economics involved, since otherwise another market participant might benefit. Since there is no quick information available on whether a quota has already been filled, an importer will tend to act to safeguard himself from the risk that he may have to pay the tariff or levy applicable to transactions outside the quota. In practice, importers into the EU will tend to capture the benefits intended for exporters to the EU in the CEEC.

EU import levies on CEEC primary products like cereals should be lowered to allow the CEEC to export to the EU in the event of local price declines below support prices. This would give a great deal of credibility to local price support actions and generally have a positive psychological effect. In practice, the quantities which could be available for export to the EU would be limited. It might be advisable in this context to introduce a monitoring system of mutual trade flows.

EU import levies on CEEC consumer foods should allow imports of these products into the EU while EU export refunds on consumer foods to the CEEC should not be such as to take away local markets from local production. A restrictive system of quotas is an effective way to throttle market development.

One approach would be to recognize the cost price differences between CEEC and EU primary agricultural products and to extrapolate from these differences the cost price differences between consumer products in a limited number of categories and then to use these price differences, adjusted for transportation costs, both as EU levies and refunds when importing from, or exporting to, the CEEC. The money that the EU would collect on levies and save on export refunds, compared with the export refunds normally granted, could in fact facilitate the granting of financial assistance to the CEEC.

Obviously such an approach is of an innovative nature and needs to be examined carefully in all its aspects: management, financing, compatibility with GATT. GATT regulations are unlikely to prohibit EU involvement in CEEC price support operations or in the setting up of land banks. However the proposed system of EU import levies and export refunds is philosophically different from the current system of EU levies and export refunds. This could create problems in GATT where other countries could claim the right to equal treatment[15].

Feasibility of the system

We are aware of the manifold difficulties our proposal will face, and we know it runs counter to many suggestions proffered to the Central and Eastern European countries in the past four years. The change of approach therefore requires, on the part of EU leaders, the political courage to affirm a voluntarist objective, both vis-à-vis their

15 See in Annex 1 an illustration of how such a price support system could function.

counterparts in the West - especially the USA - and vis-à-vis their counterparts in Central and Eastern Europe, who, while appealing for a clear position on the part of the Union, still harbour numerous illusions as to its possible content.

Furthermore, the implementation of this system of stabilization will have to overcome some real difficulties. The first stems from the diversity of situations of the farming industries in the CEEC and the different levels of development attained. Must the system be the same throughout? Is that necessary? Is it feasible? We have already addressed this question in the context of our general diagnosis, and we think the answer is still the same: despite the geographical, historical and organizational differences, the farming industries of the CEEC are going through a crisis whose main features are so similar in the various countries that the remedies can hardly be very different. It is just as urgently necessary to stabilize the prices paid to producers in Poland as it is in Romania. Moreover, an identical price stabilization system in all the CEEC will have the advantage of encouraging trade between them and inducing them to adopt similar agricultural policies. It will function as it has done in Western Europe, where the differences between farming systems are easily as great as they are in the CEEC, by drawing together the markets and standardizing practices.

The second difficulty stems from the fact that such a system entails rising budget costs. The sums to be mobilized in order to stabilize the key products remain acceptable, but it is easy to imagine the pressures that the farming world will put on the decision-makers in order to raise the level of guarantee. The only response to this risk is to lock the system <u>before</u> it starts to function, by fixing budget envelopes in advance and defining clearly the decision-making procedures for changes to the guarantee levels. It is the lack of any limit on the CAP mechanisms which has caused it to drift off course, not the mechanisms themselves.

A third difficulty stems from the GATT agreements. Is the system as described above compatible with the rules recently adopted, which will be applied within the framework of the WTO. The elements of the proposed system are different and do not have the same purpose as the old levy/refund system applied in the EU. Nevertheless, some third countries could legitimately ask to benefit from such a system, in the name of fair treatment and equality. But there is one possible solution to this, which calls for more detailed exploration, namely to get the international community to recognize the particular status and limited duration of the proposed stabilization mechanism: it is to be a transitional system, specific to the phase preceding accession, and intended to enable the CEEC to halt the decline of their farming industries and prepare themselves in the best conditions for their subsequent adherence to the rules - now recognized- of the reformed CAP.

These difficulties are undeniable but surely not insurmountable. We think things should be set in train without delay to make the implementation of the stabilization policy feasible, for it seems to us essential if further enlargement is to be achieved in good conditions for the EU and CEEC. If nothing is put in place in the near future, the social and political tensions already apparent among EU farmers and the bitter disillusionment of farmers in the CEEC will become more acute and risk leading to deadlock situations, or even eruptions of discontent. It is high time to propose that CEEC farmers embark on the path that will lead them progressively towards their fellow farmers in the West.

B. The development of a sound agricultural credit system

The setting up of a price stabilization system is a prerequisite of any recovery of agriculture in the CEEC. It alone will prevent farmers from going bankrupt. Once the system is in place, it will be necessary to turn to other crucial reform measures to enable CEEC farmers to develop and modernize their production. In this respect, the establishment of a sound agricultural credit system has to be given high priority because it will allow the restructuring of CEEC agriculture (impact on scale of production and creation of liquid assets).

The current tendencies are to fragment land ownership into units which are uneconomic for modern agriculture. In Poland 70% of the land was already owned and operated in very small scale units while in most other CEEC privatization also seems to be leading back to ownership as existed 50 years ago, largely in small lots.

In order to restructure agriculture into economically more viable units, it will be necessary to give land some reasonable value for sale and/or rent. Generally, in loss–making agriculture the value of land is small, especially where there exists on overhang of land waiting to be privatized. This is further compounded by the general lack of credit in the CEEC economies.

Credit problems in all these countries are aggravated by the fact that there is no legal framework for collecting debt and forcing companies and individuals into bankruptcy in the case of non-payment.

This is creating domino debt default situations whereby enterprises cannot pay their creditors because they are not being paid by their debtors.

Since in some areas more than 50% of agricultural producers and agro–industries seem to be insolvent and not paying on debt, governments are understandably reluctant to force all these people into bankruptcy even if a legal procedure allowing this did exist. All these countries lack a system of rural banks which might be able to police a system of input credits.

In these circumstances, land would seem to be the only viable collateral for agricultural credit. In order to realize land as collateral for credit a number of pre–conditions should be met.

Ownership rights should be clear, there should be legal means by which to take over collateralized land in case of non–payment, and, most important of all, there should be a liquid market for land. This is not now the case.

These preconditions are so important for the proper functioning of the agricultural structures that they should have a high degree of priority in discussions between the EU and the CEEC.

Current value of farmland in most CEEC lies around USD 200–300/hectare, but very little land is bought and sold. Even in remote South American areas, the value of land of lesser productive potential than in CEEC has a current market value of USD 750/hectare.

As an adjunct to price support for production, CEEC require a system to support land prices and to liquify the land market in such a way that there can be a gradual evolution to production units of an economic scale. Possibly even more important is that in this way the value of land can be mobilized as collateral for essential credits to agricultural producers.

While the organizations in the different CEEC engaged in the privatization of public land could be transformed into instruments to manage the purchase and sale of farmland and so establish clearing prices for land, it might be more expedient to start up new "land bank" entities in order to obtain private foreign finance.

The establishment of "land banks" should be examined in each CEEC, in combinations between private investors, local governments, EBRD, World Bank, and EU. These "land banks" would attempt to liquify the market for land by buying and selling land, also taking account of the desirability of establishing an economic scale of production (see in Annex II an example of how land banks could operate).

III. FLANKING MEASURES

Introduction

The foregoing pages, which concern price stabilization and credit systems, present the core of our proposals, the essential content of an agricultural policy which seems to us appropriate to the present situation prior to enlargement. Its adoption and implementation depend on the reception it receives from the Commission, the latter's willingness to propose clear and precise objectives to the CEEc on matters of agricultural policy, the reactions of the Member States, which may have contradictory but equally strong reasons for putting up with the present crisis, and, finally, the reception the proposals receive from the leaders of the CEEC.

However, without waiting for each and everyone to agree on the proposals, if it is thought they have any chance of being implemented in the manner described above or in a similar manner, it would be desirable and effective to reflect as from now upon the ways and means of applying this policy in preparation for enlargement and to explore the possible "flanking measures" which can, in most cases, be decided unilaterally by the EU in order to facilitate the gradual convergence of the agricultural policies of the Union and the CEEC.

This forward-looking attitude no doubt pre-supposes that the destination is clearly defined, if not yet decided, and that the agricultural industries of the CEEC are fully familiar to the officials and decision-makers of the EU. This is essential. For instance, how can an in-depth reform of the market regime for beef be prepared without due regard for the fact that, in a few years' time, the Polish and Hungarian beef producers will take part in the regime?

The flanking measures which we propose for immediate implementation are intended to induce the people involved to work towards rapprochement, to discuss and compare their instruments and practices, for the explicit purpose of being in a position, in a few years' time, to operate the same mechanisms.

A. Reinforcement of economic and human links

If we accept that on either side there is a need to make up considerable ground in terms of mutual knowledge, the EU must make rapid preparations to introduce itself and its ideas to its CEEC partners, while at the same time improving its own knowledge and understanding of Central and Eastern Europe.

With regard to the agricultural sector, the EU could negotiate soon with the governments of the CEEC to initiate two types of action: the first would consist in training some high-level officials and farming leaders in the technical mechanisms and development of the CAP, the second, equally important, would consist in trying to inform a more extensive audience of agricultural professionals about the realities and myths of the CAP. If this work is not undertaken very soon, in a systematic way, the EU will experience great difficulties during the negotiations and will run major risks of political misunderstanding because ignorance about the real nature of the CAP seems to be severe and widespread.

The EU will have to bear this in mind if it is to proceed fruitfully with negotiations with the CEEC. These will require more structured and intensive personal contacts between the EU and CEEC, governments and officials, than was necessary in previous contacts and negotiations concerning the possible access of western countries.

It is consequently recommended that the EU should organize a small group of experts in agriculture, dedicated to the question of cooperation with the official bodies in the CEEC.

However, even if the group is composed of highly qualified persons, it cannot take the place of the real leaders of the EU responsible for determining, expressing and monitoring the policy of the Union in this matter. A steering group for our agricultural relations with the CEEC must also be set up. It is not for us to suggest who should be in charge of this dossier, but it seems necessary and urgent to designate a "top person" to report to the Commission and possibly also to the Council of Ministers.

Apart from a small support group in Brussels, this official should have agricultural "residents" in each CEEC at his disposal. These local "residents" should be capable of having constructive contacts with local ministries of agriculture and should be able to supervise PHARE activities. They should be primarily responsible to the Brussels official indicated above, but will have delegated responsibility in the country to which they are assigned. Together with the small coordinating group in Brussels, the "EU agricultural residents or attachés" would constitute the EU agricultural support and management team for the CEEC.

These contacts and the confirmed presence of the EU in the CEEC seem essential if enlargement is to be prepared in the best possible conditions.

B. <u>Towards improved effectiveness of PHARE in the process of convergence</u>

The concept of PHARE is noble and idealistic. With the experience gained since its inception, it should be possible to make this concept correspond to the goal of giving recipient countries a maximum of effective structural economic assistance.

The EU should formulate clear longer-term goals for this assistance. These goals, and the priorities within these goals, will require political decision which can only be taken at the political level. Leaving initiatives in relation to PHARE Agriculture to the somewhat nebulous PHARE organizations at ministries in recipient countries is putting rather too much responsibility on these structures than can currently be managed usefully.

Projects undertaken in the recipient countries should fit into the clear longer-term political orientation of PHARE Agriculture, and the resulting priorities, suggested above. If at all possible, PHARE Agriculture projects should initially be rather "concrete" with a finite time horizon. Projects undertaken in any one recipient country should be limited in number at any time in order to ensure that these projects are "followed up" carefully and efficiently by the proposed local agricultural "residents". The initiation of a great number of small and somewhat indeterminate projects should be avoided. Moving from the accomplishment/completion of one project to the start of another, building on the experience gained previously, would seem to be the way to move in PHARE agricultural projects.

Contrary to the experience of the EU in previous accessions, it must be recognized that in proceedings with the CEEC it cannot be assumed that counterparts in these countries will understand what EU officials want to convey, and vice versa. The working of CEEC governmental structures is not apparent to EU eyes at first sight, just as the workings of the EU systems are not transparent to CEEC officials. In the context of PHARE Agriculture, this means that the contacts between the EU and the individual CEEC must be intensified locally through the activities of the proposed agricultural "residents" in relation to the PHARE counterparts in these countries.

The responsibility for the overall orientation of PHARE Agriculture, the responsibility for the priorities set in this orientation, and the responsibility for the individual projects, should be allocated and should be recognized and understood by all those involved with the overall PHARE Agriculture program.

C. Managing gradual development toward convergence of agricultural policies

The current status of the association agreements is not considered to be satisfactory by any of the CEEC governments which complain about bureaucratic complications with the EU as well as about the negative evolution of their agricultural balance of trade with the EU.

As suggested above, it seems advisable for the EU to organize a small body to coordinate contacts with the CEEC. Under the auspices of this body, regular monthly market management meetings should be held between experts of the EU and the CEEC concerning three fields of agricultural exchanges:

1. internal market evolution (prices, supply demand)
2. trade development (volumes, tariffs and refunds)
3. veterinary/plant health matters.

These market management meetings could recommend overriding quotas of the association agreement if they were unnecessarily restrictive. On the other hand they would monitor trade volumes and prices in such a way that disruptive trade flows could be limited. They could recommend adjusting levies and refunds when so required. No unilateral veterinary/plant health measures would be taken without prior consultations in these meetings.

It is hoped that, out of these meetings and contacts, initiatives will be developed for further coordination of agricultural policies in time. Since many bilateral contacts between the EU and the CEEC will be maintained and serviced by the new form of EU "agricultural attachés" or "residents" in the different CEEC, it would be useful for these "residents" to attend these monthly meetings at least once every three months, but potentially more frequently.

It will be vital to ensure that the officials attending these meetings on behalf of the EU and CEEC are actually responsible in their home territories for the matters that will be discussed in these meetings.

Through these procedures, the adhesion process would be made both more flexible and more pragmatic. Officials from the CEEC would become better acquainted with EU procedures and officials from the EU would become acquainted with the problems in the CEEC.

Consideration must also be given to the setting-up of an EU inspection group to help the CEEC with the supervision and control of tariffed or subsidized trade flows and possible intervention stocks in connection with the EU.

The foregoing suggestions, concerning trade, the PHARE programme and contacts between people, all spring from a single proposal: after the period of surprise, observation and benign abstention vis-à-vis the CEEC and their agricultural industries, the time has come for the EU to act and assume responsibility. It must define its objectives, announce its will to achieve them and provide itself with the requisite means, while bearing in mind all the various changes it will have to effect by the time 22 countries are involved in the common agricultural policy. One difficult and disturbing problem suffices to illustrate our position: we know that financial, veterinary and other checks have become a crucial factor of the CAP. How will they be organized in the CEEC, with all the difficulties they will face, when the countries have neither the facilities nor the personnel capable of carrying them out properly? Should this aspect be analysed and resolved before enlargement?

CONCLUSION

The enlargement of the Union to include the CEEC will undoubtedly be an extremely difficult operation: it concerns six countries with different histories, languages and structures, whose levels of economic and social development are also different and all distinctly below the levels attained in the western part of Europe. When the time comes for accession, the CEEC will be far from completing their uneasy transition from centralized economies to a market economy. What is more, the new enlargement will be prepared during a particularly unfavourable period, marked by a general economic recession which, among the peoples of western countries and the CEEC, nourishes the worst kind of nationalist, protectionist and xenophobic fantasies.

In the face of this accumulation of all types of difficulty, the path open to the Commission for implementing the conclusions of the European Council in June 1993 is obviously narrow and steep: it must propose clear and strong negotiating objectives, capable of reassuring the present Member States and public opinion therein about the short-term effects of the next enlargement, while also convincing the leaders and peoples of the CEEC of the will of the European Union to create, with them, a new common area, a "greater Europe". The conception, definition and implementation of such a project are all the more urgent now as public opinion will be more vigilant than ever before.

Against this general background we decided to make our report brief but outspoken so that it is thought-provoking and conducive to discussion.

The proposals in the report rest entirely on the idea that the EU countries and the CEEC all have a major interest in working for the convergence of their economic, social and political systems, without thereby renouncing or overriding their respective specificities. There are definite advantages to choosing the agricultural sector with which to embark on the process of convergence, which will be necessarily long and marked by crises and setbacks. One advantage is that although agriculture contributes only a small fraction of GDP it remains of strategic importance for the food supply of the nations concerned and for the occupation of the land. Furthermore, the CAP has given the EU a unique experience in the management of a process of convergence, with all its attendant difficulties, mistakes and benefits.

It should be possible for the proposals in this report to be taken up without delay to generate a process of convergence: farmers in the CEEC will organize themselves progressively along lines similar to those applied under the CAP, seeking to retain the best and reject the worst, while the EU will, while opening itself to new members, pursue its efforts to lighten and improve the instruments of the CAP, the two movements drawing strength from each other.

This rapprochement presupposes that national farm policies are non-conflicting and compatible with the reformed CAP. In other words there must be an institutional system capable of inspiring, administering and monitoring a new and more extensive CAP. There can be no convergence without common procedures and verifications, given that, in the farming sector as elsewhere, the "invisible hand" of the market cannot regulate everything.

The convergence must therefore be organized in a system of management covering more than 20 Member States. It is obvious for everyone who has had any part in decision-making under the CAP that the present institutional system will be incapable of functioning with more than 20 countries and that paralysis will swiftly set in. Enlargement of the EU to include the Scandinavian countries and Austria is already showing how very hard it is for the EU to take in new members and to remain a true community without modifying the way its institutions operate. It is therefore clear that, if the problem is not addressed before the accession of the CEEC, the EU will be unable to operate as a system of convergence of national areas.

We have neither the brief nor the specific competence to make proposals about institutional aspects. But we know that the ordinary decisions required for the day-to-day operation of the CAP have to be taken fast and, where possible, taking due account of a rational analysis of market data, budget possibilities and common interests. This is unfeasible in a Council comprising more than 20 members. But that is another matter...

ANNEX I

Example of a price support system for CEEC cereals

It is suggested that the level of price support for cereals in the CEEC/ should be based on "hard core" costs as indicated in I–B5 and have the form of a saftey net rather than a commercial price level.

The starting point of the price support system would be the price level in local currency for a crop year. It is suggested that this price level should be the local currency equivalent of a dollar price at the start of a crop year and that this local currency price would not be changed during the course of that crop year. At the start of the following crop year in principle the same dollar price could be utilized, converted to the local currency at the exchange rate than prevailing. This could give the following schematic evolution of levels of price support in a country.

Exchange rate to dollar of currency A on 1 July 1993 = 40 to 1 dollar.

Price support level for 93/94 crop year 85 dollars per ton = 3400 per ton in local currency A.

Exchange rate to dollar of currency A on 1 July 1994 = 48 to 1 dollar.
Price support level for 94/95 crop year 85 dollars per ton = 4080 per ton in local currency A.

The EU could consider changing its system of tariffs at import, and refunds at export, on agricultural products for the CEEC to reflect only the difference in production costs between the CEEC and the EU as reflected in the levels of direct price support. EU refunds would then become the mirror images of EU tariffs in relation with the CEEC. EU tariffs or refunds for other agricultural products could be derived from the EU tariffs or refunds for cereals through coefficients. It would be possible to take account of freight expenses from CEEC to the EU, probably Germany, but this could affect the symmetry between tariffs and refunds. Tariffs and refunds under such a system would only apply on the date of import into the EU c.q. export from the EU and not be fixable ahead.

While such a system would be very straightforward in principle, changes in exchange rates in the different CEEC would have to be catered for in the execution of such a system. As indicated above, support prices in local currencies would not change during a crop year from prices converted from dollar prices at the start of the crop year. Adjustments in EU tariffs and refunds following changes in exchange rates could take place as follows:

Cereals support price country A = USD 85 = ECU 62/ton = 3400 local currency
EU cereals support price = ECU 100/ton
Consequently tariff and refund could be ECU 38/ton (100*62)

Currency country A devalues by 10%, which cause currency A to change from 40 = 1 dollar to 44 = 1 dollar
Support price continues at 3400 in local currency of country A.
This support price is then equivalent to USD 77.25 or ECU 56.40.
The tariff and refund would then go up to ECU 43.60 subsequent to the devaluation (100*56.40).

In case of further devaluation during that crop year to 48 = 1 dollar, the dollar equivalent of the 3400 support price would be ECU 70.80 or 51.70.
The tariff and refund would then become ECU 48.30 (100*51.70).

At the start of the following crop year, the support price would go up in local currency of country A to the equivalent of USD 85/ton, at an exchange rate of 48 = 1 dollar, or to 4080/ton in local currency and the tariff and refund would return to ECU 38 as the start of the previous crop year.

It is to be hoped that the same tariffs and refunds could be applied to all CEEC at the start of each crop year and that differences in these tariffs and refunds would only occur during a crop year as a result of different currency adjustments of different CEEC.

ANNEX II

Example of the operation of Land banks in the CEEC

- The goal of Land banks in the CEEC would be to establish credit and liquidity in the agricultural economies of these countries on the basis of collateral and value of agricultural land.

- The preconditions for such Land banks would the following:

1. A CEEC would accept the concept of a Land bank and would participate in some way in its operation.
2. Agriculture must be potentially profitable in the CEEC in question.
3. Title to land could be established.
4. Land could be legally pledged as collateral and could be executed in case of default.

Title of land could be legally transferred.

- Credit and liquidity could initially be established as follows:

1. By creating a liquid market for land by being ready to buy and sell land. In selling land, the Land bank could promote the evolution of production units of an economically viable scale.
2. By creating production credits to individual farm operations with land as collateral, either directly or indirectly through local banks which would act as agents for the Land bank.

- The operation of a Land bank will require that a vast number of small transactions are concluded and administered. Transactions will have to be standardized and will have to be administered through appropriate automated administrative procedures. This will entail one contract for selling land, one for buying land, one for applying for production credit. In each case, such a contract would have to be accompanied by a properly endorsed title to the land in question.

The Land banks would discount the title to land that it held with third parties. These could be, for instance, the Central Bank of the CEEC in question, the World bank and/or EBRD, and/or International Merchant Banks, and/or private investors, whether or not with guarantees from the CEEC in question of from another guarantor.

Production credits could be offered in dollars or in dollar equivalent if there were dollar equivalent support prices through which dollar credits could be covered. Land purchases and sales would be likely to be conducted in local currencies, although there would be no reason in principle to exclude transactions in dollars or dollar equivalents.

ANNEX III

Comments on the statistics concerning agriculture and food processing in the CEEC

There is no shortage of statistical data on agriculture and agro-industries in the CEEC: the OECD, World Bank, Eurostat, international trade centres in the Member States, research institutes and specialist journals all produce their columns of figures and graphs, often derived from the same sources and without much scientific attention to detail.

All this material must be viewed with extreme caution by decision-makers. Without being specialists in data gathering and processing, we have tried to check, empirically and roughly, the data and information collected in the field against the available figures.

We find that three types of statistics can be regarded as probably reliable:

* statistics on use of agricultural land: the data collection systems are long-established, varied and based on data compiled by qualified geographers, used as the basis for all local administration;

* statistics on land sown to cereals: the system is also long-established, closely linked with cartography, the data being collected by centralized bodies and easily and rapidly verifiable on the basis of the yields of the regions concerned;

* statistics for foreign trade with the EU: these are customs statistics which can hardly be cast in doubt.

All other figures seem unconvincing. For instance:

* the figures showing trade between the CEEC and CIS take no account of clandestine trade;

* all the figures concerning livestock production are impossible to check, and in most cases fail to tally with observations at field level;

* the significance of variations over time is very relative. For instance it is claimed that Romania's GDP grew by 1% in 1993; but after a 35% plunge of production since 1990 and an inflation rate of 300% in 1993, what does such a figure mean other than that the downward slide of production has levelled out?

For these various reasons, we have deliberately omitted tables and graphs from this report, except for those in Annex IV. The only figures quoted in the body of the text are those which we feel, all other things being equal, we can guarantee as being reliable.

In these circumstances, we would suggest that Eurostat be provided with a working party, possibly including specialist statisticians from the Member States, to compile statistics for sectors where it is already possible to do so and to define the conditions for obtaining a full set of reliable statistics. Without reliable information, how could we, for instance, propose a milk quota to Bulgaria or Romania?

ANNEX IV

Trade in agricultural and food products between the EU and CEEC

01/06/94 FLU1.TAB

EU imports by period and by partner

Eurostat-C 01/06/1994 TABLE 1 SECTION 1.1

vers EUR S Unites = VALEUR (000 ECU)

NOM.COM. RS=4 CHAPITRE1A24
CHAP01A24 U
Annee base 1992

	Total CEEC/trend	% ('88=100)	Poland	évol % ('88=100)	Czechoslov	évol % ('88=100)	Hungary	évol % ('88=100)	Romania	évol % ('88=100)	Bulgaria	évol % ('88=100)
1988	1658243	100%	672735	100%	165801	100%	615306	100%	105750	100%	108571	100%
1989	2108313	127%	896417	133%	218709	140%	758252	123%	102532	97%	133403	123%
1990	2225764	134%	1106453	164%	212909	137%	713750	116%	40761	39%	151901	140%
1991	2515301	152%	1080300	161%	247350	159%	919637	149%	76265	72%	191749	177%
1992	2320902	140%	951594	141%	276764	178%	830587	135%	77980	74%	183077	169%
jan-nov1993	1805905	109%	723145	107%	229875	148%	623928	101%	72099	68%	156858	144%

EU exports by period and by partner

Eurostat-C 01/06/1994 TABLE 2 SECTION 1.1

de EUR S Unites = VALEUR (000 ECU)

NOM.COM. RS=4 CHAPITRE1A24
CHAP01A24 U
Annee base 1992

	Total CEEC/trend	% ('88=100)	Poland	évol % ('88=100)	Czechoslov	évol % ('88=100)	Hungary	évol % ('88=100)	Romania	vol % ('88=100)	Bulgaria	évol % ('88=100)
1988	706015	100%	327429	100%	144311	100%	90617	100%	33928	100%	109730	100%
1989	1233870	175%	760480	232%	177357	123%	111875	123%	81518	240%	102640	94%
1990	1232971	175%	614972	188%	148614	103%	119110	131%	266970	787%	83305	76%
1991	1813281	257%	996003	304%	266707	185%	152489	168%	242986	716%	155196	141%
1992	2019857	286%	924024	282%	417756	289%	228658	252%	324449	956%	124970	114%
jan-nov1993	2229427	316%	972951	297%	466998	324%	298708	330%	295774	872%	194997	178%

Balance by period and by partner

Eurostat-C 01/06/1994 TABLE 3 SECTION 1.1

avec EUR S Unites = VALEUR (000 ECU)

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Annee base 1992

	Total CEEC/trend	Poland	Czechoslovakia	Hungary	Romania	Bulgaria
1988	-952228	-345306	-11490	-524769	-71822	1159
1989	-874443	-134937	-41352	-646377	-21014	-30763
1990	-992793	-491481	-64296	-594640	226219	-68596
1991	-702020	-84307	19357	-767148	166721	-36553
1992	-301045	-27670	140992	-601929	246469	-59007
jan-nov1993	423522	249806	237123	-325220	223675	38139