COMMISSION OF THE EUROPEAN COMMUNITIES

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REPORT FROM THE COMMISSION TO THE BUDGET AUTHORITY ON THE IMPACT ON EAGGF GUARANTEE SECTION EXPENDITURE OF:

- **MOVEMENTS OF THE DOLLAR/ECU EXCHANGE RATE**
- **INCREASES IN THE CORRECTING FACTOR RESULTING FROM MONETARY REALIGNMENTS WITHIN THE EUROPEAN MONETARY SYSTEM**

PROPOSAL FOR A TRANSFER NR 50/97 TO THE MONETARY RESERVE PRESENTED BY THE COMMISSION TO THE BUDGET AUTHORITY

1997 FINANCIAL YEAR

REPORT

on the impact on EAGGF Guarantee Section expenditure in 1997 of:

- movements of the dollar/ecu exchange rate, and
- increases in the correcting factor resulting from monetary realignments within the European Monetary System

I. INTRODUCTION

The value of the dollar affects a major proportion of EAGGF Guarantee Section expenditure. A number of production aids and almost all export refunds are fixed on the basis of the gap existing between Community prices, expressed in ecus, and world prices, generally expressed in dollars (USD).

Other things being equal, a change in the value of the dollar in relation to the ecu automatically implies a change in the gap in ecus between Community prices and world prices and consequently a change in the production aids and export refunds concerned. If the dollar rises, the gap diminishes, leading to a reduction in expenditure; if the dollar falls, the gap widens, raising expenditure.

The European Council of 11 and 12 February 1988, in its conclusions, expressed the will to take explicit account of the impact of the change in the dollar on agricultural expenditure.

On that basis, by its Decision of 24 June 1988 concerning budgetary discipline,[1] the Council provided for the inclusion of ECU 1 000 million in a reserve of the general budget of the European Communities "as a provision for covering developments caused by significant and unforeseen movements in the dollar/ecu market rate compared to the dollar/ecu rate used in the budget". The latter is equal to the average market rate during the first three months of the year preceding the budget year.

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1 OJ No L 185, 15.7.1988, p. 29.

If the average value of the dollar in the period from 1 August of the preceding year to 31 July of the current year falls in relation to the rate used in the budget, the additional budget costs are financed by a transfer from the monetary reserve. Equally, savings in the Guarantee Section when the dollar strengthens are to be transferred to the monetary reserve.[1]

Recourse is to be had to the monetary reserve when the said expenditure (or, as the case may be, the saving) exceeds a margin ('franchise') - ECU 400 million up to and including the 1994 financial year. Similarly, the amount of the transfer relates to that fraction of the impact which exceeds that margin.

The Edinburgh European Council of 11 and 12 December 1992 confirmed that the monetary reserve would remain in place for the period 1993-99 but decided that the amount should be cut to ECU 500 million from 1995 onwards and the 'franchise' reduced from ECU 400 million to ECU 200 million.

Noting also that the monetary movements between the Member States' currencies at the time would substantially increase EAGGF Guarantee Section expenditure, the Edinburgh European Council agreed that adjustments should be made to the arrangements for the operation of the monetary reserve so as to make due allowance for the costs resulting from the monetary alignments between Member States.

The Edinburgh European Council also agreed that if such an increase should cause agricultural expenditure to exceed the guideline and thus jeopardise the financing of the new common agricultural policy as already approved, appropriate measures would be taken by the Council to fund the EAGGF Guarantee Section.

Under the Interinstitutional Agreement between the Parliament, the Council and the Commission of 29 October 1993 on budgetary discipline and improvement of the budgetary procedure,[2] the monetary reserve is intended to cover the financial impact on budgetary expenditure of substantial and unforeseen divergences in the dollar exchange rate as compared with that used in the budget; the reserve may also be used when the agricultural guideline prevents the budgetary cost directly due to monetary realignments within the European monetary system from being absorbed. In that agreement, the institutions took note that, if the agricultural guideline were exceeded as a result of realignments within the monetary system and the lack of available appropriations within the monetary reserve, the Council would take appropriate steps to provide funds for the EAGGF Guarantee Section.

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1 Up to ECU 1 000 million up to the 1994 financial year and up to ECU 500 million from 1995 onwards.

2 OJ No C 331, 7.12.1993, p. 1.

On 31 October 1994 the Council adopted a new Decision on budgetary discipline[1] which took account of the conclusions of the Edinburgh European Council and the inter-institutional agreement. Articles 7 to 12 of that Decision contain the provisions relating to consideration of the dollar exchange rate and of the impact of monetary realignments. The Decision specifies that the special provisions relating to the financing of costs arising from monetary realignments within the European Monetary System will apply until the end of the 1997 financial year (Article 11(3)) and that the transfers from the reserve will only be used if the additional costs (due either to the variation in the dollar rate or to monetary realignments) cannot be met from the budget appropriations entered in Titles 1 to 5 of the EAGGF Guarantee Section (Article 12(1)).

Under Article 9 of the Decision the Commission is required to present a report to the budgetary authority by the end of October each year on the impact on EAGGF Guarantee Section expenditure of:

- movements in the average dollar/ecu market rate for the period from 1 August of the preceding year to 31 July of the current year in relation to the rate used in the budget;

- the monetary realignments within the European Monetary System since 1 September 1992.

This report, which relates to the 1997 financial year, contains information to be used to assess:

- whether, on account of the impact of changes in the dollar/ecu exchange rate, a transfer should be proposed to or from the monetary reserve and, if so, the relevant amount;

- whether, on account of the impact of the monetary realignments within the European Monetary System, a transfer from the monetary reserve should be proposed and whether, if the reserve is used up, appropriate arrangements should be made by the Council to finance the EAGGF Guarantee Section in accordance with the conditions laid down in Article 11 of the Decision on budgetary discipline of 31 October 1994.

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1 OJ No L 293, 12.11.1994, p. 14.

II. IMPACT OF THE DOLLAR ON EAGGF GUARANTEE SECTION EXPENDITURE IN 1997

To gauge the impact of movements in the dollar/ecu rate on the 1997 financial year, consideration must be given, pursuant to Article 7 of the Council Decision of 31 October 1994, to the gap between the average rate recorded for the dollar between 1 August 1996 and 31 July 1997 and the rate used in the 1997 budget. The rate used to assess appropriations for the 1997 financial year is $ 1 = ECU 0.78. In accordance with the Council Decision, this corresponds to the average rate in the first three months of the year preceding the financial year in question (January, February and March 1996).

The following table gives the monthly exchange rate gaps recorded in the reference period:

	Recorded rate 1$ =ECU ...	Budget rate 1$:= ECU ...	Gap in ECU	Gap in %
a	b	c	d = b - c	e = b/c
August	0,7793	0,7800	- 0,0007	- 0,1
September	0,7880	0,7800	+ 0,0080	+ 1,0
October	0,7947	0,7800	+ 0,0147	+ 1,9
November	0,7832	0,7800	+ 0,0032	+ 0,4
December	0,7999	0,7800	+ 0,0199	+ 2,6
January	0,8226	0,7800	+ 0,0426	+ 5,5
February	0,8579	0,7800	+ 0,0779	+ 10,0
March	0,8698	0,7800	+ 0,0898	+ 11,5
April	0,8734	0,7800	+ 0,0934	+ 12,0
May	0,8701	0,7800	+ 0,0901	+ 11,6
June	0,8798	0,7800	+ 0,0998	+ 12,8
July	0,9053	0,7800	+ 0,1253	+ 16,1
Average 1.8.96-31.7.97	0,8352	0,7800	+ 0,0552	+ 7,1

Over the period under consideration the average dollar rate, rounded off, was $ 1 = ECU 0.84, 7.7% above the budget rate. That increase in the value of the dollar involved savings for the EAGGF Guarantee Section.

The recorded average rate of $ 1 = ECU 0.84 is the arithmetical mean of the daily rates for the twelve-month period in question. The average monthly rate fluctuated around that 12-month average, between a minimum of $ 1 = ECU 0.7793 in August 1996 and a maximum of $ 1 = ECU 0.9053 in July 1997.

The dollar rate tended to increase gradually over the period, with the rounded-off averages for the period January to July 1997 remaining well above the budget rate.

If an accurate assessment of the savings made owing to the appreciation of the dollar is to be made during a period when the gaps compared to the budget rate were variable, it is necessary to establish for the period concerned a weighted average dollar rate for every agricultural product for which expenditure in ecus is affected by the dollar, taking account of the seasonal variation in exports with refund or in quantities eligible for Community aid.

On that basis, savings for the EAGGF Guarantee Section as a result of the appreciation of the dollar in relation to the budget rate are estimated at ECU 244 million for the 1997 financial year.

Annex I gives a detailed calculation of these savings, which break down by sector as follows:

	(ECU million)
Cereals:	161
Sugar:	43
Rice:	5
Non-Annex II products:	29
Islands and most remote regions:	6
TOTAL:	244

It should be noted that, like last year, it was considered that the refund rates for livestock sector products were influenced very little by the short or medium-term variation in the dollar rate. There was therefore no need to evaluate the impact of changes in the value of the dollar on refunds for those products.

As the savings in 1997 of ECU 244 million are above the margin of ECU 200 million, a transfer of ECU 44 million should be made to the monetary reserve (Chapter B1-60), in accordance with Article 10 of the Decision of 31 October 1994.

III. PROPOSAL FOR A TRANSFER TO THE MONETARY RESERVE

It should be emphasised that the estimated savings for each sector need not necessarily result in identical end-of-year availabilities. Factors other than the dollar exchange rate have a very significant impact on final appropriations requirements for the various chapters for a year, for example, the volume of exports, world rates for the dollar or fluctuations in the rate of payments. The availability or otherwise of appropriations for a chapter at the end of the year is determined therefore by all of these factors.

For Chapter B1-11: Sugar, a slowing down in the volume of quota sugar exports brought down the level of exports by some 300 000 tonnes as against the budget estimates. It is expected therefore that underutilisation of the original allocation for the chapter will be around ECU 180 million and of the updated allocation around ECU 75 million.
The availability of funds for Chapter B1-11 means that the transfer can be made to the monetary reserve.

The Commission is presenting the following transfer proposal to the Budget Authority:

		ECU million
From Chapter B1-11:	Sugar	- 44
To Chapter B1-60:	Monetary reserve	+ 44

The Articles to which the transfer applies are shown in Annex II.

We would again make it clear that under Article 12(3) of the Decision of 31 October 1994, any savings made and transferred to the monetary reserve which remain in the monetary reserve at the end of the financial year are cancelled and contribute therefore to the build-up of a budget surplus which is entered as a revenue item in the budget for the following year by means of a letter of amendment to the preliminary draft budget for the following year.

IV. THE IMPACT ON EAGGF GUARANTEE SECTION EXPENDITURE IN 1997 OF INCREASES IN THE CORRECTING FACTOR RESULTING FROM MONETARY REALIGNMENTS WITHIN THE EUROPEAN MONETARY SYSTEM SINCE 1 SEPTEMBER 1992

Between the beginning of September 1992 and mid-May 1993 there were five monetary realignments within the European Monetary System.
To gauge the impact of these realignments on EAGGF Guarantee Section expenditure, two factors have to be taken into account:

- As a direct consequence of the monetary realignments since 1 September 1992, the correcting factor (switchover) used for the purposes of the common agricultural policy rose by 5.4% from 1.145109 to 1.207509 from 14 May 1993.
  Other things being equal, this increase in the correcting factor is reflected in a corresponding increase in the double rate, the coefficient expressing the difference between EAGGF Guarantee Section expenditure expressed, on the one hand, in terms of agricultural ('green') ecus, known as ECU(A) and, on the other, the expenditure charged to the budget (budget ecus), designated ECU(B).
  This increase in the double rate coefficient, from 1.145 to 1.207, thus leads to a corresponding increase in agricultural expenditure expressed in budget ecus.[1]

- Article 9 of Council Regulation (EEC) No 3813/92 of 28 December 1992 on the unit of account and the conversion rates to be applied for the purposes of the common agricultural policy[2] lays down that where the correcting factor is increased, the prices fixed in ecus are to be reduced at the beginning of the following marketing year by 25% of the percentage of the change in the correcting factor. The other amounts fixed in ecus, with the exception of certain aids provided for under the 1992 reform of the common agricultural policy, are to be altered appropriately as the need arises.[3]

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1 It should be noted that, even though the correcting factor was abolished with effect from 1 February 1995, the impact of monetary realignments on EAGGF Guarantee Section expenditure continues to be felt because abolition was accompanied by an increase in prices and aids in green ecus of 20.7509%. Without the effect of the monetary realignments which occurred between September 1992 and mid-May 1993 that increase would have been limited to 14.5109%.

2 OJ No L 387, 31.12.1992, p. 1.

3 Among the amounts excluded from the reduction are the majority of aids per hectare for arable crops, beef premiums, the amounts fixed in the context of accompanying measures and amounts of a structural nature or not affecting markets.

By virtue of this provision and in line with the increase in the correcting factor between September 1992 and May 1993, prices and aids in ecus were cut by 1.29% by the application of a reduction coefficient of 1.013088 from the start of the 1993/94 marketing year in the majority of cases. The resulting reduction in EAGGF Guarantee Section expenditure partially offsets the increase in expenditure resulting from the increase in the double rate.

Bearing in mind these two factors, the impact on EAGGF Guarantee Section expenditure in 1997 of the monetary realignments within the European Monetary System and potentially eligible for financing under the mechanisms decided by the Edinburgh European Council, as laid down in Article 11 of the 31 October 1994 Decision on budgetary discipline, is put at ECU 1 703 million, made up as follows:

	(ECU million)
- Rise in the double rate (from 1.145 to 1.207):	+ 2 072
- Cut in prices and some aids (-1.29%):	- 369
TOTAL:	+ 1 703

However, since it has been possible to finance this additional expenditure from within the budget appropriations entered in Titles 1 to 5 of the EAGGF Guarantee Section and within the agricultural guideline, there is no need to have recourse to Article 11 of the Decision of 31 October 1994.

It should also be pointed out that the change in the correcting factor also has an effect on the calculation of world prices for agricultural products expressed in green ecus.

The increase in the correcting factor has reduced world prices expressed in green ecus and, consequently, automatically increased the main export refund rates and the rates for some aids. In principle, this effect applies to all products affected by the change in the dollar rate.

The impact of the increase in the correcting factor on refunds and aids the amount of which is affected by fluctuations in world prices is put at ECU 263 million.

Overall, therefore, the monetary realignments that occurred in 1992 and 1993 have resulted in additional expenditure for the EAGGF Guarantee Section in 1997 of ECU 1 966 million, which, thanks to the favourable trend in the agricultural economy, has been covered in full within the budget appropriations and the agricultural guideline.

Annex III gives the details of the calculation of these estimates.

ANNEX I - Calculation of the impact on EAGGF Guarantee Section expenditure of changes in the dollar: 1997 financial year

	Average world price recorded	Technical adjustment coefficient	Average world price used	Weighted average rate	World price converted into ecu		Unit impact of gap in rates	Quantities concerned	Total budget impact		
					At rate 1$= ECU 0,78	At average weighted rate recorded (ECU/T)					
	($/t)		($/t)	(1 $ = ECU ..)	(ECU/t)		(ECU/t)	(1.000 t)	ECU (A) million	Double rate	ECU (B) million
a	b	c	d = b x c	e	f = d x 0,78	g = d x e	h = f - g	i	j = h x i	k	l = j x k
A. REFUNDS :											-238
Cereals and rice											
- Common wheat	155	1,00	155	0,82	120,9	127,1	-6,2	13.214 (1)	-81,9	1,004	-82
- Barley	132	1,00	132	0,82	103,0	108,2	-5,2	7.633 (1)	-39,7	1,014	-40
- Durum wheat	195	1,00	195	0,80	152,1	156,0	-3,9	343 (1)	-1,3	1,010	-1
- Other cereals	132	1,00	132	0,82	103,0	108,2	-5,2	2.231 (1)	-11,6	1,006	-12
- Starch (production refund)	127	1,60	203	0,82	158,3	166,5	-8,2	3.100	-25,4	1,012	-26
- Rice (milled equivalent)	319	1,00	319	0,85	248,8	271,2	-22,4	228	-5,1	1,026	-5
Sugar (including chemicals industry)	316	1,00	316	0,83	246,5	262,3	-15,8	2.694	-42,6	1,005	-43
Milk products											
- Butter		1,00									
- Butteroil		1,00									
- Skimmed-milk powder		1,00									
- Other in milk equivalent		1,00									
Beef and veal											
- Fresh meat		0,50									
- Frozen meat		0,50									
Pigmeat											
- Cuts and sausages		0,50									
Eggs and poultry											
- Eggs		0,50									
- Poultry		0,75									
Non-Annex products II											
- Common wheat	155	1,00	155	0,82	120,9	127,1	-6,2	285	-1,8	1,013	-2
- Barley	132	1,00	132	0,82	103,0	108,2	-5,2	560	-2,9	1,013	-3
- Durum wheat	195	1,00	195	0,80	152,1	156,0	-3,9	235	-0,9	1,013	-1
- Other cereals	127	1,00	127	0,85	99,1	108,0	-8,9	1.423	-12,7	1,013	-13
- Rice	319	1,00	319	0,85	248,8	271,2	-22,4	9	-0,2	1,013	0
- Sugar	316	1.00	316	0,83	246,5	262,3	-15,8	595	-9,4	1,016	-10
B. AIDS											-6
Fibre plants (cotton)	1.724	0,244	420,7	0,78	328,1	328,1	0,0	1.228	0,0	1,008	0
Islands and most-remote regions											
- Common wheat	155	1,00	155	0,82	120,9	127,1	-6,2	270	-1,7	1,001	-2
- Durum wheat	132	1,00	132	0,82	103,0	108,2	-5,2	118	-0,6	1,001	-1
- Barley	195	1,00	195	0,80	152,1	156,0	-3,9	5	0,0	1,001	0
- Other cereals	132	1,00	132	0,82	103,0	108,2	-5,2	388	-2,0	1,001	-2
- Rice (milled equivalent)	319	1,00	319	0,85	248,8	271,2	-22,4	16	-0,4	1,001	0
- Sugar	316	1,00	316	0,83	246,5	262,3	-15,8	39	-0,6	1,001	-1
TOTAL A + B											-244

N.B. : On the basis of the figures in the Table, a change in the dollar rate of 10 % would lead to a change in expenditure of ECU 444 million

(1) Excluding quantities exported with tax and with zero refund.

EXPLANATORY REMARKS TO ANNEX I

Column (a) of the tables gives all the budget headings which are affected explicitly and directly by movements in the value of the dollar as against the exchange rate used in the budget.

Column (b) gives estimated average world prices in dollars for the period concerned. They correspond either to average selling prices of Community products when exported or to prices used for the calculation of the various aids. These prices are multiplied by an adjusting coefficient (column (c)) indicating the weighting of the world price used to determine an aid or refund. For example, 1.6 times the world price for maize is used in the determination of the production refund for starch.

Column (d) gives average world prices in dollars corrected by the adjusting coefficient.

Column (e) gives the average dollar/ecu exchange rates recorded, established by heading on the basis of a weighting taking account of the seasonal nature of the quantities eligible for export refunds or Community aids.

Columns (f) and (g) give the corrected average world prices converted into ecus using the exchange rate adopted in the budget of $ 1 = ECU 0.78 and the recorded weighted average rates in column (e).

The unit impact of the higher value of the dollar is given in column (h) in ecus per tonne. This unit amount multiplied by the estimated quantities qualifying for aids and/or refunds during the period under review (column i) gives the impact in millions of agricultural ecus (column (j)) and in millions of budget ecus (column (l)).

ANNEX II

GENERAL BUDGET 1997

SECTION III - COMMISSION - PART B

TRANSFER OF APPROPRIATIONS No 50/97

COMPULSORY EXPENDITURE

In ECU

FROM

CHAPTER B1-11 :	SUGAR		
Article B1-110 :	Refunds for sugar and isoglucose	Commitments/ Payments	- 44.000.000

TO

CHAPTER B1-60 :	MONETARY RESERVE		
Article B1-600 :	Monetary reserve	Commitments/ Payments	+ 44.000.000

THE FINANCIAL CONTROLLER APPROVED THIS PROPOSAL ON 2.10.1997 IN ACCORDANCE WITH ARTICLE 26(7) OF THE FINANCIAL REGULATION AND CERTIFIED THAT THE APPROPRIATIONS ARE AVAILABLE

ANNEX III - Cost of monetary realignments between September 1992 and May 1993 : 1997 financial year

	Sector	Change in double rate	Monetary reduction in prices	Sub-total	Impact of change in the correcting factor on refunds and aids	Total impact
a	b	c	d	e = c - d	f	g = e + f
10	Arable crops	881	43	838	173 (1)	**1.011**
11	Sugar	87	27	60	38	**97**
12	Olive oil	109	36	73	0	**73**
13	Dried fodder and pulses				0	**19**
	Fibre plants	19	0	19	27	**50**
14	Fruit and vegetables	47	18	29	0	**69**
15	Wine	82	13	69	0	**42**
16	Tobacco	48	6	42	0	**36**
17	Other plant sectors	49	13	36	0	**21**
18		15	3	12	7	
20	Milk and milk products	163	99	64	0	**64**
21	Beef/veal	328	29	299	0	**299**
22	Sheepmeat	71	64	7	0	**7**
23	Pigmeat	29	0	29	0	**29**
24	Eggs and poultry	4	0	4	0	**4**
25	Other animal product aid measures	4	0	4	0	**4**
26	Fisheries	2	0	2	0	**2**
30	Non-Annex II products	30	17	13	20	**36**
33	Food aid	1	1	0	0	**0**
34	Interest on advance financing				0	**0**
	Distribution to deprived persons	0	0	0	0	**0**
35	Anti-fraud measures				0	**0**
	Clearance	0	0	0	0	**0**
36	Promotional measures	0	0	0	0	**4**
37	Other measures	0	0	25	0	**0**
38		4		12		
39		0				
Titles 1, 2 and 3		1.973	369	1.604	263	**1.867**
40	Income aid	0	0	0	0	**0**
50	Accompanying measures	99	0	99	0	**99**
Total EAGGF-Guarantee		2.072	369	1.703	263	**1.966**

(1)Impact on refunds and aids for cereals, less quantities exported with tax and with zero refund. In the case of oilseeds, it is estimated that, if there had been no change in the correcting factor, per hectare aids would have been reduced by a further 6%. The impact of this further non-reduction in aids is estimated at ECU 143 million.