

# European Community



European Community Information Service  
350 Sparks Street, suite 1110, Ottawa, Ontario K1R 7S8

## BACKGROUND NOTE

### A GUIDE THROUGH THE EC'S "GREEN JUNGLE"

After a 2 1/2 month delay, because of a disagreement over farm-price supports, the European Monetary System (EMS)\* was launched on 13 March 1979.

The disagreement focused on the complex "agri-monetary" system of special exchange rates for agriculture ("green rates") and "monetary compensatory amounts" (MCAs), used for farm goods traded inside the Community.

#### How Green Rates and MCAs Work

When the common market for agriculture was formed in 1962, a common monetary denominator, called the unit of account (then equivalent to one U.S. dollar), was introduced to record EC expenditure and to set uniform farm prices annually. Common farm prices ensured the unity of market for farm goods. Fixed farm prices stabilized and to some extent guaranteed farmers' incomes, which would otherwise suffer from wide variations in price and output levels.

Each of the six (and later nine) national currencies was defined at a fixed exchange rate in terms of the unit of account. When the era of stable exchange rates ended in the late 1960s, these rates had to be adjusted. After major exchange rate re-alignments in 1969, the EC decided not to adjust the exchange rates for intra-Community agricultural trade. (Thus were created the "green rates").

The reasons behind this decision were:

- a) France's concern that the devaluation of the franc (i.e. more francs per unit of account) would fuel already high rates of inflation, and,
- b) Germany's concern that its farmers would suffer loss of markets and revenue from the upward revaluation of the mark (i.e. fewer marks per unit of account).

This practice has continued to this day, with stronger-currency countries (Germany, Netherlands, Belgium and Luxembourg) resisting revaluations of their green rates, while weaker-currency countries (France, Italy, the U.K. and Ireland) have resisted devaluations. Denmark's green rate has not deviated from the real or central bank rate, and it is therefore the only country where farm prices correspond with official EC agricultural prices.

.../2

NR (79) 15  
28 March

---

\* On the European Monetary System, see our background note of 11 January 1979, no. 2

2/...

At the beginning of January 1979, farm-price support levels in the Community and the consequent monetary compensatory amounts (MCAs), in percentages, were:

	<u>Price Level</u>	<u>MCA</u>
Germany	110.8	+ 10.8
Belgium	103.3	+ 3.3
Netherlands	103.3	+ 3.3
Luxembourg	103.3	+ 3.3
Denmark	100.0	0.0
Ireland	98.0	- 2.0
France	89.4	- 10.6
Italy	82.3	- 17.7
United Kingdom	73.0	- 27.0

Thus green rates insulate domestic farm prices from the effects of exchange rate variations: when farm goods are traded inside the Community, the EC applies MCAs to compensate for the difference between green and central bank rates.

For a weaker-currency country, such as France, devaluation of the central bank rate for the franc does not lead to higher farm prices and thus higher inflation, because the "green franc" has not changed its value. Imported farm products do not become more expensive because an MCA (in the form of an import subsidy) lowers the price from the "common" level to the French domestic level. At the same time, devaluation does not encourage more farm exports, because the EC applies the MCA system as an export tax that raises farm prices to the "common" level, and even higher if the goods are destined for the stronger-currency member states.

For a stronger-currency country, such as Germany, upward revaluation of the mark does not mean lower farm prices and more farm imports. MCAs are applied as import taxes on imported farm goods to raise their price from the "common" to the German level. If a German farmer wants to export his produce, an MCA is applied, in the form of an export subsidy, to reduce the price from the German to the "common" level. Should the goods be destined for France, a further MCA lowers the price to the French level.

This helps explain why France's agricultural exports have been growing at the annual rate of 10.8 per cent (1973 to 1977), while Germany's have been increasing at the rate of 21.7 per cent.

Who is happy with this system? Consumers in weak-currency countries and farmers in strong-currency countries. Who is unhappy? Farmers in weak-currency countries and consumers in strong-currency countries.

3/...

MCAs To BE Phased Out

On 29 December 1978, three days before the European Monetary System was due to be introduced, the French Government announced that the introduction of the EMS would have to be delayed until a way had been found to dismantle the MCAs.

On 6 March 1979, the EC Council of Ministers (with the UK dissenting) reached a compromise on MCAs which enabled the French to lift their reserve on the EMS. Under the agreement, four countries would devalue their green rates: the U.K. and Italy by 5 per cent, France by 3.6 per cent, and Ireland by 0.5 per cent. These devaluations reduce the MCAs and raise domestic farm prices in those countries. For the Community as a whole, the Council of Ministers has agreed to phase out MCAs, but details have yet to be worked out.

+++++