Guest Commentary

# The European Union's Cupboard Is Bare

by Jean de la Campagne

*The author is a top French agricultural expert; his article was translated for* EIR*, and subheads added.*

Until recently, the issue of agricultural prices was not a subject of concern for the average French or European citizen. Thanks to higher productivity, prices tended downward in real terms and and contributed to lowering the proportion of food costs in the average household's budget.

This situation changed brutally starting in 2006, with the explosion of commodity prices, which began to hit retail prices at the end of 2007.

The turbulence of the markets observed in 2007 represents quite an unprecedented situation in recent history. Agricultural prices are not the only ones affected. After a period of fluctuations around a generally stable tendency following the 1973 oil shock, the totality of raw material prices has exploded since the end of the 1990s. (several estimates confirm this, using different rating methods: Prices were multiplied by 2.3 times according to the CCI Reuters index or by 5 according to the Cyclope report.)

Of course, the oil price, which went from $10 a barrel in 1999 to over $100 beginning 2008, with a doubling of its price in 2007 alone, is largely responsible for the overall rise of prices, but prices of agricultural products followed.

On world markets (where prices are fixed in dollars), the basic agricultural commodities traded—cereals and dairy products (butter and skim milk powder)—have gone through an evolution nearly as spectacular. The price of wheat tripled, from $3 a bushel in 2005, to $9 a bushel in 2007 (300 euros per ton). The prices of milk powder and butter doubled in 2007, the former going from $2 to $4 per ton. More recently, beginning in 2008, rice, which is not traded much on the world market (only 7% of production is exported) has also been hit by price hikes. The entirely new phenomenon is that these increases are being felt in Europe (price increases were slightly lower in euros, because of the evolution of euro/dollar parity).

Several causes are brought up by the experts to explain this situation: bad weather in large producer countries (Australia's drought's effect on milk); the rising living standard of emerging countries, which need more production to satisfy domestic demand; and the massive increase of the production of biofuels. The latter explanation is especially relevant for corn in the United States.

These three factors certainly have played their role, but, more and more, speculation is accused of being an amplifying element. Of course, the futures markets, hitherto used by traders to cover their potential losses due to price fluctuations, can also, in troubled times such as those we face today, be used by speculators to bet on the rise or fall of prices, and increase global instability even more.

Such turbulence is not exactly new. Since ancient times, agriculture has always been subject to harvest fluctuations due to the climate (Cf. the Biblical "lean cows"), regularly causing famine.

## Government Regulation

More recently, the 1929 crash afforded the opportunty to study the repercussions of a general depression on the prices of agricultural goods.

Franklin D. Roosevelt's economic advisors were the first to theorize the specific laws of agricultural markets, which are subject to inherent fluctuations (defined by the rigidity of demand and the time gap between the decision to produce and the harvest, independent of climate factors). These markets, contrary to the classical theory of the Invisible Hand, are not spontaneously self-regulated. This discovery led to the awareness of the need for public policies capable of ensuring necessary regulation, policies applied as early as 1933 in the United States.

France followed this example, and created its first public intervention facility in 1936, the Wheat Office. Then, after the war, other government mechanisms, covering progressively all other agricultural products, were created and put into action: In 1953, after a catastrophic fall in the price of meat, the Société Interprofessionnelle du Bétail et des Viandes (SIBEV) [Interprofessionnel Association for Livestock and Meat], and in 1955, Interlait was created for dairy products.

As of 1960, these public market agencies were transferred to the European Common Market and became what is known today as the Common Agricultural Policy (CAP).

At that time, the objective was to encourage production and food self-sufficiency. Measures were taken to prevent overproduction from causing a brutal fall in prices, and consequently discouraging production in the following years, thereby creating a vicious cycle of alternating high and low prices, unfavorable to both producers and consumers.

A look at the price evolutions inside the EU demonstrates the CAP's utmost efficiency. The means employed to enforce regulation do not imply that we are in an "assisted" economy. On the contrary, it is a combination the advantages of public intervention and the free operating of the domestic economic market within the European Union: Remunerative indicative prices are decided upon and adjusted each year to take into account gains in productivity; price levels are guaranteed by protection at the borders, so as to avoid a drop in prices due to cheap imports; and excess production goes to build up inventories.

These mechanisms allowed the European market to resist excessive fluctuations (upward as well as downward) of the world market, until recent years, although they were gradually eliminated under pressure of the World Trade Organization (WTO).

## Pressure from WTO Free-Trade Lobby

The WTO agreements call for reduced support to agriculture, accused of unfairly distorting world trade. This is aimed mainly at the rich countries, which are capable of supporting their agriculture, and are therefore accused of destabilizing world agriculture. The successive reforms of the CAP since 1992 are in large part a response to this international pressure. Even if the traditional instruments of the CAP are still in place, they are used less and less, in order to satisfy the demands of the WTO, that stipulate cutting back on the three main areas of support: protection of borders, subsidies for exports, and internal support (price parity system or direct aid). De facto, the European Commission aims to limit any intervention on the markets to the absolute minimum.

In a July 2007 report, the EU Commission was proud to announce that the grain inventory had finally been eliminated.[1] From 18 million metric tons in 2004, it was down to zero in 2006. Likewise, the EU's inventory of butter and milk powder fell to zero in 2007.

Unfortunately, that was exactly the time when inventory should have been available to drive down prices, by re-injecting stocks into the markets.

By capitulating, the CAP has failed in its original mission, stipulated by the 1957 Treaty of Rome [establishing the European Economic Community], which was a commitment to guarantee a correct price for producers, and also a reasonable price for consumers.

Europe still possesses instruments of regulation, but has forgone using them, out of ideological blindness and failure to forecast future changes. One can only wish that the current situation will bring European leaders to think twice before instituting a reform, which, according to free-trade advocates, could result in an even more brutal dismantling of the organized markets.

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1. "We expect that most regions of the EU will represent favorable conditions, with rapidly declining inventory (notably, public inventory), thanks to a poorer harvest in 2006 and 2007, as well as an expansion of domestic demand, lower productivity, and an increased participation of the world markets" (European Commission, Directory G, Agriculture and Rural Development, in: "Prospects for Agricultural Markets and Income in the EU 2007-2014," July 2007).