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C(79) 20 COPY NO 76

12 June 1979

CABINET

CAP PRICES AND GREEN POUND DEVALUATION

Memorandum by the Minister of Agriculture, Fisheries and Food

INTRODUCTION

1. The Ministerial Committee on Defence and Oversea Policy, Sub-Committee on European Questions (OD(E)) discussed on 11 June the line I should take on Common Agricultural Policy (CAP) prices and the Green Pound at the Council of Ministers on 18 June. This paper seeks Cabinet decisions.

CAP PRICES

2. The Commission has proposed a freeze on common prices for virtually all commodities; and a substantially increased co-responsibility levy on milk producers (with extensive exemptions for small producers), varying according to the level of European Economic Community production. The French want to force through a general price increase of 2 per cent, so as to enable Germany to cut her monetary compensatory amounts (MCAs) without reducing prices to German farmers. Only Italy (unreliably) joins us in supporting the Commission's price freeze, and recent rises in production costs have led to further pressures for price increases.

3. It is essential to hold down support levels and the resulting high cost of the CAP as far as possible. We must therefore try to dissuade the Commission from shifting far from a total price freeze. If they propose token increases, involving only minor budgetary cost, for products not in serious surplus, we should be prepared to concede this much, thus showing ourselves more reasonable and constructive than our predecessors. But we must stand firm on the commodities in serious surplus - pre-eminently milk and sugar; reject a milk levy that discriminates unacceptably against United Kingdom producers; and ensure that the average price increase is the smallest since Accession. We must clearly try to avoid becoming isolated. But in the last resort we must be prepared to see the negotiations break down on these issues. OD(E) endorsed this approach.

GREEN POUND

4. The failure of the previous Government to devalue the Green Pound and so increase farm support prices sufficiently was a central feature of our Election campaign. We are committed to put our farmers on level terms of competition with the rest of the Community during the present Parliament.

5. Despite good weather and high production farmers' total net income went down in 1978 by 13 per cent in real terms. Farmers' costs will increase this year by at least 12½ per cent, with wages up by 11 per cent, rents 15 per cent, fertilisers, machinery and feed 10 per cent, oil 20 per cent. Bank borrowings are 25 per cent up on last year. Without a further Green Pound devaluation real net income is expected to fall in 1979 by a further 10-15 per cent, with disastrous effects on confidence and investment. There is a crisis in the pig industry, where because of excessive MCAs on imports the herd is already 15 per cent down on 1973, bacon factories are closing and pig producers losing money.

6. I propose a general Green Pound devaluation of 7½ per cent. With normal weather this should just prevent a fall in real net income below last year's unsatisfactory level. It is the minimum needed to restore confidence, encourage investment and increase productive potential. It would increase the Retail Price Index (RPI) by 0.5 per cent eventually, reduce public expenditure by £4 million and reduce the Public Sector Borrowing Requirement by £44 million.

7. When OD(E) discussed this, the Financial Secretary, Treasury, argued that even 0.5 per cent on the RPI was too much in the light of other expected price increases and proposed a smaller devaluation. But agriculture is one of the few sectors of the economy whose competitive efficiency on level terms can be relied on to reduce imports and increase exports. To depress its productive capacity by inadequate measures now would therefore contradict not merely our statements on agricultural policy but the whole direction of our economic strategy. The farmers' unions are asking for 10 per cent: 5 per cent would be regarded as the bare minimum any Government would find necessary and not as the more positive approach we promised.

8. Given that 1978 margins were themselves unsatisfactory, the different effects of devaluations of 5 per cent and 7½ per cent on the change in real net margins (1979 compared with 1978) for the main commodities show that anything less than 7½ per cent is wholly inadequate:-

	5%	7½%
Milk	-4%	-3%
Beef	No change	+8%
Wheat	-17%	-12%
Sugar Beet	+3%	+10%

9. For pigs, a 5 per cent devaluation would reduce the MCA on competing Danish bacon from £105 to £61 per tonne at today's exchange rate. This would not be enough to safeguard either processors or producers from further decline. Even 7½ per cent leaves the MCA undesirably large at £58. I would therefore propose to follow French precedent by seeking the elimination of the MCA through an additional devaluation of up to 5 per cent for pigmeat only (it would apply to other products in 1980-81). There is no real chance of securing this, because of other countries' opposition; but it is important to be seen to try, and the attempt may help secure our aims in other areas of the negotiation.

CONCLUSION

10. I invite my colleagues to endorse:-

i. The approach suggested in paragraph 2 of CAP prices.

ii. A Green Pound devaluation of 7½ per cent, with effect from 2 July.

iii. A bid, as a negotiating tactic, for an additional devaluation of up to 5 per cent for pigmeat only.

P W

Ministry of Agriculture, Fisheries and Food

11 June 1979