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MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH

Prime Minister

I understand that the channels will be
commenting on the last paper.

From the Minister

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PRIME MINISTER

Please keep
for our work
h.a. 16. 1/2

A.S.C. 12. 1/2

11 February 1982

Bread 3/4 p.
Butter 7p per lb.
Eggs 3p per 1/2

CAP PRICES

At this morning's meeting of OD(E) I was asked to circulate a note indicating the effect of the Commission's farm price proposals upon retail food prices. I believe the subject is of general interest and I am therefore writing to you, with a copy to all members of Cabinet.

The CAP is not the only factor determining food prices. Of the £28.5 billion that the British consumer spends on food, approximately half is for the cost of the raw materials coming from our farms and from imports whilst the other half is payment for the costs of food processing, distribution and retailing. There is a common misconception that there is a direct one for one relationship between price increases decided as part of the Common Agricultural Policy and the overall increase in the price of food. It is important to recognise that the CAP price fixing is but one ingredient in the formation of food prices. Increases in world prices of such foodstuffs as vegetable oils, coffee, tea and tropical fruits, and fluctuations in commodity prices such as eggs, fruits, vegetables, many meats, arise not from CAP price fixing but by forces of supply and demand including, of course, the weather. Wage increases of the retailers and the food processors, energy and other costs have a major impact on food prices. Subsidies or taxes affect the retail price. It is therefore difficult accurately to calculate what any specific change in a common agricultural price will do to the overall price of food.

Since the end of 1978 the retail price index has risen by 51%. Food prices have risen by 37%. Of the 37% rise in food prices, some 24% was attributable to the rise in labour and other costs and the margins of processors, distributors and retailers. Only 13% was due to the rise in the cost of the basic products, and only the smaller proportion of this 13% can be directly attributable to changes in the CAP prices. The reason is that much of the 13% was due to

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increases in the price of foodstuffs not affected by CAP price fixing; in fact not much more than one quarter of the retail cost of food is directly affected by CAP support mechanisms, and the quarter that is controlled by CAP price mechanisms has tended to rise less rapidly than other main elements in the retail cost of food.

Turning now to the effects of the Commission's proposals for this year's price fixing, and excluding any variation in the green pound, it is only possible to provide a general indication, and any increases which do take place will, of course, take place over a period of time. On individual commodities the position is as follows:

There are proposals to increase the support prices for cereals by between 5.3% and 7.05%. But cereal raw material costs account for only one quarter of the retail price of bread, which inevitably will be much more affected by the costs relating to the remaining three quarters than by the price fixing for wheat. The proposed rise in the support price, if it were fully reflected in market prices, would be less than ½p on a standard loaf.

For butter, there is a proposal to increase the intervention price by 8.58%. But in practice the market price will depend upon market circumstances including changes in commercial stocks, opportunities for export, the price levels of competing products such as margarine, and, of course, the figure that is agreed upon for the future level of the consumer butter subsidy. Therefore, whilst a straight increase of 8.58% could represent 7½p per pound on butter, there are many other factors that will determine the price in the shops.

There are no direct support prices for cheese, and it is likely that any increase in the manufacturing price paid for milk would result in a somewhat smaller increase than the equivalent price effect for butter.

The Commission has proposed an increase of 9% in the minimum price of sugar beet. If reflected in the first hand selling price of refined sugar, this would be about 3p per kilogram. But it must be recalled that such are the violent fluctuations of world sugar prices that, as we saw in 1980, the Community price can protect Community consumers from the effect of world price fluctuations.

In present marketing conditions it is unlikely that the Commission's proposals for beef and lamb will have any impact upon the market price. There is therefore no immediate retail price effect that can be identified.

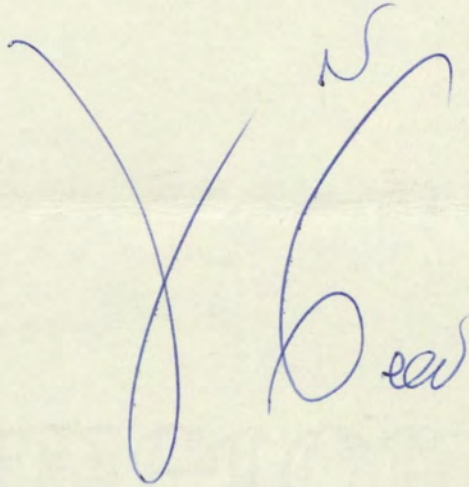
There is no price fixing as such for pork, bacon, poultry and eggs and prices fluctuate according to supply and demand circumstances, although it can be argued that any increases in cereal feed costs would have an impact on the input costs of these producers.

/As far as the ...

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As far as the overall impact of the CAP and food prices are concerned, it can only be said that during the lifetime of this Government, between May 1979 and December 1981 whilst the retail price index went up by 43%, the price of food only went up by 28.8% and farmgate prices (to November) by only 18.9%.

I am sending copies of this minute to all members of the Cabinet and to Sir Robert Armstrong.



PETER WALKER

11 FEB 1982

