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PRIME MINISTER

European Community

On 3 November Michael Jopling wrote to you to say:

(a) that he was worried about the cost of enlargement and that we ought to look at alternatives;

(b) that the EC should set up a small group of wise men to provide an analysis of future trends in European agriculture and pointers to the policy implications.

In the attached minute Sir Geoffrey Howe argues that:

(a) it would not be wise now to put obstacles in the way of enlargement - and that we will be protected against the costs if we reform the Community Budget and the CAP in the way we intend to; And if we don't?

(b) that a group of wise men is not likely to add to all the analyses which we already have of the CAP.

Would you like me to say that you are inclined to agree with the Foreign and Commonwealth Secretary?

although I have great sympathy with his points. But we are all groping for a solution Yes MT.

A.J.C.

16 November 1983

CONFIDENTIAL

Euro Pol

AJC

PM/IC

10 DOWNING STREET

From the Private Secretary

17 November 1983

European Community

The Prime Minister has seen Mr. Jopling's minute of 3 November and the minute of 16 November by the Foreign and Commonwealth Secretary about enlargement and the CAP.

While Mrs Thatcher has considerable sympathy with the points made by Mr. Jopling, she is inclined to agree with the Foreign and Commonwealth Secretary's views as set out in his minute under reference.

I am copying this letter to Roger Bone (Foreign and Commonwealth Office) and Richard Hatfield (Cabinet Office).

A. J. COLES

Robert Lowson, Esq.,
Ministry of Agriculture, Fisheries and Food.

CONFIDENTIAL

PM/83/90

PRIME MINISTER

Europe

1. I have seen a copy of Michael Jopling's letter to you of 3 November about the developments in the Community.

2. I have considerable sympathy with some of Michael's thoughts. I agree that we may well emerge from the post-Stuttgart negotiation with our relations with other EC members in a battered state, and that it is therefore important to look for ways of emphasising our positive attitude to the development of the Community generally. Hence the particular importance of the paper on new policies which we have tabled in the Special Council. It has been widely welcomed - not least as a signal of our will to press for the necessary decisions at the Athens Summit.

3. On enlargement, I too have no illusions about the difficulties ahead. But I doubt whether it would be right to rethink our attitude to Spanish and Portuguese accession. To do so would bring us into immediate collision, not only with Spain and Portugal, but with more or less all of our partners (except perhaps the French who would be delighted at the prospect of shifting the odium attracted by their own equivocal position on to us). The case for Spanish membership is, as Michael Jopling says, above all a political one and it has not lost any of its force. If anything, the effect of the EC membership issue on the outcome of the expected

/Spanish

Spanish referendum in 1985 on NATO membership, and the real possibility of getting the Gibraltar frontier fully opened with the help of the lever which Spanish obligations as a Community member create, make it even more compelling than in the past.

4. We have always accepted that there would be budgetary costs arising from Spanish accession (as opposed to Portuguese accession, which will cost relatively little). Our concern has been to ensure that they are not excessive, and that we do not bear a disproportionate share of them. The figure of 1820 mecu (not billion ecu) for the CAP costs of enlargement which Michael Jopling mentions needs to be treated with caution; it represents the long term cost of applying to Spain and Portugal an unreformed CAP, and in particular the olive oil regime (which on its own accounts for nearly half the forecast increase in FEOGA guaranteed expenditure arising from enlargement). There is no question of our continuing to apply these same regimes without improvements in financial control. As regards the olive oil regime, we are quite clear that the inclusion of Spain in the present arrangements as they stand would not be acceptable. As to the UK share of the burden, we are of course determined that we should pay no more than an equitable share of any future increase in Community spending, whether from enlargement or from any other source. Our safety net proposal would protect us here.

5. Having two new members in the Community with distinct interests of their own is certainly not going to make things easier. But I doubt whether Spain - still less Portugal - will be as prickly and difficult a partner as Greece has proved to be. An increase from 10 to 12 members may well make decision taking a little more complex, but I am disinclined to regard that as an over-riding point. What would worry me would be the possibility of serious consequences for our

/wider

wider interests which might result from slamming the door in the face of these two fragile democracies.

6. The suggestion for a group of 'wise men' to provide the Community with an assessment of supply and demand trends in agriculture and pointers to the political implications is an interesting one. Economists have of course been denouncing the CAP in increasingly strong terms for years: and not just in Britain - see for example the enclosed article in the 'Financial Times' on 1 November by the German Minister Stefan Tangermann. There is no shortage of analysis of what is wrong with the CAP and indeed much agreement on it. Another example is to be found in the European parliament's endorsement of Sir Fred Catherwood's recent report. But however weighty the criticisms, they are not as weighty as political imperatives which make it so difficult to break away from existing arrangements. I am therefore a bit doubtful whether a group of 'wise men' would get us very far. Indeed, I think there might be some risk of such a device distracting attention from the hard decisions we want the Community to take in the months and years ahead. But perhaps we should look at the idea again next year in the light of the outcome of the immediate discussion in the Council about overall control of agricultural expenditure.

7. I am copying this minute to Michael Jopling and Sir Robert Armstrong.

GH

(GEOFFREY HOWE)

Foreign and Commonwealth Office

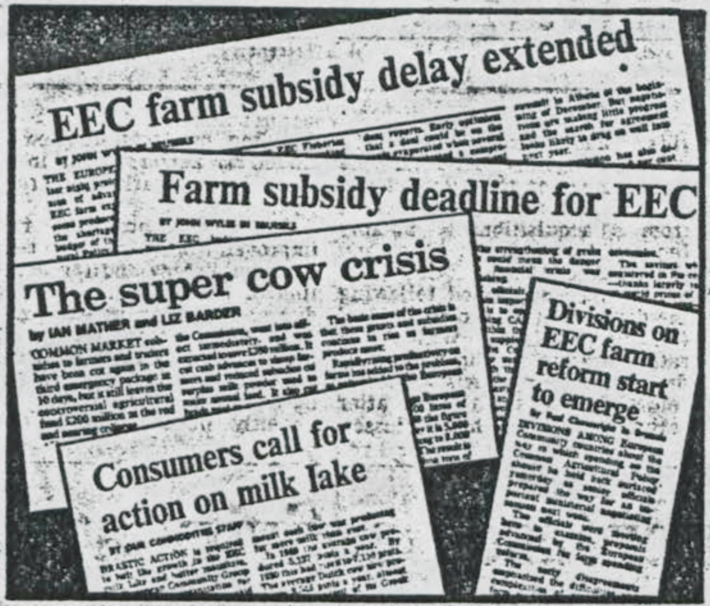
16 November 1983

MMW c1/8/1

Common Agricultural Policy

Europe and the road to serfdom

By Stefan Tangermann



WHEN Nobel prize winner F. A. von Hayek wrote his famous book "The Road to Serfdom" in 1944, he could not foresee that a European Economic Community would come into existence, that this Community would have a Common Agricultural Policy and that this policy would finally end in impasse.

Yet today his book reads like the secret script for the CAP.

One element of von Hayek's theme is the inevitable tendency of government intervention to spread. If the state starts thwarting market forces heavily at one end of the economy, this creates difficulties at another end. Governments feel pressed to do something about these secondary problems, and as they implement new measures the trouble is multiplied. Bureaucratic regulations cover more and more activities, and in the process the economy (and, indeed, the society) comes increasingly under the scourge of state control. What started in liberty ends up in serfdom.

The development of the CAP over the last few years is a faithful representation of this theme. But, it seems, the bitter end is still to come.

The CAP has run out of money. The Stuttgart summit requested the Commission to submit proposals for reform and instructed the Council to adopt solutions to the problem.

A naive observer might think that the obvious and immediate reaction is to avoid the mistakes of the past, ie, to redress farm price support and market intervention. Quite wrong! As if they had to follow von Hayek's dismal vision, like puppets hanging on invisible strings, EEC farm policy makers are

Anxious to stop gaps rather than cure the cause of the problem

anxious to stop gaps rather than to cure the cause of the problem.

To be fair, one has to admit that the Commission has included a gradual reduction of the level of farm price support as one element in its reform proposals. However, if other elements of the Commission's proposals find acceptance, it is politically rather unlikely that CAP price support will be redressed. These other elements include, amongst others, restrictions on imports of grain substitutes, quotas for milk production, and a fat tax. These measures are quite representative examples of the CAP's inherent tendency to take the road to serfdom.

The proposed fat tax has a double purpose. It is supposed to raise the price of fats competing with butter for consumer expenditure, thereby increasing demand for butter and helping to solve the milk surplus problem.

At the same time, it is seen as a source of income for the Community's budget. But it does nothing to solve the underlying problems, as it neither reduces excessive milk production in the EEC nor reduces unnecessary spending from the Brussels budget.

The fat tax is nothing more than a cheap optical illusion as it merely shifts the burden from the Community's budget to the shoulders of the consumers. Should it be adopted, it would mean expanded government intervention in EEC food markets without any economic improvement.

Restrictions on imports of grain substitutes are also a double purpose policy. Imports of feedstuffs which can be substituted for grain (such as manioc or corn gluten feed) have increasingly displaced cereals in EEC compound feeds, as the CAP has made grain more and more expensive in the Community while grain substitutes could be imported rather liberally.

Restricting substitute imports would channel grain back into feeding rations and reduce the Community's grain surplus problem. At the same time it would inflate feed costs and thereby decrease the EEC surplus output of livestock products. However, although this may appear to be an elegant way of killing two birds with one stone, it is of little use if the birds turn out to be the wrong ones.

The EEC's surplus production of grains and livestock is obviously due to excessively high support prices. Yet only a child would be so naive as to assume that a direct solution, the reduction of price support, is on the cards. EEC farm policy makers do not like direct solutions. They would rather adopt additional new measures if the existing ones turn out to have undesired side-effects.

The decisive issue in the current debate about CAP reform, however, is that of milk quotas.

Again, it appears plausible that restricting price guarantees to a given quota of milk production per farm is the "reasonable" policy reaction when the EEC has unbearable milk surpluses. Of course, milk quotas may help to restrict expenditure from the EEC budget, though not to the extent which politicians would like us to believe. It is highly unlikely that EEC farm ministers would agree to an aggregate volume of quotas significantly below current EEC milk production, as proposed by the Commission. Should they adopt the quota solution, the usual adding-up of national interests will, rather, result in a relatively high level of quotas.

But even if quotas help to restrict Community budget expenditure, this is an optical illusion even greater than in the case of the fat tax.

Farm ministers will support dairy farmers' incomes, which can no longer grow through an expansion of output because of quotas, by stepping up milk prices. This means that visible Community budget expenditure is replaced by a hidden burden on EEC consumers of milk and dairy products. And as this consumer burden is hidden there will be a tendency to increase it more and more. Experience in countries which have milk quotas demonstrates this point forcefully.

Some farm policy makers argue that problems like these are negligible as quotas will be established as an interim solution only, until difficulties in the EEC milk market are solved.

These politicians are either naive or cynical. Under the umbrella of quotas, milk prices will be raised to such an extent that it will soon be impossible to remove quotas without a massive boom in milk production or a drastic cut in milk prices, both of which will prove politically unacceptable.

Shifting the burden from the Budget to the consumer

Quotas are here to remain. Again, the history of other countries contains lessons for anyone willing to listen.

A decision to introduce milk quotas in the EEC would, therefore, be a fundamental and irrevocable change of the CAP. It would add a decisive new element of heavy government intervention to the Community's farm policy, instead of decreasing interference with market forces in the light of our unhappy experiences with the CAP.

Milk quotas would lead the CAP on the road to serfdom, on a road which would turn out to be a cul-de-sac, with no turning point at the end. Save the CAP before it is too late!

Stefan Tangermann is Professor of Agricultural Economics at the University of Göttingen.

EURO POL: Budget: Pt 22

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With DB

cc CST EST
FST MST
Mr Middleton
Mr Littler
Mr Unwin
Mr Anson
Mr Lovell
Mr Fitchew
Miss Court
Mr AJ Edwards
Mr Gray
Mr Bostock

Treasury Chambers, Parliament Street, SWIP 3AG
01-233 3000

28 November 1983

The Rt. Hon. Michael Jopling MP
Minister of Agriculture, Fisheries and Food

nb pm.
Dnb 28/11

Dear Minister,

You sent me a copy of your letter of 3 November to the Prime Minister about the Community and Agriculture.

My only comment is to wonder whether there is anything to be gained by our floating the idea that a small group of 'wise men' should examine the CAP. The failings of Community agricultural policies, and the solutions, are clear enough. As you yourself said on 30 August, at the first of the present series of Special Councils, the problem is that high prices and other support arrangements have encouraged excess production, which cannot be consumed within the Community, or sold abroad at an economic price. What we must do, both in the present negotiation and in future price-fixing discussions, is to hold down the level of support so as to rein back excessive production. I fear that a study by 'wise men' would be used by some Member States as an exercise for avoiding such action.

Copies of this letter to go the Prime Minister, the Foreign and Commonwealth Secretary, and Sir Robert Armstrong.

Yours sincerely,

John Kerr

pp. NIGEL LAWSON

[Approved by the Chancellor, signed in his absence in Brussels]

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Budget
Pt 22

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(2)

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

From the Minister

Prime Minister.

The Foreign Secretary will be commenting.

A.J.C. 4/11.

CONFIDENTIAL

PRIME MINISTER

3 November 1983

Dear Prime Minister.

EUROPE

Since your European Stategy meeting has been postponed perhaps I could offer a few thoughts on the subject.

We should have no illusions about the immediate difficulties facing us. There will be another fierce battle over the budget. Even with the weapon of the own resources ceiling, we shall have the utmost difficulty in getting both a satisfactory long term budgetary arrangement and all the improvements we would like to see in the CAP. Another bruising negotiation will inevitably leave us as an unpopular member. I agree with the FCO paper that, given this perspective, we should be looking for areas for the constructive development of the Community.

In one respect I am becoming increasingly concerned. I think all of us have now seen enough of the Greeks in action to acknowledge that they are uncomfortable bed-fellows, not only because we are dealing with a left wing Government but because their needs and aspirations are so different from ours. The entry of Spain and Portugal can only exacerbate these difficulties many times. Spain will be tough, proud and awkward. Portugal will have the greatest difficulty in conforming to the Community's rules without disastrous consequences for her economy. The CAP will become even less manageable, and more costly. Our latest calculations suggest that enlargement will add 1820 billion ecu. on agriculture alone.

/Decision making will ......

Decision making will become even more difficult. We know all these things yet we persist in pressing for enlargement because of the so-called political necessities. Is it not worth having another look at whether there are alternatives which could satisfy those necessities without pretending that Spain is just another Italy or Portugal another Ireland? Any such examination would obviously have to be handled with the greatest delicacy but I should be surprised if it hasn't been done in Paris.

As regards the CAP, our immediate efforts obviously need to be concentrated on getting the most improvement we can, including the imposition of strict financial discipline. But however successful we are with the financial guidelines, there will still be on-going decisions to be taken in the years ahead. I think we might improve our chances of getting those taken more rationally if there was to be a proper analysis of the way in which European agriculture is likely to develop over the next 5-10 years and the kind of response that the Community needs to make. This has not been attempted since the Mansholt Plan. That was a rather socialistic view of European agriculture. Given the political complexion of the majority of Governments in the Community we should be able to prevent that happening now. What I have in mind is a small group of wise men or independent experts who would provide the Community, not with a blueprint, but an assessment of trends of supply and demand and pointers to the policy implications. This would almost certainly reinforce the message we have been trying to get across about growing surpluses. In promoting such a suggestion we would need to be aware of the susceptibilities of the Commission who will think that this is part of their function. But I believe outside people would carry greater weight. Of course we should not float such an idea now but keep it up our sleeves as part of a final package, thus providing for the process of CAP reform to continue after the present round of negotiation has been concluded.

Finally, I endorse what is said in paragraph 18 of the FCO paper about the need to improve the efficiency of the Community institutions. Whatever happens about enlargement, we have an interest in seeing that the business of the Community is done expeditiously and competently. At the heart of this lies the Commission. Certainly, in agriculture, business gets done if the Commission is on the ball and if it is not the Council is paralysed. We have no interest in a feeble Commission, but we want an effective one which takes our interests into account at least as much as those of our partners and preferably more. But when next we are appointing Commissioners (and I assume we shall still have two next time round) I hope we will go for people of really high calibre; and persuade the Germans to do the same. I can think of nothing more likely to make the Community a more business-like place in which we can pursue our objectives.

/I am copying ......

I am copying this to the Foreign and Commonwealth Secretary, the Chancellor of the Exchequer and Sir Robert Armstrong.

Yours Ever

Michael

MICHAEL JOPLING