ECONOMIC GROWTH CENTER

YALE UNIVERSITY

Box 1987, Yale Station
New Haven, Connecticut

CENTER DISCUSSION PAPER NO. 301

ENLARGEMENT OF THE EUROPEAN COMMUNITY AND THE COMMON AGRICULTURAL POLICY

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November 1978

Introduction

One of the most sensitive areas in the current negotiations between the European Community and Spain, Greece and Portugal, is the whole area of agricultural policy. There are many reasons why agriculture has always been one of the stumbling blocks impeding further expansion and integration of the community. Most countries have extensive internal agricultural-support programs for both economic and political objectives such as national-security, income-redistribution or foreign-exchange objectives. Thus, governments are reluctant, if not unwilling, to relinquish control over agricultural policy and/or lessen the protection offered to agriculture, even if that entails significant costs for consumers or other sectors in the economy. Thus, one of the most difficult tasks of the European Community upon its creation in 1958 was to develop a Common Agricultural Policy (CAP) that would promote the interests of the Community as a whole but would also respect the national objectives of the individual members and protect as much as possible the already existing structures. It is this basic contradiction in the fundamental objectives of CAP that has characterized its history and is responsible for its increasingly complicated regulations.

It is also this contradiction that makes its implementation difficult any time that there are structural changes in the system such as the move in 1971 towards flexible exchange rates or the 1973 expansion of the EC to include Britain, Denmark and Ireland. Further enlargement of the community to include Spain, Portugal and Greece will thus be an additional test for CAP which will need to be revised and adjusted in order to reconcile the often conflicting interests of the member countries.

This paper attempts (a) to analyse some of the implications of the three countries' entry for the exercise of the Common Agricultural Policy

within the augmented community and (b) to provide a framework within which to study the distribution of costs and benefits between the partners once entry is completed. As this paper is supposed to serve as a guide for further study, the arguments and information presented are often sketchy. There is great need for a more systematic analysis of future developments in the relevant commodity markets and for a careful evaluation of alternative policies that could be pursued to meet the CAP objectives.

Section 1 of the paper presents a schematic overview of existing CAP regulations regarding commodities which are of basic interest to the applicant countries. These include such typical Mediterranean exports as olive oil, tobacco, fruits and vegetables and wine. Section 2 of the paper analyses some of the implications of multilateral tariff reductions and the introduction of a price support system for Mediterranean exports for inter-European trade and more specifically for the agricultural terms of trade and trade balances between the applicant countries and the Community of nine. This is done with the help of a simple and highly aggregate log-linear model of demand and supply which can easily be disaggregated by either commodities and/or countries.

The final section of the paper focuses on the nature of costs which will be potentially borne by the Community of nine due to entry and some of the possible adjustments that they might seek to enforce.

Section 1

Agriculture is still a highly significant sector in all three of the Mediterranean countries involved. Even though, as can be seen in Table 1, the share of agriculture in total Gross Domestic Product has sharply declined

Table 1

Countries	Agriculture as % of GDP (Constant prices 1970)		Employment in Agriculture as a percentage of Total Labour Force		Per Capita GDP in Agriculture as Percentage of the EEC Average	
	1960	1975	1960	1975	1960	1975
Spain	19.5	9.8	42.3	22.0	31	44
Greece	21.9	14.7	57.0	35.4	26	43
Portugal	25.7	12.3	42.8	28.1	31	27
Eur 9			17.0	8.7	100	100
France	9.6	5.6				
Italy	11.6	8.2				
Ireland	19.8	18.3				

Source: Commision of the European Communities, Economic and Sectoral Aspects: Commission analyses supplementing its views on enlargement, COM(78) 200 final.

between 1960 and 1975 in all three countries, it is still significantly higher than in most other European countries with the exception of Ireland. The importance of agriculture is even more pronounced with regard to generation of employment opportunities. In 1975, employment in agriculture was 22 percent of the total labour force in Spain, 35.4 percent in Greece and 28.1 percent in Portugal as opposed to an average 8.7 percent in the rest of the European Community. The large number of workers employed in the rural sectors relative to existing capital or land and the small size of the average farm, has resulted in significantly lower productivity of land and labour in the Mediterranean countries than in the rest of Europe. These tendencies coupled with increasing emphasis placed by governments on rapid industrialization, have resulted in low per capita incomes in the rural sectors of those countries. As can be seen in Table 1, per capita GDP in agriculture in all three countries in 1975 was less than half the corresponding figure for the rest of the Community. In Portugal per capita GDP in agriculture as a fraction of the EC average has even declined between 1960 and 1975 from 31 percent to 27 percent. According to Commission projections[1] therefore, full membership of Spain, Greece and Portugal into the EC will imply that at least in the short-run (a) the total number of people engaged in agriculture in the EC will more than double, (b) agricultural production will not increase concomitantly due to low labour productivity and (c) regional disparities within the extended community will increase.

The agricultural sector in all three countries is significant in terms of foreign exchange earnings. In 1975, agricultural exports[2], in value terms, accounted for 20.5 percent of total exports in Spain, 15.3 percent of total exports in Portugal and 30.4 percent of total exports in Greece.[3] As can be seen in Table 2, at least in 1975, the EC absorbed more than half of the

Table 3

EEC Prices as a Percentage of
World Market Prices

Commodity	1973-74	1975-76
Wheat	80	125
Rice	60	137
Maize	98	128
Sugar	66	109
Beef and Veal	111	158
Pig Meat	131	113
Butter	320	320
Milk Powder	156	266

Source: SRI International, Business Intelligence Program, Agricultural Policy of the EEC, June 1977, No. 1016.

total agricultural exports of Spain and Greece and 41.7 percent of the total agricultural exports of Portugal. This high share of trade with EC countries is largely the result of a sequence of trading agreements between the Mediterranean countries (notably Greece), and the EC ever since 1962. These have usually involved specific commodities. The high prices of EC agricultural goods in contrast to world market prices is probably the best explanation why agricultural imports from the EC into the Mediterranean countries have remained limited. As can be seen in Table 3, by 1975-76, most of the important agricultural commodities could be obtained more cheaply from the rest of the world. The implications of entry into the EC for domestic inflationary pressures due to the redirection of trade of the Mediterranean countries from cheaper to more expensive sources of supply, will be dealt analytically below. At this stage, however, it is important to note that whereas imports from the EC have been limited, exports of agriculture goods to it have already been extensive. Thus, from a static viewpoint, full membership would imply fewer gains for the exporting countries than would have been the case had Mediterranean products been excluded from the European Markets through a stringent application of the Common Agricultural Policy.

The composition of trade is roughly similar for all three countries. As can be seen in Table 4, Spanish agricultural exports consist mainly of fruit and vegetables, citrus fruit in particular, wine and olive oil. Apart from cork, Portugal exports mainly wine, preserved fish, preserved fruit and vegetables. Finally Greece exports fresh and processed fruit and vegetables, tobacco, wine, raisins and olive oil. Over 20 percent of agricultural imports in all three countries is accounted for by maize while sugar imports are almost equally significant. Since trade between the EC and the Mediterranean countries tends to be relatively concentrated in few goods, a closer

Table 2

External Trade in Agricultural Products* of Spain, Greece and Portugal

	Total agricultural exports to all destinations US $ million		Total agricultural imports from all countries US $ million		Value of agricultural exports to EEC US $ million		Agricultural exports to EEC as % of total agricultural exports		Value of agricultural imports from EEC US $ million		Agricultural imports from EEC as % of total agricultural imports	
	1970	1975	1970	1975	1970	1975	1970	1975	1970	1975	1970	1975
Spain	697.7	1,581.2	553.4	2,045.1	423.4	1,015.3	60.7	64.2	102.8	301.0	18.6	14.7
Greece	259.6	693.9	191.5	479.5	143.0	366.5	55.1	52.8	52.8	137.9	27.6	28.6
Portugal	177.1	300.4	180.1	765.6	73.1	125.3	41.6	41.7	29.2	91.5	16.2	12.0

*(Total of 0 + 1 in SITC classification)

Source: Commission of the European Communities, Economic and Sectoral Aspects; Commission Analyses Supplementing its Views on Enlargement, COM(78) 200 final, April 27, 1978.

Table 4

Main Agricultural Products Imported and

Exported by the Three Countries

Exports (% of Country's Total Agricultural Exports)				1975 Imports (% of Country's Total Agricultural Imports)			
Commodity	Spain	Greece	Portugal	Commodity	Spain	Greece	Portugal
Fresh and Processed Fruits and Vegetables	57	58	17	Live Animals and Meat	5	15	5
Wine	12	3	40	Milk Products	4	11	1
Olive Oil	5	6	2	Maize	22	26	21
Fish Preparations	-	-	15	Sugar	15	12	23
Raw Tobacco	-	21	-	Vegetable Proteins	23	8	12

Source: Commission of the European Communities, Economic and Sectoral Aspects; Commission Analyses Supplementing its Views on Enlargement, COM(78) 200 final, April 27, 1978.

look at existing CAP regulations pertaining to those commodities can be helpful in highlighting some of the issues involved in the negotiations.

The Common Agricultural Policy has evolved around three basic principles: (a) Common Pricing, (b) Community Preference and (c) Common Financing. Common Pricing implies the Community-wide regulation of prices, not necessarily however at a single level, so as to promote free trade between the areas. Target prices and intervention prices are usually set for each commodity; these are allowed to differ between major producing and consuming areas to take account of transportation costs and thus promote exports. The actual level of targeted prices is usually the result of extensive bargaining between those countries which have a comparative advantage in the production of a commodity and can thus produce it at low costs, and those which prefer to protect domestic, relatively inefficient, production by maintaining high prices.[4] An important aspect of Common Pricing is that there can be no restrictions placed on production.

Community Preference refers to those set of policies such as the import levy system, minimum import prices, the use of quotas, compensatory taxes and subsidies, which ensure that intra- EC traded products will always be cheaper than the corresponding imports.

Finally, Common Financing implies that the EC will always be willing to bear the costs associated with agricultural policy.

Regulations for each of the commodities are slightly different. Regarding those goods which are the major agricultural exports of the three applicant countries, Italy and Southern France are the major competing producers.

The first regulations pertaining to fruits and vegetables appeared in 1962 but major provisions have been added since. Domestic production is

protected from outside competition by high import duties (20 percent or more ad valorem) and reinforced by "reference prices" which are in fact minimum import prices. In the case where the domestic price of an import-competing good is even lower than the reference price, a "compensatory tax" is automatically imposed by the EC on the imported commodity involved. In the past there has been preferential treatment granted to most Mediterranean countries through the use of preferential rates with the provision, however, that export prices will be kept above reference prices. Full membership in the EC will thus imply an effective reduction of EC tariffs against fruit and vegetable exports from the three applicant countries. It will also probably imply a net increase in the price of those goods received by domestic producers and thus a concomitant expansion in supply.

Entry into the EC would also imply the effective reduction of tariffs vis-a-vis Mediterranean exports of wine. Even though preferential treatment has already been extended in the past to these countries, protection was guaranteed through the common external tariff, quality-control certificates and compensatory taxes. Even though there will be increased competition within the Community on account of entry, prices will in all probability be kept high. This might result in increased production and creation of further surpluses especially in lower-quality wines.

A similar development can be expected for olive oil, where, apart from a market target price which has traditionally been fixed at a level above world market prices, producers have benefited from direct transfers to supplement their income. Protection from outside competition has been granted in this case with the aid of market intervention and variable import levies. These still apply to the three applicant countries even

though preferential reductions in the levy have been granted.

The only one of the relevant commodities for which import duties have already been eliminated is tobacco where entry will mainly affect Greek production and exports. The major competing producers within the European Community are Italy and France, which, in 1972, contributed 59 percent and 33 percent of total EC production respectively. Price support is guaranteed by a different producer target price for each of the twenty or so different types of tobacco produced, with the intervention price still considerably higher than the price of competing imports. Community preference is established by domestic subsidies rather than a variable levy against imports and complemented by premiums paid to buyers of domestic tobacco leaves which have often ranged between 60 and 80 percent of the intervention price for most types. Thus, extension of the subsidy schemes to cover Greek tobacco production will probably increase the price of Greek tobacco and result in some expansion of production.

All of the above conclusions, however, crucially depend on the outcome of negotiations. This will be determined not only by the interaction of the two negotiating sides but also by the nature of the objectives of the applicant countries' themselves. As will become clear in Section 2, the strategy of an applicant country can be different if the government attempts to improve the terms of trade for redistributive policies than if it wants to maximize export receipts.

The preceding analysis also points to the fact that unless corresponding policies are adopted on the part of the augmented EC, expansion will entail some trade creation due to the elimination of tariffs but also increased production and surpluses of key commodities unless market prices are allowed to fall. Higher food prices for the incoming countries and losses due to

trade diversion will also be some of the harmful side-effects of entry. These issues as well as the distributive issues within the augmented EC are taken up in Section 3.

Section 2

In Section 1, we briefly outlined some of the existing regulations of CAP regarding commodities for which the Mediterranean countries enjoy a comparative advantage and traced some of the implications of entry for the future marketing of those commodities. It was concluded that for most agricultural goods entry implies a multilateral reduction in tariffs and/or other trade impediments as well as a possible increase in the net price received by producers due to the extensive support system. This exogenous increase in the net price received by producers might also be applicable for some EC exports if, on account of higher transportation costs, an upward adjustment of targeted prices takes place.

The implications of entry for terms-of-trade and balance-of-trade developments within the region, can be better understood within the framework of a simple supply-and-demand model. The model, initially developed for the analysis of exchange rate policy in developing countries,[5] can be applied here as well for the analysis of bilateral trade relations or for the analysis of trade flows between the Mediterranean countries and the Community of Nine.

Export Price Movements

On the export side, net export supply prices are stated in home currency units, p_x^n, while demand prices which include the ad volarem tariff, are stated in foreign exchange units, q_x^g. The exchange rate, e, links

p_x^g to q_x^g while the tariff level, t^f, links gross to net demand prices. The export supply function is written as,

$$\ell np_x^n = \ell np_x^o + s_x^{-1}\, \ell nX \tag{1}$$

Here p_x^o is a vertical shift parameter representing changes in domestic supply conditions, s_x is the price elasticity of supply, and X is the quantity exported. The foreign demand funtion for home exports denominated in foreign exchange units, is

$$\ell nq_x^g = \ell nq_x^o + d_x^{-1}\ell nX \tag{2}$$

where, q_x^o is a vertical shift parameter which can represent changes in world market conditions. Thus, an increase in agricultural support prices might be represented by an increase in q_x^o. The price elasticity of demand in (2) is represented by d_x and X is again the quantity exported.

To convert demand into home currency units we can use the relationship,

$$p_x = eq_x \text{ or } \ell np_x = \ell ne + \ell nq_x \tag{3}$$

The demand function expressed in home currency units is thus equal to,

$$\ell np_x^g = \ell nq_x^o + d_x^{-1}\ell nX + \ell ne \tag{4}$$

To translate finally consumer prices into producer prices we use the relationship

$$p_x^g = p_x^n(1 + t^f) \text{ or } \ell np_x^g = \ell np_x^n + \ell n\,(1 + t^f) \tag{5}$$

where p_x^g is the gross price for home goods which the foreigner pays, p_x^n is the price which the local producer receives and t^f is the tariff imposed by the foreigner. Substituting (5) into (4) and solving for p_x^n, the demand function can be expressed as,

$$\ell n p_x^n = \ell n q_x^o + d_n^{-1} \ell n X + \ell n e - \ell n (1 + t^f) \tag{6}$$

Equations (1) and (6) can now be combined to solve for market equilibrium p_x and x. The total differentials of (1) and (6) are,

$$\dot{p}_x^n - s_x^{-1} \dot{X} = \dot{p}_x^o \quad \text{and} \tag{1'}$$

$$\dot{p}_x^n - d_x^{-1} \dot{X} = \dot{q}_x^o + \dot{e} - \frac{t^f}{1 + t^f} \dot{t}^f \tag{6'}$$

The solutions for $\dot{p}_x^n$ and $\dot{X}$ are given by

$$\dot{p}_x^n = \frac{d_x}{d_x - s_x} (\dot{q}_x^o + \dot{e} - \frac{t^f}{1 + t^f} \dot{t}^f) - \frac{s_x}{d_x - s_x} \dot{p}_x^o \text{, and} \tag{7}$$

$$\dot{X} = \frac{s_x d_x}{d_x - s_x} \{(\dot{q}_x^o + \dot{e}) - (\dot{p}_x^o + \frac{t^f}{1 + t^f} \dot{t}^f)\} \tag{8}$$

Equation (7) can be rewritten as,

$$\dot{p}_x^n = k(\dot{q}_x^o + \dot{e} - \frac{t^f}{1 + t^f} \dot{t}^f) + (1 - k) \dot{p}_x^o, \tag{9}$$

where k is defined as

$$k = \frac{d_x}{d_x - s_x} = \frac{1}{1 - \frac{s_x}{d_x}} \; ; \; 0 < k \leq 1.$$

In (9), $\dot{p}_x^n$ is expressed as a weighted average of external and internal disturbances with the weights given by k. The effect of any disturbance on $\dot{p}_x^n$ will crucially depend on the magnitude of k, i.e. the ratio of the relevant elasticities of demand and supply. If the country is a price taker in export markets so that $d_x \to -\infty$, k approaches unity. Hence k can be used as a proxy for relative market power; k however, is also affected by the magnitude of the supply elasticity of exports. In eigher case, k can fluctuate between zero and unity.

Import Price Movements

The import supply and demand functions are exactly analogous to the export functions with the only exception that import supply is now given in terms of foreign exchange prices and import demand is given in terms of domestic currency. Thus supply for imports in foreign exchange can be expressed as,

$$\ell n q_m^n = \ell n q_m^o + s_m^{-1} \ell n M \qquad (10)$$

and in home currency units,

$$\ell n p_m^n = \ell n q_m^o + s_m^{-1} \ell n M + \ell n e \qquad (11)$$

Import demand, in home-currency and consumer-price terms is:

$$\ell n p_m^g = \ell n p_m^o + d_m^{-1} \ell n M \qquad (12)$$

Again the difference between the price consumers pay and the price producers receive is accounted for by domestic tariffs so that the demand function expressed in terms of net prices is,

$$\ell n p_m^n = \ell n p_m^o + d_m^{-1} \ell n M - \ell n(1+t^d) \tag{13}$$

Taking total differentials of (10) and (13) and solving for the equilibrium $\dot{p}_m^n$ and $\dot{M}$ we obtain:

$$\dot{p}_m^n = \frac{s_m}{s_m - d_m} (\dot{q}_m^o + \dot{e}) - \frac{d_m}{s_m - d_m} (\dot{p}_m^o - \frac{t^d}{1 + t^d} \dot{t}^d); \tag{14}$$

$$\dot{M} = \frac{s_m d_m}{s_m - d_m} \{(\dot{q}_m^o + \dot{e} + \frac{t^d}{1 + t^d} \dot{t}^d) - \dot{p}_m^o \} . \tag{15}$$

Equation (14) for $\dot{p}_m^n$ can be again expressed as a weighted average of external and internal disturbances with the weights k' and 1 - k' being functions of the relative elasticities of demand and supply for imports. Thus (14) can be rewritten as,

$$\dot{p}_m^n = k' (\dot{q}_m^o + \dot{e}) + (1 - k') (\dot{p}_m^o - \frac{t^d}{1 + t^d} \dot{t}^d) \tag{16}$$

where

$$k' \equiv \frac{s_m}{s_m - d_m} = \frac{1}{1 - \frac{d_m}{s_m}} ; \; o < k' \leq 1.$$

Again here, k' can be used as an index of market power on the import side, so that if the country is a price-taker in import markets so that $s_m \to \infty$, k' would approach unity. Here again the price elasticity of demand for imports critically affects the magnitude of k'.

Terms of Trade Movements

The terms of trade of a country is given by the ratio of export to import prices. Where tariffs are involved, the terms of trade can be

expressed in terms of either gross or net prices. Here we choose to express them in net-price terms; the solution in terms of gross prices is easy to obtain.

Since, $\pi^n = \frac{p_x^n}{p_m^n}$, it follows that

$$\ln \pi^n = \ln p_x^m - \ln p_m^n, \tag{17}$$

or

$$\dot{\pi}^n = \dot{p}_x^n - \dot{p}_m^n. \tag{18}$$

Substituting equations (7) and (14) for $\dot{p}_x^n$ and $\dot{p}_m^n$ in (18) we obtain the following:

$$\dot{\pi}^n = \{(k - k')\dot{e}\} + \{k\dot{q}_x^o - k'\dot{q}_m^o\} + \{(1 - k)\dot{p}_x^o - (1 - k')\dot{p}_m^o\}$$

$$+ \{(1 - k')\frac{t^d}{1 + t^d}\dot{t}^d - k\frac{t^f}{1 + t^f}\dot{t}^f\}. \tag{19}$$

Equation (19) expresses the percentage change in the terms of trade as a function of exchange rate changes ($\dot{e}$), external price ($\dot{q}_i$; i = x, m) and internal price ($\dot{p}_i$; i = x, m) disturbances, and finally changes in the level of domestic and foreign tariffs. The impact of any exogenous disturbance on the equilibrium terms of trade crucially depends on the magnitude of market power on the export or import sides or on net relative market power in the case of exchange rate changes.

Leaving aside exchange rate changes as well as domestic price disturbances and focusing instead on tariffs and potential increases in $\dot{q}_x^o$ or $\dot{q}_m^o$ due to the price support system in CAP, we conclude the following:

1. If the country or group of countries in question are price takers in both markets so that $k = k' = 1$, then, neither changes in domestic tariff schedules not shifts in external prices $\dot{q}_x^o$ and $\dot{q}_m^o$ will affect the terms of trade. These will be affected only by changes in foreign tariffs on domestic exports.

2. The terms-of-trade are worsened with a unilateral reduction in domestic tariffs or an exogenous increase in the foreign price of imports. The effect on the terms of trade depends on import-side market power as well as the initial level of domestic tariffs.

3. The terms-of-trade improve with unilateral reductions in foreign tariffs or an exogenous increase in the foreign price of exports. Again here the effect on π depends on the degree of export-side market power and the existing level of foreign tariffs.

Finally,

4. The implications of multilateral reductions in tariffs or changes in foreign prices for the terms of trade are ambiguous and depend not only on the existing tariff levels but also on the relative market power of the economy on the export or import sides.

Balance-of-Trade Implications

The balance of trade in agricultural commodities between two partners can be expressed as

$$BT = p_x^n X - p_m^n M. \tag{20}$$

If we set $p_x = p_m = 1$ initially, differentiation of (20) yields

$$dBT = (\dot{p}_x^n + X)X_o - (\dot{p}_m^n + \dot{M})M_o,$$

where X_o and M_o are initial values. If one assumes that both the exchange rate and domestic supply conditions remain unchanged so that $\dot{e} = \dot{p}_x^o = \dot{p}_m^o = 0$, substitution for $\dot{p}_x^n$, $\dot{X}$, $\dot{p}_n^n$, $\dot{M}$ for equations (7), (8), (14) and (15) yields,

$$dBT = -k\,(1 + s_x)\,\frac{t^f}{1 + t^f}\,X_o\,\dot{t}^f + (1 - k'(1 + d_m))\,\frac{t^d}{1 + t^d}\,M_o\,\dot{t}^d + k\,(1 + s_x)\,X_o\,\dot{q}_x^o - k'(1 + d_m)\,M_o\dot{q}_m^o \qquad (21)$$

From equation 21 the following conclusions can be derived:

1. A unilateral reduction in foreign tariffs or an increase in foreign prices for local exports unambiguously improve the balance of trade.
2. The effects of a unilateral reduction of domestic tariffs on the balance of trade is ambiguous depending on the sign of the expression $1 - k'(1 + d_m)$.
3. From (1) and (2) above, it follows that multilateral reductions in tariffs have ambiguous effects on the balance of trade depending on the magnitudes of the relevant elasticities, and the pre-level tariff and trade flows. The same holds true for autonomous increases in the foreign price of exports and imports.

If most Mediterranean countries are assumed to be price takers on the import side but face a less than infinitely elastic demand for their exports at least for prices above the intervention prices, then, there will probably be some net improvement in the terms of trade both on account of tariff reductions and the application of the price support system. Only if the rise in the foreign price of agricultural imports is sufficiently high to outweigh the other effects will the terms of trade deteriorate.

The effects on the net foreign exchange receipts is harder to ascertain even if simplifying assumptions are made regarding the degree of market power. Even though on tariff reduction grounds one would expect a deterioration of the balance of trade the enforcement of the price support system might raise foreign prices of exports sufficiently as to increase net foreign exchange receipts.

Section 3

Apart from changes in the terms of trade and balance of trade between the two sets of countries, entry will also create efficiency gains or losses for the community as a whole. The appropriation of these gains by a set of countries or particular economic agents within the EC, will have redistributive effects which are worth examining.

Trade creation refers to potential improvement in resource utilization by inclusion within the Community of more efficient producers. If, following entry, prices of Mediterranean goods and their substitutes are allowed to adjust downward to reflect the lower costs of production in the entering countries, then there will be net gains to the Community as a whole: the most efficient producers will expand their market share, while the gains to the consumers will exceed the total loss of both the government which would lose tariff revenue and domestic producers who would be driven out of the market. If prices, however, are not allowed to fall, then there will be no benefits to the Community as a whole due to trade creation. The incoming countries in that case will expand their production and appropriate all the gains from enlargement. EC consumers and producers will still face the same set of prices while imports from the rest of the world would be cut due to trade redirection towards the new partners. Thus, if

Greece, Spain and Portugal become full members, but prices of Mediterranean goods continue to be supported to the same extent as before, one would expect countries such as Turkey and Israel to be the major losers while the incoming countries would appropriate all the gains.

If the EC on the one hand does not want a reduction in the price of such goods as fruits and vegetables, olive oil, wine, etc. in order to protect French and Italian interests, and on the other hand, fears the creation of additional surpluses in those goods, then one would expect it to put pressure on the incoming countries to bear some of the costs of adjustment. This could be done by some form of agreement on diversification in agricultural production, limitation of total acreage, voluntary export restraints or even direct quotas on Mediterranean exports.

Turning now to trade in other agricultural goods, one should expect a worsening of resource utilization on account of enlargement. Once they are full members, the applicant countries are expected to eliminate their tariffs vis-a-vis EC exports and adopt the Community Preference policies. This would entail significant trade redirection away from third countries which, as can be seen in Table 3, happen to be the most efficient producers of basic agricultural goods, towards the more inefficient EC countries. This trade redirection will imply higher prices for domestic consumers and a net loss for the entering countries.

The trade-diversion costs will probably be even higher since enlargement might bring about a rise in minimum import prices for the community as a whole. This will probably be the case since Community Preference legislation specifies that the level of "threshold prices" (or minimum import prices) should be fixed for the most distant point in the EC so as to assure preference for EC commodities there as well. Thus, for

sugar for example, threshhold prices are fixed with regard to prices prevailing in Palermo, Sicily so that transportation costs from the main producing areas to Palermo do not negate Community Preference.[6]

Thus enlargement would probably bring about a rise in threshold prices at least proportional to marginal transportation costs to Greece and Portugal. This in fact will increase the rate of protection offered to EC producers and reduce the degree of competition.

From the above, it follows that unless some of CAP regulations are relaxed or altered, expansion of the European Community will entail a direct transfer from consumers to producers with greater benefits accruing to the producers in the entering countries than those in the Community of Nine. Even though this transfer will be probably welcome by the entering countries, it will create additional domestic inflationary pressures and will magnify the already significant problems facing CAP.

FOOTNOTES

1. Commission of the European Communities, Economic and Sectoral Aspects; Commission Analyses supplementing its views on enlargement, COM(78) 200 final, Brussels, April 27, 1978, p. 59.

2. These include food, live animals, tobacco and beverages, i.e. Sections 0 and 1 of the SITC classification.

3. Commission of the European Communities, op. cit., pp. 12, 24, 35.

4. For a more detailed discussion see, Executive Branch, Gatt Study, No. 12, The Common Agricultural Policy of the European Community, August 1973.

5. Branson, W. H. and Papaefstratiou L., "Exchange Rate Policy for Developing Countries", 1978, unpublished.

6. For a detailed discussion see, Executive Branch Gatt Study, No. 12, op. cit., p. 26.