

WHAT'S HAPPENING IN THE EUROPEAN COMMUNITIES

What EC 1992 implies for Australian agriculture

The European Community is the world's largest trading bloc. It constitutes our second most important export market, is our biggest source of imports and our most significant investment partner. It is evident, therefore, that developments in the EC will continue to have important ramifications for Australian trade and investment patterns.

Australia has a close and continuing interest in the EC's Single Market Program. The Single Market is meant by the end of 1992 to bring down barriers to trade in goods and services, capital and labour. It is intended to establish a more competitive and dynamic European economy, giving impetus to internal growth and external trade. It should simplify and liberalise business dealings with the EC in many fields.

The Government is assessing carefully, sector by sector and issue by issue, the new costs and new opportunities which establishment of a Single Market will create.

The Single Market is not yet a reality; many of the controversial decisions have still to be settled. Although the 286-odd pieces of legislation required have been tabled in the Community itself, many have not been agreed upon and few have been implemented into national laws in the Member States. In some sectors, the Single Market is fast approaching but in others it will take some years.' -

From a foreword by the Minister for Trade Negotiations, Dr Neal Blewett, to a Discussion Paper titled The European Community Single Market Program Implications for Australia, Agriculture.

The agricultural policies of the European Community (EC) have been a constant concern to Australia since the introduction of the Common Agricultural Policy (CAP) over 30 years ago. The CAP has not only led to the closing off of large areas of the European market, it also has distorted other agricultural markets around the world.

Although the word common implies that there are no trade barriers in the Community's agricultural policy, it is probably in agriculture that there are the greatest number of restrictions with regard to the movement of goods. These non tariff barriers include health regulations, labelling restrictions, quotas, variable premiums and not the least, monetary differences operated through the agrimonetary system.

The agrimonetary system, which involves manipulation of exchange rates and the application of a system of border taxes and subsidies, has shielded farmers from price fluctuations following exchange rate changes. The application of border taxes and subsidies, which are known as monetary compensatory amounts (MCAs), depends on border checks. The removal of frontier posts therefore, will have implications for the operation of the agrimonetary system and indeed the competitive position of agriculture in different member states, unless alternative measures are introduced to maintain the status quo.

EC agriculture also will be affected in a lesser way by changes in the Single Market Program to health and quarantine regulations (sanitary and phytosanitary measures) and indirectly, through changes to such things as transport, taxation, harmonisation of food regulations and environmental regulations. The dismantling of the agrimonetary system is clearly the greatest challenge of the Single Market to EC agriculture. It is the subject of intense debate within the European Commission and, although there are proposals for reform, the victory of 'liberals' over 'protectionists' is by no means clear.

Implications for third country trade are less apparent in the short term. Although preoccupation with 1992 and developments in Eastern Europe may be diverting attention away from the Uruguay Round, changes in access into the EC and the effect on agricultural exports from Europe will be determined more by the outcome of Uruguay Round negotiations than by 1992. A further factor influencing EC agriculture, is the dramatic change in eastern Europe, which includes German unification and moves towards association and possibly full membership of the EC by several East European countries.

The EC's Single Market Program should mean the opening up of opportunities in a more competitive and dynamic European economy both for indigenous business and third country exporters. Yet of all the sectors affected by the 1992 legislation, agriculture is perhaps the one where these opportunities have proved the most contentious, difficult to secure and tenuous. With a market of 340 million affluent consumers at stake, what are the implications for Australia's commodity and processed food exporters?

CAP and the Single Market

The Common Agricultural Policy (CAP) was initially designed to achieve many of the objectives, in terms of the internal organisation of agricultural markets, that are now set for the EC 1992 program in other fields.

There is the view that there is already a common market for agriculture and thus agriculture is excluded from the Single Market legislative program. As the CAP has developed, however, particularly with respect to the very complicated agrimonetary system, agricultural prices are far from common throughout the EC.

The breakdown of internal borders will have significant implications for EC agricultural production, marketing and demand

On the production side, dismantling of the agrimonetary systems will change internal price relationships which should result in shifts in production within the Community. Similarly harmonisation of plant and animal health standards should increase efficiency of production and shift production away from the less efficient producers in the Community, unless the same form of national compensation is introduced to maintain the status quo.

On the marketing side, increased efficiency in the transport sector and the introduction of uniform labelling laws should reduce costs for Community agriculture as well as for exporters of agricultural and food products into the Community.

On the demand side, the market will be influenced by increased economic growth: increased productivity and income should result in increased demand for high quality food products. Consumer demand will also be modified by environmental and health concerns.

The 1992 program will not only impact on the agricultural sector but also have a profound impact on the food industry and food prices.

Harmonisation of food labelling laws and health regulations should have implications for the food processing sector while changes to the value added tax regimes for food will have a significant effect on food prices.

The changes in Eastern Europe, particularly the unification of Germany, and the current GATT round will be key factors affecting EC agriculture.

There is increased economic integration between West and East European countries. The EC has recently concluded cooperation agreements with nearly all East European countries, providing in some cases, increased access for agricultural products. Certainly, the unification of Germany will result in the extension of the CAP to East German agriculture with consequences for EC production. Changes to the three key areas of support, - internal price support, export subsidies and market access - are critically dependent on the outcome of the current GATT negotiations.

Australian exports of agricultural products to the EC will be determined more by the GATT outcome than by the Single Market Program, but there could be significant implications for the international meat trade and wool exports.

The elimination of foot and mouth disease, if this was to be achieved, will result in a greater number of EC Member States having the potential to access Australia's most important markets and lead to pressure for export restitutions in order to be competitive in these markets.

On the other hand, the Single Market is expected to have positive implications for wool exports to the EC. Increased incomes resulting from the Single Market should increase wool consumption and because the only import barrier to wool is the 2.5 per cent tariff on tops, there would be more opportunities to increase exports.

Harmonisation of food standards will have both benefits and disadvantages for third countries.

With the harmonisation of sanitary and phytosanitary standards and food quality standards, including food additives and labelling, trading in the Community should be simpler and more cost effective because it will mean dealing with a single set of standards for the whole Community.

However, should the standards in themselves be too restrictive, there could be problems for third countries in meeting these standards. Already, the Third Country Directive on animal disease adopted by the EC has resulted in a cessation of Australia's previously limited trade in cattle, sheep and goats.

Difficulties are of course, not limited to the Third Country Directive on animal disease. With the harmonisation of standards, it is not unreasonable to expect that problems in such areas as hormones/pizzle rot will continue to arise in the future.

Although the Single Market Program will not change the access rules for Australia's agricultural exports, the removal of internal barriers should, in most cases, make trading throughout the EC easier.

Since the implementation of the CAP, imports of agricultural products by EC members have been replaced rapidly by products produced within the Community. Following the entry of the UK to the Community in 1973, Australian exports to the EC decreased dramatically.

The Single Market Program will not result in a significant change in the access rules for third countries. Access to the EC's agricultural market is very much dependent on the outcome of the Uruguay Round. If the negotiations in the Round prove to be successful, agricultural production of highly protected products in the EC could be expected to be lower with improved access conditions. These factors should be to Australia's advantage. They would not only enhance prospects for increased exports of agricultural products to the EC but also result in rises in the world price.

Although access to EC markets will not improve as a result of the Single Market, in many respects, trading with the EC will be easier. With the harmonisation of standards (e.g. hormones, bovine, antibiotics, animal welfare) exporting to countries in the EC should be easier, provided those standards are not in themselves restrictive.

The changes to the transport regimes will make movement of goods within the EC more efficient and cost effective which should be of particular benefit to exporters of highly perishable products, including fruit and vegetables.

Should the EC manage to eradicate foot and mouth disease, Australian exports of meat and meat products could be adversely affected.

Aspin-off of harmonised standards will be improved disease control in the EC in certain situations. For example, foot and mouth disease (FMD) could well be eradicated in 1992 with significant implications for the international meat trade.

If the EC manages to achieve FMD-free status Community-wide, meat products from a greater number of Member States will have the potential to access Australia's most important markets, which could lead to pressure from these States for export restitutions (despite the Andriessen Assurance) in order to be competitive in these markets.

Secondly, meat and livestock from FMD regions would face additional restriction in the EC market. A consequence of this is likely to be that more intense competition would arise in the remaining countries in the Middle East and South East Asia that accept product from FMD areas, and this could adversely affect Australia's beef and mutton trade in those countries.

With the expected economic growth, there could well be improved opportunities for specific products, particularly wool.

Australia's wool exports are not subject to the same rules as most other agricultural products. Wool is not a commodity in which the EC could aspire to self-sufficiency, and therefore it is not subject to an internal support regime.

Wool produced as a by-product of the sheepmeat regime is not suitable for clothing/apparel manufacture. As wool is an important input to the EC textile and clothing industry, it faces no barriers to entry other than the 2.5 per cent tariff on tops.

As a result of these differences, the implications for wool are somewhat different to those for other commodities. The Single Market is expected to be a positive development with increasing incomes in the Community resulting in an increase in wool consumption.

The establishment of uniform but tight environmental controls will probably result in a relocation of early stage wool processing from the EC, probably to Asia. The implications of this for Australian wool exports are expected to be a reduction in greasy wool exports but with increased exports of semi-processed product.

Other opportunities for Australian exports could arise from changes in consumer demands. As an example, there is a small but growing market for organically produced food and food produced under low and controlled input farming methods.

In terms of opportunities for specific products, there will continue to be export opportunities for quality wheat, to meet shortfalls of high protein wheat in the EC. Access to meat and perhaps dairy produce markets could be possible under negotiated access arrangements and there could be seasonal opportunities for horticultural products (except dried vine fruits) if quality standards can be met. Australian wine is selling well in the EC and there may be opportunities to expand sales further as economic and income growth increases.

How should companies approach trading with the EC in 1992?

A fundamental requisite in continuing to sell agricultural produce and processed food into the EC is the need to meet the quality requirements both in terms of health regulations set by the EC and preferences determined by EC consumers.

In general, it will be important to apply the concepts and linkages involved in agribusiness such as establishing direct linkages between the farmer and the retailer. These types of linkages are increasing worldwide and are evolving on the basis of the most efficient combinations and linkages within the global agrifood chain.

There also may be value for companies wishing to operate successfully in the EC to examine methods used by other countries which have had successes. For example, there is an expectation that Japanese companies will move into a dominant position in the food industry. The key factor which apparently gives the Japanese an advantage is their superior understanding of product engineering.

The Japanese *modus operandi* in every market has been firstly, surveying the customers and establishing perceived preferences and dislikes, then proceeding to design-out the negatives or the dislikes. They would then launch the product at a lower price than their competitors.

In an integrated European market, the need to simultaneously meet the requirements of European standards and consumer demands, including product quality, implies that the Australian processed food industry will have to apply more sophisticated methods of market analysis, increase its marketing skills and install more flexible production techniques. This in turn will require highly skilled management and staff and higher levels of investment in training.

The structure of the European food industry will change significantly with major food retailers dominating an intensely competitive market.

The European food industry traditionally has been highly fragmented. The structural diversity of the industry has been due partly to barriers to free movement of goods. However, limited trade between Member States could also be attributed to variations in market demand and cultural factors which determine food consumption patterns.

Thus, the potential for exporting national brands on a Community-wide basis has remained limited. Now only a few food products are marketed throughout the Community, indicating that even with the removal of all regulatory barriers, it is unlikely that 'Europe-wide' food products could be marketed, at least for some time.

These cultural and demographic factors have led to multinational food manufacturers concentrating on the production of foodstuffs locally, for local consumption. In terms of capital, production experience and management skills, multinational companies have retained their market advantage and will continue to be a major force in the food industry.

Australian food exporters, particularly small to medium companies, will need to be flexible and establish a presence in the EC.

While dominance of the major food retailers is likely to increase, there will remain possibilities and a place in the market for smaller companies able to react quickly and with greater flexibility who are able to innovate in response to rapidly changing market demands. The development of private label products has created valuable niche markets for small and medium sized companies.

Nevertheless, these small firms will remain very dependent on the larger scale distribution networks and may have difficulties during the process of market restructuring that will take place.

Thus, companies wishing to sell food to the EC in 1992 will need to establish in the EC, through merger and acquisition, direct contact with retailers or sell to clearing houses servicing a smaller proportion of the market.

Australian winemakers already have established this type of presence in the EC by purchasing vineyards in France and Italy. It needs to be recognised however that there may be limits to how far back in the food chain investments can be made. There have been reports that attempts to invest in European farms have proved to be very difficult.

The creation of a Single Market should result in greater economies of scale (by being able to operate Community-wide), lower costs (with the harmonisation of animal & plant health regulations), simplified cross border movement of goods and reductions in transport costs and financial savings from dealing with a European product.

Australian multinational corporations in Europe have approached the EC as one market for some time, and companies like these should be in a strong situation post 1992 in terms of production and efficiency gains and cost reductions on transport and administration as the remaining internal barriers to trade come down.

It is clear that if industry is to meet successfully the demands of an integrated European market, it will need to ensure that its management and staff are highly skilled and well trained. This implies that greater investment will be required in the area of training and development.

However, Europe 1992 is essentially a place for big business; the small and medium businesses will need to find niche markets which will yield useful returns. A unified European market will be such a huge economic system that it will not be possible to extract the full range of potential benefits without being inside the system.

Thus, 1992 will provide a challenge for Australian companies, particularly the smaller firms wishing to do business in the EC. The Single Market Program will produce larger, more efficient competitors who will be formidable rivals not only in the European market but also in third country markets.

Australian companies wishing to succeed should pay close attention to EC standards and consumer preferences and, where possible, establish the agribusiness type of linkages.

Any company with aspirations to sell into the Community in the future, should pay close attention to EC standards. To the extent standards are still to be established, those concerned should work closely with various standards organisations, and in Brussels, to make sure the standards are not unnecessarily restrictive.

The difficulty for exporters from third countries with no locally established connections is that they do not have any direct access to the standards making process for the 1992 program.

Under existing arrangements, the Commission is advised by the 'Food Advisory Committee' which is composed of representatives of consumer groups, industry established in the EC (multinationals gain access in this respect), trade and catering establishments, unions and farmers. While an EC subsidiary of an Australian company may sit on the Food Advisory Committee, third country exporters may not.

The rationalisation of standards in the food sector could result in benefits for larger third country food processing companies but smaller firms may suffer some difficulties as standards are put on a Community-wide basis.

Nevertheless, market access should be enhanced for all exporters, within the broad access rules, because only one set of standards would have to be met instead of separate ones for each of the 12 countries.

The main benefits of European integration, however, will flow from increased competition. Firms from third countries will need to take strategic positions in the market by strategic partnering and other means.

In addition, agribusiness type linkages can be expected to increase as the Single Market is established. These factors, combined with the growing concentration of retailers and the control they have over the market, will result in an extremely competitive market. In these circumstances, marketing will be a very difficult proposition if linkages are not made with retailers and agrifood businesses. Association with these entities will not only hold the possibility of export benefits, but also technology transfer with spin-offs for both the food processing industry and its support industries.

Although it is likely that consumer differences across Europe will continue to exist for some time, 'Europe-wide' products, (particularly in the growth areas of demand, that is, processed products, convenience foods and health foods) could become increasingly successful as European television and European advertising comes into play.

In addition, higher GNP for Europe means increased demand for goods and services.

Access to agricultural markets will however, be determined more by the GATT outcome and to some extent the EC's response to Eastern Europe. If there is a successful outcome in the Uruguay Round, it would be reasonable to expect lower levels of agricultural production in the EC and better access conditions. Similarly, the EC's economic and trading relations with Eastern Europe, as well as agricultural policies adopted by East European will have a significant impact on Australian exports.

Thus for those companies that can meet EC standards there will be new opportunities arising from the increase in demand.

Sweden moves towards EC membership

In October 1990, the Swedish Government made a major reversal of foreign policy in deciding to apply for membership of the EC. Previously, Sweden had taken the view that membership would be incompatible with its firm and longstanding policy of neutrality.

That stand increasingly had been brought into question by opposition parties and others, who argued that the necessity of EC membership for Sweden's future prosperity was compelling. Sweden could only lose out, they argued, by continuing to stand outside the institutional mainstream of western European economic and political development.

Sweden already was beginning to see many companies voting with their feet by taking their investment funds out of Sweden and into the EC, to establish themselves there before the completion of the EC Single Market at the end of 1992. They were also seeking greener pastures than those of Sweden, which has been beset by declining industrial production and profit margins. In October 1990, this outward flow of funds became a flood, forcing Sweden to increase interest rates by five per cent in one week in an effort to slow the trend.

The announcement to seek EC membership therefore was presented as part of a package of economic measures, which also included cuts in government spending, a 10 per cent reduction in public sector employment over the next three years, and increased property taxes on offices, shops and commercial locations.

The Government, backed by the Foreign Affairs Committee of Sweden's Parliament, subsequently elaborated the view that Sweden's policy of neutrality needed to be reinterpreted in light of the changes in Europe and in east-west relations generally during the last two years. If those changes had not occurred, the arguments in favour of Swedish membership would have been no less compelling, but the fact that they did occur meant that the biggest single objection to membership lost much of its force. Sweden would nevertheless be uncomfortable with any EC moves towards the integration of military policy, and would therefore strongly prefer that NATO remain the organisation in which West Europeans conduct defence coordination.

In an unofficial, immediate response a Deputy President of the EC Commission, the Dane, Mr Henning Christopherson, welcomed the Swedish decision and advised Sweden to look at lodging an application in 1991 with a view to becoming a member from 1993. He said the EC would be ready to accept Sweden as a member after the completion of the Single Market process.

Both the Swedish Foreign Minister, Mr Sten Andersson, and Mr Christopherson suggested that it would be appropriate for Norwegian and Finnish applications to be lodged together. This view was welcomed by Norwegian Prime Minister, Ms Gro Harlem Brundtland, then in the process of forming her Government. Finnish President Koivisto was less enthusiastic and complained that such matters should be discussed between the Nordic countries before being referred to in public.

Sweden's application will add to the pressure on those countries to consider applying for membership rather than be left isolated in a Nordic enclave of their own.

Conversely, the decision has been welcomed by Denmark, a longstanding EC member, which has long urged its Nordic sisters to join it in the Community. In February 1990, Danish Prime Minister, Mr Poul Schluter, had been critical of the course of Nordic cooperation, particularly its economic dimension, claiming that in key areas the Nordics as a group had been left behind by the process of EC integration. He said then that he thought economic realities eventually would dictate full involvement by Nordic countries in the EC's decision making processes, leading a number of Nordics to apply for full EC membership in the near future.

Though the small Left Party (formerly the Communist Party) and Greens are strongly opposed to Sweden joining the EC, within Sweden the decision generally has proved popular. Support for membership covers a broad political spectrum, and the application therefore is likely to proceed regardless of the results of the elections scheduled for September 1991. Present indications are the elections are likely to lead to a change of government, with the ruling Social Democrats polling at 31.8 per cent. In deciding to seek EC membership they have neutralised one likely election issue that could have gone against them.

On 12 December 1990, the Swedish Parliament formally endorsed the Government's decision to seek membership and gave the Government a mandate to proceed.