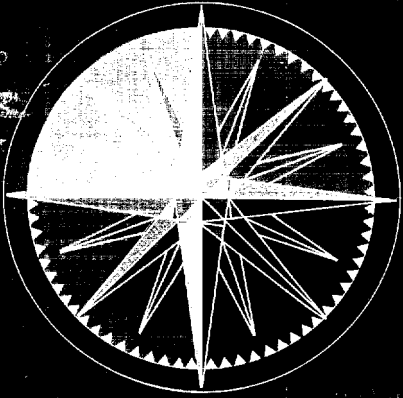


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SPECIAL REPORT

SIGNIFICANCE OF RECENT EEC FARM AND TRADE AGREEMENTS

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SIGNIFICANCE OF RECENT EEC FARM AND TRADE AGREEMENTS

The agricultural and trade policy agreements reached at Brussels in December by the six members of the European Economic Community have imparted fresh momentum to the integration process envisaged by the Common Market treaty. The agreements--concluded after arduous negotiation--are vague on important details, subject to varying interpretations, and still incomplete. Nevertheless, they have averted another community crisis over conflicting basic interests and have restored some of the sense of common purpose which De Gaulle nearly destroyed a year ago with his veto of Britain's bid for membership. Prospects for some further strengthening of community institutions are favorable, and the belief is current once more that increased economic unity will itself necessitate some form of unified political control. The goal of European political union remains elusive, however, and proposals for some kind of federal or confederal arrangement still face serious difficulty.

The Brussels "Package"

The December meeting in Brussels was largely the result of a German attempt to "synchronize" further progress toward a common agricultural policy, which will open up wider markets primarily for French products, with decisions of vital consequence for the others--notably the Germans and the Dutch--affecting their trade relations with non-members. As the 31 December deadline approached for agreement on the working program, both the French and the Germans stood firm on their respective national interests, and the final compromise gave no clear victory to either. The implementation of the agricultural regulations agreed upon is likely to be delayed longer than the French desire. On the other

hand, the Germans will be forced to await the Kennedy Round tariff negotiations, scheduled to get under way in May, before they will know how much success they had in gaining acceptance for a liberal approach on trade.

On the agricultural side, the "package" deal arrived at included regulations establishing common markets for beef and veal, rice, and dairy products, and a proposal for a regulation on vegetable fats and oils. The meeting also discussed a proposal regarding cereal prices, agreed on regulations governing a community-wide agricultural support fund, and issued a statement of intention regarding European parliamentary supervision of the support fund's management.

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The trade policy package includes EEC positions on the extent to which tariffs on industrial items should be cut in the Kennedy Round negotiations, and on exceptions to this cut. The trade package also contains a formula for determining so-called "disparities" in tariff levels, and a special formula proposed by the EEC Commission for dealing with agricultural products in the Kennedy Round.

Dairy Products

The problem of devising a regulation to establish free trade in dairy products in the EEC was complicated by the existence of large dairy surpluses in some EEC countries and the reliance of others on imports from nonmember countries to meet their large and growing demands.

The arrangement worked out to meet this problem calls for gradual adjustment of national milk prices toward a single EEC price by 1970. Germany and Luxembourg are permitted to continue direct subsidies during the transition period to ease the impact of their high-cost producers. The EEC Commission was directed, however, to "recommend" the gradual replacement of producer subsidies based on market prices with indirect "social" subsidies which do not encourage inefficient farmers. The effect of these arrangements will be to delay the opening of German markets to other member states, and Germany is permitted

to continue its imports of Danish butter. France and the Netherlands, however, will benefit immediately from increased community subsidies to finance exports of dairy products.

The Fats and Oil Problem

Arriving at agreement on the dairy products regulation was made more difficult because the competing interests of the various producers of edible oils had to be considered. Producers of milk and butter in Italy and France have insisted that the community surplus in these products could be reduced if consumers were not offered margarine at prices one third that of butter.

The Italians wished to link the dairy market with the fats and oil market--a draft regulation for which was also agreed upon--in such a way that taxes on margarine would finance disposal of dairy surpluses. This was not agreed to, but a tax on both community-produced and imported margarine was instituted, the proceeds of which will be used principally to support Italian producers of olive oil.

EEC sources anticipate that the tax will not raise the price of margarine enough to make butter more competitive. If margarine consumption declines, however, US interests could be hurt since the bulk of American soybean exports go to the Common Market for the production of margarine.

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The Rice Regulation

The conflict of interests between producing and importing countries was also the crux of the problem in the rice regulation, which establishes a clear preference in community markets for Italian and French rice. Implementing regulations still to be worked out will determine the exact degree of protection against US and other exporters. At German insistence, the members agreed to include in all agricultural market regulations a reference to an article in the EEC treaty which promises that interests of foreign exporters will be safeguarded.

Beef Products

In the negotiations regarding the beef and veal market, the French and Dutch hoped to assure for themselves an increased share of the growing Italian and German markets. The latter countries, however, sought to protect their own livestock raisers and maintain their imports from non-EEC producers. The protection agreed upon is at a higher level than originally proposed by Germany and Italy, but the Italian interest in preserving Latin American exports of frozen meat was satisfied. Concessions were made in the case of German imports of Danish beef. The US has been concerned that increased protection of the EEC market might force major world exporters of beef to find other customers, thus exerting more pressure on US markets.

Grain Prices

On the key agricultural question in the Common Market--the unification of the various national grain prices--the Brussels negotiators postponed action until next April.

Under the terms of the EEC treaty, the establishment of one price for each grain is not mandatory until 1970. However, the plan submitted by EEC Commissioner Mansholt last fall accelerates the timetable and would establish a common grain market now by unification of prices at a level about midway between current German and French price levels. Because of domestic political considerations, Bonn has rejected any such move before 1966 at the earliest, but the Erhard government may yet agree in principle to the Mansholt plan provided implementation is delayed.

While postponement of a decision on the Mansholt plan thus leaves unresolved a matter of major political as well as economic import to both the EEC and its trading partners, it also avoided the possibility of a major break between France and Germany.

Technical considerations will be important in settling the issue--e.g., the effect of the price level proposed by Mansholt in expanding French output and discouraging the higher cost German production. Considerations of political bargaining will also be important; Germany may exploit France's

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interest in getting the agricultural issue settled to promote French agreements to tariff reductions in the Kennedy Round.

The Mansholt proposal raises difficult questions for the EEC's foreign grain suppliers. To the extent that European grain production expands under the Mansholt Plan, it threatens the interests of the US and other grain suppliers of the EEC. The higher the prices set by the community, the greater the encouragement to European grain production at the expense of foreign suppliers. Moreover, early unification of grain prices would affect such exporters more suddenly than unification at the final stage of market integration in 1970. On the other hand, price levels in Europe are trending upward, and the prices proposed by Mansholt now are probably lower than those which would be set if price unification is delayed to a later date.

The Agricultural Fund

Completing the agricultural package are the decisions which will set into operation the European Orientation and Guarantee Fund. Established in 1962, but inactive up to now, the fund will provide community-wide financing for the disposal of surpluses and for the reorganization and modernization of community agriculture.

Contributions to the fund are to be made both from national budgets and, increasingly, from

the accumulated levies on imports from nonmember countries. Since West Germany is the largest importer of foodstuffs in the EEC, these arrangements will in effect result in substantial German support for the marketing of France's export surpluses. Germany succeeded, however, in obtaining a reaffirmation of the treaty provision that its total contributions to the community's budget shall not exceed 31 percent of the total budget.

Because it is unclear how the fund will work in practice and because of the huge sums involved--perhaps \$800 million by 1970--the Dutch insisted that the fund be placed under the control of the European Parliament. This will be discussed later this month in connection with the problem of reinforcing that body's budgetary powers.

The Kennedy Round Mandate

While these decisions on agricultural questions have important implications for the American farmer, the main US interest in the year-end agreements at Brussels focuses on decisions regarding the EEC's position in the coming tariff bargaining at Geneva. The member states approved as a "working hypothesis" the US objective of a 50-percent linear cut in tariffs as set forth in the US Trade Expansion Act (TEA). However, few European officials really expect this objective

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will be realized. Despite the efforts of the Dutch and Germans to induce a liberal EEC attitude on trade matters, the positions adopted at Brussels on specific TEA issues reflect to a considerable extent the protectionist views of France.

On agricultural trade, the members agreed that farm products should be included in the Kennedy Round, but on the basis of a proposal--the "second Mansholt plan"--which has raised serious objection in Washington. Under this plan an attempt would be made to calculate and to compare total amounts of agricultural support, subsidization, and protection among the various countries. The technical difficulties involved in this approach would be formidable. The Common Market's level of protection, which would in principle be the subject of bargaining in the Kennedy Round, will not be determined until 1970. The US has also taken the position that such matters as price and income supports should be treated apart from customs protection in separate negotiations on nontariff obstacles to trade. In sum, it remains unclear whether the EEC intends only to offer non-members some assurance that their present EEC markets would be preserved rather than to negotiate an expansion of trade in accordance with the general aim of the tariff conference.

The directives given the EEC Commission for negotiating on industrial products are also unclear in several important

respects. The central issue is whether the tariff cut on industrial products shall be as deep as 50 percent or something less. Closely related, however, are the problems of the number of exceptions to be allowed from any linear cut agreed upon; the terms and conditions for negotiating nontariff barriers to trade; and how to deal with tariff "disparities," i.e., sizable differences in levels of protection for the same product in different countries.

Largely because of the intense French interest in it, the disparities question has tended to predominate in the discussions. The EEC now is proposing to define as a disparity and treat as an exception to any linear tariff reduction those tariffs which in one country--say the US--are twice as high as those in the EEC and separated by at least ten percentage points. Although the number of disparity items so identified would be reduced somewhat by certain additional "qualitative" criteria, the US, British, and other observers believe the EEC's formula would permit it--in a substantial number of cases--to claim justification for a smaller reduction in its tariffs than it would expect of others.

Whether the opposition of the other Kennedy Round participants will be sufficiently strong to compel the EEC to retreat from this approach is far from certain. France's support of the disparity formula is based

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to some extent on its desire to reduce the scope of any over-all tariff reduction. The prospects thus do not seem bright that France would compromise on this point, except as part of a package which would include the other outstanding questions.

Implications for
Community Institutions

The great difficulty which the EEC countries had in reaching the year-end agreements has drawn attention once more to the problem of the future development of the community's institutions. The manner in which agreement was finally reached has resulted in a further extension of the effective influence and authority of the EEC Commission. This trend seems likely to continue because the Commission's arbitral role inevitably carries with it a measure of political authority.

Community observers have been impressed by the great skill with which the Commission played this role in the end-of-year conference. This was demonstrated in its handling of the Mansholt grain price unification plan, which even though it has not yet been accepted, helped reduce growing tension over this problem. Moreover, the Commission's agricultural-trade package as a whole was evidently so well prepared and realistic in terms of the conflicting interests involved that the French accepted it almost immediately and the Germans did so after only short deliberation.

The enactment of further common regulations in pursuit of closer economic integration has made it more difficult and expensive for any member to disrupt the Common Market. This is especially true in the case of France. By insisting on a further integration of agriculture, Paris has formalized its dependence on the other five. Moreover, despite De Gaulle's distaste for supranational institutions, he achieved his objective in this instance with the assistance of the supranational Commission, and in the process enhanced its prestige.

Fusion of Executives

Further strengthening of the institutional framework of the European community is also the objective of the plan to merge the executives of the EEC, the Coal-Steel Community, and EURATOM, which is to be discussed by community ministers in late February. A move toward a formal merger of the communities themselves at a later date, the plan would combine the three councils, the two commissions, and the High Authority, and establish all of them in a single location. If approved, such a merger would increase the prestige of the community executives, enable them to attract personnel of a higher caliber, and improve coordination among the three communities. This reorganization would strengthen the executive's hand particularly in dealing with problems such as the common energy policy which now span the competencies of the three existing communities.

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However, inasmuch as the present community administrations or "technocracies" in the eyes of some European political leaders tend already to usurp national powers, an even more centralized executive would probably give rise to new demands that it be brought under some form of control. Some of the pressures to "control the technocrats" have in the past come from those who feel that the primacy of the member states is endangered. Others are genuinely interested in assuring that the European bureaucracy is in fact controlled by the European Parliament.

Chancellor Erhard in particular has recently stressed the need to strengthen the European Parliament, but he has offered no specific proposals. In practice, the parliament has been increasingly given to debating issues under consideration by the Common Market Council of Ministers. These debates have tended to reinforce rather than limit the three community executives because of the strong federalist bias which prevails among the parliamentary members. There is at present no consensus on the need for direct election of members--a project the federalists have long attempted to push. The best prospect, therefore, for enhancing the presently weak role of the parliament is in the budgetary field, notably in connection with the adminis-

tration of the agricultural fund.

European Political Union

Apart from these specific moves to strengthen existing community institutions, there has been much talk in the capitals of the Six in recent months about possible new initiatives toward a more general European political arrangement. There has been a general feeling, reinforced by the Brussels compromises, that renewed progress in economic integration is creating a more favorable climate for political discussions. Many European observers believe that the international role which De Gaulle foresees for Europe and for France cannot be achieved without political ties among the Six--ties going beyond those the Common Market is forging. Nevertheless, all the old obstacles to political unity continue to exist, and it is still questionable whether recent events have made them less formidable.

The negotiations on a political union treaty foundered in the so-called Fouchet Committee in 1962, in part because the other five feared that France wanted to subordinate the existing community institutions to the new ones--in which Paris would retain a veto. De Gaulle has since acquiesced in the strengthening of the Brussels institutions, but he has given them no

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credit for the year-end agreements, and in his 31 January press conference, he harked back to his political union proposals of two years ago.

The 1962 talks also foundered on the question of Britain's participation in the discussions. De Gaulle referred in his 31 January press conference to the question of Britain as one of the problems which has lost its "virulence." Since December when rumors of some new initiative toward political union began to be heard, however, the British Government has made a concerted effort among France's five partners to assure Britain's participation in any such negotiations. Moreover, while none of the five has any confidence that London would contribute anything positive to such political negotiations, the Netherlands seems to have assured the British of its support.

The main reason that agreement on a European political union still seems distant, however, is that the prospective participants fear they may have to accept Gaullism as the price of unity. They are disputing not so much how the union should be organized as they are over the policies the union will follow--especially its relations with the US. In a federal union, or in league with Britain, they would feel relatively certain of not being obliged to follow where De Gaulle might lead should they choose not to do so. The other five will be gratified that De Gaulle now feels the EEC is in a better position to proceed with the Kennedy Round. They will be less comforted, however, that De Gaulle still sees European political cooperation as the alternative to "surrender of Europe to control by America." (CONFIDENTIAL NO FOREIGN DISSEM)

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