

Market failures and government failures: A theoretical model of the common agricultural policy

PETER NEDERGAARD

*International Center for Business and Politics Copenhagen Business School Steen Blichers Vej 22
DK-2000 Frederiksberg Denmark
(E-mail: pne.cbp@cbs.dk)*

Accepted 30 September 2005

Abstract. Economic theory has tried to explain the characteristics of the Common Agricultural Policy inductively on the basis of certain economic peculiarities of agriculture. However, by overlooking the so-called government failures of the political system as an independent variable in explaining the Common Agricultural Policy it is impossible to explain, for example, the strong agricultural lobbyism. The deductive theoretical model of this article integrates economic as well as political actors in order to explain the characteristics of the Common Agricultural Policy. The proposed theoretical model is not “tested”, but the criteria for such a test are presented.

1. Introduction: In Search for a Theoretical Model of the Common Agricultural Policy

The aim of this article is to propose a deductive theoretical model for analysing the Common Agricultural Policy (CAP) of the European Union. Of course, one could ask for the reasons for proposing a theory for a specific policy in a specific international area of cooperation. The arguments for proposing a specific theoretical model for the CAP are several: (a) The co-operation in the agricultural policy field of the European Union is the oldest and the most developed area of supranational co-operation which has created a large number of characteristic path dependencies, (b) the CAP is based on an economic sector with some rather peculiar economic characteristics which have to be considered in the theoretical model, and (c) the CAP also has some specific characteristics as far as interest organisations in the sector are concerned.

Whether or not a theory is a good theory depends on the criteria against which theories might be evaluated. Burchill (1996: 24) has proposed a set of criteria for an evaluation of an international relations theory: its understanding of an issue or a process, its explanatory power, its success at predicting events, its consistency and coherence, its scope, and its capacity for self-reflection and engagement with contending theories. At the end of this article, the usefulness of the proposed theoretical model will be evaluated against these criteria.

Analysis of European Union affairs often has its roots in neofunctionalist integration theory. Neofunctionalism was built around the proposition that an international society of states can acquire the procedural characteristics of a domestic political system (Rosamond, 2000: 56) through a number of

“political” and “technical” spill-overs. In 1963, Lindberg noted that groups “may change their political organization and tactics in order to gain access to, and influence, such new central decision-making centres as may be developing” (Lindberg, 1963: 9) as a result of European integration. Later on it was noted that neofunctionalism failed to acknowledge the importance of external factors for European integration (Hansen, 1969), and that it failed to identify the dependent variable of functional economic integration (Haas, 1971). Both of these criticisms will be taken into account in the proposed theoretical model of the Common Agricultural Policy in this article.

Neofunctionalism has also been criticised by the intergovernmentalists. But whereas their criticisms focused on the so-called history-making moment, such as treaty revisions or major crises in the European Union they also often neglected day-to-day politics within the European Union political system. Hence, more and more scholars have argued for a greater use of public policy literature (for example Hix, 1999; Pollack, 2003; Richardson, 1996) due to the fact that the EU political system has become more and more a “normal” political system. This can be seen by the fact that the policy-making process in the European Union is evermore characterised by conflicts over redistribution, regulation, and stabilisation with the active participation of interested actors as well as Member States and where, so far, the regulatory functions have dominated (Majone, 1996).

In this article it is argued that the Common Agricultural Policy can only be understood and explained if economic analysis is coupled with an analysis of the political system as proposed in rational choice theory. Here, it has to be taken into account that the Common Agricultural Policy (CAP) means that the European Union can be considered as *one* multi-level governance system in the agricultural policy area where the Member States function as integrated elements of the internal decision-making asymmetries that are, according to rational choice theorists, always found in democratic political systems.

In order to establish a theoretical model of the CAP, welfare economics and the concept of market failure become important as a precondition for explaining *why* such a strong regulatory framework of the CAP was set up. However, in contrast to much economics literature the independent variable in the explanation of the Common Agricultural Policy is not found in economic characteristics alone. Therefore, in Section 2 below the concept of welfare economics and market failure is contrasted with the concept of government failures in the rational choice theory. In Section 3 the basic features of the theoretical model of the CAP are explained whereas the rest of the article elaborates on the various elements of this model. In Section 4 market failures and their impact on farmers on the supply side of the economic system are analysed whereas Section 5 analyses market failures on the demand side of the economic system of agriculture. Section 6 analyses the government failures of the political system and their impact for farmers and consumers on the

demand side of the economic system. In Section 7 government failures of the political system and their impact on politicians and bureaucrats on the supply side of the political system are analysed. Finally, Section 8 concludes by considering the merits of the proposed model.

2. Market Failures and Government Failures

Agricultural politics and agricultural economics has been studied for many years with the help of economic theory in order to explain (and sometimes even justify) existing agricultural policies *and* also to propose policy instruments that are optimal according to the theory. For example, analyses based on welfare economics theory have been made of which political instruments the governments should use in order to maximise economic welfare. According to welfare economics theory, market imperfections can be corrected through public expenditures and public regulations only if they are based on a rational and scientific planning (Randall, 1985). Following this line of reasoning there are lots of proposals on how to solve the market imperfections of the agricultural economic system: direct income support, regional labour market policies, elimination of price support policies etc. These proposals have been on the table for many years as methods to correct market imperfections in a rational, scientific and welfare economic optimal way. What is common to all of these proposals is that they consider, as traditional welfare economics theory does generally, so-called market failures as their starting point.

Over the years, many economists have tried to explain the various agricultural policies of the developed countries on the basis of variations of the welfare economics theory like, for example, public economics theory. Munk (2004) is a representative of this theoretical school. He explains the supportive agricultural policies as a more or less “pure” function of two factors: (a) whether or not a country is a net exporter of agricultural products (net importers of agricultural products tend to provide support at a higher level than countries which are exporters) and (b) the level of difference between the income of farmers and non-farmers. The assumptions made in this explanatory model are that the behaviour of the political system is an outcome of the maximisation of a social welfare function based on egalitarian value preferences and that these preferences are relatively stable.

This economic “functionalist” explanatory model of the agricultural policies, however, seems unable to answer a number of questions about the characteristics of agriculture in general and the Common Agricultural Policy in particular. If agricultural support is a “pure” function of certain economic characteristics, why should farmers then invest so many resources in lobbying the agricultural political decision-makers at national as well as at European level? At the same time, if the low incomes are the explanation, why do other low

income groups not receive the same amount of support as the farming group? Besides, if claiming that low incomes is the explanation of the Common Agricultural Policy, how does this correspond to the fact that 20 per cent of the wealthiest farmers receive nearly 80 per cent of the total agricultural support included in the CAP? Finally, if the position as net importer is the explanation, why are other net importers not supported in the same way as agriculture is supported.

Instead of using economic theory as the sole basis for explaining the agricultural policies of the developed countries and thereby overlooking all characteristic features of the political system, political actors should be included in explanations of agricultural policies. In other words, the political black box should be opened, which also implies that the altruistic assumptions about the political actors should be revised because it becomes openly illogical to model actors in the economic system as self-interested whereas the same actors striving for the same benefits in the political system are modelled as altruists. In Section 3 the political black box of the CAP is opened in order to analyse the individual decision units that are the political decision-makers (European politicians and “agro-bureaucrats”) and political partners (European farmers, consumers, and taxpayers) with an interest in the agricultural policy of the European Union. Here, the proposed theoretical model is explained. The independent variable of the model is the strong organization of farmers made possible by the low cost of organizing lobbyism in the Member States of the European Union. The costs of organizing farmers implies costs of establishing farmers unions at local, regional, national and European levels including setting up a political and organizational secretariat, a board that meet on a regular basis and activities directed toward influencing political decision-makers and the wider public audience. The central argument presented here concerns why the costs of organizing farmers are so low. In short, it is argued that income problems of farmers combined with a sufficient number of selective incentives to organize farmers and a lack of counter-weights to the agricultural political decision-making process has led to a CAP which can hardly be fundamentally reformed without a strong pressure from political players outside of the European Union.

Not the least when it comes to the CAP criticism of the welfare economics theory as a sole explanation of the policy has been strong. The reason is not that the instruments and objectives in the CAP are different from what is found in many other developed countries in agricultural politics. The reason is rather that the CAP is scrutinised with great interest by many actors outside of the European Union because it has become a major player in the international markets for agricultural goods.

The US Department of Agriculture (e.g. 2001) has often analysed the impact of the CAP on production and trade. Among other things, they conclude that the CAP has considerable impact on world markets and that the world

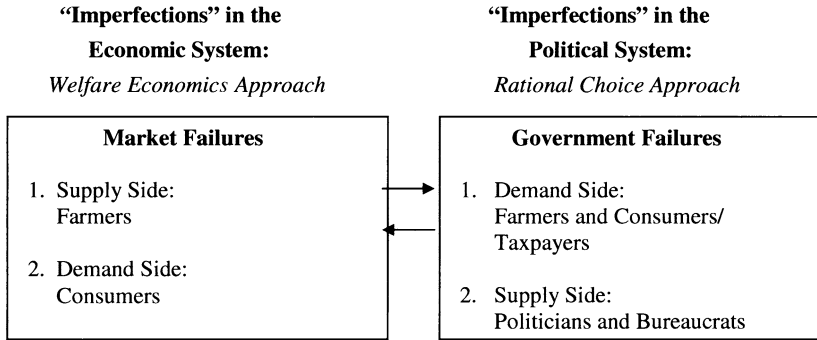
market prices have decreased and become more unstable as a result and forced a considerable contraction elsewhere. They also point to the welfare losses for European Member States as well as for traditional exporters of agricultural products outside of the European Union.

At the same time, critics have also noted that the objectives of the CAP (i.e. increase productivity, increase farmers incomes, stabilize markets, safeguard supplies, reasonable consumer prices) often contradict each other. The policy instruments of the CAP often fail to reach their objectives and, sometimes, the developments of the CAP have even moved in the opposite direction of the objectives. The aim of this article is exactly to answer why this is the case based upon a deductive theoretical model which takes its beginning in a few assumptions about the political system.

3. The Theoretical Model of the Common Agricultural Policy

In this article, it is argued that an analysis of the CAP will benefit from combining traditional welfare economic theory concerning agriculture with rational choice theory. In the proposed theoretical model, at the micro economic level the unit of analysis is the individual decision-makers in the market, i.e. producers and consumers. If the micro economic model of supply and demand model is transferred to the political system, the relevant decision-units are the political decision-makers (politicians and bureaucrats) and political partners (producers and consumers) with an interest in the political decisions in this particular area. This is the methodological individualist foundation of the theoretical model. Politicians and bureaucrats supply political decisions while producers and consumers demand political decisions. As in neo-classical microeconomics theory all parties are expected to maximise their utility function no matter whether the analysis is dealing with producers (revenue and expansion), consumers (purchasing power and purchasing possibilities), taxpayers (level of taxes), politicians (re-election and government power) or bureaucrats (power base and career possibilities).

At the micro level, market failures mean that economic actors become potential rent-seekers in the political system and create government failures which influence the microeconomic level, resulting in further increase: in market failures. In the model presented here there is a structural casuality between factors within the economic system and factors within the political system. However, there is no automaticity in the model as far from all producers facing certain market failures will eventually become rent-seekers. In order to be succesfull rent-seekers a number of producer specific circumstances have to be fulfilled. At the same time, the equilibrium between suppliers and demanders of political decisions is dependent both on how powerful the demand is and on how the demand is spread between politicians, bureaucrats, producers



Source: Compiled by the author.

Figure 1. Model for analysing the common agricultural policy of the European Union.

and consumers. In any case, it is assumed that there are a number of economic interests in the political system that try to build coalitions because different political decisions lead to different benefits and costs for the various groups in society.

In Figure 1 above the arguments put forward above are put together in a model for analysing the Common Agricultural Policy of the European Union.

Following the methodological individualism of the rational choice theory, the starting point of the theoretical model is the individual farmer producing agricultural products for the consumer. Potentially, the economic problems he is facing can bring him in contact with political decision-makers. To use the terminology of Albert Hirschman (1970), denied easy exit, the farmers try to exercise strong political voice. Of course, agricultural policy decisions taken by politicians and bureaucrats also have impact at the macro level of society, i.e. on the economic and political systems of the European Union as a whole.

The arrows between the boxes in Figure 1 indicate structural causal relations between the two boxes in the theoretical model. In other words, it is assumed that market failures in the agricultural markets via the strong political voices of farmers will potentially trigger political interventions, the character of which will eventually be decided by the equilibrium between the politicians' and bureaucrats' supply of political decisions, on the one hand, and the farmers' (the producers') and consumers' and taxpayers' demands, on the other hand. At the same time, this equilibrium is biased or asymmetric because it is dominated by the farmers demand for political interventions (strong demand = strong political voices) in the form of price support, income support, import restrictions, export restitutions etc., while the consumers and taxpayers as a whole only have few claims (weak demand = weak political voices) or a low level of interest in agricultural policy decisions. At the same

time, government failures have an impact on market failures which they often tend to increase as it will be shown below.

The model above is a theoretical model for analysing the CAP. The model has a dynamic of its own. At the same time, the causal relations in the model can be put under pressure from factors outside the European Union, as has increasingly happened in the last 15 years within the GATT and the WTO or more directly by the United States. However, it is predicted that such external pressures on the CAP will trigger internal reactions in the European Union in accordance with the theoretical model. This means that an external pressure will lead to changes and adjustments in the Common Agricultural Policy that are “filtered” through the mechanisms shown in the model.

4. Market Failures and the Supply Side: Farmers

A broad definition of market failures – at least as far as agriculture is concerned – includes stabilisation, allocation and income problems. The reason why the market mechanisms lead to these problems is certain characteristics of the supply of agricultural goods – and to a lesser extent of the demand of agricultural goods (cf. Hallett, 1981).

The supply of agricultural goods has two main characteristics. Firstly, the farms are geographically spread and great in number. This implies a specific system for collection and treatment of the agricultural produce, for example, in form of dairies and slaughter-houses. Furthermore, the production factors in agriculture are characterised by immobility and lack flexibility in response to price changes.

Secondly, the supply of agricultural goods is marked by the fact that the goods (to a larger extent than in industry) are produced on a risk market. This reflects the lack of information on future prices, exchange rates and other farmers production (Runge and Myers, 1985). One reason for this is the biological nature of agricultural products. This taken alone leads to annually unforeseeable fluctuations in the supply of agricultural products and it leads to the concentration of the supply of products to certain seasons. Besides, the biological nature of agricultural products limits the durability of the products and makes storage and processing necessary.

A result of the fact that agricultural products are produced on an inflexible risk market is that the supply is chronically unstable. This means that the supply and demand in the agricultural sector fluctuate more than supplies and demands in other sectors of the economy. This instability is often used in order to socially construct political legitimisations of institutionalised public support for agriculture. In agricultural economics the fundamental instability of agricultural production is often illustrated by the so-called cobweb theorem of which the hog cycle is an example.

According to agricultural economics, the great number of farms also means that the individual producer only has a very limited proportion of the total production and therefore has no influence on the price of the products. In other words, the individual producer is faced with a horizontal demand curve and is a price-taker. At the same time, it is often claimed that in comparison with industry, where the market is often characterised by oligopolistic competition, the individual farmer is in a situation with perfect competition. In other words, according to this view that is cultivated by farmers and their representatives, agriculture is like a perfect competition island in a sea of oligopolistic competition. The reason is that the large number of farmers producing the same products compared to the number of producers producing the same products in the industry makes it either impossible – or extremely expensive – to organize price or production “coordination” among the farmers themselves. At the same time, the organization of farmers in order to get political influence seems to be a much easier way to go and also involves much lower organizational costs due to the fact that only a few farmers need to be involved in this process even though the results of their activities benefit all farmers. In industry, the situation is the opposite. Here, a smaller number of producers often makes it much cheaper to organize “price coordination” within the market without involving the political system.

The competitive situation in agriculture might be a probable explanation of parts of the structural income problems in the sector. On the one hand, the structural income problem is used as another factor to construct a legitimisation of the institutionalised public support for agriculture. On the other hand, the specific agricultural characteristics mentioned so far cannot explain the “overconsumption” of the productive means that seems to take place when the level of incomes is considered. Rational behaviour means that the consumption of productive factors is decided by the point where the marginal product of increased factor consumption equals the marginal costs of increased factor consumption. Therefore, the factor consumption should fall in the case of falling product prices no matter whether they are produced in a market with perfect or imperfect competition (Meiners & Yandle, 2003).

However, the “overconsumption” of productive factors in a situation with perfect competition can be explained using the introduction of new technology as an example (Hagedorn, 1983). In the long run, the farmer cannot expect to improve his income position by introducing a new technology. On the other hand, he is forced to constantly introduce new technology in order to keep his relative income position. Perfect competition in agricultural markets means that the advantage of production rationalisation is widely externalised. At this point, agricultural firms are fundamentally different from industrial firms.

Olson (1985) has also analysed the differences between agriculture and industry starting from the fact that agricultural firms need land. Production based on land makes coordination and management more difficult in agricultural

firms. Therefore, diseconomies of scale are reached at a much lower level of turnover in agriculture than in industry. In the 19th century, very large farms with hundreds of employees existed in the United States, but these farms could not compete with the smaller and seemingly more efficient homesteaders. In other words, it seems that the optimal size of an agricultural firm (the owner and, perhaps, one or two employees) is much smaller than that of an average industrial firm with many thousands of employees. As a result, the number of farms is large enough to create a market with full competition.

The many and geographically spread agricultural firms are individually owned and, as mentioned, normally run by the owner and his family alone or by means of one or two employees. Hence, the variable costs are often small compared with industry. In the short run, variable costs are only things like fodder, fertiliser, energy and repair costs. While wages represent the largest cost in many industrial firms, farmers can almost never cut costs by dismissing workers.

At the same time, the costs of moving resources from agriculture to non-agricultural sectors have to be paid by the farmer himself. So, while the advantage of structural changes in agriculture is externalised, the costs are internalised (Hagedorn, 1983). In this perspective, the highly supportive agricultural policies in almost all industrialised countries could be seen as compensation for the fact that the majority of farmers do not benefit from the structural changes they work so hard to accomplish, even though other economic sectors are also under pressure from rationalisation among a few entrepreneurs. If this interpretation of the situation in agriculture is diffused to the wider public and is broadly accepted, a consequence is that it will probably be harder to oppose agricultural support by consumers and taxpayers. At the same time, the fact that it is often very costly, because of sunk costs and few alternative job opportunities, for farmers to make an exit from their business is probably a necessary incentive if farmers have to exercise a strong political voice. However, as it will be argued in Section 6, it is not a sufficient incentive.

5. Market Failures and the Demand Side: Consumers

Generally, the demand for agricultural goods is characterised by low income elasticity. According to research by agricultural economists, the food products in the European Union taken as a whole have an income elasticity coefficient of about 0.2. This means that the consumption of food products increases by 20 per cent every time income increases by 100 per cent. Adam Smith (1776), we may recall, noted that one of the differences between agricultural goods and industrial goods is that the consumption of agricultural goods is limited by the size of our stomach while the consumption of industrial goods seems to be without limits at all.

At the same time, the demand for agricultural products is characterised by small increases in consumption resulting from decreasing prices even though the changes in demand as a result of price changes differ considerably from product to product. In other words, the demand for agricultural products is characterised by both low income elasticities and low price elasticities.

In the political system, the fact that agricultural goods are both necessary goods for survival and, at the same time, are “overmatured” products on the market with low income and price elasticities can be exploited by farmers in their argumentation with the public – somewhat similar to the tradition of subsidising or protecting other “overmatured” products at the end of the product life cycle like ships, coal, and textiles. Again, however, besides being “overmatured” products, other factors must play a role, since agricultural goods are significantly much more protected than other “overmatured” products.

6. Government Failures and the Demand Side: Farmers and Consumers/Taxpayers

Market failures in agricultural markets imply a fundamental insecurity in production, and specific agricultural economic conditions do provide permanent income problems for a great number of farmers. This situation creates an incentive among farmers to view it as legitimate to use the political system through collective action as an alternative way to pursue their own economic interests. Stated in the terms of the rational choice theory, farmers see that their economic profit-seeking in the market is unsuccessful. Instead, they look for possibilities via political rent-seeking and organization in an interest group (Krueger, 1990). However, just to have an incentive to organize in order to become a political rent-seeker is not enough.

In order to be rational, when an economic actor decides to join or participate in an interest group, he has to judge whether the potential benefits exceed the foreseeable costs. Costs are incurred by the administration and co-ordination that is necessary in order to acquire political influence through an interest organization. If an economic actor belongs to a group with structural features which imply few organizational costs, this group must be expected to be easy to organise. For farmers this is an important factor for the strength of their group organization. Their preferences are similar, the size of the group is large, and the sector has some specific economic characteristics which more or less invite potential participants to be part of the group (Nello, 1984).

However, at the same time, similar to other large interest groups, farmers run the risk of some members’ free-riding when they organise themselves in order to acquire political influence with the aim of enhancing common interests. Political influence has many features in common with public goods since it is impossible to exclude non-organised farmers from benefiting from the efforts made by the organised farmers. For example, all farmers in the

European Union will benefit from a rise in the common minimum prices or increasing protectionism that are partly results of the political activity of the agricultural organizations.

Olson (1965) was the first to point out the necessity of selective incentives if individuals are to participate in a collectively beneficial activity that looks like a public good. The selective incentives of trade-union membership in many European countries are so-called exclusive agreements (=all workers at a workplace have to be organised in a certain trade union), that the unemployment benefit system is organised by the trade unions, etc. However, the selective incentives of the agricultural interest organizations are probably much more efficient. These selective incentives are partly due to the integration of agricultural interests organizations into the body of public administration. For example, that the partly publicly-financed consulting services of the farmers are administrated by the agricultural interest organizations themselves, that those applying for different kinds of public support and milk quotas are first treated by the agricultural interest organizations, etc. At the same time, the subscription fee paid by farmers is normally symbolic because the administrations and secretariats are often financed by funds, etc., that were originally created by public means. Hence, as a result, the affiliation percentage in the agricultural sector of the European Union member states and in most developed countries as well, is considerable above that of wage-earners. Additionally, the costs of acquiring political influence have been minimised among farmers because of the existence of a privileged group of farmers with considerably individual resources and money. This elite group dominates national agricultural interest organizations and, to an even greater extent, the farmers' European Union-level organization, the *Comité des Organisations Professionnelles Agricoles de la CEE* (COPA). Some would argue that the design of the CAP – even after the latest reform (cf. OECD, 2004) – is a reflection of this fact, i.e. that the CAP benefits the biggest farmers the most.

As mentioned earlier in this article, another explanation of the agricultural sector's organizational strength relates to the economic conditions to which farmers are subject. The constant pressure on incomes makes it easy for agricultural organizations to create a basic consensus and socially construct a well-defined goal to improve the incomes through protectionism, public price support or direct financial support.

One interpretation of this phenomenon is the following: The farmers find it legitimate and attractive to invest in political lobbying in order to compensate for the situation that the agricultural sector does not benefit from the introduction of new technology because the benefit from the introduction of new technology in agriculture is externalised (i.e. this externality is a benefit which is not subject to market transactions between the farmer and the consumer). Lobbyism at the national level as well as at the European level aims to ensure that the costs of introducing new technology are externalised

as well. At the same time, however, bad economic conditions are far from being an adequate explanation for the costly agricultural policies all over the industrialised world. In the retail sector and in other economic sectors as well, incomes are often on average as low as those in the farming sector. However, the retail sector and many other economic sectors have proved themselves very unsuccessful in getting support through the public budgets. The explanation of this difference offered in this article is partly that the organizational costs in the farming sector are lower due to the causes mentioned above, and partly and more fundamentally, that there are no Olsonian selective incentives in the retail sector which are necessary in order to participate in a collectively beneficial activity like being organized in a strong interest organization.

While farmers can be regarded as demanders of agricultural support and interventions, the demand of the consumers and taxpayers is expected to pull in the opposite direction. In other words, farmers are expected to be supporters of agricultural protectionism and subsidies, while consumers and taxpayers are expected to be opponents of agricultural protectionism and subsidies.

In this light, the actual level of protectionism can be regarded – according to the proposed theoretical model – as a function of the investment made in political influence on behalf of the farmers and consumers/taxpayers respectively. The result is assumed to be an equilibrium situation between opponents and supporters of agricultural expenditures and protectionism against the background of calculations of the marginal benefits, respectively the marginal costs, of the investments made in political influence.

The equilibrium situation in the agricultural political market is asymmetric because the farmers are able to press the slope of their lobby-curve downwards due to the selective incentives (see also Ballisacan and Roumasset, 1987). That is, for example, not the case for firms in the retail sector. As a result the farmers are 'over-motivated' to use money and time to further their collective interests which are reflected in agricultural protectionism and subsidies to the agricultural sector. The potential opponents of the farmers are consumers and taxpayers, but they are seldom organised at all. Besides, the marginal benefit of opposing the farmers resulting from lower taxes and consumer prices is very limited among a great number of consumers and taxpayers.

Therefore, the political decision-makers assume that consumers and taxpayers stay relatively calm and indifferent when import tariffs are introduced, food prices are kept well above the world market level, and farmers are subsidized. Farmers, on the other hand, often see the benefit of investing time and resources in protest meetings, demonstrations, attacking trains with imported agricultural products, blocking the roads with tractors, burning tyres, etc., if the import limitations, direct income support and export funds are conceived as unsatisfactory (see also Olson, 1982). A factor that might pull in the opposite direction is, perhaps, increasing environmental awareness which puts independent but, so far only comparatively weak pressure upon the decision-

makers in the agricultural policy arena. At the same time, in recent years, the suppliers as well as demanders of agricultural support have managed to redefine parts of the agricultural subsidies as compensation for achieving various environmental policy goals. Also, the enlargement of the European Union from May 1, 2004, has put pressure on the CAP, but exactly because of the asymmetry of the European agricultural political system, one should not expect a radical change of the CAP due to the enlargement as far as the costs of the CAP is concerned.

7. Government Failures and the Supply Side: Politicians and Bureaucrats

The farmers strong interest organizations (relative to other sectors) and the consumers' and tax payers' relatively weak interest organizations are necessary conditions for political decisions being pro-agricultural in a status quo perspective. Besides, political decision-makers (politicians and bureaucrats) are required to be willing to fulfil the wishes of farmers to a smaller or larger extent.

In this context, it is a widespread notion that politicians and bureaucrats in a democratic society make decisions reflecting the wishes, attitudes and preferences of the people, especially according to the political goals that are common among a majority within the electorate. Such decisions are assumed to make up the foundation of the political decisions of society.

According to the rational choice theory, however, the existence of such correspondence between the democratic, collective decisions and policy objectives based on individual preferences is a much too optimistic, although long lasting, democratic theory. Because the gain from limiting agricultural expenditures or agricultural protectionism is spread collectively among all taxpayers and consumers, extraordinary incentives are needed to mobilise taxpayers and consumers in the political process, and still, and more fundamentally, the selective incentives are lacking. In the same way, the costs of the expansion of expenditures or of protectionism have to be paid by all taxpayers and consumers. Again, extraordinary incentives are needed to mobilise taxpayers and consumers. Their loosely organised groups, however, are confronted with a smaller, but much more homogeneous group of farmers who enjoy the benefits of an expansion of the agricultural expenditures or protectionism and who are hurt by a cut in agricultural expenditures or free trade. The gains and losses of this group are concentrated and private in character.

Generally, it is predicted that the resistance against consumer-financed support is less intensive than against taxpayer-financed support because higher prices as a result of protectionism are more difficult to blame on agricultural lobbyism than higher taxes. As a result, farmers are normally in favour of price support measures. On the other hand, taxpayer-financed support is more acceptable if the measures have an "objective" character based on discretionary

and bureaucratic criteria. Besides, the fact that taxpayer financed support through the CAP originates from the EU agricultural fund which is again financed by Member States' contribution to the EU budget means that the connection between taxes paid in Member States and the CAP expenditures is not very clear for many taxpayers. Hence, one should not expect significantly stronger pressure against subsidies paid by consumers than subsidies paid by taxpayers in the European Union.

At the same time, because of the marginal impact of rising and decreasing agricultural protectionism or budgetary expenditures, electorates in general have no incentives to have a specific interest in the CAP. The individual farmer, however, has an income which is to a large extent a function of political decisions. His motive for influencing the policy is therefore very strong. Agricultural organizations will gather information about what political representatives do as far as agriculture is concerned, whereas the general public does not bother to keep themselves informed on these matters. Hence, it is no wonder that politicians are tempted to pay specific attention to the interests of agriculture.

Normally, politicians decide on a political issue according to how voters will react. Voters, on the other hand, have to consider the costs in time and money when they form their preferences and transmit them to the politicians. If the voter is rational, a minimum of benefits for him is necessary if he wants to pay the costs of collecting information and transmitting preferences to the political decision-makers (Nello, 1984). As mentioned above, just getting information about the impact and size of public support for agriculture is difficult and costly because very often either the support is "hidden" in the prices or it is "hidden" in bureaucratic measures.

In rational choice theory – where "the political market" is used as a metaphor – it is assumed in the theoretical model that politicians "supply" political decisions in order to be re-elected. According to Winters (1987) re-election depends on the following factors: the number of voters affected by the political decisions, how voters are affected by political decisions, the political influence of the affected voters, whether or not the politicians regard it as acceptable that certain groups of voters get benefits, the possibility that the affected group of voters will punish the politicians for a bad political result and whether or not a bad political result for an affected group will have an impact on public opinion or not.

Hence, one should expect a falling willingness of politicians to supply the farmers with agricultural subsidies and protectionism as the number of farmers decline. Especially in relation to agricultural policy decisions, however, it is often the case that the support of agricultural organizations is more important than indicated by the actual number of votes of the agricultural sector. The reason is that supporting agriculture gives politicians a base for attracting non-agricultural votes from rural areas. Also, in general, the agricultural

organizations have a high political profile because an important part of the farmers' incomes stems from political rent-seeking. This means that the basic condition for the survival of farmers and farmers' organizations is to be found in the creation of public awareness. Politicians with a friendly attitude towards agricultural interests will benefit from this. Additionally, in most developed countries, rural areas are over-represented through the electoral system, i.e. there is an institutional bias towards agricultural interests within the political system.

Alongside the politicians, the bureaucrats are important suppliers of agricultural decisions. In rational choice theory it is assumed – even though politicians formally take the political decisions under consultation with the administration – that bureaucrats are also independent actors who are maximising utility by preserving or expanding their power base, their career possibilities etc. In the agricultural area, bureaucrats probably have quite a considerable amount of influence in the agricultural policy area because this area is characterised by a lot of technicalities and many specific rules. A result of the technical character of agricultural policy is that politicians avoid dealing directly with the many regulatory and distributive questions in agricultural policy. When political decisions are transformed into quasi-political and bureaucratic-technical questions, agricultural policy takes on a seemingly objective character. Not least the Common Agricultural Policy has given national bureaucrats an institutionalised influence in making regulations through a network of regulatory and administrative committees. At the same time, it gives the bureaucrats making the inputs to the political process an extremely large amount of influence (Winters, 1987). All else being equal, one must therefore expect that bureaucrats in the agricultural decision-making process prefer agricultural reform which uses bureaucratic instruments instead of a liberalisation or a market orientation of the agricultural policy which would reduce the need for bureaucratic interventions and bureaucrats in general.

Normally, in rational choice theory, it is often assumed that bureaucrats involved in the agricultural decision making process gain no immediate benefits from the political decisions taken. As mentioned above, the major implicit goals of agro-bureaucrats are to increase their power bases, responsibilities, staff, and career possibilities. These goals are best achieved the more complex and technical the agricultural policy is, and the more important agriculture is as an economic sector, the more agriculture is governed politically rather than by market forces. Therefore, in general, agro-bureaucrats are expected to oppose changes in agricultural policy if it involves strong market orientation, less support for agriculture and a smaller agricultural sector. Bureaucrats must even be expected to be more in favour of continuing and building up agricultural protectionism than agro-politicians because they gain fewer benefits from taking general national or European economic and political considerations into account. Bureaucrats can normally only be expected to move away from the

agricultural protectionist line if the present agricultural policy directly weakens their relationships with other parts of the administration. For example, the Commission's Directorate-General for Agriculture has for years been pressing for a moderate reform of the CAP because continuation of the former line was creating an increasing number of conflicts with the surroundings within the Commission and with external actors outside of the Commission. In particular, the agricultural policy has been damaging the international relations of the European Union and its reputation in general.

In the CAP, the general asymmetry which – according to rational choice theory – is always present in collective political decisions, is sharpened by the “suppliers” who have independent reasons for reinforcing a complicated, protectionist “super asymmetric” agricultural policy. However, a stronger reflection of individual preferences could be achieved by limiting the general asymmetry of political decisions and by limiting asymmetry that is specific to agriculture. Generally, in rational choice theory it is recommended to set up institutions in order to put restraints on the utility maximising actors whether they are interest groups or Member States. These institutions should be designed in order to bring about a larger degree of correlation between the particular interests and the common interests. In the CAP, one way of doing so could be to strengthen the horizontal political element in the now very “segmented”, technical and highly complex agricultural decision-making process. This can be done by letting other politicians, rather than agro-politicians alone, participate in the agricultural decision-making process. Increasingly, this is also what is happening, especially because the ministers of finance, the ministers of foreign affairs, the ministers of the environment etc. have in recent years sometimes played a – however limited – role of counterweight to the agricultural policy-making process, not least in cases of major reform initiatives with regard to the agricultural policy and the EU budget.

The European Parliament is also a horizontal political element in the European decision-making process. In the constitution adopted in June 2004 (but not yet ratified) the Parliament is supposed to participate fully (before the Parliament was only “consulted”) in the decision-making procedure concerning CAP as far as legislation *and* budgets are concerned. The problem is, however, that the Parliament is long away from playing the role of an active counterweight at the European level to specific sectoral interests. Until now the Parliament has normally always taking a very positive stance concerning all kinds of European legislation and European political initiatives in order to increase its European power base. Although it should not be forgotten that the parliamentarians have no power to tax citizens and companies and, therefore, are never held responsible for increasing budgetary expenditures because of the CAP. A more radical way to reduce the asymmetric characteristics of the CAP would be to renationalise the CAP or part of the CAP. Then, of course, European integration would loose the potential neofunctionalist spill-overs from

the CAP to other policy areas. However, one could argue that these spill-overs (to the customs union, the internal market, the economic and monetary union, etc.) have already been exploited. At the same time, it is difficult to identify from where the decisive pressure could come from in order to bring about such a renationalisation of the CAP. Another way of making the asymmetric agricultural policy less asymmetric is by setting certain constraints on, for example, the EU budget for agricultural policy. Such ceilings have also been decided at the EU level by the European Council even though these ceilings still allow the agricultural expenditures to increase. The problem is, however, that the support for the agricultural sector can take many other forms than what can be seen on the budgets, and that the budgetary discipline decided upon at the European Councils is seldom followed in practise.

All in all, it is very difficult to come up with internal European “institutional solutions” in order to fundamentally change the CAP. Hence in general, according to the proposed theoretical model, fundamental changes of the Common Agricultural Policy are expected only to come due to hard pressure from actors outside of the European Union as it was seen in during the world trade negotiations in 1992 and 2003. The “iron construction” of the various interests embedded in the CAP can only be “deconstructed” in any significant extent if and when the CAP comes under fire from strong political players outside of the European Union. Still, however, such an external pressure on the CAP will lead to adjustments which are in accordance with the political asymmetries that remain in existence within the European agro-political system.

8. Conclusion

The aim of this article is to propose a deductive theoretical model of the Common Agricultural Policy of the European Union which provides an understanding of the issue, has explanatory power and able to predict events, that is consistent and coherent, covers the full scope of the research objects, and has a capacity for self-reflection and engagement with contending theories.

The proposed theoretical model is an interdisciplinary model drawing on elements from economics and political science. As argued by North (1990: 5), such a theory should build on individual choices because this theoretical approach is logically consistent, and because it can, by integrating individual choices with institutional constraints, serve as a major step toward unifying various social science theories. Hence, methodological individualism is a starting point of the proposed theoretical model.

The next point of departure for the proposed theoretical model for the CAP is the existence of a number of market failures when market failures are seen in a broad perspective. The market failures here cover certain characteristics of the supply and demand of agricultural goods as well as some peculiar characteristics as far as the production of agricultural products is concerned.

Among other things, a result of the peculiarities of agricultural economics is permanent income problems, that is, problems with economic profit-seeking which means that farmers have a potential interest to organise themselves in order to become political rent-seekers. In their efforts to organise themselves the farmers are helped by their perennial income problems and homogenous preferences. This is the foundation for their “logic of collective action.”

At the same time, normally, and more fundamentally important, the farmers have great success in avoiding ‘free-riding’, which is always a problem when interests are organised. This is due to the existence of a number of selective incentives. Besides, politicians and bureaucrats are motivated to supply farmers with public support. Still, the expected opponents of agricultural support, i.e. consumers and taxpayers, are too weakly organised and too little interested in making any forceful counterweight to farmers and agricultural politicians.

The general asymmetry between farmers and consumers is sharpened in the political system of the CAP because it is possible to push the costs of expansion of agricultural production to other Member States and countries outside the European Union. At the same time, many of the institutionalised counterweights that exist at the national level are either very weak or do not exist at the European level. This is why the political system of the European Union could be characterised as a “super asymmetric” political system as far as agricultural policy decisions are concerned.

The proposed theoretical model of the CAP is not “tested” in this article. However, such a test has some rather clear success criteria. For example, the predictions on the basis of the theoretical model are a) that the European Union has large obstacles that are almost impossible to conquer when it itself wants to fundamentally reform the CAP, b) that the level of support to the agricultural sector is very difficult to bring down in a reform process meaning that a reduction of one kind of support will probably lead to a shift to another kind of support and c) that there is a structural tendency to increasing bureaucratisation of the CAP as it changes due to, for example, external pressures and d) that the resistance from the tax payers and consumers vis-à-vis the protectionism and subsidizing of farmers will be relatively small.

Some would argue that the proposed theory is somewhat “reductionist” as it is build on a specific set of assumptions, which, if accepted, automatically lead to the next step in the theoretical model. Others might criticize that the proposed theoretical model leaves almost no room for, for example, a reform process based on ideals and principles. Still others might criticize that fundamental changes of the CAP *can* happen due to rational entrepreneurs within the European Union like the Commission.

At the same time, even though the proposed theoretical model is very much in accordance with the basic assumptions of neo-classical economics theory, and, therefore, should be no stranger to economists and political scientists,

there might be some truth in the criticism. There is a danger that theories are simply written off because they do not fit with the basic assumptions of a rational choice based theoretical model of the CAP. This might be a hindrance of self-reflection and self-critique. Therefore, of course, the proposed theoretical model of the CAP should be used with an open mind in order to integrate insights from other theoretical schools.

Acknowledgments

I would like to thank my research assistants, Kasper Lindschow and Thomas Horn, for their assistance in preparing this paper. I would also like to thank Ove Kaj Pedersen, Leonard Seabrooke, Anker Brink Lund, John L. Campbell, Gorm Rye Olsen, Anders Buch Kristensen and an anonymous referee for their comments on an earlier draft of this paper.

References

- Ballisacan, A. M., & Roumasset, J. A. (1987). Public choice of economic policy: The growth of agricultural protection. *Weltwirtschaftliches Archiv* (123), 232–248.
- Besley, T. (2004). The new political economy working paper. London.: London School of Economics and Political Science, Department of Economics.
- Buchanan, J. M., & Tullock, G. (1962). *The Calculus of Consent: Logical Foundation of Constitutional Democracy*. Ann Arbor: Ann Arbor Paperbacks.
- Buchanan, J. M. (1979). *What Should Economists Do?* Indianapolis: Liberty Press.
- Bulmer, S. J. (1983). Domestic Politics and European Community Policy-Making. *Journal of Common Market Studies*, 21(4), 349–363.
- Bulmer, S. J. (1994). The governance of the European Union: A new institutionalist approach. *Journal of Public Policy*, 13(4), 351–380.
- Burchill, S. (1996). Introduction. In S. Burchill & A. Linklater with R. Devetak, M. Paterson and J. Tone (Eds.), *Theories of International Relations*, 1–27. Basingstoke, MacMillan.
- Campbell, J. L. (2004). *Institutional Changes and Globalization*. Princeton and Oxford, Princeton University Press.
- Cochrane, W. W. (1985). The need to Rethink Agricultural Policy in General and to Perform some radical surgery on commodity programs in particular *American Journal of Agricultural Economics*, 67(5), 1002–1009.
- Haas, E. B. (1971). The study of regional integration: Reflections on the Joy and Anguish of Pretheorizing. In L. N. Lindberg & S. A. Scheingold (Eds.), *European Integration: Theory and Research*, 3–43. Cambridge Mass.: Harvard University Press.
- Hagedorn, K. (1983). Reflections on the methodology of agricultural policy research. *European Review of Agricultural Economic* 10(4), 303–323.
- Hallett, G. (1981). *The Economics of Agricultural Policy*. New York: Wiley.
- Hansen, R. D. (1969). European Integration: Reflections on a decade of Theoretical Efforts. *World Politics*, 21(2), 242–271.
- Hill, P. J. (2003). What's So Special about the Farm?. In Meiners, R. E. & B. Yandle (Eds.), *Agricultural Policy and the Environment*, 1–18. Lanham/Boulder/New York/Oxford: Rowman & Littlefield Publ.

- Hirschman, A.O. (1970). *Exit, Voice and Loyalty: Responses to Decline in Firms, Organizations and States*. Harvard: Harvard University Press.
- Hix, S. (1999). *The Political System of the European Union*. Basingstoke: Macmillan.
- Koester, U. (1991). Economy-Wide Costs of Farm-Support Policies in the Major Industrial Countries. In K. Burger, M. D. Groot, J. Post, & V. Zachariassen (Eds.), *Agricultural Economics and Policy: International Challenges for the Nineties*. Essays in Honour of Prof. Jan de Veer. 3–16. Amsterdam/New York: Elsevier.
- Krueger, A. O. (1990). 'Asymmetries in policy between exportables and import competing goods. In N. Jones, & B. Krueger (Eds.), *The Political Economy of International Trade*, 161–178. Cambridge, Mass.: Basil Blackwell.
- Lindberg, L. N. (1963). *The Political Dynamics of European Economic Integration*. Stanford: Stanford University Press.
- Majone, G. (1996). A European Regulatory State? In J. Richardson (Ed.), *European Union: Power and Policy-Making*, 263–277. London: Routledge.
- Meiners, R. E., & Yandle, B. ed. (2003). *Agricultural Policy and the Environment*. Lanham/Boulder/New York/Oxford: Rowman & Littlefield Publ.
- Moyer, W., & Josling, T. (2002). *Agricultural Policy Reform. Politics and Process in the EU and US in the 1990s*. Aldershot: Ashgate Publ.
- Munk, Knud, J. (1993). The Rationale for the Common Agricultural Policy and other Sectorial Policies. Brussels, European Economy. *The European Commission* (5).
- Munk, Knud J. (2004). Agricultural policy. A public economic explanation. Working Paper. Aarhus: University of Aarhus.
- Nedergaard, P. (1988). *EF's landbrugspolitik under omstilling*. Copenhagen: Jurist- og Økonomforbundets Forlag.
- Nedergaard, P., Hansen, H. O., & Mikkelsen, P. (1993). *Danmark og EF's landbrugspolitik. Tilpasning frem til år 2000*. Copenhagen: Handelshøjskolens Forlag.
- Nedergaard, P. (1995). The political Economy of CAP Reform, In Finn Laursen (Ed.), *The Political Economy of European Integration*, 111–144. The Hague/Boston/London: Kluwer Law International.
- Nello, S. S. (1984). An Application of the Public Choice Theory to the Question of CAP Reform. *European Review of Agricultural Economics*, 11(3), 261–283.
- Nello, S. S. (1997). *Applying the New Political Economy to Agricultural Policy Formation in the European Union*. Florens: European University Institute.
- Niskanen, W. A. (1971). *Bureaucracy and Representative Government*. Chicago: Aldine Atherton.
- North, D. C. (1990). *Institutions, Institutional Change and Economic Performance*. Cambridge: Cambridge University Press.
- OECD. (2003). *Agricultural Policies in OECD Countries: Monitoring and Evaluation*. Directorate for Food, Agriculture and Fisheries.
- OECD. (2004). *Analysis of the 2003 CAP Reform*. Directorate for Food, Agriculture and Fisheries.
- Olson, M. (1965). *The Logic of Collective Action: Public Goods and the Theory of Groups*. Cambridge, Mass.: Harvard University Press.
- Olson, M. (1982). *The Rise and Decline of Nations: Economic Growth, Stagflation and social Rigidities*. New Haven: Yale University Press.
- Olson, M. (1985). Space, Agriculture, and Organization. *American Journal of Agricultural Economics*, 67(5), 928–937.
- Pierson, P. (1996). The path to European Integration: A historical institutionalist analysis. *Comparative Political Studies*, 29(3), 126–163.

- Pollack, M. A. (2003). *The Engines of European Integration. Delegation, Agency, and Agenda Setting in the EU*. Oxford/New York: Oxford University Press.
- Piccinini, A., & Loseby, M. (2001). *Agricultural Policies in Europe and the USA. Farmers between Subsidies and the Market*. Houndsmill, Basingstoke/New York: Palgrave.
- Putnam, R. D. (1988). Diplomacy and domestic politics. *International Organization*, 42(2), 427–460.
- Randall, A. (1985). Methodology, ideology, and economics of policy. *American Journal of Agricultural Economics*, 67(5), 1022–1029.
- Richardson, J. (1996). Actor Based models of national and EU policy making. In H. Kassim & A. Menon (Eds.), *The European Union and National Industrial Policy*, 26–51. London: Routledge.
- Robinson, K. L. (1989). *Farm and Food Policies and Their Consequences*, New Jersey: Prentice Hall.
- Rosamond, B. (2000). *Theories of European Integration*. Houndsmill, Basingstoke/New York: Palgrave.
- Runge, C. F., & Myers, R. F. (1985). Shifting Foundations of Agricultural Policy Analysis: Welfare Economics when Risk Markets are Incomplete. *American Journal of Agricultural Economics*, 67(5), 1010–1016.
- Smith, A. (1776). *An Inquiry into the Nature and Causes of the Wealth of Nations*. Oxford: Oxford World's Classics. 1998 ed.
- U. S. Department of Agriculture (2001). Agricultural policy reform in the WTO: The Road Ahead. *Agricultural Report*, No. 802.
- Winters, L. A. (1987). The political economy of the agricultural policy of the industrial countries. *European Review of Agricultural Economics*, 14, 285–304.