



Reform of the Common Agricultural Policy

**Responsibility for the market, society
and cohesion of the EU**

Concept Paper of the European Milk Board

Table of contents

	Preamble	1
Chapter 1	Current orientation of EU agriculture and the dairy sector	
	Socioeconomic relevance of agriculture	3
	Deregulation in the dairy sector	6
	Current stabilisation measures in the EU and other parts of the world	10
Chapter 2	A new, responsible CAP for the market, for society and for cohesion in the EU	
	Objectives of a responsible CAP	12
	Fulfilling the new CAP goals	15
	Legal basis for an efficient crisis mechanism	17
Chapter 3	The Market Responsibility Programme: a system that reflects reality	
	Financing the system	20
	Effectiveness	20
	Contribution to international stability	20
	WTO compliance	21

Imprint

Editor:
European Milk Board asbl (EMB)
Rue de la Loi 155
B-1040 Brussels/Belgium

Contact:
Phone: +32 (0)2 808 1935
Fax: +32 (0)2 808 8265
office@europeanmilkboard.org
www.europeanmilkboard.org

© European Milk Board, Brussels 2017

Preamble

Balanced and resource-efficient

1. The societal expectations of the European Union's agricultural policy are diverse and justified. After all, it concerns nothing less than providing citizens with high-quality, healthy food as well as a resource-efficient cultivation, biodiversity and animal welfare. The citizens of the EU are in favour of balanced, responsible agriculture that adapts to the environment, rather than acting as a burden on the same due to concentrated overproduction. Agriculture should play its part in ensuring the social and cultural vitality of rural areas.

Fair pay – fair life

But it should also be about fair treatment of the people engaged in agricultural activity. Those who are contributing actively and constructively to the sector should not be neglected. Social dumping in agriculture should become a thing of the past.

Can the current CAP live up to these expectations? Does it consider the interests of EU citizens sufficiently?

2. As Chapter 1 of this policy paper clearly demonstrates, saying that the current CAP needs to be reformed is no exaggeration. Balanced production and fair income are specific aspects that it cannot guarantee in its current form. Paradoxically, real policies are moving further and further away from the legally enshrined objectives of the CAP. Though Article 39 TFEU very clearly calls for market stability and improved living conditions in rural areas through higher income, the reality presents a very different picture: the agricultural sector is characterised by **decreasing agricultural income** and **major instability**, especially in the dairy market. The constant crises that unsettle the sector can be traced back to the deregulatory policies that have characterised the dairy sector for years.

High price volatility and geographic concentration of dairy production, which negatively impacts the environmental and social fabric, are direct effects of such policies. The resulting crises have led to a detrimental regression to national interests and have negatively affected the harmonious

coexistence of people in the EU. Furthermore, deregulating the dairy sector leads to dumping and thus endangers markets in developing countries.

3. A new CAP must decisively counteract such developments and take responsibility for the markets, society and cohesion of the EU. Chapter 2 defines the six goals of such a progressive policy. The new CAP should: **a) ensure appropriate incomes; b) contribute to overcoming social inequality; c) ensure production throughout all regions; d) let producers assume market responsibility; e) make sure that production is responsible towards developing nations** and **f) abandon pure market illusions.**
4. To implement these goals, Chapter 2 also describes a **crisis mechanism** that should be included in the new CAP. The European Milk Board has developed the **Market Responsibility Programme (MRP)** to this aim. Quick and appropriate action can thus be taken in response to real developments and challenges affecting the sector. Considering the shocking regularity of crises causing upheaval in the dairy market, an effective crisis instrument is urgently needed. The MRP ensures cost-covering producer prices and thus lays the decisive foundation for balanced and fair production that considers environmental protection and animal welfare.
5. Chapter 3 tests the MRP for its conformity with respect to real conditions in the dairy sector and shows that the programme can be financed, is effective and conforms to WTO rules and can also contribute significantly to international stability.
6. The current reform is an opportunity to correct problematic developments and improve the cohesion of the EU through the agricultural policy. It is especially important to learn from past mistakes instead of blindly continuing down the path of deregulation. This is not something competent institutions and stakeholders can perhaps do, but in fact, something they must do. In this regard, we should not forget: the European Union not only has obligations towards its citizens but also has enough potential to live up to societal demands and give the agricultural policy a sustainable and fair direction. With this policy paper, we, European milk producers, would like to provide useful food for thought and thus involve ourselves in the reform discussions, so that the EU can work towards a truly common, integrative agricultural policy.

1

Current orientation of EU agriculture and the dairy sector

Socioeconomic relevance of agriculture

- Producing food
- Maintaining cultivable land and ensuring vibrant rural regions
- Generating jobs within the sector and in upstream and downstream areas
- Preserving and further developing regional traditions
- Investing in innovation and progress

7. The agricultural sector fulfils a range of important functions in the European Union. Thus, in one way or the other, it influences every single citizen of the EU. Ten million people are employed in the agricultural sector alone and this accounts for 5 percent of the total workforce.¹ As consumers, we all buy food from raw materials produced in the EU. Ninety percent of the EU population believe that agriculture plays an important or very important role.² At international level too, the EU is a clear heavy-weight. With a production value of approximately 411 billion euros³, it is one of the most important players in the global agricultural sector.
8. Milk is a raw material produced in every Member State and, at 15 percent, accounts for a significant share in EU agricultural production.⁴ In Europe and other parts of the world, milk production is very important for the socioeconomic development. It preserves lively rural areas and provides consumers with fresh, local milk products.

1 European Commission, "How many people work in agriculture in the European Union", EU Agricultural Economics Briefs, No. 8 - July 2013, p. 2. http://ec.europa.eu/agriculture/sites/agriculture/files/rural-area-economics/briefs/pdf/08_en.pdf (Download 24.02.2017)

2 European Commission, "Europeans, Agriculture and the Common Agricultural Policy" Eurobarometer Special 336, 2010, p. 8. http://ec.europa.eu/commfrontoffice/publicopinion/archives/ebs/ebs_336_en.pdf (Download 22.02.2017)

3 Figures for 2015, Eurostat

4 European Commission, "Milk and milk products", https://ec.europa.eu/agriculture/milk_en (Download 15.01.2017)

The Common Agricultural Policy (CAP) of the EU must do justice to the high importance of agriculture for Europe and other parts of the world!

9. The legal framework, in theory, takes this obligation into account. The objectives of the CAP as stated in Article 39 TFEU include ensuring a fair standard of living for persons engaged in agriculture, in particular by increasing their individual earnings, stabilising markets and assuring the availability of supplies. However, these objectives have taken a backseat in recent years and have made way for destabilising policies. As a result, agricultural income has been continually decreasing year on year, as shown by the real factor income index (Indicator A - see Table 1) or the agricultural entrepreneurial income (Indicator C - see Table 2).

Table 1: Indicator A - Index of real income of factors in agricultural activity per annual work unit, n-1=100 (compared to previous year)

Source: Eurostat

GEO/TIME	2010	2011	2012	2013	2014	2015	2016
European Union (28 Member States)	120.7	109.9	98.1	105.6	98.1	97.7	99.6

Table 2: Indicator C - Index of net entrepreneurial income of agriculture, n-1=100 (compared to previous year)

Source: Eurostat

GEO/TIME	2010	2011	2012	2013	2014	2015	2016
European Union (28 Member States)	120.7	113.1	96.2	106.6	92.4	92.8	96.8

Market stability is another goal that has not been achieved – a fact that is especially apparent in the dairy sector. The exact opposite is the case. Intensive deregulation and the related export focus have pushed the market balance out of whack. In the medium and long term, the resulting drop in the number of dairy farms (see Table 3) endangers the production and supply of regional milk products throughout the EU.

Table 3: Number of dairy farmers in the EU, 2007/2008 - 2013/2014

Source: EU Commission/ AHDB Dairy

GEO/TIME	2007/08	2008/09	2009/10	2010/11	2011/12	2012/13	2013/14
Austria	58,022	55,261	52,464	49,853	48,814	46,529	44,477
Belgium	12,626	11,932	11,329	10,672	10,261	9,836	9,390
Bulgaria	108,849	107,154	104,025	18,114	13,842	10,839	9,131
Croatia	-	-	-	-	-	-	13,036
Cyprus	433	229	225	225	219	217	212
Czech Republic	2,749	2,639	2,593	2,455	2,360	2,298	2,195
Denmark	4,940	4,538	4,320	4,152	3,968	3,801	3,622
Estonia	1,420	1,280	1,134	1,054	989	922	863
Finland	14,400	13,133	12,373	11,675	10,910	10,231	9,574
France	99,326	92,770	87,640	83,805	80,257	77,214	74,397
Germany	99,464	95,229	91,548	88,655	83,883	80,758	77,336
Greece	5,659	5,081	4,590	4,284	3,949	3,693	3,566
Hungary	6,344	6,420	6,011	5,768	4,725	4,315	4,170
Ireland	20,853	20,566	19,072	18,955	19,167	18,496	19,083
Italy	45,559	43,853	42,088	40,423	38,831	37,427	36,040
Latvia	20,280	17,589	13,639	12,225	11,558	11,186	10,654
Lithuania	69,321	60,774	50,538	46,586	44,351	41,335	38,772
Luxembourg	892	870	840	813	790	760	736
Malta	143	135	130	126	123	122	120
Netherlands	20,813	20,384	19,962	19,424	18,893	18,522	18,241
Poland	232,097	207,622	185,658	173,276	162,082	152,999	144,834
Portugal	11,011	10,045	9,186	8,057	7,487	6,959	6,471
Romania	663,231	503,582	432,837	384,959	367,971	335,037	304,692
Slovakia	798	803	875	874	850	830	807
Slovenia	10,368	9,834	9,377	8,883	8,479	8,152	7,851
Spain	25,832	24,005	23,062	21,874	20,665	19,646	18,798
Sweden	7,903	6,895	6,444	6,121	5,761	5,383	5,087
United Kingdom	17,752	16,873	16,154	15,511	14,977	14,504	14,060
EU 25 total	789,005	728,760	671,252	635,746	604,349	576,135	551,356
EU 27 total	1,561,085	1,339,496	1,208,114	1,038,819	986,162	922,011	865,179

Deregulation in the dairy sector

10. The active deregulation policy in the dairy sector was introduced in 2003. This policy reached its culminating point twelve years later with the abolition of milk quotas, which had been introduced in 1984 in response to massive overproduction at the time.

In the period from 2005 to 2015, production limits for milk were already raised by 9.8 percent in anticipation of the end of quotas, which led to a noticeable downturn in producer prices and plunged the sector into a crisis. Supply and demand were not matched and the resulting overproduction lowered prices in 2009 to 25 cents/kg milk (EU 27). The related losses for EU milk producers were to the tune of approx. 11 billion euros.⁵ This extremely low milk price forced many producers to close their farms and created a heavy financial burden for those who carried on.

Since the end of the quota system on 31 March 2015, the dairy market has been facing an even greater challenge as the system that has followed does not include any effective instruments. As a consequence, damaging overproduction cannot be avoided. Higher prices and farmers anticipating the imminent end of quotas led to a 4.3 percent increase in EU milk deliveries⁶ in 2014 alone. Together with volume increases of almost 10 percent in New Zealand and 2.4 percent in the USA, this resulted in a surplus of 11 million tonnes on the world market.⁷

11. Milk prices have continuously decreased since 2014 due to the pressure of overproduction: in the EU from 37.26 cents (average in 2014) to 28.46 cents/kg milk (average 2016), in the USA from 39.81 cents to 32.41 cents⁸, and in New Zealand from 32.58 cents to 25.54 cents⁹ in the same period. The Global Dairy Trade Index, too, moved downward. On 7 January 2014, it was at 1455 points and on 1 June 2016, it was down to a mere 697 points.¹⁰
12. The forecasts presented by EU policymakers in the lead-up to the abolition of quotas to support their deregulation strategy had predicted a moderate increase of volumes on the dairy market.¹¹ When compared with the real situation, it shows that they were way off the mark. As a matter of fact, instead of the milk deliveries of around 138 million tonnes estimated in 2010 (see Figure 1), the real volume already surpassed 152 million tonnes in 2016.¹² This situation did not emerge spontaneously, but could already be predicted when the projections were being formulated. Reliable and objective projections are, however, very important to evaluate the effects of a policy based on real conditions. **When prior estimates are cast into doubt as mere instruments to support a particular political strategy, institutions and authorities lose credibility.** But that is not all. It also paves the way for problematic developments – as has been the case in the dairy sector – leading to lasting damage to an entire sector.

5 Fink-Keßler, Andrea/ EMB, “Monitoring Agency” (short version), Kassel 2013, p. 4.

6 Gorn, Andreas, “AMI Markt Bilanz Milch 2015”, Agrarmarkt Informations-Gesellschaft mbH, Bonn 2015, p. 21.

7 Pflimlin, André, “Le marché laitier mondial est un piège pour les éleveurs et un pari fatal pour l’Union européenne”, 2015, p. 3. http://www.fourragesmieux.be/Documents_telechargeables/Marche_laitier_mondial_A_Pflimlin.pdf (Download 11.10.2015)

8 CLAL, “USA: Farm-gate milk prices”, http://www.clal.it/en/?section=latte_usa (Download 21.06.2017)

9 CLAL, “New Zealand/Fonterra: Farm-gate milk prices”, http://www.clal.it/en/?section=latte_new_zealand (Download 21.06.2017)

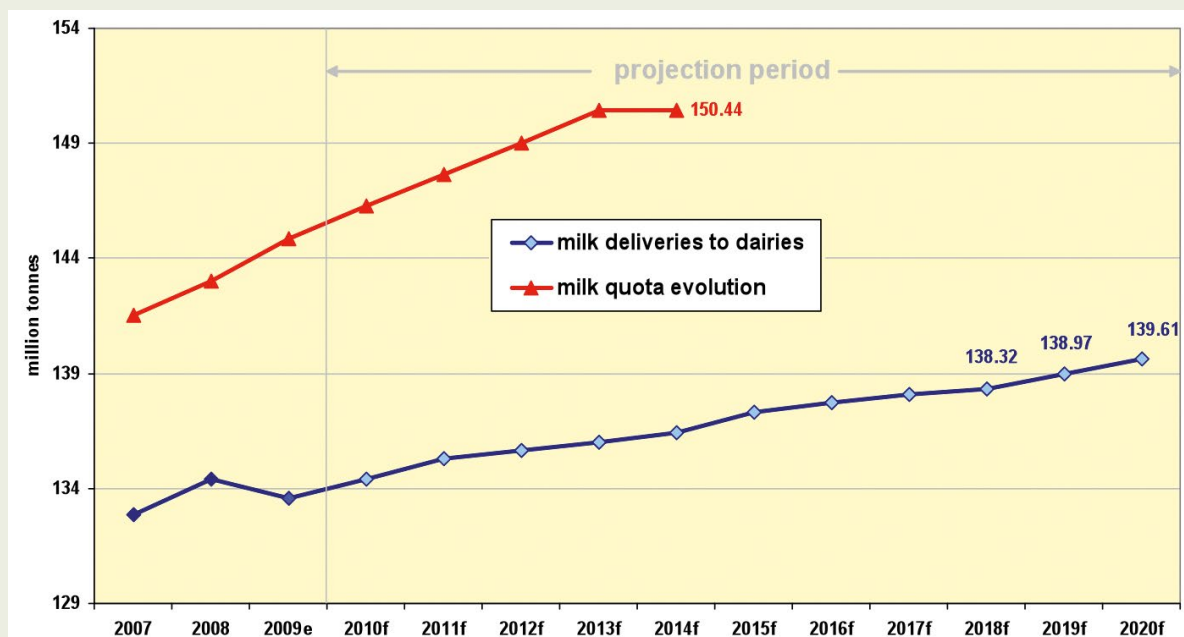
10 GDT, “GDT Price Index over 10 years”, <https://www.globaldairytrade.info/en/product-results> (Download 20.04.2017)

11 European Commission, “Prospects for Agricultural Markets and Income in the EU 2010-2020”, December 2010, p. 6.

12 Eurostat (2017)

Figure 1: European Commission’s projections in 2010 regarding milk deliveries

Source: European Commission¹³



13. The Deregulation of the EU dairy market had far-reaching negative consequences that must be addressed and eliminated in the future CAP:

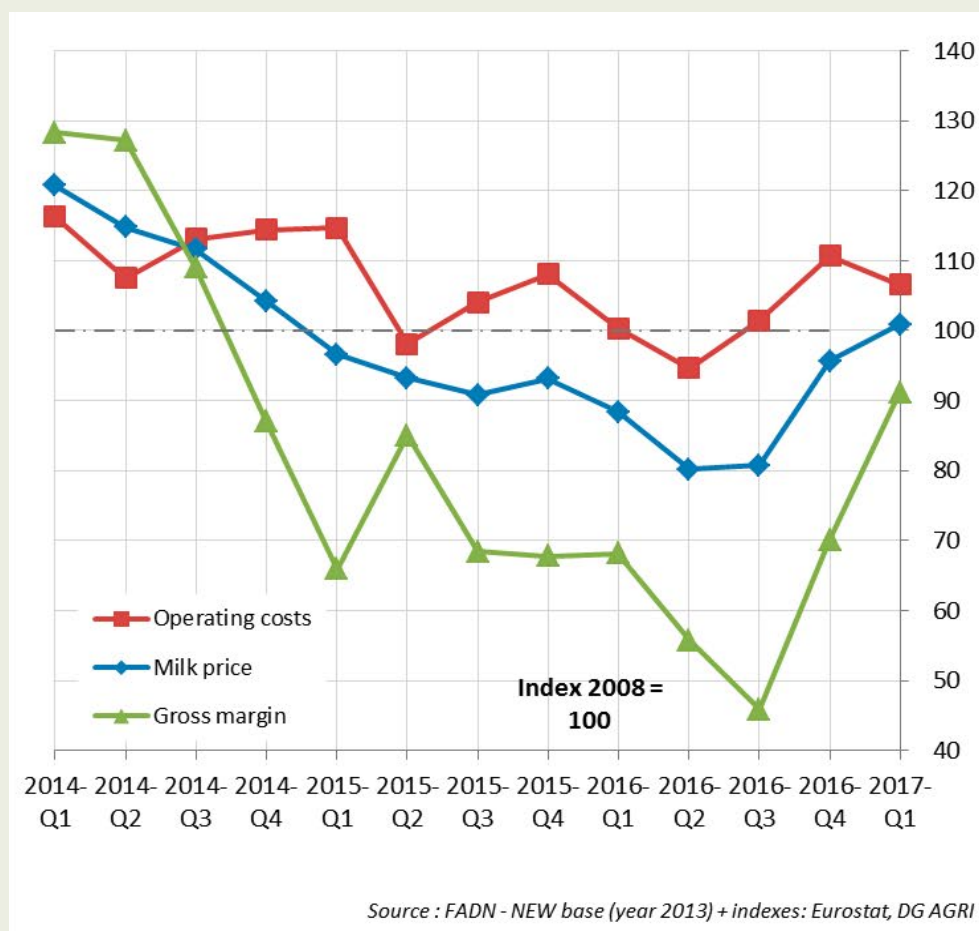
➔ As clearly shown in *Figure 2*, the drop in prices has significantly reduced the farmers’ margins and hence income, leading to numerous farms abandoning milk production as well as major difficulties for those that continue in the sector. Investments to sustain production, let alone innovation, can no longer be made in many places. This applies not only to necessary short-term investments, but also to large-scale, long-term ones over a period of 20-30 years. Previous investments have often proven to be loss-making ventures. The loans taken out to make these investments are difficult or even impossible to pay back.

Also EU direct payments cannot prop up producer income sufficiently as they are rather directed at processors and the retail sector. Therefore, cost-covering market prices are a must to improve income.

¹³ Report from the European Commission to the European Parliament and the Council. “Evolution of the market situation and the consequent conditions for smoothly phasing out the milk quota system”, Brussels, 8.12.2010, COM(2010) 727 final, p. 11.

Figure 2: Estimations of EU milk price, operating costs and margin per tonne of milk

Source: MMO, European Commission¹⁴



- The volatility resulting from the opening to the world market prevents a positive development of milk production. Price volatility in agriculture is a structural factor and increases with a rise in deregulation. In the dairy sector, too, where recent years have seen repeated lows without any strong, compensatory highs, this leads to serious problems.
- A geographic concentration of production coupled with the simultaneous disappearance of production from many regions leads to environmental problems in the regions of intensive production and reinforces their one-sided economic dependence. Furthermore, these developments also lead to major socioeconomic problems in the regions with dwindling production.
- This precarious situation has increased tensions within the EU, for example, between producers of different Member States. During dairy crises, one can observe a return to national interests, which sometimes leads to unfair treatment of fellow producers in neighbouring countries. They are held responsible for the falling prices in one's own country and foreign milk supplies are stopped or milk tanks are emptied en route.

¹⁴ MMO, "EU Gross margin", https://ec.europa.eu/agriculture/sites/agriculture/files/market-observatory/milk/pdf/eu-prices-margins_en.pdf (Download 15.07.2017)

Table 4: Some EU Member States with increased milk deliveries (1,000t)¹⁵

GEO/TIME	2014	2016	Increase in %
Ireland	5,816	6,852	17.8
Netherlands	12,473	14,324	14.8
Poland	10,581	11,130	5.2

Table 5: Some EU Member States with decreased milk deliveries (1,000t)¹⁶

GEO/TIME	2014	2016	Decrease in %
Latvia	805	740	8.1
Romania	995	953	4.2
Sweden	2,931	2,862	2.4
France	25,309	24,744	2.2

The relationship between processors and milk producers has also suffered greatly as a result of deregulation. In their position as weak market stakeholders who have been pushed into an even more disadvantaged position in recent years, producers are forced to protest time and again.

The mistrust towards policymakers has also increased, as their lines of action seem to favour the interests of multinational companies, rather than those of producers and citizens. The impression that policymakers are simply agents of these corporations does nothing to increase trust and confidence in the EU institutions.

- The aggressive export policy that has come hand in hand with deregulation also threatens markets in developing countries. EU skimmed milk powder exports to West Africa almost doubled¹⁷ between 2005 and 2015, and the development of dumping prices was supported. For example, in the West African country of Burkina Faso, milk from imported EU milk pow-

15 Base data from: CLAL.it, "EU-28 milk production and population", http://www.clal.it/en/?section=produzioni_popolazione (Download 22.2.2017)

16 ibid.

17 SOS Faim/Oxfam-Solidarité, "L'industrie laitière européenne lorgne sur l'Afrique de l'Ouest", 2016, p.14.

18 Lanje, Kerstin, Misereor Blog "Deutsche und afrikanische Milchbauern: Du bist kein Milchbauer, du bist Milchpulververkäufer", June 2016, <https://blog.misereor.de/2016/06/22/deutsche-und-afrikanische-milchbauern-du-bist-kein-milchbauer-du-bist-milchpulververkaeuer> (Download 12.08.2016)

der and vegetable fat costs the equivalent of 34 cents and thus merely one third or half the price of local milk, which is sold at 76 cents to 1.10 euros per litre.¹⁸ This leads to problems as many people earn their livelihood from milk production – an activity that also strengthens the position of the female population. Women play an especially important role in production and sales, which helps them to earn their own income and better provide for their families as well as improve their children’s education. All of this is put on the line by the EU’s dumping tactics.

14. The background for the deregulation is a policy that focuses solely on the world market. This focus adopted by the European Commission, the dairy processing industry and COPA-COGECA is largely responsible for the detrimental market developments. In 2013, only 7 percent of the total production was traded on the world market, which corresponded to 55 million tonnes of milk equivalent. The USA, New Zealand and the EU cover more than 70 percent of the world market, where mainly standardised, industrial products like milk powder are traded. It is an unpredictable and vulnerable market. It is small and severely uncontested. Prices vary up to 100 percent. Its growth also does not reflect production. As mentioned above, milk production in New Zealand, the EU and the USA increased by 11 million tonnes in 2014; over half of which came from the EU. However, during the same period, the world market only grew by 2 million tonnes.¹⁹ Leaving EU production security to such an unpredictable market was and continues to be a highly irresponsible strategy.
15. The EU’s current deregulation policy contradicts Article 40 Paragraph 2 TFEU, which states that the common organisation of agricultural markets shall be limited to pursuit of the objectives set out in Article 39 and shall exclude any discrimination between producers or consumers within the Union. The above-mentioned consequences of the current focus on cheap products with the short-term goal of increasing global market shares and turning away from demand-based production, however, are creating even greater discrepancies within the EU and are leading to discrimination against entire regions and agricultural producers.

Current stabilisation measures in the EU and other parts of the world

16. The fact that assuming responsibility for the agricultural sector is essential to one’s own socio-economic development is something that has been better understood in other parts of the world. While the EU is moving towards even more deregulation, many other countries are backing policies that support producer income and iron out market instabilities. They include income support, insurance systems or, as in the case of Canada, supply management. Aware of the strategic importance of agriculture and food sovereignty, these countries have not left the development of the sector to the forces of a free market that functions asymmetrically. For example, governmental spending in the USA was increased from 106 billion to 156 billion dollars between 2008 and 2015. This increase was due to measures like increased food aid and a safety net based on margin support for producers.²⁰

¹⁹ Pflimlin, André, “Do we need a new Commission to end milk crises?”, August 2015, p. 1.

²⁰ Momagri, “White Paper – A new strategic course for the CAP”, August 2016, p. 25.
http://www.momagri.org/UK/focus-on-issues/PAGE_ArticlesDetail.awp?LIEN_LIVREBLANC (Download 20.06.2017)

17. Lacking an appropriate framework, the EU market is sluggish and has the wrong reaction to developments and signs: when an annual sales market worth 2 million tonnes disappeared in August 2014 due to the Russian embargo and China's real imports did not live up to the ambitious import projections, there should have been an appropriate reaction on the production side. However, due to its current form, the EU market could not react suitably to warning signals nor to actual developments. In spite of prices that had clearly fallen, significantly more was produced rather than less, leading to milk surpluses.
18. The absence of effective instruments for the dairy market proved to be a major problem. Existing possibilities like intervention or private storage could do little to counteract the deep-rooted, chronic market instability. Though intervention was open throughout the year and a total 335,000 tonnes of skimmed milk powder were bought up²¹, milk prices dropped further all across the EU in 2016, until they were at less than 26 cents per kg milk in June. As intervention does not address production volume but merely takes goods already produced off the market, it does not counteract destabilising overproduction. On the contrary – even when the intervention price is set very low at about 170 euros/100 kg skimmed milk powder, the buying-up tends to lead to further production.

Aware of the rising surpluses, the EU triggered Article 222 of the CMO Regulation 1308/2013 in early 2016 and allowed producer organisations and interbranch organisations to implement voluntary production cuts for their producers. A small step in the right direction. However, there was still a problem: supply management was not centrally coordinated at EU level and it was rarely applied, and therefore could not provide any relief on the market as a whole.

19. This shortcoming was corrected mid-2016 through the EU aid package, which included a measure towards **EU-wide voluntary production cuts**. Unlike other measures, this EU reduction programme fulfilled two fundamental conditions for an effective instrument: an effect on price and acceptance by milk producers. About 48,000 farmers participated and reduced their milk production by 834,000 tonnes in the period from October 2016 to January 2017. Every applicant applied for EU aid of 14 cents/kg for an average volume reduction of 18 tonnes.²² When the programme was adopted in July 2016, the average EU price was approx. 26 cents; at the end of the programme in January 2017, it had risen to 33 cents/kg.²³ Higher and longer-lasting price increases could have been achieved if the production volumes of all EU producers had been capped during the reduction period. In view of the already highly affected market, the instrument should have been applied much earlier too. **In the future, the dairy market must have a mechanism that automatically and effectively corrects imbalances through temporary production reduction measures.**

21 MMO, https://ec.europa.eu/agriculture/sites/agriculture/files/market-observatory/milk/pdf/eu-historical-stocks-series_en.pdf (Download 23.06.2017)

22 European Commission, "Applications for payment received", https://ec.europa.eu/agriculture/sites/agriculture/files/milk/policy-instruments/applications-payments_en.pdf (Download 20.06.2017) and EU Commission press release published on 05.07.2017, https://ec.europa.eu/info/news/final-figures-reflect-success-eu-milk-production-reduction-scheme_en (Download 06.07.2017)

23 European Commission, MMO "EU historical prices", https://ec.europa.eu/agriculture/market-observatory/milk_en (Download 20.06.2017)

2 A new, responsible CAP for the market, for society and for cohesion in the EU

Objectives of a responsible CAP

20. A good agricultural policy should not drift to the extremes, but should be based on market balance. To this end, past experiences can and must play an important role. In the period between 1962 and 1992, the CAP stimulated the growth of production, which in some cases led to overproduction and excessive agricultural payments due to insufficient control. Later the focus was placed on a high degree of liberalisation in the agricultural market, which led to major instability with extremely low producer prices.

However, market balance cannot be achieved through a liberal strategy nor through the blind promotion of production growth. A new CAP 2020 should therefore link the market responsibility of producers with market observation and a response mechanism.

21. Sustainability must play a greater role in the new CAP than it has to date. According to the sustainability triangle, the equal interaction of economic stability, environmental responsibility and social fairness is key to ensuring that agriculture can make a significant societal contribution. Inspired by the UN Sustainable Development Goals, a European agricultural policy should also strive for inclusive and sustainable economic growth as well as productive employment and decent work for all (Goal 8). Reductions in inequality within and among countries (Goal 10) and sustainable consumption and production patterns (Goal 12) also need to play an important role in the CAP.²⁴

22. In this context, the following agricultural goals must be met:

a. Fair income for farmers

As stated in Article 39 TFEU, ensuring a fair standard of living for the agricultural community is one of the goals of the EU Common Agricultural Policy. To this end, we need to create

²⁴ UN Sustainable Development Goals, <http://www.un.org/sustainabledevelopment/sustainable-development-goals> (Download 20.10.2016)

a foundation that permits independent farmers and their family members working on the farm as well as employed farm workers to earn a decent living. Being a farmer is demanding and farmers play a central social role with respect to food production. Their specialised knowledge in areas like animal husbandry, growing food and feed crops, maintenance of highly sensitive machines and equipment as well as business-oriented farm management should be remunerated through a fair agricultural income.

b. Contribution to overcoming social inequality

A study by Bertelsmann concluded that the gap between the rich and the poor is not a phenomenon exclusive to developing countries: “...the rich countries in this world are no exception to the trend of a growing gap between rich and poor. Inequality keeps rising across these countries as well with the average income of the richest 10 percent of the population now being about nine times that of the poorest 10 percent. (...) Thus, a new – more inclusive as well as sustainable – social and economic model must be strived for in the future.”²⁵ This gap is evident in the EU especially between countries and between rural and urban populations. It is also highlighted in the European Commission’s “Poverty and social exclusion in rural areas” report: “... it has been shown that average living standard, as expressed as GDP per head, is generally lower in rural than in urban areas. Even taking all the limitations of the GDP indicator into account, this evidence suggests the existence of a higher risk of poverty of rural areas as compared to urban ones.”²⁶

The UN Sustainable Development Goal concerning the reduction of inequality within and among countries must also play an important role in the EU within the new CAP. The social situation in rural areas must be brought into sharper focus and it should be possible to achieve economic growth that benefits producers and rural communities as well, instead of leaving them behind. To this end, it is essential for the production costs of agricultural goods to be covered by agricultural prices – according to UN Sustainable Development Goal 8: “Promote sustained, inclusive and sustainable economic growth, full and productive employment and decent work for all”²⁷. As studies show, lower social inequality also has a general positive effect on economic growth.²⁸

c. Production throughout the European territory

Promoting regional production throughout the European territory is in the interest of our society – to ensure healthy economic activity in rural areas (jobs within and related to agriculture) and environmentally balanced production methods. Concentrating production in comparatively few regions, on the other hand, jeopardizes consumer access to regional food and burdens the environment.

25 Kroll, Christian, “Sustainable Development Goals: Are the rich countries ready?”, Bertelsmann Foundation, 2015, p. 5.

26 European Commission, “Poverty and social exclusion in rural areas – final study report”, 2008, p. 7.
<http://www.ec.europa.eu/social/BlobServlet?docId=2087&langId=en> (Download 17.12.2016)

27 UN Sustainable Development Goals, <http://www.un.org/sustainabledevelopment/sustainable-development-goals> (Download 20.10.2016)

28 Kroll, Christian, “Sustainable Development Goals: Are the rich countries ready?”, Bertelsmann Foundation, 2015, p. 72.

In this context, the dairy sector should also provide room for owner-run family farms with locally-linked circular economy, as they contribute significantly to sustainability: they produce regional products for consumers and make shorter transport routes and less environmental impact possible. They are very involved in preserving cultural landscapes and guaranteeing that rural areas remain highly attractive to tourists. If we wish to maintain these social assets, they must be reflected in the EU funding policy.

d. Responsible production within the EU: no harm to developing countries

Owing to the major external influence of the EU dairy policy, the EU also shoulders a responsibility for the development of other countries. The current overproduction in the EU dairy sector is problematic because, for example, it washes up on the shores of developing countries in the form of milk powder, damaging local markets and milk production. Local farmers thus see their possibilities to generate income becoming limited; economic growth is disturbed. However, this is precisely where positive development is needed. Farmers all over the world are going hungry. As shown by the Food and Agricultural Organisation (FAO) of the UN, small farmers make up 90 percent of the rural poor and the majority of the world population going hungry.²⁹ Economic growth can reduce undernutrition; increasing the income of family farms can drive a positive development. However, an EU policy that fuels milk overproduction and dumping counteracts this. Or as the FAO puts it: “Food sectors in developing countries that are characterized by low productivity and lack of competitiveness are especially vulnerable to import surges. A sudden disruption of domestic production can have disastrous impacts on domestic farmers and workers – loss of jobs and reduced incomes, with potentially negative consequences for food security.”³⁰

The EU should have a strong interest in the development of other countries, so that their citizens can tap into sources of income and thus provide for themselves. This is especially important against the background of the large number of refugees and migrants currently arriving all over Europe due to wars and economic misery. More responsible production in the EU should, therefore, be an important component of the new CAP.

Furthermore, rather than nations competing for market shares, greater dialogue and stronger international cooperation in terms of global food security and crisis management are a must. The EU should play an active role in this context. Rather than acting in the interest of multinational food companies, it should act in the interest of people inside and outside of the EU.

e. Allowing producers to take on responsibility

In addition to other factors, the development of the sector is also dependent on the producers' reaction. Individual reactions, such as increasing the production volume in response to low market prices, are often not conducive to the development of the market as a whole. It would be important to create a legal framework within which producers can assume joint respon-

29 FAO, “Resilient Livelihoods: Disaster Risk Reduction for Food and Nutrition Security”, FAO Edition 2013, p. ix. <http://www.fao.org/3/a-i3270e.pdf> (Download 3.10.2015)

30 FAO, “The State of Food Insecurity in the World – Meeting the 2015 international hunger targets: taking stock of uneven progress”, 2015, p. 34. <http://www.fao.org/3/a-i4646e.pdf> (Download 20.06.2017)

sibility for the production of agricultural goods and create a balanced market. This framework should be defined by policymakers and should be acceptable to consumers.

f. Abandoning pure market illusions

Supply and food security, good and robust economic development in the long term as well as social fairness cannot be achieved through a free market. The EU must take its responsibility for a sustainable agricultural policy more seriously. The new CAP must not be driven by liberal market illusions. We can see that without appropriate rules, people systematically get harmed. There is a reason why markets were restrained in the past by adopting laws against child labour, in favour of minimum wage or health and safety at work.

In agriculture, too, the ruthless exploitation of people has to be prevented. This requires sound rules. Some say that production management – a flexible alignment of supply and demand – would not be a businesslike approach. However, every big company follows the strategy of supplying its market with the volumes that ensure satisfactory income. In the case of agricultural producers, there is insufficient market leverage to effectively follow this strategy. A framework defined by policymakers that allows for coordinated reactions is, therefore, necessary.

Fulfilling the new CAP goals

23. For the dairy sector, market balance as well as the above-mentioned goals can be achieved through a special **crisis mechanism**, which must be incorporated into the new CAP. To this end, the European Milk Board has developed the **Market Responsibility Programme (MRP)**³¹. This programme can react to real developments, challenges and problems in the dairy sector in a timely and appropriate manner for the situation at hand. It uses a combination of observation and reaction.

The MRP works on the basis of a **market index** that represents the relation between production costs and producer prices. If the index falls below 100 points, it signals market imbalances. If the discrepancies are significant, the MRP comes in. It reacts to minor market inconsistencies with lighter measures like opening private storage – temporary storage of milk products so that they can be taken off the market – or through incentive schemes. If the index drops even further, then **voluntary production cuts** are initiated as the second level of the MRP. The total volume that is necessary to reinstate the balance on the dairy market is calculated at EU level. Through a tender based on the calculated total volume, milk producers are asked to voluntarily reduce their production by a few percent. Those who decide to participate receive financial compensation for every kilogramme of milk they do not produce. In many cases, these first two levels are already enough to realign the market. In the event of very strong market disturbances, however, a third level is possible. If the index falls below 25 points, all producers across the EU are obliged to reduce their production within a specific time period by 2-3 percent.

31 <http://www.europeanmilkboard.org/en/special-content/market-responsibility-programme.html> (Download 20.06.2017)

Concerns that these instruments would limit the development of dairy farms are unfounded. Level 3 would surely demand a certain degree of discipline from every producer for a short period of time in order to bring milk prices back to an appropriate level. This stable price, however, ensures that dairy farms must no longer sell at a price that is below their production cost. They can thus generate a viable income and also have the financial means to invest in the future of the farm. With the current rock-bottom prices characterising the dairy market, it is hardly possible to produce at a break-even price, let alone to make a profit. Reliable, appropriate prices, on the other hand, give producers planning security and allow them to expand their production if need be. The third level mentioned leading to compulsory temporary production cuts would only be necessary in very few cases. But prior to this, the first-level programmes as well as the voluntary supply restraint reduce market tensions. Furthermore, the MRP would only be activated in times of crisis. At all other times, the market would operate without any volume management.

24. The MRP allows producers to earn a **fair income** because the prices obtained consider real production costs as well. It is important that a fair remuneration for labour is also included in the cost calculations. In fact, a range of national studies already provides insight into the real cost situation on European dairy farms.³² Cost-covering prices have far-reaching effects. They allow producers to work optimally in terms of animal welfare and environmental protection as well as to pay fair wages on their farms and produce in a sustainable way.

As the crisis mechanism keeps producer prices at a cost-covering level, investment and thus innovation in agriculture become possible, jobs are maintained and new jobs are also created. **Social inequalities between urban and rural areas are lessened**; rural communities are no longer left behind.

The major crises and rock-bottom prices affecting the dairy sector have decimated milk production in many regions and, in some cases, wiped it out completely. In other areas, on the other hand, milk production has become more intensive, often with negative consequences for the environmental balance. A functioning crisis mechanism can maintain **balanced production throughout the territory** that is so important for the EU. To ensure the survival of family farms in the dairy sector, crisis resilience of the sector through the implementation of the MRP is imperative. In terms of direct payments, a degressive model could be used to stabilise family farms. Furthermore, special financial support, which can be provided through EU aid, is also recommended for disadvantaged areas and regions with difficult production conditions.

Fewer EU surpluses not only benefit local producers, they also help producers in other countries as the overproduction is no longer dumped in other markets in the form of cheap milk powder. This is an essential condition for **developing countries** to be able to sustain and further develop their dairy sectors.

By freezing or reducing their own production in times of crisis, **milk producers in the EU assume significant responsibility for their sector**. Crises cannot be managed suitably by ad-hoc aid pack-

32 BAL, Country-specific studies on milk production costs in Europe, <http://www.europeanmilkboard.org/en/milk-production-costs.html> (Download 20.06.2017)

ages, but can be avoided by the active collaboration of producers. This would also be a step away for producers from being dependent on subsidies towards self-sufficiency. The crisis mechanism outlined also promotes producer independence in terms of direct payments. Ensuring cost-covering prices reduces the need for EU aid payments until they slowly but surely become obsolete. Until that is the case, however, direct payments should not contribute to unfair competition between EU producers. This means that payments made to producers in the old and new EU Member States must be aligned with each other.

The introduction of the Market Responsibility Programme would initiate an important reorientation of agricultural policy. **Instead of blindly following a liberal market ideology and its proponents**, the real conditions in the sector would be considered and appropriately reacted to. Agricultural policy would give more importance to the interests of citizens and producers. The current dominance of corporate interests – whose long history is reflected in the relationships between business, politics and association representatives – would be curtailed. This is also necessary in terms of politics in general, because this dominance is a major factor influencing the lack of trust in the EU and its institutions.

Legal basis for an efficient crisis mechanism

25. It is recommended that within the framework of the new CAP the following regulations be included in the Common Market Organisation (CMO).

Article: Monitoring body (to be added to the CMO)

1. In order to ensure that the milk market is monitored and balanced, the EU Commission should implement a Monitoring Body that includes the following elements:
 - a. A market balance index, based on the changes in product quotations, milk prices and production costs (margins). The index provides information on the EU milk market's state of balance. The state "balanced market" corresponds to a situation where supply and demand of raw milk meet at a level where producer prices cover production costs.
 - b. A crisis mechanism which is activated when the index leaves the state "balanced market". The crisis mechanism works as follows:
 - i. The current market state deviates by -7.5 percent from the state "balanced market":
 - The Monitoring Body issues an early warning; private storage is opened and/or incentive programmes are activated for a defined period of time
 - This phase is maintained until the market returns to the "balanced" state
 - ii. The current market state deviates by -15 percent from the state "balanced market":
 - The Monitoring Body declares that there is a crisis and starts the voluntary volume reduction scheme according to *Article ...* (Volume Reduction Scheme)
 - The voluntary volume reduction scheme is prolonged until the market returns to the "balanced" state
 - Imposing a market responsibility penalty on all producers that increase their production during the reduction period

- iii. The current market state deviates by -25 percent from the state “balanced market”:
 - Reduction of supply of raw milk by a defined percentage during a set period of time for all producers
 - Imposing a market responsibility penalty on all producers who do not take part in the reduction programme
 - This phase is maintained until the market returns to the “balanced” state
 - c. The crisis mechanism will be financed as follows:
 - Public crisis fund
 - The market responsibility penalties of the farmers increasing their production volumes during the voluntary reduction scheme, according to Article 1.b.ii or Article2 (Volume Reduction Scheme) respectively.
 - The market responsibility penalties of the producers according to Article 1.b.iii.
 - A producer levy set per kilogramme of supplied milk, to be paid during a defined period of the year in which the crisis occurs. The levy collection period can be extended if more financial resources are necessary
2. In order for this to be possible, the Commission would need to adopt delegated acts defining the following points:
- a. The calculation of the market balance index as well as the determination of the “balanced market” state, i.e. the situation where supply and demand of raw milk are in balance and producer prices cover production costs. The calculation of costs must take into account all costs, including a fair income for the producer
 - b. The duration of the following periods:
 - i. Early warning phase according to Article 1.b.i.
 - ii. Universal reduction phase according to Article 1.b.iii.
 - iii. Period of collecting the producer levy according to Article 1.c.
 - c. The percentage of the volume to be cut during the universal reduction phase, according to Article 1.b.iii.
 - d. The amount of the market responsibility penalty paid by producers that increase their production during the reduction period according to Article 1.b.ii.
 - e. The amount of the market responsibility penalty collected from all producers who do not take part in the universal reduction programme according to Article 1.b.iii.
 - f. The amount of the producer levy per kilogramme of supplied milk, which will be used to finance the crisis mechanism according to Article 1.c.

Article: Volume Reduction Scheme (to be added to the CMO)

Programme to reduce agricultural production in periods of market imbalances

1. If the market falls into a state of significant imbalance, the Commission can financially compensate the producers of the sectors listed in Article 1(2), who, during a defined period and on a voluntary basis, reduce their production compared to the same period of the previous year (reference period). The reduction period can be prolonged if deemed necessary.

2. Each producer who supplies a larger amount than during the reference period has to pay a market responsibility penalty in relation to the extent of his oversupply.
3. In order for this to be possible, the Commission would need to adopt delegated acts determining the following points:
 - a. The maximum supply volumes to be reduced on EU level in the framework of the reduction scheme
 - b. The duration of the reduction period
 - c. The amount to be paid to producers for reducing their volumes as well as the details for funding the measures
 - d. The amount of the market responsibility penalty for the producers who increase their supply during the reduction phase
 - e. The criteria producers need to fulfil in order to be eligible for the reduction bonus as well as of the criteria for approving submitted applications
 - f. The specific conditions for implementing the programme

3 The Market Responsibility Programme: a system that reflects reality

Financing the system

26. The crisis management system does not imply any major burden on the EU budget as a large portion of the funding will be generated by the system itself. In addition to the penalty payments and a part of the EU crisis funds, levying a temporary surcharge on all milk producers can also be considered when necessary. In this way, 0.5 cents per kilogram of milk produced in a period of six months across the EU, for example, would generate a sum of approx. 380 million euros. Of course, milk producers can only pay this levy if they are being paid cost-covering prices.

An additional advantage of this system is that compared to aid packages that prop up producer income in times of crisis, it has a two-fold positive effect. Besides supplementing the income of the participating producers, the volume reduction programme will significantly relieve the market through reductions. This leads to universal price increases for all producers, making such aid packages redundant.

Furthermore, the EU agricultural budget will be under less pressure as a crisis-resilient sector with cost-covering prices means that producers are less dependent on direct payments.

Effectiveness

27. As explained in Chapter 2, the effectiveness of a key element of the MRP – voluntary production cuts – was clearly proven in 2016 in the EU. Producers and eventually producer prices reacted positively to the programme. The administrative burden was also manageable and did not lead to any obstacles in the implementation of the programme.

Contribution to international stability

28. With its large share in global milk production, the EU is an important and economically influential player. Responsible production, therefore, does not only have a positive effect on EU producer prices, it is good for world market prices as well. The EU would thus contribute significantly to

greater stability on the world market. If pressure from the EU is reduced, producers in other countries would find it easier to earn a decent living from milk production. This is another important argument in favour of the implementation of a crisis mechanism in the EU – especially for developing countries, but for producers in other countries as well.

WTO compliance

29. The principle of the crisis mechanism is also compliant with the orientation of the World Trade Organisation (WTO). This is the case with voluntary production cuts, which are a fundamental part of the proposed crisis instrument. In addition to funds generated through penalties and a levy, EU funds are also used to fund the production cuts. Such payments are allowed by the WTO. According to Article 6.3 of the WTO Agreement on Agriculture, the EU can grant public payments within the so-called Amber Box as long as the admissible total amount of these subsidies is not exceeded. For example: according to the figures sent by the EU to the WTO³³ for 2013/2014, the EU could have used 72.378 billion euros as funds from the Amber Box. However, with a real spending of only 5.972 billion euros, the available sum was significantly under-used. Furthermore, Article 6.4 of the WTO Agreement on Agriculture states that for a basic agricultural product, product-specific domestic support must only be included in the total calculation of the agricultural subsidies mentioned above if it accounts for more than 5 percent of the total value of that product during the relevant year. For the year 2013/2014, the total production value of milk was 61.599 billion euros. Subsidy payments of 181.9 million euros were thus below the 5 percent limit and were, therefore, not included while calculating the total support measures of 5.972 billion euros. There is more than enough scope for payments as part of voluntary production cuts.

Thus, the MRP crisis mechanism also qualifies as a fit-for-purpose instrument for the future of the EU dairy sector from the point of view of the WTO.

³³ World Trade Organization, Notification, 8 February 2017, https://docs.wto.org/dol2fe/Pages/FE_Search/ExportFile.aspx?id=234312&filename=q/G/AG/NEU34.pdf (Download 20.06.2017)

European Milk Board asbl (EMB)

Rue de la Loi 155

B-1040 Brussels/Belgium

Phone: +32 (0)2 808 1935

Fax: +32 (0)2 808 8265

office@europeanmilkboard.org

www.europeanmilkboard.org

