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Economic analysis of the effects of the expiry of the EU milk quota system

Preliminary results from the IDEI study

DG AGRI G-2

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Structure of the presentation

- 1 – Objectives and analytical approach
- 2 – Key results
  - Reference scenario
  - Long-term impact of quota abolition
  - Medium-term impact of alternative scenarios
- 3 – Comparison of results
- 4 - Conclusions

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Objectives of the study

- Assess the medium and long-term impacts of several quota ending scenarios for the present milk quota system and the CMO for milk and milk products on
  - Milk producers
  - EU dairy commodity markets
  - World dairy commodity markets

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Analytical approach

- Study carried out by *Institut d'economie industrielle* using the EDIM model (same model used for the 2003 CAP reform impact assessment)
- Country coverage:
  - EU15 MSs, HU, CZ, PL, EU7 aggregate, BG and RO
  - Oceania and 4 net importing regions: CIS+RoEurope, Asia, Africa+Middle East and America
- Product coverage:
  - Butter, SMP, WMP, Casein
  - Condensed milk, cream, liquid milk, fresh products
  - Cheese (fresh, soft, semi-hard, hard, blue and processed)
- Trade policy environment based on Uruguay round agreement
- Recent EU policy developments not covered: mini-milk package, 2008 quota increase proposal

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Overview of scenarios

- 'Reference' scenario
  - Current policy setting maintained post 2014/15
- 2 'soft landing' scenarios (quota increase from 2009, quota abolition in 2015; other policy measures are unchanged)
  - Annual increase in quotas by 1% ('+1%' scenario)
  - Annual increase in quotas by 2% ('+2%' scenario)
- 2 'hard landing' scenarios
  - Quota abolition in 2009 ('H09' scenario)
  - Quota abolition in 2015 ('H15' scenario)
  - In both cases other policy measures are unchanged

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Sensitivity analysis on key elements

- ‘No subsidies’ – prices are allowed to fall below intervention price levels
- ‘Low costs/high quota rents’ – alternative assumptions on base year marginal costs
- ‘Low demand’ – assuming a lower growth rate for EU and world demand
- ‘WTO scenario’ – based on a simplified reading of the Falconer proposal on draft modalities (July 2007)

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Reference scenario 1 / 4

- Determinant factors:
  - Growing EU demand for fat and protein (+0.1% and +0.5% p.a.)
  - Slightly declining EU demand for butter
  - Growing world demand for dairy commodities (+2-3% world imports)
  - Binding quotas limit production growth

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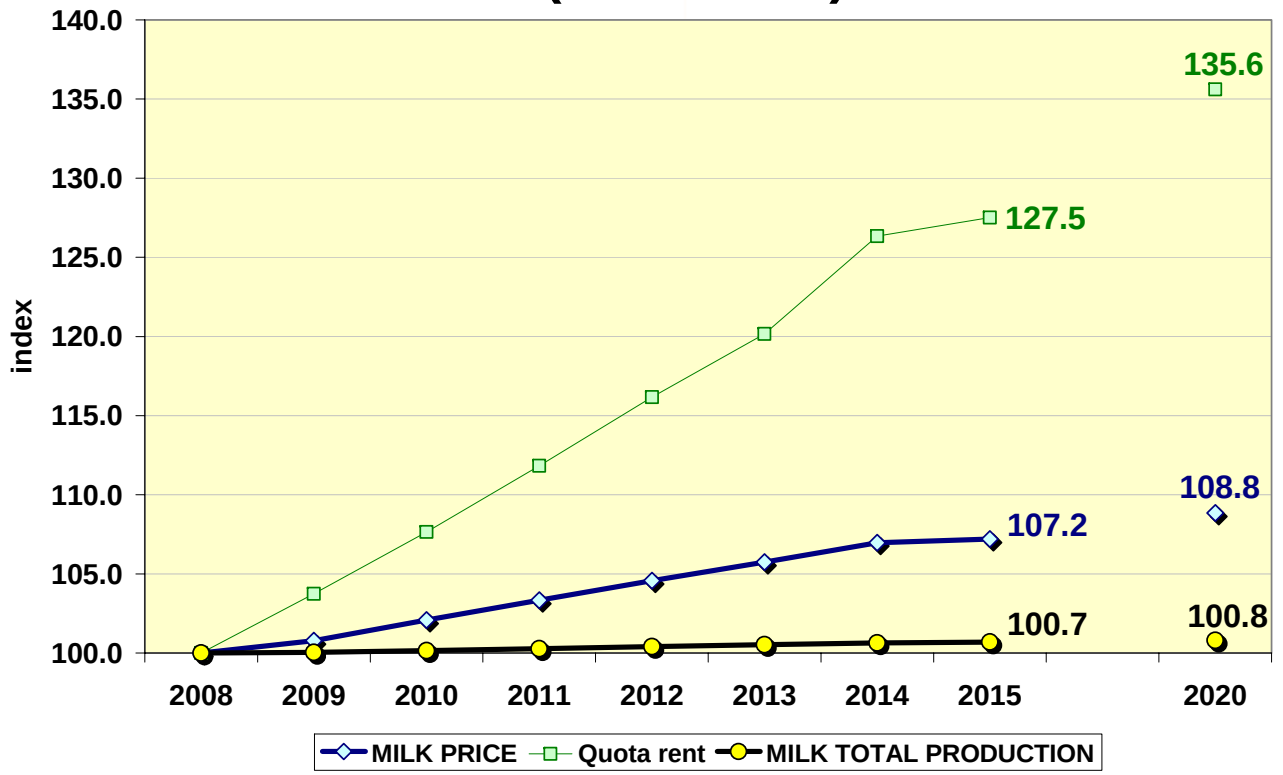
Reference scenario 2 / 4

EU milk production, milk price and quota rent (2008 = 100)



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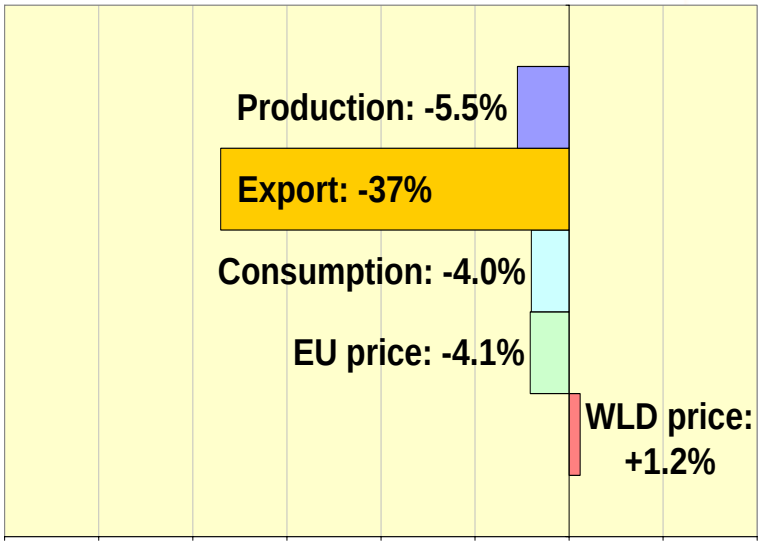
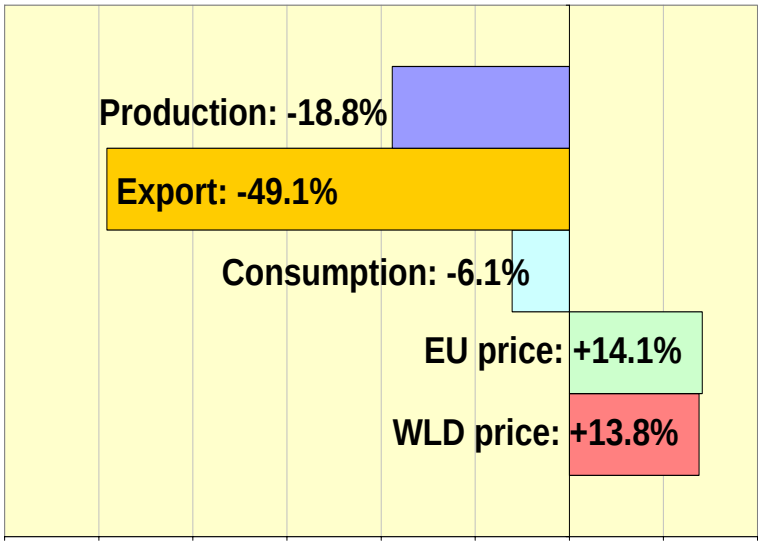
Reference scenario 3 / 4

EU bulk commodity markets in 2020 (versus 2008)

Butter



SMP



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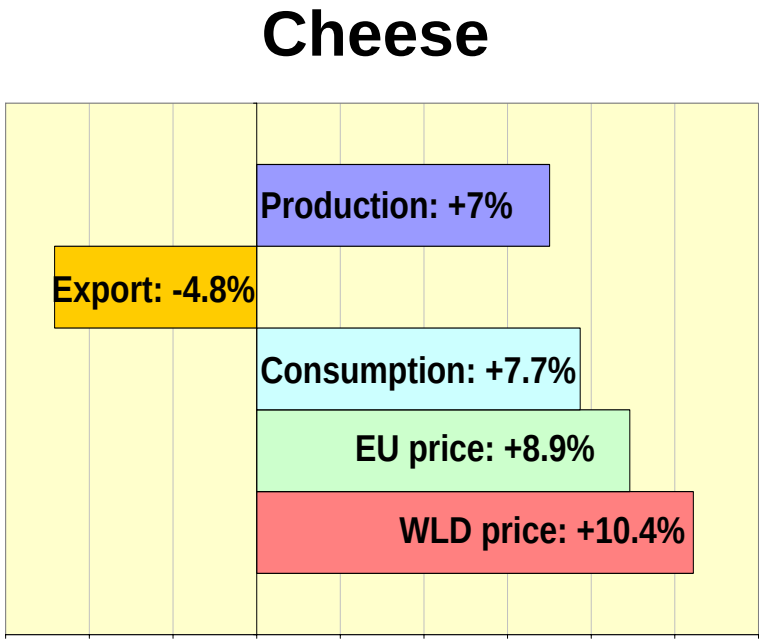
Reference scenario 4 / 4

EU value added markets in 2020 (versus 2008)

- EU demand growth exceeds production growth
  - Increasing EU price
  - Lower EU exports
- World demand growth leads to increasing world prices



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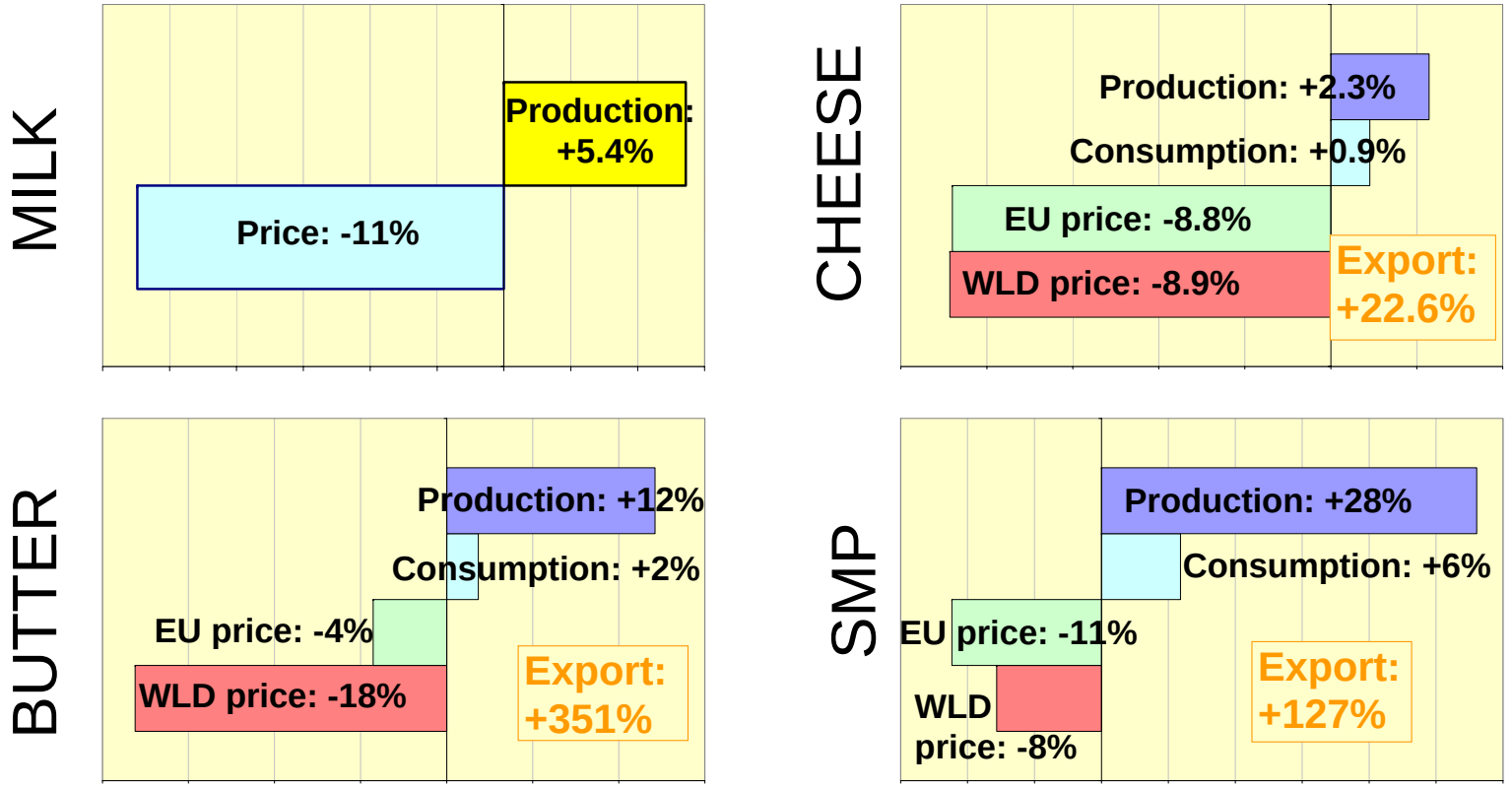
Long-term impact of quota removal in 2020

(all quota removal scenarios vs. reference scenario in %)



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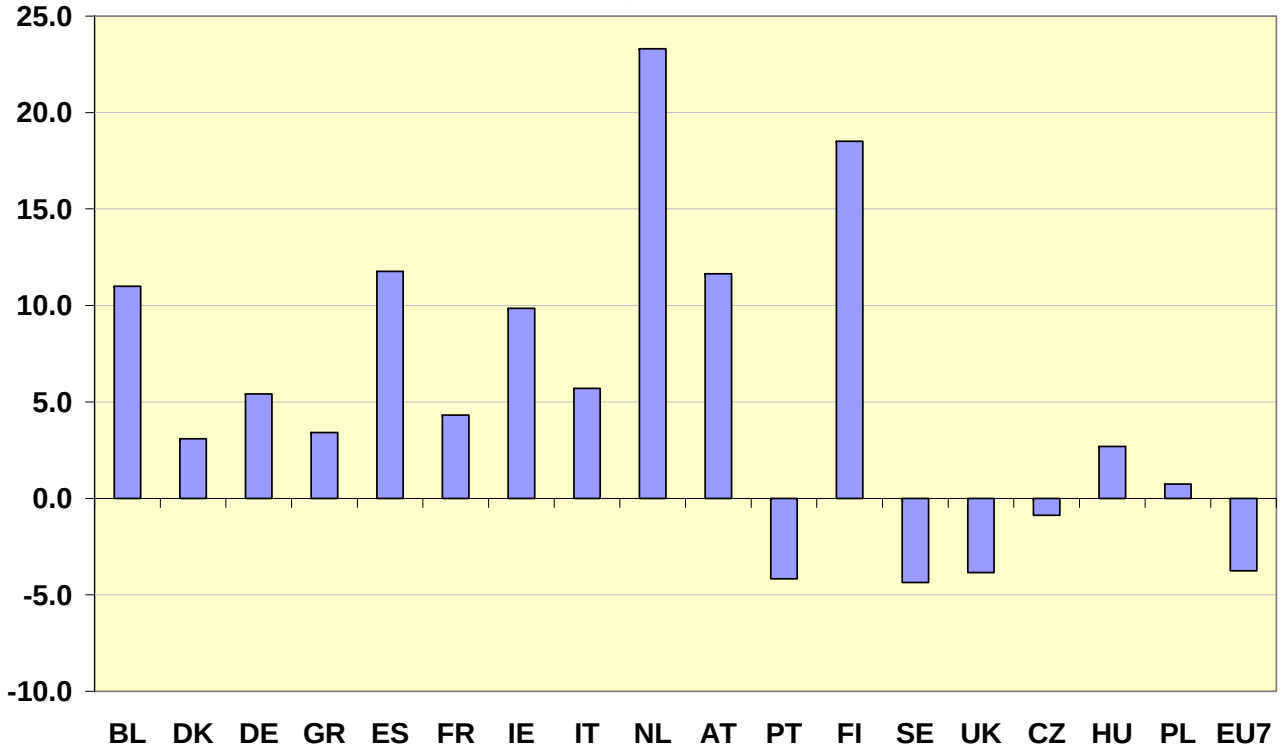
Long-term impact of quota removal in 2020 on EU milk production

(all quota removal scenarios vs. reference scenario in %)



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‘Soft landing’ – main results for +1% and +2%

		‘+1%’	‘+2%’
Milk production	**Annual increase *prior to quota removal (ie. 2009-2014)***	**+0.7%**	**+0.8%**
	Total increase *following quota removal (ie. 2015/2014)*	**+1.4%**	**+0.6%**
Milk price	**Trend *prior to quota removal***	**stable**	
	Impact of *quota removal*	**-2.9%**	**-0.9%**
SMP	**SMP price prior to quota removal:** demand growth for protein > production growth	**Increase** (at lower rates than status quo), **remains above intervention price**	
Butter	**Butter price:** production growth of fat > demand for fat	**Decrease, reaching the intervention price in:**	
		3rd year	**2nd year**

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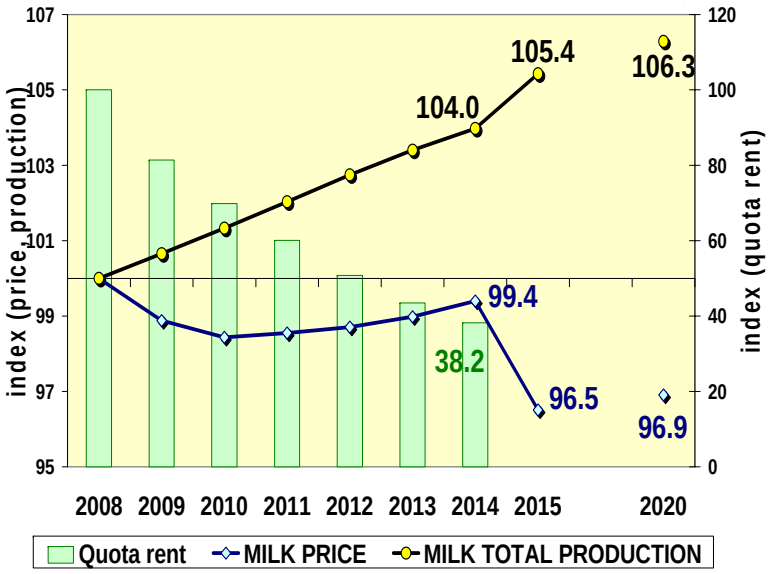
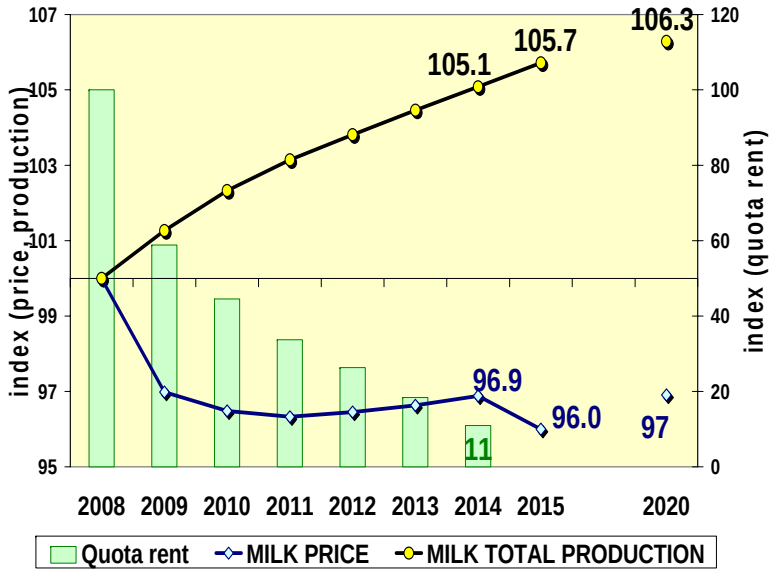
Soft landing scenarios

EU milk production, milk price and quota rent (2008 = 100)





Scenario '+1%'

Scenario '+2%'

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Impact at Member State level during the 'phasing out' period

- Three groups:
  - Production increase = quota increase: Austria, Belgium, Finland, Ireland, Italy, Netherlands, Spain (quota-fulfillment in 2014)
  - Production decrease: Sweden, UK, EU-10 Member States [due to low quota rents and impact of declining milk price]
  - Production increase < quota increase: all other EU-15 Member States (under-fulfillment of quotas in 2014)

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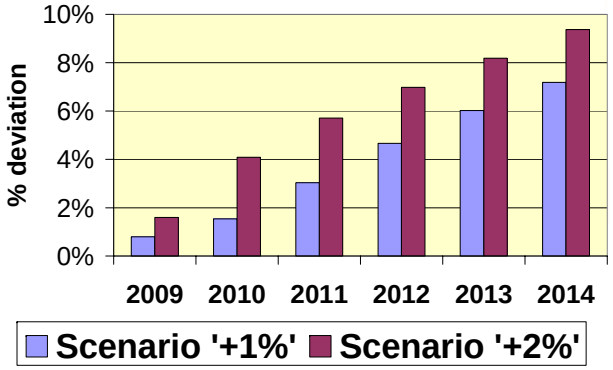
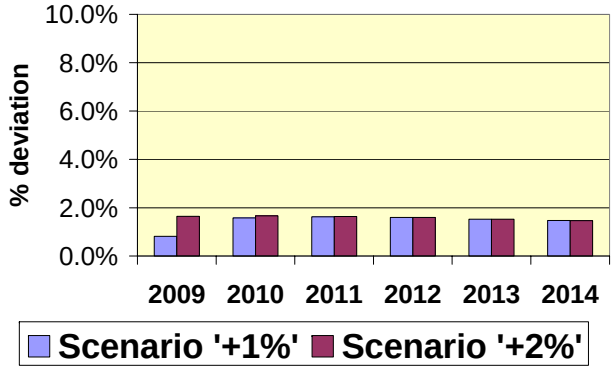
Soft landing scenarios – Butter market

(deviation from reference scenario in %, 2009 - 2014)

OUTPUT



DEMAND



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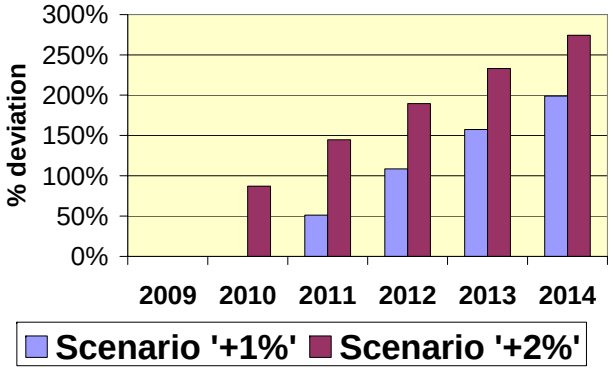
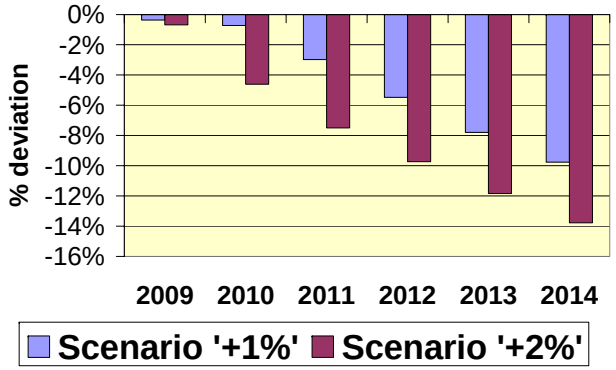


WORLD PRICE



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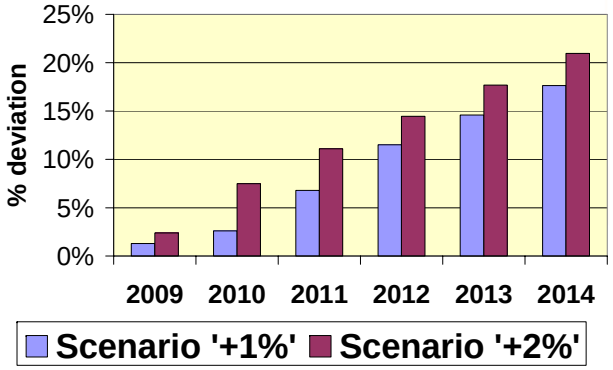
Soft landing scenarios – SMP market

(deviation from reference scenario in %, 2009 - 2014)

OUTPUT



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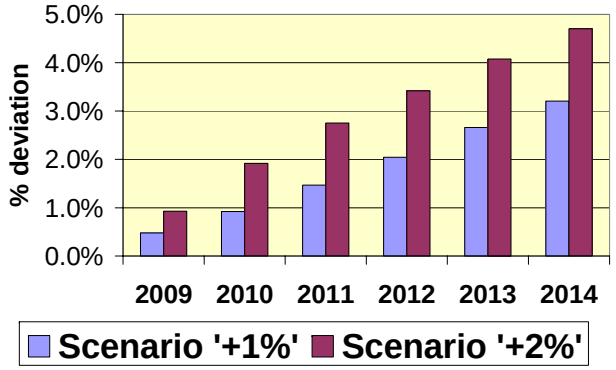

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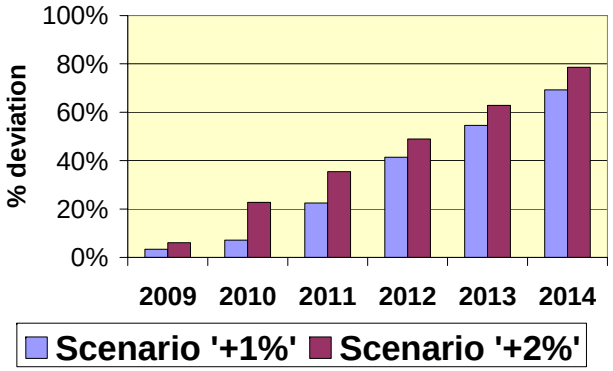

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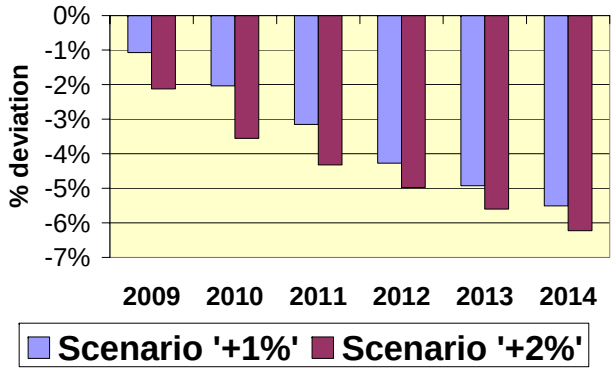

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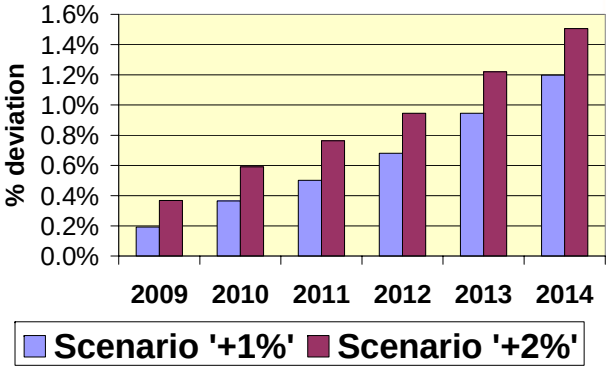
Soft landing scenarios – Cheese market

(deviation from reference scenario in %, 2009 - 2014)

OUTPUT



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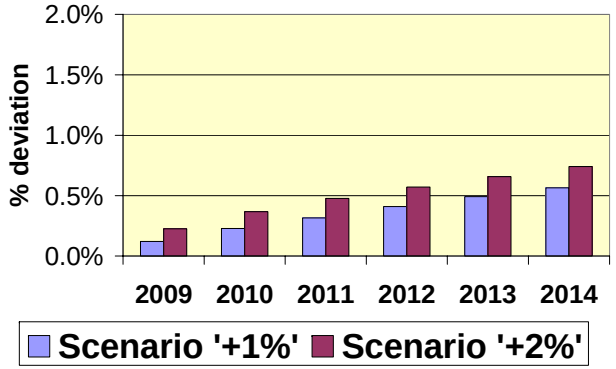

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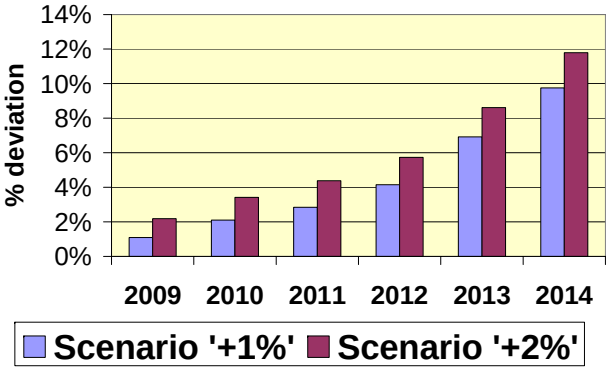

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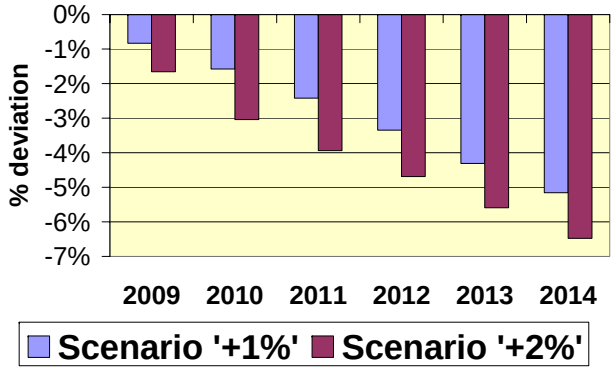

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Hard landing – main results for H09 and H15

		‘H09’	‘H15’
Milk production	Impact of *quota removal (during the 1st year)*	+3.2%	+4.0%
Milk price	Trend *prior to quota removal*	n.a.	+7.0%
	Impact of *quota removal (during the 1st year)*	-7.0%	-8.2%
SMP	Price *following quota removal*	Decrease, but remains above intervention price	
Butter	Price *following quota removal*	Decrease, reaching the intervention price	

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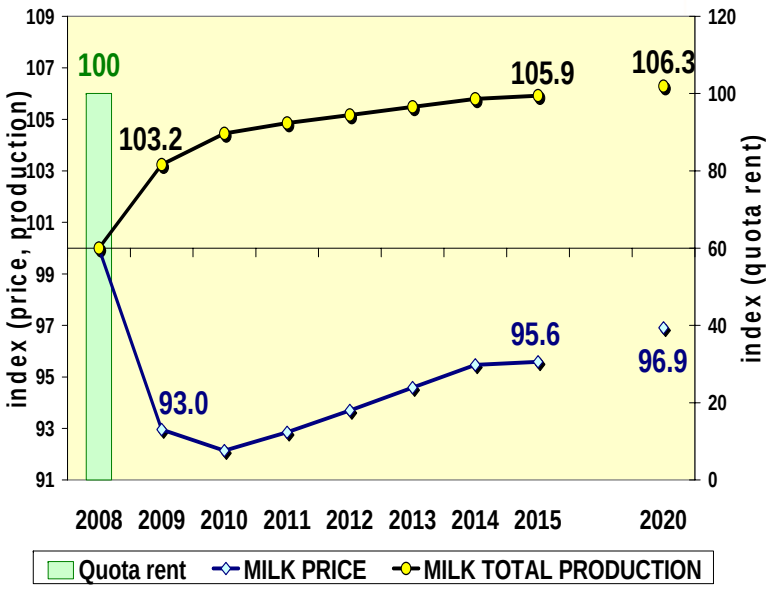
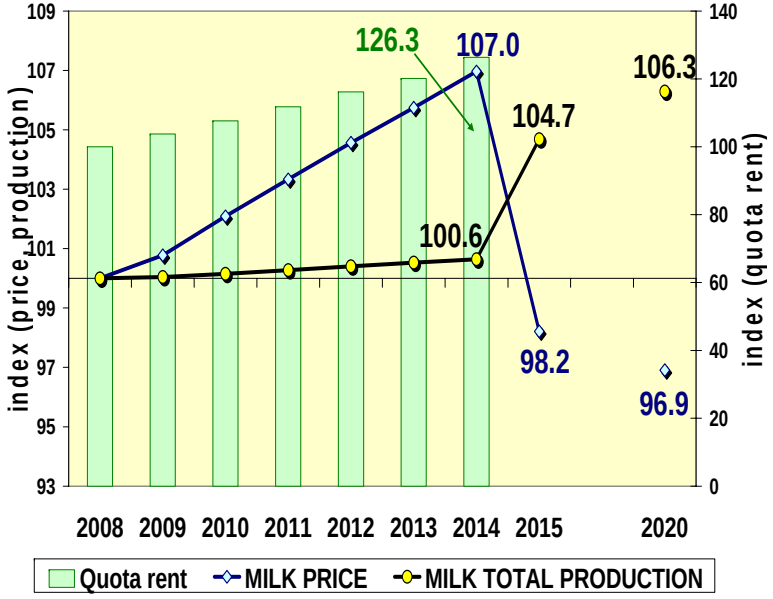
Hard landing scenarios

EU milk production, milk price and quota rent (2008 = 100)





Scenario ‘H09’

Scenario ‘H15’

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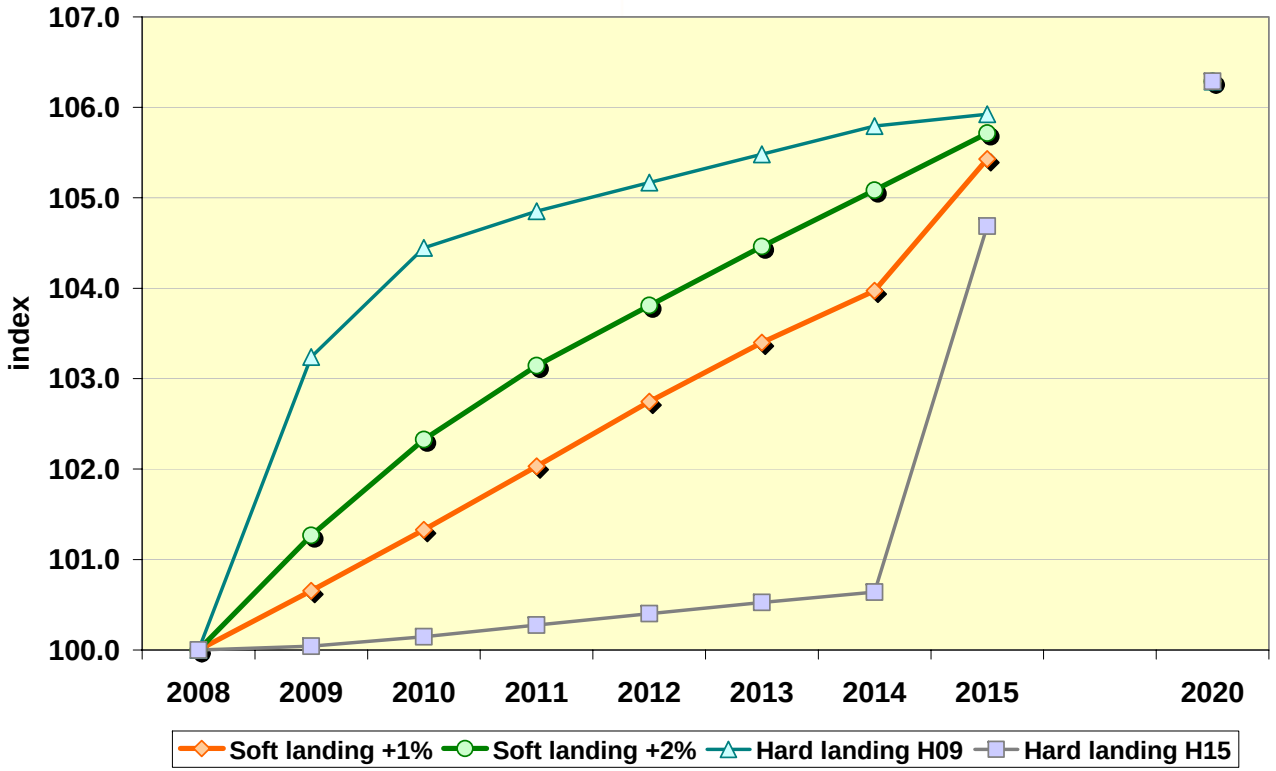
Comparison of quota removal scenarios
- Milk production -

2008 = 100



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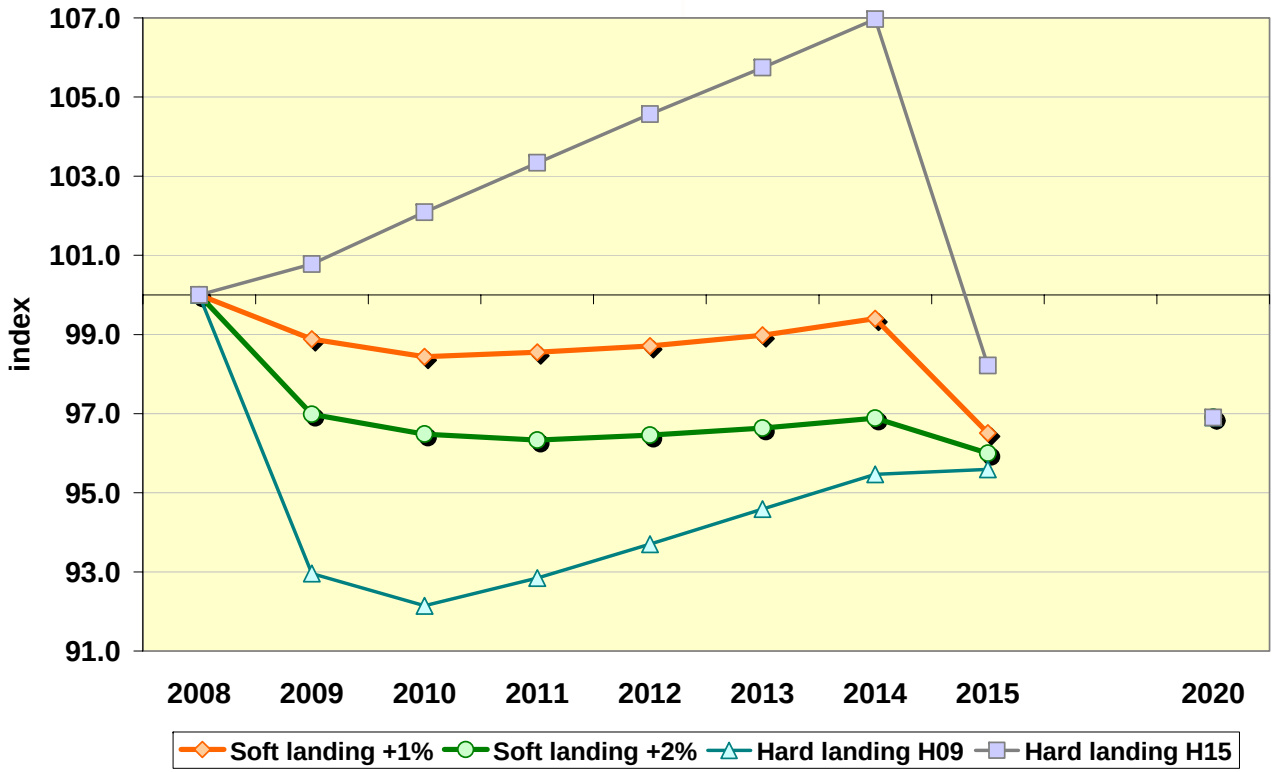
Comparison of quota removal scenarios
- Milk price -

2008 = 100



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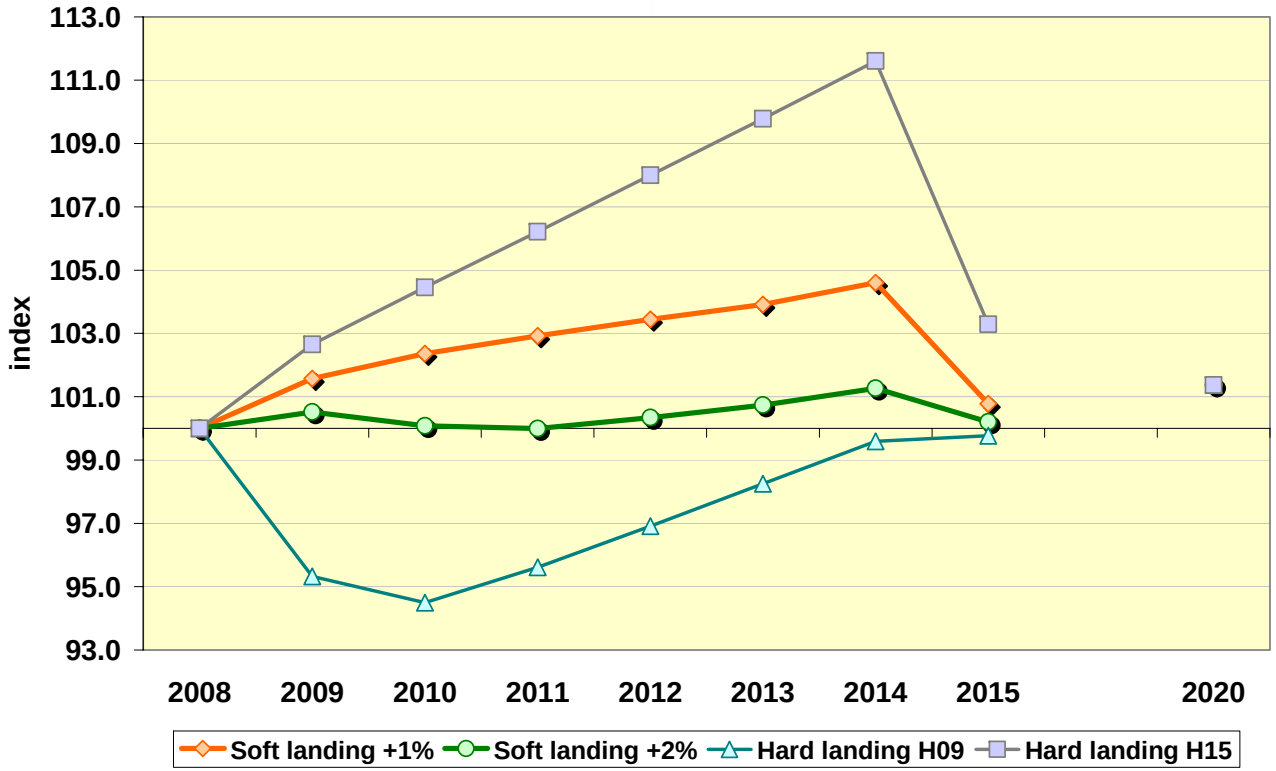
Comparison of quota removal scenarios
- SMP prices -

2008 = 100



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Sensitivity analysis

(deviation of milk price and production vs. quota removal scenarios)

Table: Results for scenario '+1%' in year 2015-16

Variant	Production	Price
No subsidies	-0.5%	-1.4%
Low costs	+4.1%	-7.7%
Low demand	-1.0%	-2.7%
WTO scenario	0.0%	-0.2%

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Conclusion

Though caution is necessary (preliminary results, normalized conditions, rapid adjustment, stylized producer behaviour/expectations) … some key findings can be highlighted

- '+2%' scenario =>smoothest adjustment / 'soft landing'
- Support mechanism for butter still plays a role in stabilising markets and milk price
- Inelastic EU demand =>higher EU exports and lower world prices
- 'Hard landing' approach => big shock & uneven development over member states (benefiting low cost producers)
- Bulk dairy products more affected than higher value products
- Assumptions on quota rents => key for assessing market impact