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Preparing for long-term success in the dairy sector

Seminar on Dairy sector in the context of the Health Check Review of CAP

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[Ladies and gentlemen],

Let me start by repeating the welcome which you've already heard from Lars. I'm very glad that so many people have made the effort to be here today.

No one would claim that the dairy sector has been living in uninteresting times! 2007 was quite extraordinary.

The press was full of the boom in dairy prices. And if you believed some journalists, the big culprit was the Commission - that was supposedly unwilling to respond. There was plenty of talk about extra costs for consumers; there was much less talk about sorely-needed profit for farmers.

For me, there was no reason to take dramatic action, because there was no real shortage of milk, nor an exceptional increase in milk prices. There was only the fact that our intervention stores were empty. Speculation did the rest.

Market forces pushed prices up, just as now they are bringing prices down. The high prices were good news for farmers, and they created a new dynamism in the sector that had not been seen for a long time. Let's remember that prices had been sliding downwards almost since the beginning of the eighties. Consumers of course were at the other end of the line.

In any case, not for the first time, feelings have been running high about many aspects of our dairy market system.

This means that it's all the more important to have you in here, today, to tell me your thoughts as the Health Check exercise gathers pace.

Today's consultation is a **real** consultation. I don't have a set of conclusions printed in advance, locked away in a drawer in my office. I do want to hear from you.

But obviously, my thinking about the Health Check isn't simply a blank sheet of paper for others to write on. I do have some provisional thoughts, and it's worthwhile that I share these with you.

I'll start by talking about dairy market measures other than milk quotas.

At the top of my list for today, I have **export refunds**. And my fundamental message is simple: don't bank on these staying around for ever.

As you know, we have conditionally agreed within the Doha Round of WTO talks to phase these out by the end of 2013. But whatever happens in the Doha Round, I think we should assume that the days of export refunds are numbered.

It's hard to see how they can contribute to the competitive, market-oriented agriculture that we want. And they draw criticism from around the world again and again, especially with regard to development issues.

This doesn't mean that we should abolish them tomorrow. For the time being, we should keep the right to start paying refunds again if need be. But they should not be part of our long-term vision.

The wind of change could also be blowing for **intervention**.

The Commission's communication on the Health Check sets out an important principle: that intervention should work as a genuine safety net, which we can use without relying on subsidised sales. We should not be using it to set market prices.

Recent reforms have brought us some of the way towards this goal in the case of dairy intervention. Have they brought us all the way? We need to ask the question.

In particular, it's an interesting point that the respective intervention prices for butter and skimmed-milk powder are the reverse image of world market prices. The world is prepared to pay more for SMP than for butter; but our intervention system pays less. Should we allow this inconsistency to continue? Or should we consider cutting the butter intervention price? Again – important questions.

We should revisit **private storage**.

As you know, we abolished private storage aid for SMP in the so-called Mini-Milk-Package adopted last autumn, but there is still a compulsory scheme for butter and cheese.

One of the original purposes of private storage aid for butter was to act as an alternative to intervention. But we have already slimmed down the role of intervention, and the 2003 reform also gave us a much tighter control over the use of butter intervention by introducing the basic ceiling and the tendering system.

In view of this, should we still automatically offer support for private storage every year? Or could we give ourselves the freedom to make a decision each year on the basis of the market situation?

These questions are even more pertinent for cheese, which has been the star performer of the dairy sector in recent decades.

We also have to ask ourselves whether we still need our various **internal disposal measures** for butter and skimmed-milk powder.

These were designed to be artificial outlets for large stocks which were always in danger of getting out of control. They were also intended to create artificial demand in the marketplace.

Nowadays, the intervention stores lie empty and we're trying to get away from using artificial outlets. And since we have reduced the support prices by the amount equivalent to the disposal aids, we may wonder what use these systems are.

So perhaps there's a straightforward way here to simplify our dairy policy!

The world has also changed since the year when we first started to use another tool in our dairy market system – **quotas**.

That year was, of course, 1984 – though milk quotas don't get a mention in George Orwell's famous novel of that title!

1984 was a time when the European Community's agriculture budget was exploding, just like our stocks. Quotas were part of the response to that situation, and they had widespread support.

Now, like shifting tectonic plates, opinion among Member States has moved firmly against quotas. Gone are the days when it was just four Member States that campaigned for the system's abolition. There is now a dominant view that quotas should be allowed to expire in 2015, as agreed in the 2003 reform. Predictability will be a key.

As I have said on many occasions, it's time to accept that reality and move on. In the capital-intensive dairy sector, farmers and processors want to know how to invest their money. We owe it to them to provide as much clarity as possible.

So how should we prepare for the end of the quota system?

This afternoon, Pierre Bascou will present some analysis of the likely impact of the end of quotas, and of various options for increasing quotas before 2015.

I don't want to steal too much of his thunder, but there are one or two points that I would like to highlight briefly.

First, the study shows that in the years after quotas end, the milk price will more or less come back to where it was at the start of 2007. Of course, such forecasts are not cast-iron predictions of the future, but nonetheless they're useful for giving us the big picture.

If we're likely to get back to our starting-point in terms of price, a key issue is what path the price would take between now and 2015 – whether it would move smoothly (under a "soft landing" scenario), or with sharp changes (a "hard landing").

Unsurprisingly, if we gradually increase quotas each year from quota year 2009, our analysis forecasts a relatively smooth price path.

On the other hand, if we do nothing before 2015 – when the quota system expires – things would be less smooth. Prices would rise for a few years as growing demand chased static supply, then they would drop sharply when quotas ended.

This makes me think of an air pilot who takes off, gains height and then asks his passengers to kindly leave the aircraft – with or without a parachute. This is not standard flying practice!

I leave it to you to draw conclusions from the more detailed presentation that Pierre will give this afternoon.

In the meantime, as you know a number of Member States have asked for an increase in quotas. Therefore I have proposed a quota increase of two per cent to take effect in the coming quota year.

I emphasise strongly: the market can take this. That point emerges very clearly from our dairy market report, which Martin van Driel will present in just a few minutes.

Furthermore: the market **needs** this increase! Consumers want more dairy products, both in the European Union and outside it. It seems ridiculous to me to let non-European producers sweep up all these opportunities – and there is widespread support for this view in the Council.

There is great demand for our high value-added products around the world.

Any future quota increases beyond this initiative of two per cent are a matter for the Health Check.

Obviously, increasing quotas is not the only possible way of preparing for the end of the quota system. Various other methods have been suggested.

One of these is to **allow quota trade between Member States**.

This is not a simple issue.

On the surface, quota trade across national boundaries might seem attractive. It would allow production to move around – which is what will happen when the quota system ends.

But the forces behind the movement would not be identical in the two cases.

Without quotas, we could reasonably expect that, over time, production will take place mainly in areas where it's most competitive.

With quotas, competitiveness is not the only important factor which decides where production takes place. Another is access to capital – because quota rights cost money.

Also, many Member States don't allow free quota-trading even within their own territory, so it's rather unlikely that they would accept a proposal for an EU-wide system!

On the other hand, there are various other options for action before 2015 which are more realistic. These include:

- eliminating the levy;
- eliminating or phasing out the fat adjustment; and
- balancing unused quota and quota overshoots at the level of the European Union.

And let's also talk about ways of helping areas which are particularly concerned about the coming end of the milk quota system. I mean those areas – especially but not exclusively mountainous areas - which depend very heavily on dairy production, because no other economic activity would be viable for them.

As I have said before, there's more than one possibility for assisting them. One is through rural development policy. Another solution could be to set up specific support measures under a revised **"Article 69"**. This article is in the Regulation on the Single Payment Scheme. It allows Member States to top-slice decoupled payments and spend the money on particular types of farming and quality projects in a given sector. I think we could make the rules more flexible to help meet new challenges.

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In conclusion: as you can see, I have a number of ideas on the boil about the future of the dairy sector. And within the Health Check I think we have a real opportunity to take action that would benefit both farmers and processors.

But what do you think? Where do you see the risks and opportunities? Please speak up freely! Because I want to hear comments now, within the consultation process, rather than hear demonstrations outside my office building two years from now!

Thank you for your attention.