



EUROPEAN PARLIAMENT

2009 - 2014

Committee on Budgetary Control

16.11.2009

WORKING DOCUMENT

on Special Report 14/2009 of the European Court of Auditors on The instruments for managing the milk market and dairy products - have they achieved their main objectives?

Committee on Budgetary Control

Rapporteur: Christel Schaldemose

1- General context

Milk is one of the main agricultural products of the European Union. More than one million farms produce 148 million tonnes annually with an approximate value of 41 000 million euro, which is 14 % of the value of European agricultural production (EU-25, 2006). The European Union is the world's biggest producer of milk (27 %), ahead of India (20 %) and the United States (16 %) and well ahead of Oceania (5 %).

Milk processing employs around 400 000 people in Europe with total turnover of approximately 120 000 million euro. Raw milk delivered to dairies is processed into a wide range of products for both human and animal consumption, or for use in industry.

The Community dairy policy, as is the case with other agricultural sector policies, is based on the global objectives set out in Article 33 of the Treaty establishing the European Community. It refers to the following four objectives:

- to provide equilibrium to the milk market and to reduce structural surpluses as sustained by ECA and European Court of Justice case law;
- to stabilise the prices of milk and milk products;
- to ensure a fair standard of living for the agricultural community by increasing farm productivity through gradual structural adjustments;
- to improve the sector's competitiveness on international markets aligning European prices with world market prices, which are structurally lower.

The common market organisation in milk and milk products entered into force in 1968 under the Common Agricultural Policy. Then, the introduction of milk quotas in 1984 was one of the reforms dealing with structural surpluses. Accordingly, the 2003 reform initiated the liberalisation of the milk sector by reducing price support, creating direct income support and introducing ceiling on production.

The following market management instruments were put in place:

- the milk quota regime,
- public storage of butter and skimmed milk powder,
- aid for private storage (abolished in 2007),
- measures to aid disposal on the internal market, import levies / export refunds for certain products and income support for milk producers during the period 2004-2007 (milk premium and additional payments).

2- Audit scope and approach

The audit considered how effectively the Commission manages the market for milk and milk products. The audit had the main objectives and more precisely to assess:

- the achievement of market equilibrium.

After some initial reticence since 1984, the use of quotas was accepted by a majority in the sector as a powerful and politically acceptable instrument for regulating production. So the introduced system has been effective because the Community production complied with the ceiling imposed. During the 1995/1996 to 2004/2005 years the quota was exceeded less than 1 % as compared with subsequent marketing years when it was under-used as for example in 2007/2008, it was 1,682 million tonnes for the EU-25 (1,2 % of the quota), and 2,222 million tonnes (1,0 % of the quota) for the EU-27. Also, the Court based its arguments on a comparative study of the Member States that most frequently exceed in relative terms their quotas as Italy, Germany, the Netherlands, Austria, Denmark, Cyprus and Luxembourg. However, from 1984 to 2004 the quota regime did not put an end to overproduction and it was necessary to resort to intervention for market regulation. The Court recommended in its Special Report No 6/2001 adjustments to the milk quota regime that is extended until 31 March 2015.

- the stabilization of milk price.

The milk quota system limited supply and allowed nominal prices to be maintained at a relatively high and stable level. Allowing for seasonal variations, prices recorded in the EU for raw milk varied little during the 1984-2007 period compared with the period before the introduction of quotas.

The average nominal price calculated by the Commission was 29 euro/100 kg in 2006 that corresponds to a price range of between 20,1 euro/100 kg in Lithuania to 40,4 euro/100 kg in Cyprus. The Court sustains, based on Eurostat data, that price stability had therefore been achieved after 1984 compared to main world milk producers: USA, New Zealand and Switzerland.

However, over a long period milk producers never actually benefited in real terms from stable prices, because only nominal producer prices were maintained.

- the impact on producers' incomes.

The audit notes that subsidies form a major and increasing part of this income and the net incomes at current prices of agricultural enterprises specialising in milk grew at the same pace as the incomes of farms as a whole during the 1989-2006 period. This can be explained by sectorial reorganisation, the increase in the size of holdings, milk premiums, single payment and rural development aid. More specifically, the unequal restructuring of the milk sector contributed from one side to a fair standard of living for milk producers and an increase in farm productivity, but at the same time in 50 % lost of EU-15 dairy farms between 1995 and 2007.

- the competitiveness of milk products on world markets.

The Court analyzes the world market for milk products that only accounts for 6 % of world milk production (2007) with volatile prices.

In 2007 the EU exported approximately 9 % of its total production in milk equivalent, which makes it the second largest exporter in the world after New Zealand. At the same time the European Union has greatly reduced its export aid for milk products which is to safeguard the Community's international trade in milk and milk products and only from June 2007 to December 2008 the rate of refund set by the Commission was zero for all products.

3- Findings of the European Court of Auditors

The Court highlighted the need for the market liberalisation process, which will involve withdrawal of the milk quota scheme. To complete the analysis made and test the relevance of the initial conclusions on the situation in the milk sector and its prospects, and on the management of the common market organisation.

The EU's milk policy was designed to meet a complex range of objectives¹ and the Court's report analyses the degree to which these objectives have been achieved and draws attention to those facts which are proving to be the most critical in the process now underway of liberalising the European milk sector.

4- Recommendations of the European Court of Auditors

Since 1984 milk quotas have been the keystone of European milk policy with strict limitations on production. National ceilings were set on the basis of historical production and a number of national quotas, notably Italy's, have been systematically exceeded. Even if at the end of 2006 and in 2007, for the first time the surpluses almost disappeared, in 2008 and 2009 it reappeared again.

Four main recommendations can be summarized:

1. The Court of Auditors considers that the Commission must continue to supervise the development of milk and milk products market to make sure deregulation of the sector does not lead to the recurrence of overproduction.
2. The Court reiterates that the price formation in the food sector must be subject to regular monitoring by the Commission together with the Member States to ensure that the concentration of processing and distribution companies does not reduce milk producers to mere price-takers and does not restrict the final consumer's welfare.
3. Another recommendation of the Court to the Commission was to identify specific problems of milk production in mountain areas and to tackle the environmental consequences of the geographical concentration of milk production. The Court also proposes to put in practice price support and direct income in accordance with the regional and social aspect.
4. It considers that the Commission and the Member States had to reorganize the milk production by satisfying the needs of the European domestic market and to concentrate towards the production of cheeses and other products of high added value which can be exported without budgetary assistance.

¹ The main EU's milk policy objectives: to reach a situation of market equilibrium, to stabilise the prices of milk and milk products, to ensure a fair standard of living for producers and to improve the competitiveness of European milk products on international markets.

5- Replies of the European Commission

Milk quotas will end on the 1 of April 2015 as decided by the Council, acting on Parliament's opinion from 2003. The purpose of the reform of the dairy sector in line with CAP reform was to make production more market-oriented. The measures were intended to support increased competitiveness and help milk producers prepare for future challenges on international markets, whilst providing income support by way of direct payments.

It is relevant to note that the asymmetric development in producer and consumer prices has raised concern about the functioning of competition in the chain from stable to table. As well, rural development measures have been and continue to be available to help farmers restructure and adapt to new market conditions. Gradually dairy farmers no longer receive any support related to their milk production.

The Commission considers that the stability of nominal prices and the fall in real prices was common to the milk sector. Moreover, it suggests that price developments must be assessed in the light of international market developments and the price differential with the world market price must be reduced.

It should be emphasised that high production capacity of third countries pushed EU producers to focus on developing and expanding high-value markets for products where Europe has a more sustainable competitive advantage, such as cheese.

Finally, it is important that the reform takes into consideration the socio-economic dimension of the rural areas.

The Commission will implement a series of initiatives proposed by a High Level Group on the Competitiveness of the Agro-Food Industry in view of improving the functioning of the food supply chain and monitoring the food prices. Furthermore, it will be implemented a simultaneous monitoring and data collection by national competition authorities in order to have a fast-track survey of dairy market and to provide better transparency to all interested stakeholders.

Also, the specific situation of mountain areas will be addressed by a Commission working paper to be presented in November 2009 taking account the Court of Auditors' Special Report No 4/2003.

At the same time the Commission is convinced that action should be taken at the legislative level through compliance with environmental protection standards and at the incentive level through aid for introducing greener agricultural practices.

6- Comments and recommendations of the rapporteur for inclusion in the resolution on the Discharge for the financial year 2008-Commission

1. Reminds the Court of Auditors that there is not just one way of securing market equilibrium, price stability, a fair standard of living for the agricultural community and improve the competitiveness for the EU milk markets.

2. Refers to the fact that the Court of Auditors in 2001 in a special report recommended an abolition of the milk quotas. This recommendation has been followed by the Council, Commission, and the European Parliament. Requests the Court of Auditors not to create confusion about the development of the CAP and requests the Commission to continue the implementation of the political decisions to avoid any unnecessary confusion for the milk sector.
3. Notices that the Court of Auditors are particular concerned for the consequences in mountain areas and less favoured areas. This concern is sheared by the Parliament but the Rapporteur reminds the Court of Auditors that the milk quotas and support for agriculture should not be an instrument to consider the interests of these areas. The European policy for rural areas and the subsidies are - and should be - used to accommodate these problems.
4. Disagrees that the EU milk market should primarily focus on the internal market and not aim at competitiveness in the world market. The global competition is a reality the EU has to face. When the world market is further liberalised the milk farmers in the EU should be able to keep up. In the long term competitiveness in relations to the world market will be a way of increased prosperity among farmers. By not trying to be a part of this will lead to reprehensible use of the common funds and will in the long term mean a reduction in the earnings of the European milk farmers.
5. Agrees with the opinion of the court concerning the need for a continuing supervision of the development of the milk market, and therefore recommends the commission to continue the good job done.
6. Recalls moreover that the various objectives of the common agricultural policy are contradictory and consider more than ever necessary a detailed and exhaustive debate on the purpose of the CAP.