

Common organisation of agricultural markets (CMO): simplify the common agricultural policy (CAP), creation of one single Regulation ("single CMO Regulation")

2006/0269(CNS) - 08/12/2010 - Follow-up document

Council Regulation (EC) No 1234/2007 (Single CMO Regulation) provides for the Commission to present a report before 31 December 2010 and 31 December 2012 regarding the evolution of the market situation and the consequent conditions for smoothly phasing out the milk quota system. This present report is the first of the two reports. It is made up of two parts: the first part describes the evolution of the market situation for cow milk from 2008, the year when the [Health Check](#) was decided, till the middle of 2010 and outline medium term prospects. A second part examines the phasing-out of the milk quota system.

Evolution of the market situation for milk: after a significant fall in prices and producers' incomes in 2008-09 that followed the price spike of 2007, the dairy market situation has recovered in the second half of 2009 and continuously improved in the first half of 2010. The report notes that the milk sector went through a period of high price volatility from 2007 to 2009. Since then, the market situation has improved and prospects are broadly positive. Overall, the milk sector is gradually heading towards more market orientation. The process has been affected by the economic crisis in 2008 and 2009. Volatility, which is a standard phenomenon in a market oriented sector, has become more pronounced and therefore damaging due to the convergence of exogenous factors, among which the fall in household consumption for lack of purchasing power in the wake of the economic crisis.

With regard to medium term prospects, milk production is projected to return to an increasing path from 2011 onwards, driven by a fairly optimistic demand outlook based on improved macroeconomic prospects. EU-27 milk production in 2020 would exceed the 2009 level by about 3%. Milk deliveries would be expected to increase by a slightly higher rate, the difference being due to gradually declining on-farm consumption in the EU-12. In the context of quota abolition, the EU-27 milk production is projected to depict a very modest reaction to the end of the quota regime with EU deliveries. The outlook appears favourable for higher value added dairy commodities, driven by growing demand for cheese and fresh dairy products. Production of fresh dairy products (including drinking milk, cream, yoghurts, etc.) is projected to increase by about 8% (from 2009 to 2020) and cheese output is depicted to grow by about 10%. Prospects for cheese exports can be deemed as favourable, notwithstanding an assumed gradual strengthening of the Euro currency, with the EU maintaining a steady share in global cheese exports above 30%.

Phasing out of milk quota system: the Council decided to increase milk quotas by 2% on 1 April 2008. The Health Check decisions of November 2008 resulted in an annual increase in milk quotas by 1% over 5 consecutive years, beginning on 1 April 2009, plus an adjustment of the fat correction factor which resulted in a further de facto 1% increase in quotas. There remains 3 times 1% annual increase until the expiry of the quota system on 1 April 2015 (except for Italy where it was decided to frontload the 5% increase already as of 1 April 2009).

Year on year, milk quotas are gradually becoming less relevant, as milk production falls short of quota in an increasing number of Member States. While surplus levy had to be paid by 6 Member States in quota

year 2008/09, only 3 are on course to pay one in quota year 2009/10. According to official notifications by the Member States, the 2009/10 quota year is estimated to have ended with EU milk deliveries approximately 7% under quota.

EU milk production grew only marginally in 2008 despite the 2% quota increase decided for the 2008-09 quota year and the relatively favourable milk price paid to producers over the calendar year. The economic recession impacted negatively EU and global demand for value added dairy commodities, which put dairy product prices under pressure and led to a significant fall in milk producer prices in 2009. These low milk prices contributed to a slight contraction in EU milk production in 2009 and early 2010. As a consequence, the 2008-09 quota year finished with a record undershoot of EU deliveries in relation to quota. This undershoot increased even further in the 2009-10 quota year. EU milk production recovered in the course of 2010, but remained significantly below quota level.

The slow response to quota increase is linked to economic recession, which triggered lower demand for dairy products, but also to higher production costs and resulting lower margins. Experience gained from the impact of the 2008/09 quota increase indicates that the response of milk production at the aggregate EU level remained fairly modest, despite a significantly higher average producer price for milk. Latest figures until July 2010 show a stronger production response to increased milk prices.

Milk quotas becoming less and less relevant, EU milk supply can better respond to market opportunities, farmers' response to price signals is less distorted and efficiency gains can be achieved through restructuring.

"Soft landing" is on track in an overwhelming majority of Member States. Milk quota prices have a very low value, already at zero in some Member States, and decreasing in most of the others with a view to reach zero in 2015. Milk quotas have ceased to work as a production limit in most Member States, especially in the new Member States, and market orientation is already the leading principle in a number of them.

The conclusion is that **under these circumstances there is no reason to revisit the Health Check decisions** with regard to the gradual increase in quotas and the end of the quota regime on 1 April 2015. In order to pave the way towards quota abolition in 2015, the Commission would like to raise for consideration a further step to assist in the process of soft landing: in order to increase awareness and reinforce the responsibility of operators in the dairy chain to better take into account market signals and adapt supply to demand, transparency should be enhanced, as pointed out by the High Level Group on Milk. In addition to the information systems already in place, meetings would be organised for the experts of the Management Committee for the single CMO jointly with the Advisory group on milk to follow market developments in order to assess the market situation and prospects. In case of serious imbalance, as a further tool to stabilise the market and as an exceptional measure if other measures available under the single CMO appeared insufficient, the Commission could consider a system based on Article 186 of the single CMO ("disturbance clause") that would allow milk producers, on a voluntary basis, to reduce their deliveries against compensation. Experience gained during the milk crisis shows that it may be sufficient to take 1 or 2% of overall milk production out of the market to correct imbalances and restore stability. A further report will be tabled by the end of 2012.