Opinion of the European Economic and Social Committee on:

— **the 'Proposal for a Council Regulation amending Regulation (EC) No 1255/1999 on the common organisation of the market in milk and milk products' (2003/0011 (CNS)), and**

— **the 'Proposal for a Council Regulation establishing a levy in the milk and milk-products sector' (2003/0012 (CNS))**

(COM(2003) 23 final — 2003/0011 + 0012 (CNS))

(2003/C 208/12)

On 10 February 2003 the Council decided to consult the European Economic and Social Committee, under Article 37(2) of the Treaty establishing the European Community, on the above-mentioned proposals.

The Section for Agriculture, Rural Development and the Environment, which was responsible for preparing the Committee's work on the subject, adopted its opinion on 25 April 2003. The rapporteur was Mr Voss.

At its 399th plenary session on 14 and 15 May 2003 (meeting of 14 May), the European Economic and Social Committee adopted the following opinion by 77 votes to 13 with 17 abstentions.

1. **Introduction**

1.1. Regulation (EEC) No 804/68 brought in the common organisation of the market in milk and milk products. Key market instruments have included common prices, state intervention and private storage, internal consumption aids and export refunds. In addition, in 1984, when there were large dairy surpluses in the Community, a dairy quota system was introduced aimed at supporting producer prices while at the same time limiting production and expenditure.

1.2. Although the number of dairy farms has shrunk, dairy cattle farming in the disadvantaged regions has held steady since the introduction of the quota system. Eurostat figures indicate that nearly 50 % of dairy farms and around 38 % of dairy cattle are to be found in the disadvantaged regions.

1.3. The Berlin European Council of March 1999, as part of the reform it approved for the Common Agricultural Policy, stipulated the following for the dairy sector: extending the dairy quota system until 2008, cutting back intervention prices by 15 % and introducing direct payments as of the 2005/2006 marketing year, as well as raising the quota by around 2,4 % as of 2005. 0,9 % of the quota was already allocated in some Member States in 2000. Moreover, as part of the Mid-term Review, the European Commission was instructed to compile a report on the impact of the reform measures and to submit proposals for the dairy sector post 2008.

1.4. On 10 July 2002, in a report on the dairy quotas (SEC (2002) 789 final), the Commission put forward four options as a basis for the Mid-term Review:

Option 1: Continuation of the Agenda 2000 measures up to 2015 (no additional reform measures);

Option 2: Repetition of the Agenda 2000 approach (further lowering of the intervention prices and an additional 3 % increase to quotas);

Option 3: Introduction of a two-tier quota regime (reducing the 'A' quota on production for the internal market and not placing any limit on the 'C' quota on production for exports);

Option 4: Removing quotas in 2008 and cutting intervention prices by a further 25 %.

1.5. Over half of the approximately 1,7 million beef producers in the EU keep milk cows (1997 figures). Around 2 million people are employed in the dairy sector, including the processing industries. In most Member States and in the EU as a whole, dairy production constitutes the biggest area of farming activity. The dairy sector on its own makes up around 14 % of total agricultural production in the EU. Of this, producers account for approximately EUR 38 000 million and the processing industries around EUR 80 000 million. 80 % of the value added from farming in grassland areas comes from dairy production.

1.6. To a large extent, the diversity of the cultural landscape in Europe has been shaped over time by cattle farming and the use of pasture. Both regional differences in soil and climate conditions and different ways of using and farming the land have given rise to extensive species diversity in cultivated land. Despite increasing use of concentrated feed, dairy cattle farmers are still the heaviest users of grassland in central

Europe. The key environmental importance of dairy farming is also demonstrated by the fact that in some countries a high proportion of dairy farms practise environmentally friendly production methods.

1.7. Another factor is the wide variety of regional dairy products associated with dairy farming in Europe; furthermore, these products are of exceptionally high quality. The European dairy production and processing sectors operate to high technological standards.

1.8. In economic terms, there is a strong link between dairy cattle farming and beef production. If interest in cattle fattening declines (e.g. if prices fall or premium payments are decoupled) then calf prices will come under pressure and dairy producers' incomes fall.

2. Content of the reform proposals

2.1. The Commission is proposing to extend the existing dairy quota system beyond 2008 until the 2014/2015 marketing year.

2.2. The method adopted in 1984, which consists of applying a levy to quantities of milk collected (115 % of the target price) or sold for direct consumption above a certain guarantee threshold (quota), is to be maintained. To this end, for each Member State a specific guaranteed total quantity is set for a reference milk-fat content.

2.3. The Agenda 2000 reforms relating to this sector are to be brought forward by a year to 2004/2005, since unanticipated budgetary resources have become available for a reform of the dairy market.

2.4. On the basis of Option 3 of the Milk Quota Report, each Member State's milk quota is also to be raised by an additional 1 % per year in 2007 and 2008.

2.5. The originally scheduled uniform price cut of 15 % (a three-stage reduction of 5 % a year) will be replaced with asymmetric intervention price cuts over 5 years. A 17,5 % reduction in skimmed milk powder prices together with a 35 % cut in butter prices equates to an overall reduction of 28 % in EU target milk prices over five years, down to 22,21 cents/kg from 30,98 cents/kg today.

2.6. The Commission is proposing a limit of 30 000 tonnes per annum for intervention purchases of butter. Beyond that limit, purchases can be carried out under a tender procedure.

2.7. Partial compensation for the price cuts will be paid out to milk producers in 2007 and 2008 in the form of direct payments. The partial compensation for price cuts will climb from 0,575 cents/kg to 2,874 cents/kg between 2004 and 2008.

2.8. Additional national supplementary ceilings for milk can also be transferred to individual reference quantities or paid out in another way. It has thus been extrapolated that in 2008 a total of 4,17 cents/kg of milk will be paid out in compensatory payments, which corresponds to a partial compensation of just under 50 %.

2.9. Once the reform begins in 2004, direct payments are to be decoupled and paid out as area-based farm payments. Their calculation is based on the historical premium payment for individual farms.

2.10. In contrast to other market areas, the base date for calculating the level of premium payments based on milk production lies not in the past but in the future (31 March 2004).

3. General comments

3.1. Average production costs for milk in the EU stand at 30-35 cents/kg. However, variations in local conditions, climate, farming structures and quota costs may mean that production costs sometimes lie significantly above 45 cents/kg. Competition is distorted as a result of farmers with arable land having had the advantage of lower feed costs since 1992. Because farmers cultivating 100 % plant silage fodder crops (silage maize) are eligible for premium payments, they have so far had an economic advantage over grassland farmers.

3.2. In various opinions on the multifunctional nature and the European model of farming, the EESC has highlighted the importance of milk production [1]. The demand on the part of EU society and, in particular, consumers for high quality in both dairy products and production conditions and the need to protect production locations call for special support for dairy production by introducing protective measures aimed at products imported into the EU.

3.3. The EESC supports the Commission's proposal to continue to apply the dairy quota system beyond 2008, since opting out of the quota system would lead to an increase in production and an unquantifiable fall in prices. Despite lower costs in some areas (e.g. for quota leasing), producers' incomes would fall sharply and the number of farmers leaving the business would rise, since particularly in grassland areas there is no economically viable alternative to dairy farming. This

(1) OJ C 368, 20.12.1999, pp. 76-86.

would have an enormous impact on the objectives of maintaining broad-based agriculture and preserving environmentally important grassland areas.

3.4. The EESC notes that only 6 % of worldwide dairy production is traded on the 'world markets'. Overall demand for milk and milk products is growing slightly. However, with a current annual volume of trade amounting to approx. 30 million tonnes, the 'world market' is already very nearly saturated. Different production costs and conditions have created a situation where EU milk production is at a disadvantage vis-à-vis some regions, such as Oceania and South America; increasingly the world market is being supplied with mass-produced dairy products from these regions. On the other hand, the higher quality segments of the market still offer growth opportunities for the EU.

3.5. The EESC does not share the Commission's view that national and international markets' take-up of European dairy products will increase. Contrary to the Commission's assessment, it is more the case that the market options are very limited because:

— the supply of dairy products has increased world-wide;

— demand is poor due to flagging growth in purchasing power;

— growth in demand for cheese has settled down again now that the BSE crisis has died down;

— demand has declined as a result of turmoil in the world economy in the wake of 11 September 2001;

— EU exports are at a disadvantage due to a stronger euro;

— subsidised exports from regions with surpluses;

— major trading partners such as Russia and the USA are restricting imports; and

— competition is being distorted by national dairy trade organisations (New Zealand) and tax measures (USA).

4. **Specific comments**

4.1. The Commission believes that the 28 % reduction in the target price 'justifies a(n) ...increase in the total ... reference quantity for milk following each price reduction, with a view to keeping production in balance with the expected trend in consumption and avoiding any disturbance of the market in milk products'.

The EESC notes that:

— In the past, the milk intervention price provided the basis for the actual price paid for milk; this was about 10 % higher than the intervention price. Consumer demand for milk products is inelastic. It is not realistic to assume that a significant increase — totalling 4,4 % — in the milk quota linked to supply rights will lead to a price reduction amounting to only half of the cut in the intervention price.

— Since the quota increases and the intervention price cuts are to be carried out in parallel with the annual dairy/food trade price negotiations, the discounters' price dumping strategy will be underpinned. Thus the intervention price is turning into a guideline for price cuts, no longer fulfilling its true function as a safety net.

— The price compensation payments to be paid out as of 2004/2005 can only compensate for about half of the drop in price. Given the many jobs on dairy farms (SMEs) and the large number of other production areas associated with this sector, this proposal is unacceptable. It is imperative that the compensatory payments for milk be set at the same level as those paid out to date for cereals and beef, i.e. around 90 %.

4.2. Storing surplus dairy products in intervention stocks and subsidising dairy product exports to non-EU countries not only generates costs but is also an approach being questioned by society. At the same time, the internal market is experiencing stagnating demand for butter and only slightly rising demand for cheese and fresh dairy products. The EESC therefore feels that the Commission's proposal to increase dairy quotas by 1 % a year in 2007 and 2008 is in no way warranted. At the same time, there is no justification in market policy terms for the Commission's plans to bring forward the quota increases laid down in Agenda 2000. Rather, on the basis of the decisions taken in Berlin, the quota increases that have already been decided should only apply when the market can absorb the increased quantities without subsidies.

4.3. Measures to reduce butter intervention to 30 000 tonnes, limit it in time and allow the possibility of further private storage will mean that intervention will no longer meet the requirements of price support. As a result producer prices will fall well below the intervention price. On the other hand, unlimited intervention creates situations where, in unfavourable market conditions such as at present, extensive intervention stocks are built up which can weigh on the market for years. The EESC therefore calls on the Commission to introduce a flexible quota system as a permanent component of its dairy market policy. In the event of intervention stocks accumulating, there should be an automatic adjustment; when such stocks shrink, then quotas could be expanded. A further indicator for dairy quote adjustment should be price thresholds for important basic dairy products. In this way, the interests of milk producers, consumers, taxpayers and the dairy industry could all be reconciled.

4.4. The EESC notes that putting the Commission's ideas about quantity increases and price cuts into practice will probably push up the budgetary cost of dairy compensatory payments to EUR 4 895 million by 2013. The Commission has calculated that market measures, such as export refunds, public and private storage and internal aids, will amount to EUR 1 328 million in 2013 compared to EUR 2 360 million at present. With the reforms, the milk market would cost around EUR 4 000 million more in 2013. In addition, European milk producers will be losing EUR 4 to 5 000 million in income from milk production every year.

4.5. The EESC is most concerned about the reference periods (1999-2001) proposed in the Harbinson paper [1] for dismantling the Blue Box, as called for by the WTO. Since the compensatory payments for milk did not exist at that time, and are in fact only to be paid out in the future, they are at particular risk from the dismantling process.

4.6. The EESC disapproves of the planned drastic price cuts and the approximately 50 % compensation through premium payments. It would point out that other compensatory payments have made up for around 90 % of price cuts. Equality of treatment would seem justified, especially given the particular multifunctional importance of dairy production. Where the location (such as in upland areas) is the cause of extreme disadvantages, compensation should be provided under the second pillar.

4.7. The Committee would underline that, because of the Berlin agreements, EU milk quotas have already been increased by 0.9 % in some countries. These quotas are now pushing down the producer prices without milk producers receiving any compensation.

4.8. The EESC fears that the Commission's proposals for dairy market reform will entail major restructuring in rural areas of the EU. It is not clear how the second pillar of the CAP can even come near to putting right the damage to rural areas which will be caused by this dairy market reform. It is more the case that the financial resources for the second pillar are becoming more meagre: throughout Europe, only an additional EUR 1 481 million will be available in 2013 for rural development from modulation and degression. However, Poland alone has been allocated an additional EUR 900 million per annum for rural development.

4.9. The Commission proposals will, to the Committee's mind, create a situation where milk production in grassland areas and low-yield disadvantaged regions will continue to suffer from major competitive disadvantages. In its proposal the Commission states that, because of the positive environmental impact involved, steps must be taken to encourage the preservation of permanent grassland so as to pre-empt a wholesale changeover to arable farming. The intention of a ban on ploughing grassland, implemented by the Commission as of 31 December 2002, is to specify land-use as part of the cross compliance measures. However without added value, even a ban on ploughing is not enough to preserve grassland. The option granted to the Member States by the Commission to level out regional premium payments offers one solution. The levelling out of regional premium payments could, however, mean milk producers in regions with a higher than average proportion of arable land gaining competitive advantages vis-à-vis producers in regions with a low average proportion of arable land, as is often the case in alpine regions. The Commission is therefore urged to develop further its proposal for taking account of the different situations in the Member States, thus allowing premium payments to be distributed more fairly.

4.10. If the EU should be obliged, for reasons associated with world trade policy, to take the path of price cuts and decoupled compensatory payments, then dairy compensatory premium payments should likewise be decoupled.

4.11. The EESC attaches particular importance to the dairy quota system as an instrument for maintaining regional added value. Here the Committee calls on the Commission to be more specific about the horizontal measures set out in Annex 4.

4.12. The thinking behind and aim of having a national reserve does make sense. No requirements are laid down, however, as to its minimum size. There has to be a definition of the 'objective criteria' determining the distribution of national quotas so that structural policy aims (e.g. encouraging young farmers) are made quite clear.

4.13. The definitive date for setting premium payments for milk is 31 March 2004. The EESC would point out that this date in the future will lead to speculation on the market for quotas. Small milk producers who, knowing that prices are going to fall, do not see any future in milk production, will try to sell off their supply rights at the highest price possible. This will accentuate the structural change. Valuable jobs in small and medium-sized enterprises will be lost.

4.13.1. It makes sense in structural and budgetary policy terms to rule out the subsidising of quota purchases.

4.14. The EESC likewise feels that the changes to fat and protein price support make sense.

(1) WTO — Committee on Agriculture Special Session — Negotiations on Agriculture. FIRST DRAFT OF MODALITIES FOR THE FURTHER COMMITMENTS TN/AG/W/1 — 17.2.2003. Such draft has been revised on 18.3.2003 (TN/AG/W/1/Rev.1 — 18.3.2003 (03-1585)).

4.15. The horizontal proposals include one option for reconciling the interests of tenants and lessors: up to five years' break from claims for premium payments in the event of tenants and lessors not reaching an agreement.

5. **Conclusions**

5.1. The EU must provide milk producers with stability as regards political decisions beyond 2008, so that they are in a position to make plans. The EESC therefore in principle welcomes the extension of the dairy quota system up to 2015. However it feels that the Commission's other proposals counteract the aims of a quota system (regulating production volume, guaranteeing income in disadvantaged areas, securing jobs in the dairy industry and reducing the burden on the budget).

5.1.1. The EESC calls on the Council and the Commission to develop a new, flexible instrument for adjusting production volumes, and thus to react to market circumstances.

5.1.2. At the present time, against the background of the current market conditions, the EESC does not support any commitment to expand milk production in 2007 or 2008.

5.1.3. Given the growing intervention stocks, the Committee also urges the Council and the Commission to revise the decision on a 1,5 % quota increase based on the Berlin decisions. Quotas should only be increased when market conditions allow.

5.2. The EESC disapproves of the Commission proposals on intervention price cuts and the measures to restrict butter intervention to 30 000 tonnes. Where price cuts have to be made, it also calls on the Commission to make the same compensatory payments as provided for in the organisation arrangements for other markets (around 90 %).

5.3. Existing market instruments such as aid, refunds and intervention should be used selectively and for supporting the market. Their effects should be constantly assessed and they should be adjusted accordingly.

5.3.1. In order to help firms in extremely disadvantaged locations, additional aid instruments under the second pillar should be constantly developed and adjusted.

5.4. The EESC attaches particular importance to milk production in grassland areas. It therefore considers it imperative to remove the competitive disadvantages suffered by these areas, which were brought about by the 1992 agricultural policy reform. To this end a compensatory premium payment under the first pillar of the CAP is needed.

5.5. The Committee would strongly advise the Commission, in the WTO negotiations, to push through quality requirements applying to imports of milk and dairy products, so as to protect high-quality EU products and to defend the European model of multifunctional farming.

5.6. The Committee feels that the Commission has not adequately investigated the impact of the legislative proposals on the milk sector. Above all there has not been enough analysis of the repercussions on the sectors concerned or of the extent to which these proposals tie in with the aims of the various EU policy areas. The options for, and costs of, offsetting the negative impact of the reform must also be set out. Of particular importance here are the repercussions on the labour market, the number and structure of small and medium-sized enterprises, upstream and downstream economic sectors and the environment. The results from the impact studies available to date confirm the EESC's fears in this respect.

Brussels, 14 May 2003.

The President

of the European Economic and Social Committee

Roger BRIESCH