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COMMITTEE OF THE PROTOCOL REGARDING CERTAIN MILK POWDERS
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Statement by the European Communities on 20 June 1988
to the Committees of the Protocols

COMMON AGRICULTURAL POLICY: FOUR YEARS OF REFORMS
AND THE EFFECTS ON THE DAIRY SECTOR

Four years ago the European Economic Community undertook one of the most important as well as most difficult actions: the reform of the Common Agricultural Policy. Not only did the Community begin the process in the dairy sector, but it is also the one which has shown the greatest effects, both on the internal market and on world markets.

During discussions in the Committees of the Protocols of the Dairy Arrangement and also in the International Dairy Products Council, the Community sometimes has the impression that neither the reasons nor the effects, achieved or expected, are sufficiently well known.

I have therefore been instructed by my authorities to give you, with your leave, Mr. Chairman, an overview of the reform of the Common Agricultural Policy over the last four years, as well as what the Community expects to reap from this reform in the near future.

1. Reasons for the reform

The spectacular development of European agriculture and the deep changes in the general economic setting and in world markets since the early 1980s made it essential to restructure the Common Agricultural Policy. The growing imbalance between supply and effective demand typical of this situation was the consequence, as stressed in the communiqué of the OECD Ministerial Meeting in May 1987, of excessive support policies carried out by all Western countries.

A trend leading to the build-up of stocks that could not be sold at commercial prices therefore had to be corrected.

The adjustment of the CAP mechanisms was all the more necessary since this market situation was leading to an intolerable rise in budgetary expenditure on agriculture. Over ten years, the Community's spending more than doubled.

Such a rate of increase in spending was all the less justified in that it had not been reflected in stable farm incomes. Over this period, per capita farm incomes declined and the agricultural sector's value added dropped by 25 per cent (in real terms); the reason being that an increasing part of agricultural expenditure was devoted to the financing and disposal of stocks.

There have been three major stages in the reform of the Common Agricultural Policy during the last four years:

- 1984, with the introduction of milk quotas, which were subsequently reduced;
- 1986 and 1987, with limits imposed on market support (recourse to intervention) in the cereals and dairy products sectors;
- finally 1988, with the introduction of stabilizers in all market organizations, accompanied by very strict budgetary provisions.

2. Principles on which the reforms are based

- (a) The market must be given back its rôle of guiding production.

This has two essential consequences:

- Prices must be progressively brought back to a level at which supply and demand can be balanced. Action on prices is therefore the main instrument used to manage production.

In the case of milk, a quota system had to be introduced because the market imbalance was such that the necessary drop in prices would have been unacceptably drastic. Nevertheless, even in this sector a restrictive price policy has been followed, and prices have fallen in real terms by 10 per cent since 1984.

- For the market to fulfil its rôle properly, the intervention mechanisms providing an unlimited outlet also had to be corrected. In the case of dairy products this was done for butter (permanent official buying-in limited to 180,000 tons) and milk powder.

The measures thus adopted by the Community go in the direction recommended by the OECD: (influence of market signals on the orientation of agricultural production).

- (b) However, to be politically and socially accepted such a market-based agricultural policy had to be accompanied by measures that would make it bearable for the less-favoured farmers. It should be recalled that following the enlargements of the European Community the number of agricultural holdings has more than doubled since 1981, and the number of small holdings (less than 20 hectares) has risen from 4.3 million to 7.6 million.

The complementary measures taken to this end which also affect the dairy-products sector are in particular:

- increase in the compensatory allowances paid to mountain and hill farmers and farmers in less-favoured regions;
 - introduction of a system of aids to give up farming.
- (c) The third principle on which the reform undertaken is based is that of budgetary discipline, which now has the force of law.

At its session last February, the Council fixed the annual overall budget for expenditures that could be covered by the EAGGF-Guarantee until 1992. The amount fixed as the basis for 1988 and following years is that of actual expenditure in 1987. But in 1987 the two new Member States were not fully integrated into the CAP; thus the EAGGF will henceforth have to bear the expenses of a twelve-member Community within the limits of this overall budget. Until 1992 expenditure will not be able to increase by more than 1.9 per cent annually (in real terms) instead of the 7.5 per cent recorded since 1975; which is a 75-per-cent drop in the rate of increase.

3. The results for the dairy-products sector may be summarized as follows:

- . Between 1984 and 1989, the EEC dairy herd will have been reduced by nearly 20 per cent, or nearly five million cows slaughtered, which is the equivalent of half the dairy herd of the United States.
- . Milk collection will fall from 103.7 million tons in 1983 to 92 million tons in 1989, a decline of 11.3 per cent. On the basis of past trends, if the Community had not introduced quotas the level would have reached 121 million tons in 1989.
- . Butter production in 1989 will be 600,000 tons less than in 1983 (by way of comparison, the world butter market is about 1 million tons).
- . Finally, public butter stocks, which had reached 1.3 million tons in 1986, will be well below 300,000 tons by the end of 1988.

This effort to curb production is all the harder to justify, let alone improve, when other producers are continuing to increase production and, in some cases, price guarantees and support have been further improved.

A detailed description of the various measures adopted since 1984 is attached.

MILK AND DAIRY PRODUCTS

I. Basic indicators (EUR 12)

	1984	1985	1986	1987
<u>Herd of dairy cows</u> (million head)	26.7	26.0	25.5	24.0
<u>Production (Million/tons):</u>				
- Milk	116.7	116.3	117.3	111.5
of which milk deliveries	107.1	105.8	106.9	101.4
- Butter	2.1	2.1	2.2	1.9
- Skimmed milk powder	2.1	2.0	2.2	1.7
<u>Imports (000 T)</u>				
- Butter	90.1	79.8	84.6	78.5
<u>Exports (000 T)</u>				
- Butter	379	387	331	622
of which commercial exports	235	173	191	280
- Skimmed milk powder	298	295	267	390
of which commercial exports	146	183	173	315
<u>Public intervention stock</u> (000 T) ¹				
- Butter	841	996	1,283	860
- Skimmed milk powder	617	520	772	473
<u>Target price for milk (EUR 10)</u> (annual rate of change in % and in real terms) ²	-2.3	-2.1	-1.9	-4.9

¹EUR 10 for 1984 and 1985

²With impact of related measures and agri-monetary decisions

II. Measures to improve market conditions

The measures introduced to restore market equilibrium in this sector essentially concern the introduction of production quotas as from 1984, and a restrictive price policy together with complementary measures aimed at financial co-responsibility of producers and more flexible application of market support measures.

(a) Production quotas

Given the nature of the sector, a drastic price fall would have brought serious income problems for many producers. The Community therefore introduced a production quota system in April 1984.

The mechanism is based on the establishment of a reference quantity by farmer and/or by dairy. If a farmer and/or dairy exceeds the allocated reference quantity, they must pay a levy amounting to 100 per cent of the target price.

The introduction of the set of measures adopted will lead to a considerable decline in milk deliveries. This decline will take place by stages. The introduction of quotas in 1984 led to a first fall of about 4 per cent. Subsequently, in the light of consumption trends, the Community decided on a further reduction which could amount to 9.5 per cent in 1989. This reduction results from a voluntary system of quota repurchase (-3 per cent), a temporary suspension (-5.5 per cent) and a strengthening of the levy system (-1 per cent).

The implementation of these measures led to a reduction of 2.7 million head of cows between 1984 and 1987; a further reduction of 1.4 million head is expected by 1989. Between 1983 and 1989, the sector is expected to undergo the following adjustments:

- 19 per cent reduction in the dairy cow herd (-5.3 million head);
- 10.7 per cent reduction in milk deliveries (-11.7 million tons);
- 25 per cent reduction in butter production (-588,000 tons);
- 45 per cent reduction in milk powder production (-1,100,000 tons).

(b) Restrictive price policy

Despite the introduction of production quotas in this sector, the Community pursued a restrictive price policy which led to a drop of about 10 per cent in real terms in the milk support price between 1984 and 1987. This result was achieved both by a reduction of the intervention price for butter and skimmed milk powder and by much greater flexibility of the intervention system on which market support in this sector is based. Since the milk year 1987/88, intervention buying of

skimmed milk powder have been totally suspended during the winter period and may also be suspended during the summer period as soon as they reach 100,000 tons per milk year.

The same applies to butter, for which the permanent system of intervention buying may henceforth be suspended during the year once the quantities offered for intervention reach 180,000 tons. In that event, the permanent system of intervention for butter is suspended and replaced by a system of intervention by tender, which concerns much smaller quantities at much lower buying-in prices than the intervention price. This occurred during 1987.