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*Committee on Agriculture and Rural Development*

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## **DRAFT REPORT**

on prospects for the EU dairy sector – review of the implementation of the  
dairy package  
(2014/2146(INI))

Committee on Agriculture and Rural Development

Rapporteur: James Nicholson

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## MOTION FOR A EUROPEAN PARLIAMENT RESOLUTION

### on prospects for the EU dairy sector – review of the implementation of the dairy package (2014/2146(INI))

*The European Parliament,*

- having regard to Regulation (EU) No 261/2012 of the European Parliament and of the Council of 14 March 2012 amending Council Regulation (EC) No 1234/2007 as regards contractual relations in the milk and milk products sector<sup>1</sup>,
- having regard to Regulation (EU) No 1308/2013 of the European Parliament and of the Council of 17 December 2013 establishing a common organisation of the markets in agricultural products and repealing Council Regulations (EEC) No 922/72, (EEC) No 234/79, (EC) No 1037/2001 and (EC) No 1234/2007<sup>2</sup>,
- having regard to the Commission report of 13 June 2014 entitled ‘Development of the dairy market situation and the operation of the ‘Milk Package’ provisions’ (COM(2014)0354),
- having regard to the Commission report of 10 December 2012 entitled ‘Evolution of the market situation and the consequent conditions for smoothly phasing-out the milk quota system – second ‘soft landing’ report’ (COM(2012)0741),
- having regard to its resolution of 11 December 2013 on maintaining milk production in mountain areas, disadvantaged areas and outermost regions after the expiry of the milk quota<sup>3</sup>,
- having regard to its resolution of 17 September 2009 on the crisis in the dairy farming sector<sup>4</sup>,
- having regard to the Commission communication of 15 July 2014 on tackling unfair trading practices in the business-to-business food supply chain (COM(2014)0472),
- having regard to the Commission proposal for a regulation of 13 January 2015 on the European Fund for Strategic Investments (COM(2015)0010),
- having regard to Rule 52 of its Rules of Procedure,
- having regard to the report of the Committee on Agriculture and Rural Development and the opinions of the Committee on Development and the Committee on Budgetary Control (A8-0000/2015),

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<sup>1</sup> OJ L 94, 30.3.2012, p. 38.

<sup>2</sup> OJ L 347, 20.12.2013, p. 671.

<sup>3</sup> Texts adopted, P7\_TA(2013)0577.

<sup>4</sup> OJ C 224 E, 19.8.2010, p. 20.

- A. whereas the ‘Milk Package’ came into force on 3 October 2012 and applies until 30 June 2020;
  - B. whereas, as decided in the 2003 Mid-Term Review of the CAP, dairy quotas will expire on 31 March 2015;
  - C. whereas the global dairy market is increasingly volatile, with the highest ever price since records began noted in January 2014, followed by substantial drops in prices throughout the rest of 2014;
  - D. whereas the Russian ban on European dairy products since August 2014 has had a significant impact on the EU internal market and demonstrated the importance of securing diverse export markets for EU products;
  - E. whereas the Milk Package brought in the possibility for Member States to introduce compulsory contracts to help producers and processors plan their production volumes;
  - F. whereas the Milk Package obliged Member States to recognise producer organisations;
  - G. whereas the Milk Market Observatory was established in April 2014 to improve monitoring of the dairy sector for both the Commission and the industry;
  - H. whereas a large number of dairy farms are located in disadvantaged, outermost, remote or mountainous areas;
  - I. whereas compulsory declarations of delivered volumes of milk will apply from 1 April 2015;
  - J. whereas European dairy products significantly contribute to the success of the EU’s agri-food industry and the prosperity of rural economies;
1. Recalls that a sustainable and competitive dairy sector with responsive tools is the goal of the Milk Package; stresses that the issues identified in the Milk Package remain a barrier to a competitive and equitable milk market and a fair income for farmers;
  2. Highlights that dairy farmers are particularly vulnerable to income variations and risks owing to high capital costs, volatile dairy commodity prices, input and energy costs, and that a sustainable livelihood from dairy farming is an ongoing challenge as production costs are frequently close to or above farm gate prices;
  3. Urges the Commission to address the crisis currently facing the dairy sector as a result of a dip in global demand, global price volatility and the Russian embargo, and recognises the targeted measures taken thus far in addressing the impact of the Russian embargo;
  4. Recalls that the dairy crisis of 2009 occurred under the quota structure; reminds the Commission that the delay in responding to the crisis forced many dairy farmers out of business, and expresses concern regarding the Commission’s capacity to respond rapidly and effectively to market crises;

5. Notes that the medium and long-term prospects for the dairy sector in both domestic and global markets remain favourable and, as a key part of the agri-food industry, the dairy sector has significant long-term growth and job creation potential which should be targeted under the new Investment Plan;
6. Acknowledges the important socio-economic contribution dairy farming makes across the EU and its particular importance in disadvantaged and outermost regions, where it is often the only type of farming possible;

### **Challenges and opportunities facing the dairy sector post-quota**

7. Notes that volatility will be a continuing challenge facing the dairy sector and urges the Commission to consider measures to mitigate the risks arising from increased exposure to the world market;
8. Recommends that, in order to prevent further market instability, previous decisions on milk quotas should be maintained;
9. Takes the view that EU dairy policy after the expiry of milk quotas presents an opportunity for the EU economy, and considers that any future measures must strengthen its competitiveness and facilitate growth and innovation;

### **Milk Package and CAP measures**

10. Highlights that implementation of the Milk Package is still at an early stage; expresses disappointment, nevertheless, with the low levels of implementation;
11. Stresses that strengthening contractual relations represents a concrete method of ensuring equitable distribution along the supply chain and reinforces the responsibility of stakeholders to take account of the market situation and respond accordingly;
12. Notes that the sector could further explore the potential offered by longer-term integrated supply chain contracts, forwards contracts, fixed margin contracts, and the opportunity to 'lock in' a milk price for a set period of time; believes that the option to avail of new instruments in contractual relations should be available;
13. Highlights the important role of producer organisations (POs) in increasing the bargaining power and influence producers have in the supply chain, and regrets the fact that there have only been limited moves towards setting up POs; highlights that POs can benefit from financial support under Pillar II and urges further incentivisation to create and join POs as a tool to address imbalances in the supply chain;
14. Reminds the Commission of the importance of transparency across the whole supply chain for the sector to encourage stakeholders to respond to market signals; notes the increased importance of accurate and timely information in the post-quota market;
15. Emphasises the importance of the Milk Market Observatory (MMO) in disseminating and analysing market data and calls for an increased role for the MMO; recommends that the Commission take the necessary action to ensure that the MMO is in a position

to communicate early warnings to the Commission, Member States and relevant stakeholders, when the market situation so requires; considers that the information provided by the MMO should involve updates on market and price trends, and should be easily accessible and user-friendly for all stakeholders;

16. Underlines the importance of Member States providing the relevant information to the MMO in a timely manner for the benefit of all stakeholders, and recommends that the Commission consider additional means of ensuring this information is received on time;
17. Notes that, under Pillar I, optional coupled support is a tool available to assist the dairy sector, while under Pillar II producers can avail of advisory services to support business decisions and sound financial management – if necessary, Member States can use insurance measures such as the Income Stabilisation Tool; calls on the sector to investigate the development of further insurance tools when the market is strong;

### **Potential for the EU dairy sector on the world market**

18. Points out that global dairy demand is predicted to grow by 2 % per annum, offering opportunities for products of EU origin; notes, however, that the market is increasingly dominated by dried dairy products;
19. Underlines that bilateral trade negotiations may represent strategic opportunities for the EU dairy sector;
20. Stresses the continuing need to identify and develop new markets, increase the EU global market share, secure fair access for EU exporters and stimulate export growth;

### **Promotion/quality schemes**

21. Points out that the dairy sector could benefit from increased promotion initiatives on the domestic and third country markets under new Promotional Measures;
22. Stresses the need for the sector to move away from unprocessed bulk production; considers that full use should be made of research measures to develop innovative high-value dairy products in high growth markets such as medicinal nutritional products and nutritional products for infants and athletes;
23. Notes that the sector has not engaged with the Protected Designation of Origin (PDO) and Protected Geographical Indications (PGI) schemes in a meaningful manner; calls on the Commission to simplify access to these schemes;

### **Managing risk in the dairy sector**

24. Stresses that existing ‘safety net’ measures such as public intervention and private storage aid are not suitable tools to address persistent volatility or a crisis in the milk sector;
25. Calls on the Commission to implement more responsive and realistic safety net provisions, and for the intervention price to be more reflective of production costs and adapted as the market changes;

26. Underlines the importance of a more responsive and realistic crisis instrument, and recommends that the Commission engage with the sector on the possibility of using risk management instruments such as the futures markets to take advantage of the volatility in the sector to increase its competitiveness;

#### **Unfair trading practices in the dairy supply chain**

27. Stresses that dairy producers are particularly vulnerable to imbalances in the supply chain, in particular owing to fluctuating demand, rising production costs and decreasing farm gate prices; considers that the downward pressure on prices by retailers from own-brand labelling and the persistent use of liquid milk as a 'loss leader' by retailers undermines the work and investment of producers in the dairy sector and devalues the end product for the consumer;
28. Instructs its President to forward this resolution to the Council and the Commission.

## EXPLANATORY STATEMENT

### *Challenges and opportunities facing the dairy sector*

In 2003, with the Mid Term Review of the then CAP, the Member States of the EU agreed to put an end to the quota regime from 31 March 2015. The ending of the quota for milk production after thirty years presents both challenges and opportunities for the dairy sector.

Volatility will be a continuing challenge facing the dairy sector. Dairy farmers are particularly vulnerable to income variations due to high capital costs, volatile dairy commodity prices and fluctuating input and energy costs. Furthermore, dairy farmers often occupy a weak position in the overall food supply chain and are particularly exposed to unfair trading practices. The ageing demographic of dairy producers is also a matter of concern and encouraging and supporting generational renewal via new and existing tools is essential for future growth and sustainability for the sector.

Overall the medium to long term prospects for the dairy sector are positive on both the internal and world market. Demand is strong, particularly in emerging economies. The OECD and FAO, in their most recent Agricultural Outlook report, predict that global dairy demand will grow by around 2% per annum up to 2023.

Identifying and securing export markets should be prioritised by the sector and promotion of dairy products on third markets must be targeted and effective. The improvement of knowledge transfer, research, innovation and measures to improve quality and labelling will bring further added value to EU dairy products and increase their competitiveness on the internal and world market.

The opportunities for the sector for growth and development via instruments under the European Strategic Fund for Investment should be fully explored and the sector should be facilitated and assisted in reaching its potential, developing sustainable jobs and boosting economic growth in rural areas across the EU.

In many disadvantaged areas and outermost regions dairying remains the sole generator of farm income and employment and its continuation is essential to avoid land abandonment. While it is too early to fully examine the effects of the Milk Package on the milk sector in disadvantaged regions, it is clear that the measures put forward under the Package must be combined with the options open to Member States under the CAP to support farmers and ensure the continued economic and social contribution of small-scale dairy farms in these regions. The Commission's Report raises the possibility of a more targeted approach to assisting disadvantaged regions, given the heterogeneity of these areas between Member States.

In recent months, a drop in demand from external markets, global price volatility and the Russian embargo have placed increased pressure on the sector and downward pressure on prices. Though the swift action taken by the European Commission to address the impact of

the Russian embargo, particularly in the Baltic Member States, is to be commended, it is clear that the crisis measures and tools the European Union have in place are not designed to respond to the realities of the modern dairy sector.

The existing safety net measures such as public intervention and private storage aid are not suitable to address persistent volatility or a crisis in the milk sector. The Commission's Report noted that there are doubts on the capacity of the EU regulatory framework to deal with episodes of extreme market volatility or with a crisis situation after the expiry of the quota regime, especially with a view to ensuring the balanced development of milk production across the EU and avoiding extreme concentration in the most productive areas. In this regard, it is necessary for the Commission to implement a more responsive and realistic safety net and for the intervention price to be more reflective of production costs. The current price, unchanged since 2008, needs to be revised to take into account increasing production and input costs and should be revised on a regular basis.

### ***Rapporteur's position on the operation of the Milk Package***

The Milk Package, in force since October 2012, offered farmers tools to meet the challenges facing the dairy sector. Strengthened contractual relations and increased bargaining power via Producer Organisations and Interbranch Organisations were introduced. The Rapporteur remains of the view that measures put forward to improve transparency and increased comprehensive data analysis of EU milk production are essential to a sustainable and functioning dairy sector.

The use of formalised written contracts and strengthening of contractual relations offered farmers a strong tool, and reinforced the responsibility of the operators in the dairy chain to take into account market signals, improve price transmission and adapt supply to demand, as well as help to avoid unfair commercial practices. Member States were obliged to formally recognise Producer Organisations (POs), but were given flexibility to determine whether a minimum number of members or a minimum volume of marketable production would constitute a PO.

Implementation of the measures put forward in the Package is uneven across the Member States and take up has been disappointing. The overall strength of the dairy sector and favourable market conditions in the intervening period have been put forward as reasons for the reluctance of producers to organise themselves in POs. Other barriers need to be identified and addressed, such as the lack of awareness of the role of a PO. The Rapporteur has recommended further incentivisation to create and join POs as a tool to address imbalances in the supply chain.

### ***Commission report on the operation of the Milk Package***

Under Article 225(b) of the CMO Regulation, the Commission was required to present a report to Parliament and Council by 30 June 2014 on the development of the market situation in the EU milk sector and the operation of the Milk Package. The Commission's report covered three main areas:

- Market analysis
- The operation and take-up of the Milk Package in Member States
- The position of dairy farmers in disadvantaged regions

The report notes that under the revised CAP a multitude of tools exist to help the dairy sector in exceptional circumstances, for example coupled support and additional safety net provisions and Rural Development Programme schemes, however the report does not rule out the possibility of additional tools to cope with the end of quotas.

The report also acknowledges that a limited number of Member States have applied rules to regulate the supply of PDO/PGI cheeses, upon the request of a PO, Inter-Branch Organisation or a PDO/PGI group.

In terms of the operation of the Milk Package, the report suggests that it has improved relationships throughout the supply chain although it is still too early to see significant effects on the milk sector.

### ***Supporting a competitive and sustainable dairy sector***

Given that the level of implementation of measures under the Milk Package has been disappointing, the Rapporteur encourages stakeholders along the dairy supply chain to avail of the measures under the Milk Package, as well as offering recommendations on new instruments which should be considered by the Commission and industry.

The Rapporteur foresees the Milk Market Observatory (MMO), launched in April 2014, as playing a crucial and enhanced role in the EU dairy sector in the years ahead. The MMO disseminates and analyses market data, allowing stakeholders to make better financial and investment decisions. In the Commission's June 2014 report, it was envisaged that the MMO would 'send early warnings to the Commission services' allowing the Commission to act more rapidly in the initial stages of a crisis.

This report puts forward the position that the Commission should take necessary action to ensure the MMO can fulfil its full potential. The information provided by the MMO should involve updates on market and price trends, and should be more easily accessible and user-friendly than its current format. The MMO should be supported in its operation by Member States providing the relevant information in a timely manner, and also recommends that the Commission explore additional means of ensuring this information is received on time. In December 2014 as many as 9 Member States did not provide the relevant information to the Commission on time.

The importance of accurate and timely information in the post-quota era will be significantly increased, and the MMO should aim to provide more frequent and up-to-date information to all relevant stakeholders. The data that is made available could assist in strengthening contractual relations and could also be used in workable dairy trade derivatives.

The Commission should explore the possibility of a futures market to bring medium-term predictability to pricing structures and increase the sector's competitiveness. Such a market would permit producers and processors alike to hedge against risk by knowing prices in advance, allowing for better investment decisions.

The strengthening of contractual relations, foreseen in the Milk Package, represents a concrete method of ensuring a more equitable distribution along the supply chain. The report asks the Commission and other actors in the EU dairy sector to explore the potential offered by longer term integrated supply chain contracts, forwards contracts, fixed margin contracts, A B contracts and the opportunity to 'lock in' a milk price for a set period of time. There are many examples of the industry itself moving towards these measures and they should be considered further, as hedging instruments, such as fixed-margin contracts could offer certainty, flexibility and responsive options to farmers. Long-term planning and farm management to manage volatility is more important than ever and through contracts the competitiveness and sustainability of the sector for farmers and for supply could be strengthened.