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Eucolait general comments to the Agricultural Market Task Force

With this paper, Eucolait, the European Association of Dairy Trade, wishes to contribute to the work of the Agricultural Markets Task Force (AMTF) as far as the situation in the dairy sector is concerned. This follows our specific comments on market information and transparency as well as on futures markets.

Need to maintain the market orientation of the CAP while dealing with price volatility

Eucolait believes in a healthy and competitive European dairy sector with a leading position on the global market and therefore fully supports the market-orientation of the Common Agricultural Policy (CAP). This market orientation needs to be accompanied by comprehensive, reliable and timely market information to provide operators in the dairy supply chain with the right signals.

As rightfully stated on the AMTF website, increased market orientation has brought opportunities for the dairy sector but also more uncertainty in the form of increased price volatility. It is crucial to be honest about the fact that volatility is here to stay and that the EU, with the chosen policy direction, cannot shield market participants from the effects of that volatility, notwithstanding the use of the safety net consisting mainly of public intervention and private storage. Consequently, the focus of policy should be on supporting the use of market driven tools and on enhancing the competitiveness of the EU dairy sector.

Finally, it has to be stressed that the present down cycle in the dairy market which is now nearing its end, is a result of multiple factors, including the gearing up of production globally in the period of high prices in 2013 and the first half of 2014, the investments made to increase production in light of the quota abolition and the simultaneous slowdown of demand growth resulting notably from the Russian embargo, from China temporarily importing far in excess of its consumption needs and from the reduction of buying power of oil-driven economies. The low milk prices should therefore not be seen as a symptom of structural imbalances in the dairy supply chain.

Contractual relations along the supply chain

The dairy supply chain is much more complex than the commonly presented producer-processor-retail image would suggest. Milk is processed into a multitude of dairy products which can be broadly split into consumer products and ingredients for the food industry. Some dairy products like cheeses and butter are both consumer products and ingredients, whereas dry dairy products (milk powders, whey derivatives and casein(ates)) are used for further processing except in the case of reconstituted milk. Consumer products are sold via retail and the food service sector while dairy ingredients are used in a

huge number of applications (including dairy) such as chocolate, bakery products, processed cheese, pizza, various ready-to-eat foods, sports nutrition and infant formula. In addition, all consumer dairy products, ingredients and the composite products incorporating dairy ingredients are sold both on the EU market and in third countries. The demand developments in all these segments ultimately influence the milk price. However the returns for the 'surplus commodities' butter and SMP have the highest impact on milk prices due the substitutability of milk and the obligation or at least commitment of dairies to collect all milk delivered to them.

Eucolait believes in the freedom of contract and is not in favour of additional regulatory initiatives to manage the relations between the various links in the supply chain. Such interference places additional burden on operators and is damaging to the market dynamics without bringing any value added. While we await the conclusions of the second report on the implementation of the 'milk package' due later this year, it seems that its impact on market developments has been negligible, despite its initial controversy due to the derogation from competition law. In the end, prices are always driven by supply and demand fundamentals which cannot be changed through supply chain regulation unless prices or production volumes are being fixed which should certainly not be the objective. Producer organisations can however have a role in helping its members adjust supply to market requirements and in contributing to the development of tools to manage their price risk.

That said, unfair trading practices (UTPs) should of course be addressed. To this end, Eucolait believes the Supply Chain Initiative to be the appropriate tool at EU level. In addition, the comparison of existing legislation in this area at Member State level is certainly a worthwhile exercise in order to determine whether a higher degree of harmonisation should be envisaged, while keeping in mind this is essentially a Member State competency.

Market driven solutions

There are various private tools for risk management, such as fixed milk price schemes, insurance products, flexible loans, mutual funds as well as futures and other derivatives where the EU can have a supporting role. Fixed milk price schemes can only be developed by dairy processors, be it cooperatives or private dairies, in cooperation with the supplying producers. However public authorities can promote their use by communicating about best practices.

Eucolait particularly supports the development of dairy futures markets in Europe because they can help market participants securing their margins. In addition to managing price risk, futures increase price disclosure, thus enabling better planning by all actors in the dairy supply chain. Futures can also allow processors to offer fixed price contracts to their supplying producers. The Commission can contribute to improving futures markets by further enhancing the accuracy and timeliness of the data on the MMO website (please refer to our separate paper on futures for more details).

The need to preserve the internal market and to further increase exports

The importance of the EU internal market is evident since a vast majority of European milk is consumed in Europe in the form of various dairy products. But also the world market is essential as EU exports account for approximately 13% of its milk production and this share will have to continue growing as increases in milk production are outperforming the moderate consumption growth in EU. Global demand for dairy on the other hand is expected to continue increasing by about 2% per year on average on the back of population growth, an increased demand from a larger middle class, changing eating habits and the development of modern retail practices. We believe the EU dairy sector is well placed to serve this demand.

Traders limit market inefficiencies by matching supply with demand, i.e. by ensuring that all dairy products find a home either within the EU or on the global market. The involvement of traders helps securing value for all participants in the supply chain and reducing price volatility. Hence it is crucial to create new trading opportunities through free trade negotiations to make sure European companies compete at least on a level playing field with other dairy exporters and to avoid any dysfunctioning of the EU market through measures designed to impede the free movement of goods.

While acknowledging the mandate of the AMTF, we would like to stress that from our perspective the key challenges looking forward are to preserve the integrity of internal market and the functioning of the EU as a whole against increasingly nationalist and protectionist tendencies in numerous Member States and to overcome the anti-trade climate which is currently slowing down trade negotiations or blocking them altogether. In this vein, improved communication on how a well-functioning common market and the trade deals negotiated by the EU are in the interest of the whole dairy sector, including producers, is required. This is a joint task for the public authorities and stakeholders.