How the European Commission is tackling dairy surpluses

European File

Annual milk production in the European Community today stands at 100 million tonnes — equivalent in volume to a lake ten kilometres long, two kilometres wide and five metres deep. One farm in three produces milk, and dairy production itself represents about one-fifth of the Nine's total agricultural output in value terms.

In both the History of Man and in the life of man, milk figures prominently. The Bible spoke of the promised land overflowing with milk and honey. No single product, say the dieticians, can equal its extraordinarily rich composition.

Increasingly, milk is being processed: pasteurised milk, sterilised milk, powdered milk, butter, cheese, yoghurt... and consumers find themselves offered an increasingly large assortment of high-quality products. Parallel to this, the economy of the dairy sector has diversified. Of course, the farmer is still the basic element, but the "agri-food" industries, shopkeepers, and exporters have assumed an important role.

When the dairy sector hits the headlines in the European press — as often happens — it is almost always for negative reasons: increases in the milk surplus, rising farm support costs, subsidised sales outside the Common Market. The bad press it receives is not always unjustified. But before examining all the aspects of the "milk problem", we should not forget that it still supports two million European farmers: a large number of small farmers are still earning a living in this sector.

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The butter mountain: how it came about

The production of milk and dairy products has well exceeded consumption. This bluntly, is the root of the milk problem. Whilst production in other agricultural sectors periodically exceeds consumption, the situation is usually only temporary. A smaller harvest the following year usually brings the market back to equilibrium. this is not the case in the milk sector where surpluses are "structural", i.e. permanent, and reach very high levels since about 10%-15% of total production cannot be sold on the normal market.

The surpluses are bought up by public organisations financed by the European Community under its Common Agricultural Policy. Special and quasi-permanent measures — particularly substantial price reduction to encourage consumption and exports — helped bring about a reduction in stocks of butter and milk powder at the end of 1979: the level of these stocks (calculated at the end of December of each year) has changed as follows since 1974:

	1974	1977	1978	1979
Butter (thousand tonnes)	148	190	418	390
Milk powder (thousand tonnes)	374	965	674	225

But the European dairy policy and the financial support involved is expensive (and increasingly so). Funds needed in 1979 were of the order of 4.6 billion European units of account [1] which represents close one-third of the Community budget: In 1978, expenditure in the dairy sector already amounted to 4 billion EUA, compared to 2.9 billion in 1977 and 1.3 billion in 1974. Clearly, the current situation is intolerable and action must be taken.

At the root of the surpluses are three principal factors: the increase in production, the stagnation of consumption and the operation of European price guarantee mechanisms:

☐ Increase in production: the increase in European milk production is not due to a greater number of cows but to a constant increase in the milk yield per cow. On average, the "European" cow currently produces 4 000 kilos of milk per year, compared to 3 400 in 1970, 3 000 in 1960 and 2 400 in 1950. In less than twenty years, cows in the European Community have almost doubled their yield.*

This rise in yield is due to a certain number of factors:

- better selection of cattle through artificial insemination techniques;

- greater effectiveness in countering animal diseases;

[1] 1 EUA = about £ 0.63 or Ir. £ 0.68 (at exchange rates current on 4 February 1980.

- modernisation of farms and throughout almost all of Europe, the replacement of manual labour by mechanisation;

- greater use of green fodder, the production of which has been stepped up through progress in research (new varieties of grass and fertilisers, etc.);

- and, above all, the extensive use of concentrated animal feedstuffs, often imported from America, which enable milk to be produced independently of the quantity of fodder available locally. This technique is perfectly profitable: a kilo of food compound costs less, in general, than a litre of milk whilst it enables at least two litres to be produced.

The traditional dairy farm, in its closed world, is therefore on the way to being replaced by the modern specialised farm handling both rearing and processing. We can perhaps envisage cows disappearing from the countryside and being housed in cattlesheds day and night, all seasons of the year.

Today, more than 90% of the milk produced (compared to 60% twenty years ago) is sent to the dairies which are being rapidly modernised. Processing milk into butter, cheese and yoghurt, etc., has become an industrial process which can no longer be compared to old traditional methods.

☐ Stagnation in consumption: in the European Community, consumption patterns differ greatly from country to country. The Irish are the leading consumers of dairy products, essentially milk and butter, followed by the British who also consume a great deal of milk but very little butter. The greatest cheese consumption, as could perhaps be expected, is found in France (six times greater than in Ireland). Finally the smallest consumers of milk products (excluding cheese) in the Community are the Italians. Butter consumption in the Netherlands is also very low even though a great deal is produced there. Overall, however, the consumption of dairy products in the European Community has been stable for a number of years. Consumption of certain products such as fresh cream and cheese is on the increase whilst consumption of butter is on the decline.

☐ Price guarantee mechanisms: the Community's dairy policy is based on three principles which are also the basic principles of "Green Europe":

- the free movement of goods i.e. the removal of all obstacles — customs duties, quantitative restrictions etc. — which prevent goods from moving from one Common Market country to another;

- Community preference, i.e. the priority accorded to Community products over imported products. A "levy" is imposed on these imports when they enter the Common Market to cover the gap between world prices and prices — generally higher in the Community;

- financial solidarity i.e. sharing the costs of the Common Agricultural Policy amongst all Community countries.

In reality, the following happens: each year the Nine agricultural ministers determine — usually after long and heated discussions — a grid of guaranteed prices covering a large proportion of agricultural produce. These are the prices at which public organisations will buy from producers the goods they cannot sell on the market. This is what is known as intervention. When a sector is in general equilibrium, supply corresponds, roughly, to demand and public organisations are only called upon to intervene for very limited quantities which are stored for a short time before being resold.

This mechanism provides a certain price stability. When supply is less than demand and prices rise in consequence, the public authorities sell off certain quantities to bring down the market rate. Conversely, when supply is greater than demand and when prices consequently fall, the public authorities buy in the surplus products.

But the functioning of these mechanisms is upset when they are applied to the unlimited quantities arising in a sector with a structural surplus, as is the case with milk products. The greatest proportion of the quantities bought by the public authorities cannot be resold at normal prices and stocks of butter and skimmed milk grow and grow. Considerable money is spent both in financing the storage and finding alternative uses for at least part of the stocks.

The necessary reform

European integration has gone furthest away in the agricultural sector. Therefore, any setback in this field could bring into question the whole idea of constructing Europe. To save the Common Agricultural Policy — which provides secure food supplies for some 260 million European consumers and which protects the income of more than 8 million farmers — the Community's dairy policy must be reformed.

There are a number of difficulties involved in achieving this:

- ☐ the divergent interests of Community countries according to the size of their output and degree of modernisation.

- ☐ the social problems relating to hundreds of thousands of farmers who can only survive with guaranteed prices. This economic crisis in Europe makes this aspect of the problem even more crucial. Given the current high level of unemployment in the Community, farmers who have to leave the land have difficulty finding work in other economic sectors. The opportunities for changing to other types of farming activities are also very limited and pose difficult financial problems for small farms. It is not possible simply to abolish the guaranteed price system for dairy products. The large majority of farmers have small farms and the price guarantee constitutes in reality a minimum salary.

- ☐ the complexity of the "Green Europe" mechanisms and the European decision-making process.

To reduce the surpluses without hitting producer incomes too hard, imagination is required to combine a wide range of measures dealing with both the demand and the supply of dairy products.

Expanding consumer demand

Consumption of milk products is currently stagnant and could be stimulated, particularly in cases where price keeps down consumption and where the Community imports substitute products such as margarine. The European Commission is proposing that the Community extend the measures it has already taken to reduce surpluses and encourage consumption of dairy products.

☐ School milk: milk is a perfect drink between meals and meets many physiological requirements, particularly for young people for whom breakfast is often insufficient. Price reductions offered in this area help consumption habits at an early age.

☐ Cut-price butter: subsidised butter (at up to 70% less than normal price) is delivered to charitable institutions, hospitals, the army, and the poorest social groups. During the end of year celebrations — periods of great consumption — all Community consumers can benefit from "Christmas butter" at price 25-30% less than the normal prices. In some Community countries a permanent subsidy is offered to consumers which reduces the price of all butter packaged in small quantities.

☐ Supplies to industry: certain sectors of the food industry (bakers, biscuit manufacturers, ice-cream manufacturers) also receive butter at prices which are reduced to make them more attractive relative to other fats. The European Commission intends to extend its efforts in this field.

☐ Animal feeds: aid is given to farmers who increase the consumption of skimmed milk on the farm for animal fodder. This overcomes the problem of processing the milk into milk powder and further increasing European stocks.

☐ Export aids: sales of milk products outside the Common Market benefit from "restitutions" which cover the difference between the European and the world price. No Community butter can find a buyer outside the Common Market if it is sold at the European price which is significantly higher than the world price. Exports aid can be justified by the following economic calculation: the average consumption of butter in Europe will only rise from 8 to 9 kilos per person per year, if the prices fall below 0.6 EUA for each kilo sold, which implies that the taxpayer will have to support a subsidy of 5.4 EUA per consumer to reduce the butter mountain one kilo. Since the export of 10 000 tonnes involves a cost of 20 million EUA, this is effectively only 2 EUA per kilo. These subsidies are unpopular, however, and increasing European exports may be difficult given the surpluses existing in other regions of the world. [1]

[1] Following the events in Afghanistan, subsidised sales of butter and butteroil to East bloc countries have been reduced or stopped.

- Food aid to developing countries: since 1970, the European Community has been operating an extensive programme supplying milk products to the Third World. This food aid is composed of skimmed-milk powder and butteroil, butyric fat which is easily preserved and well suited to the needs of these countries. The extent of this free aid today amounts to some 150 000 tonnes of milk powder and for butteroil, 55 000 tonnes of "butter equivalent", or close to 30% of normal exports. Food aid, however, is limited by the lack of transport and distribution infrastructure in the receiving countries: apart from aid following natural disasters, a massive increase in this area would also risk discouraging production by Third World farmers.

- Limiting imports into Europe of vegetable protein and fats: in the context of Community enlargement and the entry of Greece, Spain, and Portugal — small consumers of milk products — the Commission wishes to re-examine this problem. It also wishes to open negotiations with countries supplying soya to obtain self restraint over their exports.

Reducing the supply of milk products

The rapid growth of milk production is the root cause of the surpluses. The European Commission is not in favour of direct and compulsory measures such as quotas implying maximum production quantities per farm, dairy, region or even country. Such a system would be difficult to reconcile with the principles of free enterprise and free trade between the Nine. There are other measures, however, which are likely to hold back production:

- a prudent pricing policy: each year as we have seen, the Council of Ministers of the Nine sets a new grid of guaranteed prices following proposals from the European Commission. Of all agricultural products, the price policy has its most direct repercussions on dairy products. Supply is permanently higher than demand and it is the guaranteed intervention price which determines the level of payments to producers. A prudent price policy is therefore a fundamental factor in bringing about equilibrium in this sector. As a consequence, in 1979, the Council of Ministers — following proposals from the Commission — voted against any European price increases in the milk sector. A similar policy is likely to be continued in 1980.

- an increase in the coresponsibility levy: since September 1977, the milk producer has been paying a kind of tax calculated as a percentage of the price of the milk. A part of the income from sales of dairy products is taken from the producers and put into a fund specially aimed at extending the market for its products. The European Commission, supported by the European Parliament, has proposed raising this coresponsibility levy from 0.5% to 1.5% of the milk guide price. For social reasons, exceptions would be allowed for to help smaller farmers working in regions faced with difficult conditions. The Commission has also suggested that an additional levy be introduced. This levy would affect the dairies processing milk quantities in 1980 which exceed 99% of the volume brought in 1979. The dairies, would be able to pass on this additional levy to the producers. In consequence, the dairies, like the producers, would be encouraged not to increase the quantity of milk they sell.

- non-delivery and reconversion premiums: the measures already existing in this area for a number of years should be continued. These permit a certain number of cows to be taken out of milk production. A reconversion premium could be offered to farmers who agreed to abandon the most milk-productive species and turn towards rearing cattle for meat. The non-delivery premium varies depending on the quantity of milk which is not sold to the dairies. It is accorded to farmers who agree to slaughter their milking cows or to use part of the milk produced on their own farm for animal feeds, in particular.

- the suspension of investment aid: efforts to end or at least reduce the increase in production should not be thwarted by other measures which directly or indirectly aim to stimulate the same production. The European Commission takes the view that investment aid by public authorities in the milk sector should be provisionally suspended at least where these investments do not serve to create or improve new products, promote new markets, save energy or protect the environment. In contrast the Community should increase — in less sensitive sectors than milk — its structural development aid for the least prosperous agricultural regions.

△

The Community's milk policy enables numerous farmers to live — often modestly — from the efforts of a job for which alternative work is becoming increasingly rare. The multiplication of modern enterprises in this sector which are veritable "milk factories" requires certain elements of this policy to be modified, if we want to continue to derive social and regional benefits from it. The growing cost of supporting the milk market may end up by compromising even the principle of the common policy: the cost will become unbearable both for the taxpayer and for the budget of the Community whose resources are limited and which finds itself prevented from taking the action needed in other areas and sectors in difficulty in the European economy ◘

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