

COMMISSION OF THE EUROPEAN COMMUNITIES

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REPORT FROM THE COMMISSION TO THE COUNCIL ON THE DAIRY SITUATION IN THE COMMUNITY, THE WORLD MARKET AND IN NEW ZEALAND IN RELATION TO THE IMPORT OF NEW ZEALAND BUTTER INTO THE UNITED KINGDOM

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I. Introduction

1. Article 5(2) of Protocol 18 of the Act of Accession states that:

"Appropriate measures to ensure the maintenance, after 31 December 1977, of exceptional arrangements in respect of imports of butter from New Zealand, including the details of such arrangements, shall be determined by the Council, acting unanimously on a proposal from the Commission, in the light of that review."⁽¹⁾

2. On this basis the Council adopted Regulation (EEC^o No 1655/76 of 29 June 1976 extending the transitional arrangement for the import of New Zealand butter into the United Kingdom at the following levels⁽²⁾:

1978:	125 000 tonnes,
1979:	120 000 tonnes,
1980:	115 000 tonnes.

Furthermore, the same regulation lays down the conditions under which these quantities can be imported.

3. In adopting the above-mentioned regulation the Council entered the following statement in its Minutes (Doc. R/1574 f/76 (AGRI 461):

"1. The Council decides not to include Article 9 of the draft regulation which referred to the possibility of appropriate measures to be adopted concerning the imports of New Zealand butter after 1980 as it considers that, notwithstanding the

(1) OJ No L 73, 27.3.1972, p. 174

(2) OJ No L 185, 9.7.1976, p. 1.

periods specified in this regulation, further application of Article 5(2) of Protocol 18 is not excluded.

2. The Council draws attention to the desires expressed by the Heads of Government in the Declaration of the European Council in Dublin on 10 March 1975 to the effect "that in the same spirit which the Community approaches the application of Protocol 18, an even-closer co-operation be developed between the institutions of the Community and the New Zealand authorities with the objective of promoting in their mutual interest an orderly operation of world markets."

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II. The Community and world markets for butter

1. The Commission submitted to the Council on 27 September 1978 a full report on the milk situation within the Community (COM(78) 430 final). That report contains a detailed analysis of the trends in production and consumption and draws attention to the imbalance on the Community market for milk products and its consequences. The Commission outlined a series of measures which in its view were necessary in order to face up to this situation and has subsequently made specific proposals (COM(79) 10 final). The arrangements for New Zealand must therefore be seen against the background of continuing difficulties requiring action in the Community market.
2. Butter production in the Community reached about 1.96 million tonnes in 1978, an increase of 156,000 tonnes compared with the 1977 level. This, together with an opening stock of 195,000 tonnes and imports of 125,000 tonnes of New Zealand butter, resulted in a total availability of butter during 1978 of 2.2 million tonnes. Total off-take in the Community is estimated at about 1.63 million tonnes or a decrease of about 80,000 tonnes from 1977. An important series of special measures have been set in train in order to give Community consumers the benefits of surpluses and to stimulate the use of butter. These measures include

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sales of butter at reduced prices for bakeries and for the production of ice cream; cheaper butter for armies, hospitals and social welfare; special programmes such as "Christmas butter sales"; and general butter subsidies now being applied in Ireland, Denmark, Luxembourg and the United Kingdom. The Community is now strengthening these actions. The difficulties of disposing of surplus butter have increased. Such measures cannot be developed much further without risk of reduced economic and financial effectiveness.

3. The Commission remains firmly committed to an active export policy for milk products and to a reasonable share of skimmed milk powder and butteroil in the food aid programme, subject to the needs of the recipients.

At present export refunds for butter represent about 70% of its value. Compared with the special measures for disposal on the Community market the budgetary cost of exports of dairy products is generally lower. Sales possibilities on the world market, however, remain limited, particularly for butter.

4. The Commission has already stated in COM(78) 430 that "it is false to believe that stopping imports would solve the milk problem in the long term and relieve the Community of its responsibility to restore balance." Nonetheless, the importance of the action necessary on the internal market should certainly be reflected in the approach to obligations on imports of butter from New Zealand from the period after 1980.

5. Following a general depression of the international trade in dairy products during 1975, the situation on world markets improved during 1976 and notably during 1977. In 1977 total world trade increased by 52% for skimmed milk powder, 23% for butter, 47% for whole milk powder, 16% for condensed milk and 9% for cheese compared with 1976.

The Community's commercial exports of dairy products during 1978 showed a general improvement compared to 1977, which in itself was a good year. Exports of all products except those of condensed milk were higher. Exports of butter (including butteroil equivalent) were 2.7% higher; skimmed milk powder + 0.4%; cheese + 5.2%; and whole milk powder + 1.5%. Moreover, first results in 1979 again show an increase in the Community's exports of many dairy products.

6. The general price level for dairy products on the world market improved gradually during the past two years, mainly reflecting increased costs and the depreciation of the U.S. dollar. Returns from the world market

e, however, relatively low. Actual offer prices range from 1,100 to 1,200 US\$ (85-90 ECU/100 kg) fob for butter and from 1,275-1,350 US\$ (97-103 ECU/100 kg) fob for AMF compared with the EEC intervention price level for butter of 284.97 ECU/100 kg.

Looking to the immediate future there are more factors pointing towards increases in global milk production than elements tending to limit production. Given favourable economic conditions (economic growth/ industrialization) there is still scope for increased consumption at commercial level both in developed and developing countries. The influence on world trade is, however, difficult to forecast as the degree of self-sufficiency is influenced by increases in production and because new bilateral and international agreements make it difficult to forecast trade patterns. Total world milk production in 1978 increased by approximately 2%, compared to an increase of 3% in 1977. Hence, a 5% increase in the Community in 1978 was countered by slight reductions in North America and U.S.S.R. and more pronounced reductions in Oceania. However, important increases have also taken place in certain European countries outside the EEC (Switzerland, Sweden, Spain, Czechoslovakia, East Germany and Hungary) and in Japan.

Notwithstanding the slower growth in 1978, total world milk output continues to substantially exceed commercial demand. For this reason most countries with interests in milk production or in the international milk market have started to discuss or to introduce measures aiming at a better balance between output and demand.

7. Medium-term forecasts up to 1982 show an expected increase in milk production in OECD countries by 1% per year corresponding to 2 million tonnes milk equivalent. This reflects a slow down in the expected increase in milk output in the Community. It is possible that the supply of the world market from OECD countries which, with Eastern European countries, account for the dominant share of the trade in dairy products, will increase each year by the equivalent of about 80,000 tonnes of butter and 160,000 tonnes of skimmed milk powder. The Commission estimates that for milk products as a whole the likely production increase will outpace actual changes in consumption. The possibility of a significant supplementary disposal by means of food aid does not seem practicable in

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the short-term, because the recipient countries are hampered by inadequate distribution and structural systems.

8. It is estimated that the actual world commercial trade in butter/butteroil (excluding food aid) averages around 500,000 tonnes (1975-77) per year. If the import of New Zealand butter into the United Kingdom is deducted, about 375,000 tonnes remains. This is small in relation to the total world production of about 6 million tonnes. Export figures are:-

(000 tonnes)

Exports of butter (including butteroil equivalent but excluding EEC food aid)

	<u>EEC</u>	<u>New Zealand</u>
1975	32	65
1976	73	104
1977	219	63
1978	213	56

III. Economic situation in New Zealand dairy sector

1. The agriculture sector has always been the most important part of the New Zealand economy accounting for the major part of New Zealand foreign exchange. New Zealand has managed to reduce the share of the agricultural sector in its export earnings from 83.5% in 1970 to 73.9% in 1977, while the share of the non-agriculture sector increased from 5.6% to 14.8% in 1977. It is clear, however, that agriculture will remain for a long time the main item for export from New Zealand and that diversification to industrial exports will remain slight, because of the scale of their economy and geographic situation.

New Zealand's serious economic difficulties are illustrated by the fact that the recent recession has involved a 14% fall in real income per head.

2. The New Zealand dairy industry earns 17% of the country's total foreign exchange. Dairy cow numbers have declined slightly in recent years but this has been offset by increases in production per cow. Total milk production in recent years has been -

	<u>1,000 tonnes</u>
1973 - 74	5,688
1974 - 75	6,096
1975 - 76	6,269
1976 - 77	6,648
1977 - 78	6,080
1978 - 79	6,118

There will probably be around 5.5 million tonnes of milk or between 250 000 and 260,000 tonnes of milk fat available for processing annually in the near future. Around 80% of the milk fat is processed into butter and anhydrous milk fat (AMF). Cheese production was held down in recent seasons as a result of limited opportunities in overseas markets. There has been a substantial increase, however, in the production of other whole milk products, particularly in whole milk powder.

3. Although total butter consumption in New Zealand has declined, it still amounts to 46,000 tonnes annually or 14.1 kg per capita. Little change is expected in this pattern in the near future. As a consequence, New Zealand will be seeking export markets in the future for the equivalent of around 200,000 tonnes of butter.
4. The bulk of the exports of butter still go to the United Kingdom. Efforts to diversify its trade in butter have been made by New Zealand. In Japan, in particular, strong pressures have been applied to obtain stable access. These are continuing but at this moment there is no tangible evidence of a new stable outlet for New Zealand dairy products in Japan.
5. Exports of the major New Zealand products during the last 3 years are given below:-

Table 1: New Zealand's exports of dairy products
(tonnes)

	<u>1976</u>	<u>1977</u>	<u>1978</u>
1. Butter: EEC (UK)	111,935	138,373	126,501
Other	<u>59,908</u>	<u>27,177</u>	<u>27,377</u>
Total	171,843	165,550	153,878
2. AMF + Ghee	36,388	29,670	28,883
3. Cheese: EEC (UK)	32,273	12,772	-
Other	<u>47,158</u>	<u>60,878</u>	<u>58,592</u>
Total	79,431	73,650	58,592
4. Skimmed milk powder	127,391	167,178	130,717
5. Whole milk powder	34,869	65,785	62,160
6. Casein EEC	7,617	12,559	9,019
Other	<u>41,001</u>	<u>60,889</u>	<u>54,466</u>
Total	48,618	73,488	63,485

6. It should be noted that cheese exports increased to Japan and the United States. Export diversification into whole milk powder and casein has been very successful. For butter, however, the Community remains substantially the most important market for New Zealand.

IV. The Multilateral Trade Negotiations

The Dublin declaration of the European Council of March 1975 notes that an even closer co-operation be developed between the Institutions of the Community and the New Zealand authorities with the objective of promoting in their mutual interest an orderly operation of world markets and that such co-operation should provide a basis from which to achieve, in a wider framework, the conclusion of an effective world agreement. The Commission considers that this co-operation was shown in the dairy sub-group of the Tokyo Round of the Multilateral Trade Negotiations and contributed substantially to the achievement of an international agreement of dairy products. This agreement should lead to improved stability in the international market for butteroil, skimmed milk powder, whole milk powder and cheese.

V. Problems in the current arrangement for New Zealand butter and possible adaptation

1. Under the present arrangement for the import of New Zealand butter into the United Kingdom until the end of 1980, New Zealand has to respect a specific price c.i.f. United Kingdom. Monetary compensatory amounts are paid. A special levy is fixed to bring the price of New Zealand butter in line with the market price for butter of Community origin sold on the United Kingdom market.
2. The implementation of the special arrangement for the import of New Zealand butter has given rise to difficulties. It has not been easy to determine on a continuing basis the special levy to

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bring the selling price for New Zealand butter to the appropriate level in relation to butter of Community origin on the United Kingdom market. Since the bulk of New Zealand butter is normally imported between September and February and at certain periods of the year there can be substantial stocks already imported and available for sale over a relatively long period, it is necessary when fixing a new levy to foresee the future evolution of butter prices in the United Kingdom. A new special levy only has an effect on the price for New Zealand butter after existing, already imported stocks have been sold.

Changes in intervention price levels in the United Kingdom resulting from the Act of Accession, changes in the value of the green pound, changes in monetary compensatory amounts and the introduction or withdrawal of consumer subsidies affected the development of butter prices in such a way that reliable forecasts of the prices development have not been easy to make. The Commission has, therefore, concluded that, if any special arrangement for the import of New Zealand butter is continued after 1980, the present system should be modified so that these problems can be avoided.

3. The following modifications in the special arrangement would be possible. Instead of the fixation of a) a specific c.i.f. price to be respected at import by New Zealand, b) a special levy which has to be adapted to the market development and c) the application of monetary compensatory amounts to the New Zealand butter imports, the new system could merely consist of the establishment of
 - an annual quota and
 - a special levy which would, in principle, be fixed.
4. Such a system would avoid the difficult management of the special levy and would in the view of the Commission remove the problems which variations in the special levy have sometimes caused for the Community's own butter producers. The New Zealand Dairy Board, being the sole exporter
 - will recognize that it is in its own interest not only to use the quota but also to maximize its financial return from the market. As the special levy would not be variable, the Board would be able to arrange its shipments, storage in bonded or debonded stores and sales programme in the light of the development of the

market rather than of the special levy.

5. A system based on quota and a fixed levy can only be acceptable for both the Community and New Zealand if at least two conditions are fulfilled - first, that the Community market should not be disturbed and, secondly, that New Zealand receives a satisfactory return in terms of export earnings. The special levy, therefore, should represent the difference between a predetermined and satisfactory "take home price" on the one hand and an acceptable selling price for New Zealand butter on the other.

Under the proposed new system monetary compensatory amounts would no longer apply. It would be necessary to provide that, in the case of an important adjustment in the value of currencies or other major economic changes, the amount of the fixed levy could be reviewed.

VI. Future arrangements

1. The Commission considers that the factors to be taken into account in the decision on imports of butter from New Zealand after 1980 are:-
 - 1) the importance of the United Kingdom market as an outlet for the Community's own producers of butter
 - 2) the high level of production within the Community and the necessity to take measures to restrain increases in milk production, including restraints on Community producer's prices
 - 3) the maintenance of butter consumption through reasonable prices to consumers
 - 4) the traditional links between New Zealand and the EEC
 - 5) the desire for closer co-operation between the institutions of the the Community and the New Zealand authorities with the objective of promoting the orderly operation of world markets in their mutual interest and the fact that such import arrangements will obviously be of mutual political and economic interest to both parties. In regard to the latter point it should be borne in mind that not only New Zealand is dependent on the Community market but also that the New Zealand market is important to the Community
 - 6) the need to avoid drastic effects on the New Zealand economy, taking account of the long-standing position of New Zealand as a butter exporter

- 7) the need to assure a certain stability in the Community butter market (and, in particular, the United Kingdom market) to the benefit of all suppliers.
2. Taking account of these factors and of the particular short-term difficulties in the United Kingdom butter market, the Commission will recommend to the Council that decisions in the autumn, on the basis of Commission proposals, should deal at the same time with ways of improving the U.K. butter market situation, mainly in the interests of Community producers in the remainder of 1979 and 1980, as well as with future arrangements after 1980. In order to change the quantity in 1979 and 1980 it will be necessary to have the agreement of New Zealand and the Commission has accordingly begun consultation with them.
3. The elements which should be considered in this approach would be as follows. First, in view of the present overload on Community butter markets, New Zealand would be asked to make some reduction in the volume of sendings to the United Kingdom market in 1979 and 1980 below the entitlement. Secondly, it should be the objective to establish the New Zealand take-home price, now substantially below the return to Community producers and subject to difficult arrangements for review, at a somewhat higher level and to maintain it in a more realistic and continuing relationship to the Community intervention price. Thirdly, consideration should now be given to future import arrangements for New Zealand butter on a more lasting basis. Such arrangements should be made for the Community as a whole and not only for the United Kingdom. In the light of the effort which the Commission considers that the Community's own producers need to make in order to restore a better balance in the Community's milk product market, it is essential that there should be some element of quantity reduction and degressivity upon the establishment of a longer-term arrangement for access for New Zealand butter to the Community market. Fourthly, in the interests of a stable market situation, a regular pattern for debonding New Zealand butter into the Community market should also be considered. Fifthly it is clear that an important element in the recent pressures on the United Kingdom butter market has been that Community producers found themselves competing for a share of a decreasing market. It would, therefore, be desirable in a new arrangement for New Zealand to make provision for review if for reasons not foreseen when the arrangement is settled the volume of butter consumption should decline substantially. Finally, the Commission is of the opinion that recent events have strengthened the case for early introduction of the improvements in the operation of the system referred to in section V above.

4. The Commission is preparing proposals on these lines and considers that on this basis it will be possible to improve the opportunities for the Community's own butter producers in the United Kingdom market, in terms both of quantity and market stability, while continuing to provide a smaller but nonetheless important outlet for New Zealand butter in the Community.

TABLE INEW ZEALAND BUTTER EXPORTS

(tonnes)

Region	1976	1977	1978
EEC	112 113	138 675	126 848
Eastern Europe	9 100	3 503	4 000
Other Western Europe	9 212	2 046	626
North America	171	204	323
Japan	9 778	38	263
West Asia (Middle East)	10 467	6 120	6 179
South East & East Asia	2 312	3 434	7 749
African Continent	9 290	618	924
Caribbean & Central America	4 402	4 550	2 049
South America	1 729	3 027	1 195
Oceania	3 267	3 711	3 722
TOTAL	171 829	165 550	151 878
NZ Exports Outside EEC	59 716	26 875	27 030

Source : NZ Department of Statistics

TABLE II

NEW ZEALAND'S EXPORTS OF ANHYDROUS MILK FAT (AMF)

(tonnes)

Region	1976	1977	1978
EEC	-	-	22
Eastern Europe	-	-	-
Other Western Europe	-	-	-
North America	535	536	536
Japan	945	466	252
West Asia (Middle East)	683	1 150	895
South East and East Asia	12 577	15 707	8 411
African Continent	3 294	1 720	1 667
Caribbean & Central America	8 374	4 329	} 9 080
South America	9 201	4 702	
Oceania	770	1 059	2 812
TOTAL	36 379	29 671	23 675

Source : NZ Department of Statistics

