



**COUNCIL OF
THE EUROPEAN UNION**

Brussels, 15 February 2010

6063/10

AGRI 34

NOTE

from: Presidency
to: Council

Subject: Future of the CAP: Market management measures post 2013
- Presidency paper and questionnaire

Delegations will find attached (in Annex) the paper and questionnaire drawn up by the Presidency with a view to structure the exchange of views at the Council (Agriculture and Fisheries) meeting on 22 February 2010.

1. Introduction

The CAP is the EU's instrument of governance for achieving, in the sphere of agriculture, the objectives provided for in the Treaty, and for addressing the various challenges and preoccupations of European society.

Fifty years after it was set up, the general objectives of the CAP remain valid under the Lisbon Treaty (increasing agricultural productivity, ensuring a fair standard of living for producers, stabilising markets, guaranteeing the availability of supplies and ensuring supplies at reasonable prices). However, the means of achieving these objectives has evolved over time, adapting to new demands from society as regards sustainability, competitiveness, market orientation, conservation of the environment, rural areas and biodiversity, as well as contributing to combating climate change.

The CAP responds to a single concept, even though it is implemented by means of different interrelated instruments, which can be analysed separately provided sight is not lost of the unity of objectives and global strategy.

The above applies to the configuration of the CAP model as from 2014 - what has become known as *Horizon 2020*. In 2008, under the French Presidency, the Council initiated the debate on the future of the CAP with an overall reflection on the challenges that would be faced by the CAP in the future. In 2009, at the initiative of the Czech and Swedish Presidencies, the Council specifically examined the outlook and alternatives as regards direct payments to farmers and rural development policy.

This document aims to complete the analysis of the major issues facing the CAP in the future through a general discussion of the market and crisis management instruments, as a prior step to the overall examination that will take place at the informal Council meeting.

2. World agricultural commodity markets - scenario

World food demand is increasing. According to FAO estimates, the production of food will have to increase by at least 70 % in order to feed an estimated world population of 9 000 million in 2050.

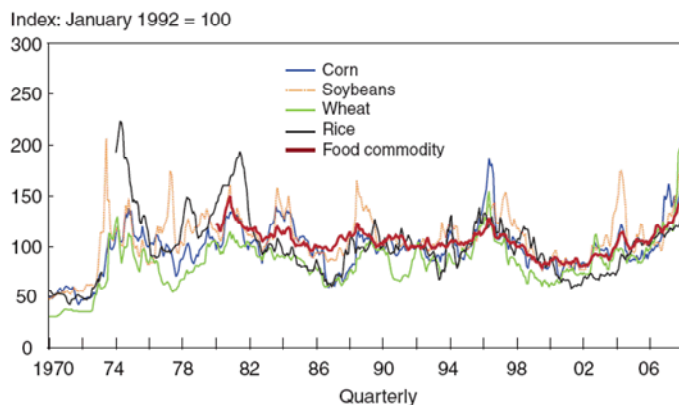
This rise in global demand for food, combined with the time lag in the response from production as a result of the biological processes and the effects of climate change, will generate increased instability on international markets and situations of uncertainty such as those experienced in 2007 and 2008.

2006 witnessed an international rise in the prices of raw material in general, and of agro-food products in particular, which was accentuated in 2007 and the first half of 2008. This situation had a particular impact on less advanced economies, which are highly dependent on imports of basic products. In general, it indicates the start of a new phase characterised by price volatility.

BOX 1 TREND OF MAIN AGRICULTURAL COMMODITY PRICES FROM 1970 TO 2008.

The situation of generalised high prices of basic agricultural products for human or animal consumption experienced in 2006-2007 is not new. There have been similar phenomena over the last 40 years, generally associated with energy crises (such as in the 70s), which push the prices of agricultural commodities (mainly cereals and oilseeds) to record levels.

Food commodity price spikes since 1970



Source: International Monetary Fund: International Financial Statistics.

The economic crisis has also had repercussions for the agricultural sector at world level. Although the impact of the crisis varies from country to country, it is clear that there has been a slowdown in the growth of demand as a result of the fall in purchasing power; which has had a knock-on effect on the commodity markets and on demand for high added-value processed products.

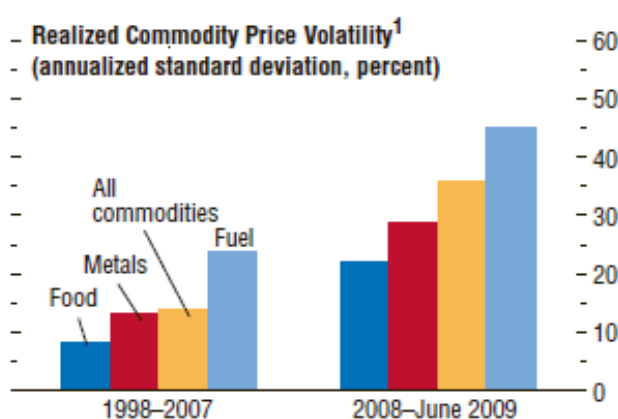
Crisis situations and the major impact of high prices throughout the food chain have restored agriculture's role as a strategic sector at world level. The essential function of supplying safe food, produced in a sustainable manner, is again one of the important challenges facing Europe in the future. This has led to a re-opening of debates that seemed to have been resolved such as the need to guarantee food supplies at world, regional and national levels.

At the same time, it is to be expected that the increase in demand will lead to more volatility in the markets. Once agreement has been reached in the Doha Development Round of the World Trade Organisation (WTO), tariffs will be subject to cuts in order to meet the market opening commitments obtained by Member States. Export refunds will also disappear and other mechanisms for supporting exports will be restricted. All of these factors will result in world markets operating in a freer and more interconnected way.

BOX 2 VOLATILITY OF FOOD PRICES

The constant variations in food prices in the 2005-2008 period were linked to a significant rise in price volatility. According to the International Monetary Fund (IMF), the food price index rose from 110 in 2006 to 127 in 2007 and then to 157 in 2008, before falling back to 134 in 2009 (2005=100). According to IMF data, volatility measured by the annualized standard deviation of monthly price changes increased from about 8% for the decade through 2007 to more than 22% since 2008.

An Overview of Food Price Volatility



¹ Annualized standard deviation of monthly percent changes in the spot price included in the IMF Commodity Index

Source: "World Economic Outlook: Sustaining the Recovery". Series of economic and financial studies, IMF. October 2009

It follows from the above that, in the future, price and supply crises are likely to be more frequent and more severe. This will have a definite negative impact on the incomes of producers, on the economy as a whole and, of course, on food availability, particularly for the poorest population groups.

It will therefore be necessary to develop regional agricultural policies that promote and reinforce a minimum food production in order to ensure a certain level of food supply at global, regional and national levels (as reflected in the Declaration of the FAO World Summit on Food Security held in November 2009). This objective is especially important in the agricultural policies applied in developing countries and the least developed countries.

The above points to the need for strategy and governance in agricultural policies at all levels. The economic crisis has reinforced the strategic nature of agriculture, over and above its economic value, as an essential component of food security and population stability.

3. The EU's internal market for agricultural products

The situation on the international markets is reflected in the internal Community market, currently characterised by a certain level of protection at its borders. It should, however, be borne in mind that the EU market has a number of special features, linked to the high purchasing power of its consumers and the high requirements in terms of quality, safety and health, and hygiene rules and regulations, including animal welfare, to which European products are subject.

The current composition of the European Union has modified the Community market, with an increase in production and consumption.

Moreover, the continued process of CAP reform has resulted in agricultural producers becoming more market-oriented. The measures to support agriculture provided for in the CAP have been gradually adapted, with the market support mechanisms for agricultural products being transformed into income support measures for producers. This change in emphasis has facilitated an improved balance between the demand for products and market supply.

The existence of market management mechanisms has a double effect: the mere fact of their existence means that they act as market stabilisation tools in the event of supply variations; and they also serve to mitigate the negative effects of market imbalances (sectoral crises).

The regulatory effect of cereals intervention, a sector with an enormous impact on the other agricultural markets, is an example of the first of these functions.

As examples of the second, it is worth recalling the major loss of confidence by consumers as a result of the emergence of BSE ("mad cow disease") at the end of 2000, or the appearance, outside EU borders, of the highly pathogenic avian influenza in 2006. These episodes resulted in drastic falls in the consumption of beef and poultry, with a sharp decline in market prices and large production surpluses.

The period beginning in 2013 is shaping up as a challenge for European agricultural markets. New trading conditions, new financial perspectives, the disappearance at Community level of export refunds - which will require all Community products to position themselves on the world market under competitive conditions - and greater market volatility, amongst other factors, make for a more uncertain backdrop against which the CAP will have to continue to meet its objectives.

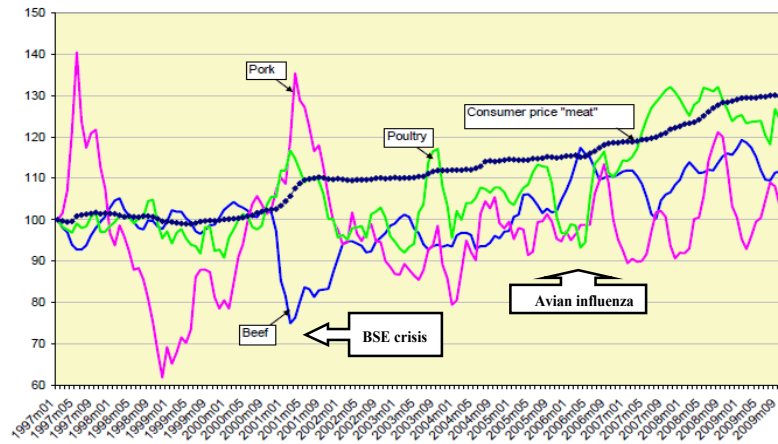
The EU must have an agricultural model with the tools necessary to stabilise markets and deal with price volatility, a model in which the economic activity of agriculture provides farmers with fair incomes that reflect their contribution to society and in which farming is the mainstay of life in rural areas.

The agro-food and distribution industry will shape the market for consumers, who will have access to competitive, safe and high-quality products, prepared using methods that respect the environment. Accordingly, in the run-up to 2020, it will be necessary to focus more on the value chain of agricultural supplies, on interbranch organisations, and on compatibility between the agricultural sector and competition policy.

A Community agricultural market of this type would undoubtedly provide added value for the Community as a whole.

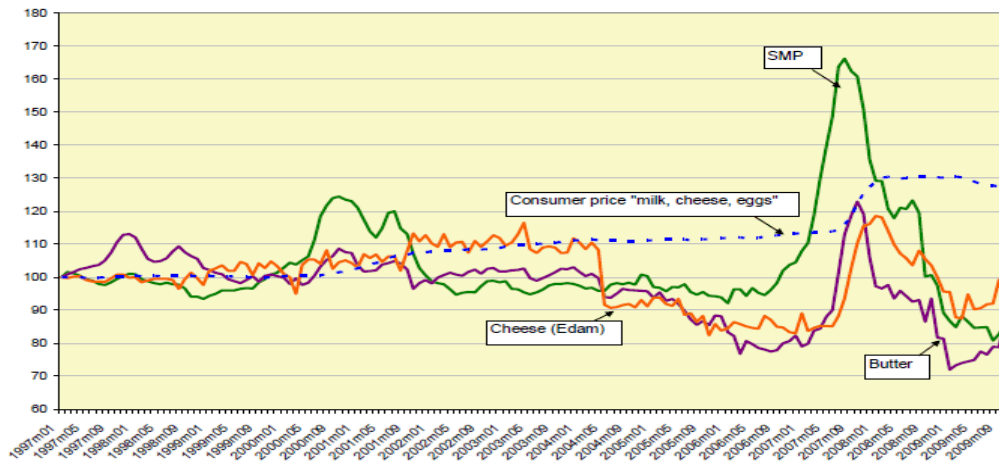
BOX 3 PRICE TRENDS OF AGRICULTURAL PRODUCTS (MEAT, MILK AND DAIRY PRODUCTS, CEREALS AND BREAD) IN THE EU.

TREND OF MEAT PRICES IN THE EU



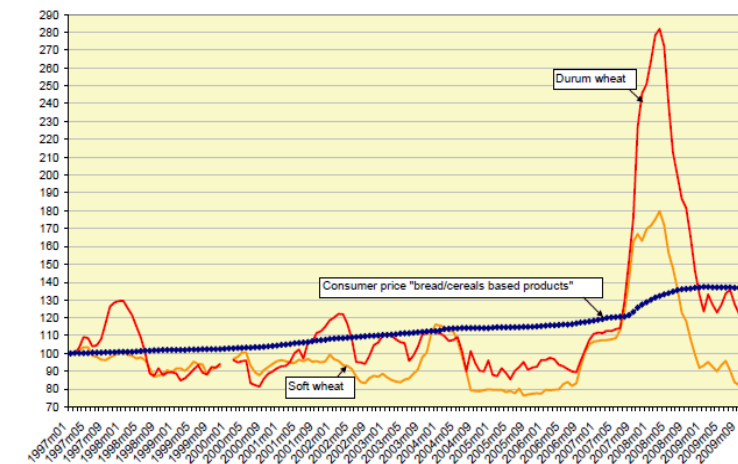
Source: AgriView, Eurostat.

TREND OF MILK AND DAIRY PRODUCT PRICES IN THE EU



Source: AgriView, Eurostat.

PRICE TRENDS OF CEREALS / BREAD AND CEREAL-BASED PRODUCTS IN THE EU



Source: AgriView, Eurostat.

4. Current market and crisis management instruments

The process of CAP reform and the introduction and consolidation of direct aid for farmers has led to a simplification of the intervention mechanisms of the various sectoral common market organisations (CMOs), culminating in a single CMO (Regulation (EC) No 1234/2007) in which the most recent reforms have been incorporated. In addition to the simplification and standardisation of the instruments for managing the different CMOs, a genuine safety net has been put in place to provide the necessary protection in increasingly open markets.

The market-management instruments of the single CMO are shown in the following table, followed by a number of comments.

<p>BOX 4 MARKET MANAGEMENT IN THE SINGLE CMO</p> <p>Internal Market</p> <p>Intervention measures</p> <ul style="list-style-type: none">Public intervention and private storageSpecial intervention measuresProduction limitation systemsAid schemes (specific). <p>Provisions concerning marketing and production.</p> <ul style="list-style-type: none">Marketing standards and production conditionsProducer organisations (OP), Operator and interbranch organisations. <p>Trade with third countries</p> <ul style="list-style-type: none">Imports.Exports. <p>Competition rules</p> <ul style="list-style-type: none">Rules applying to undertakings (agriculture).State aid rules

Special intervention measures are exceptional actions to support specific markets in response to the appearance of diseases in animals and consequent limitations on free movement. Moreover, measures of this kind may be adopted only in certain sectors in cases of loss of consumer confidence owing to the existence of public health or animal health risks.

At present there are systems for limiting production such as production quotas for milk, potato starch and sugar, as well as limits on the production of wine. Some of these limits will disappear over the period of implementation of the future reform of the CAP.

In addition to market management instruments at Community level, in certain sectors there are regulatory instruments where the Member States or the producers themselves, through their organisations, decide on implementation. This is the case of fruit and vegetables or wine, for which there are no common intervention and market management mechanisms, but which do have a specific system of aid. Their regulation is based on product withdrawal or non-harvesting mechanisms.

The appropriateness and effectiveness of some of these mechanisms for other products has yet to be evaluated, although it can already be said that they probably require an improvement in existing Community legislation, particularly with regard to compatibility with competition rules, which envisage special treatment for agricultural products as provided for in the Treaty. This is reflected in the single CMO.

With regard to trade, in the light of the possibility of an agreement in the WTO's Doha Development Round, it is likely that export refunds will disappear and that there will be greater discipline as regards export credits or international food aid, to the extent that they have an impact on markets.

With respect to market access, the reduction envisaged in the Doha Round for Community tariffs on agricultural products will be an average of at least 54%. A complex mechanism will enable smaller reductions to be applied to certain sensitive products, but with an increase in market access. In any event, bilateral and regional agreements will continue to be negotiated.

It should be noted that the market regulation instruments that remain in operation after the "health check" have been effective in mitigating the negative effects of various sectoral crises. In the pigmeat sector, for example, the opening of private storage and export refunds for a few months facilitated a price recovery at the end of 2007.

Another very recent example is the authorisation of the private storage of olive oil in 2009, which contributed to a recovery in prices and subsequent market stabilisation.

The world food crisis in 2007 was a good example of how these tools perform their market stabilisation function. In the face of the sudden rise in world commodity prices and the restrictive export policies of third countries, it became necessary to make an adjustment between supply and demand in the European Union, which was possible owing to the Community public storage of 14 million tonnes of cereals. These entered the Community market in 2007 until cereal intervention stocks were reduced to zero.

In short, it seems that the current management instruments have contributed to the management of agricultural markets by acting as a safety net, avoiding serious consequences for producers, manufacturers, consumers and the food chain as a whole. The recent crisis in the dairy sector is an example, although the seriousness of the situation made it necessary to adopt exceptional measures against the background of economic crisis and budgetary difficulties.

5. Analysis of the market and crisis management instruments in the future CAP

In the light of the foregoing, the basic issue revolves around which market management mechanisms should form part of the CAP model as from 2014. In this respect, it would appear necessary to find a balance between market orientation, as a basic principle of European agriculture, and a full guarantee of the viability of agricultural activity, avoiding extreme volatility which would have a negative impact not only on agricultural incomes, but also on the industry, distribution, consumers and the economy as a whole.

In view of the greater openness of markets in the near future, it will first be necessary to examine common ground rules, i.e. the need to ensure proper reciprocity so that European producers are on an equal footing with those of third countries as regards complying with the increasing number of health and safety requirements. A similar objective would have to be pursued in relation to environmental and animal welfare requirements by means of international standards.

There is also the need for access to the market instruments of the single CMO as a safety net. As well as discussing ways of improving these established instruments, it is important to continue discussions on other instruments which could complement those already in force.

- The single payment entitlement gives agricultural incomes some stability. Over time, these single payment entitlements will lose their historical references, making it difficult to use them as market management instruments.
- Although authorisation for national State aids could be a one-off solution for minor localised problems, it would not appear to be an appropriate solution for dealing with serious crisis situations in the Community market, since it would give rise to competition problems in the internal market and would imply a clear re-nationalisation of the CAP.
- An approach involving earnings or income insurance is an additional instrument being considered, pending an assessment of its possible effectiveness and efficiency as well as its compatibility with the WTO framework. It could be worth continuing to examine this option.

- Further examination of the option of operator and interbranch agreements and arrangements is another possibility. Progress, however, would need to be made on two fundamental issues which could represent obstacles: an insufficiently organised productive structure and a lack of negotiating power on the part of farmers. With regard to the latter question, a regulatory review facilitating the adoption of agreements within producer organisations and associations or interbranch organisations, without calling competition principles into question, could be a worthwhile alternative.
- Account needs to be taken of the possibility of major crises in sectors with a significant Community presence such as milk, meat and cereals, caused by serious imbalances on world markets or arising as a result of animal diseases. Situations of this kind will require major Community market management interventions. In the context of the CAP post-2013, it is important to ensure that a lack of financial resources does not restrict rapid and efficient management, particularly in cases in which the margins available under the limits established in the financial perspectives are exceeded.

6. Questions

Following the most recent reforms and in the context of the above scenario:

- Do you consider that the market orientation of European agriculture is sufficient?
- Do you consider that current market management instruments provide a sufficient safety net in the event of a scenario of growing volatility? How could the situation be improved?
- Do you consider it appropriate to examine complementary instruments in addition to those provided for in the single CMO? Which? How?
- Do you think that the future CAP should have a financial mechanism to deal with situations of serious crisis which offers flexibility in responding rapidly to such cases?