CAP drivers for change
Global challenges and prospects

COPA-COGECA Workshop
"Main challenges for a future CAP"

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Tassos Haniotis
Director

Economic analysis, perspectives and evaluations; communication
DG Agriculture and Rural Development
European Commission
Outline

1. The shifting environment of agricultural markets...
2. ...its impact on existing trends, drivers and challenges...
3. ...and its relevance for CAP prospects
Drivers of agricultural and food markets

- Macroeconomic and trade environment
- Food supply and demand interaction
- Climate, energy and natural resources
- Population, diets and the food chain
- Price and income prospects have turned more uncertain

Price and income prospects have turned more uncertain.
Main uncertainties

The macroeconomic picture

- The persistence of sluggish GDP growth – now also expanding to emerging economies
- The exchange rate volatility – leading to price declines appearing as price increases for others
- The long-term price level of crude oil - will disinvestment hit supply post-2020?

The demand side picture

- Population dynamics are characterised by significant asymmetries in trends
- Dietary patterns also reflect different, often counter-intuitive developments
- Diverging trends and cross-cutting effects exist within the same group of commodities

The supply side picture

- The wider energy picture – not just crude oil but also impacts from natural gas etc.
- Short-term and long-term impacts of climatic events, including from climate change
- Diverging productivity patterns (and not just in yields..., e.g. RTD, innovation, etc.)
Trends in real commodity prices

(2010 = 100)

Source: World Bank
Annual change in real commodity prices, 1961-2015

Source: DG AGRI calculations on World Bank data.
Monthly change in nominal commodity prices, 2007-15

% monthly change

Source: DG AGRI calculations on World Bank data.
## Commodity price changes during specific periods

<table>
<thead>
<tr>
<th>Period</th>
<th>Agriculture</th>
<th>Fertilisers</th>
<th>Energy</th>
<th>Metals/Minerals</th>
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</thead>
<tbody>
<tr>
<td>2008/1997</td>
<td>29%</td>
<td>336%</td>
<td>298%</td>
<td>107%</td>
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<tr>
<td>2009/2008</td>
<td>-7%</td>
<td>-45%</td>
<td>-34%</td>
<td>-29%</td>
</tr>
<tr>
<td>2011/2009</td>
<td>21%</td>
<td>20%</td>
<td>43%</td>
<td>47%</td>
</tr>
<tr>
<td>2015/2011</td>
<td>-24%</td>
<td>-31%</td>
<td>-48%</td>
<td>-39%</td>
</tr>
<tr>
<td>2015/2008</td>
<td>-15%</td>
<td>-54%</td>
<td>-51%</td>
<td>-36%</td>
</tr>
</tbody>
</table>

Source: AGRI calculations on World Bank data.
World annual growth: cereal consumption vs population (%)

* provisional/estimation for 2012-2015. Size of bubbles represents total average consumption over the period.

Sources: FAO, OECD, USDA
World annual growth: meat consumption vs population (%)

* provisional/estimation for 2012-2015. Size of bubbles represents total average consumption over the period. Sources: FAO, OECD, USDA
World annual growth: fluid milk consumption vs population (%)

* provisional/estimation for 2012-2015. Size of bubbles represents total average consumption over the period. Sources: FAO, OECD, USDA
World annual growth: dairy product consumption vs population (%)

* provisional/estimation for 2012-2015. Size of bubbles represents total average consumption over the period. Sources: FAO, OECD, USDA
The new agro-food prospects

The new market environment

- Commodity markets seem to have returned to more “fundamental” drivers
- The commodity “super-cycle” effect of China seems to be over
- The impact on price level is more clear than impact on co-movement or on volatility

The new trade environment

- Trade in both food commodities and food products will remain strong
- Demand in most emerging economies will grow faster than their domestic production
- Yet, as always, in agricultural markets the surprise is around the corner...

The new price environment

- Despite significant declines, prices are still higher than pre-financial crisis levels
- The terms of trade for agriculture may improve some if energy prices stay low, but lost a lot...
- Where in-between the highs and lows of the post-2008 situation does the likely price path lie?
The likely wheat price path (2016 DG AGRI Outlook)

Source: DG AGRI Agricultural Markets Outlook 2016-2025.
Dairy price challenges...

EU and world dairy prices

Source: DG Agriculture and Rural Development calculations
...placed in a broader perspective

Multiple causes lie behind the recent dairy crisis – opinions for their weight differ

- World oversupply coincides with slowdown in Chinese imports and the Russian embargo
- Broader macro developments (exchange rate, oil) push all commodity prices down
- Recent increase of the EU dairy herd reverses a very long downward trend

The EU's main policy response focused on targeting income

- By addressing immediately the cash-flow difficulties farmers were facing
- By attempting to stabilise markets, maximising the use of existing measures
- By aiming to improve the functioning of the supply chain (setting of Ag Markets Task Force)

The EU's policy response refrained from replacing market signals

- Higher price signals in the context of oversupply will amplify price pressures
- Long-term competitiveness and market orientation of CAP need to continue
- Similar price pressures exist also under very different farm policy regimes
Cumulative change in milk production, 2007-15

- EU: 16 Million t
- USA: 12 Million t
- New Zealand: 8 Million t
- Australia: 2 Million t
- Argentina: 0 Million t

% change:
- EU: 15%
- USA: 10%
- New Zealand: 20%
- Australia: 30%
- Argentina: 40%
Main short-term dairy market challenges...

**Demand**
- Jan-Nov 2015 world consumption -1.1% (first decline since 2008)
- Jul-Nov 2015 global demand picking up again + 3 %

**Supply**
- Main producing regions increase supply by 1.6% in 2015
- EU supply up stronger, by 2.5% in 2015 (multiple reasons)

**Trade**
- Expected future world import growth of roughly + 2 % annually
- EU exports + 5.2 % Jul-Non 2015 (despite Russian ban)
CAP reform path and CAP budget, 1980-2020

Source: DG AGRI.
Long-term trends in EU-world price gap

Percentage gap between EU and world price

Source: AGRI calculations based on European Commission AGRI and OECD data.
EU28 agri-food trade, 2005-15

Source: COMEXT
Source: AGRI calculations based on ESTAT and ERS/USDA data.
CAP reform path and CAP budget, 1980-2020

Source: DG AGRI.
Issues that require rethinking in the long-term

The reasoning of income support and the pertinence of Direct Payments

- Income support component (logic, distribution) still questioned, and its impact very often ignored
- Two parallel systems of DPs still in place, with weak agronomic (or even economic) specificity
- Voluntary coupled support “combines” EU value-added logic and its exact opposite

The role of CAP controls – their logic and its relevance for simplification

- “Error rates” require a reference – with respect to what are farmers erring?
- The lowest possible tolerance reflects policies based on support for the delivery of private goods...
- ...yet the CAP has moved towards the support of public good – what prospects for rethinking?

The converging(?) universe of all EU policies – big challenges ahead

- Identifying CAP’s wider contribution on jobs and growth is the biggest challenge
- The CAP is a mixed bag of potential opportunities and challenges for climate and the environment
- Bottlenecks in the food chain provide opportunity to refocus (some) policy responses
Is the two pillar structure still pertinent?

- CAP objectives stress more the "jointness" rather than the division of existing policy instruments
- The old budgetary argument for distinction is already overtaken by policy changes
- The core element of CAP support - land use – requires a unified approach and complementarity

Is the distinction between “old” and “new” MS still relevant and desirable?

- Gaps among and within MS are not anymore specific to “accession age” or agriculture
- Redistribution aspects are still valid, but should be linked to a common and pertinent yardstick
- Designing land-based support void of land market realities needs rethinking and re-assessment

Jobs and growth requires a broader investment strategy for EU agro-food complex

- The starting point of EU food production is - and will continue to be - EU agriculture
- Enhancing EU food competitiveness and innovation is both skill- and region-specific
- Shifting RD measures into other measures will suppress EU growth, jobs and exports
How do we treat land in the CAP?

The “virtuous” layer: research, innovation, extension
To work, it needs an holistic link to overall long-term policy objectives

The “control” layer: still driven by risks linked to private goods
To work, it requires shift to reflect new policy logic and objectives

The “RD” layer: agri-environmental and climate measures
To work, it requires specific link to GAEC, costs and income

The “Greening” layer: to address soil, air and biodiversity challenges
To work, it also requires regional definition of agro-economic conditions

The basic layer: Good Agricultural and Environments Conditions
To work, it requires regional definition of agronomic conditions
Drivers and relevance for the policy instruments

Pressure from markets – a counter-cyclical or competitive agriculture?

- Arguments for increased market support will hardly convince a squeezed EU economy
- Existing market instruments have limited margin for improvement in their efficiency
- Which trade-off between existing measures and risk management is possible and/or desirable?

Pressure on land use - scrap or re(de)fine “greening”?

- Land use and climate impacts ignore national frontiers, thus impose EU-wide response
- Even if “greening” did not exist, we would need to invent coherence on land use
- Are perceived problems with greening is the concept, the scope, or the implementation?

Link to other EU policies - strengthen or shift CAP’s competitive angle

- Investment in the economy of rural areas is mainly linked to the broader food chain
- Coherence with other EU funds should address both regional and EU-value added angles
- EU food competitiveness starts from the recognition of internal market realties
Relevance of risk management in the EU

The search for ways to enhance risk management tools is not new

- Preparation of both reform of 2008 and 2013 included extensive analyses on the issue
- An EU-wide scheme was considered unlikely (budgetary rules; distribution impact)
- MS were granted flexibility in rural development measures (but little appetite so far)

Some risks are covered in most MS, but at different levels and degree

- Weather-related risks covered both ex-ante, and ex-post (but mainly with MS money)
- Debate on whole-farm vs sector-specific approaches limits popularity in RD measures
- Fixed income support so far worked better than alternatives (results vs recognition)

Future policy orientation will determine degree of complementarity

- Competitiveness and market orientation imply farmers need to assume some risk
- Animal/plant disease and weather risks are more pertinent (and difficult) to address
- Balance among sectors and MS requires choices of shift from existing tools (e.g., VCS)
An (apparent) policy paradox and its causes

Why do EU and US farm policies target farm income support so differently?

- Differences in the structure of their respective farm sectors explain some...
- ...differences in institutional setting and decision making explain more...
- ...yet differences in underlying policy objectives may explain most

**US farm policy still focuses on different ways of product support**

- All forms of farm income support retain some link to past production references
- Price reference, with high concentration on few crops, constitutes bulk of support
- Increase of insurance programmes reflects past product-specific support

**EU farm policy focus has gradually shifted away from product support**

- Land-based support tools have broken link to price and past production references
- Land use has become the main focus of income support and its justification
- Broader CAP objectives reflect preference for a wide product and regional diversity
The bottom line for EU (and every) agriculture

Agriculture as the 2 % sector

- Narrow focus on sectorial interests exposes agriculture’s low GDP share and overall economic weight
- Product-driven concerns are real and justified; yet product-driven responses divide policy objectives
- Policy is driven on the defensive to justify its spending, instead of justifying its broader objectives

Agriculture as the 40 % sector

- Land use, the new focus of the CAP, addresses both environmental and climate challenges
- Wider territorial policy scope brings wider growth and employment links to the forefront
- Technology and innovation will determine land-use, climate and environmental performance

Agriculture as the 100 % sector

- Food demand-driven policy concerns unify policy focus and reform opportunities
- Up-stream, down-stream and horizontal linkages are potentially growth and job enhancing
- Technology and innovation will also determine net employment effect across the food chain
Reports and data available at:

http://ec.europa.eu/agriculture/index_en.htm


http://ec.europa.eu/agriculture/trade-analysis/index_en.htm

Thank you for your attention!