

## High Level Group (HLG) on the Competitiveness of the Agro-Food Industry

### CIAA submission and contribution to the discussions of the Working Group: “Prices Issues”

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#### **Background and issue**

Access to competitively priced agricultural raw materials is vital for the food and drink manufacturing industry. The industry has recently been experiencing unprecedented surges in the price of some agricultural raw materials, which are proving challenging for EU manufacturers and indeed consumers.

Over the year 2007, prices on key EU markets went up by approximately 68% for wheat, 35% for maize, 17% for butter, 62% for rapeseeds and 104% for sunflower seeds. While these upward trends follow a long period of relatively lower prices of EU agricultural products, the rise in raw materials' prices is without precedent in terms of number of products concerned and the extent of the increases over a limited period. The reasons for the surge in global commodity prices are multi-factorial and include both short-term temporary as well as long-term structural changes in supply and demand including:

- ✓ Fall in supply due to climatic conditions (drought or excessive rainfalls) and slowdown in yield productivity =>the climate change is likely to increase weather risks in the coming years;
- ✓ Increased demand for bio-fuel production => the trend is very likely to continue considering the policies that countries around the globe are implementing or strengthening;
- ✓ Increased demand for food and feed due to dietary changes in large emerging countries, e.g. China and India. => with enhanced wealth the trend will continue.
- ✓ Speculative intervention from corporate or government investors on global commodity markets; => with prices of raw materials subject to high volatility, this increases incentives to speculate on their development.
- ✓ With the EU GMO process leading to asynchronous approvals, access to agricultural raw materials is more limited due to low-level presence of un-authorized GM material; => the technology factor can offer solutions to the need for more raw materials, the question is whether Europe will be able to make use of better technologies
- ✓ Increase in energy prices, which also affects raw material prices.

It is also worth noting that stocks of many agricultural products (cereals, oilseeds, milk powder and butter) are low, livestock production is decreasing and successive

CAP reforms have led to a more market-oriented agricultural policy. This has increased price volatility.

### **Examples**

Agricultural price developments based on a monitoring of **official price quotations** from selected representative agricultural markets provide the following picture:

#### **Coarse grains**

<b>Growth rates for EU and world coarse grain prices</b>			
	<b>Sept06-Sept07</b>	<b>Jan07-Jan08</b>	<b>March07-March08</b>
Maize World	23,7%	10,4%	35,7%
Maize EU	63,1%	34,9%	28,8%
Wheat EU	94,5%	68,3%	87,4%
Wheat World	95,7%	92,9%	133,8%

Main cost drivers for coarse grains:

- Bad weather conditions causing poor productivity and quality exacerbating a situation where over several years now production is lower than demand and has led to low global stocks.
- Rising demand of Bio-Ethanol producers affecting exports from traditional grains exporters.
- Speculative intervention from government and corporate investors on global commodity markets.
- Governments intervention in markets through export restriction (taxes).
- More rigid European legislation for cereals used for human consumption.

#### **Dairy products**

<b>Growth rates for EU and world dairy prices</b>			
	<b>Sept06-Sept07</b>	<b>Jan07-Jan08</b>	<b>March07-March08</b>
SMP World	114,9%	35,6%	10,8%
SMP EU	77,7%	11,7%	-4,5%
Butter World	112,7%	87,4%	69,6%
Butter EU	82,0%	16,7%	7,7%

Main cost drivers for dairy products:

- Increasing demand for dairy products from Asia, especially from China
- Drought in Oceania
- Depleted EU intervention stocks

#### **Oilseeds and vegetable oils**

<b>Growth rates for EU and world oilseeds and vegetable oil prices</b>			
	<b>Sept06-Sept07</b>	<b>Jan. 07-Jan. 08</b>	<b>Mar07-Mar08</b>
Soybeans world	55,5%	58,5%	56,2%
Sunflowerseed EU	101,8%	104,8%	132,8%
Rapeseed EU	38,0%	61,9%	93,5%
Sunflower oil EU	80,1%	113,1%	128,6%
Soybean oil EU	50,0%	64,1%	79,9%
Rapeseed oil EU	26,3%	56,5%	73,7%
Palm oil World	58,2%	58,5%	75,7%

Main cost drivers for oilseeds and vegetable oils:

- Rising demand for bio-diesel production

- Rising demand due to growing consumption in Asia, mainly in India and China
- Shortage on coconut, palm and sunflower due to lower crops in 2007

### Cocoa

Growth rates for the world cocoa price			
	Sept06-Sept07	Jan07-Jan08	March07-March08
Cocoa World	16,5%	16,7%	21,4%

Main cost drivers for cocoa:

- Bad weather conditions in producer countries
- Speculation from investors on cocoa market.

### Outlook

However, the views on price developments diverge considerable. According to the International Monetary Fund, agricultural commodity prices are likely to stay high for the foreseeable future as supply would require new investment and policy reforms.

Other official sources consider that, in the short term the trend will face a reduction. But in the longer term prices are certainly to see an upward trend. Costs of agricultural raw materials will rise due to structural challenges such as increased world wide demand for agricultural products, the market being created for biofuels and the segregation of GM and conventional markets.

### Effects of increased costs on food and on consumer prices

The impact of increased raw material prices on the costs of processed food depends notably on the raw material used, on other input costs and on the added value contained in the finished products. The increase of the input costs at the level of the food and drink industries increases ex factory prices. But the manufacturer is not in control of the extent to which this is reflected in food prices paid by consumers. This is also dependent on other factors and players in the chain.

According to the recently published Harmonised Consumer Price Indexes (Eurostat), since the end of 2006, but particularly since July 2007, food prices in the EU have increased more rapidly than overall inflation. The same pattern was observed for the euro area. In April 2008, the annual increase in food prices in the EU was 7.1%, compared with 3.6% for overall inflation, as measured by the all-items HCPI. In the euro area, the annual increase in food prices was 6.2%, compared with 3.3% for overall inflation.

March and April 2008 recorded the highest annual increases in food prices in both the EU and the euro area since the beginning of the series in 1996. In April 2008, the highest yearly increases in food prices were found in Bulgaria (25.4%), Latvia (21.7%), Estonia (18.3%) and Lithuania (18.1%). The lowest increases were registered in Portugal (3.2%), Netherlands (5.4%), France (5.5%), Cyprus (5.8%) and Italy (5.9%). However, between 1996 and April 2008, food prices have risen in total at a similar rate to overall inflation: +31% and +27% respectively in the EU, and +30% and +27% respectively in the euro area.

The weight of food in the all-items HICP reflects the share of food purchases in household consumption expenditure. This share is 14.6% at the EU level. The weight of food in the index varies from 9.5% in the United Kingdom and 9.7% in Luxembourg, to 34.5% in Romania and 23.2% in Lithuania.

### **CIAA Priority Objectives and Recommendations**

Considering the important variations in the assessment of the reasons, both temporary and structural, for the surge in prices of agricultural raw materials, a comprehensive assessment should be carried out by the Commission in view of identifying precisely the contribution of these different factors in market price developments. This would allow to identify more adequately and notably prioritise the policy responses.

For CIAA, considering factors identified as having an impact on the development of agricultural prices, action should embrace in a comprehensive and food policy approach the policy areas listed below. The recommendations made in the contribution to the debate on “access to raw materials” are equally critical to address the “prices issues”:

- **Common Agricultural Policy;** it must anticipate the changes in supply and demand; adjust policy tools; remove instruments that constrain European production; favour a farming sector that is efficient, innovative and rapidly responding to market developments; and invest funding in agricultural technological advances.
- **GMOs Policy;** it is necessary to speed up approval process within the EU; find a solution to the low-level presence of GM events approved in the exporting country, which have not been approved in the importing country; and develop a public, evidence-based, debate about the use of GM supplies in EU markets.
- **Biofuels policy;** it must avoid competition between food and fuel markets by fully meeting the 2007 Spring European Council decision; a full, comprehensive impact assessment must be commissioned; a formal review clause and mechanisms to avoid crisis situations must be introduced.
- **Pesticides policy;** a full EU-wide impact assessment must be commissioned which takes into account the impact of the “cut-off” criteria on food supply and prices.
- **Monitor Agricultural Markets;** or at least formalise existing monitoring mechanisms by introducing a feedstock observatory to look closely and regularly at availability and price of agricultural raw materials to anticipate trends.
- **Energy policy;** it needs to be considered what actions on the political level can be undertaken in order to stop the dramatic increase in prices for all energy sources (oil, electricity, gas) and soften the consequences for the economy.
- **Research;** agriculture will require further research into new technologies to be able to provide crops that are more productive, better adapted to local requirements; and responding to new agronomic requirements. Research will also need to be stepped up to develop the most efficient feedstock for the use as bio-fuels with a view to increasing possible sources of raw materials and to enhancing feedstock availability.