15 EQ11: Relevance

This question requires the CAP measures applicable to the dairy sector to be evaluated with respect to the needs and problems of the main stakeholder groups influenced by dairy policy.

As explained in the evaluation methodology, questions of relevance are important in ex ante evaluations where strategic issues and how they are mapped into policy instruments are under discussion and can be modified. In a retrospective evaluation it is possible to examine whether the needs and the problems of the main stakeholder groups have actually been addressed by the policy. The initial step is therefore to identify the stakeholder groups and to list their concerns. Such a list is derived here partly from the recitals in the legislation, or what is implicit in the recitals, and also in part from extensive background knowledge about the sector and the dairy policy context. Based on this list, the analysis explores to what extent the policy impacts have delivered results in response to these needs, and whether particular stakeholder groups have grounds for being more satisfied with the outcomes than others. This involves designating one or more indicators that reflect policy outcomes and are also associated with specific stakeholder concerns.

The question explicitly mentions farmers, processors and consumers as the groups most involved. However, in order to encompass all the objectives and the changes realised, several other groups (taxpayers, and ‘beneficiaries of the environment’ – that is, current and future citizens of the EU and beyond) should also be mentioned.

For the purposes of this evaluation, four stakeholder groups are therefore distinguished: milk producers, milk processors, consumers of dairy products, and ‘society’ (comprising people in their roles other than dairy product consumer, namely as taxpayer and citizen). For each of these groups, a number of commonly expressed concerns are identified, namely:

**Milk producers**: level and stability of income, administrative burden, constraints on production choices, constraints on expansion,

**Dairy processors**: milk prices, availability and stability of raw milk supplies,

**Dairy product consumers**: consumer prices,

‘**Society**’: environmental sustainability, animal welfare, GHG emissions and climate change, food security, cost of the CAP, cost of agricultural policies.

It is clear that there are trade-offs between different stakeholder needs (in certain cases, maximising the perceived needs of one group may be incompatible with doing the same with respect to other needs of a different group). There are also limits to what can be delivered by policies. For example, consumers want cheaper food, many also want higher-quality food, whereas others (and maybe some of the previous groups), in their role as ‘citizens’, also want their food to be produced in a more environment- and animal-friendly way. If the most recent changes in dairy policy have not been able to deliver undisputed improvements with respect to all these needs, it may not be because the policies lack relevance but

---

perhaps because the internal constraints linking these objectives make it impossible to maximise across them all at the same time. Similar trade-offs exist between the commonly perceived needs of producers and processors, and there are limits to what dairy policy can deliver with respect to curbing the methane emissions of dairy cows, without which there would be no dairy products at all. When interpreting the findings relating to relevance, these issues need to be taken into account.

15.1.2 Methodology used for answering EQ11

The methodology adopted here consists in assembling all the evidence presented in earlier EQs, structuring it according to the stakeholder groups and their particular concerns, and making a synthetic summary in table form. Very few new indicators are used and little new material is provided. This methodology is entirely appropriate for addressing the issue of relevance ex post. If material on the effectiveness and efficiency of CAP dairy policy were not adequate or not appropriate for assessing the extent that the policies have met relevant needs, then a priori this would indicate a poor match between the objectives, instruments and impacts of the policy on the one hand, and the needs and problems of the stakeholder groups on the other.

15.1.3 Judgement criteria, indicators and judgement criteria used for each indicator

The indicators used to answer this EQ are set out in Table 15.1.

Table 15.1 Judgement criteria and indicators for EQ11

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Data requirement</th>
<th>Information sources</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Milk producers</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Level and stability of income</td>
<td>Evidence presented for EQ2, EQ3, EQ5 and EQ10.2</td>
<td>This report</td>
</tr>
<tr>
<td>Administrative burden</td>
<td>Evidence presented in EQ9</td>
<td>This report</td>
</tr>
<tr>
<td>Constraints on production choices</td>
<td>Evidence on cross compliance costs presented in EQ10.1 Impact of decoupling</td>
<td>This report</td>
</tr>
<tr>
<td>Constraints on expansion</td>
<td>Future evolution of the quota scheme (Table 2.38, EQ9)</td>
<td>This report</td>
</tr>
<tr>
<td><strong>Processors</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Milk prices</td>
<td>Evidence presented in EQ2 and EQ5</td>
<td>This report</td>
</tr>
<tr>
<td>Product prices</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Stability of raw milk supplies</td>
<td>Evidence presented in EQ1</td>
<td>This report</td>
</tr>
<tr>
<td><strong>Consumers</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Consumer price</td>
<td>Reduction in support coming from consumers</td>
<td>EQ9</td>
</tr>
<tr>
<td></td>
<td>Evidence on price transmission</td>
<td>DG AGRI report on price transmission</td>
</tr>
<tr>
<td><strong>'Society' (citizens, taxpayers etc)</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Environmental sustainability</td>
<td>Indicator(s) calculated for EQ10.2</td>
<td>This report</td>
</tr>
<tr>
<td>GHG emissions</td>
<td>Dairy cow trends (EQ10.2)</td>
<td>This report</td>
</tr>
<tr>
<td>Cost of the CAP</td>
<td>Evidence from EQ9</td>
<td>This report</td>
</tr>
<tr>
<td>Administrative costs of agricultural policies</td>
<td>Conclusion reached in EQ9</td>
<td>This report</td>
</tr>
</tbody>
</table>

New judgment criteria will not be used for each indicator separately. Instead, the judgement already reached regarding the indicator when used earlier in the report will be carried over to this EQ. The judgement criteria for assessing the overall impact on stakeholder need and problems involve considering all the main changes in terms of their ability to meet stakeholder concerns, and drawing conclusions from the picture that emerges.

However, it would still be within the scope of dairy policy to create incentives for producers to adopt production and feeding systems, dairy breeds, etc., that minimise these emissions, given the current state of our technological knowledge.

117
15.2 Milk producers

15.2.1 Level and stability of income

Evidence presented in EQ3 shows that trends in producer income have been maintained and that the position of dairy farmers relative to other types of farming has not deteriorated.

As argued in EQ10.1 based on evidence from EQ2, EQ3 and EQ5, the post-2003 configuration of policy measures revealed itself inadequate for shielding EU markets from the world market turbulence of 2007-2008. Prices for raw milk and for dairy products in wholesale markets rose close to or at times above world market price levels, and the volatility of these prices on a monthly basis was comparable with that of world market prices. However, the increased share of direct payments in the income of farmers from 2004 onwards (fully achieved by 2007) meant that a smaller proportion of their income was vulnerable to this volatility. Clearly, the ‘cushioning’ provided by direct payments was not enough to meet milk producers’ expectations or to allay their fears, and they expressed their concerns very forcefully, particularly during the sharp downturn in prices in 2009. If a similar episode of high and volatile world market prices should occur again, the same impacts are likely to be felt in the EU dairy sector.

15.2.2 Administrative burden

The administrative burden for milk producers due to the CAP has increased. This was to be expected, given the way policies have been evolving (in particular, the shift away from price support and towards targeted transfers to particular groups who have to justify their eligibility for payments and their compliance with the payment conditions). This increase was confirmed by the producer survey (see EQ9). Much of the perceived increase has been due to environmental restrictions (mainly associated with cross compliance) and relatively little of it (according to respondents) from the payment mechanism associated with the SPS/SAPS.

15.2.3 Constraints on production choices

The issue here is whether cross compliance places new constraints on production methods or technologies. Producers were asked about the costs of cross compliance, and virtually all replies concerned investment costs (adaptation of buildings, waste storage, animal ear tags and so on) but virtually nothing about costs of being obliged to produce in milk on a different way. A question asking specifically about this potential effect was not directly asked in order to avoid any bias that may have arisen by appearing to expect or solicit the reporting of such an effect. Instead, a more general and open-ended question was asked about the “costs of cross compliance”, which allowed producers themselves to identify the costs they had faced. In the replies given to this question, there was no mention of constraints on production methods.

As regards constraints on the choice of what to produce, it is clear a priori that the decoupling of the dairy premium removes a constraint on producers’ choices, as it is no longer necessary for them to hold quota at the end of the current year in order to receive the payment. There was little evidence that this acted as an incentive to quit dairying, although common sense suggests that if there are other reasons for wanting to quit, the decoupling of the payment may facilitate the decision. There are also no signs whatsoever that the decoupling has acted as an incentive for milk producers to continue to produce milk but at a lower level, whilst diversifying into other commodities. On the contrary, all the signs are that milk producers are still seeking economies of scale through herd-size expansion, and that the share of milk coming from specialist dairy farms (i.e. those for whom more than two-thirds of their gross margin comes from dairying) is increasing. However, it is also true that decoupling has removed a (potential) constraint on producer choices that may be relevant for a minority of producers.

15.2.4 Constraints on expansion

Table 2.38 shows the planned levels of national quota ceilings up to abolition in 2015. It shows that already (since 2008) quota ceilings are higher and that across the EU quota will become even more available before 2015. In 2010, all but two Member States had delivery levels below their national
ceilings, indicating that at national levels for that year, quota availability was no longer a constraint on production. Despite this development, even in 2009/2010, there was still a small price for quota purchase (see Table 13.9) by producers not wanting to face the risk of having to pay the superlevy when expanding production. Overall, however, many producers in different parts of the EU are already operating without an effective quota constraint, as a result of the changes decided in the 2003 dairy policy reform or subsequently.

15.3 Processors

15.3.1 Milk prices
The switch of some producer income support out of the milk price and its replacement by a direct payment has undoubtedly lowered the price that processors need to pay for raw milk, ceteris paribus. Figure 6.1 shows that the underlying trend in milk price between 2004 and 2006 was indeed downwards (following the phased reductions in intervention prices). In the following period (2007-9), price levels and movements were severely disrupted by market instability. However, one can expect that the advantage to processors of lower milk prices will persist in more normal conditions. This observation was made by some of the respondents to the processor survey.

15.3.2 Product prices
Product prices were expected to be affected in a downward direction by the lowering of intervention prices. This has turned out to be the case for butter (see Figure 9.1). However, the price of the other intervention product, SMP, remained rather steady during 2004-2006, as did that of WMP which often serves as an alternative on the production side to butter and SMP (see Figures 9.3 and 9.5). In the case of cheddar cheese (chosen as a representative cheese), prices did fall slightly during 2004-2006. It should be noted that between 2003 and 2006, there was a noticeable decline in expenditure on cheese export refunds (see Figure 13.3), which could explain the slightly declining internal price.

15.3.3 Availability and stability of raw milk supply
In principle, the dairy policy changes under review should improve the availability of raw milk for processing, for the same reasons given in section 15.2.4 above. Of course, whether this occurs will depend on the milk price and whether it is high enough to keep production at current levels and to encourage producers to expand further when they are no longer constrained by quota. If this does not happen (indeed, some models suggest that after quota abolition prices may fall low enough that the production increase will be quite limited\(^1\))\(^8\), then local shortages could develop. Recent discussions have focussed on a possible imbalance of bargaining power between producers and milk processors in various EU Member States. To the extent that this occurs, the milk price may be forced below its level would be in competitive conditions, and both market and policy signals received by producers are distorted. As the sector becomes more market-oriented, the role played by price becomes more important, so that if processors find they are facing a tight market for raw milk supplies, they will have to use price increases to secure the supplies they need.

Regarding stability of supply, the recent reduction in supply in some Member States has prompted the question as to whether they are ‘cyclical’ variations or one-off, irreversible reactions to the combination of policy changes and market turbulence of recent years. In general, it can be expected that, as constraints are removed and the dairy sector becomes more market-oriented, total supply becomes less predictable than it was before the 2003 reforms. Here again, processors can make greater use of proven mechanisms (such as long-term contracts) to remedy the situation. A potential concern is that if market power is unequally distributed between processors and producers, the terms of such contracts may be unfavourable to producers. It is therefore important that forms of contract are used that preserve producers’ access to a share of any income gain due to higher prices in product markets in return for bearing the risk of loss from variability of milk production conditions.

\(^{18}\) See for example Witzke and Tonini, 2008.
In general, given the nature of the production processes involved and the specificity of the investments in milk production, large year-on-year variations in supply are very unlikely. It is interesting to note that respondents to the processors’ survey did not consider that any of the policy changes relating directly to dairy farmers would impact on stability of supply.

15.4 Consumers

15.4.1 Consumer price

Since the dairy policy measures under review do not directly target consumer markets, none of the indicators used for other EQs can shed light directly on the extent to which the 2003 reforms have responded to the consumer’s wish for reasonable product prices. What has been established is that some income support has been shifted out of wholesale product prices into direct payments by reducing the support to intervention products (this was called in EQ9 a reduction in the ‘consumer transfer’). However, it is not guaranteed that the lower wholesale price was transmitted to the price paid by final consumers.

A recent study\textsuperscript{119} of price transmission along the supply chains for a number of food products in some Member States concludes that the dairy supply chain is one of the cases where price transmission works least well. Among the conclusions of this report is the finding of “asymmetric behaviour across the dairy chain where dairy consumer prices have been fast to increase, but slow to decline in the wake of the sharp drop in milk producer prices (e.g. Slovenia, United Kingdom, Denmark, Lithuania). Furthermore (this) price transmission pattern in the dairy sector has significantly strengthened since the commodity price surge in 2007” (p.56). Moreover, for some dairy products, the typical delay between a fall in milk price and a downward reaction of consumer price could be 12 months, and tends to be longer in the EU-12 countries examined than for the EU-15 countries considered.

It is an integral part of the objective to improve market orientation that all segments of the chain should share in the benefit from the resulting efficiency gains. In fact, it is inconsistent with the principle of market orientation that price transmission between any particular segments of the chain should be impeded.

This is an unresolved issue where not only more empirical analysis is needed but also more attention to effective policy design. To understand and measure the extent of price transmission (in either direction) along the entire length of the supply chain between primary producer and final consumer requires a perspective that embraces the whole chain. Such a whole-chain perspective is also needed in order to formulate appropriate policies about price transmission or to make recommendations for ensuring its smooth functioning. Given that price transmission along the supply chain is not part of the remit of CAP dairy policy, this issue is not directly addressed in the present evaluation study. However, in this evaluation question, where the relevance of EU dairy policy to the main stakeholder groups in society is under discussion, it is very important to point out that price transmission is one of the two crucial links between policies targeting the milk-producing sector (both as regards their objectives and the instruments used) and the interests of consumers.\textsuperscript{120} If price transmission is not working well, two negative consequences of direct relevance to this evaluation may arise. First, instruments that operate at intermediate stages in the chain downstream from milk producers (such as the intervention system) but which are intended to affect outcomes in the milk-producing sector may be prevented from achieving their aims. This issue has already been discussed in Chapters 4 and 6. Second, consumers may not benefit from efforts to achieve greater efficiency in milk production, whether these efforts are market- or policy-driven.


\textsuperscript{120} The other link concerns product quality, and the preservation of its integrity, as regulated at the raw milk stage, along the entire chain to consumers. Quality issues are not the focus of this evaluation, and it assumed throughout that this aspect of consumer concerns presents no issues product quality.
15.5 Society

15.5.1 Environmental sustainability

In EQ10.2, several indicators relating to the incentives for environmental sustainability provided by CAP dairy measures were assembled. A priori, when some income support is shifted from price (which means total income support is less dependent on the quantity produced) and is paid as a guaranteed fixed amount, this should lessen the incentive to push for yield increases and to intensify the use of fixed resources (cows, land, labour). Nevertheless, the evidence reviewed suggests that the policy changes have not lessened the incentive to produce more intensively in EU-15 Member States, and that there was a risk of increasing environmental problems in areas where dairying becomes more concentrated. At the same time, cross compliance requirements and the relatively high participation rate of dairy farmers in agri-environmental schemes may help to offset any potential environmental degradation that might occur because of greater intensification.

15.5.2 GHG emissions

In contrast to the general concern about resource use and the environment, EQ10.2 concluded that although the level of milk output has remained relatively constant, emissions of methane per tonne of milk produced have fallen thanks to the ongoing decline in the number of dairy cows in EU27. This is largely due to the secular increase in milk yields. Establishing a link between this trend and the 2003 policy reform would involve demonstrating a link between the new policy signals, a growth in the share of milk coming from specialist dairy farms (where milk yields are higher) and the rather small increase in the rate of decline of dairy cows since 2003. As already demonstrated in earlier chapters, the empirical evidence supporting this causal chain is weak.

15.5.3 Cost of the CAP

The evidence presented in EQ9 shows that the total cost to society of dairy support has been falling, and this is true even when the decoupled ‘ex-dairy premium’ (now part of the SFP) is also included in the calculation. However, the conclusion relies on the savings in the ‘consumer transfer’ component of total cost being acknowledged, and for this fall to be shared widely across social groups it requires that consumers should benefit from the market price reductions for dairy products at the wholesale level. In order for the wider societal benefit of the 2003 dairy reform to be appreciated, not only does the shift from more costly support (in social terms) via the market to more efficient support via direct payments need to be explained to the wider public, but more importantly the lower prices on which this benefit rests actually have to reach final milk consumers. This point is closely linked to the argument presented in 15.4.1.

15.5.4 Administrative costs of agricultural policy

Examination of the cost of public administration relating to dairy policy in EQ9 was based on the experience of only two Member States\(^{121}\), and therefore had to remain inconclusive as regards the EU as a whole. In the two cases examined, the tentative conclusion was reached that public administrative savings through the simplification of policies and their implementation had been delivered by the 2003 reforms. However, other stakeholder groups (farmers, milk processors) also bear part of the policy implementation cost in the form of (unpaid) administrative tasks. The milk producer survey found that farmers perceived the administration burden of dairy policy to have increased since 2003, whereas the perception of milk processors was mixed depending on the type of marketing activities (e.g. exporting or producing solely for the domestic market) or product mix (e.g. focus on basic (intervention) products, or on PDO cheese) undertaken by the firm.

The difficulty experienced by the evaluation team in finding more extensive hard evidence on public administration costs of these policies is symptomatic of the lack of transparency surrounding this item of

\(^{121}\) The relevant administrations in Member States where case studies were performed were contacted with the request to provide information on administration costs. Despite follow-up approaches, only two Members States provided information that could be used to address this part of the evaluation question.
policy cost. Unfortunately, this lack of transparency can provide fertile ground for the propagation of unrepresentative anecdotes alleging administrative inefficiency in implementing CAP procedures, which may lead to a perception of inefficiency that is largely unfounded. The general public (taxpayer and citizen), as well as the image of the CAP, would benefit from more transparency and more rigorous measurement of administrative costs than seems to exist at present.

### 15.6 Conclusions

Table 15.2 gives a summary of the points raised in this section. The scoring conventions used are those adopted for Table 14.11 in EQ10.2. The scores and the density of the remarks in the table suggest that milk producers and society at large are the two groups most affected by CAP dairy measures. However, it needs to be borne in mind that for society, what happens in the EU dairy sector is just one of many other pressing and not so pressing concerns, whereas for milk producers it is an important factor in determining their livelihood, the future for their families, the way they spend their working time, and is clearly of utmost importance to them.

#### Table 15.2  Summary of CAP dairy policy measures according to how their outcomes have responded to stakeholder concerns

<table>
<thead>
<tr>
<th>Stakeholder Group</th>
<th>Milk producers</th>
<th>Processors</th>
<th>Consumers</th>
<th>Society</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Policy change</strong></td>
<td><strong>Stakeholder Group</strong></td>
<td><strong>Stakeholder Group</strong></td>
<td><strong>Stakeholder Group</strong></td>
<td><strong>Stakeholder Group</strong></td>
</tr>
<tr>
<td>Package of changes involved in switching from market price support to a decoupled payment (including lower prices and more visible support through budget payments)</td>
<td>+++ (income levels maintained) ++ (more flexible production choices without losing support entitlement)</td>
<td>+ (lower prices for raw milk, but also potentially lower prices for processed products)</td>
<td>++ (potentially lower prices, BUT receiving them depends on price transmission along the chain)</td>
<td>+++ (the package is more efficient)</td>
</tr>
<tr>
<td>Introduction of cross compliance requirements for milk producers</td>
<td>-- (investment costs, greater administrative burden)</td>
<td>0</td>
<td>0</td>
<td>++ (makes dairying more environmentally friendly, helps to gain support for the CAP among the wider public)</td>
</tr>
<tr>
<td>Gradual increase and then abolition of quotas</td>
<td>++ (more scope for expansion, scale economies)</td>
<td>+ (more abundant milk supplies)</td>
<td>0</td>
<td>? (fear of negative environmental consequences, disappearance of dairy farming in mountain areas/family farms)</td>
</tr>
<tr>
<td>Reduction of intervention to a safety net</td>
<td>-- (greater risk of price instability)</td>
<td>-- (greater risk of price instability)</td>
<td>0</td>
<td>+ (large intervention stocks often seen negatively by society)</td>
</tr>
<tr>
<td>Simplification of policies</td>
<td>Milk producers perceive greater complexity rather than simplification</td>
<td>(depends on the type of activities of the company)</td>
<td>0</td>
<td>? Difficult to obtain a balanced picture, more transparency needed</td>
</tr>
</tbody>
</table>

Key: --, --, and – indicate that the outcome has been contrary to one or more of the concerns of a particular stakeholder group, with the number ‘–’s indicating the degree to which this has occurred; 0 indicates that the outcome of the particular measure has been largely unrelated to the concerns of the corresponding stakeholder group; +, +++, indicate that the outcome has been met or been supportive of one or more concern of the stakeholder group. ‘?’ indicates that conflicting tendencies, or insufficient evidence to conclude.
Consumers are the stakeholder group with the fewest impact items, and yet the one issue registered for them (price falls and their transmission to final consumers) is crucial. Milk and dairy products are consumed daily by most people, and the expenditure of a typical family on dairy products over the year is significant. Although all the stakeholder groups score at least one ‘+’ in the first row of the table (switch in delivery mechanism of income support), this element of the policy package can only be considered an unqualified success if the benefit of the increased efficiency reaches consumers at the end of the chain.