

# The 2016 EU Agricultural Outlook Conference

*Income volatility and risk management in the EU*

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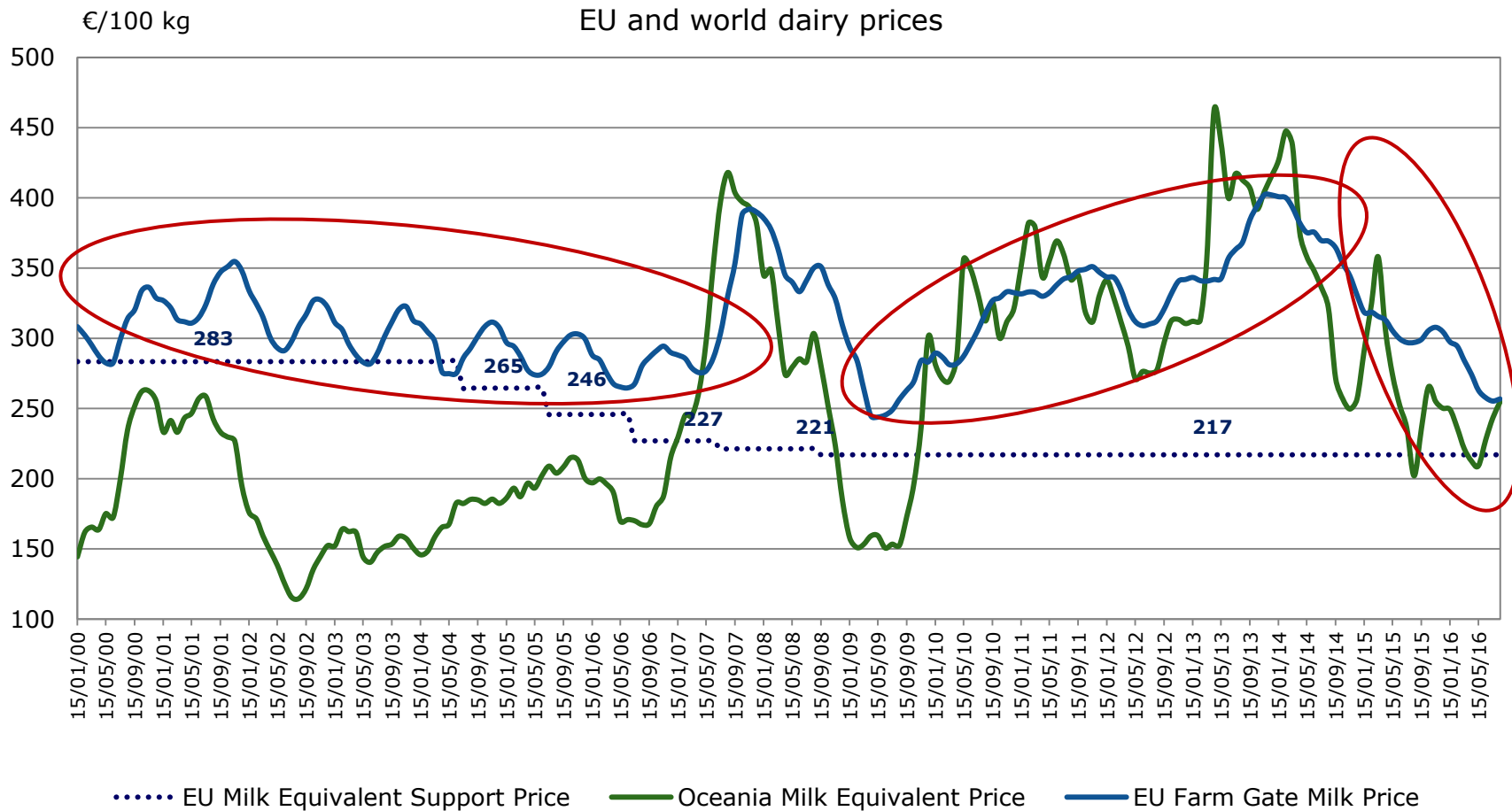
**Brussels, 6-7 December**



## **Outline of issues covered**

- 1. Types of risks affecting EU agriculture**
- 2. CAP measures addressing risks**
- 3. Update of risk-relevant analyses**

## Introducing the recent dairy challenge...



Source: DG Agriculture and Rural Development calculations based on ESTAT and OECD/FAO data.

## ...and placing it in a risk-management context

### **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 that 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 Agricultural 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*

➤ ***Recovery started, but questions on how to avoid similar events in the future (and what to actually avoid) remain***

## What lessons from the dairy crisis?

### Opinions on the causes of risk in agricultural markets differ, namely on

- *The influence and role of external/exogenous versus internal/endogenous factors*
- *The role of market-driven developments against policy-driven interpretations*
- *The role of price volatility and its difference to "excessive" price volatility (and how to define it)*

### Risk management addresses different risks: price-related, production, or income

- *Level of future prices, excessive price volatility, co-movement of commodity prices*
- *Climatic/nature events (drought, flooding, wildlife, etc...), plant and animal diseases, climate change*
- *Increased income variability, farm cash-flow constraints, bottlenecks in the food chain*

### Different policy measures address these risks

- *Price risks are addressed via intervention schemes, futures markets, or contractualisation*
- *Production risks are addressed via insurance schemes, mutual funds, ex-post natural disaster aid,*
- *Income risks are addressed via decoupled, coupled or counter-cyclical support schemes*

➤ ***Whatever lessons learned now need to be translated into forward-looking policy proposals***

## What CAP choices for price risks?

### **The CAP reform process has opted for gradual market orientation**

- *CAP now has measures that increased exposure of farmers to world price fluctuations*
  - *Price gap between EU and world market prices was either closed or reduced*
  - *Agro-food trade turned positive with value-added production main beneficiary*
  - *Income became more volatile, but reversed previous negative trend*

### **Price safety net is still available – but at lower price levels**

- *Public intervention, and exceptional measures, still very much operational*
  - *Public intervention has had very limited use, except during the two dairy crises*
  - *Private storage removed some pressure from the market in cyclical price downturns*
  - *Yet existing measures have limited scope in improvement of their efficiency*

### **Price volatility remains inherent in agricultural production**

- ***Policy question: Is there a different policy mix desirable and feasible?***

# What CAP choices for production risks?

## Ex-ante risk management

- *Measures exist in both Pillars of the CAP*
  - *In sector-specific operational programmes (fruits & vegetables; wine) – Pillar I*
  - *In insurance schemes and mutual funds in Rural Development programmes 2014-20*
    - ❖ *12 RDP's (10 MS) supporting insurance premiums (2.2 billion €)*
    - ❖ *3 RDP's mutual funds (357 mio € economic compensation for animal/plant diseases)*

## Natural disaster aid (mostly ex-post)

- *Compensation is based on both EU and MS funding*
  - *Implemented by MS, mainly through state aids*
  - *Address mainly regionally specific risks*
  - *RD restoration and preventive measures are available (limited to investment aids)*

## Production risks increase output, and thus income volatility

- ***Policy question: Why is the uptake of production-reducing risk schemes limited?***

## What CAP choices for income risks?

### The CAP has chosen to directly support farm income

- *At EU-level via common policy measures*
  - *Via area-based decoupled income support for more than 90% of direct payments*
  - *Via limited voluntary coupled support in sectors presenting production risks*
  - *Via additional targeted aid during crises (Russian ban, dairy and livestock sectors)*

### RD measures have expanded the possibility of income support

- *At MS-level via new or enhanced instruments in RD*
  - *Income Stabilisation Tool included in Rural Development Programmes for 2014-2020*
  - *Limited uptake - 3 IST's (Italy, Hungary, Castilla y Leon) totalling €130 million*
  - *Questions have been raised about the conditionality of the measure*

### Income volatility is expected to continue, or even increase in the future

- **Policy question: Why is the uptake of different income support schemes limited?**



# What reasons explain limited uptake of IST in RD?

## Budget unpredictability

- *Annual structure of budget rules excludes such schemes from Pillar I*
- *Significant amounts of funds need to be blocked with uncertainty on their use*
- *Despite caveats, direct support presents more certainty, thus limiting scope in RD*

## Definition of income in Basic Act

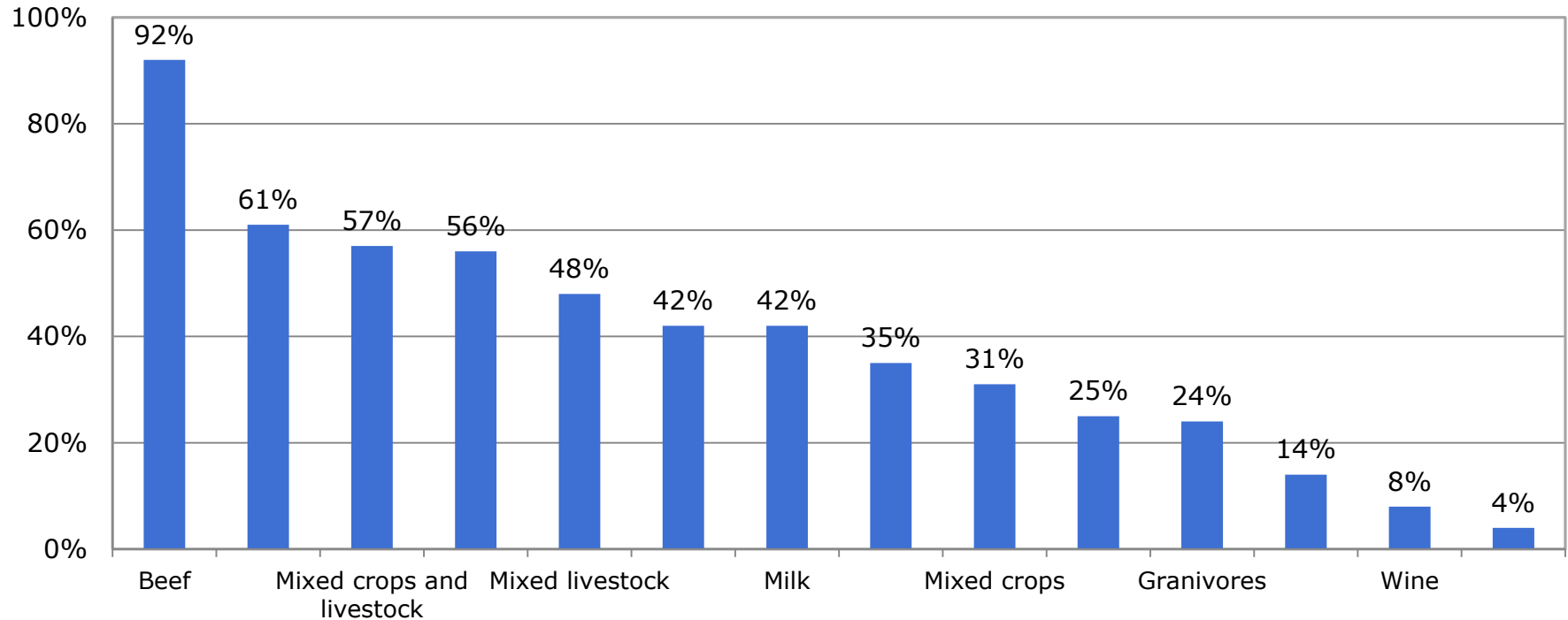
- *Income is defined as total revenues + public subsidies – input costs*
- *High reliance of some sectors on total public support (e.g. livestock, dairy)*
- *Thus, even in severe market crises, the trigger would not easily be activated*

## WTO Green Box requirements

- *Targeting of specific sectors is not possible*
- *Income trigger of a minimum loss of 30% has to be respected*
- *Need to calculate income losses at individual farm level (use of indices not allowed)*

## The role of subsidies in EU farm income by sector

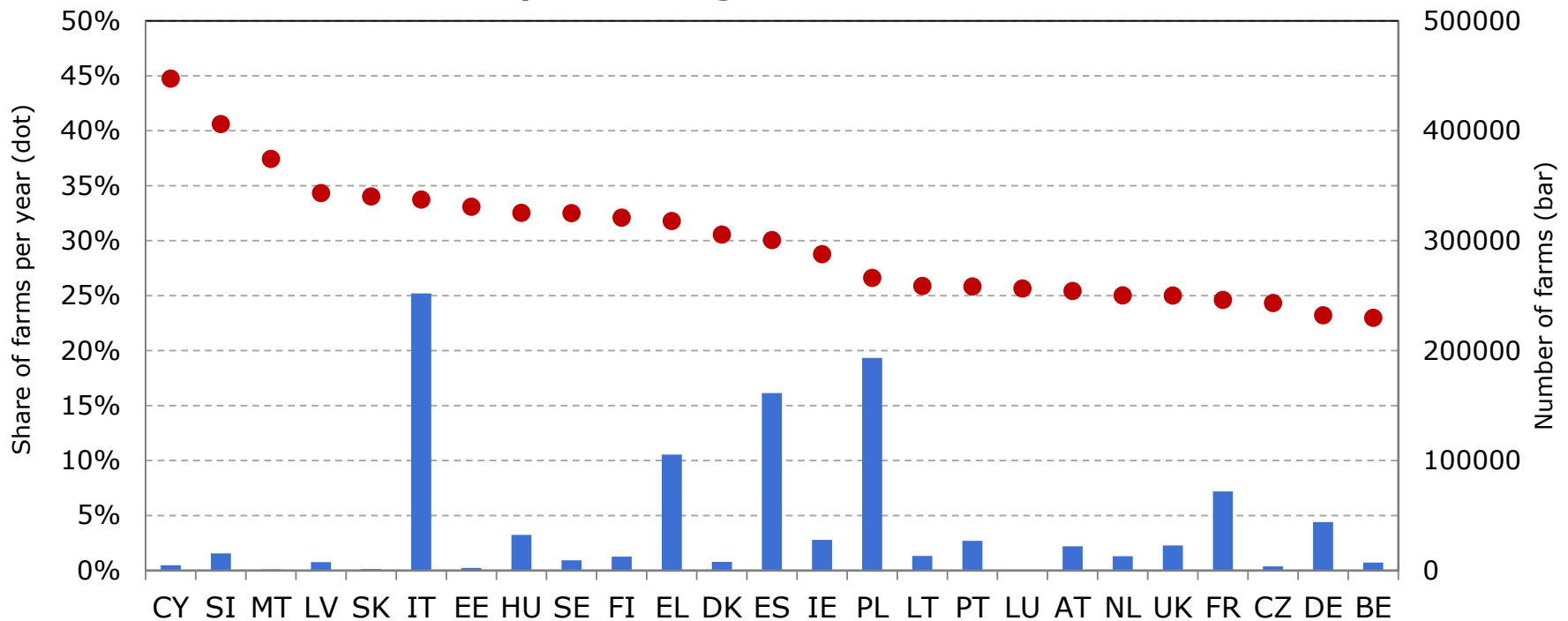
**Proportion of subsidies (excluding on investments) to farm income (FNVA) by type of farming (avg 2007-2013)**



Source: DG Agriculture and Rural Development calculations based on FADN.

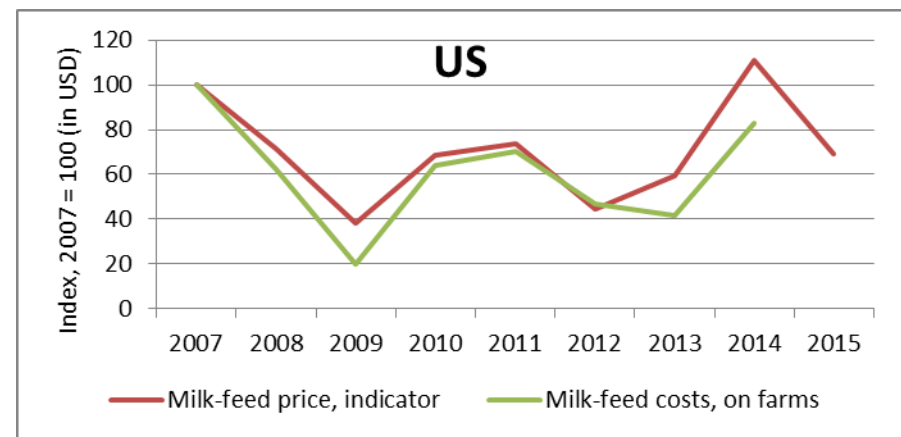
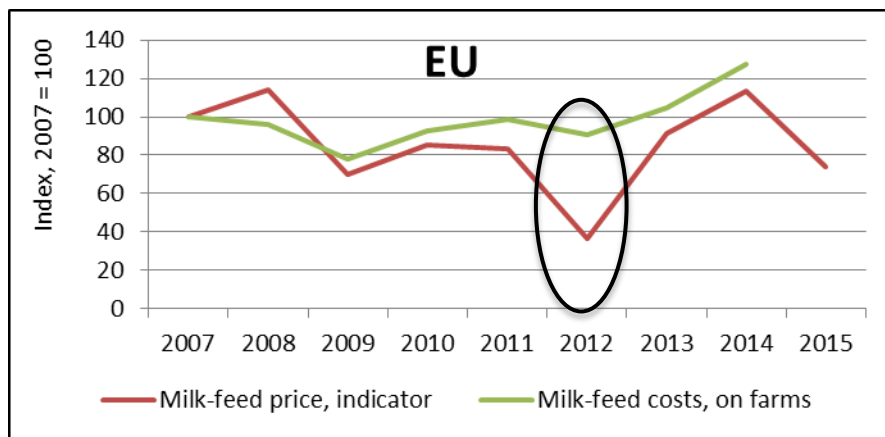
# Share of farms with income losses exceeding 30% - by MS

**Number and % of farms where  
farm income (FNVA) losses exceed 30%  
per MS, avg 2007-2013**



Source: DG Agriculture and Rural Development calculations based on FADN.

## A US-type indicator reflects US farm reality

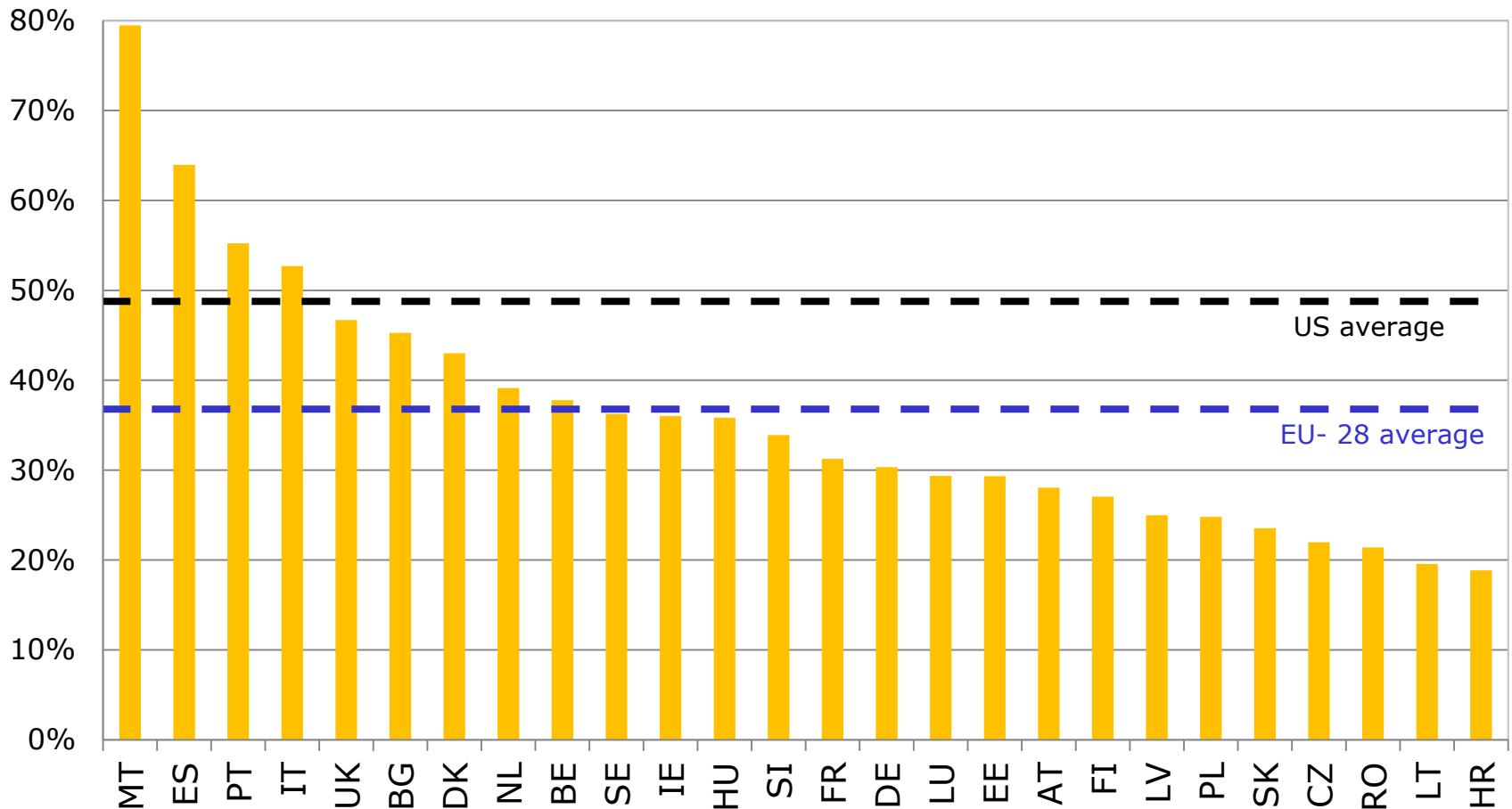


Source: DG Agriculture and Rural Development calculations based on ESTAT, FADN and USDA/ERS.

### Why?

- The US indicator accounts for hay (up to 28% of the ration), whose price varies much less than maize and soymeal prices
- EU farmers sell milk at current (monthly) market price, buy feed when prices are low, don't use futures
- When feed prices are high, farmers adapt rations to reduce costs (farmers have ways to adapt!)
- Purchased feed weighs less in EU systems than in the US

## Share of purchased feed in operating costs by MS



Source: DG Agriculture and Rural Development calculations based on FADN and ERS/USDA.

## The "take away" messages

### Caveats of an EU-wide Income Stabilisation Tool

- *Too big administrative burden, huge technical difficulties to implement at EU level*
- *A system of monitoring individual farm income developments would be needed*
- *It implies important redistribution of support, in favour of only a few Member States*

### The update of analysis confirms previous conclusions

- *Smaller economic sizes report higher income losses (but also depend more on DP)*
- *Higher income volatility does not necessarily affect sectors with high income pressure*
- *Very significant differences exists among MS, reflecting their different structures*

### To increase the actual uptake by MS for ISTs, what is needed is

- *To explore the possibility and feasibility for sector-specific IST (Omnibus proposal)*
- *Lowering the income loss trigger or focus on market revenue (Omnibus proposal)*
- *Explore the requirements to introduce and use of indices (market transparency essential)*

➤ ***Whatever final choices are made, a distinction needs to be made between the complementarity or the trade-offs between different policy options***

Reports and data available at:

[http://ec.europa.eu/agriculture/index\\_en.htm](http://ec.europa.eu/agriculture/index_en.htm)

[http://ec.europa.eu/agriculture/policy-perspectives/impact-assessment/index\\_en.htm](http://ec.europa.eu/agriculture/policy-perspectives/impact-assessment/index_en.htm)

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[http://ec.europa.eu/agriculture/markets-and-prices/index\\_en.htm](http://ec.europa.eu/agriculture/markets-and-prices/index_en.htm)

**Thank you for your attention!**