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Prospects for agricultural markets in the European Union

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DG AGRI Economic analysis of EU agriculture

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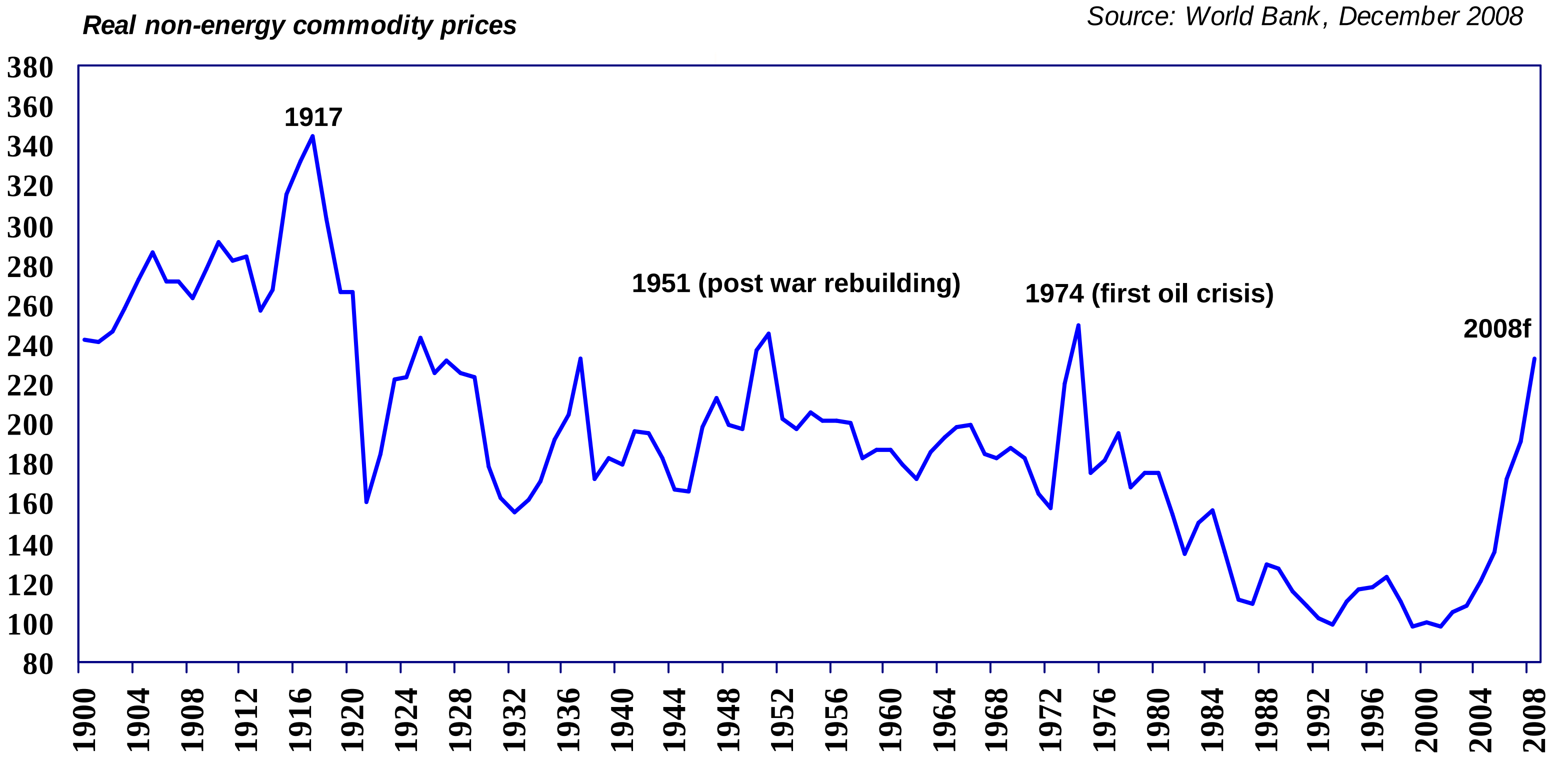
Outline

- ***Short-term market developments: from boom … to bust***

- ***The medium-term perspectives for EU agricultural markets***
  - ***Cereals***
  - ***Meat and dairy sectors***

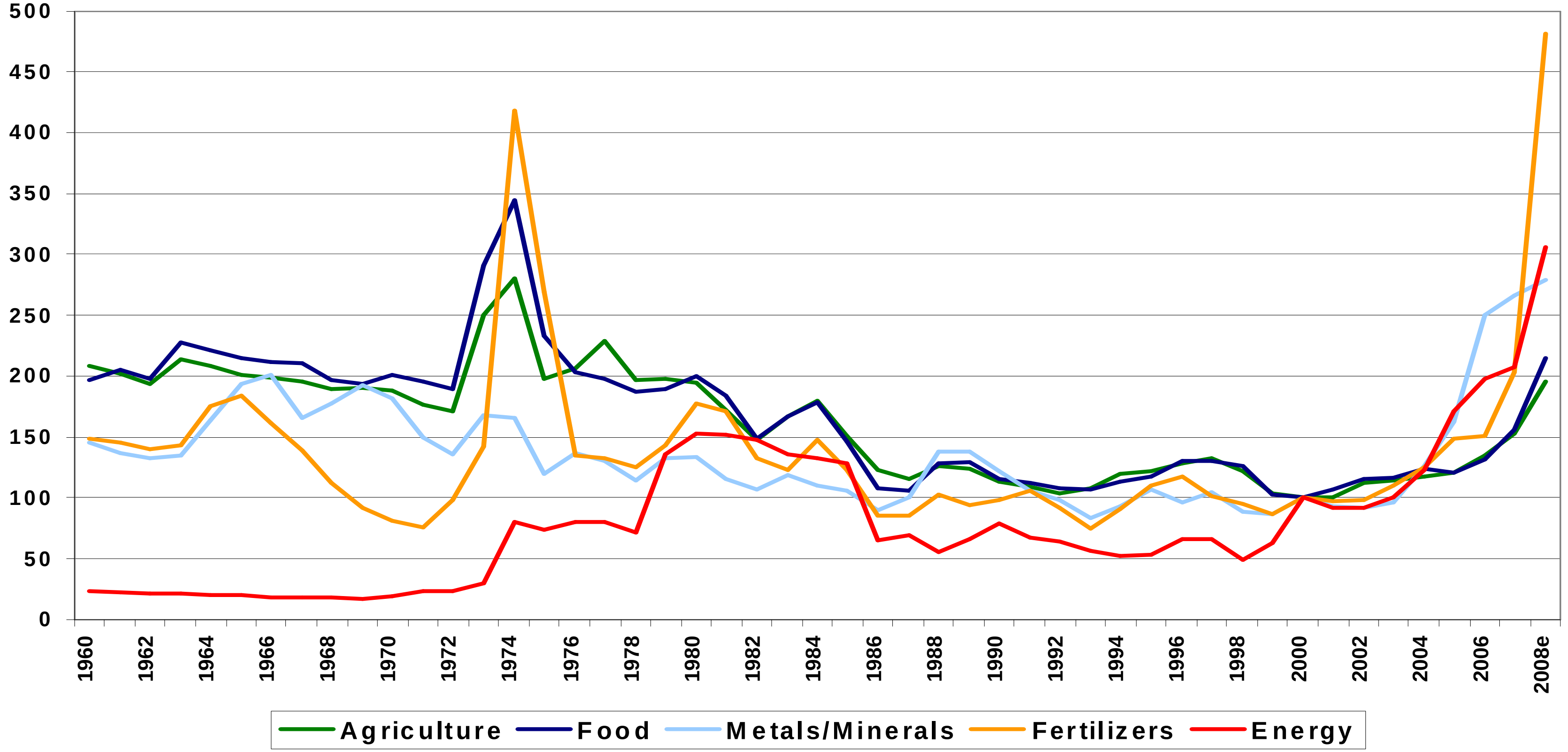
- ***Main uncertainties***

The "longest/largest bubble since 1900" (WB)...



… driven mainly by the non-agricultural commodities …

Real commodity price indexes (1960-2007)



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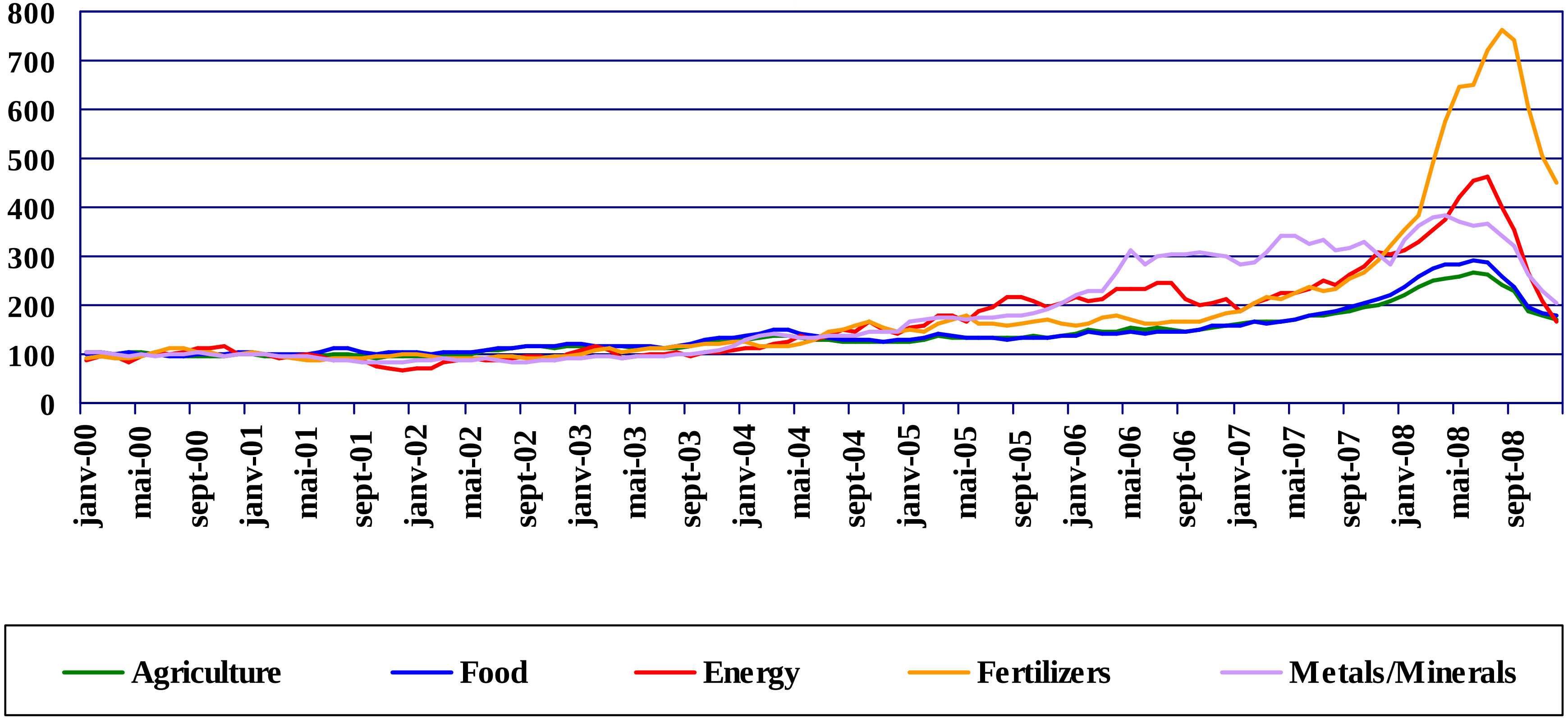
…has finally burst

In current prices

Source: World Bank, January 2009



In the agricultural sector, the price boom was driven by a series of factors whose contribution varies across the agricultural sectors (food grains vs. maize/oilseeds)

- ***Structural factors ➔ their impact to continue over the medium-term***
  - Gradual rise in global food demand, emergence of biofuel sector, slow down in world food crop yield, characteristics of agricultural markets/products (thin markets, slow adjustment capacity, inelastic S & D)

- ***Short-term factors ➔ their impact to decline over the medium-term***
  - Series of adverse climatic conditions, restrictive trade behaviour of some exporting countries, impact of investment funds on commodity markets, low stock levels and rise in energy prices

Then prices declined sharply in response to ...

- Strong **producer response** to high prices (additional production factors, e.g. land, and higher production intensity mobilised globally particularly in the developed world, e.g. dairy, wheat, oilseeds …)

- and the **rapid policy responses** (e.g. EU removal of mandatory set-aside of arable land, suspension of cereal import duties, dairy quota increase)

- before gathering pace in the wake of increased nervousness and uncertainty about **economic outlook** and turbulence in financial markets

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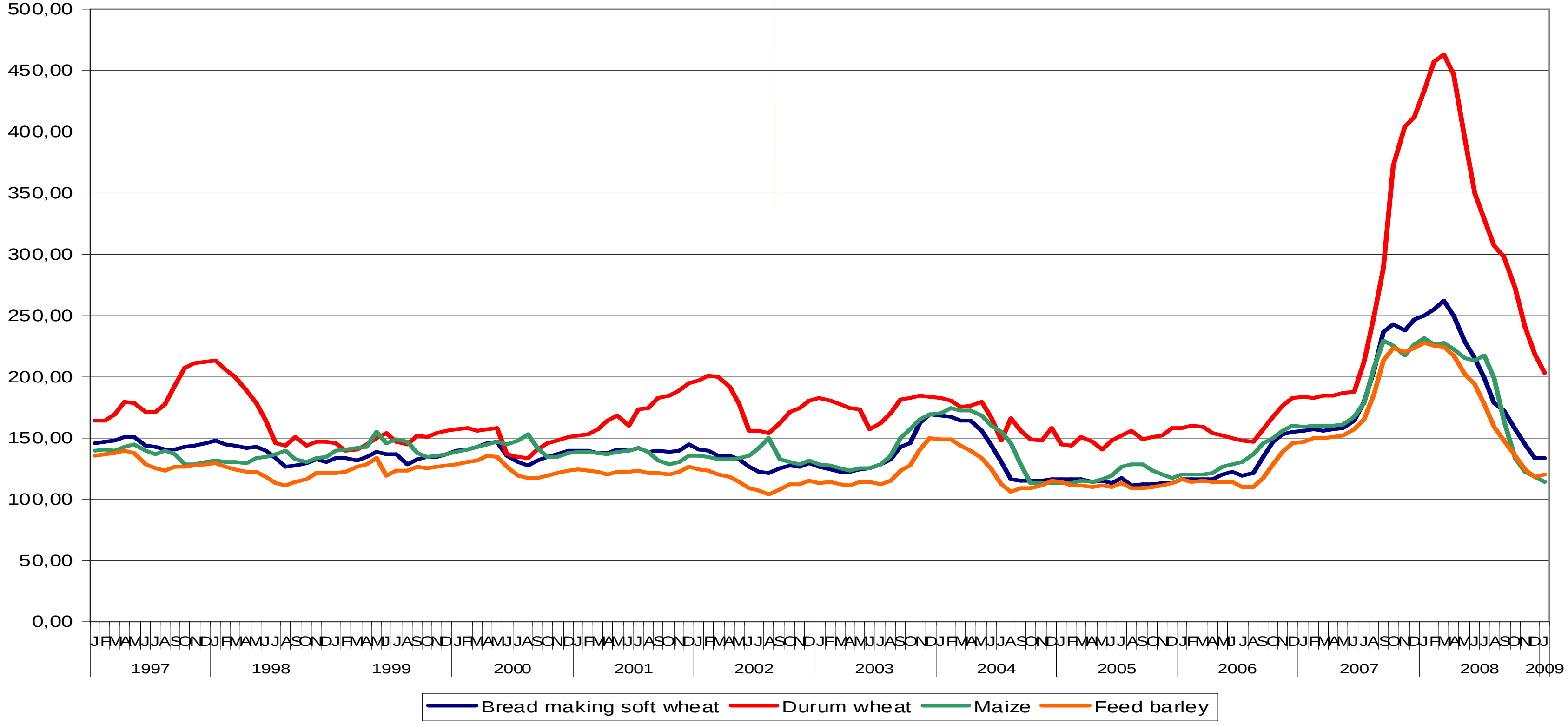
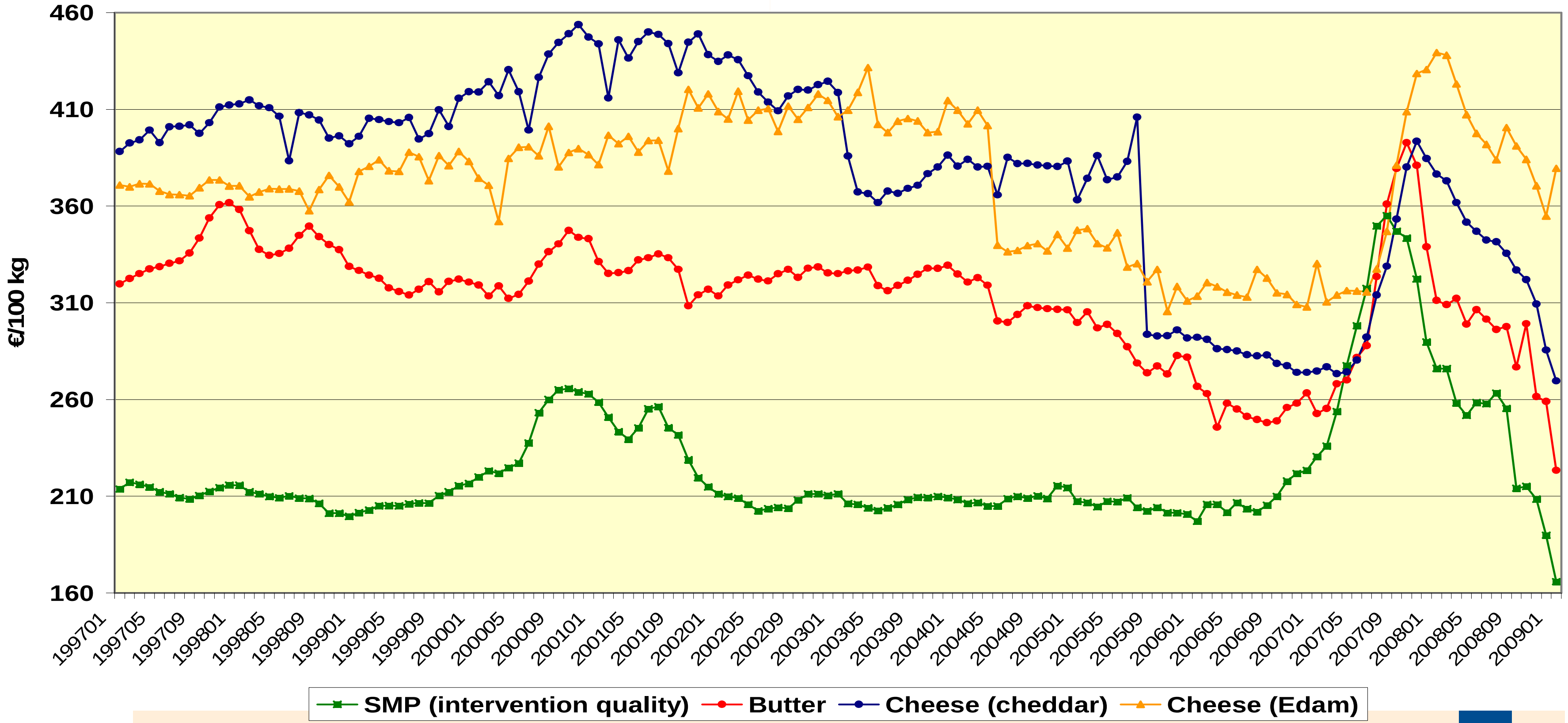
The prices of cereals have fallen very sharply since Spring 2008 in the EU (by more than 40%) ...



... whereas EU dairy prices dropped dramatically

Monthly EU dairy market prices (in €/100 kg, 1997-2009)



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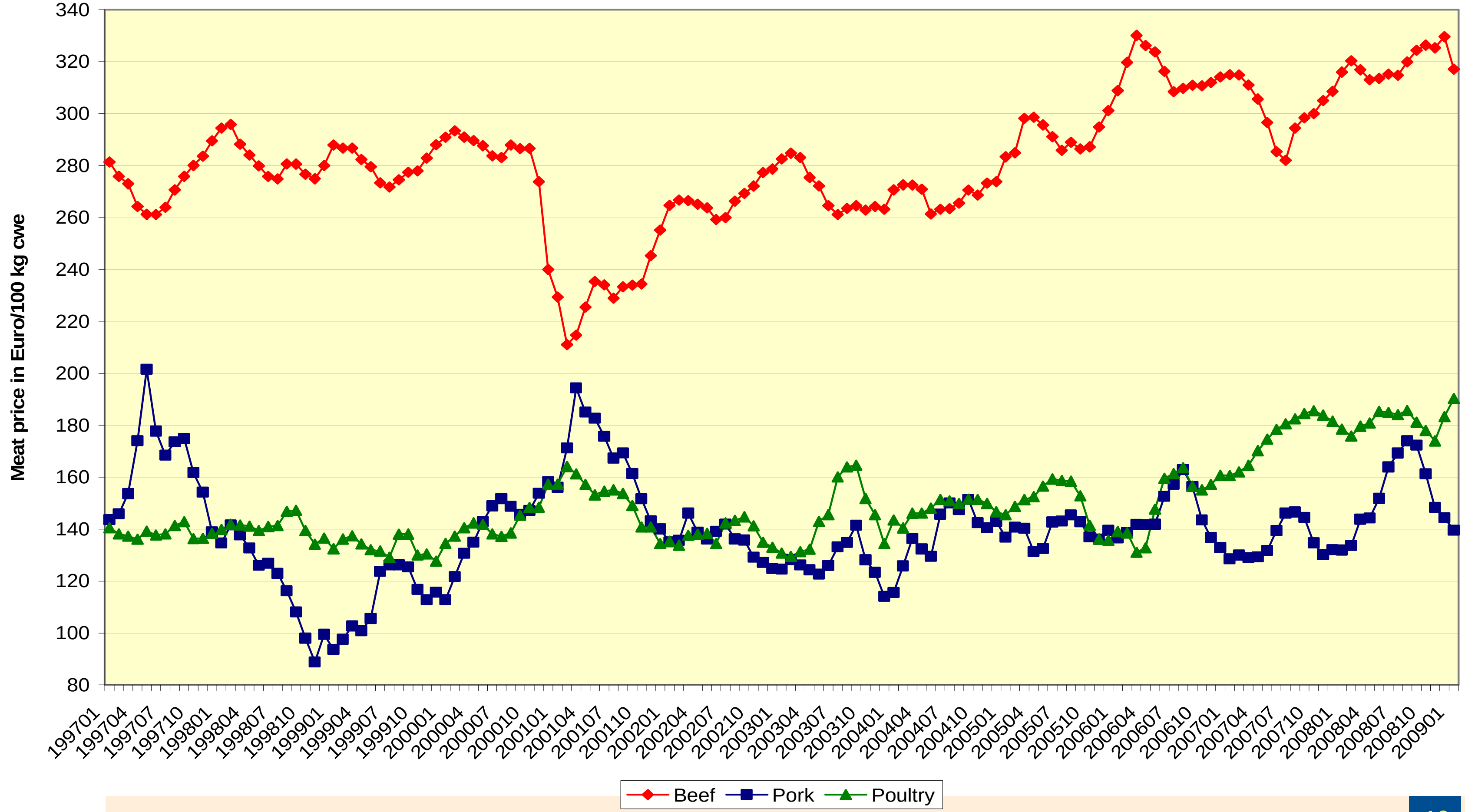
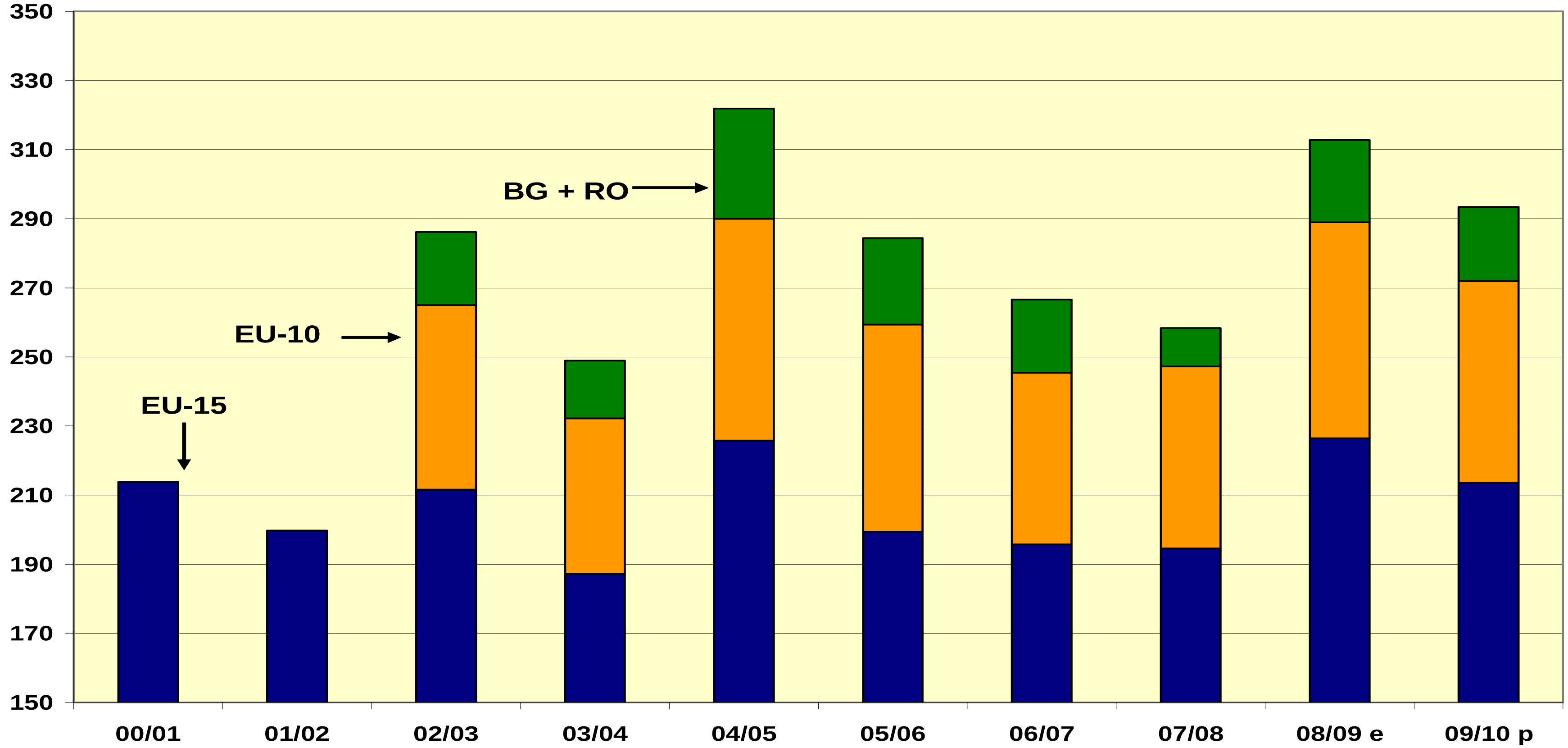
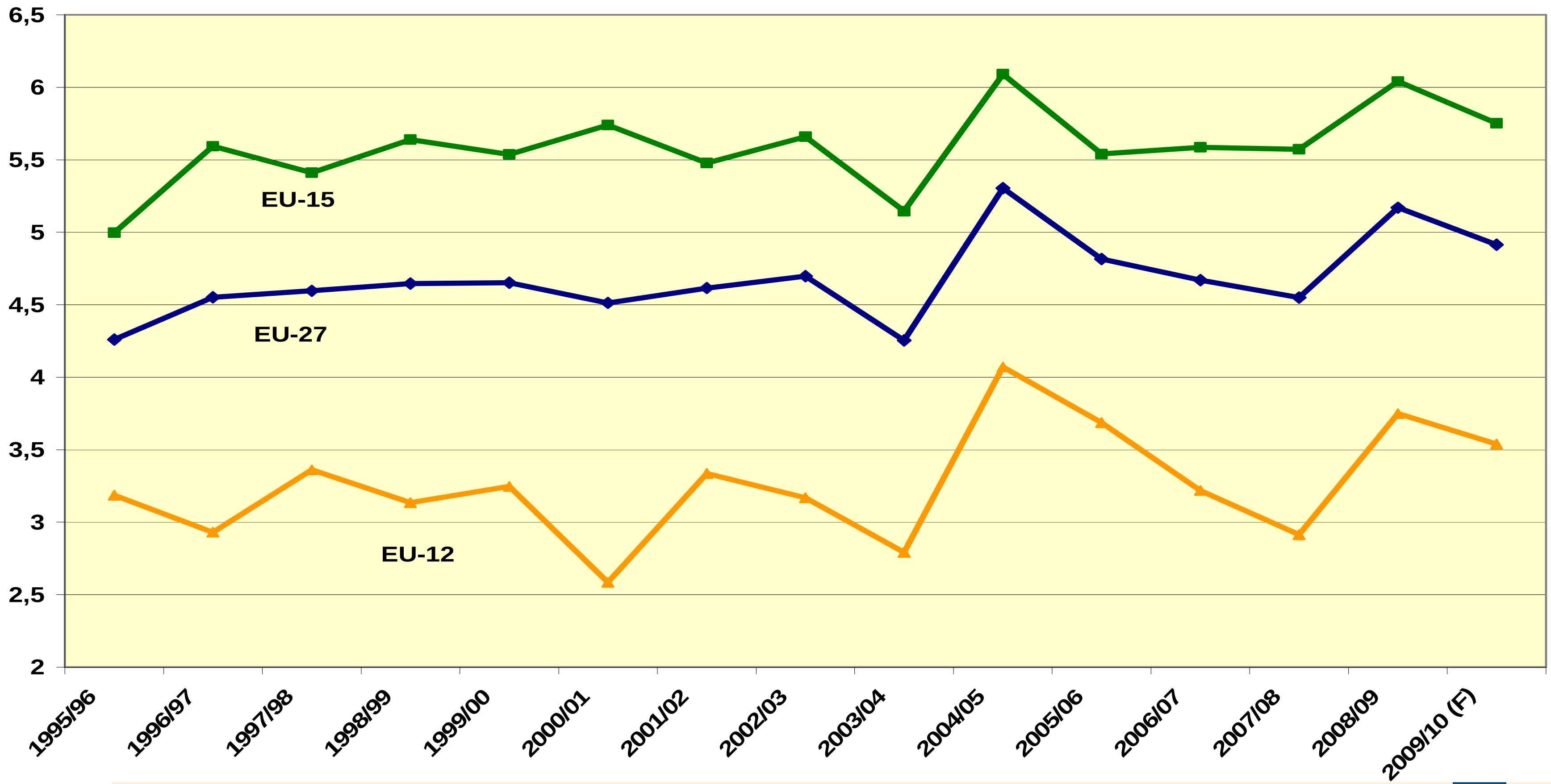
... with diverging situation in the animal sector



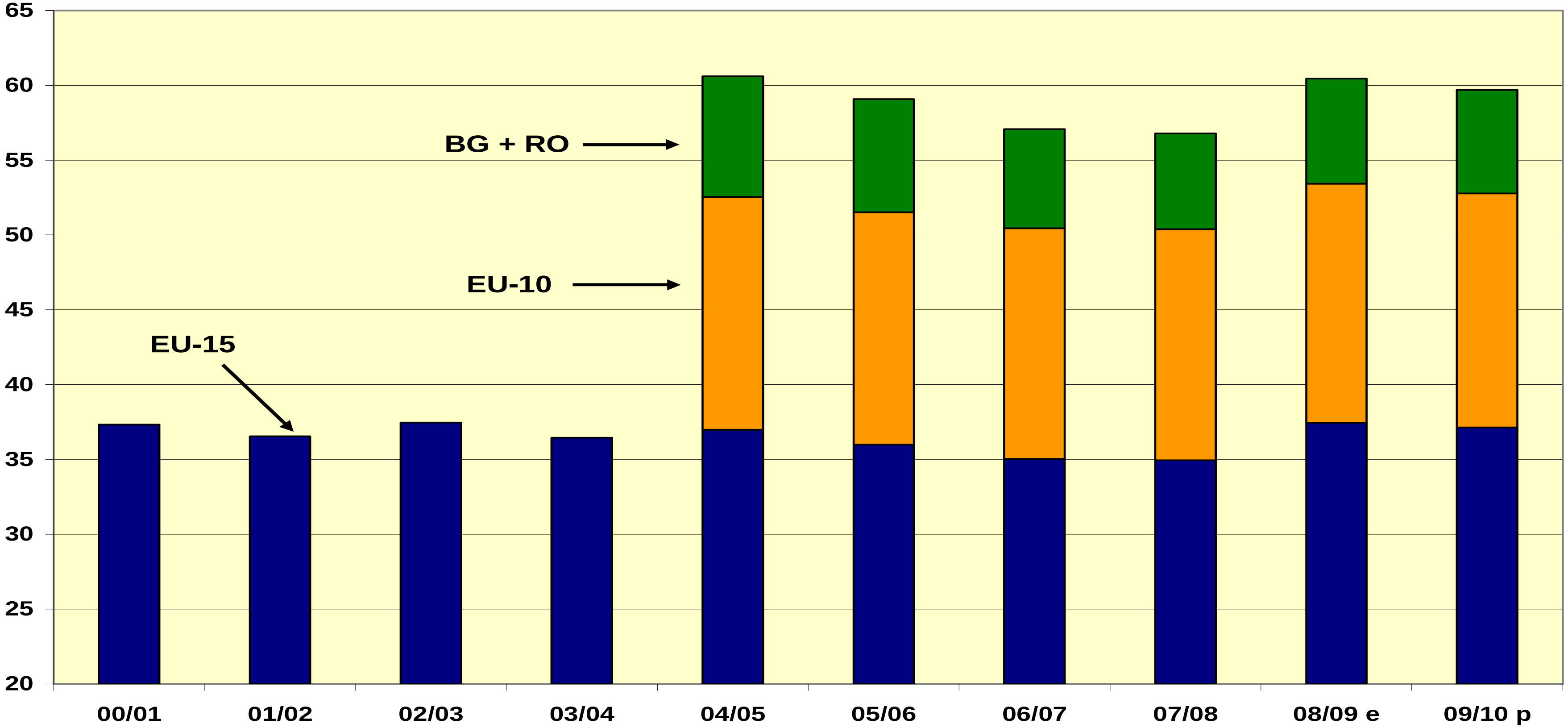
The strong increase in EU cereal production in 2008 (+54 mio t) should trigger a significant rise in stocks (+18 mio t) by June 2009



… thanks mainly to a significant rebound in cereal yields



… but also to an increase in cereal area



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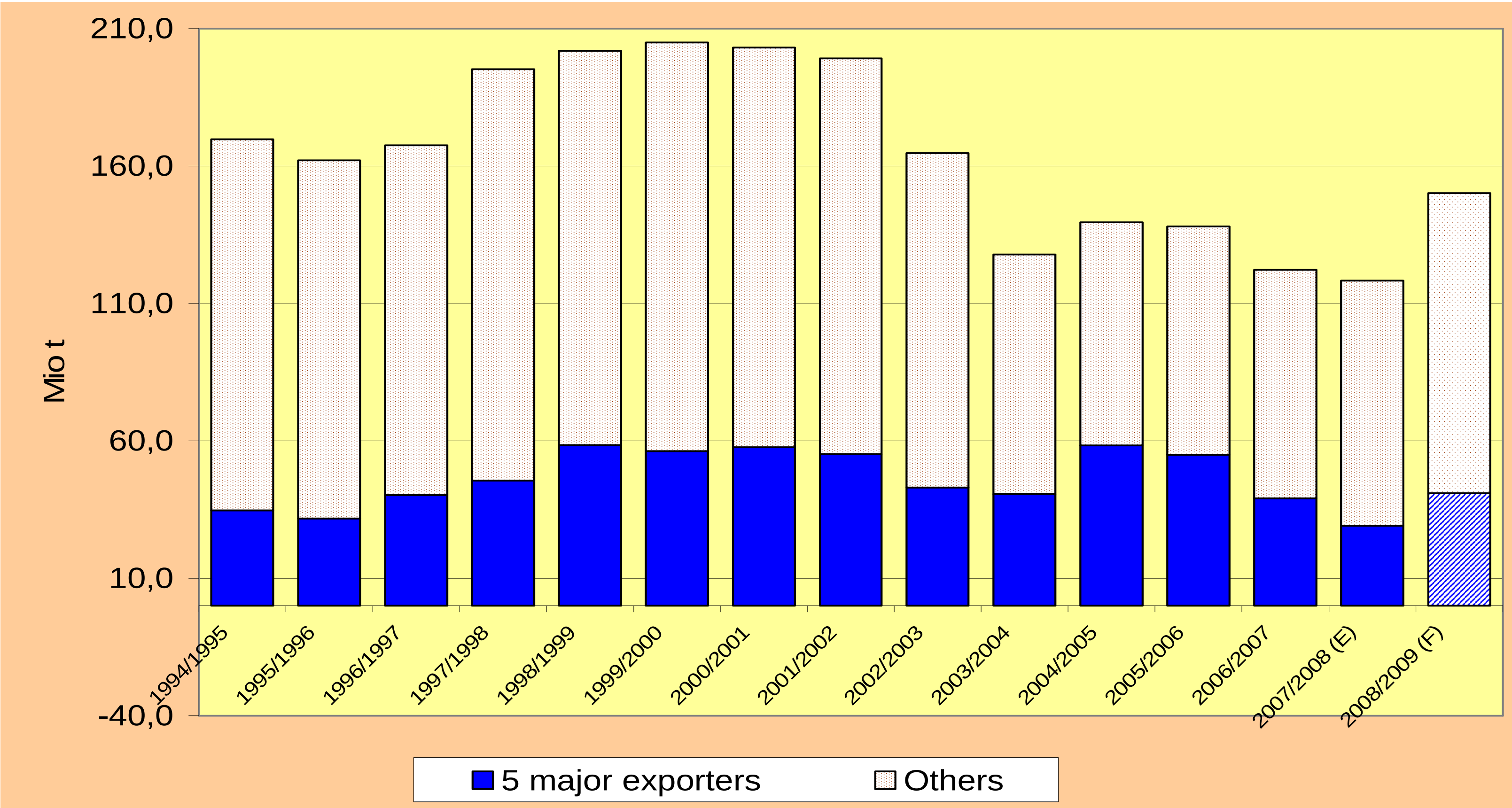
However despite an improvement, the situation for world wheat stocks remains fragile



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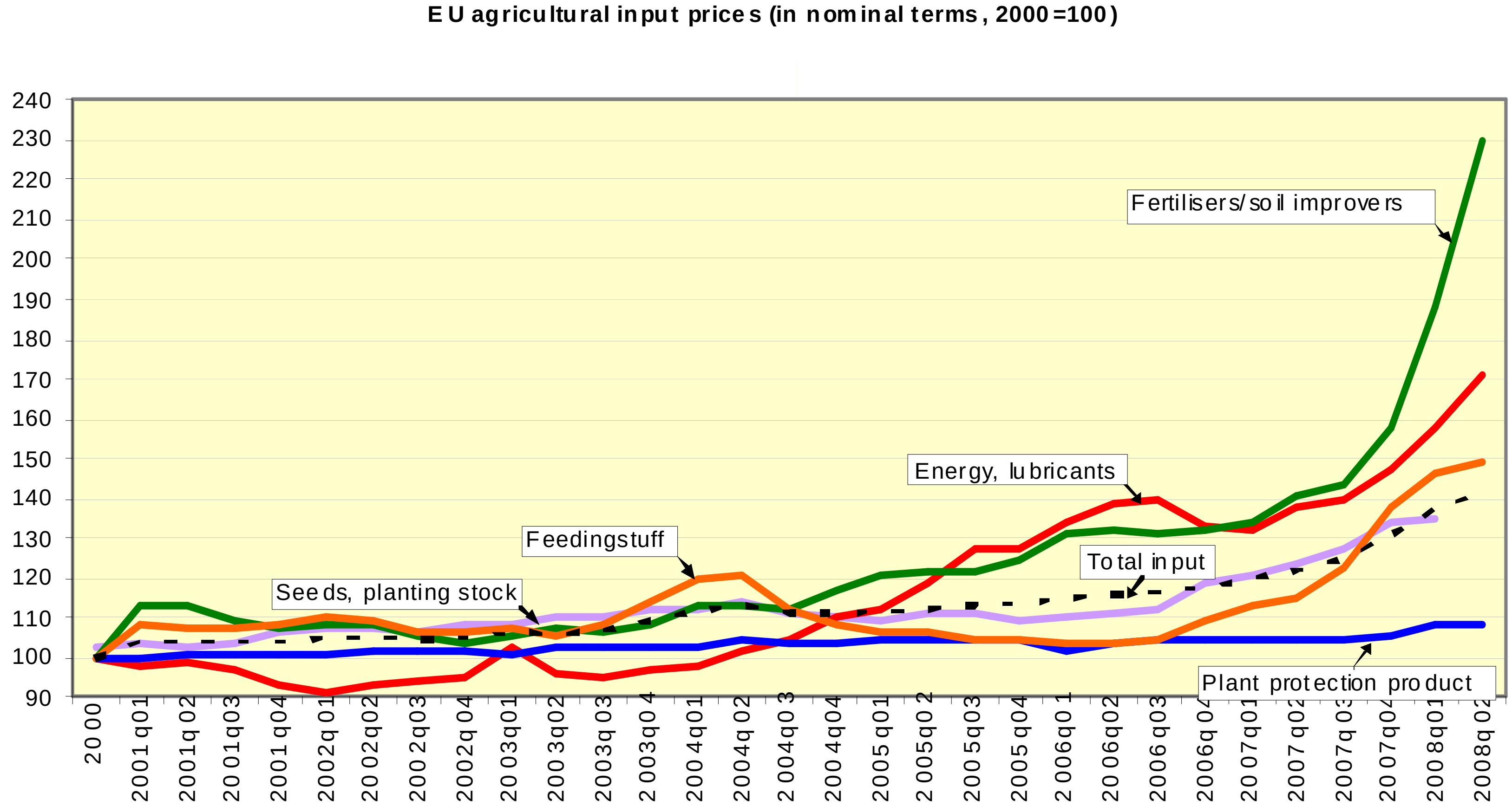
Impact of lower output prices exacerbated by high input prices: risk of price squeeze



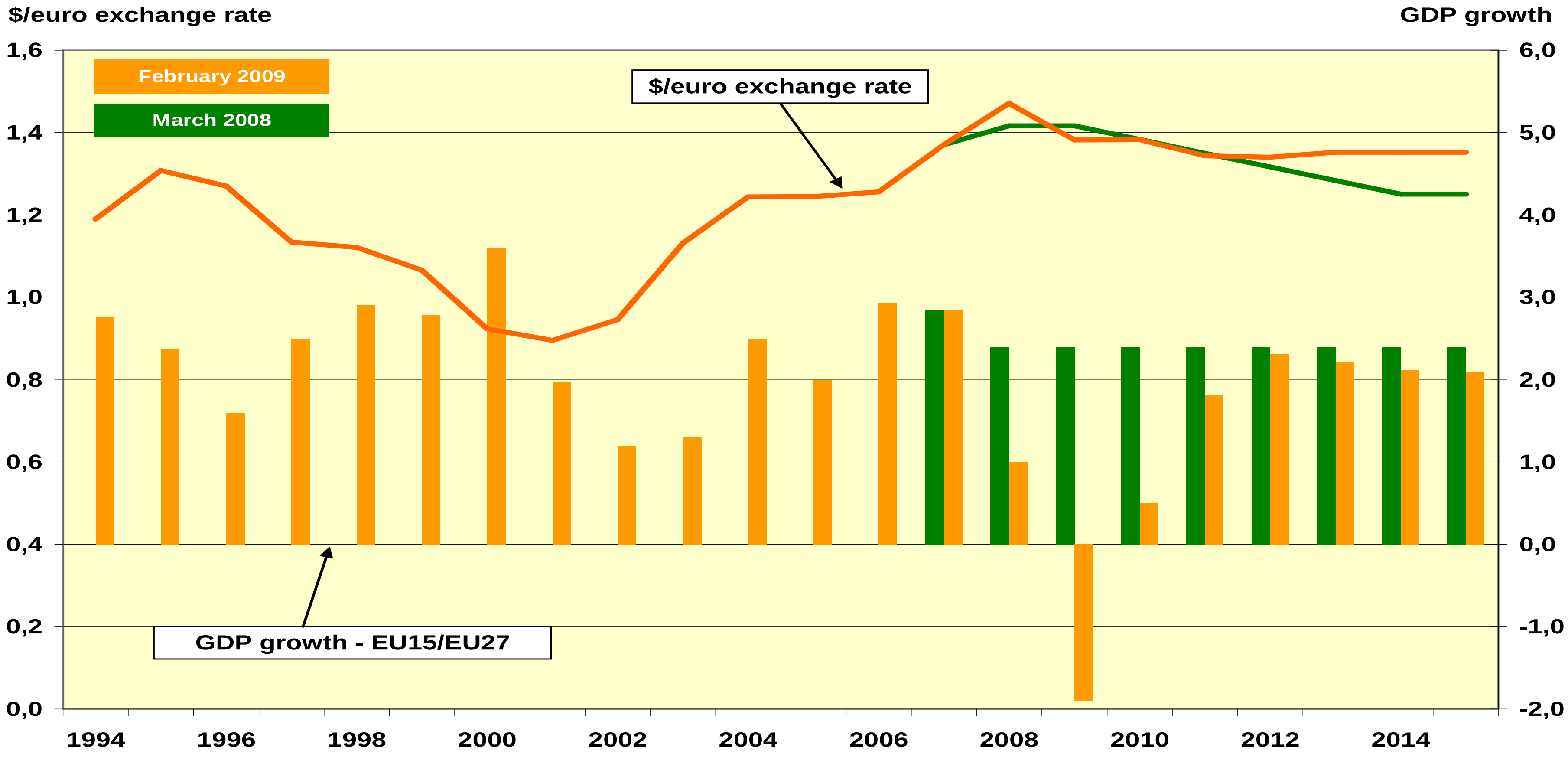
The market outlook over the medium-term should largely depend on

- The pace of recovery from the economic crisis
- The policy environment
- Structural factors that should sustain market prospects
  - *the increase in global food demand*
  - *the emergence of the biofuel sector*
  - *the long-term slow down in productivity growth in many sectors*
- Higher input costs (energy and fertiliser prices) should lift commodity prices
- Low stock levels

Potential impact of the economic crisis

- ***Features of the economic crisis***
  - Severity undeniable – will be deeper and last longer than all previous post-war
  - Path of recovery still unknown – especially on future consumption patterns
- ***Impact on agricultural markets***
  - Unclear yet if long-term trends have changed
  - Small annual changes in GDP growth could have significant long-term effects
  - Uncertainty not only affects output prices, but input prices as well
- ***Impact on EU agriculture***
  - Potential impact on asset values and financial situation of farms
  - Asymmetric impact by MS (net budgetary position)

Economic growth revised sharply downwards compared to March 2008



Prospects for EU cereal markets are relatively positive

1. Cereal prices are projected to be sustained (expanding biofuel demand and exports, moderate yield growth and low stocks)
2. Low risk of (regional) imbalance on EU cereal markets
3. Changing price relations in favour of coarse grains (maize and barley)
4. … but greater risk of price fluctuations

… but more modest perspectives for the meat sector

1. Beef sector to continue its long-term decline with declining production (falling dairy herd, impact of sanitary crisis, impact of decoupling policy)
2. Pork sector to show moderate growth driven by domestic demand
3. Poultry sector to become increasing net importer as demand grows faster than production
4. Sheep sector to continue its declining trend

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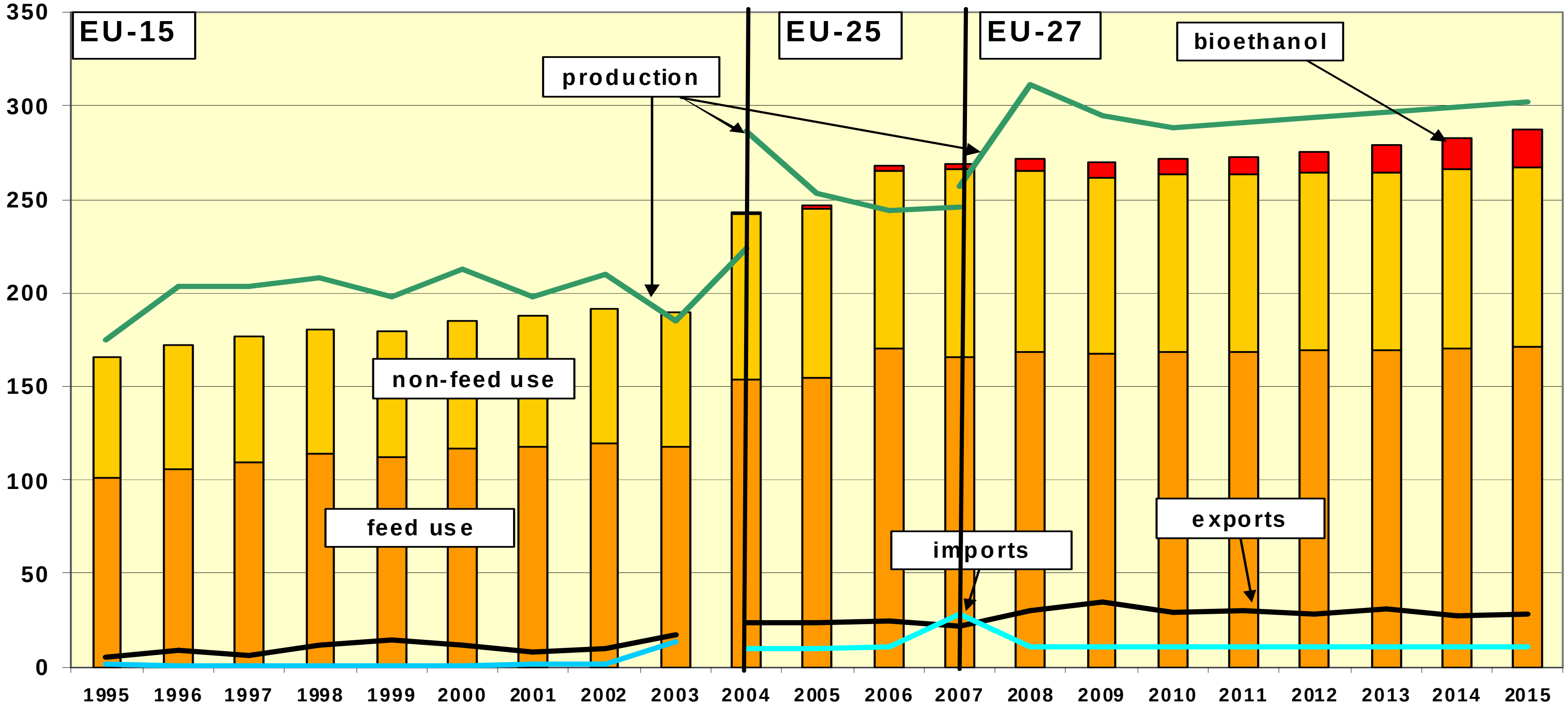
Slightly expanding EU cereal markets and emerging bioethanol markets….

Development of cereal markets in the EU, 1995-2015 (mio t)



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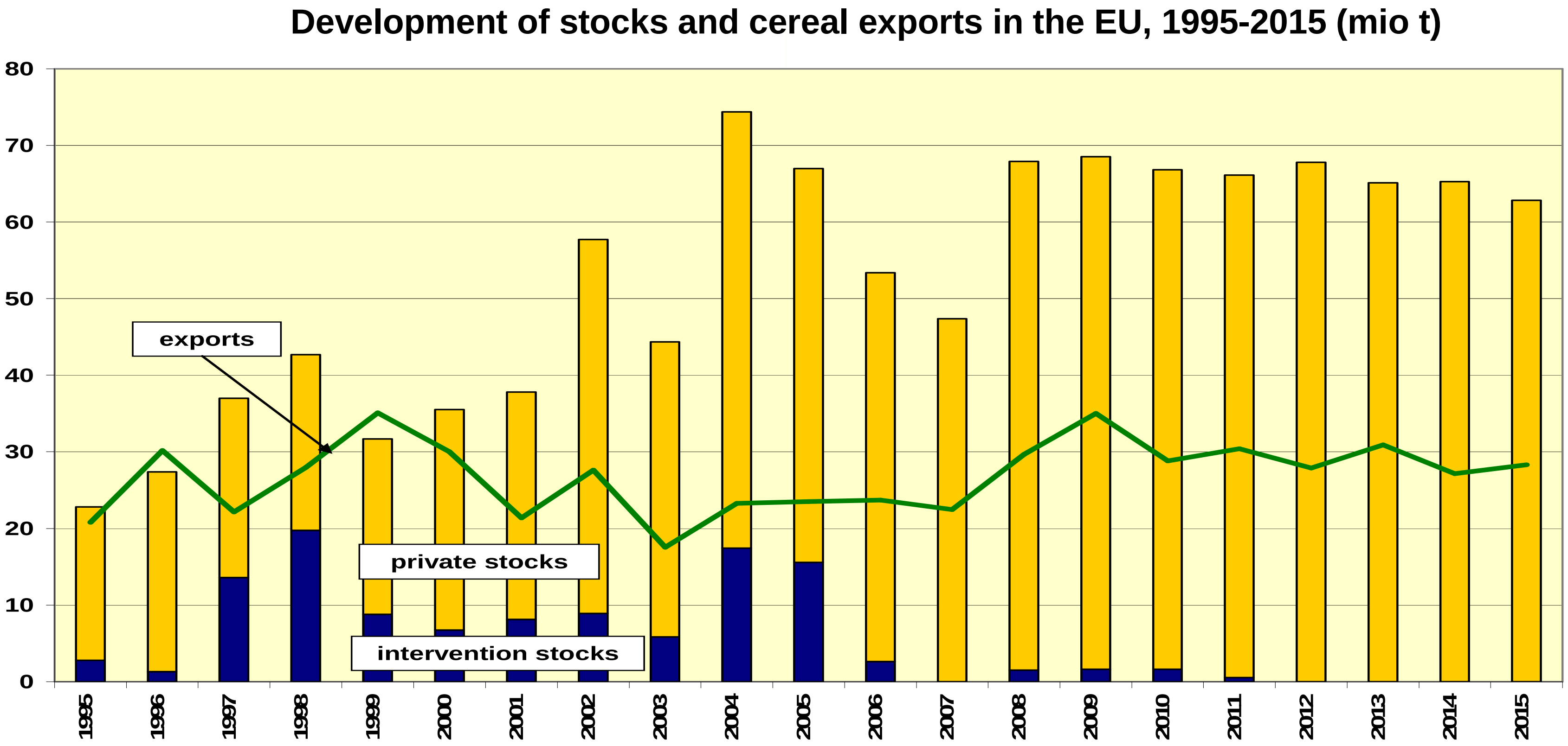
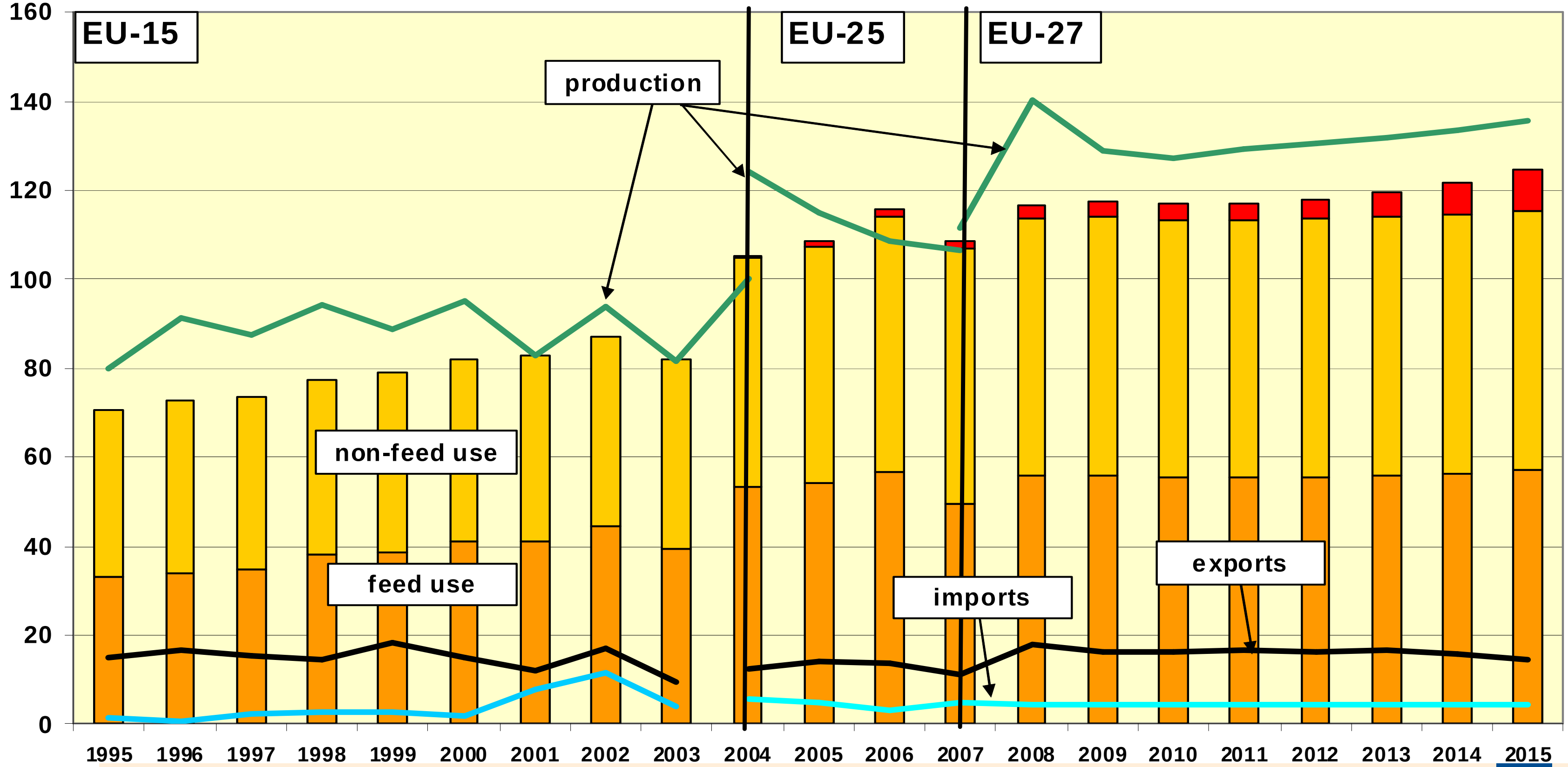
… would lead to a return to relatively modest levels of stocks on EU cereal markets ….

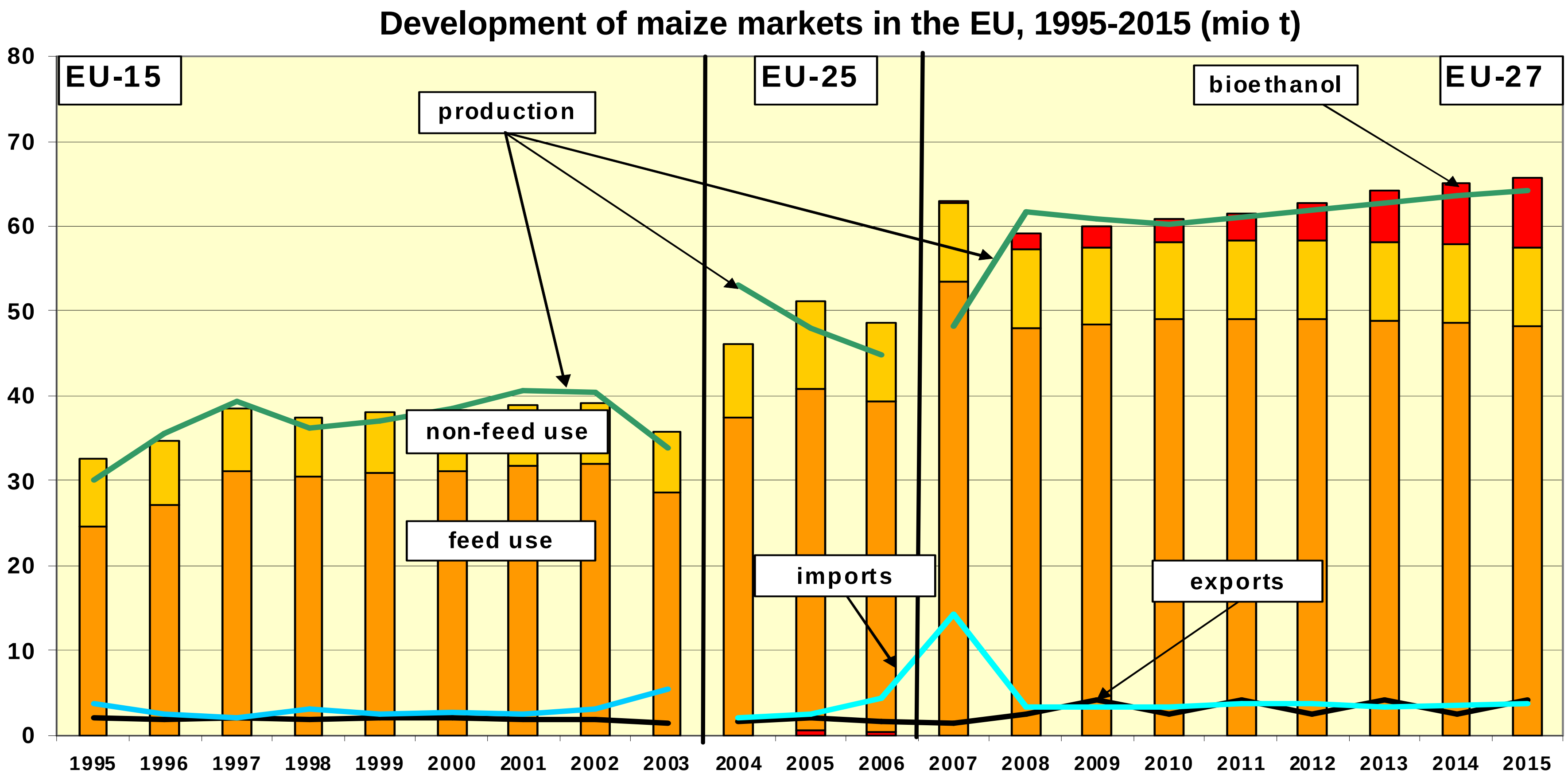


… mainly driven by the wheat markets….

Development of wheat markets in the EU, 1995-2015 (mio t)

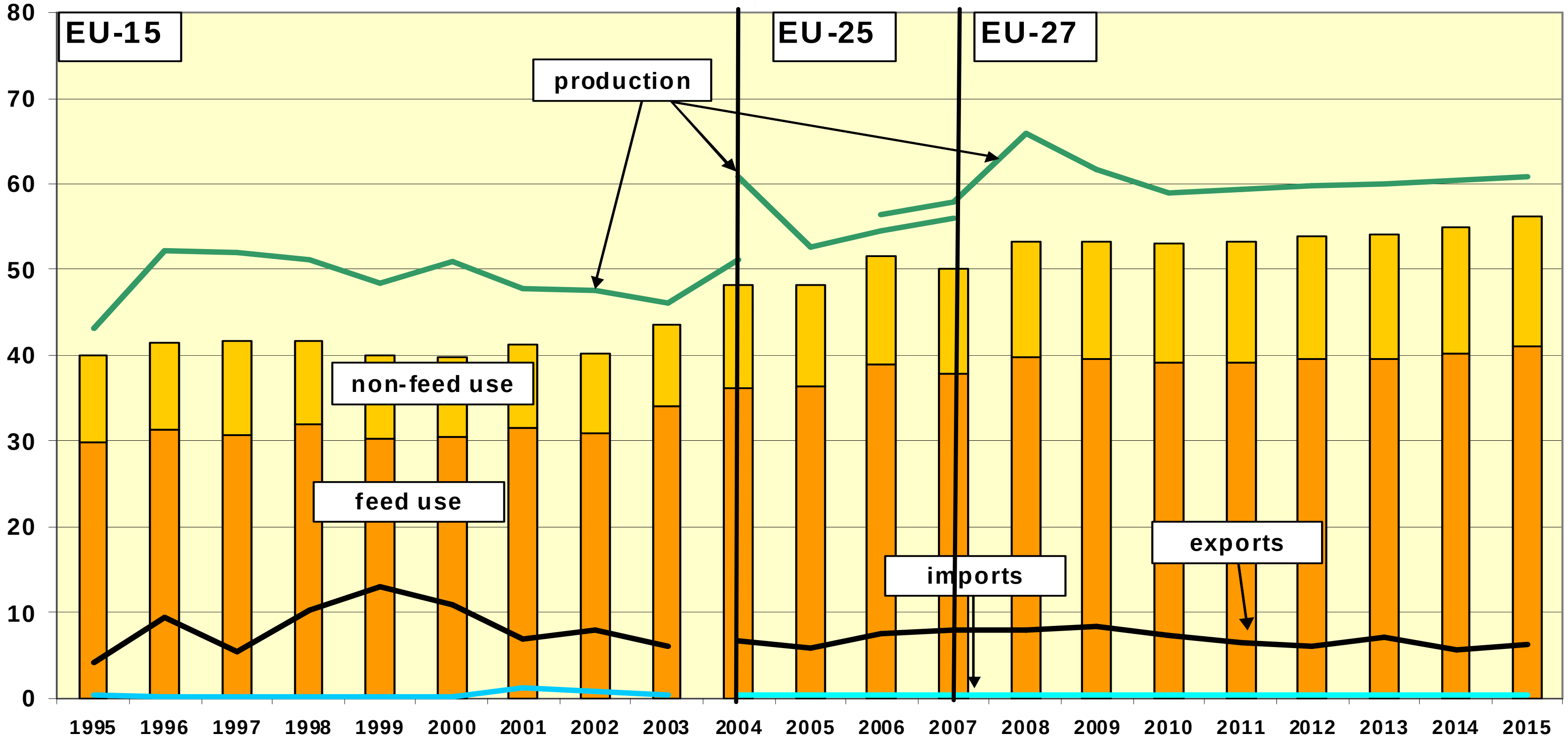


and the maize markets ….



… whereas the barley markets would stabilise ….

Development of barley markets in the EU, 1995-2015 (mio t)



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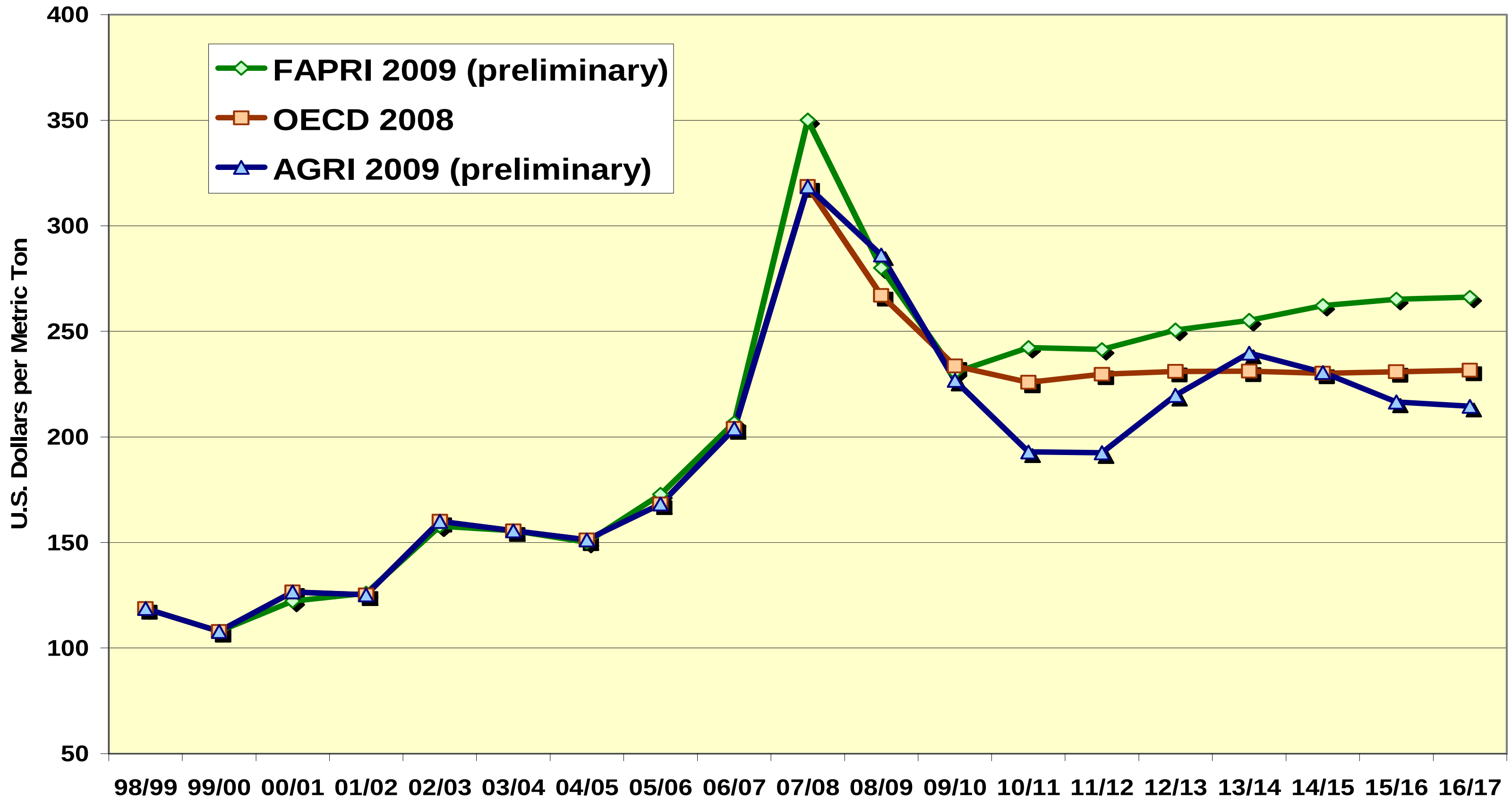
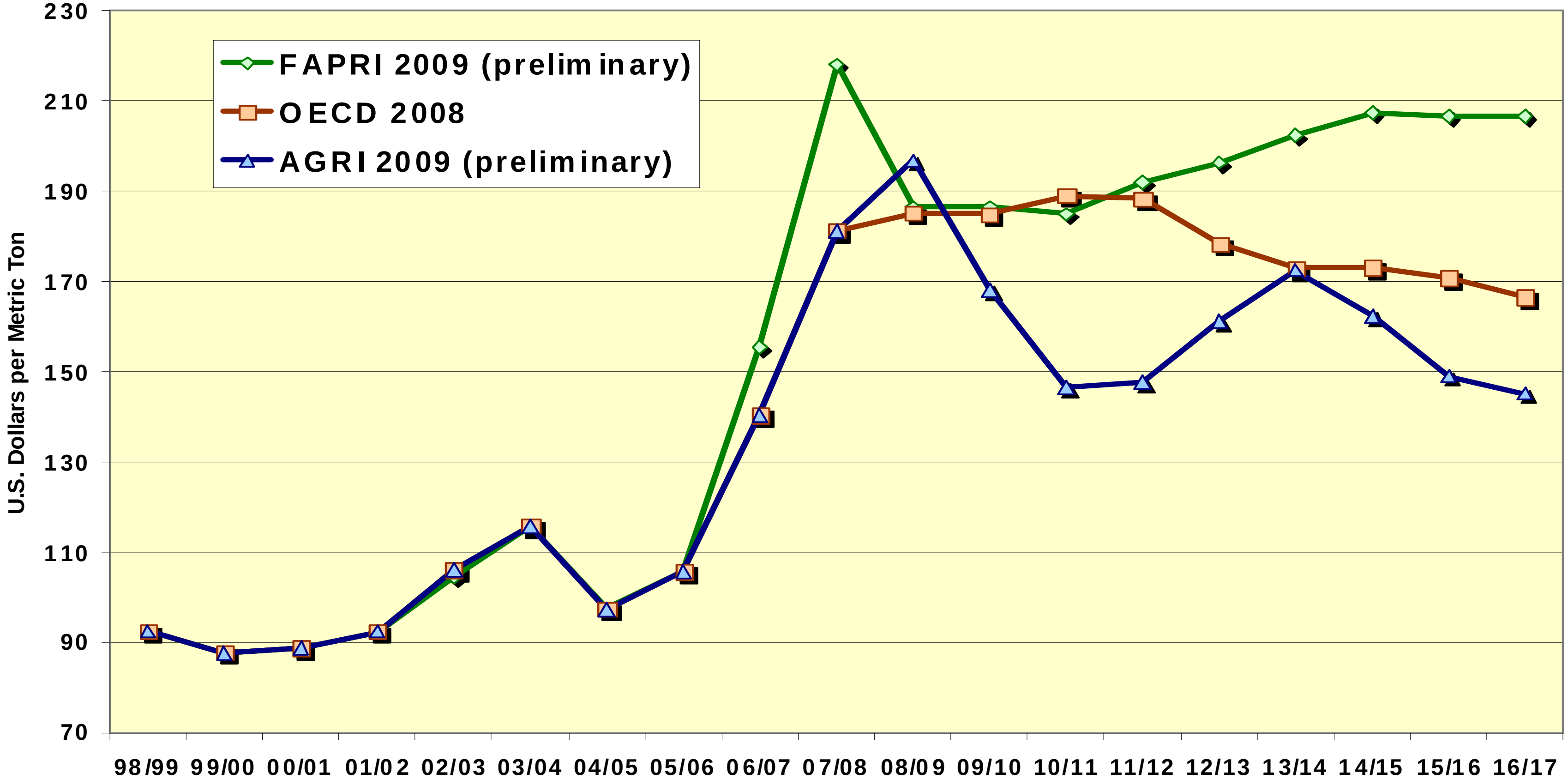
Projected world wheat prices over the medium-term

(HRW US Fob Gulf, $/t)



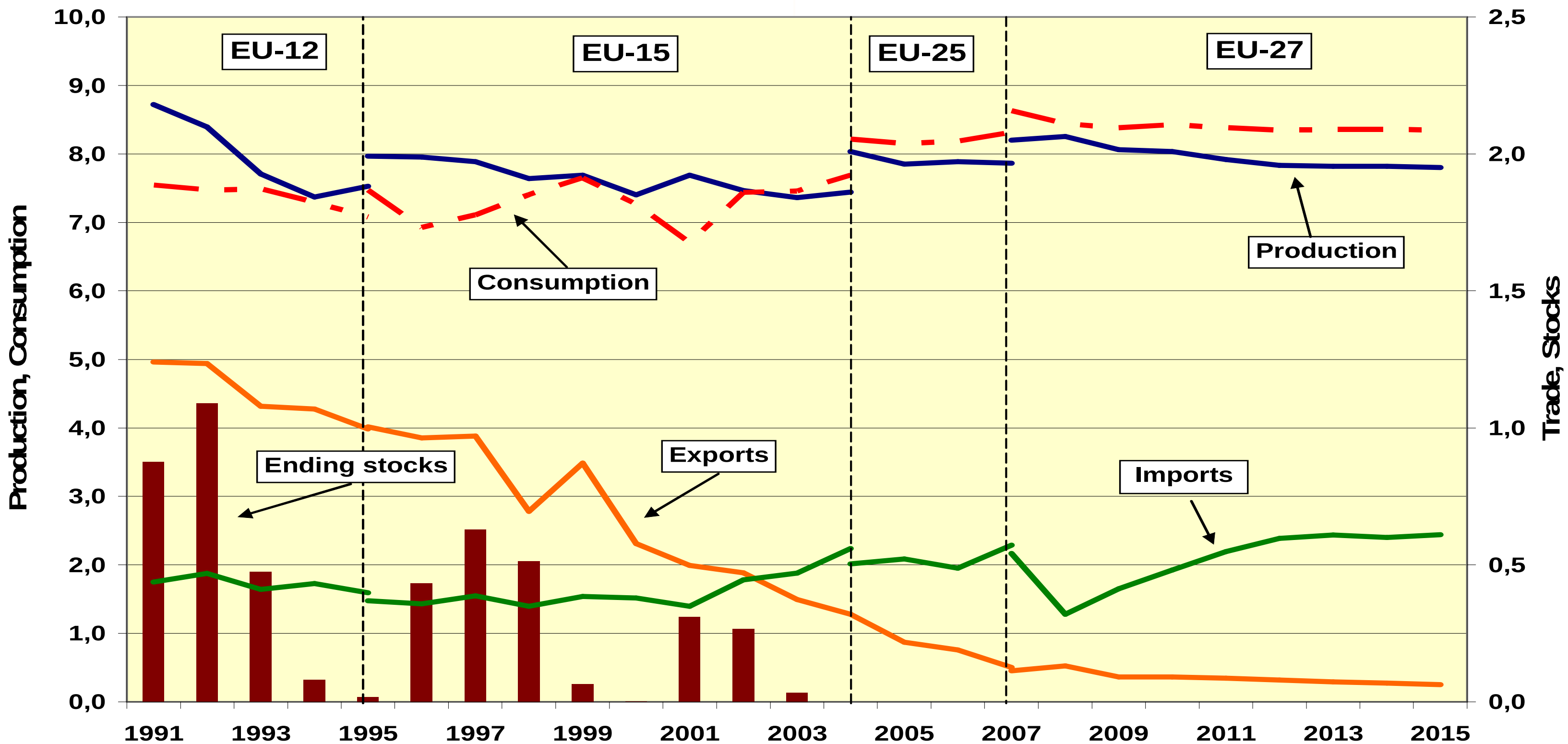
Projected world maize prices over the medium-term

(US Fob Gulf, $/t)



The beef sector would continue to decline slowly

EU production, consumption and trade (mio t c.w.e.)



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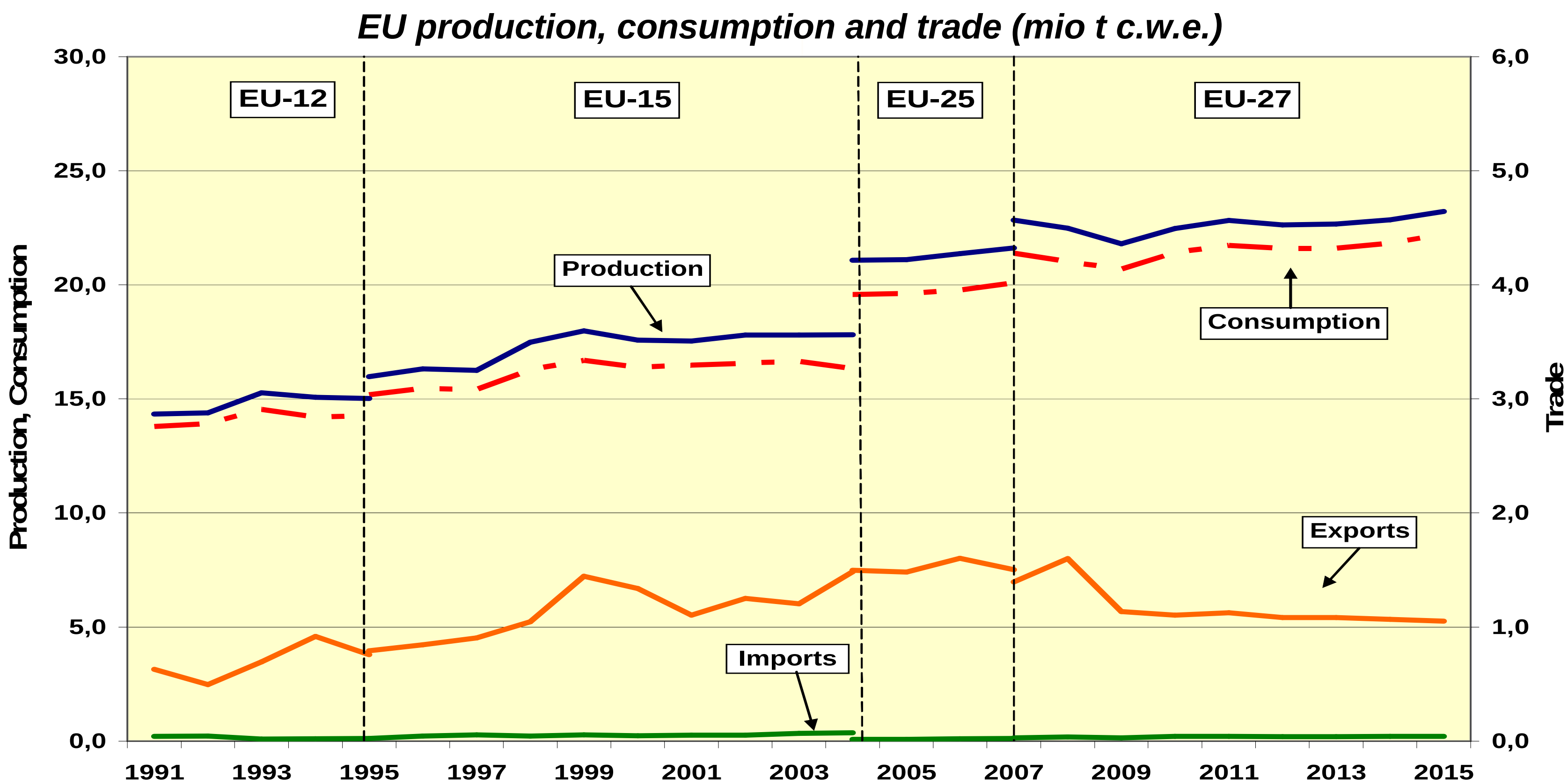
Moderate, though continuous expansion of the EU pig meat sector



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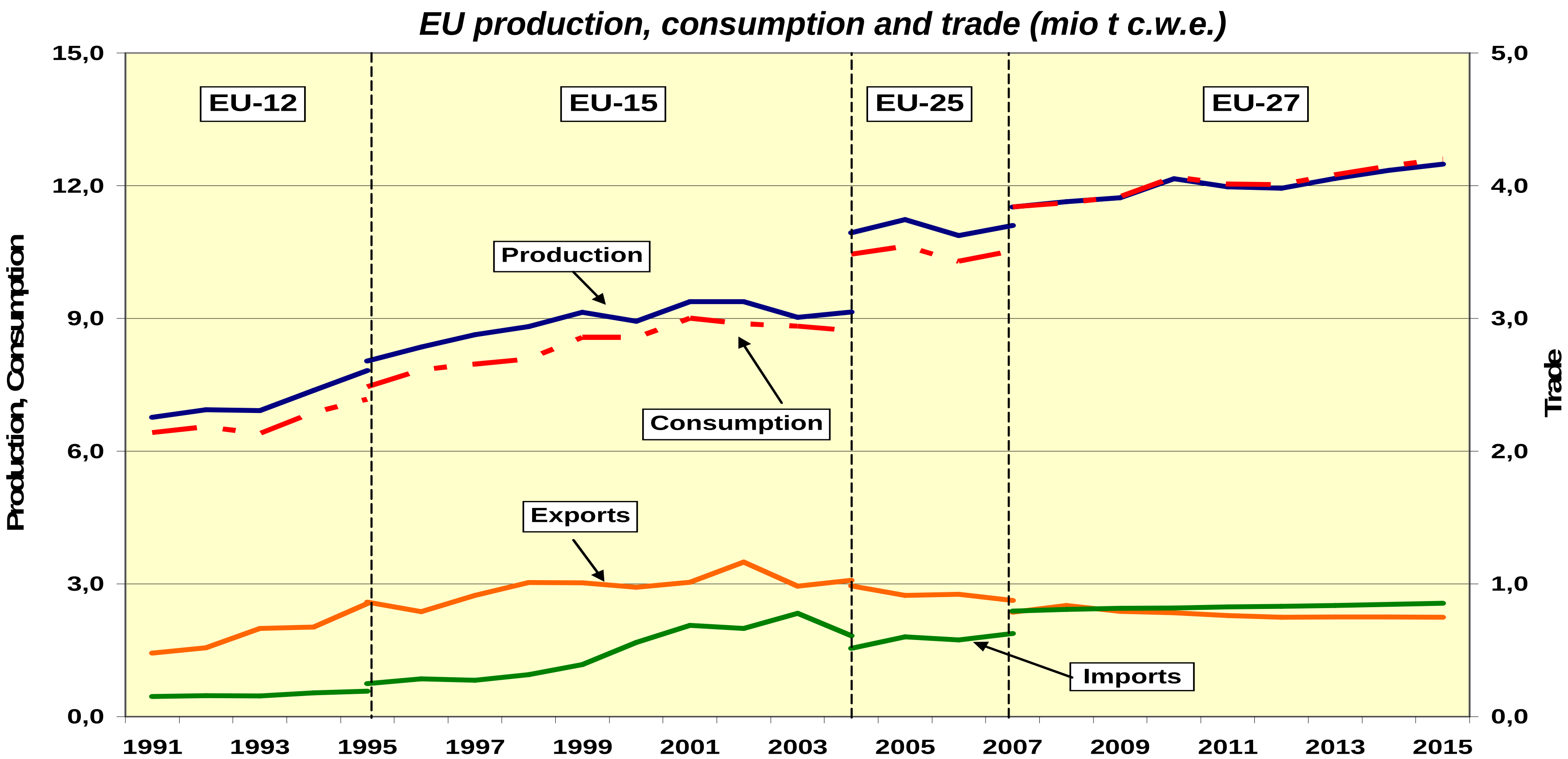
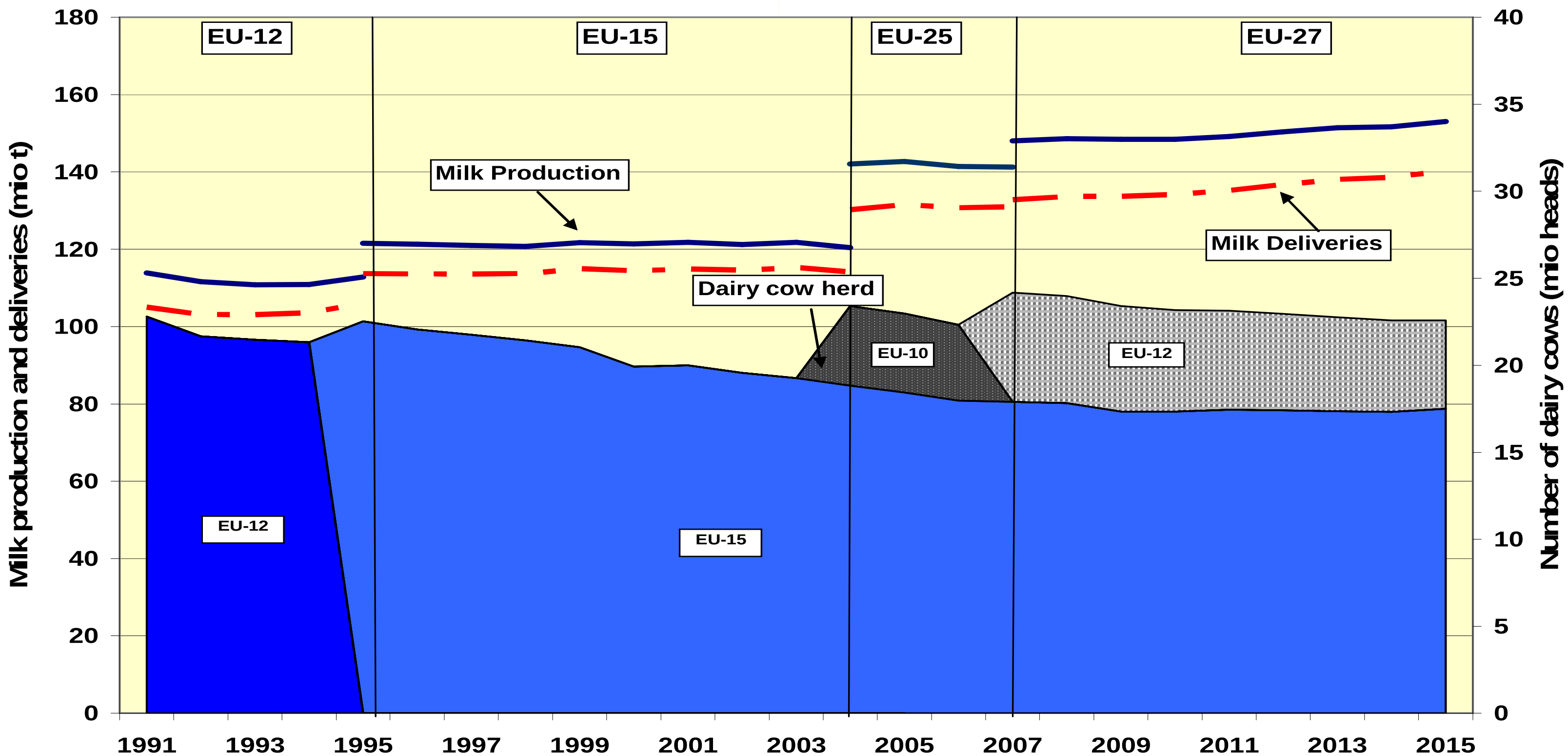
EU poultry sector to grow at a faster rate



EU milk production increases thanks to the gradual phasing-out of dairy quotas

EU milk production, deliveries to dairies, dairy cows



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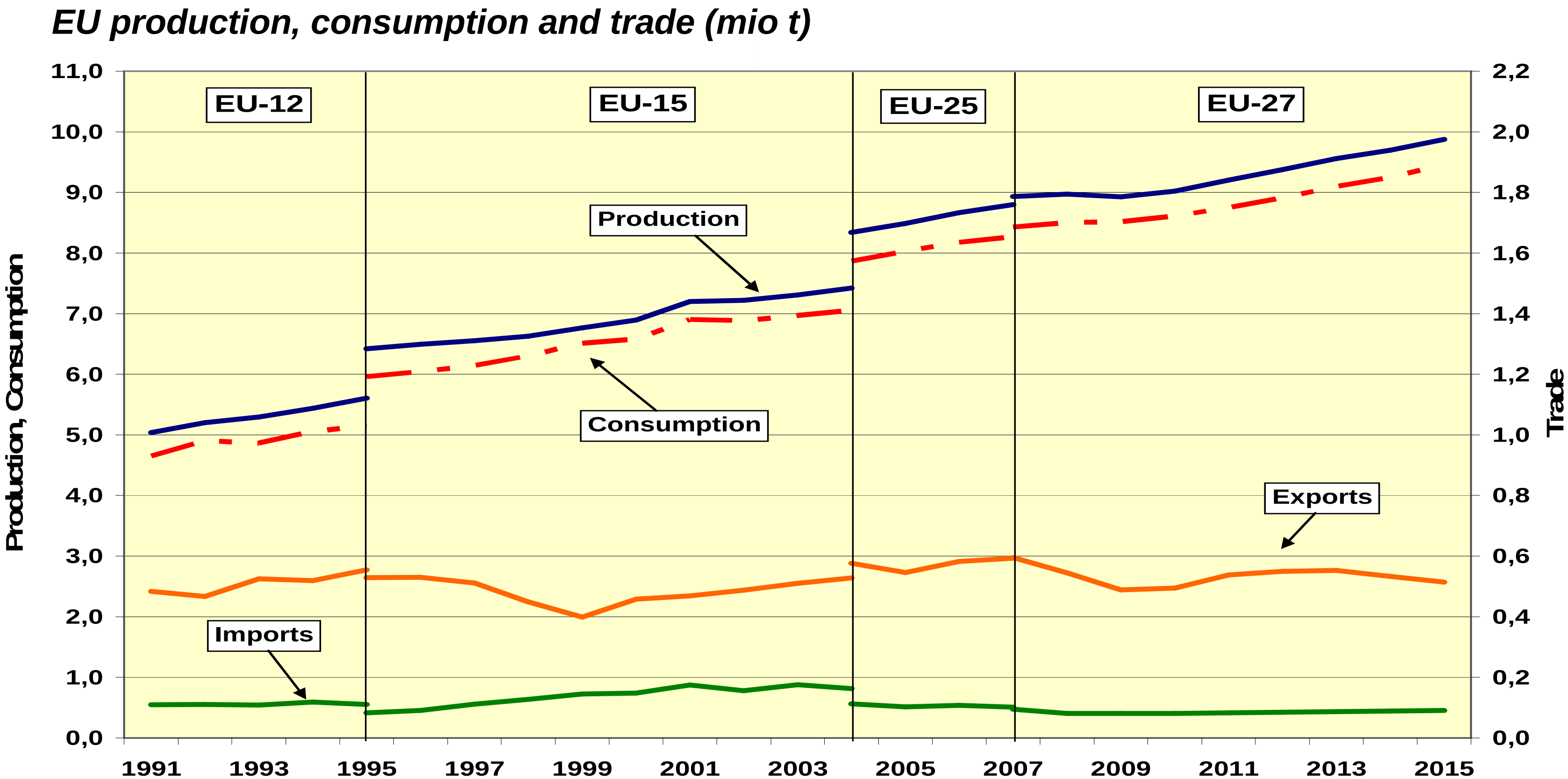
EU cheese market keeps its steady growth over the medium term driven by domestic demand



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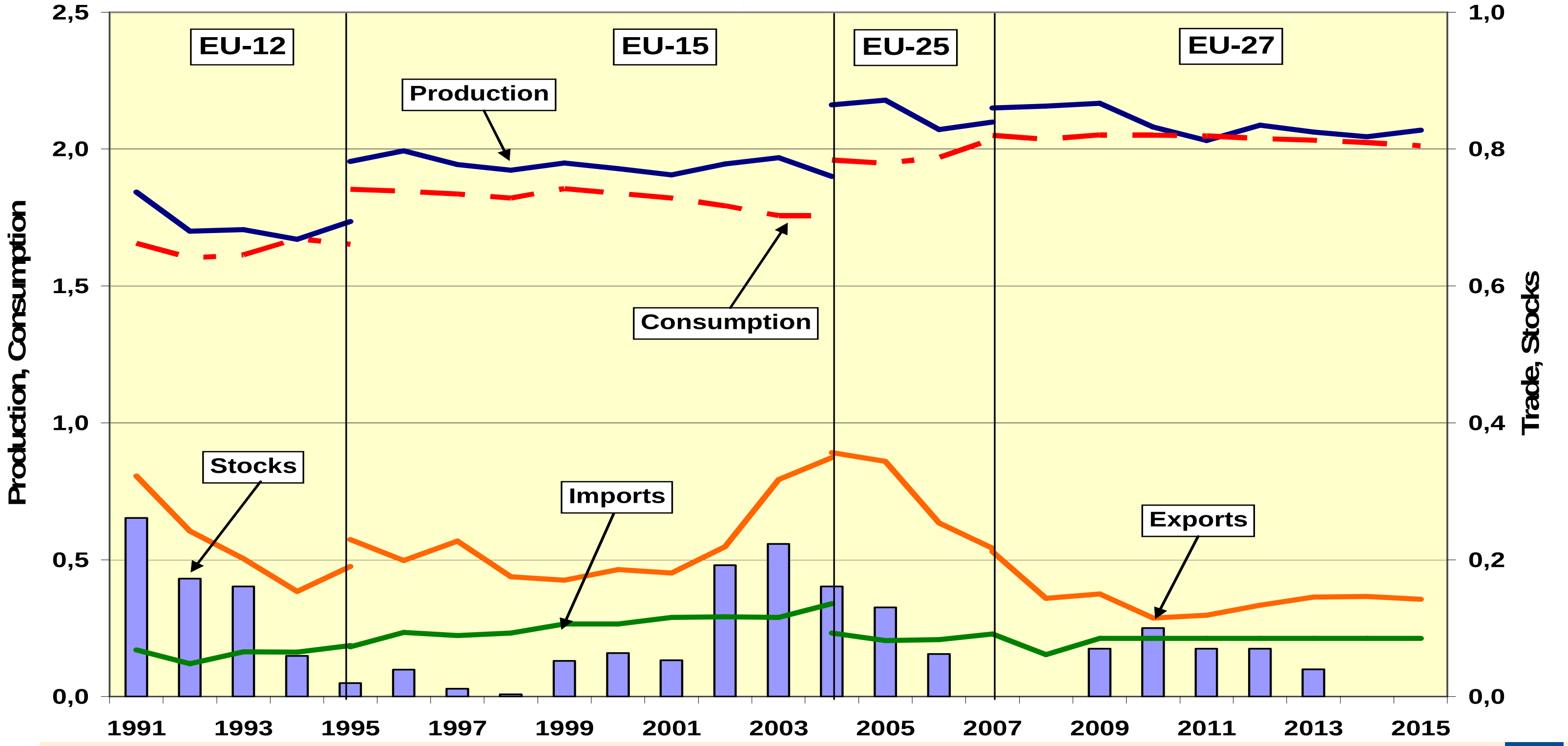
EU butter market to show some short-term imbalance as domestic production and consumption decline gradually

EU production, consumption and trade (mio t)



In summary, relatively favourable market and price trends over the medium-term but … many uncertainties remain

- *Potential implications of further trade liberalisation and a changing policy environment*
- *Future development of world commodity markets: will structural factors continue to support commodity prices?*
- *Economic environment: dependent on the depth and breadth of the economic crisis, pace of recovery and impact of higher energy prices*
- *Climate change, technological developments (GMO), biofuels, sanitary conditions, higher costs of production factors (e.g. water)*