Bundesverband Deutscher Milchviehhalter e.V.

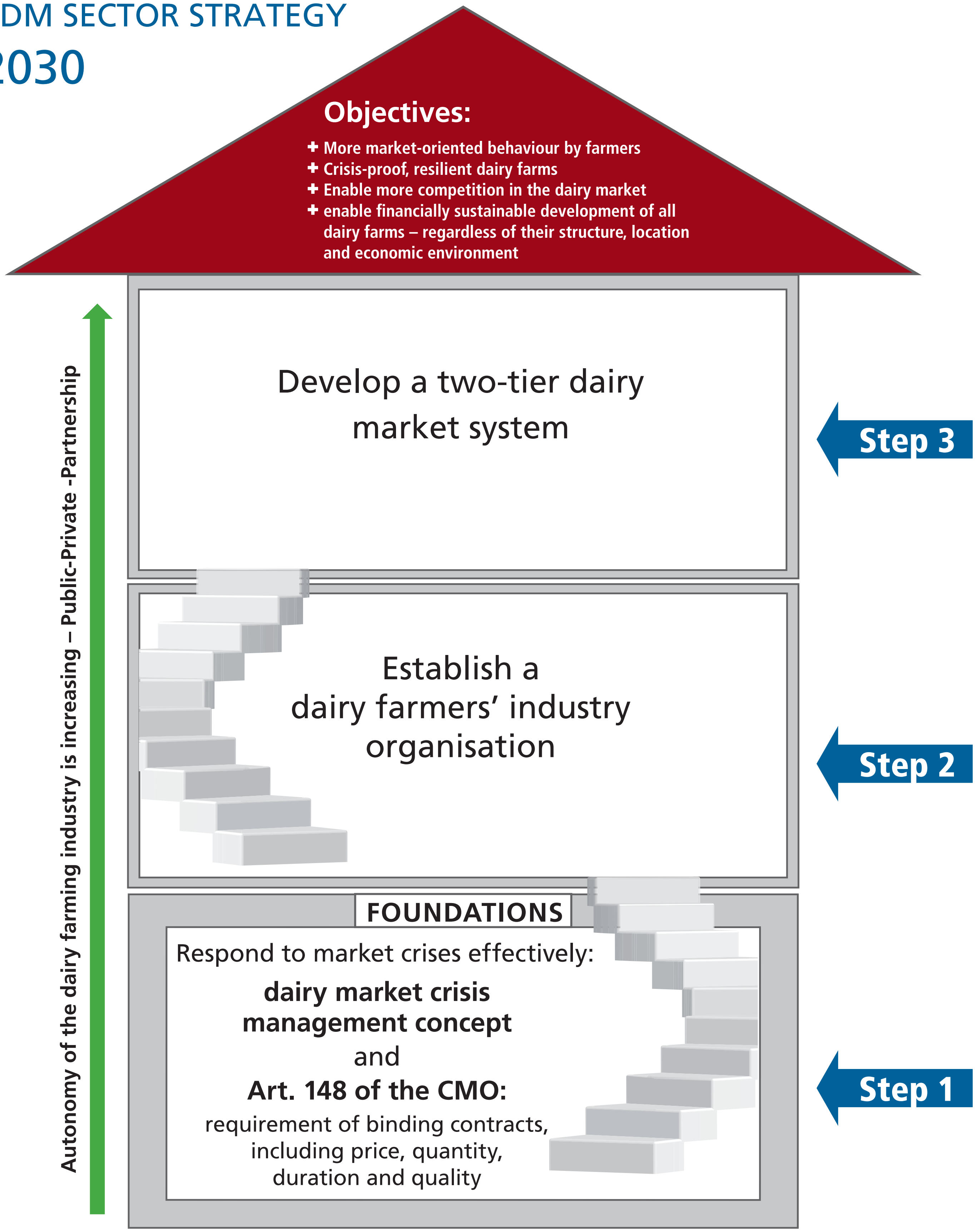
Sector Strategy 2030

for a sustainable dairy market

Compiled by Bundesverband Deutscher Milchviehhalter BDM e.V.

Content

BDM SECTOR STRATEGY 2030



„Sector strategy 2030" remit

„To really make good progress when overcoming challenges, we need one thing above all else: strategies, and especially those that really deserve the name strategy! An effective strategy defines clear objectives and plausibly demonstrates which stages and resources should be used to achieve these." Prof. Dr Folkhard Isermeyer's[1] guiding principle for CAP discussions should also apply when developing a sector strategy for 2030.

Intra-industry consensus regarding the path that we must jointly pursue certainly makes it easier and simpler to implement that strategy politically. But the stakes are high for dairy farmers – real change is needed. A strategy is required for the sector – rather than simply a sector strategy. They need more than the lowest common denominator, which is inevitably all that industry members, with their sometimes completely conflicting interests and differing powers of assertiveness, can agree on. The best solution is important for dairy farmers – and this is the result of open competition to find the best idea. The BDM is facing up to this competition and presenting a sector strategy 2030 that explains the necessary strategic options for the future with sufficient clarity, and also includes visionary thinking.

In the BDM's view, describing this as „sector strategy 2030" already signals that it not only deals with what is currently possible and immediately achievable, but also confronts brave new and partially even visionary thinking.

Although the BDM, as an association that consistently represents the interests of active and future-oriented dairy farmers, is pursuing this sector strategy approach, this does not mean that it would not be amenable to compromise – in the interests of dairy farmers.

In order to find a sustainable compromise and good, appropriate solutions, Bundesverband Deutscher Milchviehhalter BDM e.V. is asking politicians to broker this process and strategy between the various interests and unequal market players, in accordance with a reasonable reconciliation of interests, and make target- and results-focussed decisions in the event of possible conflicts of interest. The BDM is firmly convinced that the effort required to achieve this will be worthwhile!

As an association with links to 20 professional organisations in EU member states via the European Milk Board (EMB), the BDM would also like to point out that a strategy for the sector must target the European dairy market. Given the global dairy market, multi-national businesses and similar issues facing European dairy farmers, purely national strategies are neither timely nor expedient.

The BDM's sector strategy 2030 also reflects the fact that the industry must take more responsibility, as politicians are increasingly retreating from direct influence on the dairy market.

Why is a sector strategy 2030 needed?

A review of the current situation

The 2015/16 dairy crisis made it abundantly clear that there is an urgent need for action in the dairy sector. Repeated market crises, outdated and inadequate market crisis tools, the not (entirely) market-oriented delivery procedures of dairy farmers, enormous value creation losses, huge milk powder mountains, multi-million aid packages and intervention buying are clear signs of this. The relationship between dairy farmers and processors and the political tools for the dairy market has remained largely unchanged since the 19th and 20th centuries, while the dairy market and the corporate structure of many stakeholders have changed dramatically. This has consequences that are leading to significant misalignments. The Bundeskartellamt (Federal Cartel Authority) identified this back in 2012, in the extremely clear final report of its dairy sector investigation, and reaffirmed it in 2017 in its technical progress report on administrative procedures for milk delivery terms: considerable competitive restrictions on the regional markets for the sourcing of raw milk were identified, as was a market power gap to the detriment of dairy farmers.

[1] President of the Johann Heinrich von Thünen Institute, Federal Research Institute for Rural Areas, Forestry and Fisheries in Braunschweig/Germany. The Thünen Institute is a German research institute

Quotes from the Bundeskartellamt's interim report on its dairy sector investigation:

”The Decision Division has identified a power imbalance in the relationship between dairies and farmers to the detriment of farmers, despite the vertical integration of many farmers in co-operative dairies. In the investigators' opinion, farmers also no longer perceive larger co-operatives as their 'own' dairies, and their market behaviour reflects this.“

”Neither private nor co-operatively organised dairies basically have any incentive to pay the highest possible milk price in the interests of dairy farmers. [...] The profit maximisation strategy of each processing company is aimed at keeping procurement costs as low as possible.“

”The nature of the pricing at co-operative dairies ('upside down') means that they have no original self-interest in achieving high prices for their dairy produce, because they as dairies only bear limited financial risk.“

The Bundeskartellamt has therefore concluded that, overall, prices for dairy farmers are not currently being determined in a viable competitive and market environment. [2)]

The sector must therefore reposition itself, in order to meet the challenges of the future.

A brief overview of the situation of dairy farmers:

- Market position of dairy farmers between extremely weak and inadequate (see Bundeskartellamt's findings – these must finally be adequately considered as part of the sector strategy!)
- Concentration of general market risk – especially during market crises – at the expense of dairy farmers
- Rapidly increasing proportion of external capital in dairy farms.
- Unrestrained structural change, even during more economically relaxed market phases.
- No significant competition for raw milk, meaning there is a lack of marketing alternatives and higher added value from sale proceeds.
- Continuing decline in the willingness of potential successors to continue to manage and develop dairy farms that are basically still extremely economically stable. The context for this trend is the lack of financially sustainable prospects.
- Relocation of dairy farming to so-called favourable locations, which would make nationwide dairy farming increasingly important, especially against the background of climate change (more variety, increased supply security, etc.)
- Market risk and price concessions can be transferred to dairy farmers under competitive pressure due to „upside down“ pricing – an almost ideal economic situation for the milk-processing industry and retailers.
- While processors and retailers earn money, dairy farmers can simply break even and/or constantly lose money.
- Refinancing periods of 25 years and over for investments in dairy farms.
- The economic power of some rural areas has been significantly weakened – even well-meaning government programmes to strengthen and develop rural areas have been unable to effectively counteract this.

A sector strategy 2030 must tackle the problems facing this sector and therefore place increased emphasis on the interests of dairy farmers, particularly because this is where there is an urgent need for change.

However, if the interests of processors, industry and commerce are considered equally or even more important, almost no changes are required.

While processors, industry and commerce are also facing new challenges, their opportunity/risk ratio is much more favourable than that of dairy farmers.

For example, although the consequences of climate change mean more work and more uncertainty for businesses, they also provide new market opportunities. Expanding dairy markets in China, India and Russia are offset by a growing global population

[2)] Bundeskartellamt, Interim Report December 2009, Dairy Sector Investigation (B2-19/08), page 135 and increasing purchasing power in developing countries and new export nations, etc.

The bottom line, however, is that processors, industry and commerce are already receiving a great deal of support, thanks to the current focus of EU agricultural market policy on low raw ingredient prices and international competitiveness, to subsidies from public funds, to numerous publicly-financed export initiatives and the political support for these – and, last but not least, to the transfer of general market risk to dairy farmers.

Objectives of sector strategy 2030

A review of the current situation therefore gives rise to the following objectives, which the BDM believes must be pursued with a sector strategy 2030:

- To strengthen dairy farmers‘ market position vis-à-vis the dairy and processing industry
- To curb extreme market volatility
- To strive for more market-oriented behaviour by farmers
- To significantly increase added value for farmers
- To allow the fairer distribution of market risk along the value chain
- To create crisis-proof, resilient dairy farms
- To reduce the need for political (market) intervention
- To enable more competition in the dairy market – no competitive distortion of contractual relations
- To reduce the burden on taxpayers (fewer emergency aid programmes)
- To strive for adequate, calculable milk volumes for dairies
- Retail/industry: healthy food with high standards, variety as a marketing opportunity (mountain, meadow, pasture milk, etc.) – an aspect that should deliver considerable marketing benefit in future, especially given the fact that dairy farming on mega-farms is steadily being expanded in China/Russia/India.
- Climate objectives: To once again reinforce the principle of circular economy that was originally firmly anchored in agriculture. There can hardly be any question of EU animal feed imports amounting to three times the size of Germany‘s agricultural area any longer. More circular economy also makes sense from the point of view of maintaining an agricultural system that is as comprehensive as possible.
- To strengthen/maintain the vitality of rural areas: dairy farming requires a great deal of investment, is regionally based and provides many jobs, including in upstream and downstream sectors.

Overarching objectives:

- To enable dairy farming to develop in a financially sustainable manner with good future prospects.
- To make dairy farming acceptable to society and diverse.
- To achieve profitable value creation through milk as a product and reduce dependence on taxpayers‘ money.

To achieve the stated objectives will require the efforts of all market stakeholders – and especially dairy farmers. However, political decision-makers in the EU member states and the Brussels institutions also have a specific responsibility. Even though the sector must become more independent and autonomous in future, politicians must provide the necessary framework conditions for the EU dairy market, which allow the financially sustainable development of all dairy farms, regardless of their structure, location and economic environment. The tasks are multi-faceted and can therefore only be achieved by the dairy farming sector and politicians in partnership.

The content of the BDM sector strategy 2030 and how to implement it

Step 1:

– Effectively respond to market crises – using the BDM milk market crisis management concept

– Requirement of binding contracts between dairy farmers and dairies via specific agreements regarding delivery quantities, dairy farmer prices, duration of the supply relationship and corresponding quality features

Step 2:

– Establish a dairy farmers' industry organisation

Step 3:

– Develop a sustainable dairy market system for dairy farmers

The further development of the dairy sector will necessitate considerable changes for dairy farmers. The timescale needed for this should not be underestimated, since the decades-long focus of the Common Agricultural Policy on supplying the food and dairy industry with affordable raw ingredients has created structures that cannot be quickly and effortlessly changed. The BDM therefore considers the gradual implementation of the necessary elements of its sector strategy 2030 to be essential.

Every step of the BDM sector strategy allows the necessary political intervention and action to be gradually reduced. Initially, there is an even greater requirement for politicians to provide better market conditions and enable dairy farmers to actually assume independent responsibility. Previous dairy farmer initiatives in this regard have regularly failed, especially in terms of marketing, as there was little they could do to offset competitive pressure and, in some cases, strategic playing off of actors against one another in the purchasers' market.

Previous initiatives in the sector and their results

Some dairies supposedly follow the Bundeskartellamt's recommendation to strengthen the market mechanism by agreeing fixed prices in advance instead of relying on upside-down pricing as previously customary, thereby enabling improved regulation of milk volumes. They announce their monthly milk price in advance of delivery. However, this does not necessarily mean that they are abandoning upside-down pricing, because they still have the option to change the dairy farmer price during the ensuing period, in line with their interests.

Another very serious, competition-limiting trend is the introduction of multi-price models, as already established in some other EU countries. Most of these models are also closed-shop models. Ostensibly, these are justified by the fact that dairy farmers are encouraged to bring their delivery volumes more in line with the market.

The higher so-called A milk price gives the impression that all dairy farmers receive greater added value. Overall, however, the lower B milk price significantly depresses milk prices. These multi-price systems fail to produce the quantitative effect hoped for by some academic commentators and interest groups, due to insufficient differences between the individual price segments. Multi-price models would only serve to control volumes if extremely low prices were paid for any surpluses, reflecting their lack of marketability, at least in times of dairy market crisis.

Bundling and marketing initiatives by dairy farmers regularly fail due to the market power of the processers – especially in a buyers' market. And even large dairy farmer groups and their umbrella organisations have so far been unable to improve the market position of dairy farmers or their share of added value.

Initiatives by the milk processing industry and retailers to gain competitive advantages in the fiercely contested market for dairy produce and open up new markets by means of special qualities are generally welcome. However, the more clearly the market for raw milk becomes a buyers‘ market, the easier it is to enforce new labels and programmes that unilaterally impose more stringent production criteria on dairy farmers that often far exceed the legal standards, without any compensation for the additional costs.

All these examples show that step 1 of the sector strategy – managing dairy market crises efficiently and the requirement of binding contracts for quantity, price, duration and quality – are an important basis for a largely balanced dairy market, and thus effective industry initiatives.

Ref. to step 1 – part 1:

The ability to effectively overcome market crises!

Market crises are caused by an imbalance between supply and demand. Whether this imbalance is the result of the excessive growth of raw milk supply or a fall in demand is irrelevant. The main cause of each of the dairy market crises of the past 10 years has been a 1 to 3 percent increase in EU milk production, which could only be sold on the global dairy market at abysmal prices or for which no customers could be found.

Avoiding milk surpluses instead of storing them up: In times of crisis, when too much milk depresses the market, it makes more sense to curb milk surpluses at an early stage instead of producing these in the first place and then storing them in private warehouses with government intervention – with huge financial consequences for dairy farmers.

This primarily requires market-appropriate delivery behaviour by dairy farmers and their responding rapidly to the altered market. While contractual agreements allow milk volumes to be adjusted to the respective dairy capacity, they cannot prevent global market crises.

What is crucial for faster market adjustments is realistic, timely presentation of global and national dairy market trends, which must be easy for dairy farmers to read, almost at a glance. The market observation and assessment of the EU Milk Market Observatory (MMO) must therefore be further developed, their reporting regulations possibly revised, and compliance with current reporting deadlines respected. The Milk Market Observatory (MMO) already provides many datasets regarding changes in global marketplaces and at an EU level. It also records developments on the commodity futures exchanges in order to present market trends at an even earlier stage.

Market trends, which can be certainly be scanned holistically relatively quickly, but only evaluated by analysing a great deal of individual data, must be easier to grasp. This requires the development of an index that allows every market player to see at a glance where the dairy market is heading if supply and demand parameters are unchanged. Appropriate algorithms could be used to derive the necessary market adjustments that enable a timely market response, rather than becoming entangled in endless discussions and market interpretations that possibly send out the wrong market signals to dairy farmers.

The BDM‘s milk market crisis management (MMCM) concept, with its stepwise approach based on the findings of the Milk Market Observatory, also follows the principle that price signals must be sent to dairy farmers earlier, in order to encourage market-appropriate behaviour. By stage 1 (early warning) at the latest, the market trend is clearly visible to every dairy farmer. They can adapt their behaviour to the market to offset a crisis. This includes a preventative and proactive aspect that other concepts lack, which understand "early communication of price signals to dairy farmers" to mean merely a rapid reduction in farmers‘ prices. Crises can be actively offset; it is not enough to simply mitigate their consequences (see, for example, hedging commodity futures exchanges).

The MMCM in a few key words

The MMCM concept

- sconsistently addresses the cause of market crises – the imbalance of supply and demand
- is based on an organised approach at EU level. National approaches in a now global dairy market do not produce the appropriate effects.
- is limited to market phases that can be described as crises due to certain criteria
- is based on the trend in global and national marketplaces for dairy produce as evidenced by the EU Commission‘s Milk Market Observatory (MMO), as well as the trend in the commodity futures exchanges
- includes the development of margins in milk production
- results in virtually no hardship cases, by determining extremely timely reference periods when implementing quantitative disciplinary measures
- does not impede the development of dairy farms, as there are no quota costs.

The basic parameters:

Three-stage approach

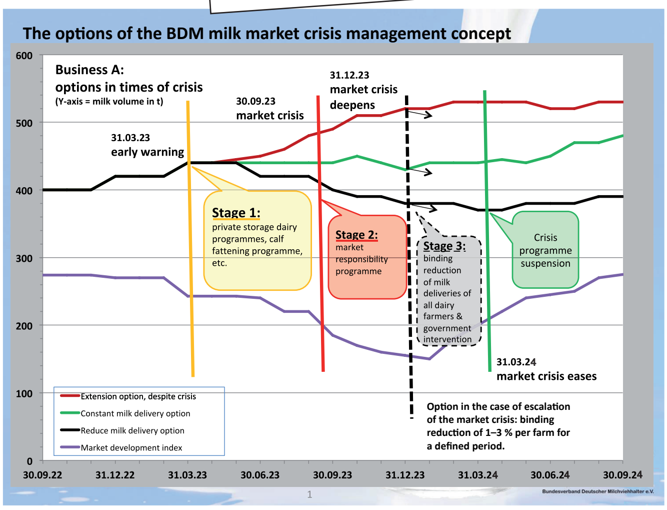
Stage 1:

Early warning system in the event of acute danger of a dairy market crisis: Early warning is issued by the EU Commission‘s Milk Market Observatory if the market index drops accordingly (e.g. by 7.5% or 10%). Dairy farmers who increase their milk supply despite this early warning must expect to pay a high market responsibility levy for their additional supply when crisis mode is reached. In parallel with this, private warehouses could be opened.

Stage 2:

If the index continues to fall (e.g. by 15%) despite this early warning, a market responsibility programme for dairy farmers could offer an incentive programme for a temporary reduction in operational milk supply in the form of appropriate compensation. This could be financed through the EU crisis fund, market responsibility levy and, if required, a crisis levy to be paid by EU dairy farmers. In order not to thwart the market impact of this stage, a temporary cap on milk supply is required.

see chart/Annex p. 19



Stage 3:

If the index continues to fall (e.g. by 25%), despite the previous stages, there will be a temporary reduction in milk supply by all dairy farms, without any compensation. Experience from recent crises has shown that volume changes of just 1–3% have a very clear market impact. Stage 3 should be supplemented by government intervention.

Stage 2 could possibly be optional, but stages 1 and 3 must be included in the safety net for the EU dairy market.

In principle:

These tools could possibly be implemented and handled via an industry organisation for EU dairy farmers and/or at a national level via the German Federal Office for Agriculture and Food (Bundesanstalt für Landwirtschaft und Ernährung, BLE). An industry organisation for EU dairy farmers would have to be given special powers for defined exceptional situations (such as a crisis), which go beyond the existing catalogue of permissible industry tasks.

The MMCM concept is aimed at modernising and expanding the

EU safety net for the agricultural/dairy market. It should be used if all other measures, such as the contractual arrangements for supply relationships, are not sufficiently effective. At the same time, the MMCM concept is a kind of basic safeguard against dairy farmers having to conclude binding contracts with processors on abysmal terms.

The MMCM concept does not contradict the market-oriented approach of agricultural policy. It is only used on a temporary basis in times of market crisis and is by no means a reinstatement of permanent volume regulation. Consequently there are no delivery rights etc., which would need to be managed and would involve costs for farmers.

Even in a market crisis, corporate decision-making freedom is not at risk, because individual businesses are free to decide how they want to behave. Ultimately, the way they behave is determined simply by a cost-benefit analysis. In the so-called free market, however, this is the case with every business transaction.

The milk processing industry does not therefore lose any market share, as all existing contracts can still be easily fulfilled. Only excess volumes are reduced, for which there are no customers and which put the entire market under severe pressure.

Ref. to step 1 – part 2: implementing Art. 148 of the CMO

In the view of the BDM, another element that must be implemented immediately is the possibility of specifying binding contracts between dairy farmers and processors via specific agreements regarding delivery quantities, dairy farmer prices, duration of the supply relationship and corresponding quality features, in accordance with Art. 148 of the CMO.

Article 148 of the CMO must be implemented, despite its limited impact on the overall market. The binding requirement to agree specific quantities, prices and the duration of the delivery commitment is vital, given the extremely limited competition for raw milk identified by the Bundeskartellamt. Upside-down milk pricing is outdated, places the market risk in the value chain on dairy farmers alone, and also contradicts the position in which dairy farmers must confront the market.

The following arguments are therefore important:

Benefits of binding specification of specific price, quantity and duration agreements for all milk supply relationships

- The contractual partners must get to grips with the prevailing market conditions (supply and demand) and agree appropriate parameters.
- Recurring, specific contract negotiations are required, while keeping an eye on current and future market trends.
- This could result in dairy farmers and/or their associations receiving multiple comparable bids, leading to increased competition.
- Prior to farms undertaking expansion, the purchase of any surplus must be contractually regulated.
- Binding contractual agreements, especially with co-operatively structured firms, could prevent co-operative dairies from offering price concessions too quickly during contract negotiations with the food industry and food retailers.
- If rapid price concessions are offered, contractual agreements prevent these from being immediately passed on to dairy farmers. This increases the need for dairies to undertake stringent planning, as premature price concessions would be at their own expense, at least in part.
- The need to address the development of supply and demand, which is also highlighted by the Milk Market Observatory, could at least partially tackle emerging market crises.
- Milk volumes can be adjusted to the processing and marketing capacity of the respective dairy – without this affecting the overall market situation.

What contractual agreements are unable to do

- Contractual agreements make it possible to adapt milk volumes to the respective dairy capacity, but not to adjust supply and demand at a national, European and global level.
- Contractual agreements between dairies and dairy farmers cannot prevent supply and demand from drifting apart at a national, European or global level.
- The onset of a crisis cannot be prevented (for example: volume agreement in a good market situation, subsequent change in the situation as a result of an unexpected slump in demand, e.g. due to political events).
- EU-wide harmonisation of different corporate strategies (e.g. utilisation of processing capacity, filling of shelf space etc.) to achieve a common, market-based approach in times of crisis is not possible.
- Options to contain market crises (which always have a global nature) are limited or even non-existent, as effective EU-wide crisis management for politically induced market distortions such as an embargo cannot be achieved by individual agreement.

Possible side effects:

- Different corporate interests prevent any action affecting the overall market situation.
- Dairy farmers' negotiating position is extremely dependent on volume supply of the overall market. Problem: individual dairies will always have a tendency to ensure that a slight milk surplus is available, in order to maintain/assume pole position among their competitors. There is a great danger that permanent volume pressure will lead to a poor negotiating and price situation for dairy farmers.
- Use of freed-up milk quotas within the dairy and/or farmers' organisation requires an allocation formula and/or incurs costs.
- If relative volumes and price scales are agreed instead of specific volumes, there is a great danger that all the positive aspects of a specific contract arrangement will be undermined. There is then less need for market-adjusted volume planning even by dairies, and dairy farmers obtain milk prices that significantly depress the milk price level.
- There is a great danger that dairy farmers will have to accept price reductions for surpluses and/or shortfalls (cf. contracts in France), without any necessity for this arising from the overall market situation.

Timeframe: All the measures mentioned in step 1 are to be implemented in the short term.

Bundesverband Deutscher Milchviehhalter e.V.

Ref. to Step 2: Establish a dairy farmers’ industry association/organisation

Both politicians and professional associations are aiming to establish a recognised industry association, which should be supported by representatives from the entire value chain as far as possible. According to current EU legislation, at least two stakeholders (e.g. dairy farmers and processors) are required to establish and manage an industry organisation (dairy IO) in the dairy sector. Advocates of a dairy IO based on existing legislation believe there is a need for an equal number of dairy farmers and dairy industry representatives to be appointed to the management committee. According to them, under no circumstances should a dairy IO whose scope extends beyond milk production be used to strive for market equilibrium. Rather, one of the main tasks of a dairy IO should be to enforce jointly defined production standards.

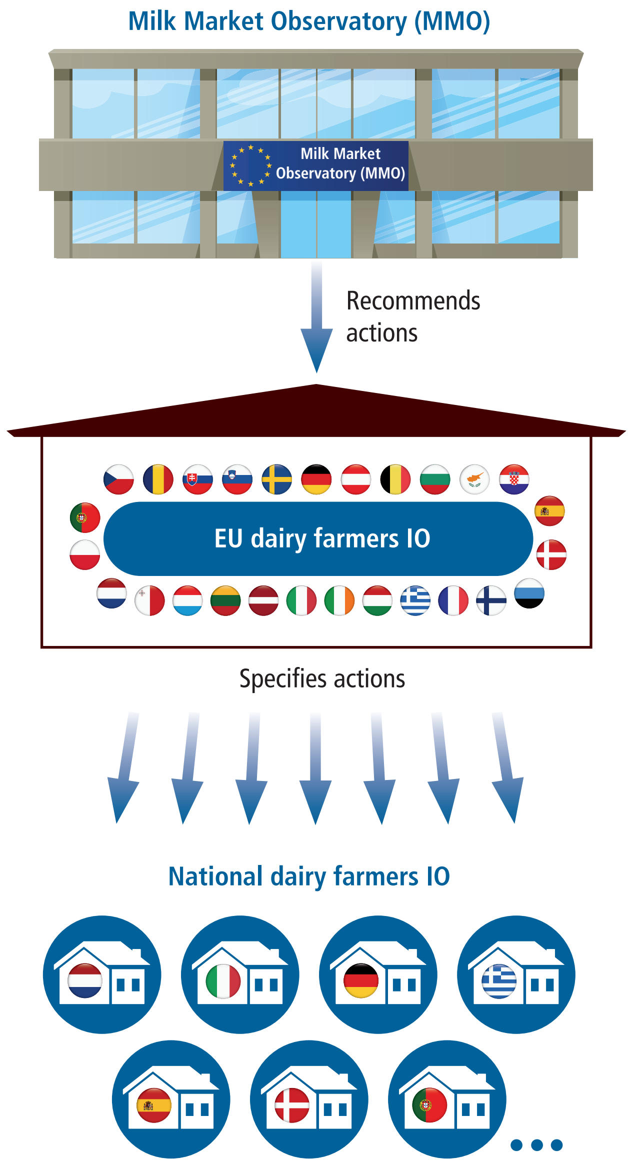
In the BDM‘s view, it makes no sense to establish a dairy IO with the structure described here, as it cannot achieve the objectives of this sector strategy.

It is unrealistic to assume that, in a dairy industry organisation constituted as above, milk processors who are members of the industry organisation would act to their own disadvantage and change a situation that is profitable for them. An equal composition of the IO would, in fact, replicate the balance of power in the market. There can be few effective results if vertically integrated market players in a value chain, who are heavily dependent upon each other, are supposed to develop solutions for structural problems arising from precisely this interdependency in the context of a joint IO. If such agreements were made there, this would also have to be regarded as a massive intervention in the competitive system. Accordingly, severe constraints have already been put in place by EU legislation in the existing catalogue of possible tasks for an industry organisation. According to these, there should be no consultation regarding price and quantity in milk marketing in any circumstances. But even in the case of the permitted stipulation of production standards for raw milk, the conflict of interest between dairy farmers and processors is brought to bear: dairies are increasingly anxious to gain competitive advantage over their competitors with higher production standards that exceed the legal requirements. The farmers are only partially rewarded for the resulting higher milk production costs, and usually not permanently.

With the multi-tier (primary and secondary tier) composition of IOs, even with equal representation on the committees dairy farmers would not be able to bring about any majority decisions with regard to their interests, at least on critical points. At best, they could prevent negative decisions through voting parity – but only if no votes were cast by representatives on the dairy farmers’ side who also sat on the committees of co-operatively structured dairies.

From the BDM‘s viewpoint, establishing a dairy IO only makes sense if dairy farming is organised as an independent industry and recognised by European legislators. The term ‚industry‘ is not clearly defined. Essentially, however, it is believed that an industry is characterised by a certain substitutability of industry members and competitive practice between them. In the multitier composition described above, however, there is strong interdependency between industry members. It is therefore perfectly appropriate to recognise dairy farming as a separate industry that can then be given special powers. If politicians want to withdraw from the dairy market and leave more and more tasks to the industry itself, they must make any necessary changes to EU legislation, in order to enable dairy farmers to resolve their problems autonomously and above all effectively. A look at other industries reveals that it is perfectly possible to treat dairy farming as an independent sector. (Bundestag members‘ deliberations regarding EU industry associations in the dairy farming sector are heading in a similar direction.) The steel industry is quoted as one of many examples: here there is an IO which represents the steelmaking industry, namely the REFA-Branchenorganisation Stahl. The WSM Wirtschaftsverband Stahl- und Metallweiterverarbeitung e. V. is another IO that represents the processing sector, and therefore the steelmaking industry‘s customers.

Brief summary of the main features (structure, tasks, etc.) of a dairy farmers' industry organisation (IO):



Composition/structure:

DG Agri – external data sources – expert advisory board

Tasks:

– Market observation
– Market analysis
→ Recommendations for action

Composition/structure:

representatives of 27 national industry associations in an „EU dairy farmers' IO (DFIO)": places allocated according to milk yield/number of DFs? … possible additional members?

Tasks:

– Setting parameters
– Implementing market initiatives

Composition/structure:

national industry organisations/associations in 27 countries
Members: dairy farmer associations, milk producer groups
! Only DFs with no role in dairies and their associations, etc., without political mandate?

Tasks: national implementation

– Market responsibility tax collection
– Storage/removal intervention
– Processing/invoicing
– Monitoring/control
– Controlling impact analysis

EU dairy farmers' industry organisation (DFIO):

- Responsible body: dairy farmers' industry organisations of the respective EU member states.
- The EU Commission's Milk Market Observatory undertakes market observation/analysis.
- Only active dairy farmers who are not officials of dairy industry associations and/or dairy companies sit on the committees/ bodies.
- Located alongside the EU Commission's Milk Market Observatory.
- Connection with/involvement of EU dairy farmers via national DFIO.
- NB: Co-operatives and/or DFAs that are exclusively assigned to a dairy are not part of the dairy industry, despite their shareholder base – the conclusions of the Bundeskartellamt must be observed in this case.

Possible supervisory bodies:

- EU Commission
- EU Council
- EU Parliament

Possible advisory institutions:

- Scientific institutions (Wageningen, Thünen Institute, etc.)
- Co-operatively structured milk processing industry associations

Possible remit:

- MMO legislative instrument
- Source of market information for dairy farmers, politicians, etc.
- Defining the market parameters/marketplaces etc. to be used to represent the market situation
- Defining/deriving market action steps via algorithms
- Adjusting volumes in times of crisis
- Storage/removal, undertaking of warehousing + logistics
- Financial administration
- EU crisis fund
- Collecting/invoicing market responsibility levy (MVL)
- Allocation management
- Compensation administration
- Supervisory body
- Sanction body

National dairy farmers' IO tasks:

In step 2, these are primarily represented by national branch offices at member state level, with the following tasks:

- See Federal Office for Agriculture and Food (BLE) remit
- Possible additional marketing initiatives, etc.

In step 3 (see explanations below), the remit of the national IO is expanded.

Timeframe: all the measures mentioned in step 2 are to be implemented in the medium term.

Ref. to Step 3: Develop a sustainable dairy market system for financially viable dairy farming

In order to create genuine competition for raw milk, far-reaching approaches must be considered that are a complete departure from the contractual arrangements established for decades between dairy farmers and/or their associations and the milk processing industry. At first glance, it might be argued that this vision is unrealistic and not expedient, but upon closer examination it becomes clear that in a drastically altered, liberal dairy market with multi-national firms and global dairy flows, change should not stop at milk marketing structures. Ever since Carl Petersen founded the Städtische Sammelmolkerei Oldenburg in 1875, the upside-down pricing system of co-operative dairies has remained virtually unchanged. In light of the ever-increasing challenges facing dairy farmers, a fundamental overhaul of milk marketing structures is long overdue.

The BDM envisages that the dairy farmers' IO should play a decisive role in a new, two-tier dairy market system. Together with all its affiliated milk producer groups, it will be the dairy industry's contractual partner when it comes to supplying it with raw milk and possibly also with primary products.

An essential element of such a marketing strategy is the uncoupling of the direct contractual relationship between individual dairy farmers and dairies.

Other requirements:

1. Uncoupling of capital and the obligation to supply[1] in the co-operative sector

A two-tier dairy market invalidates the bond between investors and milk suppliers. This bond is endorsed by the co-operative dairy industry, as it means a secure supply of raw milk, without having to make a special effort to find suppliers. In order to be able to create a raw milk market and make this efficient, the uncoupling of the two factors, capital and the obligation to supply milk, is required.

2. Interest payments on co-operative equity investments

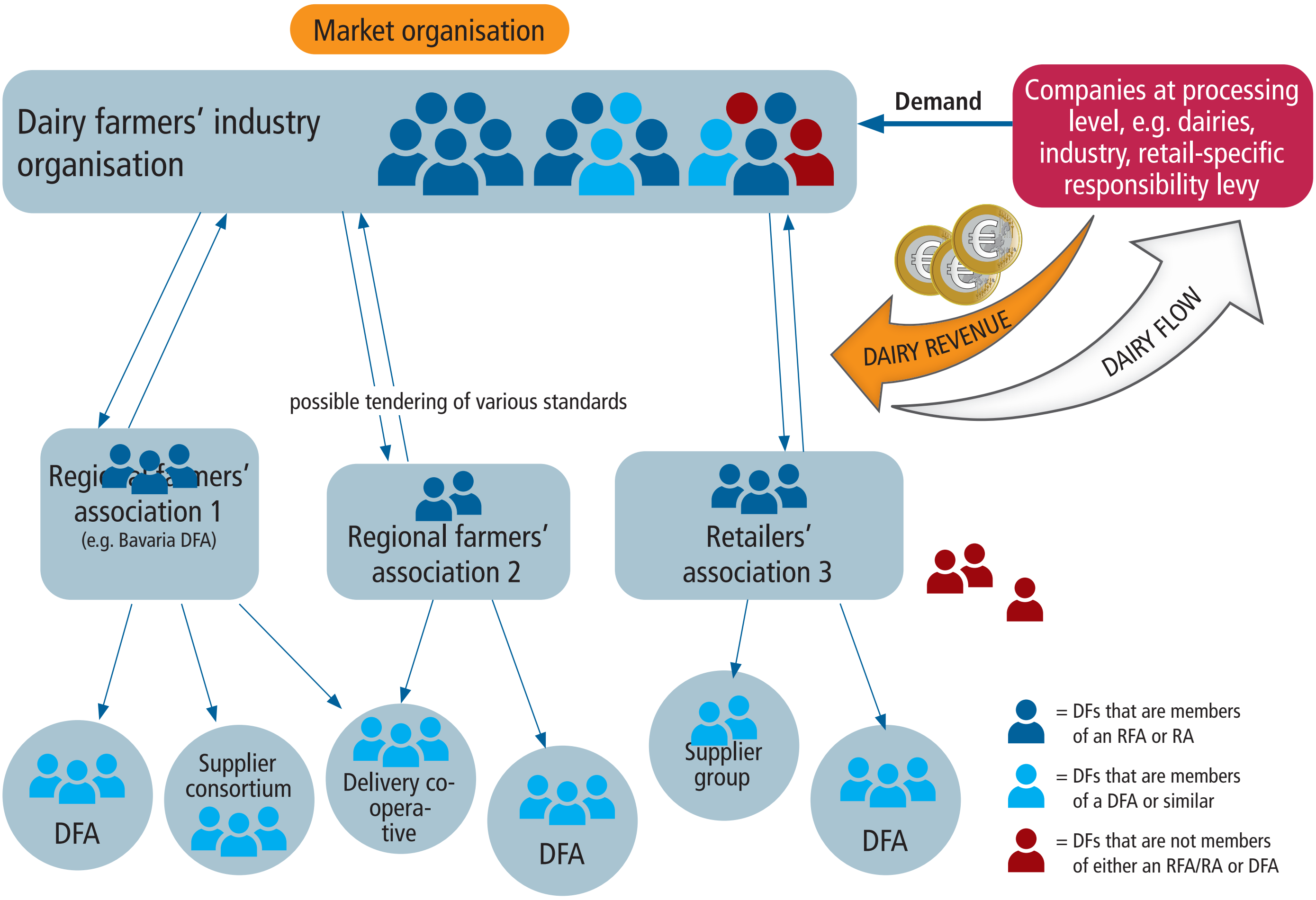
The uncoupling of capital and the obligation to supply does not mean abandoning the co-operative model. It would simply mean that the milk processing co-operative sector would be on equal terms with other sectors. For example, membership of a co-operative purchasing group does not automatically mean that the member can only make purchases there. Dairy co-operatives can also meet their demand for raw milk by buying from non-members, dairy merchants, etc. Any dairy farmer could join a co-operative, whereby they would pay interest on their invested capital depending on their operating results.

Functioning of a two-tier dairy market:

- The dairy farmers' IO (DFIO) concludes contracts for the supply of milk to the processing industry, covering quantity, quality, price and the relevant duration.
- The necessary quantities of milk are procured via contracts with milk producer groups affiliated with the DFIO; direct contracts between the DFIO and dairy farmers are also conceivable.
- The DFIO organises the collection, inspection and possibly also the initial processing of raw milk via the DFAs.
- The DFIO could, if necessary, arrange to supply the dairy industry with appropriate processing products.
- The DFIO organises market equilibrium (seasonal adjustments, short-term market changes)

[3] To date, in the German co-operative sector farmers are generally obliged to supply the milk they produce exclusively to their respective dairy.

National dairy market model



Functioning/structure of the national dairy farmers' IO:

- **Marketing** is undertaken by independent dairy farmer retailer associations on behalf of the dairy farmers' IO (DFIO).
- Members of the retailer associations automatically become members of the dairy farmers' IO.
- Dairy farmers who are not members of retailer associations, but want to supply dairies directly, must also be bound by the marketing initiatives proposed by the DFIO (general liability, cf. chamber of commerce membership, social security, etc.).
- DFs have voting rights in the dairy farmers' IO via their retailer/regional farmers' associations, for the purpose of agreeing market initiatives.

Timeframe: all the measures mentioned in step 3 are to be implemented in the long term.

Other important aspects for a sustainable dairy market

Further development of the CAP 2020

A major obstacle to the objectives formulated in the sector strategy is the target formalised in the preamble since the MacSharry reform: to „reduce agricultural prices", thereby making the food industry competitive, and help agriculture adjust by providing them with direct payments. This Common Agricultural Policy (CAP) focus on the objective of supplying the food industry with cheap raw ingredients must be revised and abandoned. An agricultural policy that does not ensure that food-producing farmers can generate their main income from the sale of their produce is not sustainable. The increasing dependence on taxpayers' money for almost 30 years until now, combined with the associated burgeoning bureaucracy, has increasingly led to a refusal by the younger generation to take over what are actually sustainable businesses.

In order to safeguard long-term agricultural farm funding, the BDM believes it is necessary to link this to specific services that farmers provide to society in the form of climate action and conservation measures. Above all, the social benefits of livestock businesses that can secure a great many jobs should be particularly rewarded when calculating agricultural funding – at least during the transition to a common market organisation which approves prices for agricultural produce that allow the sustainable economic development of livestock businesses.

The specific definition of sustainability

The term „sustainability" is interpreted in a very flexible way, as is the level at which sustainability has to start. In the BDM's view, all production stages are required to engage with this issue and implement potential improvements. This applies both in the field and in the cowshed, but is usually associated with additional costs. Potential savings in the form of equipment or higher yields are often offset by investments in related technologies. In this regard, farmers are open to new technologies such as smart farming or precision farming, but these technologies are associated with high initial investments that must be affordable. Here too, it is clear that in future much more added value will be required from the sale of milk.

Above all, politicians are also required to create important framework conditions for the dairy market, by means of a sustainability-focussed agricultural policy. An agricultural policy that leads to increased animal feed imports into the EU from overseas markets, so that products can be cheaply exported, that does not permit cost-covering farm-gate prices and, all in all, that leads to nutrient surpluses with their associated environmental problems, at least in certain regions, is not sustainable.

Government support for even more animal welfare in dairy farming

Animal welfare depends on many factors, not just the type of husbandry system. One very important factor is the working time required to care for livestock, which must be expended by livestock farmers. Nonetheless, all-year-round tethering is a type of husbandry that urgently requires improvement, as it is increasingly becoming less socially acceptable, much like keeping sows exclusively in farrowing crates. The further development of animal welfare standards, be it towards combined solutions (outdoor yards, etc.) or free-range husbandry, involves enormous costs that are barely justifiable financially or not at all, due to often uncertain succession planning under the given economic conditions. Therefore, the money available to support investment should mainly be used to improve animal welfare. Even more important for these businesses, however, is a financial perspective that allows the refinancing of improvement measures over manageable timeframes (e.g. 10 years). This too requires significantly higher market revenues.

Implementing the sector strategy 2030 steps

When deciding which steps should be taken to shape the market in future, the BDM believes that dairy farmers should be included, via a ballot. This would ensure a genuine grass-roots democracy and opinion-making that is independent of the associations, as well as broader acceptance of the necessary changes. Association discussions about who represents the voices of farmers would then become obsolete. In order to deliver viable long-term solutions for dairy farmers, politicians and scientists should support this process and strategy involving unequally matched market players by appropriately balancing their interests, and deciding in favour of vital rural areas rather than the food industry in the event of potential conflicts of interest. The aim must be to once again make it financially viable for external successors to take over and continue to manage farms.

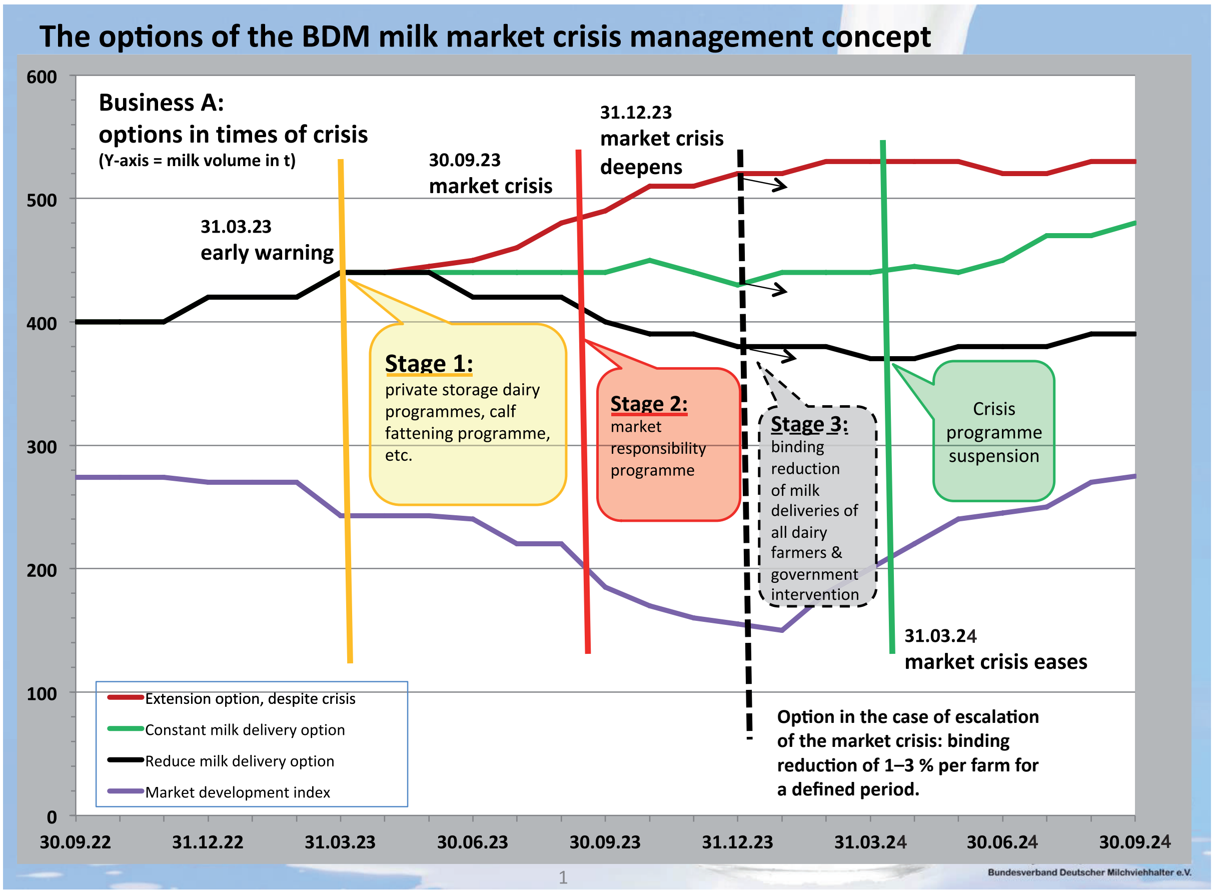
It is clear that the dairy sector needs more competition – not less. All those involved in the industry must therefore take action and support the changes. The BDM regards not embracing real change, but demanding public funds when existing structural problems are leading to market imbalances, as a „fully-comprehensive-insurance-mentality“ that is harming dairy farmers.

The necessary changes must be made step by step, always keeping an eye on which objectives have to be achieved.

An essential element of the BDM concept has already been installed, namely the MMO. Moreover parts of the BDM concept have already been applied, namely the reduction programme of the 2nd EU aid programme and the BMEL's national special dairy allowance.

Progress should continue to be gradual. Approaching a task positively and courageously, making improvements as required, is always better than specifically looking for weaknesses and using these as a pretext for initially failing to begin implementation at all. What have we got to lose? This sector strategy 2030 paper will also be continuously updated with new ideas and findings. The effort is well worthwhile!

ANNEX:



Bundesverband Deutscher Milchviehhalter e.V.
Gutenbergstr. 7-9 l 85354 Freising
info@bdm-verband.de l bdm-verband.org