

Influence of the CMO-wine reform on the Hungarian vineyard potential

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Abstract

The CMO-wine reform was introduced in 2008 and its several new regulation measures fundamentally modified the production potential management in the European wine sector. First, the EU introduced a grubbing-up system for three years with a highly motivating premium in order to obtain a better market equilibrium, and second, abolished the planting rights regime and the liberalization of plantations until 2015.

In our paper, we analyze the influence of CMO-wine measures linked to the vine potential management on the evolution of the Hungarian vineyards and wine sector. We examined the consequences of grubbing-up scheme of 2008-2011 on the total wine production and vineyard evolution by wine regions. We studied the result of vineyard restructuring and conversion regarding the variety structure of new plantations by wine regions. We also analyzed the implementation of planting rights regime in Hungary and the amendments of national regulations since the EU accession. Finally, we analyzed the wine market situation in Hungary.

Key words: CMO wine, reform, Hungary, vineyard, production potential, grubbing-up, restructuring

Introduction

The CMO-wine reform was introduced in 2008 and its several new regulation measures fundamentally modified the production potential management in the European wine sector. First, the EU introduced a grubbing-up system for three years with a highly motivating premium in order to obtain a better market equilibrium, and second, abolished the planting rights regime and the liberalization of plantations until 2015 (DG Agri, 2007). Because of the expected unfavourable socio-economic effect of the liberalization of planting rights (Montaigne et al, 2012, European Parliament, 2012) with the CAP reform of 2013, the end of planting rights lessened at a limited authorization of new vine plantings after 2016 corresponding to 1% of total area of wine producing member states. The measures of vineyard restructuring and conversion have been maintained as one of the tools of reinforcing the competitiveness of European vine-growers.

In general, the Nerlove model is used to evaluate the agricultural supply response to market price (Bräulke, 1982). In this adjustment model it is supposed that farmers make their production decisions by evaluating information about expected prices. Farmers base their production plans on the assumption that current prices will be available in the market in the future according to the Cobweb Theory (Ezekiel, 1938). These reflections are especially suitable in the case of perennial plants such as grape vine, of which vine growers make decisions after carefully taking into consideration the medium or long term wine market trends.

A recent study (European Parliament, 2012) underlined after the analysis of dynamics of wine growing areas in the main wine producer Member States with Nerlove model that in the European Union, there is no evidence of a significant effect of wine market prices on vine growing areas, except the case of France.

In the EU, the supply control policy had an important market stabilizing effect with restriction of new plantations and distillations. Vineyard grubbing up that was one of the most important instruments in the EU during the period of 1988-1996 in order to retain the market equilibrium, but used rarely before the CMO wine reform in spite of the overproduction problems¹ (European Commission, 2006), had no significant results in terms of wine growing area response to prices. The EU study (European Parliament, 2012) highlights that prices for grubbing up premium do not change the structure of the supply model and confirms the existence of strongly conservative elements in wine growers' decision making.

In our paper, we analyze the influence of CMO-wine measures linked to the vine potential management on the evolution of the Hungarian vineyards and wine sector. We have to underline as well that beyond the grubbing-up scheme, vineyard restructuring and planting rights that determine directly the Hungarian wine production potential, the other regulating measures like the PDO/PGI wine production rules, the new wine labelling rules linked to the varietal wines, producer and inter-branch organizations, or investments in wine production have also effect on the evolution of vineyard surface. Finally, we have to mention the economic situation of Hungarian wine market (production, import and wine price trends) as an influencing factor of wine growing area.

Our evaluation is based on the database of European Commission, Ministry of Rural Development, Agriculture and Rural Development Agency (ARDA-Hungarian paying agency) and the National Council of Wine Communities (HNT). We examined the consequences of grubbing-up scheme of 2008-2011 on the total wine production and vineyard evolution by wine regions. We studied the result of vineyard restructuring and conversion regarding the variety structure of new plantations by wine regions. We also analyzed the implementation of planting rights regime in Hungary and the amendments of national regulations since the EU accession. Finally, we analyzed the wine market situation in Hungary.

1. Evolution of wine production potential in Hungary

Area actually planted with grape vine covers 64 188 ha (in 2013) and decreases continuously. This tendency could have been observed since the end of 1960's when Hungary possessed 220 000 ha of vineyard. The evolution of wine growing area already registered a strong decline and transition period contributed to the worsening of the situation. In 1989, Hungary still possessed 140 000 ha of grape vine; in 2004 at the moment of EU accession vineyards covered 93 000 ha. During the last 25 years 54% of wine growing area was lost in Hungary (Chart 1.). This quick decline has several origins:

1. Privatization procedure of land, co-operatives and state firms that integrated every technical itinerary of wine production was completely broke up. One part of new owners without viticulture competence grubbed up their vineyard, changed the culture or let land out.
2. Many grape vine growers abandoned vineyard because of the low profitability of viticulture or the collapse of wine market after 1989.

¹ Main wine producer MS (Spain or Italy), did not implement abandonment premium in the period of 1999-2007 in spite of their surpluses and they withdrew great volumes of wine with distillation measures such as the support for potable alcohol distillation (10-12 million hl table wine/year) or crisis distillation that played an important role in the wine market stabilization.

3. Low rate of vineyard conversion during 1990's: between 1990 and 1998, when only 2 500 ha of grape vine were planted in Hungary in spite of 3000-5000 ha/year necessary for renewing vineyards (Erdész, Radóczné, 2000).
4. During the transition period, agriculture and the development of agricultural markets involved high risk that made difficult to obtain credit for investments in the wine sector.
5. Implementation of state support system in the pre-accession period (1998-2003) in order to encourage new plantations was not sufficient to stop the fall of vine production potential.
6. After EU accession, definitive abandonment premium become available also for Hungarian wine growers. First, Hungary planned to avoid the implementation of this measure while the objective was to maintain the production potential, but this strategic principle was abandoned quickly with the effect of the unfavourable market situation (increasing stocks, price drop) and because of the pressure of wine growers. Due to temporary overproduction in 2004/2005 and grape vine growing characterized by weak profitability, producers eliminated 5 406 ha² of vineyard with EU support (Table 1).
7. Grubbing-up program of the CMO-wine reform accelerated the decrease of Hungarian vineyard surface. After the reform, 5 703 ha of grape vine were eliminated in the period of 2008-2011 with European subsidy³.

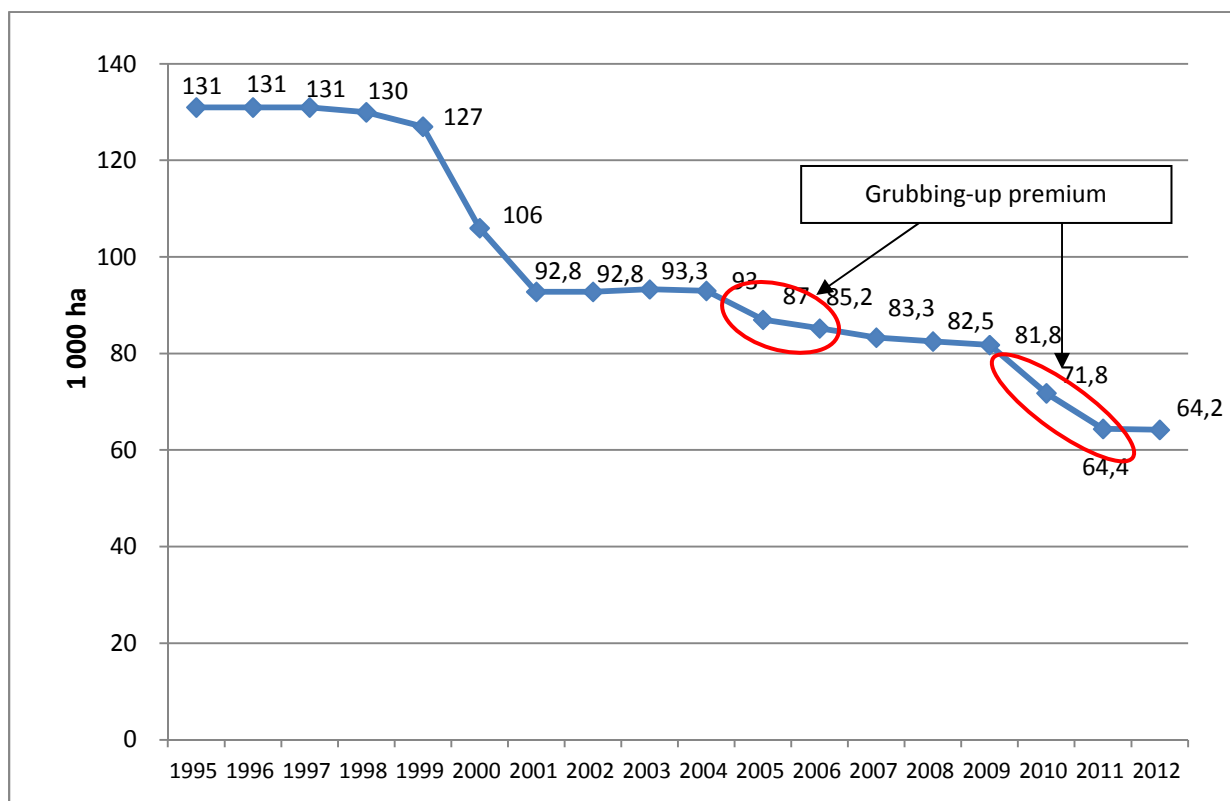


Chart 1. Changes in the area planted with grape vine in Hungary (source: National Council of Wine Communities – HNT)

² Source : ARDA (Mezőgazdasági és Vidékfejlesztési Hivatal – MVH), 2011

³ Source : ARDA (Mezőgazdasági és Vidékfejlesztési Hivatal – MVH), 2011

1.1. Consequence of grubbing-up scheme in Hungary

The estimations of the European Commission (2012) illustrate that with the removed area (6.7% of the total wine growing area) between 2008 and 2011, Hungary - among the Member States – is at the first place with 11.3% of wine production reduction (366 000 hl) considering their average production (in comparison with Spain - one of the most important wine “over-producers” – wine production reduction is estimated at 10.9% as a consequence of this measure). This result is remarkable, while since 2005 – except the 2008/2009 wine year – the Hungarian wine market has been characterized by production deficit. Furthermore, during the recent period we registered the negative records of wine production (1.8 million hl in 2010 and 2012) because of the unfavourable weather conditions (Chart 2). Total wine production reduced by 31% in the recent period.

Table 1. Abandonment premium in the period of 2005-2011

Year	Grubbing-up (ha)	Amount of support 1000 €
2005/2006	3 604	21 637
2006/2007	1 802	10 958
2008/2009	1 425	9 756
2009/2010	1 995	12 828
2010/2011	2 283	13 490
Total	11 109	68 669

Source: DG Agri and ARDA– MVH

As a consequence of the abandonment premium program of the CMO-wine reform, the majority of grubbing up was carried out in Kunság (78%), Mátra (11%) and Csongrád (4%) wine regions, the other 19 wine regions shared the rest⁴.

We also have to emphasize that Hungary have never contributed to the overproduction and the imbalances of the European wine market. Grubbing-up premium obtained its popularity due to the encouraging amount of support (in average 6 325 €/ha). 75% of beneficiaries were grape growers older than 55 years old or producers without a successor.⁵ The defenceless situation of viticulturists, the low profitability level of grape-growing, the lack of their organization and vertical coordination played an important role in their grubbing-up decision.

⁴ Source : ARDA (Mezőgazdasági és Vidékfejlesztési Hivatal – MVH), 2011

⁵ Source : ARDA (Mezőgazdasági és Vidékfejlesztési Hivatal – MVH), 2011

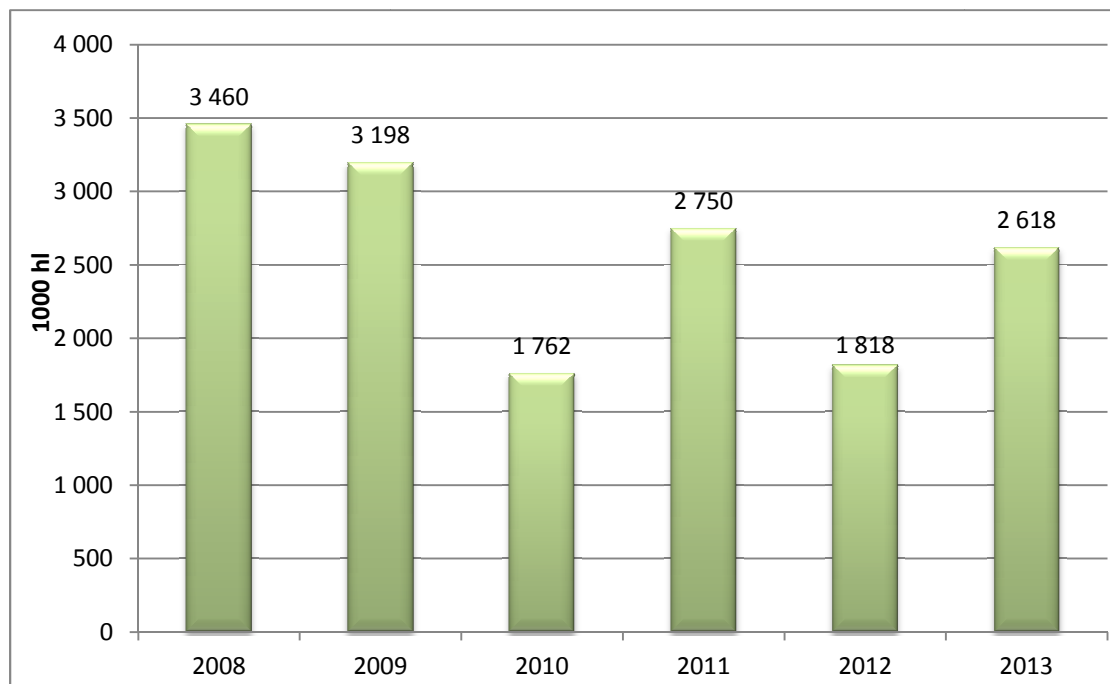


Chart 2. Wine production in Hungary (2008-2013) Source: DG Agri

1.2. Vineyard restructuring and conversion

Parallel to the decreasing vineyard surface, we can register a significant qualitative development in several wine regions during the last 15 years thanks to the state subsidies in the pre-accession period (1998-2003) to encourage new plantations adapted for market demand, then to the European subsidies. Since the EU accession, the vineyard reconstruction and conversion considered the most important measure financed by the CMO-wine. As a result, 15 647 ha of vine were planted by EU financial support in the period of 2004-2012⁶.

In the national support program where Hungary received 122 123 000 € as national envelope for the period of 2009-2013, 84% of the budget was spent to the vineyard reconstructions (Table 2 and Chart 4), while vine plantation without subsidy became insignificant (only 5% of the total plantation since the EU accession).

⁶ Source: ARDA (Mezőgazdasági és Vidékfejlesztési Hivatal – MVH), 2013

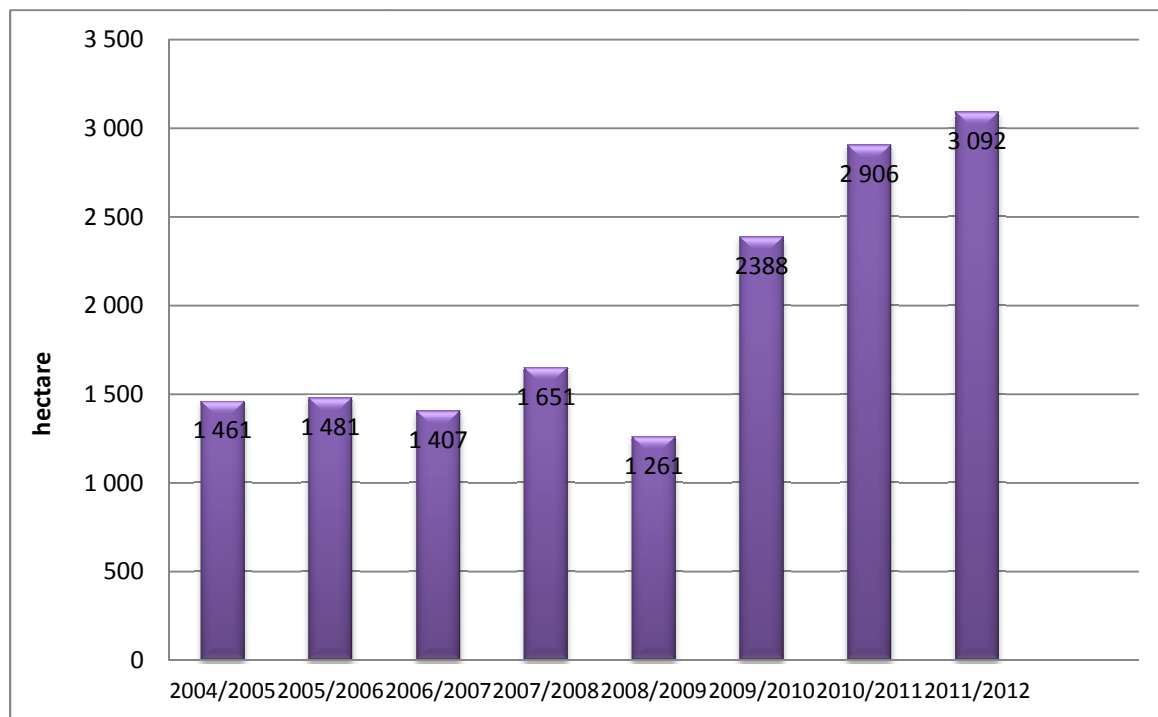


Chart 3 Surface planted with vineyard restructuring and conversion (2004-2012) Source: ARDA (MVH)

Table 2. Financial execution of the National Support Program in the Hungarian wine sector (2009-2013)

Measure	EC 555/2008	2009	2010	2011	2012	2013	Total	%
1. SPS	Art. 8a	0	0	0	0	0	0	
2. Promotion	Art. 9	0	0	0	0	0	0	
3a- Restructuring and conversion of vineyard	Art. 10	13 798	19 098	21 511	25 640	22 592	102 639	84%
3b- Ongoing plans	1493/1999		0	0	0	0		
4. Green harvesting	Art. 11	0	0	0	0	0	0	
5. Mutual funds	Art. 12	0	0	0	0	0	0	
6. Harvest insurance	Art. 13	0	0	0	0	0	0	
7. Investments in enterprises	Art. 13a	0	0	1 063	2 619	5 739	9 421	8%
8. By-product distillation	Art. 13b	1 963	1 628	758	800	750	5 899	5%
9. Potable alcohol distillation	Art. 13c	438	1 757	0	0		2195	2%
10. Crisis distillation	Art. 13d(1)	0	0	0	0		0	
11. Use of concentrated grape must	Art. 13e	611	519	475	394		1999	1%
Total		16 811	23 002	23 807	29 452	29 081	122 153	100%
<i>Budget allocated (EC 479/2008 Annex II)</i>		<i>16 816</i>	<i>23 014</i>	<i>23 809</i>	<i>29 455</i>	<i>29 081</i>	<i>122 175</i>	

Source: DG Agri and ARDA (MVH)

It is necessary to underline that in spite of the relatively great surface of grubbing-up, the majority of vineyard restructuring and conversion was also realized in the Kunság wine region. 2/3 of this investment was carried out in this wine region mainly with resistant hybrid varieties (such as Bianca and Aletta). The change in area planted with these varieties is significant: the area covered by Bianca tripled and Aletta (1 184 ha in 2012) spread widely during the last ten years. Bianca with 4 023 ha became the 4th most important variety in Hungary regarding the area covered by vines. That means a producer behaviour striving for production cost reduction, harvest security and mass production in spite of quality development to achieve high added value wines in certain wine regions (Kunság and Csongrád). Among the most important varieties, the area of Csereszegi fűszeres, Merlot and Cabernet sauvignon increased slightly, while the area of traditional local varieties like Kékfrankos, Ezerjő, and Olaszrizling dropped significantly, only Furmint preserved its position during the last period (Chart 4).

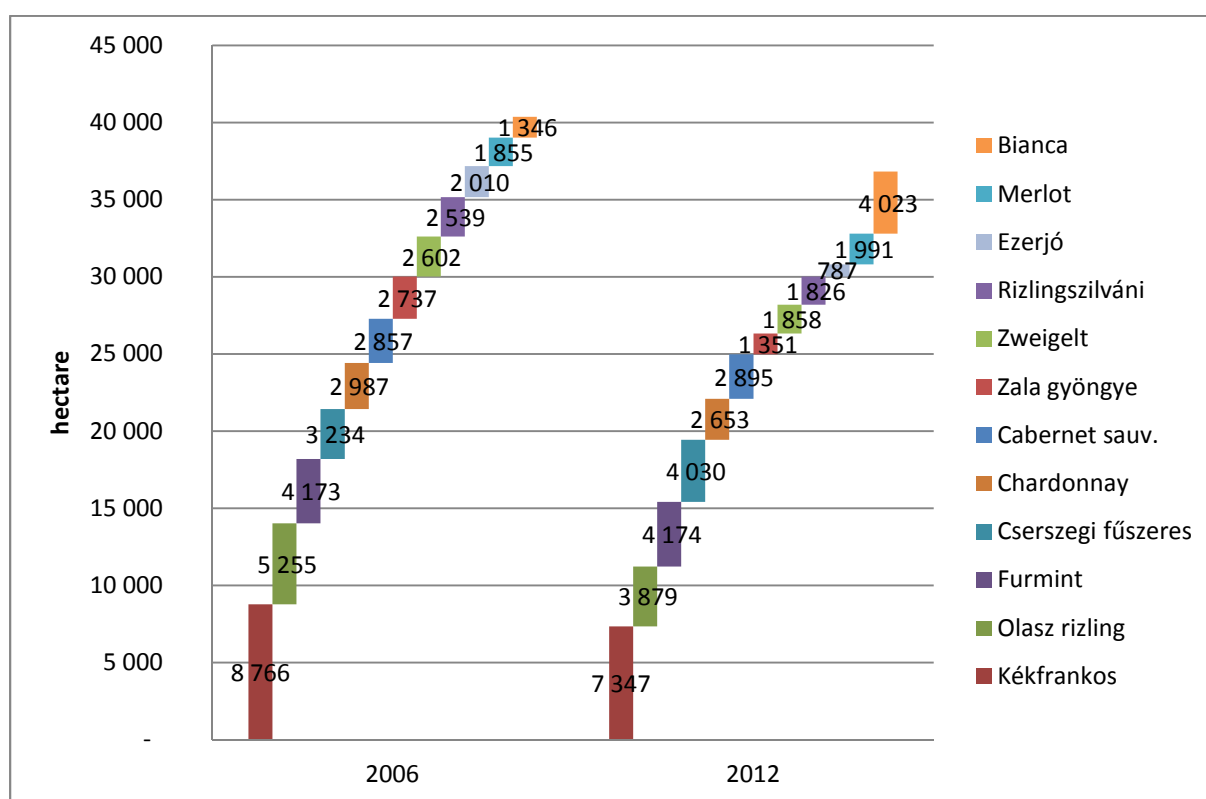


Chart 4. Change in the area covered by the most important grape vine varieties in Hungary (Source HNT, 2013)

Regarding vineyard restructuring, the other appellations remain further behind Kunság, in order of their area: Tolna (5.7%), Mátra (5.3%), Balatonboglár (4.4%), Villány (3.5%), Hajós-Baja (3.5%), and Tokaj (3.3%) are the wine regions where the vineyard restructuring measure can be considered as important. These wine regions invest rather in the plantations that give raw materials for high quality wine production of PDI wines.

We have to note that a part of the grubbing-up support was reinvested in the vineyard restructuring. In several cases the producers used abandonment premium for financing the new plantations, thus to ensure investment at vineyard modernization. It was an important

solution, because restructuring is a post-financed measure (ARDA pays subsidy only for the realized investments). In family owned enterprises this type of transfer is typical between the members of family. In general they are individual grape vine growers, thus the member of family over 55 years old assuming the grubbing-up the entire vineyard received the abandonment premium, then the young members of family carried out the new wine plantations with this resource and received the vineyard restructuring support.

Considering the total Hungarian wine production, the results of these investments are visible: the production of grape vine classified in PDO compared to the total production increased from 40% to 60% in the period of 2004-2013 (Chart 5). Actually, the area under vines classified in PDO covers 46.430 ha (72.3% of the total area under vines), the PGI are spread out to 9 342 ha (14.6%) and grape vine area for the wines without geographical indication attains 8 916 ha (13.1%).

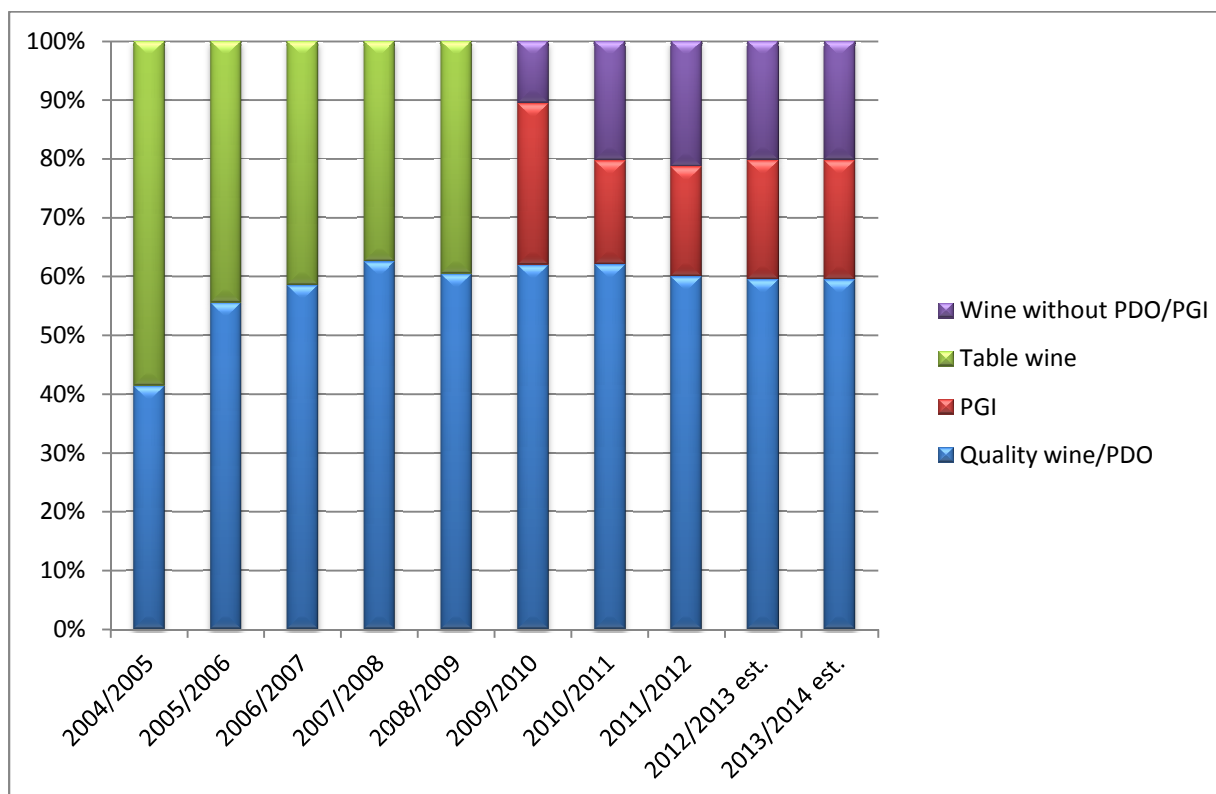


Chart 5. Hungarian wine production by categories (2004-2012) Source: DG Agri and HNT

2. Planting rights regime

Planting rights regime is one of the most important tools of the wine market organization and the wine supply regulation in the EU.

The method of planting rights management and its legal framework changed several times since its introduction in the Hungarian wine sector. Before the EU accession the vine plantation was attached to the wine communities' authorization without using planting rights but linked to an authorization process and area classification on the basis of favourable pedo-

climatic characteristics. The implementation of CMO-wine introduced the planting rights regime in Hungary without national reserve and regulated market that contributes to free exchange of planting rights among producers and regions. Wine communities treated the planting rights database but ARDA delivered the plantation authorizations. After the CMO-wine reform, ARDA centralized the planting rights, managed the national reserve and regulated the planting rights market. In 2013, in order to simplify administration linked to vine plantation authorization, the planting rights management was transferred to National Council of Wine Communities.

In Hungary the planting rights regime is not considered as an obstacle of new plantings while grubbing-up (without abandonment premium) always exceeded the surface of new plantations. At the moment of the EU accession 12 500 ha planting rights beyond the total 93 000 ha of vineyard area existed. During the last ten years 11 109 ha of vineyards were grubbed-up with abandonment premium, planting rights were not generated while the objective of this measure is the definitive elimination of one part of production potential. Planting rights generated after grubbing-up (around 17 700 ha) have abundantly covered the planting rights demand for new plantations.

3. Market situation

Average wine production volume in the period of 2009-2013 was 2.6 million hl (-19%) compared to the average of previous 5 years (2005-2009), due to the grubbing-up and unfavourable weather conditions.

Wine production is conducted in 22 wine growing regions, where 31 geographical denominations for PDO and 5 for PGI can be found.

Hungary exports around 650 000 hl of wine (625 000 hl in 2012) that is equivalent of 25% of total Hungarian wine production. After a period with relatively stable exported volumes of around 700 000 hl of wine, this volume has been decreasing since 2010 (-25%). The most important destinations of Hungarian wines are in order of volume: Germany (24%), Czech Republic (14%), Slovakia (14%), Great-Britain (8%), and Lithuania (6%). 90% of Hungarian wines are exported to other EU member states. During the last five years, several negative changes occurred, Hungary could not profit from the growing market of Poland and Russia, where Hungarian wines registered a loss of their positions.

Wine consumption trend showed a slight increase in Hungary between 1998 and 2007, but the economic crisis had a negative effect on wine consumption, in 2011 it attained 26 litres/capita/year (-22% than in the period before crisis).

Despite the fact that Hungary produces a sufficient amount of wine for covering the domestic consumption, Hungary imports a considerable volume of wine. Since the EU accession, imported volume augmented significantly from 42 000 hl to 591 000 hl between 2004 and 2013. The majority of imported wines (75%) arrive from Italy. Hungary imports cheap red bulk wines in order to satisfy the supply of mass wines. These products have extremely competitive prices (average price of Italian import: 45 €/hl⁷, red bulk wine 16 000 HUF/hl in 2013⁸) compared to the price level of Hungarian bulk wines. In general, the Hungarian bulk

⁷ Source: KSH (Hungarian Central Statistical Office) and National Council of Wine Communities (HNT), 2014

⁸ Source: AKI, 2014

wine price at production level (20 000 HUF/hl in case of red bulk wines)⁹ approaches or exceeds the French bulk wine price level (19 000¹⁰ HUF/hl in case of red bulk wine and 62.97 €/hl for every bulk wine in 2013¹¹).

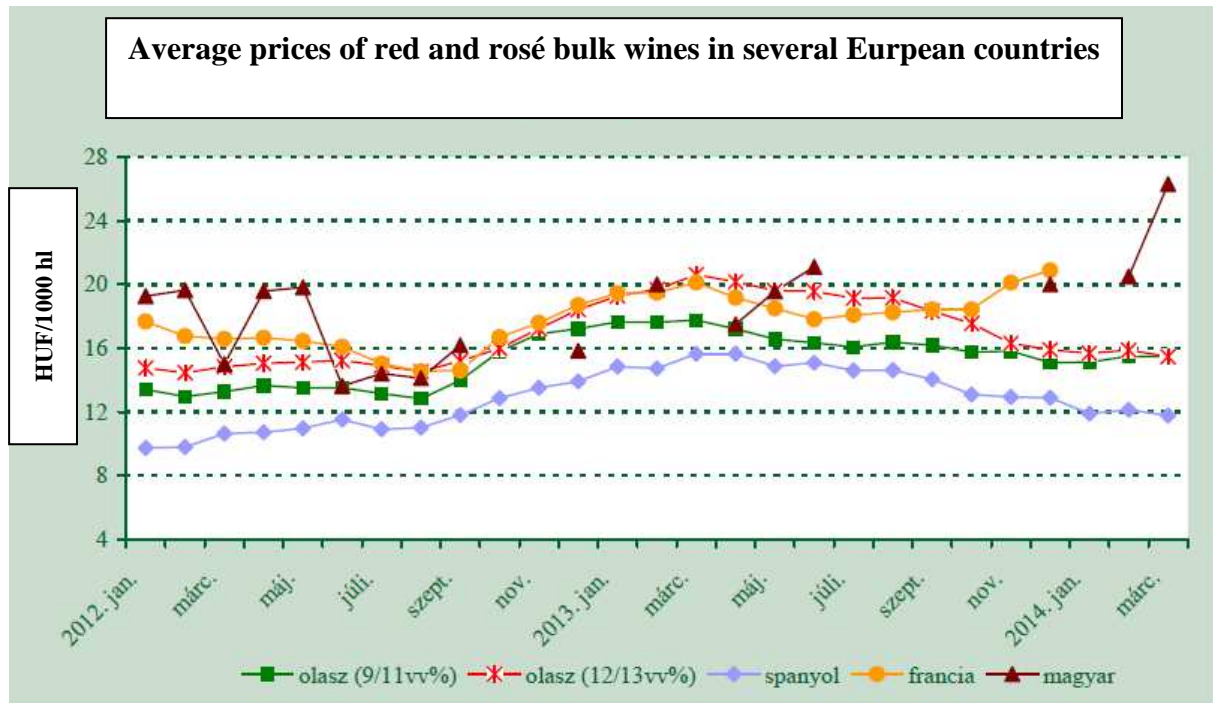


Chart 6. Italian, Spanish, French and Hungarian red and rosé bulk wine price evolution
(source: AKI, Borpiaci információk p. 4. 7. ábra)

The limited authorization of new plantings – introduced by recent CMO reform – after 2016 can contribute to enlarge the Hungarian vineyard potential by 1% of total wine producing area, but regarding the market organization and situation of Hungarian wines (decreasing production, significant growth in imports) and growing competition on the wine market, we do not anticipate increasing vineyard plantation, rather proceeding shrinkage of production potential. The new regime will simplify the administrative procedure and administrative costs of vineyard planting.

Conclusion

Implementation of CMO measures linked to the wine growing potential had dual effects on the area of Hungarian vineyards. Abandonment premium accelerated the long-term decreasing trend of Hungarian grapevine area, while restructuring and conversion measures contributed to the renovation and modernization of Hungarian vineyards on an increasing area since the EU accession and more significantly after the CMO-wine reform. Vineyard reconversion measure also has a dual effect: this measure aims the development of wine growers' competitiveness and contributes to their free choice of wine types demanded by consumers. In

⁹ Source: AKI, 2014

¹⁰ Source: AKI, 2014

¹¹ Source : FranceAgrimer, 2013

Hungary, in the mass wine producer regions, the hybrid resistant varieties became dominant because of the rationalization of grape growing costs, while in the other regions the investments at high quality raw material production is characteristic. In Hungary, the planting rights regime has no real market regulation effect because they are abundantly available, while grubbing-up overtakes new plantations. The limited authorization of new plantings after 2016 permits to enlarge the Hungarian vineyard potential by 1% of total wine producing area, but regarding the market organization and situation of Hungarian wines (decreasing production, exponential growth of imports, cheap imported wines) and growing competition on the Hungarian wine market, we do not anticipate increasing vineyard plantation, rather proceeding shrinkage of production potential. The plantation choice of producers could be influenced by a more efficient vertical coordination of the actors of the wine sector and with the introduction of medium (or long) term contracts that represent a more predictable situation for grape vine growers.

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