

MARKET IMPLICATIONS OF GOVERNMENT PURCHASES OF DAIRY PRODUCTS TO SUPPORT FARM PRICES

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The dairy price support program is simply a purchase program for dairy products. The Commodity Credit Corporation in effect becomes a customer for designated dairy products. Non-recourse loans or deficiency payments or other kinds of price support mechanisms have not been a part of the program. The dairy price support program has the basic purpose of supporting the price paid dairy farmers for milk. But the means of attaining that objective is to buy dairy products from manufacturing plants, not milk from dairy farmers. Therefore, milk producers do not have a direct sense of what the program does for them, or what the program does to the market for milk. Many agricultural price-income programs have their focus at the farm. This was even true to some extent for dairy when the Milk Diversion and Dairy Termination Programs were in operation. But the purchase program used to support milk prices to dairy farmers is implemented at the plant level and is not very visible from a dairy farmer perspective.

Procedures Used in the Dairy Support Program

The products that the Commodity Credit Corporation (CCC) has elected to purchase for price support purposes include butter, nonfat dry milk, and cheddar cheese. These dairy products have been selected because they:

- are storable;
- are concentrated relative to the volume of milk required to manufacture them;
- are transportable at relatively low freight costs;
- are useable in a wide range of domestic and foreign outlets;

- account for nearly 50 percent of the annual utilization of milk in the United States, and;
- are produced in large volumes with a standard product identity or definition.

In the four-year period from 1988 through 1991, the Commodity Credit Corporation purchased the following quantities of product for price support purposes:

Year	Butter	American Cheese (million lbs.)	Nonfat Dry Milk	Total Solids Equivalent (billion lbs.)
1988	313	214	267	6,692
1989	423	24	0	3,950
1990	387	22	128	4,515
1991	443	122	271	6,977

Source: Agricultural Stabilization and Conservation Service, USDA.

As the data show, the Commodity Credit Corporation purchased the equivalent of anywhere from 4 to 7 billion pounds of milk annually in the form of butter, cheese, and nonfat dry milk in the 1988 through 1991 period.¹ No other single customer for dairy products in the United States came even close to the quantities purchased by CCC. The largest quantity of dairy products ever purchased in a single calendar year was 1983 when 18.8 billion pounds milk equivalent or 13.7 percent of milk marketed off farms was acquired for price support purposes. However, over the history of the dairy price support program, purchases have been more modest. From the beginning of the program in 1949 through 1978, annual price support purchases averaged only 4.2 percent of marketings on a milkfat basis and 6.4 percent of marketings on a solids-not-fat basis.

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¹Milk equivalent aggregates of different dairy products are expressed here on a total solids basis, not the traditional milkfat basis. See Leaflet P-2 for further details.

For each of the products, using 1991 as the reference point, the CCC purchased:

- 32 percent of butter production
- 3 percent of cheddar cheese production
- 30 percent of nonfat dry milk production.

It is evident that as the government purchases such substantial quantities of dairy product, it must have a substantial effect on the market for milk—on price, on supply, on demand.

Purchase Price Computations

The CCC purchase prices for the products purchased at plants are established at levels that should permit those plants to pay at least the support price for manufacturing grade milk. As of July 1, 1990, the support price was established at \$10.10 (averaging 3.67 percent butterfat). The effective 3.5 percent butterfat support price for milk (effective May 13, 1992) is \$9.97 per cwt. The announced CCC product purchase prices established to make the \$10.10 goal achievable as of mid-1992 are as follows:

- Butter, grade A—\$0.7625 per pound
- Cheddar cheese—\$1.1175 per pound
(40 or 60 pound blocks)
- Nonfat dry milk extra grade, unfortified—
97.3 cents per pound

The purchase prices for products are established by adding an assumed industry-wide make-allowance to the announced support price for milk. The make-allowances that the USDA has adopted since 1979 have been \$1.37 per hundredweight of milk for cheese and \$1.22 for butter and nonfat dry milk. The make-allowance for cheese is reduced by the butter-value of the whey cream by-product, bringing the net allowance to \$1.18. There are no further adjustments for by-products of either cheese or butter and nonfat dry milk. The gross (wholesale) values for product are then divided by assumed yield factors to establish a national purchase price per pound of each product. For example, if the support price for milk is \$10.10, the cheese make-allowance of \$1.37 is added to that to establish a value of cheese and whey per 100 pounds of milk. The value of whey fat per 100 pounds of milk for cheese is currently estimated at 19 cents; it is subtracted from the gross value as CCC does not buy whey cream and the plant can realize the whey cream value in the market.² The gross value of the cheese per 100 pounds of milk then is \$11.28. The \$11.28 value is divided by the cheese yield factor of 10.1 pounds. A purchase price for cheese of \$1.1175 per pound is established by this procedure. The idea is that if a plant can sell its cheese to the CCC (presumably as a last resort) for \$1.1175, it should be able to pay its dairy farmers the targeted support price of \$10.10. (Table 1 is a reproduc-

² By-products are commented on more fully in a later section of this paper.

Table 1. Calculation of CCC Purchase Prices for Dairy Products with Support of \$10.60 and \$10.10 per cwt.

Item	Effective July 1 through December 31 1989	Effective January 1, 1990
Support price for manufacturing milk, \$/cwt at 3.67% milkfat	10.60	10.10
Support price for manufacturing milk, \$/cwt at 3.5% milkfat	10.35	9.88
Average milkfat test, percent	3.67	3.67
Butterfat differential ¹	14.5	13.1
Yields per 100 pounds of milk at average test (pounds)		
Butter	4.48	4.48
Nonfat Dry Milk	8.13	8.13
Cheese	10.1	10.1
	(\$/cwt)	(\$/cwt)
<u>Butter-Nonfat Dry Milk Price Calculation</u>		
Return to butter-NDM	10.60	10.10
CCC manufacturing allowance for converting 100 pounds of whole milk into butter and nonfat dry milk	1.22	1.22
Value of butter and nonfat dry milk (U.S. average) made from 100 pounds of milk	11.82	11.32
<i>Nonfat dry milk purchase price (rounded), \$/lb.</i>	.7900	.7900
Value of nonfat dry milk per 100 pounds of milk ²	6.42	6.42
Value of Butter:		
Dollars per 100 pounds of milk	5.40	4.90
Dollars per pound (calculated) ³	1.20535	1.0937
<i>Butter purchase price (rounded), \$/lb.</i>	1.2050	1.0925
<u>Cheese Price Calculation</u>		
Return to cheese	10.60	10.10
CCC manufacturing allowance for converting 100 pounds of whole milk into cheese and whey	1.37	1.37
Value of cheese and whey per 100 pounds of milk	11.97	11.47
Value of .25 pounds of whey fat: ⁴	.30	.27
Value of cheese:		
Dollars per 100 pounds of milk	11.67	11.20
Dollars per pound (calculated) ⁵	1.1554	1.1089
<i>Cheese purchase price (rounded), \$/lb.</i>		
Block	1.1550	1.1100
Barrel	1.1150	1.0700

¹Butter purchase price times 0.12. ²Nonfat dry milk price per pound times 8.13. ³Value of butter per 100 pounds of milk divided by 4.48. ⁴Butter purchase price times 0.25. ⁵Value of cheese per 100 pounds of milk divided by 10.1.

Source: Dairy Market News, USDA-AMS; Vol. 56, Report 52, December 25-29, 1989, p.10.

tion of USDA's announcement of CCC purchase prices effective January 1, 1990.)

Similar procedures are used for establishing butter and nonfat dry milk (NDM) purchase prices. A make-allowance of \$1.22 is added to the \$10.10 support price. However, because butter and nonfat dry milk are joint products, and because butter only carries the milkfat and nonfat dry milk only carries the solids-not-fat, an additional arbitrary decision must be made on how much of the value of milk should be in the milkfat and how much in the solids-not-fat. With a support price of \$10.10 and a make allowance of \$1.22, the gross value of milk made into butter and NDM is \$11.32. The USDA yield factors are 4.48 pounds for butter and 8.13 pounds for nonfat dry milk. In its May 6, 1992 purchase price decision, the USDA essentially concluded that milkfat was worth only about 30 percent (\$3.41) of 100 pounds of milk and the solids-not-fat was worth 70 percent (\$7.91). The butter price was therefore established by dividing \$3.41 by 4.48 pounds (equals 76¼ cents), and the nonfat dry milk price by dividing the \$7.91 by 8.13 pounds (equals 97.3 cents).

Obviously in a year such as 1991 when CCC purchased 443 million pounds of butter, the purchase price for butter does have massive effects in the marketplace—for milk, for milkfat and cream, and for products having a high cream content, as well as butter. Although purchases of cheese and nonfat dry milk have been trivial recently, when these products have been in surplus, their purchase prices have had similar effects.

Demand Issues in the Dairy Price Support Program

The intent of this discussion is to consider more closely the demand side of the market implications of the purchase program. There are obviously supply side effects as well. For example, the higher producer prices generated by the price support program when surplus milk is in evidence generates a farm supply response. Also, the reduced price and income risk in milk production due to the fact that a price support program is in operation is a factor associated with increased milk production. The dairy price support program can have a galvanizing impact on the level of milk production, particularly when the support price departs significantly above a market-oriented focus.

Three market-demand issues associated with the CCC purchase program for dairy products can be identified. They include 1) the price relationship or the so-called "tilt" between milkfat and solids-not-fat (SNF) caused by the respective CCC purchase prices for butter and nonfat dry milk, 2) the potentially adverse demand effects on milk and dairy products caused by higher price levels due to higher wholesale and raw milk prices resulting from the support program, and 3) the virtual exclusion of most U.S. dairy products from export markets in most periods of time due to fact that CCC purchase prices generally exceed world product prices.

Milkfat - SNF Price Relationship

The tilt question relative to milkfat and solids-not-fat caught industry-wide attention in the spring of 1989 when the U.S. Department of Agriculture was required by the Disaster Assistance Act of 1988 (drought relief) to increase the support price for milk for three months. The increase was from \$10.60 to \$11.10 per cwt, but it was not taken equally on butter and nonfat dry milk.

A change in the support price for milk requires a change in the CCC purchase prices for product. The purchase prices for butter and nonfat dry milk can also be changed in an offsetting way without a change in the support price for milk. A realignment of butter and NDM prices has now occurred four times with milk at the \$10.10 support price. The 1990 farm bill permits the USDA to adjust the butter-NDM price relationship twice within a calendar year. Butter and nonfat dry milk purchase prices were changed in January and May of 1992.

The component tilt question does not affect cheese very much because cheese carries both the milkfat and solids-not-fat in milk, but when the butter price is reduced there is a very slight increase in the cheese price as the value of whey cream is reduced.

Changes in the relative prices announced for butter and NDM can have substantial impacts in the marketplace. The following example helps illustrate the point. Assume that the support price for milk is to be increased 50 cents per cwt. The new purchase price for cheese is calculated simply by dividing the 50 cents by the accepted CCC yield factor for cheese—10.1 pounds of cheddar cheese per hundredweight of milk. Fifty cents divided by 10.1 equals 4.95 cents, therefore the new purchase price for cheese would be announced at about 5 cents per pound higher than the previous price.

For butter and nonfat dry milk, however, an arbitrary decision must be made as to how much of the 50-cent increase should be put on the milkfat side, and how much on the SNF side. If it is determined that one-half of the increase should be placed on the milkfat and one-half on the SNF, as was the case during the latter 1970s, the purchase price calculations would be as follows:

50 cent increase in milk support price,	
25 cents milkfat	25 cents solids-not-fat
+	+
4.48 lbs. butter/cwt milk	8.13 lbs. NDM/cwt milk
equals	equals
+ 5.6 cents	+ 3.0 cents/lb.

In this example, with a 50/50 split, the purchase price for butter is increased by 5.6 cents per pound and the purchase price for powder is increased by 3.0 cents per pound. What if the USDA determined that there was surplus butter relative

to nonfat dry milk as has been the case in the late 1980s and early 1990s? In that case, they could add 100 percent of the increase on the SNF side and increase NDM prices by 6.15 cents per pound (50 cents divided by 8.13 pounds), while leaving the butter price alone. In the opposite situation, assuming a shortage of milkfat relative to solids-not-fat, the butter price could be increased by 11.2 cents per pound (50 cents divided by 4.48 pounds) and the nonfat dry milk price left alone. For that matter, there is nothing to prevent USDA from tilting butter and nonfat dry milk prices by more than the change in the support price, when the support price changes. As noted earlier, the price relationship has been changed when there was no change in support. Hypothetically, USDA could make butter free and put all the support value on milk. Thus, USDA must decide how much of a change is needed to bring the relative balance of supply and demand into alignment without unduly disrupting wholesale markets.

Obviously, there is a wide discretionary range in which to operate in establishing the joint butter-powder prices. The decision can have major market implications. In Table 2, the changing price ratios for butter and nonfat dry milk as reflected in CCC purchase price decisions are shown for selected years since the price support program started.

Table 2. Milk Support Price, CCC Purchase Prices for Butter and Nonfat Dry Milk, Selected Years, 1949-1992.

Year	Support Price 3.67% (\$/cwt)	Butter Price (\$/lb)	Nonfat Dry Milk Price ¹ (\$/lb)	NDM/Butter Price Ratio (%)
1949	3.14	0.59	0.1225	0.21
1960	3.06	0.58	0.1340	0.23
1970	4.66	0.70	0.2720	0.39
1974	6.57	0.606	0.566	0.93
1981	13.10	1.49	0.940	0.63
1988	10.60	1.32	0.7275	0.55
1989	10.60	1.205	0.790	0.66
1992 (1/17)	10.10	0.8725	0.912	1.05
1992 (5/13)	10.10	0.7625	0.973	1.28

¹From 1949-1959, price reported for barrels and drums; from 1960-1970, for 100 lb. bags; and from 1971 on, for 50 lb. bags.

Source: 1988-89 Dairy Price Support Program - ASCS Commodity Fact Sheet, USDA-ASCS, April, 1989.

The relative value of nonfat dry milk trended slowly upward in the 1950s and 1960s. The USDA placed more emphasis on nonfat dry milk, mostly because commercial demand for butter was dropping rapidly. As the data indicate, the early 1970s marked a turbulent period. In the early to mid-1970s with milk in a fairly tight supply-demand balance and periodic shortages of nonfat dry milk, the USDA, in retrospect, made butter-powder price decisions that did much damage to the powder market without doing much to save the butter market. In 1974, the CCC purchase price for nonfat dry milk (56.6 cents) was almost as high as the CCC purchase

price for butter (60.6 cents), a record ratio of 0.93. In several years during that period, as the support price for milk was increasing, more than 100 percent of the increase was placed on powder, and the purchase price for butter dropped. Per capita sales of nonfat dry milk dropped from 5.4 pounds in 1970 to 1.9 pounds in 1987.

The commercial market absolutely rejected the high prices for nonfat dry milk. By 1980, the CCC ended up purchasing 634 million pounds of nonfat dry milk or 55 percent of all of the nonfat dry milk manufactured that year. The point here is not to criticize past decisions but to emphasize how important and far-reaching are the market implications of the relative values arbitrarily assigned to butter and nonfat dry milk. It is not an easy choice for USDA to make each time the support price changes. Any relative price relief for the one commodity forces a relative price burden on the other commodity.

The prices established for butter and nonfat dry milk translate into the basic values for milkfat and solids-not-fat in all dairy products (assuming that there is surplus milk and that wholesale butter and powder prices have dropped to CCC purchase price levels).

An additional criterion, other than market implications, also is recognized by the USDA as it considers the relative purchase prices for butter and nonfat dry milk. This criterion has to do with the effect on costs or net expenditures for dairy price support. For example, if one of the commodities is in shorter supply than the other, and carries a wholesale market price above the CCC purchase price, the USDA would consider placing more of the price emphasis on the commodity in shorter supply. Such an action would presume that even at the higher purchase prices, the Commodity Credit Corporation would not have to buy much if any of the commodity and could therefore reduce total purchase costs, even at a higher support price. This was basically the case in the second quarter of 1989 when all of the required 50-cent increase in the support price for milk was placed on nonfat dry milk, and the butter price stayed the same. Three months later, on July 1, 1989, all of the required 50-cent decrease in the support price was placed on the butter, and the nonfat dry milk price stayed the same. Similar logic has justified the decreases in the butter price and increases in the nonfat dry milk price that have occurred at the \$10.10 support price. In the short run, such actions probably are good fiscal strategy. In the longer run, however, such strategy can boomerang as evidenced by the damage done to the nonfat dry milk market in the 1970s.

Product Price Tilts

A second and substantially different type of tilt can also occur in the dairy price support program. This second tilt is more of a product tilt and has less to do with the milkfat-SNF value relationship. As an example, in the summer of 1973, the support price was increased from \$5.29 to \$5.61. In establishing the new CCC purchase prices, the decision was made to

favor cheese relative to butter-powder. Therefore, for cheese an additional 25 cents was added to the milk support price to provide a level of \$5.86. That same 25 cents was subtracted from the \$5.61 support price to give a butter-powder support level of \$5.36—a 50-cent spread between the products. The CCC purchase price for cheese was computed from the \$5.86 base, and the purchase prices for butter and nonfat dry milk were computed from the \$5.36 base. The USDA acknowledged that it was engaging in a policy of encouraging cheese production through this process. The product tilt occurred only that one time in the dairy price support program, but it is one additional tool in the program that can have substantial market implications.

By-Product Values

A third type of tilt that can occur in CCC purchase prices concerns the manner in which by-products are recognized in the purchase price calculations. For example, the USDA currently is not permitted (by law) to recognize nonfat whey solids by-product values in the cheese price calculation. As a result, purchase prices for cheese are established at somewhat higher levels that would be the case if an adjustment for whey solids values was made, especially in periods when the whey solids market is very strong. Similarly, butter-powder purchase price calculations have never incorporated by-product adjustments for buttermilk or dried buttermilk,³ even though these by-products may have significant values.

Demand Effects of the Purchase Program

The dairy price support program adversely affects the demand for milk and dairy products only to the extent that producer milk prices are established at higher levels than they would be in the absence of a dairy price support program. Some interests would find this proposition arguable, suggesting that the relative stability that comes to milk prices because of the support program is a positive demand factor. The elasticity of demand with respect to price varies among the several dairy products. However, the price-quantity demand relationship is still inverse, and higher milk prices mean lower quantities demanded.

Numerous demand studies have indicated a more inelastic demand for fluid milk products as compared to manufactured dairy products. Typically, analyses have reported elasticities in the neighborhood of -0.2 for fluid milk products and -0.7 for manufactured dairy products. Therefore, the market impact of higher prices generated by the dairy price support program comes down harder on manufactured dairy products. However, in the case of both fluid and manufactured dairy products, the price elasticity coefficients are inelastic. If the demands were not inelastic, the economic

rationale for using a purchase program to support milk prices would not exist.

Because butter, cheese, and nonfat dry milk are the products used (purchased) to support the price of milk, the burden of price support falls most directly on them. The levels of CCC purchase prices over the years clearly have depressed the quantities demanded for butter and nonfat dry milk. However, commercial demand for cheese has continued to increase at a strong rate even though there have been extended periods when wholesale cheese prices simply sat at the cheese purchase price level. In other words, wholesale cheese prices would have been at lower levels except for the “floor” price that the support program provided, but this has not appeared to adversely impact the demand for cheese.

The butter market has been hurt by the CCC purchase program because butter has effectively been prevented from competing price-wise with margarine. Per capita consumption of margarine moved ahead of per capita butter consumption back in 1957, and in the early 1990s we stand at 11 pounds of margarine and four pounds of butter per capita. Price has not been the only factor, but it has been the key factor in bringing about this change. The substantial decreases in CCC purchase prices for butter in recent years promise to make butter more price competitive with margarine in the market.

The nonfat dry milk market has also been hurt because of “high” prices. As nonfat dry milk prices moved up by seven or eight times over their 1960 level into the 1990s, there was a visible retreat from the commercial demand for this product. Dairy processors stopped fortifying fluid milk products, bakeries stopped enriching flour with nonfat dry milk, ice cream manufacturers looked to whey solids as a substitute, household use of nonfat dry milk slowed down, and other use categories shrank, particularly where lower priced casein and vegetable protein could be substituted. Only the Commodity Credit Corporation remained to purchase what the commercial market did not want at high prices. The 1988-89 phenomenon of a tight world market for nonfat dry milk did not reflect a strong demand situation but instead reflected a short world supply situation.

The dairy support price, to the extent that it leads to higher milk prices than would be the case without the program, means higher raw milk costs and presumably higher wholesale and retail milk and dairy product prices than would otherwise be the case. The impact of higher milk prices is greater on those dairy products for which the farmers’ share of the retail dollar is higher. For example, for butter and nonfat dry milk, a high proportion of the consumer price derives from the raw milk cost. For products such as ice cream and yogurt, which have high flavor and sugar costs, expensive processing and packaging costs, and relatively

³ This is not the beverage buttermilk one finds in the dairy case. It is a by-product something like the “whey” from a butter churn.

high distributing costs, the raw milk cost is a lower proportion of the consumer price. Higher marketing margins mean lesser effects from changes in the producer milk price. Dairy products reflect the following declining order in farmers' share of the consumer dollar:

<u>Product</u>	<u>Farmers' Share</u> (percent)
Butter, nonfat dry milk	70
Fluid milk products	50
Cheese	40
Ice cream	30
Yogurt	25

The support price for milk and the CCC purchase prices used to achieve the support price can have substantial impacts on prices and therefore on the demand for all dairy products. But the price impacts are diluted for those products that have smaller proportions of their retail value accounted for by producer milk prices.

Milkfat and Skim Milk Values

Under traditional methods of cost accountability, the value or price of milk is the sum of the values of milkfat and skim milk. Therefore, if the value of milkfat declines, and the per cwt price of milk stays the same, then the value of skim milk accordingly must increase. These price adjustments occur automatically through the butterfat differential, and follow the same logic as tilts in butter and nonfat dry milk prices.

Butterfat differentials are computed each month as a function of the monthly wholesale grade A butter price at the Chicago Mercantile Exchange. In most markets, the butterfat differential is computed by multiplying the butter price by a factor of 0.138 and subtracting 0.28 percent of the M-W price at test. For example, with a wholesale butter price of \$0.86 and the M-W price at test of \$11.50, the butterfat differential is 8.7 cents.

Because milkfat and therefore butter has been in surplus supply, the wholesale price for butter at Chicago generally has been virtually the same as the CCC purchase price for butter. Any changes in the CCC purchase price for butter are followed by similar price changes in the wholesale butter market.

On May 13, 1992, the CCC purchase price for butter dropped by 11 cents per pound, from \$0.8725 to \$0.7675. As a result, assuming that the wholesale butter market drops similarly, butterfat differentials would drop by about 1.5 cents per point. One effect is on the supply side where prices to dairy farmers reflect the lower butterfat differentials. On the demand side, lower butterfat differentials mean lower milkfat costs but relatively higher skim milk or SNF costs. In terms of the different dairy products, costs and therefore prices for higher fat products are reduced relative to lower fat

products. Even within the class I or fluid milk category, the effect of such price changes is to lower costs or prices of whole milk relatively more than the costs or prices of lowfat milk and skim milk.

Impact of Dairy Price Support Program on Dairy Exports

Exports of dairy products from the United States historically have represented only a very small share of the commercial milk market. For the 1965 through 1991 period, at five-year intervals, exports on a milk equivalent basis are reported as follows:

<u>Year</u>	<u>Dairy Exports</u> (bil. lbs., milkfat equivalent)
1965	2.36
1970	0.99
1975	1.57
1980	0.99
1985	2.73
1990	3.33
1991	1.93

As the data indicate, annual U.S. dairy exports accounted for less than three billion pounds, or one to two percent of the market for milk in recent years. However, export quantities do not completely reflect the picture because milkfat equivalent data do not capture nonfat dry milk exports. Even so, although world supplies of nonfat dry milk were tight in the second half of 1989 and exports increased, the milk equivalent exports are a reasonable measure of the limited nature of U.S. dairy exports.

Three reasons generally are advanced in explanation of why dairy exports are so meager. A first point is that total world dairy trade is very limited. Only an estimated five percent of world milk production shows up in international trade. Even so, the U.S. share of that five percent is very small.

Second, the rules of the General Agreement on Tariffs and Trade (GATT) prohibit the subsidization of exports if such subsidized exports interfere with existing market shares of other exporting countries. While these rules may be challenged or tested on occasion, they have proved to be effective in limiting dairy exports from the United States. Because wholesale prices for dairy products in the United States are generally higher than established "world" trade prices it normally requires a subsidy on exported product to expand export outlets. As such, the United States finds great difficulty in developing larger export markets.

The third reason and the major factor that inhibits export of U.S. dairy products is price. Wholesale dairy product prices in the United States have generally exceeded international trade prices by substantial margins. Note the following comparisons that prevailed in April 1992:

	U.S. Wholesale Price (\$/lb.)	World Price, F.O.B. N. European Ports (\$/lb.)
Butter	0.87	.64
Cheddar cheese	1.30	.86
Nonfat dry milk	1.10	.71

Source: Dairy Market News, USDA-AMS, Volume 56, Report 40, October 2-6, 1989, pp. 7-8.

In April 1992, the U.S. butter price was 36 percent higher than the announced “world” price. Actually, through most of the past twenty years, the difference has been even larger. Similarly, the U.S. price for cheese was 51 percent higher than the “world” price, even though the difference was not as great as it generally has been. Nonfat dry milk prices were the exception in early 1989, with “world” prices at or above the wholesale price in the United States. However, the nonfat dry milk price situation has been an unusual phenomenon. In most periods through the past two decades, wholesale nonfat dry milk prices in the United States have been twice as high as the world price.

The basic reason that wholesale dairy product prices in the United States have been higher than world prices goes back to the dairy price support program. The levels of dairy price support have required CCC purchase prices for butter, cheese, and nonfat dry milk to be established at levels that

would achieve the price goal for milk. These product support prices, for the most part, have been substantially above world prices for these products, and these CCC products purchase prices have effectively become price floors in the wholesale markets. As a result, the purchase program used by the Commodity Credit Corporation to support producer milk prices has prevented the milk industry from engaging in price competition in world markets. In this way, the CCC purchase program has had major market implications with respect to export trade possibilities. It should also be noted that the price policies of other countries, especially the European Community, have resulted in a heavily subsidized, and therefore low-priced, world market.

Summary

In summary, the dairy price support program is a major institution in the marketplace. It is the key player in the milk fat-SNF value relationship. It affects producer milk price levels and therefore raw product cost level into processing plants and all the way through to retail prices. It holds U.S. dairy product prices higher than established “world” market prices. As changes in support prices are considered, or as ways of changing the procedures used to support the price of milk are considered, or as ways of changing the procedures used to support the price of milk are considered, the market implications of such changes must be recognized.