

Economic History of Dairy Markets or How Economic and Political Events Transpired to Result in a Complex Web of Dairy Policies

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Economic History of Dairy Markets

“Those who cannot remember the past are condemned to repeat it.”

George Santayana, 1905

“History is more or less bunk”

Henry Ford

“History’s most important lesson...is that man has not learned much at all from history.”

Aldous Huxley

“Yes, reading history will make you a better citizen and more appreciative of the law, and of freedom, and of how the economy works or doesn’t work, but it is also an immense pleasure....”

David McCullough



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The era of pre-market economy (before the late 1700s)

producer, processor, seller are one and the same

there is no “market” for much of the food production system and what market exists likely involves barter as well as simple cash transactions.

1558

↳ *Juan de Onate brings dairy cattle from Mexico to his fledgling colony in what will become New Mexico*

1611

↳ *Sir Thomas Dale brings 100 dairy cattle to Jamestown*

1600s

↳ *Major “import” of African slaves, more than white/European immigration*



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Era of small-scale competition

(late 1700s to about 1880)

Only federal intervention directly affecting dairy product markets is import tariffs

Federal government's role is extremely modest, limited to international and interstate issues, and starved for funding

1789

- George Washington is inaugurated

1790

- A 4¢/lb. tariff is levied on cheese imports, the U.S. is exporting butter and cheese

1800s

- Mechanical revolution (tractor, cotton gin, threshing machine, reaper, etc)
- Westward expansion of USA (manifest destiny)
- Population growth (immigration of whites but different parts of Europe)



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Era of small-scale competition

(late 1700s to about 1880)

farms move away from cities and into the hands of fewer people

emergence of the 'middle-man', i.e., marketing functions are not all carried out by the producer

advantages of specialization in production and marketing

1804

- Connecticut Dairy Farmers milk marketing cooperative

1838

- Milk moves from N New England to Boston by train

1841

- Milk is regularly shipped by rail from Orange County, NY to NYC, pricing is at a flat rate and milk moves 100 or miles or more packed in ice and sawdust

1851

- Jesse Williams opens the first U.S. commercial cheese factory in Rome, New York; plants opening in Wisconsin

1857

- Gail Borden establishes the first milk condensary in Connecticut
- Gustav De Laval invents the cream separator



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Era of small-scale competition

(late 1700s to about 1880)

milk price determined by negotiation; both sellers and buyers are small and numerous

major problem of the day is milk quality (bacteriological and physical contaminants)

seasonality a major marketing challenge affected prices; high price in winter, low price in spring

around time of Civil War, dealers begin to develop a bargaining edge on farmers, major advantage is better market information

1862 Homestead Act

- Permitted any citizen, or any person who intended to become a citizen, to receive 160 acres of public land, and then to purchase it at a nominal fee after living on the land for five years

1862 Morrill Act

- Donated Federal lands to the "several States and Territories" which may provide Colleges for the Benefit of "Agriculture and the Mechanic Arts"

The rise of "scientific agriculture"

Mid to Late 1800s

- Farmers deliver milk to plants on their own, begins system of "plant point pricing"

1884

- Harvey Thatcher invents the milk bottle in Potsdam, NY, created sator retail container and one that retains shape and standard volume

Late 1800s

- Irregular bulk milk containers standardized to tin-plated 40qt cans; leading to pricing by cwt.



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Era of price domination by dealers (circa 1880 to 1916)

largest dealers and/or milk dealer associations set prices if co-ops exist, they are largely ineffective or are 'captive' to a processor although co-ops existed throughout 1800s, toward end of this era farmers began following the lead of labor unions, farmers look to co-ops as only way to compete with buyers

- 1880-1901
 - Classified pricing and pooling introduced in Boston market
- 1882
 - The Milk Exchange, Ltd. is formed in New York.
- 1889
 - Milk production in the U.S. is about 45 billion pounds. New York has 13% of the total and is the leading state. Kansas and Indiana are in the top ten; Wisconsin and California are 1.
 - New York farmers form the Milk Producers Union to counter prices set by milk dealers.
 - The Milk Producers Union becomes the Five States Milk Company, which tries to buy, handle, and dispose of all members' milk.
- Early 1900s
 - New England cooperatives develop and introduce the "baise ratings plan", something like the CA Class 1 quota, designed to ration access to Class 1 value



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Era of price domination by dealers (circa 1880 to 1916)

many pricing innovations introduced, e.g., differentials based on freight, quality, and butterfat content; however, such changes of more interest to buyer than farmer

- 1890
 - S.M. Babcock invents his chemical test for fat content in milk
 - Primary motive is to eliminate opportunity to "water" milk, which is a health problem as well as a nutrient quality issue
- 1916
 - Wisconsin becomes leading milk producing state
- Early 1900s
 - Development of trucks creates new competition for train transport
 - Train system of flat transportation rates proves uncompetitive with truck rates based on distance
 - In NY a system evolves of hauling costs based on 10 mile zones



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Early US Economic Policies - Competition

Anti-Trust Policies

- Generally intended to prevent abusive business practices that would result in unfair competition, between buyers and sellers or among sellers or among buyers
- Trusts of at the turn of the 19th Century primarily sought to eliminate competition with buyers through coordinated industry-wide conduct that lowered production and raised prices
- The **Sherman Anti-Trust Act of 1890** (principles)
- The **Clayton Anti-Trust Act of 1914** (behaviors)
- The **Capper-Volstead Act of 1921** (exceptions)

- 1891
 - The NYS Attorney General accuses the Milk Exchange of price fixing.
 - The Milk Exchange dissolves and reforms itself in New Jersey as Consolidated Milk Exchange, Ltd.
- 1892
 - The Five States Milk Company is sold at a Sheriff's auction.
- 1907
 - The Dairymen's League is formed in New York.
- 1910
 - A 1¢/quart increase in retail prices of milk by all NYC dealers on one day in 1909 precipitates a major investigation by the NYS Attorney General. He finds that prices paid to producers were "unreasonable and unprofitable." No charges are filed; no state action is taken.
- 1910
 - An investigation chaired by NY Senator Charles Wick concludes that government can help dairymen by playing a more aggressive role in fostering and assisting cooperatives.
- 1916
 - Dealers reject price offers of the Dairymen's League, a bitter "strike" lasts for two weeks until dealers give in.



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Era of collective bargaining (1916 to 1933)

initially cooperative action and collective bargaining work well

co-ops try many new ideas to enhance revenue for farmers and stabilize markets, including classified pricing

major disagreements between cooperatives re bargaining and marketing strategy, e.g., how militant to be in bargaining, how deeply involved to be in marketing/plant ownership

- 1918
 - ↳ Classified pricing and pooling reintroduced to Boston market and remains active until 1932 and the prospect of federal intervention
- 1921
 - ↳ The Dairymen's League becomes the Dairymen's League Cooperative Association and becomes very active in buying failing country milk plants to protect farmers markets and increase their ability to handle members' milk directly. Membership falls as the cost of ownership grows.
 - ↳ Other NE farmers favor coops limited to the price bargaining role (Sheffield Farm, Eastern)
- 1927
 - ↳ A series of meetings between dairy farmer leaders in New York presses for greater unity among competing cooperatives and sees little role for government.



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First Formal Study of Milk Prices Reveals a Pattern of Regional Differences, High Prices Where Milk is Short Relative to Demand 1929 Harvard Study (prior to FMMOs):

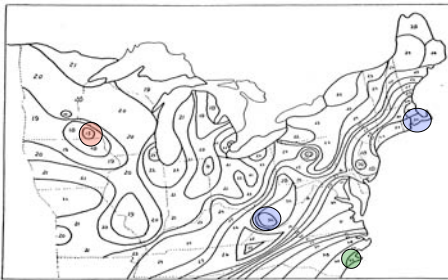


FIGURE 11
Farm Prices of Milk, 1929



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Early Policies Related to Agriculture

Agriculture was called on to increase production for World War I
After the war,

- ↳ the farm economy became depressed
- ↳ Cooperative bargaining became less effective as non-cooperative firms learned new ways to bargain with farmers and many coops overreached their grasp.
- ↳ **Packers and Stockyards Act of 1921** protects ranchers from "unscrupulous practices" of meat packers
- ↳ McNary-Haugen bills, vetoed twice by President Coolidge in mid to late 1920s, sought to stimulate exports by having a federal agency buy surplus products for export sale at reduced prices

The stage was set for government regulation but the form it took was problematic and things had to get a bit worse before we were ready to do it

The Great Depression made it "worse" enough



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Era of collective bargaining (1916 to 1933)

dealers re-group, as economic conditions improve, member defections become a serious problem

ability of co-ops to deal effectively erodes during 1920, Great Depression convinces most people that cooperative action can't do it alone

1929-1933

- ↳ A study chaired by New York Senator Perley Pitcher recommends that dairy cooperatives should be bolstered to provide a long-run solution to the persistent problem of low profits in dairy farming.
- ↳ Although government intervention in price setting was not even contemplated when the Study was initiated, it gains support as the nation plunges into the Great Depression.
- ↳ The final report contains a lengthy appendix on "Legal Aspects of Milk Control," including a section on treating milk as a public utility.



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Era of public regulation (1933 to ?)

learning from modest efforts of the 1920s to bolster cooperation and spurred by the Depression, government develops an attitude of 'don't just sit there' and 'let's try it'

Agricultural Adjustment Act of 1933 has primary goal to improve farm incomes by boosting farm prices

intent of act was to control over-production and thereby raise prices to parity levels; methods to do this were ruled unconstitutional

for dairy, co-op leaders pushed in the direction of the reforms that they had tried unilaterally without success

1933

- ↳ New York passes a Milk Control Law; President Roosevelt signs the Agricultural Adjustment Act. Dairy was included in each of the 3 key sections of the AAA:
 - ↳ Authorized adjustments of production through use of contracts with producers, benefit payments, and processing taxes:
 - ↳ Authorized marketing agreements with processors, handlers, and producers/cooperatives.
 - ↳ Authorized licensing as a means of eliminating unfair practices



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Era of public regulation (1933 to ?)

Establishing the Support Price Goal

AAA of 1933 tells Secretary to maintain the purchasing power of farmers relative to a base period -- thus the concept of parity is introduced

- ✓ Directs the Secretary of Agriculture to support the price of manufacturing grade milk through CCC purchases
- ✓ In setting the support price, the Secretary of Ag. is required to ensure an "adequate supply of milk."

Concept of 'parity' emerges in Ag Act of 1938. Prices "now" should be on par with price/cost relationships in 1910-14, the most recent period of "fair" prices. Parity pricing becomes the cornerstone of ag policy - intended to ensure "parity income".



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Era of public regulation (1933 to ?)

Purchasing Dairy Products to Support Farm Milk Price

Jan 9, 1930, federal Farm Board made a loan to LO'L to purchase surplus butter. LO'L purchased 5 million pounds during the Spring & sold it back in the Fall at a profit

Agricultural Adjustment Act of 1933:

- Secretary of Ag authorized LO'L to purchase surplus butter
- 11 million pounds donated to Federal food program
- butter price increases from 18 cents to 24 cents a pound

Dairy products purchased 1933 to 1941, but purchases are small -- geared to food relief and school feeding programs



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Era of public regulation (1933 to ?)

The Birth of the Dairy Price Support Program - a permanent approach to supporting prices

during WWII, Congress spurs food production, support price at 85% parity in 1941, 90% in 1942, market prices exceed supports in all but 2 years from 1941 to 1947

after war, farm production grows, Congress decides to get out of business of setting price each year

Agricultural Act of 1949

- ↳ Last farm bill enacted without an expiration date, i.e., permanent legislation
 - ✓ Moved to quadrennial bills until 1996, after which it has been lengthening in part by design and partly because we find it hard to finish
- ↳ becomes bedrock legislation for agriculture, concept of flexible parity is introduced, i.e., for milk, Secretary must choose in range between 75% and 90%
- ↳ Dairy Price Support Program becomes part of permanent law



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Era of public regulation (1933 to ?)

Early experience with DPSP

- "teaches" us
 - ↳ Be careful about sellback
 - ↳ We want to enhance prices, not stabilize them

Dairy import quotas - Strict quotas are implemented via Trade Agreements Extension Act of 1951 and Section 22 of AAA of 1933, recognized we could not risk supporting world prices

Quotas terminated by the Uruguay Round General Agreement on Tariffs and Trade

Tariffs: WTO allows for minimum market access and restrictive tariffs on amounts above that level.

1950

- ↳ Support program revenues exceed costs for the first and only time.

1952

Truman Graf joins UW faculty

1953-54

- ↳ USDA net removals hit a record 11.3 billion pounds (milk equivalent), net expenditures soar to \$474 million. Secretary drops support back to 75% of parity (a big cut) and markets adjust fairly quickly over the rest of the decade.

Andy Novakovic joins human population - demand curve shifts right

1956

- ↳ U.S. milk production is 125 billion lbs.
- ↳ Wisconsin is America's Dairyland and has 14% of the total. New York ranks 2nd with 8%; California is 4th, and Texas falls out of the top ten.



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Era of public regulation (1933 to ?)

The Gestation and Birth of Federal Orders

1934 amendment to AAA

- ↳ Strengthens authority of US to intervene, relying on broad interpretation of interstate commerce clause
- ↳ Authorizes classified pricing and marketwide or handler pooling
- ↳ Refers to Marketing Agreements

1935 amendment to AAA authorizes first marketing orders, by that name, replaces licenses

- ↳ Very detailed provisions which are allowable, to avoid the impact from Supreme Court decisions in the Schechter Poultry and Panama Refining and facilitating AAA regulation of milk markets.
- ↳ Greater regulatory and enforcement authority than agreements
- ↳ Handlers would be "ordered" to comply vs voluntarily "agree"

1936

- ↳ U.S. milk production tops 102 billion pounds.
- ↳ Wisconsin ranks 1st with 11% of the total.
- ↳ Minnesota and New York rank 2nd and 3rd with about 7% each.
- ↳ California is 5th; Texas is 10th.



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Era of public regulation (1933 to ?)

The Birth of Federal Milk Marketing Orders

3 June 1937 the Agricultural Marketing Agreement Act was passed to preserve existing marketing agreement and order language and add a few new details

- ↳ Permanent law
- ↳ Permissive, not mandatory
- ↳ Four regulatory options

Four forms of Regulation

1. Mediation or Arbitration
2. Marketing Agreements
3. Marketing Orders with Agreements
4. Marketing Orders without Agreements

1938

- ↳ First farm bulk tanks replace milk cans.

1940

- ↳ The American Dairy Association is formed.



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Key Points about Marketing Agreements

Marketing Agreements

- ✓ Voluntary, written, public terms of trade involving both producers and processors, joined by the Secretary of Agriculture
- ✓ Requires "due notice and hearing", like Orders
- ✓ Does not specifically require use of classified pricing and pooling, although eligible to use all the tools of Orders
- ✓ Implemented "if and when (signed by) such number of handlers as the Secretary shall deem sufficient"
- ✓ Not effective for "non-assenters"
- ✓ Signatories have immunity to antitrust law, within agreement



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What Does the AMAA 1937 Allow?

Marketing Orders

- ✓ Final Decision offers processors a Marketing Agreement. If they sign, a Marketing Order is approved with a companion Marketing Agreement. This occurs in fruit and vegetable orders but not milk. (doesn't mean much)
- ✓ If processors do not all sign an agreement, then the Final Order is written without a Marketing Agreement
- ✓ Thus, Agreements are the culmination of a negotiation process, Orders are "promulgated"



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So What Did We Actually Do or Use?

First Marketing Agreement was in Chicago in 1933

- ↳ 200 requested in 1933, 15 approved
- ↳ Chicago abolished in 1934 but then revised and re-implemented as an Order
- ↳ Topeka Agreement lasted until 1947

First Marketing Orders in 1936 - St. Louis

1. St Louis, Kansas City, Topeka, Dubuque, DC, Fall River MA
2. Boston, LaPorte IN in 1937
3. NYC, Cincinnati, Fort Wayne, Toledo in 1938
4. Chicago, Lowell-Lawrence MA, Omaha, New Orleans in 1939

By 1940 there were 20 Federal Marketing Orders

- ↳ Primarily Northeast and North Central US

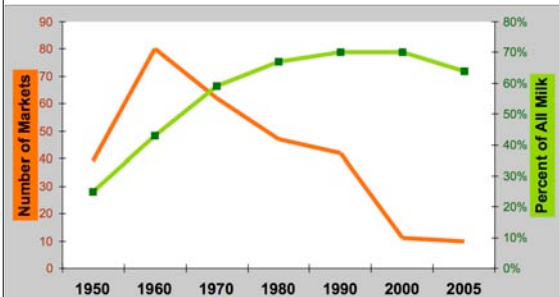
States get in the act too

- ✓ Wisconsin 1932 but over by 1940
- ✓ NY in 1933, still in effect
- ✓ Some 29 states get involved in dairy price regulation of some type
- ✓ By 21st Century, there are 8 left



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Marketing Orders Grow Over Time



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A Spatial Pricing Model

Following huge market surplus in 1953, and resulting collapse in prices, USDA initiated study of “regulatory impediments to increased consumption of milk”

- ↳ Objective was to help price by helping sales
- ↳ States believed to have regulations (sanitation, inspection) that hindered interstate sales and made system (goods) more costly
- ↳ Hence penalized consumers and reduced sales

USDA statistician Harry Trelogan and economist Louis Herrmann tasked to find out if state regulation effects were real and significant



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A Spatial Pricing Model

Trelogan and Herrmann documented Statutory programs but needed to answer the question “do these regulations result in distorted prices or markets”

To get at this, they decided to look at existing farm prices and see if these prices could be explained by predictable, normal economic forces. If not, then a case could be made that regulation is causing the distortion.

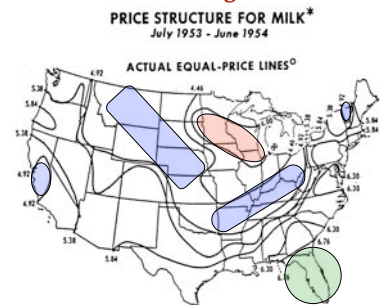


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Market Prices vs Regulated Prices

Using existing farm price data, T&H created price maps

They saw a pattern of progressively higher prices starting in the Upper Midwest and progressing East and South - not so clean a pattern to the West. (cf. Cassels 1929)



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Market Prices vs Regulated Prices

The Statistician and Economist sought to estimate a systematic geographic relationship in milk prices

If so, they could compare actual prices in an area with a "predicted" price. If the actual was higher, that might support the contention that States had effectively raised barriers to interstate trade.

They decided to focus on the eastern half of US, which looked to be more systematic and was also where most of the state regulation existed.

Using the nascent tools of OLS, they estimated:

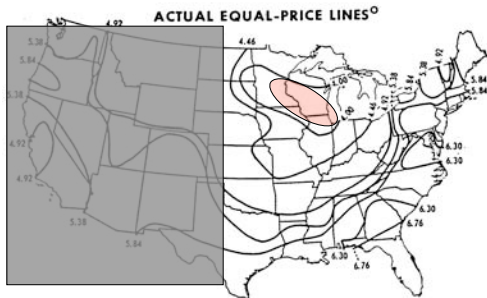
- ↳ The difference between Grade A and Grade B prices
 $PA_i = a + PB_i$
- ↳ The difference between Grade A prices in the base zone and other locations, as a function of distance
 $PA_j = PB + bD_{ij}$

So what is the Base Zone?



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PRICE STRUCTURE FOR MILK* July 1953 - June 1954



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The Seminal Class I price model - Where is the base?



WI was the logical choice for a base, but where exactly?

Rand McNally Household Good Carriers Road Atlases of the day provided distances between a relatively small sample of cities across the US

There were only two choices in WI for cities located in rural, large dairy areas - Eau Claire and Wausau

Flip a coin - E.C. wins



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What did they find?

The simple econometrics indicated there was a systematic relationship in market prices based on distance from Eau Claire

- Remember, most milk was unregulated at this point in time
- The interpretation was that this was a measure of market forces, not a measure of what regulation caused.

The economist compared

- the "intercept" to the cost of converting from Grade B to Grade A and
- the Distance parameter to hauling rates quoted by commercial carriers

And concluded that these were logical economic interpretations to the statistical results

Voilà! -

Eau Claire, single base point pricing was borne as the explanation of market price patterns and later become the *de facto* rationalization for Class I pricing decisions, and



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The Rise of Regional Cooperatives (1964 to 1998)

the birth of a new era or part of the phenomenon of public regulation? co-ops become more involved in negotiating (setting) prices (over-order premiums) and in processing and marketing milk

public regulation is still a mainstay public policy pathologists ask is the relationship between cooperatives and government symbiotic or parasitic? (cf. 1930s)

Also saw a rise in not just aggressive advocacy but also political involvement by large scale cooperatives (AMPI and Nixon)

1964

- Plastic milk containers are introduced.

1966

- U.S. milk production has fallen to 120 billion pounds.
- Wisconsin share is 15%. New York stays ahead of Minnesota. California is a distant 4th.

1971

- The United Dairy Industry Association is formed to bring together the American Dairy Association (promotion), the National Dairy Council (nutrition), and Dairy Research, Inc. (product development). The dairy industry starts talking about a "total marketing concept," i.e., farmer controlled marketing of milk from "gate to plate".



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The Rise of Regional Cooperatives (1964 to 1998)

1973 A blue ribbon USDA special study team reports to then Assistant Secretary Clayton Yeutter that it is time to seriously explore alternatives to pegging federal order class prices to the Minnesota-Wisconsin (M-W) price.

1973 Agr. Act of 1949 amended to raise minimum support price from 75% to 80%

1976 The last federal milk marketing order switches to the M-W as the basic price mover for all class prices.

1976 Newly elected President Carter delivers on campaign promise of \$9 milk



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The Rise of Cooperatives - The Fall of the Dairy Price Support Program

1977 and 1979 Congress twice passes special legislation to ensure support price equals 80% of parity, adjusted semi-annually (\$9 was 80% of parity when Candidate Carter proposed it)

1980 13.1 B lbs (m.e.) establishes new record for annual support purchases. Cost hits \$2 B. Rises further through 1983.

1981

April: the day after he was shot, President Reagan signs legislation from his hospital bed that revokes the last semi-annual adjustment.

Agricultural Act of 1981 eliminates parity as the standard by which the support price is calculated. Instead, current price is tied to adjustments based on level of CCC purchases and net government costs -- a trigger mechanism (cf. FCEA of 2008)

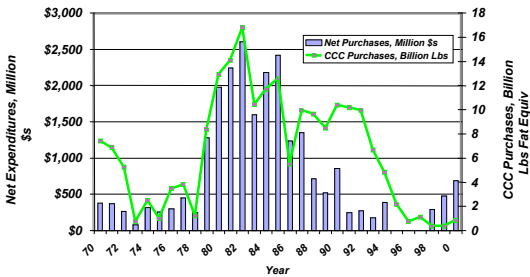
1982 Producers are assessed 50¢/cwt. on all milk marketed as a means to reduce price support program costs, resulting from language in Omnibus Budget Reconciliation Act, not a farm or dairy bill.

1983 Sales of dairy products under the price support program peaks at 16.8 billion pounds milk equivalent, 12% of all milk marketed.



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Net Government Expenditures and CCC Purchases Under Support Program, 1970-2000



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The Rise of Cooperatives - The Fall of the Dairy Price Support Program

1983/1984 The Dairy Production Stabilization Act mounts a three pronged attack on the surplus.

- The support price is reduced for the first time since 1962. (The cut in 1962 was 20¢ smaller but over twice as large in percentage.)
- Assessments are continued
- the Milk Diversion Program starts. Farmers can sign up for payments to reduce marketings 5-30%
- The National Dairy Promotion and Research Board is formed. Farmers tax themselves 15 ¢/cwt.
- Milk production is temporarily but sharply reduced. Milk prices rise sharply, but also very temporarily.



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The Rise of Cooperatives - The Fall of the Dairy Price Support Program

1986 Dairy is revised yet again in the 1985 Food Security Act (farm bill).

- ↳ Support price is scheduled for small but persistent cuts from 11.60 to 11.10 from 1986 to 1987
- ✓ “Formalized” a trigger mechanism for changing support level in 1988, 1989, and 1990
 - * Prior to Jan 1, Secretary of Ag projects CCC purchases
 - * If exceeded 5 billion pounds, reduce support \$0.50
 - * If less than 2.5 billion pounds, increase support \$0.50
- ↳ Further assessments
- ↳ The Dairy Termination Program begins. Farmers place bids for payments to go out of business, selling cows for slaughter or export. Legitimizes farm sales. 12 B lbs bought out (less when taking into account prior reductions). Pits dairy farmers against cattle ranchers. Tightens markets in short term and for a while after program implementation. Prices strengthen for a while.
- ↳ Compensating changes in class I differentials to offset regionally biased reductions in marketings. (The Chicago meeting.)
- ↳ Dairy Export Incentive Program



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The Fall of the Dairy Price Support Program

Despite MDP, DTP and all the rest, in the end a 22% cut in the support price was needed to get markets back in balance. This marks the point in time at which the support price became almost meaningless as a factor in setting milk prices and led to farm milk price instability not seen since 1920s

New York Coffee, Sugar and Cocoa Exchange develop futures markets for dairy products. (Hershey buys cocoa and NDM.) Chicago Mercantile Exchange develops new products, and becomes the dominant venue for current and future price discovery.

1988

- ✓ U.S. milk production hits 145.5 billion pounds.
- ✓ Wisconsin leads all states with over 17% of the total. California represents just under 13% of the total. New York has less than 8%.
- ✓ The top five states account for over 52%, and the top ten states account for two-thirds.
- ✓ Texas passes Ohio for 7th place and contends with Michigan for 6th place.

Dec 1989

- ✓ The M-W peaks at \$14.93 (3.5¢ lb) in, \$4.60 over the support price

1 Jan 1990 - 1990 Farm Bill

- ✓ Support price drops to \$10.10 on, \$3 per cwt less than it had been ten years earlier.



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The Fall of the Dairy Price Support Program

Fluid Milk Promotion Act of 1990 (implemented 1993)

Processors decide to “do it right” and start collecting their own money to promote fluid milk. A few years later “Got Milk” becomes a joint campaign

1996 The Federal Agriculture Improvement Act

- ↳ Ends producer assessments
- ↳ Initially raises support price to \$10.35 and then phases down to \$9.90 for 1999
- ↳ 2000 CCC purchase program terminated and replaced by recourse loan program..... or at least that was the plan

1993 CA takes over from WI as nation’s leading milk producing state. Rest of top five (NY, PA, MN) retain their positions, but next five are jockeying for new positions.

1998 Mega merger of Mid-Am and other coops results in Dairy Farmers of America

- ↳ Still quite a few dairy coops, but regional debates become internal debates for DFA
- ↳ The market power of the large coop may be at its zenith, but the political power is largely spent in 1980s.



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Federal Order Policy Begins to Unravel

1995 USDA conducts hearings to head off Gunderson's attempt to legislate reform.

- ✓ "system-wide hearings are the most sweeping and comprehensive since the early 1960s"
- ✓ Orders move to front burner as DPSP fades as a venue for regional solutions
- ✓ Order consolidation is more prevalent than order expansion
- ✓ Numerous questions are raised about basic federal order pricing concepts
- ✓ Response from USDA is prolonged and fails to appease reformers



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Federal Order Policy Begins to Unravel

1996 Federal Agriculture Improvement and Reform Act requires federal order "reforms". Must reduce number of orders from over 30 to 10-14 and strong hints of encouragement to change class 1 differentials, broaden use of multiple component pricing, bring CA into the federal system, and simplify provisions

1999 Following much political maneuvering, final changes to Federal orders are finally authorized October 1999 with implementation on 1 January 2000

Federal order reform has numerous consequences but in the end is fairly uneventful in impacting regions.

- the switch to product formula pricing and use of "the higher of" manufacturing class prices results in increased instability in producer prices and class 1 prices, furthering calls for using futures markets to manage price volatility.



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Federal Order Policy Begins to Unravel

The Northeast Dairy Compact is implemented by six New England states and ratified by Congress as a temporary measure under the 1996 Farm Bill to appease Senator Leahy of VT.

- Scheduled to expire after federal orders are "reformed"
- The Compact becomes a rallying cry in the Northeast and Southeast but is bitterly opposed by the Upper Midwest and processors nationally. While in effect, it successfully adds premiums to Class 1 milk prices when federal order prices fall below an historically high benchmark price.
- Numerous Southern states pass necessary state legislation, but to no avail
- Compact supporters continue to lobby for restoration, but no hope in sights



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Dairy Trade Protection Begins to Unravel

Passage of WTO under Uruguay Round of GATT (1984-94) begins to seriously open US markets to new imports. Opportunities exist for exports, but these remain limited by continuing, albeit reduced, EU subsidies for dairy exports. Trade issues become increasingly troublesome for dairy, but with little sympathy outside the industry.

Doha Round (starting in 2001) hopes for more of the same, but becomes seriously stuck under protests by displaced laborers, environmentalists, and developing countries that want greater ag trade liberalization by US and EU and also less "trade distorting" domestic programs



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Agricultural Policy Begins to Unravel

"freedom to farm" concept in 1996 Federal Agriculture Improvement and Reform Act gives direct, decoupled payments to dairy farmers

Payments occur in several "emergency" and non-emergency forms.

Billions of dollars spent to make up for low prices, but this only causes low market prices to persist.

Payment limitations make low prices a better deal for smaller farmers and higher market prices a better deal for larger farmers



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Agricultural Policy Gets a Second Wind

The Farm Security Act of 2002 includes temporary continuation of DPSP, encourages use of futures markets, and creates Milk Income Loss Contracts (MILC) that provide cash payments to dairy farmers.

- ✓ MILC blends CCP payment for "program crops" and NE Dairy Compact style pricing

2002

- ↪ National milk production approaches 170 B lbs
- ↪ CA milk production continues to expand while WI holds still. #1 state now exceeds #2 by over 50%.
- ↪ NY and PA hold firm to #3 and #4, while MN slides to #5.
- ↪ ID jumps up the ranks to #6 and is in spitting distance of MN. NM solidly moves to #7 while MI and WA slide slightly to #8 and #9. TX stays in top 10 but has slipped from #6 over the last 10 years.
- ↪ The biggest dairy states east of Mississippi tend to hold their own, while western states surge, moving some previously obscure states (e.g., NM and AZ) from no where to notoriety.



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The Era of Public Policy and Intervention dodges a few bullets and the Beat Goes On

In preparation for 2007 Farm Bill there are three big questions

- ✓ What do farmers want?
- ✓ What will WTO tell us is feasible or allowable?
- ✓ What can we afford?

In finalizing the 2008 Food, Conservation and Energy Act, the only question that seemed to really matter was What Do Farmers Want, with a slight tip of the hat to What Can We Afford

Federal Orders deal with:

- Termination of Western Order in 2004
- Producer-Dealer issue in AZ and Pacific NW, stay tuned for the Sequel
- High energy costs led to re-examination of Class I differentials and make-allowances, along with NDM price reporting scandal this adds to undermining of confidence in Product Price Formula pricing
- Market changes in months, Orders change in years, a bad mix

All in favor of changing Federal Orders say "Aye"

What changes did you have in mind?????