IMPLICATIONS OF THE DAIRY OUTLOOK TO THE DAIRY INDUSTRY

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The dairy industry is headed into a new year, and a new decade with big money at stake. Last year cash receipts to farmers for milk were about $15 billion, with industry sales to consumers approaching $30 billion. The dairy industry is therefore important not only to its members, but also to the nation's entire economy. Where then is the dairy industry headed, and what are likely developments and changes confronting it?

In my presentation I will deal with the following "outlook" issues as they impact on dairy farmers and the dairy industry.

1. Five year changes confronting dairy farmers.
2. Important upcoming issues confronting dairy farmers, including:
   a. Impact of imports on domestic cheese, imitation cheese and nonfat dry milk powder.
   b. Future of price support program and threats to it.
   c. Future of Federal Milk Orders and threats to them.
   d. Minnesota-Wisconsin price series - where is it going?
   e. Dairy cooperatives - importance to dairy farmers and threats cooperatives face.

Five Year Changes

"Traumatic change" best characterizes the dairy industry of the future. The next five years will likely see the following changes in U.S. dairying. First, let's look at approximate increases -- which will generally be a plus for the dairy industry.
1. A one-eighth increase in production per cow -- to approximately 12,950 pounds of milk annually.

2. A fifty percent increase in the number of cows per farm to an average of about 40. Future herd size in states such as Wisconsin, where farmers raise much of their feed and roughage, will eventually increase to about 50 head, which is the maximum for a family operation. Over this level, additional help must be hired, thereby increasing unit costs. At present, Wisconsin's average herd size is 37.

3. A five percent increase in milk production, to approximately 130 billion pounds annually -- as production per cow increases faster than cow numbers decrease, farmers must "sell" increased production -- or prices are jeopardized.

4. A marked increase in concentration of milk production, with major dairy states such as Wisconsin and California, which together produce over 27% of the nation's milk, and a few others substantially increasing production, while others gradually move away from dairying into other agricultural enterprises. This will result in greater centralization and geographic concentration.

Four of the five leading dairy states -- Wisconsin, California, New York and Pennsylvania, are substantially increasing production and their dominance in nationwide milk production. Minnesota is slipping a bit, but still produces over 7% of the nation's milk. Others coming up fast are Texas, Washington, Vermont, Florida, North Carolina and Georgia. Your states of Idaho and Oregon are also increasing milk production. Idaho is up 15%, and Oregon 11%, since 1968.

In all, 14 states are becoming more prominent in dairying. These are the ones the industry will find it most profitable to concentrate on.

5. A one-fourth increase in the volume of milk handled per plant, with a substantial increase in the number of plants handling over one million pounds of milk daily, a trend emulating developments in your cooperative. This increased processing concentration will also contribute to increased concentration of milk production.
6. Conversion to about 90% Grade A farm milk -- from 83% currently, and 70% a decade ago, because of substantial price differentials between Grade A and Grade B -- averaging about $1.50 per cwt. increased herd size, increased plant size, and narrowing of differences in sanitary standards between the two grades. The shift to predominantly Grade A carries with it the need for Wisconsin to increase fluid sales, or share in fluid utilization in other markets, or Grade A farm blend prices will fall. If they fall in Wisconsin, the ripple effects will be felt all the way out to California. We currently have only about 30% Class I utilization, so can't afford any more erosion in fluid utilization.

7. Complete conversion from can to bulk tank procurement of farm milk, encouraged by increased production per farm, and the shift to Grade A milk.

8. A one-fifth increase in the volume of milk regulated under Federal milk orders -- to approximately 90% of all Grade A milk. Present criticism of milk orders will subside, and they will expand, not contract coverage. Your situation here is an example of that trend. Also, there will be more inter-regional orders, with mergers reducing the present 47 by more than one half.

This increased scope of Federal Milk Order price regulation will tend to stabilize conditions in the dairy industry, and therefore provide more stable markets.

9. A one-half increase in the price support level for farm milk to about $17 per hundredweight, reflecting increased parity prices and constant percentage support levels. Farm milk prices will rise proportionately. Government involvement in maintaining income to dairy farmers will continue and expand, thus buoying up farm milk prices.

10. A favorable milk feed price ratio reflecting heavy grain production, in turn encouraging heavier farm feeding.

Now let's look at approximate "decreases" for the next five years. These will have a mixed impact on the dairy industry, and therefore represent both plus and minus factors.
1. A one-fifth decrease in the number of dairy plants.
2. A one-third decrease in the number of dairy farms.
3. A seven percent decrease in the number of milk cows.
4. A decrease in per capita consumption of milk equivalent, reflecting further decreases in consumption of milk fat, and increased use of imitation dairy products, particularly imitation cheese.

The first and second factors could help the industry because of increased concentration of production associated with them. The decrease in cow numbers will be offset by increased milk production per cow -- and therefore feeding rates on the remaining higher productivity cows. Therefore, it will be only a modestly adverse factor for the industry. However, the decrease in per capita consumption of milk equivalent will be a negative factor for farm milk prices and also for dairy processors, and poses a challenge to the dairy industry to expand its dairy promotion and merchandising programs.

**Important Upcoming Issues Confronting Dairy Farmers**

A. **Imports.** Impact on domestic cheese, imitation cheese, and nonfat dry milk powder. The recent government trade bill permitting increasing cheese imports of 14% will make it more difficult to balance dairy supplies with sales, and will cost U.S. dairy farmers $76 million annually. (+350 million pounds milk equivalent at 9¢ per cwt. for 500 million # imports.) This amounts to 6 1/4¢ per cwt., or about $400 annually for average Wisconsin producers, in addition to 35¢ per cwt. -- $2,240 annually -- because last year imports exceeded exports by about 2 billion pounds of milk equivalent. Working to maintain import protection will be in the best interests of all dairymen.

**Casein.** Average annual casein imports in the last three years (1977-1979) are up 41% over the 1960-69 levels, and will be above 150 million pounds in 1979. Much of the increase in casein imports was used in food products, thus causing the dairy industry much concern.
The approximately 150 million pounds of casein imported this year equates to about 450 million pounds of domestic nonfat dry milk.

Nonfat dry milk or nonfat solids would likely be interchangeable with at least one-half of the imported casein used for food and feed products if prices were comparable. This equates to potential displacement of about 200 million pounds of nonfat dry milk in 1979, and therefore cuts into your nonfat dry milk markets.

Approximately one-fourth of U.S. farm milk is used in cheese. The problem of imported casein interfering with the domestic agricultural program for cheese is of particular concern because of the rapid increase in production of imitation cheese -- a major user of imported casein. Current U.S. production of imitation cheese is generally estimated to be in the range of 3-9 percent of U.S. production of natural cheese, which in 1978 totaled 3.52 billion pounds. On this basis, imitation cheese production is in the approximate range of 100 to 300 million pounds annually. Further rapid increases in production of imitation cheese are anticipated because of price savings, in turn attributable in part to use of lower priced imported casein priced at only about one-third the price of domestic dairy components. Testimony by casein advocates at the recent ITC & House of Representatives Hearings indicated a 25% to 50% price savings for imitation cheese, compared to natural cheese. One specific wholesale price comparison was $.79 per pound for imitation cheese, compared to $1.52 per pound for natural cheese -- a 48% price savings. Labeling of imitation cheese is also very critical to dairy farmers. At present Federal/state regulations do not always insure accurate branding of imitation cheese, and a law suit on this issue has been filed by National Milk Producers Federation.

Casein in imitation cheese is therefore displacing nonfat solids in domestic natural cheese, and imitation cheese made in part with imported casein is displacing natural cheese and therefore cutting into your cheese markets, which is especially critical to you, since you are involved in a major expansion in cheese production.
Imported casein is therefore hurting the dairy industry and particularly the cheese industry. Dairymen are very concerned about this, and are pressing for import quotas on casein -- an action which would also be in your interests to cooperate in.

B. Dairy Price Support Program: A continued increased in the price support level for farm milk will be needed because of increased farm costs. For example, the support price will need to be increased at least another 75¢ to 80¢ per cwt. to about $12.00 per cwt. (3.5% B.F.) by April 1 of this year to cover increased costs. Dairy farmers need continuation of the 80% parity minimum support, beyond the current cut off date of September 30, 1981, and without the "trigger" mechanism, reducing supports to 75% parity when USDA purchases exceed 3 1/2 billion # milk equivalent, which the administration has been pushing. Justification for a continuation of a minimum 80% of parity support level include:

(a) Prices paid by farmers for production items are increasing as fast as farm milk prices.

(b) Farm milk prices as a percent of parity are lower than many other farm commodities for which computations are made.

(c) The dairy farmers' share of the consumers' dairy dollar is very low -- only 51%.

(d) In 26 of the past 30 years, farm milk prices were above price support levels. Thus, maintaining minimum price supports for milk at 80% of parity is an insurance policy which protects both farmers and consumers against wide swings in prices and supplies with no or only modest increases in milk prices to consumers.

(e) 80% of parity provides dairy farmers with only 80% of the purchasing power that farm milk generated 65 to 70 years ago (1910-14), hardly an unreasonable goal for current day dairy farmers. Even the upper limit of support provided for in current law (90% of parity) provides only 90% of the purchasing power farm milk had in 1910-14.
Current dairy support levels are modest, not exhorbitant. For example, annual income (return to labor and management) per Wisconsin dairy farmer with 50 dairy cows, keeping electronic farm records, averaged $13,820 during 1976-78, compared to average annual earnings of $13,085 for Wisconsin manufacturing workers and $15,575 for U.S. construction workers during the same period. Dairy farmers with $300,000 investment are generally netting less than urban workers with a zero dollar investment in their jobs -- an indication that price enhancement for dairy farmers must continue.

Thus, maintenance of a minimum price support level for milk at 80% of parity is clearly justified in terms of maintaining farm incomes at a level necessary to meet production costs, production of an adequate supply of milk, and as insurance against wide and unpredictable price and supply variations, thereby benefiting both farmers and consumers.

C. Federal Milk Orders. Federal milk orders have reached a crossroad after almost a half century of operation. Until recently, Federal milk order controversy largely remained "within the family" -- involving farmers, dairy plants, the USDA, etc. However, since Watergate anti-milk order sentiment has surfaced throughout society. Critics of Federal milk orders include House and Senate members, Federal Trade Commission, U.S. Justice Department, Council on Wage and Price Stability, Council of Economic Advisors, Community Nutrition Institute, and other consumer groups, trade groups, and most recently and perhaps most deadly, the Presidentially appointed "National Commission for Review of Antitrust Laws and Procedures."

Criticisms. (a) U.S. Senator Edward Kennedy: "There is something wrong with a system that first sets regulated prices artificially high, and then allows monopolistic cooperatives to extract premiums over and above those prices. This conference is a starting point for a Congressional inquiry."

(b) Jonathon Rose, Assistant Attorney General for Anti Trust: "Federal milk order regulation has perversely contributed to declining milk consumption by creating a price beyond the financial means of those who need it most."
(c) William Lilly, Council on Wage and Price Stability: "Milk pricing is an area too important to be left to the people who have been working on it."

(d) John E. Kwoka, Jr., Economist, Federal Trade Commission: "At least in its current form, Federal regulation of milk markets is one idea whose time has passed."

In addition to CNI conference criticisms, the U.S. Justice Department Task Group on Antitrust Immunities criticized Federal milk orders for (a) creating an overproduction of Grade A milk by setting prices too high, and (b) reducing the consumption of fluid milk and other dairy products by raising the price of Grade A milk for fluid purposes, and in conjunction with the price support program, elevating the general price level for dairy products to consumers. There is also the current reconstitution issue -- proposing SNF used for reconstituting milk be put into Class III rather than Class I. This can weaken the classified pricing system and hurt your farm milk prices and you should oppose it.

Evaluation. The major criticism of Federal milk orders appears to be that they have unduly enhanced farm milk prices to the detriment of consumers and society generally. I do not see evidence to support this charge. On the contrary, even with Federal milk orders, dairy farmers are still struggling to achieve equitable prices in light of their costs.

Federal milk orders have stabilized market conditions, and assisted farmers in bargaining for reasonable prices relative to their costs -- the legislative objective of orders. However, they have not set artificially high farm milk prices. Evidence is presented below.

(a) The primary source for U.S. Justice Department and many other attacks on milk orders charging that they result in significant social costs, concludes that social losses of Federal and state milk regulation are "roughly" 9 million dollars annually. These losses are less than .1 percent of farm milk sales, and are trivial compared to estimates of a monopoly cost in food manufacturing industries of approximately $12 billion annually (7 percent of sales).
(b) Farm costs have been rising about 5 percentage points faster than Federal order blend prices to farmers.

(c) The consumer prices for dairy products were 108% higher in 1979 than in 1967, compared to a 120 percent increase in all prices to consumers, and an 133 percent increase in the price of food. Price increases for dairy products were less than other products.

(d) Milk prices have been declining rather than increasing relative to wage levels. The "real" price of milk in terms of wage rates dropped 25 cents per half gallon, or 12 1/2¢ per quart between 1967 and 1978. Wages are going up faster than milk prices, further negating the "undue price enhancement" issue.

D. M-W Series. The Wisconsin Grade B milk price has averaged $.18 per cwt. above the M-W price during the past twelve months. Obviously the M-W price is understating prices actually paid for manufacturing milk in Wisconsin -- your major manufactured product competitor, and yet it is being used to price your milk here in Idaho, and Oregon -- and throughout the U.S.

What can be done about the distortions and inaccuracies in the M-W series? In my view, this primary mechanism for pricing milk in this country is on the verge of becoming obsolete, especially since every one cent per cwt. change in M-W price results in $12.2 million change in milk income to U.S. dairy farmers.

Manufacturing grade milk fell from 31 percent of all U.S. milk marketings in 1966 to 16 percent in 1979. For Minnesota and Wisconsin, the percentage of Grade B milk fell from 63 percent to 35 percent during the same period, further encouraging transition away from M-W pricing.

The imminent erosion of this competitive price system, as a result of dwindling Grade B milk production, will require the development of a new pricing mechanism for manufactured dairy products in federal order markets.

Major alternatives to the M-W price are: (a) new competitive price series or (b) product price formulas. These two appear to be the most promising. Two others -- (c) direct pricing by public hearings, and (d) economic indicator formulas, are unwieldy and less responsive to market conditions.
These are some alternatives to the M-W series you should be giving serious consideration to. There may be others, but the important fact is that the M-W series needs revising or change, and it will be to your advantage to work in that direction.

E. Dairy Cooperatives. Hopefully dairy cooperatives will survive the barrage of charges, litigation, and investigations stemming from the Watergate crisis, and maintain if not increase the volume of milk handled by them.

Realistically, however, the future of agricultural bargaining is in doubt, and Wisconsin dairy farmers are very concerned about this trend -- as you should also be. For more than a half century, the U.S. Government encouraged farmer cooperatives to bargain for their members. However, in recent years, strong government anti-bargaining and anti-cooperative developments have occurred. The U.S. Department of Justice is moving on several fronts to weaken cooperative bargaining, particularly dairy cooperative bargaining. Anti-cooperative legislation has been introduced in the U.S. Congress; the Council of Economic Advisors and the Office of Management and Budget are asking for a reevaluation of the Capper-Volstead Act.

But the most serious threat to cooperative bargaining is contained in the Recommendations of a presidentially appointed 22-member National Commission formed to examine anti-trust immunities. Commission recommendations made early last year propose new legislation that would weaken agricultural bargaining.

The Commission also recommends amendment of the Capper-Volstead Act to curb what critics call co-ops' "undue price enhancement" of milk.

The basis of the recommendation is a U.S. Department of Justice contention that dairy co-ops have a "monopolistic control of milk supply." That control is supposed to result in "social losses" of $60 million each year. The contention is disputed by economists, but even if true, the amount is only about one-half of one percent of farm milk sales. This amount is trivial, compared to an estimate of
monopoly costs in the food manufacturing industry of $12 billion annually or about 7 percent of sales.

Agricultural leaders also question the commission’s singling out of farmer cooperatives for their effect of “lessening of competition.” They point out that farmer cooperatives (a) are smaller than other segments of the farm marketing system, marketing less than 30 percent of the farm products compared to over 70 percent for noncooperative businesses. (b) The five largest cooperatives had 1977 sales of only $8 billion compared to $25 billion by the five largest noncooperative food companies.

(c) Only eight of Fortune Magazine’s list of the 500 largest industrial corporations are cooperatives. (d) The 10 largest farmer cooperatives had 1977 sales of about $10.7 billion -- less than one-fourth the sales of the single largest investor-owned company of about $45 billion. And finally, these farm leaders note that (e) many nonfarm groups have also organized cooperatives, including small retail stores in pooling of their purchases, newspapers through Associated Press, and gigantic brokerage houses in their business operations.

Based on research we recently conducted, Wisconsin dairy cooperatives are incurring average net costs of approximately 6.5¢ per cwt. in performing market services that benefit the entire market and hence consumers, but which cooperatives alone paid for. The cooperatives also incurred average net costs of .21¢ per cwt. in performing services that helped achieve more orderly marketing at the national level, and 2.41¢ per cwt. in increasing the efficiency of farm-to-plant milk hauling that benefited the overall market and consumer. Cooperative transportation of milk and a variety of other services benefit the entire market for milk -- including cooperative members, nonmembers, and consumers. But the costs of these services are paid for solely by the cooperatives. More equitable cost sharing to cover coop costs are needed.

Cooperatives have been good not bad for farmers -- and society overall. Where does the individual farmer get represented in the world? The cooperative does
this job for farmers. Your cooperative is important to you -- and your milk check. It will be worth your while to support and fight for your cooperative. It is your major economic friend and benefactor.