

Product Formulas and Competitive Pay Prices as Class I Price Mover: Historical Perspective

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Key Topics

- Perspective
- Studies considered
- Criteria for evaluation
- Options and consequences
- Concluding thoughts

Perspective

- Importance of fundamental economic change
- Importance of understanding the problem
- Importance of objective analysis
- Importance of understanding economic relationships
 - Key economic variables
 - Causal relationships (directional effects)

Conditions Leading to Studies Considered

- Nourse Report 1962
 - Evolution of national market
- Milk Pricing Committee Report 1970-72
 - Disappearance of M-W Grade B price series
 - Evolution of Basic Formula Price (BFP)
- University Study Committee 1996-97
 - Evaluation of longer term options
 - Cheese price manipulation charge

Common Study Conditions

- Major changes in economic conditions
- Unhappiness with how the Federal Order system was performing
- Lack of internal Dairy Division response

Criteria to Consider

- Reflect supply-demand conditions
 - Stocks the key variable
- Reflect changes in manufactured product prices
- Price stability
- Transparency/simplicity

Options considered

- Competitive pay prices
- Butter-powder-cheese formula
- Butter-powder formula
- Component pricing

Broad-Based Competitive Grade A Pay Price Findings/Issues

- Moderate in reflecting National supply-demand conditions
- Poor at reflecting product prices
- Relatively stable
- Choice of product used for updating important
- Does not require a make allowance

Butter/Powder/Cheese Formula

- Lagged in reflecting National supply-demand conditions
- Moderate in reflecting product prices
- Superior stability
- Suggested make allowance based on model plants in West, Midwest, and East

Butter/Powder Formula

- Poorest in reflecting National supply-demand conditions
- Superior in reflecting product prices
- Poorest in price stability

Component Price Formulas

- Superior in reflecting National supply-demand conditions
- Superior in reflecting product prices
- Stability depends upon industry conditions
- Overall the most superior in terms of economic performance
- Is industry ready?

Concluding Thoughts

- Market conditions have changed in four major ways:
 - International markets more important
 - Increased energy prices
 - Improved futures market performance
 - Components recognized as being more important