

New Challenges, New Ideas: An Overview of Dairy Issues and Policies Leading to the 2012 Farm Bill

Andrew Novakovic
The E.V. Baker Professor of Agricultural Economics
Charles H. Dyson School of Applied Economics and Management, Cornell University
316 Warren Hall, Ithaca, NY 14853
a.novakovic@cornell.edu

An Outline

1. The status of dairy markets and need (or desire) for new solutions
2. Contrast with the status of other major US agricultural sectors
3. What is the direction of US agricultural policy?
4. What is presently authorized?
5. What are the new ideas?
6. What is the likely timetable?
7. “Big Picture” issues that will affect dairy and the farm bill?

Introduction

Dairy markets have exhibited increased volatility since the withdrawal of significant federal prices supports during the late 1980s. However, the events of 2009 and continuing uncertainty about economic recovery for dairy farmers have created an increased sense of urgency for new dairy policy. The dairy, agricultural, and general economic climate is increasingly tumultuous and difficult to predict. National politics and the ability of the US government to develop legislative responses are bedeviled by a general agreement that many things need to be changed and changed dramatically but by a large disagreement on what those changes ought to be.

While volatility in milk prices have been a great catalyst for recent industry efforts to dramatically change federal dairy policy, there are a number of issues that are of large and perhaps growing importance to dairy farmers.

Issue #1: Volatility in Dairy Farm Income

The challenge of volatility in farm milk prices has been immensely compounded by volatility in the prices of farm inputs, especially feed. This has drawn our attention to thinking about the economic problem as one of volatility in dairy farm income, more so than the price of milk.

We might ask ourselves, what is the nature or characteristics of farm income volatility. Is it:

1. Cyclical or random?
2. Unpredictable?
3. Increasing?

Is it caused by:

1. Volatile milk prices?
2. Volatile feed prices?
3. Volatility in other input costs?
4. Production risk?

Familiar graphs of milk prices amply convey a sense of volatility. Monthly patterns show very large swings in price compared to the last half of the 20th Century. However, if one looks at the national average milk price from the first half of the last century, it is clear that volatility, or at least large variations in monthly prices is not really new to the US dairy sector. Indeed the relative swings in milk prices in the first 25 years of the 20th Century easily rival recent patterns. What emerges from an investigation of these data is evidence that the Dairy Price Support Program, operated in the 1940s and made permanent in 1949, had a considerable effect on dampening milk price volatility that seems to be inherent. The reduction in the federal support price during the dairy surplus crisis of the 1980s resulted in a Price Support program that offered much reduced protection and therefore offered little moderation to milk price volatility in the 1990s. The completion of the Uruguay Round negotiations of the GATT, and the creation of the new World Trade Organization (WTO) opened the door to both the US market as well as provided greater access to the world market for US processors. Both seem to have added to milk price volatility.

In assessing the calamitous economic events of 2009, it is tempting to conclude that these were the result of a very unusual combination of economic factors that are unlikely to repeat any time soon. However, the economic climate in the years before 2009 and the brief period since leave many industry participants feeling that there is both justification and need to find a different set of tools to help dairy farmers deal with turbulent markets. Other issues are also of importance to dairy farmers, and perhaps increasingly so.

Issue #2: Environmental Policy

The current status of agricultural environmental policy is uncertain, but the trend has been for it to become tougher. In assessing environmental policy and regulations applied to agriculture, one might ask:

1. Are stricter environmental controls “right”: is there really an underlying problem
2. Are stricter controls “good”: is what you want me to do actually a solution
3. Is it “fair”
 - a) What is the cost vs. the benefit
 - b) How much should I have to pay (vs. government/society)

Issue #3: Regional, Product Sector and Structural Issues

The dairy industry is often described as being conflicted along regional lines. To the extent that there is disagreement among dairy farmers about appropriate or existing policies, it is probably incorrect to attribute all of these to some kind of dairy regionalism. Many opinions are more correlated with things like farm size, production systems, or marketing systems. Some of these may be somewhat correlated with region. For example, there may be more small-scale farms in

New England, but their views may be more similar to small-scale farmers anywhere than with other New England farmers.

Some issues do have a theme that is more clearly regional. For example, farms that produce their own feed experience feed price volatility very differently from those who rely on purchased feed. These alternative systems can theoretically exist anywhere but agronomic and climate conditions vary regionally and have a lot to do with the feasibility of one system over the other.

State regulations are inherently regional. These play an important role in both the description and enforcement of regulations related to: 1) environmental standards, 2) labor, and 3) animal welfare.

Some differences in policy perspective are associated with the Product Sector to which a farmer sells milk. These could include various aspects of a sector, for example:

1. Fluid vs. Soft vs. Cheese vs. Butter/powder vs. NDM/SMP/MPC etc
2. Organic vs. conventional or pasture-based or rBST free
3. Farm value-added

Another set of factors impacting perspectives on dairy policy relate to industry structure. For example:

1. Low cost production systems vs. Value Added system
2. Local food systems vs. cheap food systems
3. Dairy as producer of milk vs. Dairy as producer of a tapestry of social, economic and environmental benefits
4. Availability of choices
 - a) Where to sell my milk
 - b) Where to buy my inputs
5. Competitiveness of markets
 - a) In terms of choices available and
 - b) Market power wielded by those alternative buyers

Competition or the competitiveness of markets has been of sufficient concern to draw the attention of the US Department of Justice and various members of Congress. No particular sweeping or general allegations or actions have taken place as yet, but this remains fertile ground for debate and concern.

In evaluating the competitiveness of US dairy markets, one might ask: Competition with whom? Of what kind? Do Competitive Markets mean:

1. Low prices, constrained choices
 - a) Few cooperatives is a bad thing
 - b) Few processors is a bad thing
 - c) The CME is a bad thing
 - d) Few retailers and restaurants are a bad thing
 - e) New products are a threat
 - f) We need strong regulation

2. Higher prices, new markets
 - a) Strong cooperatives are a good thing
 - b) Strong processors are a good thing
 - c) Healthy competition keeps us lean and on the cutting edge
 - d) We are better positioned relative to external competitors and international markets
 - e) New products are an opportunity
 - f) We don't need a lot of regulation, especially of the economic variety

In evaluating existing or proposed regulations, we might also ask ourselves about the unintended as well as intended effects of those regulations. Do our fences hold us in or keep the bad guys out? For example,

1. Do Product Identity Standards
 - a) Defend the purity of core dairy products, or
 - b) Inhibit innovation
2. Do Trade restrictions - market access, tariffs, quality and safety standards – protect us from importers or inhibit us as exporters
3. Do Price or income supports protect us from the excesses of markets or do they stifle innovation
4. Are Federal Milk Marketing Orders the benign umpire that keeps the game flowing smoothly or are they a relic of a past that has no relevance to today's marketplace.

What is our optimal strategy in international markets

1. Opportunistic seller (of commodities)
2. Consistent and committed seller (commodities or ?)
3. Active player (value added products?)

Prospects for Changes in Dairy Policy

Although the 2008 Farm Bill is scheduled to be in effect through 2012, many voices in the dairy sector have called for change on a much-accelerated timetable. Then House Agriculture committee chair, Collin Peterson obliged in 2010 with a number of hearings and a clearly stated ambition to reform dairy policy soon, certainly in 2011. Secretary of Agriculture Thomas Vilsack appointed the first ever USDA dairy industry advisory committee to help him think through actions he could take or which he could advocate to improve dairy farm profitability and reduce milk price volatility. The National Milk Producers Federation and other dairy farm advocacy groups offered bold new ideas for dairy policy.

The November 2010 election, which changed the political dynamic at the federal level, has had a profound effect on the trajectory of new dairy policy, and probably agricultural and other policies as well. At this point, what will happen and when it will happen are quite uncertain. To be sure, there will be discussions in 2011, but whether these will result in changes to dairy policy in advance of 2012 farm bill discussions remains to be seen. Indeed, there is some speculation that the next farm bill will not be discussed in earnest until after the 2012 national election.

NOTES
