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Record milk production and a record level of government purchases despite improved commercial disappearance highlight the 1982 dairy situation. Potentially, 1983 presents the same picture. Milk production will be larger and commercial disappearance will likely improve, but USDA will continue to remove large amounts of product from the market.

#### Milk Price Support: Recent History

Before looking at the outlook for production, use and prices in 1983 let's review the recent history of dairy price supports. The Food and Agriculture Act of 1977 and the 1979 amendment mandated the minimum price support be 80 percent of parity with semiannual adjustments. Early in 1981 legislation was enacted to forego the April 1, 1981 semiannual (mid-year) adjustment in support prices. Thus, the support price on April 1, 1981 was held at the October 1, 1980 level of \$13.10 per cwt for milk with a fat content of 3.67 percent (\$12.80 at 3.5 percent fat) until September 30, 1981. Then the support level was raised (as required) on October 1 to 75 percent of parity--\$13.49 per cwt--because the 1977 Act had expired. Subsequent special legislation, enacted on October 20, allowed the level of support to be "rolled back" to \$13.10.

The December 22, 1981 enactment of the Agriculture and Food Act (Farm Bill) allowed the level of support to be continued at \$13.10 for the rest of the 1981/82 marketing year. In addition, the 1981 Farm Bill set minimum levels of support for the final three years of the bill--\$13.25 for 1982/83, \$14.00 for 1983/84 and \$14.50 for 1984/85. The Act also contained provisions for higher levels of support, 70 to 75 percent of parity, if Government removals and/or costs remained below certain "trigger levels".

On March 22 and 23, 1982, USDA held a public dairy symposium at Kansas City to gather input for drafting recommendations to Congress about changes in the price support program. On May 5 USDA announced an emergency dairy plan to deal with surplus milk production, surplus stocks disposal and improving dairy product demand. Some parts of the plan were to be implemented administratively, but other sections required legislation. The key section being that the Secretary of Agriculture be given discretionary authority to set the price support lower than allowed in the 1981 Farm bill.

During the spring and summer several different bills were introduced in Congress calling for changes in dairy legislation to deal with the surplus milk production and the expanding government holdings of butter, cheese, and nonfat dry milk. The Senate and House held hearings on the

dairy problem and the different bills. The House included dairy provisions in the budget legislation that would override the 1981 Farm bill. Likewise, the Senate also included dairy provisions in its budget legislation--but different from those of the House.

During August the House and Senate worked out the differences between their versions of the budget bill, including the dairy provisions. Enactment of the Omnibus Budget Reconciliation Act of 1982 on September 8 resulted in new dairy legislation. The new law set \$13.10 per cwt as the minimum support price for the marketing years beginning October 1, 1982, and October 1, 1983. For the marketing year beginning October 1, 1984, the minimum support will be the level of parity that \$13.10 represents on October 1, 1983. In addition, effective October 1, 1982, to September 30, 1985, the Secretary of Agriculture may provide that 50 cents per cwt be deducted from the proceeds of the sale of all milk marketed commercially by producers, if net price support purchases for the marketing year are expected to equal or exceed 5 billion pounds milk equivalent. The funds are to be remitted to the Commodity Credit Corporation (CCC) to offset part of the cost of the milk price support program. Effective April 1, 1983, to September 30, 1985, the Secretary may provide for deduction of an additional 50 cents per cwt, if net marketing year purchases are expected to go over 7.5 billion pounds milk equivalent. At the same time, though, a program must be established to refund the second 50-cent deduction to those producers who lower their output by a specified amount.

Today's outlook is based on the assumption that the minimum support level provision of the budget (dairy) law and the deductions are implemented. Thus, the support price that was set on October 1 at \$13.10 per cwt for manufacturing grade milk with 3.67 percent fat (\$12.80 at 3.5 percent fat) will be unchanged until October 1, 1984. This support is the minimum allowed and is the same support price that was put into effect October 1, 1980. In addition, the Secretary of Agriculture will implement a 50-cent-per-cwt deduction for all milk marketed beginning December 1 and a second 50-cent-per-cwt deduction beginning April 1, 1983. The deductions are expected to remain in effect for all of 1983 and 1984.

#### Milk Prices Below 1981

Prices received by farmers for milk in October were up seasonally from the July level, but were still below a year earlier. The gain from July reflects the higher fat content of October milk compared with July and a higher fluid utilization proportion. The price shortfall from a year earlier was primarily the result of continued surplus production, but also the result of the slightly lower support price. The support level was \$13.49 per cwt for the first 20 days of October in 1981 and then was "rolled back."

October prices for manufacturing grade milk averaged \$12.80 per cwt--up 50 cents (4 percent) from July but 10 cents below a year earlier. The October price of Grade B milk after adjusting to 3.67

percent fat, was \$12.62 per cwt, 48 cents below support. Thus, October marked 31 consecutive months that manufacturing grade milk prices (adjusted for fat content) have failed to reach support.

Prices received by farmers for all-milk reached a seasonal low in June and have risen since--averaging \$13.80 per cwt during October. For first-half 1982, the all-milk price averaged 25 cents per cwt (1.8 percent) below a year earlier. Farm milk prices may rise 10 to 20 cents by December; due to a normal increase in fat content and a higher fluid milk utilization rate caused by seasonally lower production and higher fluid sales. In 1983, the all-milk price is expected to be little changed from 1982. But, the effective returns per cwt received by farmers for milk in 1983 could average 6 percent or more below 1982, given the 50-cent deduction beginning December 1 and the second 50-cent deduction starting April 1.

### Feed Prices Lower

The decline in feed ingredient (corn and soybean meal) prices this summer have partly been reflected in lower dairy feed prices. The price of 16-percent protein dairy ration was \$171 per ton during October, down \$12 (6.6 percent) from a year earlier and \$10 below May. This decline in feed costs, coupled with an all-milk price which decreased less--1.4 percent in October--has resulted in a milk feed price relationship of 1.61, the highest value since January 1979.

With the record harvest currently being completed, feed prices likely will show little upward movement and therefore will trail year-earlier levels at least through the first half of 1983. Meanwhile, with farm milk prices expected to show a seasonal decline from January to June, the milk-feed price relationship will move lower, but will remain above this year throughout the first half of next year. However, if the milk price is adjusted to account for the forthcoming 50-cent-per-cwt deductions the milk-feed price relationship moves below year-earlier levels starting next April, but remains above 1980 levels.

### Output Gains Continue

Milk production during the second quarter of 1982 increased 1.1 percent from a year earlier. The gain was due to 93,000 more milk cows and a modest increase in output per cow of 7 pounds (0.2 percent) from a year earlier. During the third quarter production was up 2.3 percent, the result of 101,000 more cows and an increase of 42 pounds (1.4 percent) in output per cow. With the number of dairy herd replacements per 100 cows record large on July 1, some additional expansion in the herd will likely occur this fall. In addition, the milk-feed price relationship is expected to continue very attractive for heavy concentrate feeding. Thus, year-over-year gains in output per cow will likely occur. As a result, milk production is expected to continue to increase this fall, as it has since mid-1979. This year's production will be about 2 percent above the record 132.6 billion pounds in 1981.

Dairy farmers' reactions to the December 1 and authorized April 1 deductions will play a key role in determining the size of 1983's milk production. The deductions add uncertainty to other economic factors that point toward additional milk production--low feed prices, large forage supplies, and unfavorable farm and non-farm alternatives. If farmers react quickly to the forthcoming deductions and start to reduce their herds or leave the industry, production late in 1983 could be less than year earlier levels, leaving total output about 1 percent above this year. However, if producers delay reactions until after next spring's flush production period, total 1983 output will show a sizable increase from 1982.

#### Dairy Product Prices Unchanged

Wholesale prices for butter, cheese, and nonfat dry milk continue stable. They have been nearly unchanged since October 1980 because supplies are more than ample and the CCC support purchase prices are unchanged. In September, the Bureau of Labor Statistics (BLS) index of wholesale dairy prices was 249.3 (1967=100), up only 1.5 percent from a year earlier. Since the support price and the support purchase prices did not increase this fall and the 50-cent deductions have no direct effect on processor costs for milk, wholesale dairy product prices are expected to be near current levels through mid-1983.

Retail dairy product prices are expected to average 1 to 2 percent higher this year than in 1981, because farm-to-retail marketing costs are up more than the decline in farm prices. The September BLS index of retail dairy prices was 247 (1967=100), up 1.1 percent from September 1981. Retail dairy products prices will likely increase somewhat again in 1983, also because of higher farm-to-retail costs.

#### Use of Milk Improves

Commercial disappearance of manufactured and fluid dairy products during January-September increased 1.7 percent from a year earlier, on a milk-equivalent, fat-solids-basis, a gain of 1.5 billion pounds. Total disappearance for 1982 is expected to be 122 billion pounds, a gain of 1.9 billion pounds and a strong recovery from 1981, but less than expected given the decline in real dairy prices this year. The weak general economy and gains in unemployment were likely the principal causes, but increased domestic donations of dairy products by USDA and the reduced expenditures on school feeding programs probably also had an impact. Commercial disappearance is expected to again be up 1.5 percent in 1983. Real prices of dairy products will likely decline again, next year, but the same factors that slowed the gains in commercial use this year will again be important in 1983.

USDA purchases during 1982 on a milk-equivalent, fat-solids-basis are expected to increase 1.6 billion pounds--partly because of the 2.6 billion gain in production compared with the gain in use of 1.9 billion, but mostly because of a reduction in commercial stocks of nearly 1 billion pounds. With commercial disappearance projected to improve in

1983, but with some gains in milk production expected, little reduction in the level of USDA purchases is likely. Government stocks as purchases exceed donations, in 1983 will continue to expand.

To recap, the dairy industry can expect 1983 to be similar to this year. Milk production will likely increase enough to offset a gain in commercial use, thus USDA removals will remain large and keep farm milk and retail dairy product prices near year-earlier levels.

Table 1--Dairy summary, 1980-82

Item	Unit	1980	1981	1982	Percent change :1981-82
			Annual 1/		
Milk production	Bil. lb.	128.5	132.6	135.1	+1.9
Milk per cow	Lb.	11,889	12,147	12,252	+0.9
Number of cows	Thou.	10,810	10,919	11,024	+1.0
Milk prices: All-milk	DoI./cwt.	13.00	13.80	13.55	-1.8
Manufacturing grade	do.	12.00	12.70	12.65	-0.4
Cash receipts	Mil. doI.	16,605	18,106	18,226	+0.7
Value of dairy rations	DoI./cwt.	7.42	8.05	7.45	-7.5
Milk-feed price ratio	Lb.	1.48	1.44	1.54	+6.9
Utility cow prices, Omaha	DoI./cwt.	45.73	42.01	39.85	-5.1
			January-September		
Wholesale prices:					
Butter (Chicago, Grade A)	Ct./lb.	136.6	147.6	147.6	0
American cheese (Wisconsin assembling points, 40-lb. blocks)	do.	130.5	139.1	137.6	-1.1
Nonfat dry milk (High heat, F.O.B. Central States)	do.	86.73	93.00	93.13	+0.1
Dairy products (BLS)	1967=100	227.4	245.1	248.5	+1.4
USDA net removals:					
Butter	Mil. lb.	207.6	307.1	337.7	+10.0
American cheese	do.	307.5	489.8	525.4	+7.3
Nonfat dry milk	do.	524.2	676.8	779.0	+15.1
Evaporated milk	do.	11.8	14.6	15.5	+6.2
Milk equivalent	do.	7,351	11,212	12,198	+8.8
Retail prices (BLS): 2/					
All foods	1967=100	251.3	273.6	285.3	+4.3
Dairy products	1967=100	224.8	243.1	246.8	+1.5
Manufactured products output:					
Butter	Mil. lb.	865.6	925.8	963.7	+4.1
American cheese	do.	1,806.5	1,997.4	2,059.0	+3.1
Other cheese	do.	1,172.8	1,193.9	1,268.4	+6.2
Nonfat dry milk	do.	929.2	1,022.9	1,100.4	+7.6
Canned milk	do.	562.2	564.4	553.9	-1.9
Cottage cheese	do.	639.4	597.0	573.9	-3.9
Ice cream	Mil. gal.	653.0	651.5	663.5	+1.8
Ice milk	do.	237.3	236.0	233.9	-0.9
Imports of dairy products:					
Total milk equivalent	Mil. lb.	1,230	1,453	1,786	+22.9
Commercial disappearance:					
Total milk	Mil. lb.	88,945	89,650	91,140	+1.7
Butter	do.	641.0	621.6	653.0	+5.1
American cheese	do.	1,488.0	1,567.1	1,610.8	+2.8
Other cheese	do.	1,284.3	1,341.9	1,412.1	+5.2
Canned milk	do.	507.6	504.2	485.9	-3.6
Nonfat dry milk	do.	426.1	346.2	319.6	-7.7
Fluid sales in Federal order markets:					
Whole milk	Mil. lb.	15,071	14,443	13,980	-3.2
Low-fat milk	do.	10,796	11,140	11,262	+1.1
Total	do.	25,867	25,583	25,242	-1.3

1/ 1982 estimated. 2/ For all urban consumers.