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Comparing U.S. and EC Dairy Policies

Political Economic Analysis of U.S. Dairy Policies and European Community Dairy Policy Comparisons. *By Mary A Marchant New York Garland Publishing Co , 1993, 273 pages*

Reviewed by Larry Salathe

This book compares the dairy policies and the performance of the dairy sectors in the United States and the European Community (EC) and presents theoretical and empirical models to explain changes in the U S support price for manufacturing milk The book also graphically depicts the effects of various policy instruments on domestic production, consumption, prices, and the international market for dairy products, reviews past studies that examine the effects of the U S milk price support and federal order programs, and contains a very thorough bibliography (in excess of 50 pages)

The book begins by providing a historical review of the dairy policies and trends in production, consumption, prices, surpluses, and government dairy program costs in the United States and the EC The author discusses the history of federal milk marketing orders and the dairy price support program in the United States and the EC's Common Agricultural Policy (CAP) Economic models are presented to graphically illustrate the domestic and international effects of these policies Despite the complexities of the U S and EC dairy programs, this material is very readable

Unfortunately, the discussion of dairy policies and trends ends in the mid-1980's In the mid-1980's, U S dairy program costs averaged about $2 billion per year and the federal government was purchasing large amounts of butter, cheese, and nonfat dry milk Since the mid-1980's, reductions in the support price, marketing assessments, and the dairy termination program have greatly reduced government surpluses and the cost of the diary program In FY 1992, U S dairy program costs amounted to $232 million and butter was the only dairy product in which the government held significant surpluses

The succeeding chapter reviews theoretical and empirical models that endogenize government behavior The motivation for reviewing this literature is to develop a model that can be used to predict the level of the support price for manufacturing milk The author provides a more than adequate literature survey, which suggests two possible approaches for endogenizing government behavior The first approach is to estimate an econometric equation that relates the policy instrument to a variety of variables that may influence the policy outcome These variables could include noneconomic variables, such as political contributions by special interest groups The second approach assumes policymakers set policy instruments to maximize a social welfare function, which equals the weighted summation of producer surplus, consumer surplus, and taxpayer cost Solving the first order conditions yields a system of equations that may under certain conditions be solved for the implied weights that policymakers attach to consumers, producers, and taxpayers and relates the level of a policy instrument to sector variables The author discusses each approach in detail and demonstrates how the use of a social welfare function can be used to derive the implied weights policymakers attach to various groups

The final chapter of the book presents an econometric model of the U S dairy industry The model includes econometric equations to estimate the supply and demand and support price for manufacturing milk The support price for manufacturing milk was found be positively related to the support price lagged and negatively related to the level of government stocks of dairy products, total farm income lagged, and the federal budget deficit An alternative specification indicated the support price was positively related to the support price lagged and negatively related to the federal budget deficit, the ratio of dairy program costs to the total cost of farm programs, and the difference between the U S support price and the world price for manufacturing milk

The coefficient of the lagged support price was significantly above 1 in each econometric equation presented by the author, which leads to the conclusion that the support price will increase significantly from year-to-year even though all variables remain constant This result appears to be in conflict with the more than 30 percent decline in the support price since 1981 Over the past several years, reducing the federal budget deficit and the cost of the dairy and other farm programs were the primary motivating factors for lowering the support price That was not the case prior to the early 1980's when parity was used to establish the support price for manufacturing milk

Salathe is a staff economist with the Economic Analysis Staff, USDA

Maximization of the social welfare function leads the author to conclude that the support price is determined by the net change in government stocks of dairy products However, the reported econometric equations indicate that a significant negative relationship does not exist between the support price and government stocks In addition, this approach leads to the conclusion that policymakers place a negative weight on producer surplus and on consumer surplus This result is inconsistent with traditional welfare analysis, which places positive weights on producers, consumers, and taxpayers

This very readable book provides a good reference for those interested in models of the dairy industry and models that endogenize government behavior It also contains an indepth description of the origin and evolution of dairy policy in the United States and the EC up until the mid-1980's The graphical analysis of dairy programs is extremely helpful in demonstrating and explaining the economic consequences of the U S and EC dairy programs