Farm Service Agency Programs

Milton Madison

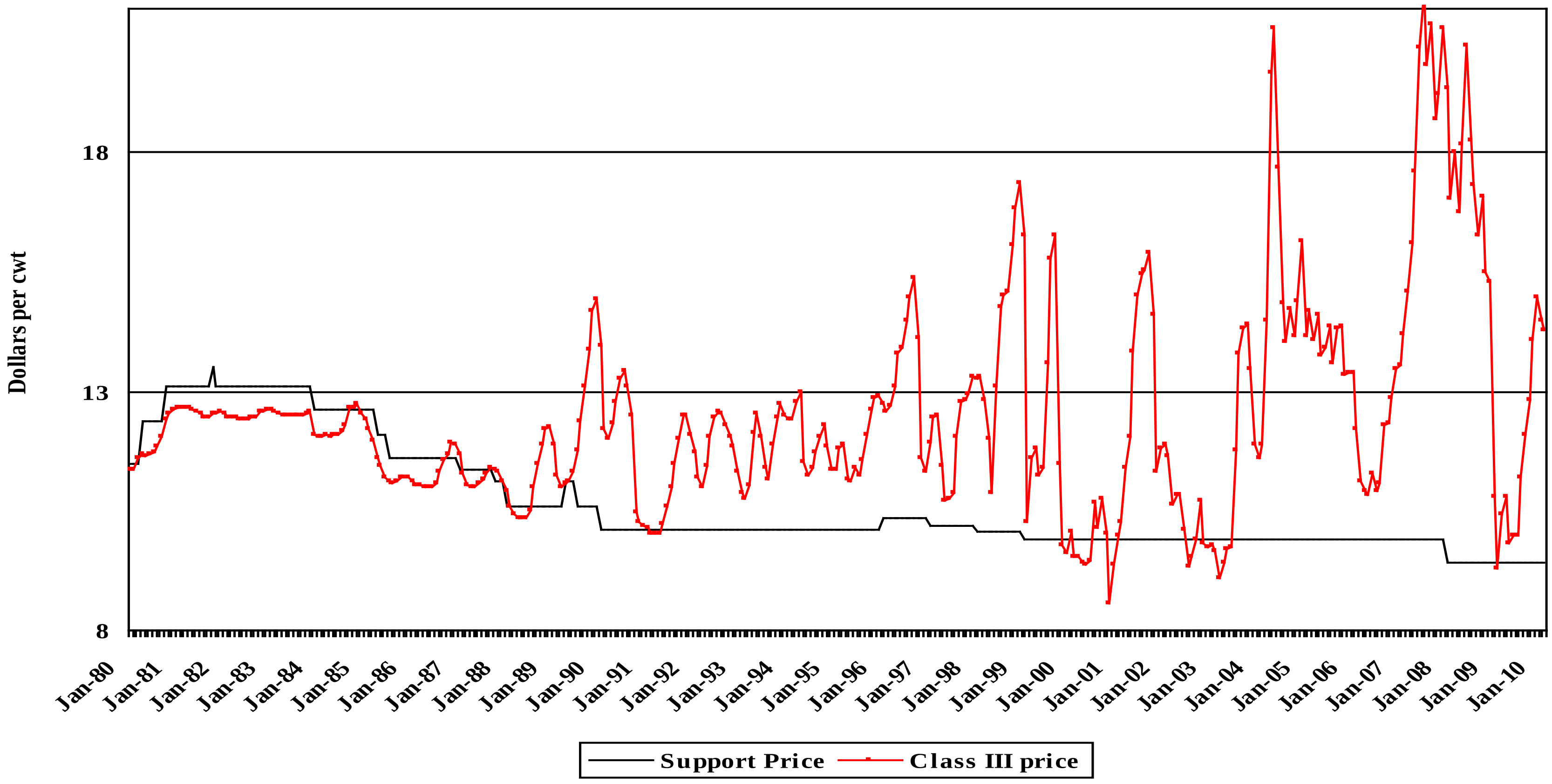
Overview

- Background
  - FSA operates two primary dairy programs
    - Dairy Product Price Support Program (DPPSP)
      - Supports dairy farmers by purchasing dairy products
      - Standing offer to purchase products at an announced price
    - Milk Income Loss Contract Program (MILC)
      - Direct payment program with formula established by Farm Bill
      - Feed cost adjuster was added in the 2008 Farm Bill
  - These two programs (why?)
    - Can be viewed as two tiered support
    - MILC starts at higher price level

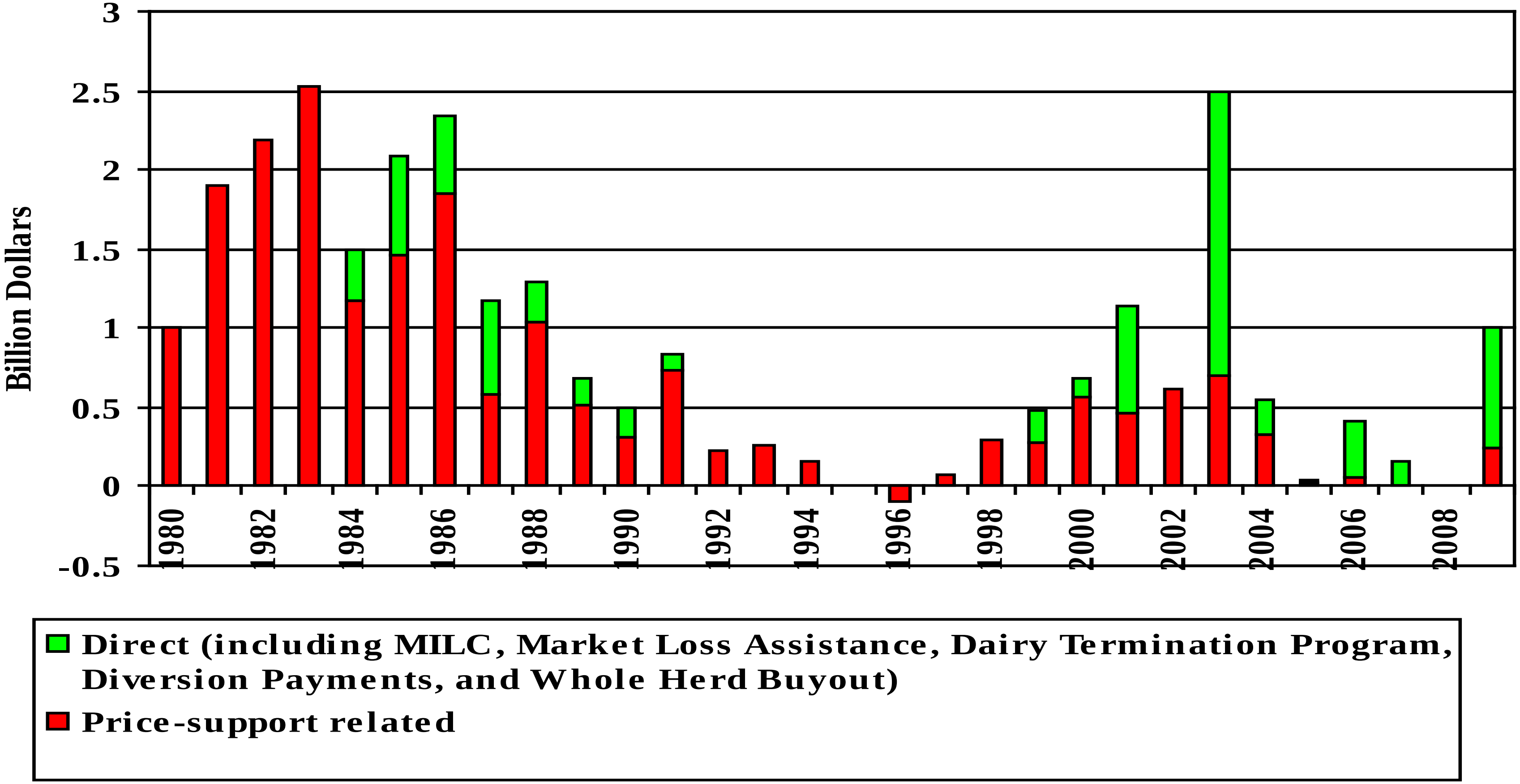
DPPSP Limits Milk Price Declines

- DPPSP was initially authorized by the Agricultural Act of 1949, and has been reauthorized by subsequent Farm Bills.
- Minimum purchase prices for cheese, butter, and NDM are currently set the 2008 Farm Bill.
- Previously, purchase prices were set so producers received an average price not less than the support price for milk with 3.67% butterfat.
- Increasing support levels in the late 1970s tied to parity led to large purchases and outlays but stable producer milk prices.
- Congress reacted by reducing the level of support, imposing producer assessments and authorizing the dairy termination and milk diversion programs. As the support level has declined, price volatility increased.

Class III Price (cheese) Has Been More Variable In Recent Years



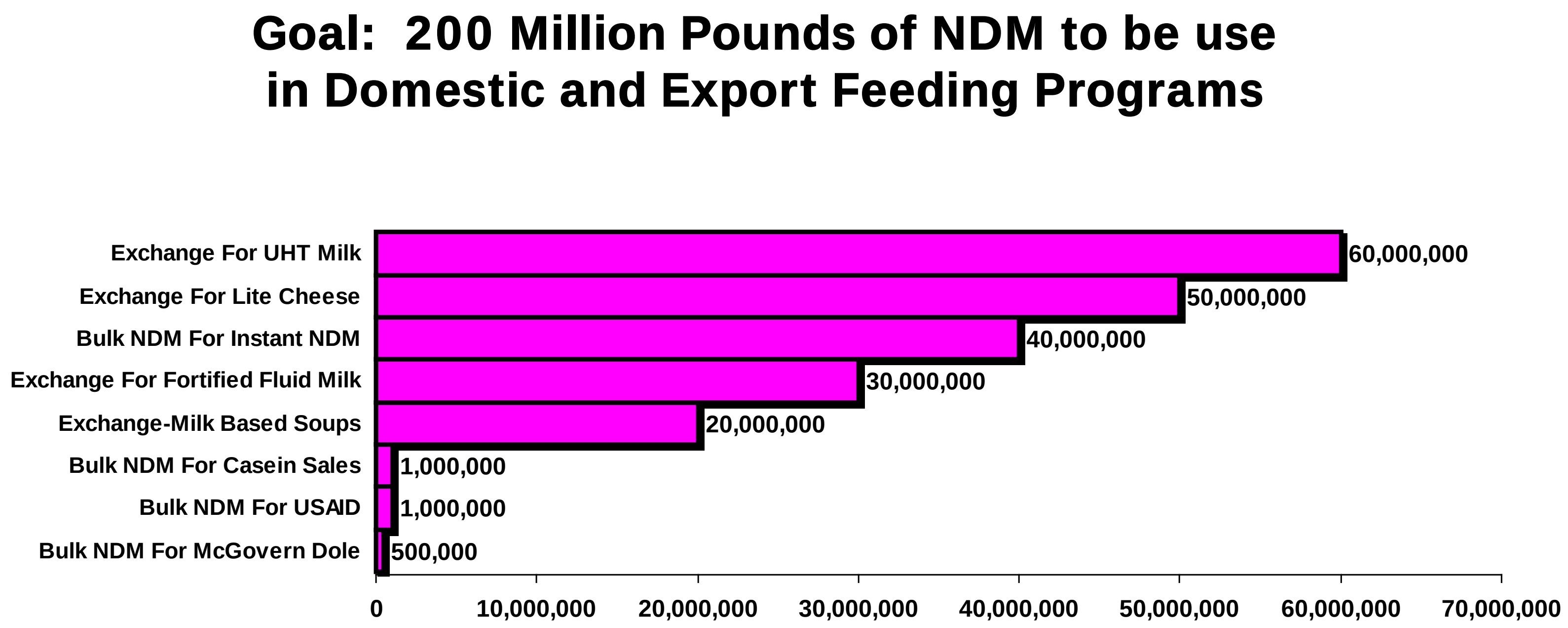
Since the 1980s, price support costs have fallen while direct payments have risen



DPPSP Benefits Come From Market

- DPPSP supports producers through higher market prices rather than direct payments.
- Assuming the demand for dairy products is inelastic, the increase in farm income from purchasing product can exceed the initial purchase cost.
- While purchases boost milk prices in the short term, USDA must store and dispose of a perishable product that if allowed to enter commercial channels will lower producer milk prices.
- DPPSP may discourage ingredient use by food manufacturers and stifle new dairy product development.
- Imports may substitute for higher-priced domestically produced product.

NDM Dispositions



MILC: Authorized By The 2002 Farm Bill To Provide Counter-Cyclical Style Payments

- Monthly payments to eligible producers are made when the Boston Federal Order Class I price for fluid milk falls below $16.94/cwt.
- Payment rate equals 0.45 times the difference between 16.94 adjusted for feed costs if greater than $7.35 per cwt. and the Class I Price in Boston.
- Feed costs include the prices as reported by NASS for corn, soybeans, and alfalfa hay with weights of 51% for corn, 8% for soybeans and 41% for alfalfa hay.
- Payments per registered dairy operation are limited to 2.985 million pounds of milk (equivalent to ~ 145 cows) per fiscal year.
- As farm size increases, the percentage of production covered by MILC payments declines.

MILC Payments Are Concentrated In the Northeast and Upper Midwest

- Traditional dairying states (with smaller farms) receive the bulk of MILC payments:
  - 54 percent of MILC payments for FY 2009 production went to producers in 6 states: NY, VT, PA, WI, MI, and MN…
  - …which account for 35% percent of the milk supply.
  - California received only 12 percent of MILC payments although it produced 22 percent of milk supply.
- Producers received an average of $475 million per fiscal year under the 2002 farm bill in MILC payments.
- MILC payments under the 2008 Farm Bill have totaled $918 million.

MILC Benefits Come Directly From Government Outlays

- MILC payments directly benefit milk producers but some more than others due to the limit on production eligible for payment.

- Economic theory suggests that direct payments may lead to higher milk production when milk prices fall, prolonging price recovery.

- To the extent that MILC payments limit the response to low milk prices by smaller producers, the largest producers may be worse off since their payment production is capped.

- Consumers may benefit from slightly lower milk prices if MILC payments reduce the incentive to liquidate herds when milk prices fall.

Summary

- Milk prices have become more volatile after Congress lowered the support price in the early 1980s.
- Government price support purchases boost milk prices in the short term but create storage and disposal issues.
- Higher dairy product prices through price support purchases may discourage ingredient use by food manufacturers, and stifle new dairy product development.
- Providing counter-cyclical payments to producers can help offset the effects of low producer milk prices but may prolong needed production response.
- MILC payments primarily benefit smaller producers due to the limit on production eligible for payment.

For more Information

- Farm Service Agency Program Fact Sheets and general information:

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