1978

Initiated Measure: Repeal of Milk Marketing Act

Cooperative Extension South Dakota State University

Follow this and additional works at: https://openprairie.sdstate.edu/extension_fact

Recommended Citation
https://openprairie.sdstate.edu/extension_fact/514

This Fact Sheet is brought to you for free and open access by the SDSU Extension at Open PRAIRIE: Open Public Research Access Institutional Repository and Information Exchange. It has been accepted for inclusion in SDSU Extension Fact Sheets by an authorized administrator of Open PRAIRIE: Open Public Research Access Institutional Repository and Information Exchange. For more information, please contact michael.biondo@sdstate.edu.
Initiated Measure:
Repeal of
Milk Marketing Act

Cooperative Extension Service
South Dakota State University
U.S. Department of Agriculture
Initiated Measure:
Repeal of Milk Marketing Act

Galen Kelsey
Extension economist — public affairs

The proposed initiated act seeks to repeal the state's Dairy Industry Marketing Act, more commonly known as the milk marketing act.

Both sides agree that the price of milk to the consumer would be cheaper at stores in larger towns and there may be more brands of milk to choose from, if the repeal is passed in the November voting. But neither can say how long cheaper prices will last.

The impact of repeal upon the Grade A milk producers is also hard to predict. That would depend upon how much Grade A milk from surrounding states would be transported in.

The Background

Both production and demand for fluid milk vary from day to day and by season. Production is highest in the spring; demand is greatest in the fall. Milk, being a perishable product, cannot be stored for any length of time. Therefore, surpluses and shortages would probably cause the retail price of milk and milk products to fluctuate under a free market system.

But milk is not sold under the free market system which reacts to supply and demand. CCC price support programs, federal milk marketing orders, and state control laws have overridden fluctuations in supply and demand, and have given consumers, milk handlers, and dairymen alike the benefits of stable prices and ample supplies of milk year round. Today, over 95% of all fluid Grade A milk in the U.S. is regulated in some way.

Federal orders establish only the minimum prices processors must pay producers for Grade A milk. Some states also regulate wholesale and retail prices. In May 1978, nine states regulated wholesale prices and six states were authorized to set retail prices. Twenty-eight states and Puerto Rico regulated trade practices. In 1976, 15 states regulated wholesale prices and 14 controlled retail prices.

The current South Dakota law, in effect, sets wholesale and retail prices, prohibits sales below cost, and regulates trade practices. Six other states have similar authority.

The Dairy Industry Marketing Act

The Dairy Industry Marketing Act passed in 1966 (SDCL 37-3-8 to 37-3-72) is designed to prohibit unfair trade practices in the marketing of fluid milk and thereby protect the state's dairy industry. The act makes it unlawful for a milk handler to sell milk below cost at either the processor, wholesaler, or retailer level.

Costs at each level are to be determined by a seven-member dairy products marketing commission appointed by the Governor. The law states, in substance, that in the absence of specific evidence to the contrary, the minimum markup the retailer must charge is 10% above the price he pays for milk delivered to his store.

The 10% minimum represents the allowance for cost of handling and profit. The retailer may charge more but not less. Volume discounts to the retailers of up to 8% based on cost savings are allowed.

The membership of the dairy products marketing commission, by law, is composed of one dairy processor, one active Grade A milk producer, and three consumers who in no manner are or have ever been connected with the production, processing, or sales of dairy products. The sixth member is either an accountant, auditor, or dairy economist; and the seventh member is a retailer of dairy products.

It is the function of this seven-member commission to determine the processing and marketing costs upon which the final minimum retail price is based. (The price paid to the Grade A producer is established by the federal milk marketing order program.)

The law has several sections which prohibit the use of any kind of premium by the processor-distributor to the retailer to encourage the sale of one dairy product brand over another.

Other Programs

The South Dakota milk marketing act is only part of the dairy products pricing picture. There are also the dairy price support program and the federal milk marketing order program. These are both federal programs.

The dairy price support program explicitly puts a floor under the price of manufacturing grade milk, which effectively maintains a floor under all milk prices. The Food and Agriculture Act of 1977 sets a minimum price support level of 80% of parity until changed by Congress.

The federal milk marketing order program establishes minimum prices paid to producers for Grade A fluid milk in those areas of the country where producers have voted to initiate the market order program.
There are three market order areas that include part of South Dakota: the Eastern South Dakota, Upper Midwest and the Black Hills areas. Only the Black Hills area is completely within the boundaries of the state. The Eastern South Dakota area includes 28 South Dakota counties, a few in southwestern Minnesota, and Rock County in Iowa. The Upper Midwest consists of all of Minnesota except those few counties in the Eastern South Dakota area, one third of Wisconsin, about a third of North Dakota, and seven counties in northeast and north central South Dakota. It is the largest of the three and one of the largest in the country.

Prices for three classes of Grade A milk are established monthly in each of the market order areas. These are the minimum prices the milk processor must pay the dairyman for the raw product delivered to his plant. Prices are based upon the cost of production and fluctuate from month to month.

The price of manufacturing grade milk in the Minnesota-Wisconsin area is used as the basis for determining the price of milk all over the country. This is because this is the area of high production and competition in the manufactured dairy products industry. Production costs in these two states are assumed to be the lowest in the nation. The prices of milk in New York, Dallas, or Rapid City are calculated on the basis of the Minnesota-Wisconsin price plus adjustments for transportation and other economic factors.

Prices are established for three classes of Grade A milk in each of the market order areas. (Prices are established for classes I and II only in the Black Hills area.) Class I milk is bottled* Grade A fresh milk, flavored milk, buttermilk, etc. Class II milk is produced under Grade A standards but used in the production of ice cream, cottage cheese, yogurt, and ice cream mixes. Class III milk is processed into hard cheese, butter, powdered milk, and similar products.

Because it's just "milk" when the processor buys it from the dairyman, the price paid to the dairyman's cooperative or the independent Grade A producer is a "blend" price based upon how the milk in the marketing area is used.

The prices of the various classes of milk in April 1978 are shown in Table 1.

<table>
<thead>
<tr>
<th>Class</th>
<th>Price per 100 pounds</th>
<th>% Utilization</th>
</tr>
</thead>
<tbody>
<tr>
<td>I</td>
<td>$10.40</td>
<td>47</td>
</tr>
<tr>
<td>II</td>
<td>9.34</td>
<td>12</td>
</tr>
<tr>
<td>III</td>
<td>9.24</td>
<td>41</td>
</tr>
<tr>
<td>Blend price</td>
<td>9.84</td>
<td>—</td>
</tr>
</tbody>
</table>

*The term bottled milk includes fresh milk packaged in paper and plastic containers.

The blend price paid to producer cooperatives in April was $9.84, which was calculated on the basis of the weighted average price of all the milk bought and used in the three market classes. The blend price in the Black Hills region during April was $10.16 per hundred.

<table>
<thead>
<tr>
<th>Class</th>
<th>Price per 100 pounds</th>
<th>% Utilization</th>
</tr>
</thead>
<tbody>
<tr>
<td>I</td>
<td>$10.12</td>
<td>18.7</td>
</tr>
<tr>
<td>II</td>
<td>9.34</td>
<td>3.5</td>
</tr>
<tr>
<td>III</td>
<td>9.24</td>
<td>77.8</td>
</tr>
<tr>
<td>Blend price</td>
<td>9.46</td>
<td>—</td>
</tr>
</tbody>
</table>

The Sides of the Question

Defenders of the South Dakota Dairy Industry Marketing Act maintain that, if the law is repealed, South Dakota will be flooded with surplus bottled milk from surrounding states. This will lower our utilization percentage (percentage sold in bottles) and thus the blend price for the South Dakota producer. As shown in the tables, in April the Eastern South Dakota Class I usage of Grade A milk was nearly half, while less than a fifth of the Minnesota Grade A milk was bottled milk. There would be an incentive for bordering state firms to raise their utilization percentage and thus their blend price at the expense of the South Dakota producer.

Both the defenders and opponents of the law agree that the retail price of milk would probably go down in the larger towns of the state because of competition with the surrounding states' cheaper milk and lower distribution costs. Milk prices might rise in the smaller towns and remote areas because of higher distribution costs.

Under the Dairy Industry Marketing Act distribution costs are shared. If the law is repealed consumers will pay the true costs of distribution; some will pay more, some will pay less.

Another factor to consider in the pricing policies of Grade A milk is the premium paid by the bottlers to the milk processors. Most of the milk in South Dakota is collected by producer owned cooperatives. Bottlers purchase their needs from the cooperative and pay the prices determined under the federal milk marketing order program.

In addition the cooperative may charge a premium which is negotiated each month between the bottler and the producer cooperative. The amount of the premium varies from month to month depending in part upon the differential between the Grade A milk price and the price of manufacturing milk.

When the demand is high for manufacturing grade milk (usually in the fall when milk supplies are low)
the announced price differential between classes of milk is narrow and the premium on Grade A milk, in effect, maintains the price spread between classes.

Not all of the premium is paid to the cooperative to maintain the price spread. A portion of the premium is payment for the many services performed by the cooperative, such as quality control, transportation, etc. The amount of the premium paid per 100 pounds for this purpose is rather constant and stays with the cooperative to help pay its expenses. The balance is a passthrough to the producer, and serves the purpose of maintaining the price differential between Grade A and manufactured milk.

Repeal of the Dairy Industry Marketing Act will not affect the practice of paying premiums. It may affect the amount of the premium in two ways.

First, because it is paid only on Grade A milk, if the utilization percentage goes down, the premium received by the producer and his cooperative will be less. Second, premiums paid in Minnesota are usually lower because milk supplies are higher the year around. Premiums paid in Nebraska and Iowa are higher than in South Dakota. If the bottler of South Dakota milk purchases part of his supplies from surrounding states, he is under no obligation to pay a higher premium for South Dakota produced milk.

Advocates of the law's repeal maintain that even though the price to the producer in surrounding states is lower, this does not account for the higher retail price of milk in South Dakota. There are 11.6 gallons of milk in 100 pounds. The Class I price differential plus the premium per hundred pounds between Eastern South Dakota and Minnesota is about 40 cents, or about 3 3/4 cents a gallon. (In the Black Hills region the differential is about a dollar per hundred pounds or about 8 1/2 cents a gallon.) The advocates of repeal claim that the retail price differences are a direct result of the action of the dairy marketing commission. They argue that the commission has allowed cost increases which are above the milk handlers' actual costs, resulting in higher priced milk and larger profits for the processor.

Proponents of the South Dakota law respond that the lower retail prices of milk in Minnesota and surrounding states are the result of pricing policies of retail stores. Milk is used as a loss leader to lure customers to their stores, and these losses are absorbed by higher prices on other goods.

Probable Impacts of the Law's Repeal

Minnesota and Wisconsin can produce and process all the Grade A milk consumed in South Dakota.

Both sides agree that some milk prices will be lower if the law is repealed. How much lower is impossible to project because there is no way of knowing if milk will be sold at, above, or below cost.

The full impact of repeal upon the South Dakota Grade A dairy producer depends upon whether or not the retailer can buy bottled milk cheaper from surrounding states. If South Dakota retailers purchase a portion of their milk from surrounding states, which is likely in bordering towns, the blend price to the South Dakota producer will be reduced in proportion to the drop in the percentage of South Dakota milk sold in bottles.

Repeal of the law is of vital interest to the South Dakota milk processors. They cannot buy cheaper milk from surrounding states in bulk for processing because they must pay the prevailing order price in the area where the milk is processed, not where it is produced. For them, the price of the milk is the same except that they would have higher transportation costs on milk from neighboring states.

They predict that wholesalers in surrounding states will adopt predatory trade practices currently outlawed by the milk marketing act and sell bottled milk to South Dakota retailers at prices South Dakota bottlers cannot meet. When they have eliminated the competition from the local bottlers they will be free to raise prices at will.

The impact of repeal upon the manufacturing milk producer will be minimal and indirect. The Commodity Credit Corporation (CCC) supports the price of manufactured products through purchases in the open market when prices of such products as cheese or butter fall below 80% parity (until September 1979). Prices can, and often do, go above 80% of parity, depending upon supply and demand. If supplies of manufactured dairy products increase, prices will tend to remain near the 80% level. In the long run it will make little difference in manufacturing milk prices if more South Dakota milk goes into manufactured milk uses and an equal amount of milk in surrounding states is taken out of that marketing class and sold as bottled milk.

South Dakota voters in November must decide if they want to continue outlawing unfair trade practices and fix Grade A milk prices to protect the South Dakota Grade A milk industry or to allow market forces to operate within the constraints of the federal milk marketing order program and the CCC price support program.

Issued in furtherance of Cooperative Extension work, Acts of May 8 and June 30, 1914, in cooperation with the USDA. Hollis D. Hall, Director of Cooperative Extension Service, South Dakota State University, Brookings. Educational programs and materials offered without regard to age, race, color, religion, sex, handicap or national origin. An Equal Opportunity Employer.

File: 5.3—20,000 printed at estimated 3 cents each—8-76mb—2563A