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Dairy's Financial Problems Outstrip Usual Ups And Downs

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One of the pleasures of our job is the opportunity to get out of the office and speak to farm organizations and listen to what farmers from various parts of the country are experiencing and thinking. Last winter we began to hear stories of price problems in the dairy industry.

Depending upon the location, milk prices had been in the $19-$20/cwt range in July 2008 and then fell below the cost of production by February 2009, affecting small and large producers alike, with some losing thousands of dollars a day. One of the problems facing diary farmers is the high cost of feed with 2008 crop year corn prices nearly double what they were a few years earlier.

By mid-summer milk prices were in the $10 range and the plight of dairy producers had reached the ears of those in Congress.

During the first week of October 2009, Congress is expected to approve $350 million in aid for dairy farmers. Of that aid, $60 million would be used for the purchase of cheese and other products for US food donations.

The other $290 million would be distributed to dairy producers in the form of direct aid. One of the regionally sensitive issues is the means by which the aid gets distributed to farmers.

Eastern producers, who are generally smaller than Western producers (primarily in California and Arizona), would like to see a cap on benefits set at three million pounds of milk. Western producers with very large operations argue that setting a cap at that level discriminates against those who produce the largest proportion of the milk in the US.

At the present time various Congress members are weighing in on behalf of their dairy producers.

In addition to Congressional action, a farmer-funded organization, Cooperatives Working Together, has given payments to farmers to reduce their herds by 226,000 producing cows. The group is in the process of accepting bids for a third buyout round.

Prices in the dairy industry are cyclical with four valleys and three peaks in prices paid to farmers since early 2001. What dairy farmers lack is a shock absorber to temper the price swings that take them from feast to famine in a short time.

Adding to the price of feed and sharp fluctuations in export demand is a new technology that allows farmers to expand their herds quickly by producing mostly heifer calves. When prices were high, farmers were told that they needed to produce more milk and so they responded by adopting the new technology that allows artificial insemination firms to mark and separate out male sperm from female sperm.

The new technology allows farmers to produce 90 percent heifer calves and 10 percent bull calves instead of the usual 52 percent bull calves and 48 percent heifers. This new batch of heifers is coming to maturity just as demand shrinks and prices hit the bottom.

Like with grain farming, supply-increasing technologies are important to ensure that agriculture has the means to meet future demand, but in the short-run they often result in price and income problems.

Some are worried that raising the support price will stimulate production because the support price will reduce market signals and result in overproduction. While that may be true to an extent, it must be recognized that the present glut is in part the result of market signals that were in place a year and a half ago.

While printing plants can respond quickly to swings in market signals by closely managing their orders of ink and paper, drawing on the stock they have on hand in bad times, dairy farmers do not have that luxury. When demand is high, the industry needs additional cows, but that takes time: heifers have to be conceived, carried, born, and then raised to maturity. The response time is much slower than it is in the printing industry, for instance.

Likewise, when prices are in the tank and price signals are calling for a reduction in producing cows, one still has to account for those heifers that were raised in anticipation of increased demand. Balancing out the supply is not as easy as just drawing down inventory. Here again, the response time to price changes is much slower than in many other industries. In down times excess supply in the dairy industry will continue for some period of time, with or without price supports.

What is needed in this situation is a combination of price supports, industry financed capacity reduction, and the management of government programs to take the excess supply off the market so farmers make their living from the marketplace and not the mailbox. Government support can be tied to supply management programs to prevent government holdings from getting as large as they once were. Δ

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