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Dairy Policy Brief #2: Dairy Product Price Support Program

What is the Program?

Dairy price supports have been a fixture of U.S. dairy policy since 1949. Price supports are a ***market intervention*** program, meaning that the government (USDA's Commodity Credit Corporation or CCC) offers to purchase non-perishable dairy products (butter, cheese, and nonfat dry milk) from manufacturers at specified (intervention) prices. The program is dormant when market prices are above intervention prices. It is activated when the overall milk supply exceeds demand, causing excess milk to be diverted into production of nonperishable products and lowering their prices to levels that make sales to the CCC more profitable than commercial sales. Until 2008, product intervention prices were linked to a price support level for manufacturing milk that was set by Congress. The current Dairy Product Price Support Program (DPPSP) sets product prices, but not in reference to a minimum milk price.

What are the issues?

- ***Ineffective price floor***. Using federal milk marketing order formulas, the current CCC purchase prices translate into Class III and Class IV milk prices of $9.00-$9.50 per hundredweight. This is well below the cost of producing milk given today's high input costs. Moreover, dairy price supports have not always been successful in maintaining established floor prices for milk or dairy products. Because of non-standard product, packaging, and payment specifications, it costs more to sell some products to the CCC than to commercial buyers. So market prices for these products, especially cheese, sometimes fall below intervention prices. This has led to a call by many dairy groups to raise the intervention prices to reflect the higher costs of selling to the CCC. Others have proposed that the milk price safety net be solidified by flooring the product prices used in federal milk marketing order pricing formulas at the intervention prices. Still others have proposed that the CCC place a standing bid on the Chicago Mercantile Exchange (CME) cash markets for cheese, butter and nonfat dry milk at the CCC purchase prices for these products.

- ***Incompatibility with world trade liberalization***. Dairy price supports have been a big contributor to the U.S. *aggregate measure of support* (AMS), which the World Trade Organization (WTO) uses to gauge trade-distorting domestic agricultural subsidies. The change in 2008 from supporting *milk* prices to supporting prices for *dairy products* should reduce the AMS attributable to the support program. Nevertheless, permitted AMS will very likely be reduced as part of ongoing WTO negotiations. Major changes in the DPPSP—or termination—may be necessary to conform to a new WTO agreement. The DPPSP has also been criticized for impeding growth in U.S. dairy exports. When low prices occur, U.S. dairy firms turn to the CCC and away from world markets. This tends to cast the United States as an unreliable supplier.

- ***Market price distortions***. Dairy price supports have affected milk utilization by setting a price floor for some products but not for others. The best example of this market distortion relates to nonfat dry milk, which is a source of dairy protein in many food applications. There is a large U.S. market for other dairy-based proteins, notably milk protein concentrate (MPC) and casein. Most MPC and all casein used in the U.S. come from imports. Because nonfat dry milk is purchased under the DPPSP, it is less risky and usually more profitable to produce nonfat dry milk than other forms of dairy proteins. Similarly, since the CCC purchases only cheddar cheese, more cheddar is likely produced at the expense of other cheese varieties, at least when cheese prices are low.