**Dairy Policy in the Context of the Farm Security and Rural Investment Act of 2002 (The 2002 Farm Act)**

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The subjects I will cover are:

- •The 2002 Act in general
- •Dairy Title (but left to Hal's presentation mostly)
- •Dairy Policy in Historical Context

**The Act in General**

1. The bill was politically popular from inception through completion:

   -- the main commodity groups and farm organizations were unified on major crop programs, beginning with their testimonies before the House Ag Committee

   -- the bill passed 280 to 141 in the House, 64 to 35 in the Senate

   -- the President signed with praise on May 13, 2002, Administration never opposed its main provisions (although some low-keyed disagreements were floated)

2. Yet there has been a steady chorus of criticism since passage

   -- national media castigated the bill; "Mother of all Pork," said the Washington Post

   -- many foreign governments are complaining that the U.S. preached free markets to other countries and then enacted big subsidies.

   -- economists have criticized the fall-back from market orientation that the 1996 Act suggested might ensue

3. Some details were contentious within the agricultural community, and dairy was one:

   --dairy policy, especially the Northeast Dairy Compact

   --scope of conservation programs

   --regulation of livestock contracts; ban on packer ownership (ultimately deleted from the Act)

4. Congressional Budget Office estimates cost to government, above current-law baseline, of $49.2 billion over the 6 years, and $80 billion for the ten years until FY2011.[1] Of that cost, $37.6 billion is for the Title 1 Commodity Programs, and $6.5 billion is for Conservation Programs. Most of the Commodity Program additions are for Counter-Cyclical Payments ($23.5 billion). See Table 1 for more detail.

**Table 1: CBO Projections for 2002 Farm Act New Outlays**

billion dollars

| Fiscal Year (Oct-Sept) | Title 1 | Title 2 | Other Titles | Total |
|---|---|---|---|---|
| 2002 | 1.0 | 0.4 | 0.3 | 1.6 |
| 2003 | 7.2 | 0.5 | 0.7 | 8.4 |
| 2004 | 8.0 | 0.9 | 0.9 | 9.9 |
| 2005 | 7.8 | 1.3 | 1.1 | 10.2 |
| 2006 | 7.2 | 1.7 | 1.1 | 9.9 |
| 2007 | 6.5 | 1.8 | 1.0 | 9.3 |
| 6 Years | 37.6 | 6.5 | 5.1 | 49.2 |

Details of Title 1 Costs

| | Direct Payments | Counter-Cyli-cal Payments | CCC Loan Programs | Dairy Program | Other |
|---|---|---|---|---|---|
| 2002 | 0.0 | 0.0 | 0.7 | 0.2 | 0.1 |
| 2003 | -0.1 | 4.6 | 1.0 | 0.4 | 1.3 |
| 2004 | 1.2 | 4.9 | 1.0 | 0.4 | 0.5 |
| 2005 | 1.2 | 4.9 | 0.7 | 0.3 | 0.7 |
| 2006 | 1.2 | 4.7 | 0.6 | 0.1 | 0.6 |
| 2007 | 1.2 | 4.4 | 0.4 | 0.1 | 0.4 |
| Total | 4.7 | 23.5 | 4.4 | 1.5 | 3.5 |

[1] Even though Act authorizes most programs for six years, the ten-year budget is important for scorekeeping with reference to overall Congressional spending limits. The bill was limited to $73.5 billion over the previous-law baseline. CBO's estimate of $80 billion is consistent with this because the $73.5 billion was defined with reference to an April 2001 baseline; the $80 billion was estimated with reference to a March 2002 baseline, when commodity price forecasts were lower, so costs of some program changes were higher. (Note also that both baselines were controversial in projecting Production Flexibility Payments into the 2003-2011 period, even though the 1996 Act ended them in 2002).

5. Developments since the Act's passage in May 2002: (a) higher prices as of early fall 2002 mean possibility of no CCPs for grains and soybeans in FY2003, (b) likely reduction in loan deficiency payments of about $4 billion, (c) likely addition of disaster payments of several billion dollars; (d) dairy program cost much higher, perhaps $1 billion + in FY 2003 instead of $0.4 billion in original CBO score.

6. Is the Act WTO compliant? This is important because Congress accepted the idea that WTO compliance is important, and included a provision mandating the Secretary of Agriculture to scale back programs if necessary to meet compliance.

> In the most probable (baseline) case, we would not breach WTO ceilings.
>
> The U.S. ceiling for "amber box" domestic support after 2000 is $19.1 annually. Baseline spending for commodity programs is above that level, but does not all count against the $19.1 billion. Some is in the "green box," notably direct payments. Some is excluded by "de minimis" provisions that exempt spending that is less than five percent of a commodity's value (for commodity-specific programs) or five percent of all agricultural commodities produced in a country (for programs not tied to a specific commodity). Countercyclical payments are expected to be declared non-commodity-specific, which means that with $190 billion in aggregate agricultural output, $9.5 billion will not count toward the ceiling. But dairy support was notified at $4.3 billion in 1998 and this will increase substantially in 2003.
>
> Despite current price increases due to drought-induced crop losses, in the out-years prices could even be lower than the CBO projection assumes (which is a slowly rising level as export markets pick up steam). The Food and Agricultural Policy Research Institute at the University of Missouri published an estimate that there is a 1 in 5 chance that prices will fall so low that the U.S. will breach WTO ceiling despite the green box and de minimis escape hatches.

**Dairy Title Highlights**:

-- End of Dairy Compacts
-- Milk Income Loss Program (Deficiency Payments)
-- Federal Orders Continue
-- Price Supports Continue at current levels
-- DEIP continues

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**Historical Evolution of Dairy Policy**:

Despite talk of how highly agriculture is protected in the 2002 Act, and despite new dairy program, both the support price for manufacturing milk and the markup between Class I milk and other milk under marketing orders has shrunk notably over time. The following figures tell the story both in terms of U.S. averages and price differences between selected states.

Figure 1 shows Class I price and the price of all other milk sold under federal marketing orders. The "all other" price was estimated by taking the blend price times the total quantity of milk under marketing orders, subtracting out Class I receipts, and dividing the remaining receipts by the quantity of milk in classes other than Class I.

Figure 2 shows the same Class I price but compares that to the average price received by farmers for all milk as estimated by USDA's National Agricultural Statistics Service.

Figure 3 shows NASS all-milk prices for several states.

All prices are deflated by the GDP deflator (1992=100) to put them in real terms.

**Figure 1. Real Price of Class I and All Other Milk, U.S. Marketing Orders**

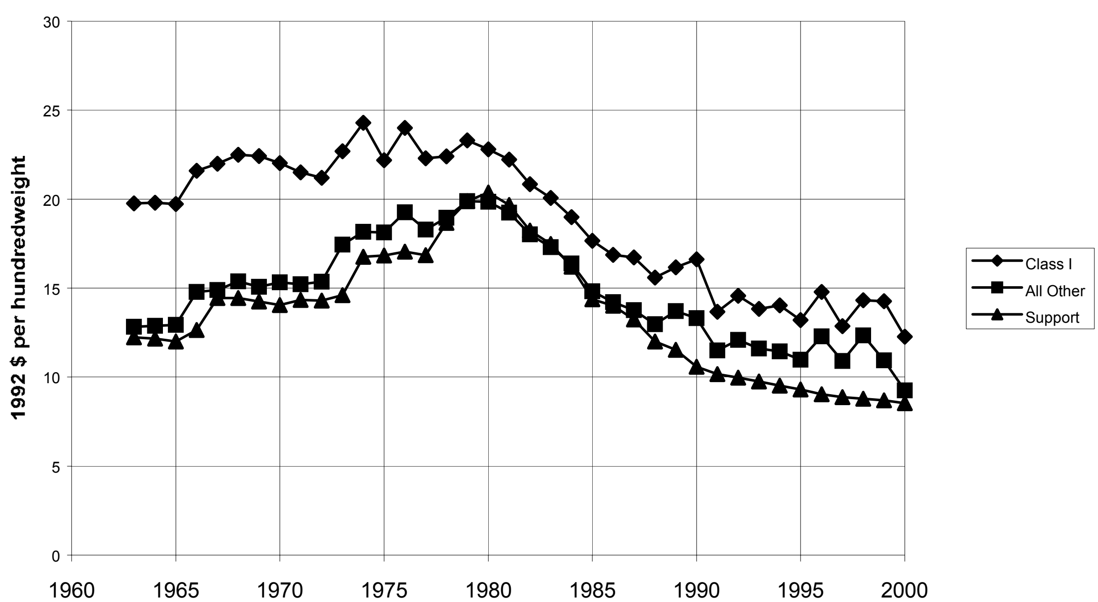

**Figure 2. Real Price of Class I and All Milk**

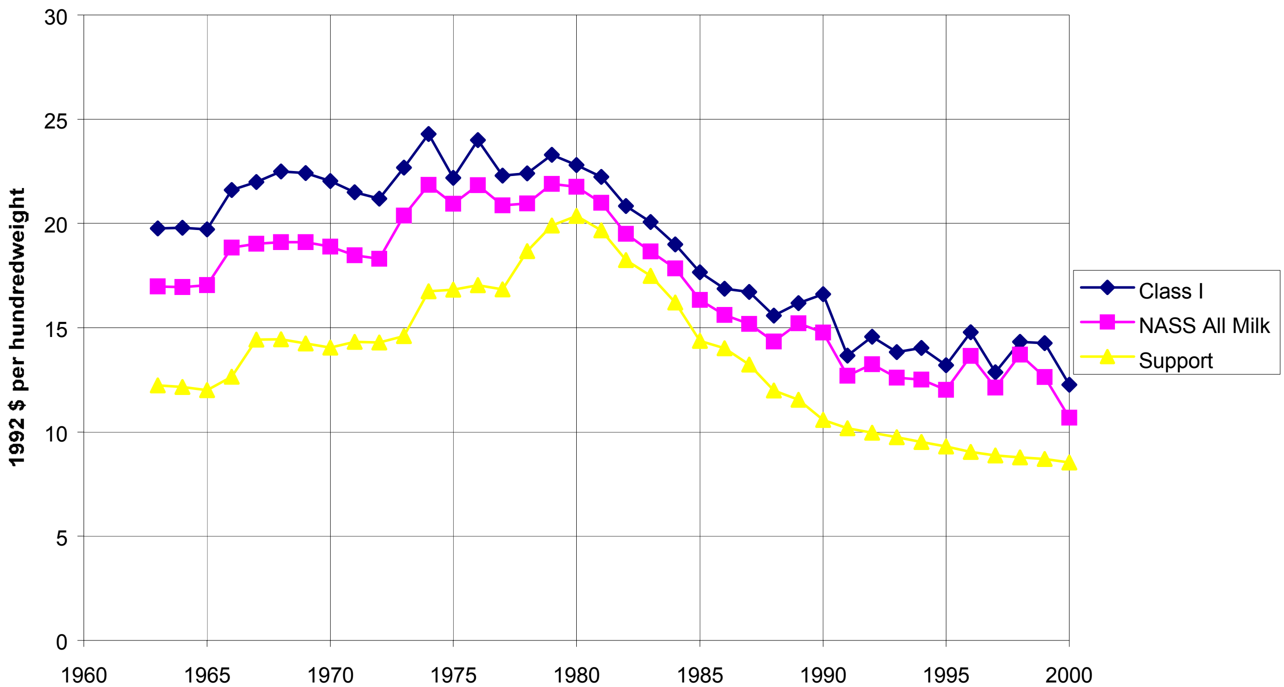


**Figure 3. State-Level NASS All-Milk Farm Price**