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Are Dairy Farmers Getting Their 15 Cents Worth?

by

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Since 1984, dairy farmers have been contributing 15 cents for each cwt. of milk they sell to fund state and national advertising to increase milk product consumption. The main reasons for this generic advertising program are to reduce government surpluses of dairy products and to raise farm prices. The funds available to state and national dairy promotion organizations from this assessment have averaged over \$200 million annually since 1984.

A relevant question to ask, given the large amount of money involved, is: are dairy farmers getting their 15 cents worth? I recently tried to answer this, as well as other questions, using a model developed to simulate quarterly farm prices from 1980 through 1987 with and without generic dairy advertising (prior to 1984, there was some advertising funded in some of the states). Here are some of the answers I found.

Does generic advertising reduce government purchases of surplus dairy products?

Compared with no advertising at all, the current program has reduced government purchases of dairy products under the price support program by 37 percent. Government purchases averaged 3 billion pounds of milk equivalent per quarter with advertising in the simulation, and 4.75 billion pounds without advertising. Hence, it appears that dairy farmers are taking an active role in reducing milk surpluses by funding the generic dairy promotion program. This is the main benefit of the program to taxpayers because government costs of dairy programs are lower with generic advertising.

Is generic dairy advertising effective in raising the prices farmers receive for their milk?

This simulation revealed that dairy producer prices nationwide would have been, on average, 14 percent lower during the 1980s had there not been a generic dairy promotion program. This is because these programs were responsible for increasing consumption by 7.5 percent compared with no advertising. Furthermore, the model results showed that fluid product advertising is significantly more effective than manufactured dairy product advertising in raising farm prices. The farm price was almost 13 percent higher with fluid-only advertising than no advertising, whereas it was not at all higher with manufactured product advertising.

Do the benefits of a higher price outweigh the cost of the 15 cents per cwt. assessment?

The results indicate that based on the current advertising expenditures, farmers receive \$1.60 back for each \$1.00 they invest in the program. This "marginal" benefit-to-cost ratio was calculated by dividing the additional revenue farmers receive for each \$1.00 that is invested in the program. From an economic standpoint, while farmers are benefiting from the current program, a marginal benefit-to-cost ratio that is greater than one implies that producers could profit even more by investing more on generic advertising.

How much more should be invested?

To find out, the model was re-simulated assuming incremental increases in the national advertising budget. The results indicated that the optimal level of funding is about 27 cents rather than 15 cents per cwt. The 27 cents per cwt. is the breakeven level between benefits and costs of the program.

This research was the first investigation of the generic dairy program conducted at the national level. The results showed that from a national viewpoint both dairy farmers and taxpayers benefited from the 15 cents that producers pay for advertising milk products. In addition, fluid advertising was found to be more effective in raising producer prices than was manufactured advertising.

It should be noted that not all researchers have produced identical results. The majority of other studies, which have been conducted mainly at local and regional levels, have concluded that generic advertising for milk has increased milk product consumption. Some of these studies, however, have also concluded that farmers would be better off spending less than the 15 cents on

advertising. Why the discrepancy between results? There are two reasons. First, there are differences among the models and data used by analysts so it is common to have diversity of results. Second, as already noted, previous studies have examined the effectiveness of regional programs, e.g., New York City fluid program, whereas this study looked at the overall effectiveness of fluid and manufactured products at the national level. It is entirely possible that there is over-investment in, say, New York City, but under-investment in other areas. Yet, the difference in results between this study and other research should be viewed with caution. That is, there is still not enough research on the subject to form conclusive evidence as to whether farmers are spending too much, too little, or just the right level for generic advertising of milk products.