AGRICULTURAL EXPERIMENT STATION
Oregon State College
Wm. A. Schoenfeld, Director
Corvallis

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CONSIDERATIONS RELATING TO STATE AND FEDERAL REGULATION OF FLUID MILK PRICES IN OREGON

by

D. B. DeLoach
Agricultural Economist

Introduction

Experiments in regulating minimum fluid milk prices have been carried on for ten years by the Federal and state governments through various laws administered by boards, commissions or bureaus. The United States Department of Agriculture has been active since 1934 in controlling producer prices in the principal milk markets by means of producer-dealer marketing agreements with the Secretary of Agriculture. These Federal agreements usually regulated the market supply in a manner to prevent market surpluses and a resulting decrease in prices to producers. None of these agreements was operative in Oregon.

Several states passed laws patterned after the Federal legislation which granted producers the right to organize and regulate the flow of milk to market. Other laws, such as the Oregon Milk Control Act of 1933, created a milk board to determine a minimum price for the product. The Oregon Milk Control Board was authorized within certain limits to take the actions necessary to maintain an established legal minimum price on fluid milk. The Oregon legislature abolished the Milk Board in 1943 and transferred its functions to the Director of the State Department of Agriculture.

The problem of maintaining minimum prices on fluid milk came to an end in 1941. Since that time governmental agencies, at the behest of consumer groups, have concerned themselves with the problem of preventing abnormal increases in the price of the product. The Office of Price Administration, by order of the President of the United States, was vested with power to control the upper limit of prices. The Price Administrator established ceiling prices on fluid milk on April 28, 1942. After more than a year of operation this Federal agency finds itself unable to meet satisfactorily the demands made on it to stabilize prices and at the same time maintain the output of producers. This failure of the Office of Price Administration to satisfactorily regulate milk prices is due in no small way to administrative inexperience, but the condition can be attributed mainly to the operation of inflationary forces outside the control of the Office of Price Administration.

Government control of the ceiling prices on milk is not to the immediate benefit of producers. Maximum price controls, however, are to the distinct advantage of consumers. Even though the purpose of governmental price regulation has changed as a result of war demands on our economy, many of the problems of administering price regulations remain unchanged. It seems therefore that a review of Federal and state experience in attempting to control fluid milk prices should furnish a basis for a better understanding of our war-time problem.

Maximum Prices Introduced

World War II brought rapid changes in the conditions of producing and marketing farm products. Former food surpluses were eliminated in a short time. The impetus given to consumer demand by rising wages and the greater employment of workers caused prices to rise. Under these conditions laws regulating minimum prices had become unnecessary. The problem of price control became one of regulating maximum prices, not minimum prices. And of greater importance still was the task of fairly apportioning the available food supplies among those who needed them.

Recognizing the existence of an increased demand and anticipating a further increase, food dealers began to bid for available supplies. Buyer psychology was such that these merchants could easily pass along to the consumer almost any price increase without measurably affecting demand. In fact, consumers in many cities had reached the point where they were bidding against one another for the food products offered for sale.

Without entering into a detailed explanation of the many factors causing the rapid increase in consumer demand for goods and services, sufficient evidence is available to show that an abnormal demand situation was arising. Prices were getting out of control to a point where the war efforts of the nation would have been seriously handicapped unless some restraints were instituted. It was under these conditions that the President, by an executive order, created the Office of Price Administration to exercise certain controls over the price of goods and services offered for sale in order to stop the rise in living costs. One of the first important actions of this new agency was to institute an order establishing the maximum prices on many food products, services, and rents. The General Maximum Price Regulation order of April 28, 1942, together with the several amendments thereto, forms the basis for many of the problems affecting Oregon agriculture.

Fluid Milk Price Control in Oregon

Oregon milk prices controlled by state since 1934. The maximum resale price regulations on fluid milk introduced by the Office of Price Administration are the second type of governmental economic controls placed on the Oregon fluid milk industry since 1934. The present attempt of the Federal Government to regulate maximum prices follows the efforts of the Oregon Milk Control Board to maintain minimum prices from 1934 to date. (Administration of Oregon law was transferred to the Director of Agriculture in June 1943.)

Milk Board fixed legal minimum prices. State economic control of the Oregon fluid milk industry between 1934 and 1942 was primarily to maintain legal minimum prices for which dealers could buy milk from the producers and sell the pasteurized product in wholesale and retail trade channels. Producers who marketed their own product were placed under similar restrictions. The Oregon Milk Control Board attempted to administer the Milk Control Act in a manner to maintain legal minimum prices by placing arbitrary restrictions on the amount of milk that could be sold in Oregon markets. The economic restrictions on supply were assumed to be justified on the basis that they were needed to stabilize the fluid milk market. It was assumed that stability in the industry was essential to assure the continuance of the delivery to market of an ample supply of milk of an approved sanitary quality.

Adjustments in industry resulting from war are rapid. The problem of maintaining minimum prices changed quickly during the spring of 1942 as market surpluses disappeared. Competition for the supply of milk increased rapidly as a result of increases in consumer and government purchases of fresh milk, and the higher prices being paid for manufacturing milk. Under these conditions the Milk Control Board began to establish minimum prices to producers sufficiently high to prevent existing producers of fluid milk from turning to factory outlets to sell their product. Adjustments were also made in Board rulings to permit new producers to enter the fluid milk market more easily than had been possible before this time. In spite of these actions by the Board to maintain supplies, consumer demand remained sufficiently strong at prevailing prices to absorb most of the available supplies. This condition favored the producers' bargaining position considerably, thereby resulting in persistent pressure for higher producer prices.

Two factors appear important with respect to this demand condition; namely, milk meeting the official minimum sanitary requirements could be sold to government agencies outside the usual sales area, and the rising incomes of industrial workers made it possible for them to purchase greater amounts of fresh milk for home use.

While the demand for fresh milk rose rapidly there was not a corresponding increase in the quantity of milk of officially acceptable sanitary quality delivered to the metropolitan markets. This condition is not surprising to those familiar with the Oregon fluid milk industry. New industries were opening up to offer good wages and steady employment to part-time farmers. Farm labor was demanding higher wages, and feed costs were increasing rapidly from the depressed prices that prevailed between 1933 and 1941. Finally, it became increasingly difficult for producers of factory milk who desired to change to fluid milk production to obtain the necessary labor and materials to equip their plants to meet the fluid milk sanitary demands of the municipal or state authorities, even had these producers been willing to make such investment to obtain the higher prices offered fluid milk producers. It is doubtful if any one of these developments would have been of sufficient importance to the producers to cause a noticeable unwillingness to increase production and deliveries of milk to market. The combination of conditions was enough to change supply conditions radically.

Competition for milk supplies improves producers' bargaining power. By August 1942 it was evident that a sufficient number of governmental and civilian markets outside Portland were open to Portland quota holders to enable them to divert a substantial part of their supplies of milk from the city unless price increases were granted. Further shifts of officially acceptable milk to other markets would have left the Portland supply much below its requirements unless new producers could be qualified on a sanitary basis and granted quotas or unless the sanitary regulations of the city could be changed to permit supplies of manufacturing milk to be sold in the fresh milk channels.

The Board was face to face with the fact that the Portland market could be arbitrarily left short of milk by quota holders diverting their product to new markets in Washington and to new Army posts in Oregon unless their requests for price increases could be met. The Board was handicapped in obtaining new producers by its ruling preventing milk from being brought into market by new producers whose place of business was more than 30 miles from the city, and by the fact that no new producers had been granted quota in the Portland market for a number of years. The latter situation had caused many producers to hesitate in applying for quota under new market conditions because they had been discouraged from even making application in the past.

Portland lowers sanitary standard to admit "C" grade milk.1/ The only alternative for certain city markets was to permit milk produced under lower sanitary standards to be sold in fresh milk channels. The City of Portland did adopt a change in its ordinance to permit sale of "C" grade milk for human use provided it is satisfactorily pasteurized. This action of the City of Portland made eligible for sale in the city a supply of milk previously excluded on the basis that it was dangerous to public health. The change in sanitary requirements altered the entire fluid milk supply picture for the principal market in Oregon.

None of the producers willing to supply "C" grade milk for the Portland market held a quota in the city market. Opposition to granting quotas to these producers arose immediately from existing "A" and "B" grade quota holders who objected to additional supplies being made available to Portland consumers, even though the milk had met all new requirements of the City Health Bureau. Up to March 1943 no market quotas have been issued to "C" grade shippers. In spite of this fact several thousands of pounds of "C" grade milk are being delivered daily to pasteurizing plants in the city.

Fluid Milk Price Control Taken Over by Federal Government

Maximum prices established by Office of Price Administration. On April 28, 1942, the Office of Price Administration issued its General Maximum Price Order establishing the maximum wholesale and retail prices on milk at the highest level existing in March 1942. The effects of the maximum price order were felt immediately. The minimum prices established by the Oregon Milk Control Board became the highest legal prices that could be charged for milk in wholesale and retail trade channels under the ceiling price order. Milk Board regulations protecting dealers from price cutting had become unnecessary. The Board's power to establish minimum prices at which dealers could buy milk from producers continued to be of real importance, however. Prices paid to producers for milk were not frozen. In view of the fact that no upper limit was placed on the price to producers, the Oregon Milk Control Board could establish a minimum butterfat buying price for dealers above the level prevailing in March. Such an action would reduce the dealer's spread on milk handled, because the dealer could not pass the increase on to the consumer. In several areas the Board took just such an action. The butterfat price at which dealers purchased milk from producers was increased from 80 to 87 cents per pound in Portland; from 75 to 81 cents in Salem; and from 67 to 75 cents in Medford. Other markets were also affected by Board action in raising the dealer's butterfat buying price. It must be recognized that in taking such actions the Board arbitrarily reduced the percentage spread granted to dealers for their services at a

1/ The Portland "Standard Milk Ordinance" defines "C" grade milk as "raw milk which violates any or all of the requirements for grade B raw milk." Such a definition implies that practically all milk produced in Oregon is eligible for sale in Portland on a sanitary basis. All milk must meet the requirements of the Oregon Pure Food and Drug Act from the standpoint of purity and cleanliness.

time when operating costs due to labor and materials were increasing. On the other hand, dealers were allowed to introduce economies in service to partly offset the reduction in spread on each unit of product.

Part of program to control inflation. The primary objective of the OPA's maximum price order was to stabilize the cost of living by fixing the upper limit of prices below the level that would prevail if the market prices were left uncontrolled. The effect of the ceiling price on the supply and demand for a particular commodity was of secondary importance. Complications arose immediately as a result of the Government's action to exercise control over prices without placing some restrictions on consumer demand.

Existing market prices adopted as ceiling prices. Most of the opposition that arose against the new milk price ceilings was in anticipation of injury rather than any actual injury caused immediately by the operation of the maximum price order. Prevailing milk prices at the time of the ceiling order were the legal minimum prices fixed by the Oregon Milk Control Board, and no particular pressure had been exerted on the Board by the producers and dealers in the several markets to have the legal minimum prices raised. Admittedly there were a few exceptions, especially in those areas adjoining the newly established military posts. Even in most of the areas where pressure was being exerted on the Board to raise the legal minimum price, the industry had refused to take the risk of increasing prices above the legal minimum because of the fear of price cutting. In view of the conditions existing in the milk markets of Oregon in April 1942, it is doubtful whether any serious inequities resulted immediately from the establishment of the ceiling prices on milk at the March price level.

Changes in industry following issuance of ceiling price order cause injustices. Inequities soon arose in the course of the operation of the maximum price order. They developed from an attempt on the part of the government to regulate fluid milk prices without regulating the factors that controlled the production and consumption of this product. Labor, feed, consumer demand, and even government demand were undergoing a rapid change. At the time the order was instituted, labor costs were rising, but not out of proportion to others; feed was adequate and relatively low in price; and war industries and the military services had not yet begun to make any serious inroads into the supply of dairy farm labor. Important changes occurred in this comparatively favorable situation within a period of four months after the price ceiling order was issued. Since neither wages nor feed prices were controlled, these costs rose rapidly in response to competitive bidding for available supplies.

The high wages offered by war industries caused many hired workers to leave the dairy farms for higher wages and shorter working hours. In addition, the selective service boards began calling young men who were employed on dairy farms as hired workers or as joint operators of a family-sized dairy herd. A scarcity of labor began to assume a greater importance than the rising level of farm wages.

The Oregon carryover of hay feed from the 1941 hay crop was one of the smallest on record, and the 1942 hay feed crop was no better than average. As a result what would have been a fairly adequate supply of feed vanished rapidly due to heavier demands. By November 1942 a shortage of hay existed in most parts of Western Oregon. Inasmuch as feed prices were not controlled they rose at an exceptionally rapid rate.

Payrolls rose rapidly in the war industries in the Portland area after July 1942. Population increased as a result of the movement of workers and their families from rural communities to the industrial center, and due to influx of workers from other states. The rising money income of the employed workers and the increased number of consumers created a new demand for milk and milk products. The Portland sales of fresh milk in December 1942 were approximately 30 percent more than the sales for the corresponding period in 1941. Higher increases in consumption than those given for Portland are reported in several smaller cities in Oregon.

Government-guaranteed prices on condensed milk, cheese, and dried skim milk enabled manufacturing concerns to pay a price for manufacturing milk equal to, if not higher than, the price paid to producers of milk for the fresh milk trade. These competitive government buying prices on cheese, condensed milk, and dried skim milk were increased considerably after the Office of Price Administration issued its original maximum price order in April 1942. Government competition, therefore, caused the price of milk for factory use to rise abnormally. It became increasingly difficult to maintain the necessary supplies of Grade A fresh milk for pasteurization in the usual markets under the established ceilings. Producers who cared to, and were able to qualify to supply milk for the fresh milk trade, were usually designated as producers for military posts. This type of outlet appealed to the producers because of the higher prices paid for milk used for the military establishments.

Federal Government fails to coordinate program. The Federal Government failed to coordinate its program relating to purchasing agricultural commodities for war purposes and to regulating prices and consumption. The lack of a well-defined policy assured the Office of Price Administration a fair share of trouble in maintaining its price ceilings on milk. It was forced, therefore, to begin immediately to consider upward revisions in milk price ceilings to meet pressures caused by changing conditions of supply and demand.

Producers lead opposition to price ceilings on milk. The campaign to raise the wholesale and retail ceiling prices was led mainly by producer groups. The purpose of producers in campaigning for an increase in distributors' wholesale and retail milk ceiling prices was to enable the Milk Board to increase the minimum consumer prices. This action would permit an increase in the minimum price distributors could pay producers for their milk without reducing the spread allowed these dealers under the original ceiling price order. The only alternative was to induce the Milk Board to increase the minimum distributor buying price without regard to retail price maximums set by the Office of Price Administration. Such an action would narrow the dealer's spread to the extent of price increase to producers. It appears that producers recognized that the Board could not go much further in increasing their price under existing wholesale and retail ceilings without causing a serious upset in methods of distributing fluid milk. Under these conditions the producers began to advocate an increase in ceiling prices.

While the Milk Board minimum price orders did not prevent dealers from paying prices to producers higher than the Board's legal minimum, several dealer-producer contracts had been signed in which the legal minimum price was established as the contract price. In one market a large producer organization entered into certain exclusive supply contracts with its dealers whereby the producers accepted the Board's minimum price as the supply price for a stipulated period. The dealers agreed to pay the Board's minimum price for milk for a stipulated period in the event of the repeal of the Oregon Milk Control Law.

Power to Make Adjustments in Ceilings Vested in Regional Office of Price Administration

Authority to alter milk ceiling prices was originally vested in the Washington, D. C., Office of Price Administration. Subsequent action by the Administrator delegated this authority to adjust milk ceiling prices to the regional offices. The San Francisco Regional Office acted under general instructions from the Administrator relating to milk price ceiling adjustments when it issued certain changes in the several milk markets in Oregon. The authority permits the Regional Office to make changes in price ceilings where it can be shown that (1) competition between fluid milk markets is such that a higher ceiling price in one milk market would cause an abnormal movement of supplies to that market from milksheds where lower ceiling prices prevail, or (2) the ceiling prices established by the original order caused injustices as a result of abnormal conditions existing at the time the order was issued. It can be seen that the foregoing regulations do not permit upward price adjustments to allow for increased production and distribution costs following the issuance of the original order, nor do they permit higher ceiling prices to encourage production or maintain production at existing levels.

Milk ceiling prices raised in Oregon. Between November 8, 1942, and January 18, 1943, the San Francisco Regional Office of Price Administration granted increases in the wholesale and retail milk price ceilings ranging from one-half of one cent to two cents per quart in most sections of Oregon outside the Portland sales area. The revised order granted a further increase in price in most sections of the state by permitting dealers to lower the butterfat content of their milk to 3.8 percent from the previous levels ranging as high as 4.5 percent butterfat. This permissive reduction in the butterfat content of milk amounts to an increase in the price ceiling, because milk is bought from producers on the basis of the butterfat it contains.

Industry demands further adjustments in price ceilings. The increases in the wholesale and retail ceiling prices of fluid milk failed to meet the demands of the milk industry. Strikes were threatened by producers but none occurred. To relieve the constant pressure from producers for further price increases the Regional Office of Price Administration encouraged the sale of milk with a fat content below the 3.8 percent basis established in its official order of January 15, 1943, adjusting the prices in the state. In most sections of the state this action of the Office of Price Administration permits dealers to lower the butterfat content of the product from a level ranging as high as 4.5 percent to a minimum for milk of 3.2 percent as established by the Oregon State Department of Agriculture. By lowering the butterfat content of the milk contained in the consumer-sized container the distributors could afford to pay producers a higher price for their product. The soundness of the foregoing method of raising prices is open to serious question. From a public standpoint it is neither a means of forestalling price increases nor an honest method of dealing with the public.

Maximum price to producers established. Organized producer pressure for milk price increases began in earnest following the fairly general upward revision in Oregon in January. The producers' program was to request increases in consumer prices sufficient to permit distributors to buy their milk at a price ranging from $1.00 to $1.10 per pound butterfat. Many milk distributors who were buying raw milk for pasteurization and sale were fearful of the public reaction in case of further price increases, even though they were fretting under the squeeze resulting from the Milk Board raising prices to producers while the dealers' selling prices were frozen by the Federal Government. Dealers, therefore, began to press harder for the Office of Price Administration to establish ceiling prices on raw milk bought by dealers. Temporary producer maximum prices were set for a period of sixty days by the Office of Price Administration on February 15, 1943, at the highest price paid to the producer during January 1943. The control agency anticipated that adjustments of temporary ceilings will be necessary in several localities. Necessary adjustments have been held up, however, as a result of the President's price "freezing" order of April 8, 1943.

Maximum price established on alfalfa hay. Alfalfa hay prices were placed under control at the same time producer milk price ceilings were fixed. This action has not had much bearing on production costs for the 1942-1943 crop year because most of the marketable hay out of the 1942 crop has been sold and the hay feeding season for 1942-1943 is gradually coming to an end.

Other Factors That Will Affect Supplies of Fluid Milk

Labor. The wages paid to workers remain uncontrolled. Competition of war industries for the available supply of farm labor remains severe despite the several half-hearted measures that have been taken to correct the situation. Wages paid to dairy farm workers are rising rapidly. Inasmuch as labor costs constitute approximately 30 percent of the cost of producing milk in Oregon in normal times, it is evident that production costs cannot be kept down with labor costs continually rising. A factor of further importance in the problem of the unit labor cost of producing milk is the decrease in the relative efficiency of labor available for farm work.

Sanitary standards. The gradual relaxation of sanitary standards for milk officially accepted for sale in fresh milk channels is apparent. The official acceptance of "C" grade milk by Portland for sale to the fresh milk trade is having a material effect on the fresh milk supply in that city. Inasmuch as the milk produced under lower and less expensive sanitary standards is being purchased at the same price as fluid milk produced under more stringent and more costly sanitary requirements, there is no reason to believe that producers will continue to pay the cost of maintaining an "A" or "B" grade production dairy as long as there is no premium paid for the product. In fact, the present pricing program makes it difficult to enforce existing sanitary regulations among "A" and "B" grade producers.

Changes in the legal sanitary standards under which fluid milk must be produced to be eligible for sale can have a very material bearing on the total supply of the product in any market. At the present time the shortage of labor and materials makes it almost impossible for a producer of "C" grade milk to make the changes in his plant that would be necessary to qualify as an "A" or "B" grade producer. For all practical purposes the number of "A" and "B" producers cannot be increased under existing conditions. It therefore appears that the only easy way to quickly increase the supply of fluid milk for market is to admit "C" grade milk whenever it is needed.

The effects from the use of milk of a given sanitary quality on public health is not within the scope of this study. It is necessary, however, to indicate the influence of changes in sanitary regulations on milk supplies and the cost of production. The maintenance of price uniformity in any market depends to a great extent on the degree of quality uniformity. If milk sanitary standards can be made to fluctuate widely in order to meet a given consumer demand condition of price situation, a question might be raised as to whether sanitary regulations have been used to protect public health or to control the number of milk producers in the market.

Summary

The Office of Price Administration placed ceilings on fluid milk prices on April 28, 1942. Under the ceiling price order the highest March price charged by each wholesaler and retailer for milk became the legal maximum price for those dealers. Since the amount dealers can afford to pay producers for their milk is directly dependent on the individual dealer's resale prices, producer groups became immediately interested in the price ceilings established at wholesale and retail trade levels.

Efforts of milk producers to obtain higher prices from distributors were refused because of the ceiling price order which would not permit higher dealer buying prices without materially reducing dealer spreads. Despite this limitation certain minor increases were granted, but these adjustments did not satisfy the producer groups. By the force of circumstances the principal opposition to the new price ceilings arose from the producers. This group attempted to show that existing dealer resale price ceiling would not permit the dealers to buy milk from producers at a price that would return cost of production. Claims were made also that production would drop and a shortage of milk would occur in the principal Oregon markets unless the ceiling were changed. This investigation disclosed these facts relative to the operation of the industry under ceiling price orders between April 28, 1943 and May 15, 1943:

1. Ample supplies of fluid milk have continued to be available to Oregon consumers although the City of Portland found it necessary to revise its milk code in order to admit milk formerly excluded from that market on the basis of the city's sanitary regulations.

2. The Office of Price Administration granted wholesale and retail price ceiling increases to most markets in Oregon outside the Portland sales area in January 1943.

3. The price increases granted by the Office of Price Administration ranged from 1/2 cent to 2 cents a quart.

4. The office of Price Administration official price order permitted unit prices on milk containing a minimum of 3.8 percent butterfat. In many areas this allowed dealers to reduce the fat content of their product from levels ranging as high as 4.5 percent. This was equivalent to a 15.6 percent increase in price in addition to the allowable monetary increase on the quart unit of product or a total increase in some cases of 35.6 percent.

5. Since the date of the January ceiling price adjustment Office of Price Administration officials have publicly encouraged a reduction in the butterfat content of milk below the requirements of their official order. This action constitutes a permissive lowering of the butterfat content in milk offered to the consumer and a resulting increase in price to dealers.

6. Temporary ceilings were established on the prices distributors could pay for milk bought from producers. This order became effective February 9, 1943.

7. The sanitary standards that must be maintained by the producers of fluid milk have been lowered materially since the summer of 1942. Practically all milk produced in Oregon now meets the sanitary requirements for sale in the Portland market. For all practical purposes a similar condition exists in most other parts of the state.

8. If production costs continue to rise it is doubtful whether producers will continue to maintain their present sanitary standards as long as fluid milk ceilings are the same regardless of sanitary quality.