

Modernizing Milk Supply Management: An Independent View



GEORGE MORRIS CENTRE

MAKE INFORMED DECISIONS

**Al Mussell
Senior Research Associate**

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1. Introduction

Milk supply management has attempted to manage a balance between the producer interests in controlling surpluses and supporting milk prices, and the operating needs of processors. This has always been a difficult challenge as marketing regulations replace many of the balancing and adjustment functions of a market, in an environment ridden with the uncertainties of weather, animal biology, international trade, and many other factors. Milk supply management has evolved, through many difficulties, to create an environment in which dairy farms and dairy processors can be profitable. However, new and past challenges continue to pressure the system at an accelerating rate, leading to very active discussions on “modernizing” milk supply management.

Significant changes have occurred in milk supply management over the years that have allowed for adjustment, some resulting from skirmishes over specific issues, with most being driven by dairy farmers. To a large extent these reflect the desire for more of a national regulatory framework for milk supply management over the fundamental provincial basis for the system. It remains, however, that there are many changes that have occurred in the marketplace that are placing pressure on milk supply management as never before. Many of these are well understood, and have been enunciated in the dairy industry under reform initiatives such as the Dairy Industry Producer-Processor Dialogue (DIPPD) and the producer Ingredient Strategy.

These changes include the following:

- The system is buffeted by new dairy protein products that substitute for traditional dairy ingredients, most of which is imported at zero or minimal tariff
- The price point of milk protein concentrates (MPC’s) and milk protein isolates (MPI’s) pressures pricing of solids-not-fat (SNF) in Canadian milk
- The structural surplus of skim milk powder (SMP) has (once again) grown to burdensome levels that are expensive to finance, in large part due to imports of MPC’s and MPI’s
- Canada is limited in its access to the export market in consideration of its sales of the structural surplus, as well as for dairy products more broadly. This appears to effectively cut off exports as a means of industry growth.
- Import threats are increasing, with new Canadian market access for cheese granted to the EU under CETA, and prospects of further access for imports under TPP.

Thus, the industry focus for reform of dairy policy and milk supply management has been to contemplate changes in the rules governing the milk supply management system that can address these issues. This has been pursued in the work of industry technical committees to arrive at changes in the instruments that operate supply management. It has yielded proposals, still in development, that demonstrate both commitment to the system, and ambition in terms of potentially far-reaching changes to its mechanics that will allow for improved adjustment and opportunity.

At the same time, while these efforts are focused and have urgency attached to them, it is unclear that these proposed changes reflect the full depth, gravity, and rate of change gripping the

Canadian dairy industry. This is a critical issue when changes to some of the fundamental precepts of milk supply management are being contemplated.

The purpose of this paper is to provide a survey of some of the broader issues influencing milk supply management and Canadian dairy policy, the challenges in having these broadly addressed, and some direction for bolder, more sustainable policy direction.

2. Purpose, Intents and Interests of Parties to Canadian Dairy Policy

Milk supply management has had producers as its focus, with a requirement that consumers have satisfactory access to quality dairy products. For example, the objects of the Canadian Dairy Commission are stated as

..to provide efficient producers of milk and cream with the opportunity of obtaining a fair return for their labour and investment and to provide consumers of dairy products with a continuous and adequate supply of dairy products of high quality.¹

With this acknowledged, the nature and interests of producers in relation to milk supply management has changed over time. Other interests are more evident today than in the system's formative years. This section provides an overview of these.

2.1 Producers

At the time that the legislation establishing the Canadian Dairy Commission and most provincial milk marketing boards were established, dairy farmers in many parts of the country had suffered through a prolonged period of economic hardship, as described by Mussell *et al* (2012). The apparent interests of producers in developing dairy policy at the time were the following:

- Control milk and dairy product surpluses
- Increase farm milk prices to provide returns to cover costs of production
- Provide for greater equity in returns among dairy farmers

The policy instruments that developed in the 1960's and early 1970's were consistent with these interests. Mussell *et al* provide a detailed description of these, but in general:

- Provinces conducted reviews of milk marketing, and consolidated fragmented producer representation into single entities, eventually establishing producer groups with marketing board powers to represent and market milk on behalf of farmers
- Federal subsidies under the Agricultural Stabilization Act were capped and Subsidy Eligibility Quotas (SEQ) were issued to producers. Small producers were given an industry exit payment in lieu of SEQ
- Federal-provincial agreements on market sharing of industrial milk were signed, leading to Market Share Quotas (MSQ) as the successor to SEQ
- The Canadian Dairy Commission took over butter and SMP purchases that had occurred under the Agricultural Products Board as a means to support industrial milk prices. These were linked to an industrial milk cost of product formula established in the mid-1970's.

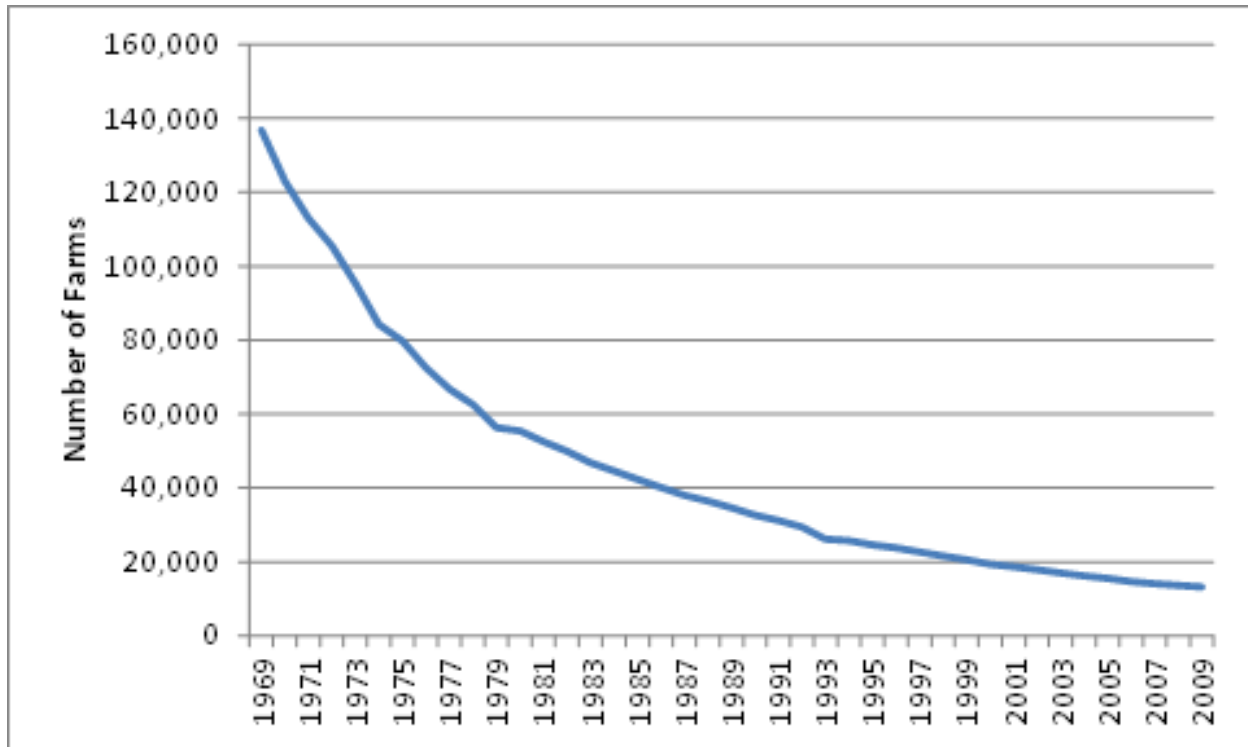
¹ Canadian Dairy Commission Act <http://laws-lois.justice.gc.ca/eng/acts/c-15/>

There was a diversity of interests among producers and provinces at this time- some provinces had multiple organizations representing segments of dairy farmers, some had a strong allegiance to cooperatives (notably Quebec). Some producers were heavily involved in marketing dairy cattle genetics with their milk marketing focused around breeds. Farmers located close to large cities had better access to fluid milk markets and better returns; others lacked this access and had less favorable returns. However, dairy farmers at this time were ultimately mobilized and eventually united by the general economic malaise gripping the producer segment of the industry.

Measuring producer attitudes and interests in dairy policy today can only be anecdotal and somewhat speculative. However there are some apparent differences between the situation framing attitudes forty years ago and today:

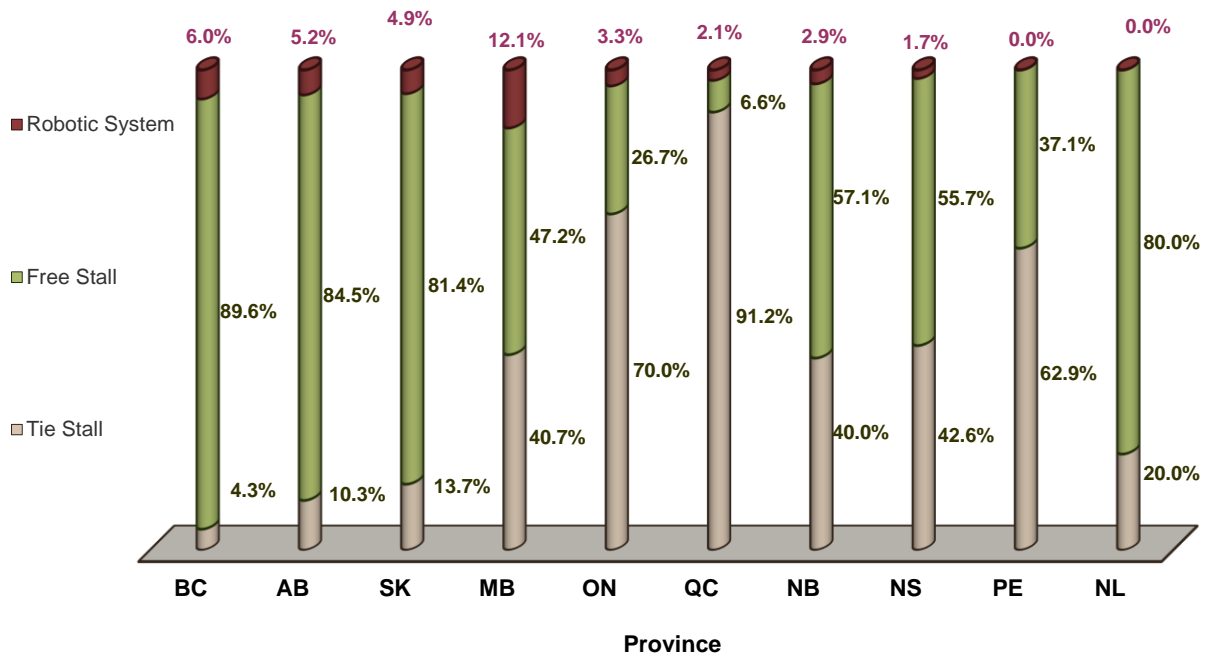
- There are far fewer dairy farms in Canada today compared with the 1960's/early 1970's, as shown in Figure 2.1 below. Over time, many of those with the interests described above have moved on. Where dairy policy might readily have translated into rural economic policy in some areas due to the sheer number of dairy farms, this is greatly reduced today
- Dairy farmers today, broadly speaking, are in a very different economic situation today compared with 1960's/early 1970's, in large part due to the disciplines and effects of milk supply management. There is little market-driven variation in dairy enterprise costs and returns, and broadly positive earnings
- While technological improvements in dairy farming are probably not changing as rapidly today as they were in the late 1960's, there are sharp discrepancies across farms. Perhaps the most fundamental is tie-stall housing vs. free-stall housing, as illustrated in Figure 2.2 below. Free-stall housing is almost universally chosen for the design of new dairy barn structures, and free-stall facilities have known economies of scale and are better suited to expansion over time. In some regions (notably Ontario and Quebec), tie-stall facilities still predominate, while free-stalls dominate in the West.
- The stability of positive earnings in dairy farming has been manifest to increasing dairy farm asset values. As such, many dairy farmers have a much improved personal/family wealth status than would have been the case forty years ago. The data in Figure 2.3 below illustrate the growth in per farm and aggregate dairy farm asset values since 2005.
- The increase in dairy asset values may have essentially caught up with the positive earnings stream; in other words, dairy asset values may be approaching full capitalization. Some evidence of this is presented below in Table 2.1, which gives the ratio of farm operating returns to the market value of assets across farm types, based on the public database. It suggests that dairy farm returns compared with asset values are comparable with other farm types. One interpretation of this is that there must be a strong demand on behalf of dairy farmers to retain a positive earnings stream in order to retain this level of return on investment into the future.
- The combination of slow growth in dairy markets, high quota prices, and restrictions on quota transfers and exchanges in eastern Canada have created what amounts to barriers to entry among both prospective and existing producers. The costs and access to sufficient production quota to establish viable scale dairy farms is an ongoing difficulty

Figure 2.1 Dairy Farms in Canada



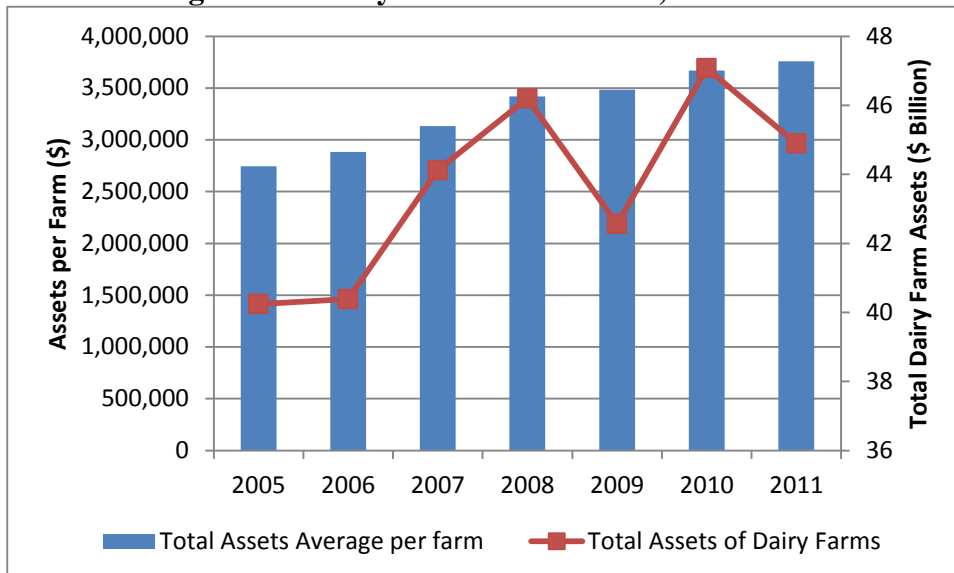
Source: Statistics Canada

Figure 2.2
Proportion of Dairy Barns by Type



Source: Herds on milk recording, Canwest DHI, Valacta. 2012 data

Figure 2.3 Dairy Farm Asset Values, 2005-2011



Source: Statistics Canada Cansim

Table 2.1 Farm Operating Income/Assets, Canada, 2005-2010

	2005	2006	2007	2008	2009	2010
	Land-Based					
Field Crops	0.02	0.02	0.03	0.04	0.04	0.03
Cattle <\$1 Million	0.02	0.02	0.02	0.02	0.02	0.02
Horticultural	0.04	0.04	0.04	0.04	0.04	0.05
	Margin-Based					
Cattle >\$1 Million	0.01	0.01	0.04	0.04	0.03	0.01
Hogs >\$1 Million	0.05	0.03	0.04	0.02	0.02	0.04
	Supply-Managed					
Dairy	0.03	0.03	0.03	0.03	0.03	0.04
Poultry and Eggs	0.04	0.03	0.03	0.03	0.03	0.03

Source: Statistics Canada FFS and TDP data, unaudited. Assets at market value

for the latent group of new dairy farmers. For many existing dairy farmers attempting to bring the next generation of family into the farm business, or improve the utilization of existing capital (especially in freestall barns), expansion has been difficult. For these existing or aspiring dairy farmers, these issues are immediate and strongly held concerns

- For another subset of farmers, perhaps a majority in some provinces, these issues are not of great concern. Market growth is not an immediate concern, and expansions are not easily accommodated (especially in tie-stall barns). Industry growth that is accompanied by risks to core elements of the milk supply management system are not encouraged, or welcomed by this group.

2.2 Processors

Processors are deeply impacted by milk supply management, but in practice have had little role in shaping the system. As far back as 1981, Barichello noted that "... a representative of the National Dairy Council sits as an ex-officio member of the Canadian Milk Supply Management Committee. However, the role of these organizations is more one of reacting to policy than of proposing, creating, and implementing policy".

It is not clear that this has changed much under the successor industry association to the National Dairy Council, the Dairy Processors Association of Canada. However, in observing this, it should be noted that unlike producers, processors view one another quite rationally as competitors. Dairy processing firms shape themselves to some degree to compete within the regulatory structures of milk supply management. As such, changes to the system can act to change the competitive dynamics among competing firms. Thus, it is perhaps not surprising that processors have been limited in acting collectively in shaping dairy policy.

The difficulty with this situation is that changes have occurred rapidly in dairy processing.

- Dairy processing technologies have evolved rapidly. More efficient cheese-making allows lactalbumins and lactoglobulins to be captured in cheese, where in traditional cheese-making those proteins passed into the whey.
- High protein dairy ingredients (MPC's and MPI's) are effective substitutes for proteins in raw milk, and it appears likely that whatever additional functionality value exists with these ingredients today may grow in the future
- The number of dairy processing plants has decreased markedly from the 1970's, though not as dramatically as the number of dairy farms. The bigger change has been concentration into a small number of large firms. Today, four firms are dominant in primary dairy processing; three operate at a multinational scale (two of which are Canadian-owned multinationals)
- Grocery retail and foodservice customers for dairy processors are increasingly concentrated. They require large-scale suppliers to provide them with product. The downstream retail and food service customers are increasingly assertive with suppliers

on pricing, product specifications, and supplier terms. Among the concerns regarding this are calls for a grocery retail “code of conduct”²

- Canadian dairy markets are mature, at least in aggregate. There are specific domestic segments experiencing rapid growth, and others that are in decline. Access to export markets, some of which are growing rapidly, is capped by past trade rulings against Canada. Dairy processing firms and their financiers look for growth markets as places to invest; this has limited new investment in Canadian dairy processing and shifted it elsewhere. Apart from marginal, caretaker types of investments, it appears that growth either through the domestic market, or through increased export market access may be required to induce material new investment in dairy processing.

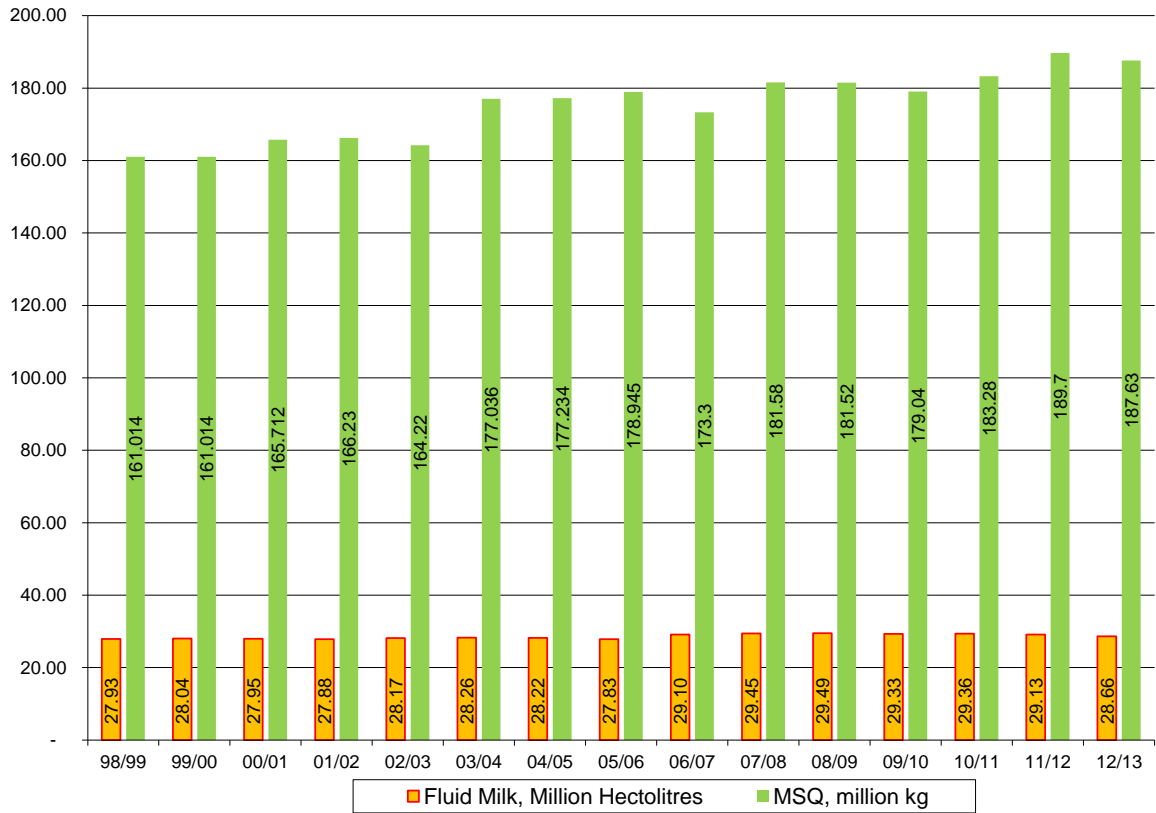
2.3 Dairy Markets

Canadian dairy markets have evolved greatly over time, from a limited set of staple products forty years ago to a much more diverse range of products today. This is consistent with certain other categories of food products, but Canadian dairy markets also have certain nuances.

- In aggregate, dairy markets in Canada are mature. This can be seen through the trends in milk marketed in fluid classes and in the MSQ shown in Figure 2.4 below. Fluid milk marketings have ranged around 28 and 29 million hectoliters for over ten years. The MSQ has seen some growth, but has essentially ranged around 180 million kg since 2003/04.
- The aggregate market dynamics obscure growth in specific market segments. For example, yogurt has seen impressive growth, increasing from just over 3 litres per capita to over 8 litres per capita since the early 1990’s; ice cream has seen precisely the opposite trend (Figure 2.5). Similar dynamics have occurred with specialty cheeses (growing) and butter (declining)
- The dairy case has been the site of a great expansion in brands and product formats, as well as new and differentiated products. To some extent, this has tended to link production and process characteristics with brands. One instance of this is a renewal of interest in on-farm processing and marketing, and links to dairy farming in dairy product marketing.
- Canada is trade deficit in dairy products, and this deficit is increasing, as illustrated in Figure 2.6. This trend is a function of increasing imports, and the stark reality of exports capped at historic levels.
- International dairy product prices are relatively strong, and this is expected continue. Figure 2.7 below presents aspects of the February, 2014 long term outlook for US dairy markets by the USDA. It envisions non-fat dry milk prices at or above \$US 1.60/lb out to 2023, and milk prices in the US ranging around \$US 19/cwt near term and then increasing out to 2023. Throughout the first quarter of 2014, western US non-fat dry milk prices exceeded \$US 2/lb.

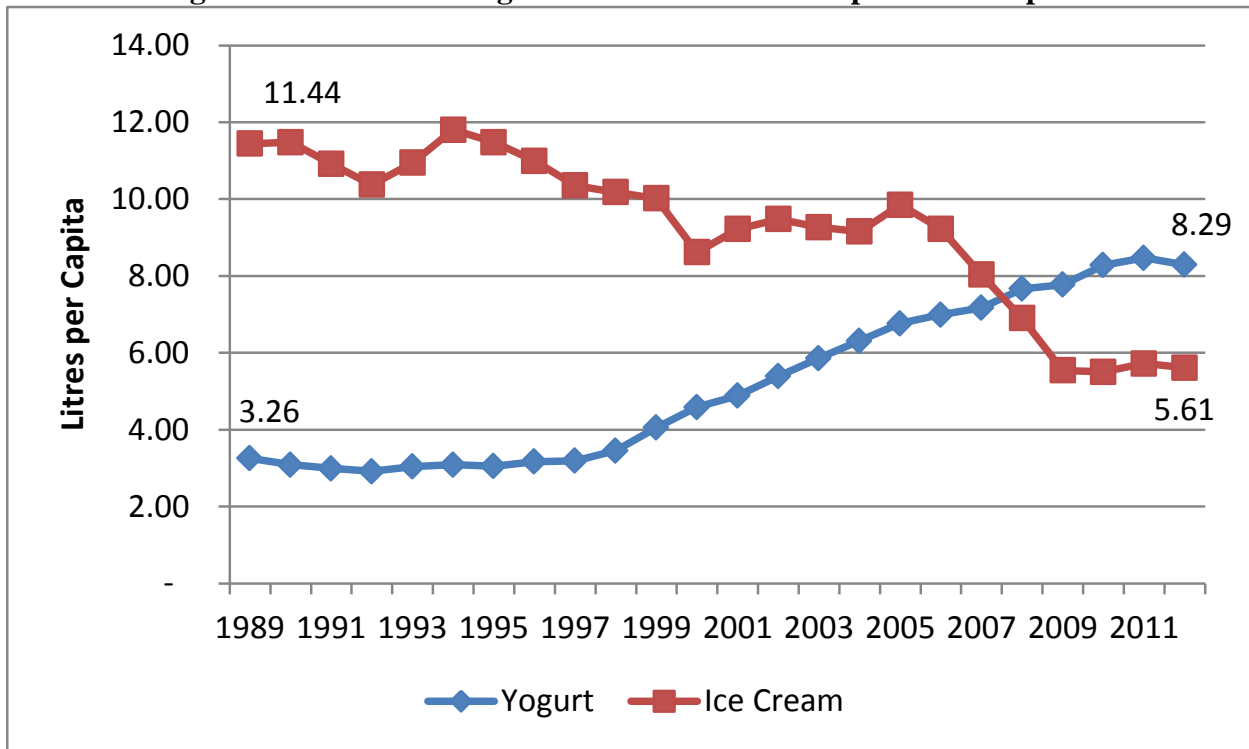
² See for example <http://www.theglobeandmail.com/report-on-business/grocers-call-for-code-of-conduct-between-retailers-suppliers/article17381094/>

Figure 2.4 Canadian Fluid Milk Volumes, Market Sharing Quota



Source: Canadian Dairy Information Centre

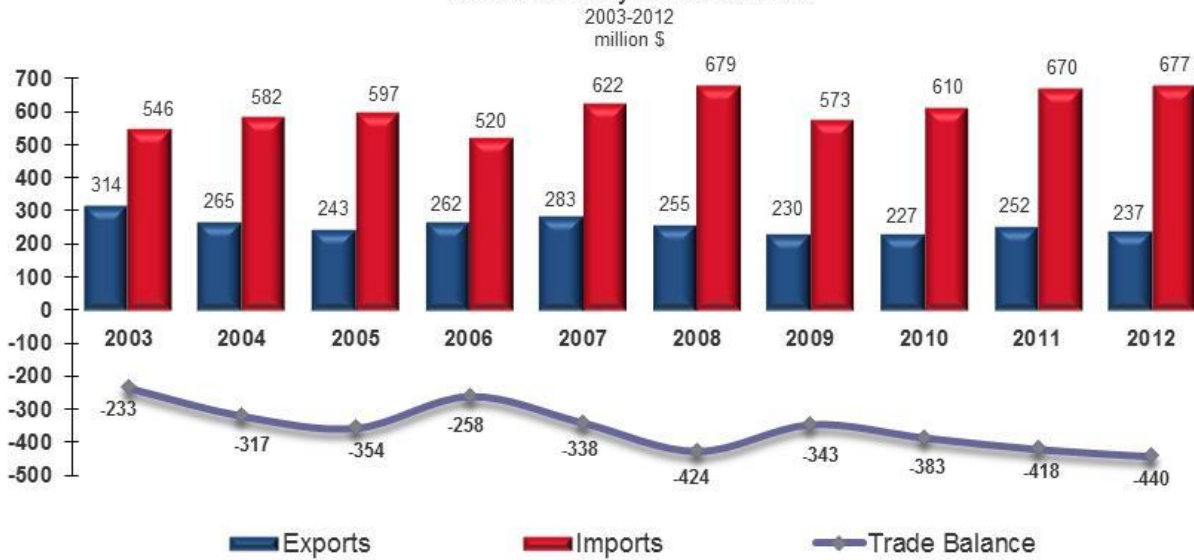
Figure 2.5 Canadian Yogurt and Ice cream Per capita Consumption



Source: Statistics Canada
 Calculations done by AAFC-AID, Dairy Section

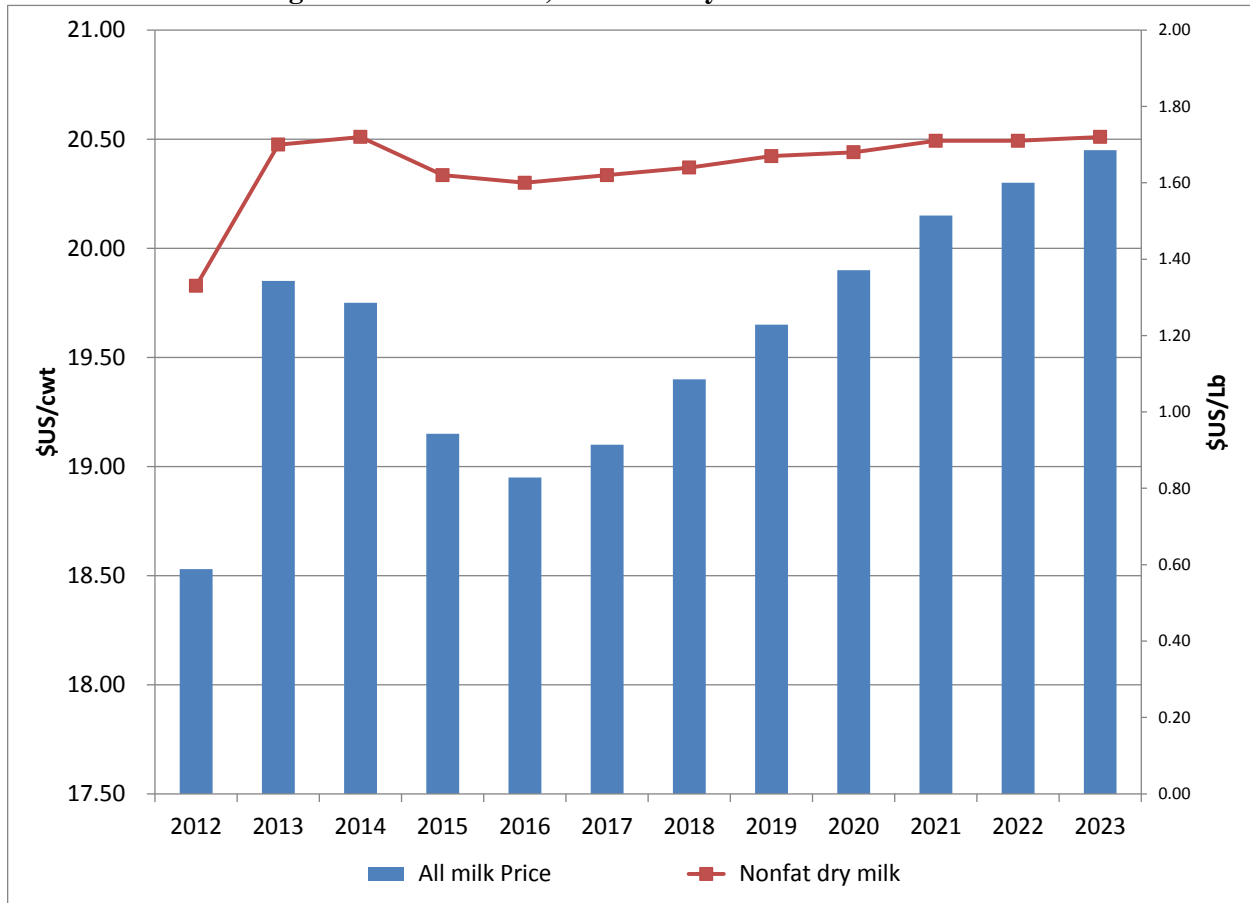
Figure 2.6

Canadian Dairy Trade Balance



Source: Statistics Canada Animal Industry Market Information System" (AIMIS)

Figure 2.7 USDA Milk, Non-Fat Dry Milk Market Outlook



2.4 Governments, and Broader Economic Policy Direction

Federal and provincial governments have generally been very active supporters of milk supply management from its earliest days. Publicly, this remains today, but there have been important shifts in governments’ approaches to broader industry/economic development.

- The development and delegation of authority to the Canadian Dairy Commission and provincial marketing boards in the late 1960’s and early 1970’s was broadly consistent with a Keynesian view in which market intervention was a core element of economic development. This is evident, for example, in a willingness of the federal government to implement wage and price controls, and to intervene in energy markets through the National Energy Program in the 1970’s
- The situation is rather different today. Economic growth and industrial policy appears firmly rooted in freer trade. This is immediately evident in the extensive effort put forth by the federal government in major trade negotiations. These include:
 - Canada-EU (complete)
 - Canada-South Korea (complete)
 - Trans-Pacific partnership (in process)
 - Canada-Japan (in process)
 - Canada-India (in process)
 - WTO-Doha (in process)

- Consistent with a freer trade theme in industrial policy, there appears to be generally less willingness of governments use regulation to control or influence the economy. While this is not uniformly consistent (for example, new federal compositional standards for cheese were introduced in 2008), the agreement between Canada and the US to establish a Regulatory Cooperation Council with a goal to reduce regulatory burdens is an indicator. There seems to be fewer resources available for regulation in both federal and provincial governments, and a reduced willingness of regulatory agencies to take on new mandates.

3. Implications for the Evolution of Canadian Dairy Policy

The context discussed above suggests a very different environment confronting milk supply management. This section provides a synthesis of these factors, and draws together the apparent implications into recommendations for future policy development.

3.1 Pressures on Dairy Policy, Then and Now

The key policy pressures and factors in the early days of milk supply management are relatively well known:

- Reduce the incidence of milk and dairy product surpluses
- Provide for pricing that allowed sustainable returns
- Improve equity among producers
- Counter processor market power
- Economic/industrial policy amenable to marketing regulation and supply management

Many of these policy pressures remain today. There is an ongoing demand from producers for farm milk pricing that provides returns to cover the cost of production. There are fewer and more consolidated dairy processors than there were historically, potentially giving rise to market power fears among some; on the other hand there is some acknowledgement that large processors are required to supply large retailers. Other pressures have abated; milk pooling across end-uses and regions of the country and the product homogeneity established as a result must surely have reduced many of the producer inequities perceived in the past.

There are important new pressures on dairy policy:

- An important priority of dairy farmers is the preservation of their capital that has appreciated as dairy farm asset values have increased.
- Some producers (but not all) seek market growth and flexibility to expand that will allow them to make improved returns on their dairy farm assets and/or attract the next generation to dairy farming. Other producers are cautious or even antagonistic to market growth and flexibility
- Processors are a more significant element of dairy policy, even if they have not been highly involved in policy development. Policy initiatives undertaken by producers will increasingly require coordination with dairy processors. There is greater interest in product marketing that links farm attributes to consumer dairy products

- Market growth is a priority for Canadian dairy processors. Processors look for improved market growth in the domestic market, and improved access to the export market
- Growth in the domestic dairy market is closely linked to differentiation and heterogeneity in products and brands, not the homogeneity consistent with pooling
- Retailers and food service customers exercise market power on their suppliers as never before. Their actions can profoundly impact producers and processors operating in supply management, yet they operate outside of the system
- Industrial policy is freer market, trade oriented, with less tolerance for industrial regulation and fewer resources with which to regulate. In this environment, increasing imports can be expected to pressure Canadian dairy markets and milk supply management.

3.2 Implications and Recommendations for Prospective Policy Direction

The agenda for Canadian dairy policy has both shifted, and become more crowded. The risk in this environment is that adjustments to the existing parameters of milk supply management will be insufficient to address the pressure of new demands. This suggests the needs for a broader reconsideration of dairy policy direction.

1. The essence and objectives of Canadian dairy policy need to be revisited

Milk supply management has been predicated on producer objectives. However, there are some apparent producer objectives today that were not evident in the design of the system initially. This includes the preservation of dairy farm capital that has appreciated under supply management, but extends to the preferences of some farmers for growth, flexibility, and renewal. Some of the existing objectives may be less important to producers today than they were historically. These objectives need to be determined and enunciated as part of a dairy policy renewal process. In particular, clear, meaningful, proactive producer objectives can be expected as a requirement on behalf of provincial governments if they are asked to loosen some of the provincial rigidities in milk supply management.

It is plainly unreasonable to suppose that renewed dairy policy could be developed without the intimate involvement of processors. Indeed, some producer-led initiatives, such as a reduction in the structural surplus of skim milk powder through increased domestic MPC/MPI manufacturing, clearly require active participation by processors. The apparent processor objectives in dairy policy relate to growth in the domestic market, and an expanded access to the export market—particularly given the broader dairy market outlook.

The contemporary meaning of “market power” in the dairy supply chain should also be understood in developing the renewed purpose for Canadian dairy policy. There are fewer, larger processors so there may be perceived a latent threat of processor market power. At the same time, there are benefits from processors operating at efficient scale, particularly in consideration of concentration at the retail and food service levels, and the scale of dairy processing required to supply them. Retail and food service market power is receiving increasing attention, with this level of the market operating essentially outside the scope of supply management.

Finally, the realm of possibility for renewed dairy policy will be constrained by broader economic/industrial policy and external factors. CETA, with its increased market access granted for cheese, has signaled that Canada's freer trade stance will be accompanied by some tolerance for increased domestic dairy market access, and more of this is expected under other trade agreements, notably TPP. Demands for new labeling standards and regulatory enforcement will need to confront limited resources in federal and provincial governments and regulatory enhancement/red tape reduction efforts. These will act to constrain dairy policy. The fact that world dairy prices are high, and with an outlook envisioning strong prices well out into the future, may open new possibilities for reform not previously envisioned.

2. Design regulatory instruments that can implement the objectives

Milk supply management today is a nexus of federal and provincial rules that fit together somewhat akin to a jigsaw puzzle of past agreements, accommodations, and carve-outs. The system administrators in provinces and federally have been effective in managing this environment, and some flexibility has been attained within it. However, because it is a nexus of interacting regulations, it can prove to be cumbersome and frail in the face of major external changes in multiple directions. Worse, the existing structure may lead reform down a path that is unduly limited, simply because of familiarity and the manner in which the system operates now. The pressures on dairy policy are of sufficient magnitude and in multiple dimensions that renewal efforts cannot boil down to the search for a more elegant solution to problems with the existing system, using refinements to existing instruments.

The renewed objectives and external constraints should guide reform efforts, with the constraints of the existing structure, at least for now, set aside as the model for a renewed system to allow for more creativity. This will allow the crafters of renewed dairy policy to focus on what is wanted rather than (necessarily) retaining significant components of what we have now. This will be needed in order to produce bold change.

3. Consider expanded use of market instruments

Regulatory instruments within milk supply management can be very effective in disciplining markets and controlling behaviour. However, by nature, regulations do not foster smooth adjustments to change; rather, regulations impede change, and may later be subject to revision to match conditions in the face of sustained change, which in turn creates abrupt and potentially harsh adjustment. An environment in which product/marketing differentiation is increasingly valued is one which needs a more flexible environment with smooth adjustment, in which farms and firms can more readily experiment, and not one confronted by regulatory inertia, followed by harsh adjustments. Similarly, if external market forces will increasingly bear upon Canadian dairy markets, elements of market adjustment should be wired into Canadian dairy policy to anticipate this. Finally, the pressure for growth through exports can be expected from processors and a subset of dairy farmers. Increasing export market access will be a difficult challenge given the existing structure of the system; increased reflection of dairy markets within a regulated dairy policy system in the future can only enhance our prospects for export.

4. Engage provincial governments

In the early 1970's when provinces entered into what would later become the national milk marketing agreement, they agreed to abide by a national industrial milk quota and share the market, along with future growth in the national market. In return, provincial dairy industries (farm production and dairy processing) were brought into the national system, with an understanding that these would be protected, under strict provincial autonomy and control. Thus, destructive price wars between provinces (such as the "Chicken and Egg War" between Ontario and Quebec of the early 1970's) were prevented; this was later complemented by regional milk pooling agreements. Over time, market forces coupled with new products, technologies, etc. have pressured this arrangement at the margins, but the fundamental "deal" between provinces, the federal government, and producer organizations has remained essentially intact.

Today, as the dairy market has become increasingly national with much more concentrated grocery and food service customers, and plant efficiencies are achieved at much larger scale, this arrangement which fragments national allocation to the provincial level is an encumbrance to milk supply management and dairy industry growth. The development of new, national scale plants is made more difficult because the new plant must be located somewhere; if the new plant is not purely incremental market growth, quota must be made available from elsewhere within the province hosting the new plant. Historically this has been tractable, especially where plants are small and provinces' quota allocations are large. New measures have been developed that attempt to ease this, such as interprovincial redirection of skim milk. But these can only partially address the overriding issue. It is made worse by the fact that individual provinces have the authority to allocate milk to plants within the province, and have historically used different mechanisms to do so. The uncertainty associated with this must surely affect incentives for processors to invest in new, efficient scale dairy processing plants.

As part of dairy policy renewal, the provincial fragmentation of quota should be formally engaged. Producers have over 40 years of experience with milk supply management, and any reticence in terms of whether the system would "work" on behalf of provinces (in the interest of their producers) should have long ago dissipated. Indeed, the producers have championed a truly national P10 system. This would support investment by national-scale processors. The new deal that needs to be struck between the federal government, provincial governments, and producers is to make dairy policy truly national, and in return the system may be sustainable and capable of delivering on the demands of its stakeholders. Failure to secure this deal places the system under risk of renewed balkanization and prolonged lack of investment in dairy processing.

5. Seek external input and analysis

Milk supply management agencies have significant resources for planning and analysis. These must be fully utilized in planning renewal of dairy policy. However, in as much as agency staffs have valuable expertise and corporate memory, they are fully ensconced in the detail of the current system. Relying solely on agencies' expertise in policy development and analysis can thus lead to a type of "path dependence", in the sense that new approaches are developed from existing ones, rather than coming from the freshness of independent analysis and experience elsewhere.

As described above, processor associations lack the resources of the producer/milk supply management agencies, and they have not taken a proactive role in policy development or analysis. Processor associations are limited in this role because their members are companies that are competitors, and companies orient themselves and shape their operations and product mix given the regulations they operate under. Changes to regulations under supply management can benefit some processing firms and harm others, and influence the competitive environment. Thus, it can be difficult for processor associations to engage directly in development and analysis on dairy policy renewal; however, this is urgently needed by processors as they must play a more active role in the process. Processors and their industry associations will need independent external assistance in analysis to fill this role.

4.0 Conclusions

Milk supply management in Canada appears to have quietly entered a phase in which more ambitious reforms are being contemplated and proposed. This is a rational response to pressures from an increasing structural surplus of skim milk powder, increases in imports (with additional imports anticipated in the future), with no immediate prospect that the increased imports can be offset with increased exports, let alone growth through exports. By itself, these factors present the prospect of a shrinking or declining Canadian dairy industry; thus the urgency to act on a renewal of dairy policy.

The challenge then is to craft a renewed Canadian dairy policy that can effectively anticipate and adjust to these forces pressuring it, and effectively accommodate the objectives of its principal stakeholders. This will be a daunting task, as some of the factors identified here are structural and far-reaching. Moreover, effective processes to motivate the extent of bold change that may be required are not in hand. For example, there is not an established, sanctioned process for producers to “negotiate” with processors; rather, processors have been included on an ex-officio or observer basis in producer-driven processes such as the Canadian Milk Supply Management Committee (CMSMC). Other processes have been *ad hoc*, such as the Dairy Industry Working Group, and endorsed by governments only on this *ad hoc* basis. It seems unlikely that governments would wish to lead this process.

Similarly, provincial milk marketing boards are granted sweeping powers over milk marketing, which gives them legal authority to make major changes in how milk supply management operates. However, it is less clear that, in the face of very significant changes to milk supply management, they have the *political* authority to make these changes, which is a source of latent risk to provincial marketing boards. This suggests a need for meaningful, broad, public consultations among dairy farmers, processors and other stakeholders as supply management modernization goes forward and dairy policy preferences develop.

This type of consultation process in policy development has not been the tradition in Canadian dairy policy, and indeed this may be uncharted territory. Perhaps the best example is a past bold change in milk supply management- the quota crisis of 1976. Scullion (2006) describes the lead up to the 1976 decision, which ultimately resulted in an 18% reduction in the MSQ, as very much an internal dialogue among the CDC and CMSMC, ultimately driven by the federal

Department of Finance. If producers or processors may have known that something was coming, but they certainly were not offered the opportunity to provide input. The fallout of the decision later resulted in bitter feelings toward the system among many producers, particularly in Quebec where producers felt they bore the brunt of the decision. This later led to a protest of 10,000 farmers on Parliament Hill, and federal agriculture minister Eugene Whelan being sprayed with milk and other objects from the angry crowd. Presumably Minister Whelan held supply management agencies to greater account following the incident.

Thus, an improved dialogue on the future of milk supply management and dairy should proceed acknowledging producers, processors, governments and others as stakeholders, as well as the totality of pressures it faces. It should also proceed with a willingness to allow policy objectives and constraints to guide the development of appropriate instruments, rather than rely on retrofits to existing policy instruments. It should also strive for an improved process that will be respected and binding upon the parties, and allow for fully public consultations to iron out conflicts and achieve consensus. There appears to be much work to do.

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