SUPPLY MANAGEMENT: PROBLEMS, POLITICS – AND POSSIBILITIES

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SUMMARY

Despite a professed commitment to free trade, Canada has retained a staunchly protectionist supply management regime in several agricultural sectors, notably in the dairy industry. Canada’s dairy farms are governed by a system that prices milk based on intended usage, locks out most foreign products with exorbitantly high tariffs and even determines how much farmers can produce — in other words, a cartel. Everyone suffers. Canadians are forced to pay twice the amount for four litres of whole milk as Americans, while the farmers are barred from taking advantage of the opportunities and efficiencies a truly free market affords. At the same time, Canada’s insistence on protecting supply management makes it difficult for Canada to open up access to international markets. This means that all other Canadian enterprises that rely on trade (including the farmers in the non-supply-managed sectors who make up by far the majority of Canadian farmers) — all those who would benefit from Canadian participation in trade arrangements such as the Trans-Pacific Partnership, are being denied lucrative access to some of the world’s largest and rapidly growing markets. The system needs to go. However, it is possible to dismantle it fairly. Australia managed it by offering dairy farmers transition payments over eight years, financed by a temporary retail levy on milk, which was still less than what consumers were paying under protection. Consumers now enjoy lower prices and Australia has one of the most dynamic and efficient dairy industries in the world. New Zealand did away with its own tariffs and subsidies even faster, and its dairy sector has become that country’s largest export earner. The potential gains for Canada are very real. At the same time, and, just as importantly, the threats to risk-averse politicians from the dairy lobby are, contrary to widely-held assumptions, negligible. Since 1971, the number of Canadian dairy farms has dropped by a staggering 91 percent. There are now few, if any, ridings where dairy votes could plausibly swing elections — particularly compared to the votes of all those in those same ridings who would benefit from dismantling supply management. This paper assesses Canada’s political, agricultural and economic landscape, highlights the problems with the present regime, challenges long-held political assumptions, and draws on lessons learned from the most successful reforms abroad to make the case for liberalizing the Canadian dairy industry. With lucrative free trade agreements being considered, and in particular the prospect of joining (or being refused access to) the Trans-Pacific Partnership, now is the time for the Harper government to reach out to the provinces and farmers, and move away from supply management for the good of all Canadians.

* The author wishes to acknowledge the helpful comments of the anonymous referees.
LA GESTION DE L’OFFRE: PROBLÈMES, POLITIQUES – ET POSSIBILITÉS

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RÉSUMÉ

Malgré son parti pris avoué en faveur du libre-échange, le Canada maintient un régime de gestion profondément protectionniste dans plusieurs secteurs agricoles, en particulier celui des produits laitiers. Ce secteur est régi par un système qui établit le prix du lait en fonction de l’usage prévu et s’appuie sur des tarifs douaniers exorbitants qui empêchent les produits étrangers d’accéder au marché, en plus de déterminer la quantité de lait que les producteurs peuvent produire. En d’autres mots, il s’agit d’un cartel. Tout le monde en souffre. Les Canadiens doivent payer deux fois plus cher pour quatre litres de lait entier que les Américains tandis que les producteurs ne peuvent pas jouir des avantages et des économies que comporte un marché réellement libre. Dans la foulée, le pays a plus de difficulté à accéder aux marchés internationaux parce que le Canada insiste pour protéger la gestion de l’offre. Par conséquent, toutes les autres entreprises canadiennes qui s’appuient sur les échanges (y compris les agriculteurs dans des secteurs où la gestion de l’offre n’est pas régie, c’est-à-dire la très grande majorité des agriculteurs canadiens) — tous ceux qui profiteraient de la participation du Canada à des accords commerciaux tels que le Partenariat transpacifique se voient refuser l’accès lucratif à certains des marchés les plus importants et qui croissent le plus rapidement au monde. Il faut se débarrasser de ce système. Toutefois, il est possible de le démanteler équitablement. L’Australie y est parvenue en offrant à ses producteurs laitiers des paiements de transition échelonnés sur huit ans, financés par une taxe au détail temporaire sur le lait, laquelle demeurait inférieure à ce que les consommateurs devaient payer quand le prix était protégé. Les prix pour les consommateurs sont maintenant plus bas en Australie et son industrie laitière est une des plus dynamiques et des plus efficaces au monde. La Nouvelle-Zélande s’est débarrassée de ses propres tarifs et subventions encore plus rapidement, et son secteur laitier est devenu la principale source de revenus à l’exportation de ce pays. Les gains possibles pour le Canada sont bien réels. En outre – ce qui importe tout autant – la menace que représentent les groupes de pression du secteur de la production laitière sur les politiciens réfractaires au risque est à peu près inexistant, contrairement aux idées reçues. Depuis 1971, le nombre de fermes laitières au Canada a chuté radicalement de 91 pour cent. Aujourd’hui, il existe peu de circonscriptions, voire aucune où le vote des producteurs laitiers est prépondérant, et qui pourraient faire pencher la balance, comparativement à tous les électeurs qui profiteraient du démantèlement de la gestion de l’offre. Cet article évalue la situation politique, agricole et économique du Canada, illustre les problèmes du régime actuel, examine les préjugés tenaces sur le plan politique et tire les leçons des réformes les plus efficaces à l’étranger pour soutenir la libéralisation de l’industrie laitière au Canada. Tandis qu’on envisage de conclure des accords lucratifs de libre-échange, et en particulier l’adhésion possible (ou le refus possible de cette adhésion) au Partenariat transpacifique, il est maintenant temps que le gouvernement Harper en appelle aux provinces et aux producteurs et abandonne pour de bon la gestion de l’offre pour tous les Canadiens.

† L’auteure souhaite remercier des lecteurs anonymes pour leurs commentaires utiles.
INTRODUCTION

The recent surge of interest by the Canadian government in participating in the Trans-Pacific Partnership (TPP) trade negotiations has come as a welcome surprise. It is certainly welcome to all who support Canada’s efforts to engage in more international trade and to embrace global economic opportunities.

But why a surprise? Because a key reason that existing TPP members are not welcoming Canada with open arms is our supply management regime for dairy, poultry and eggs — and until now, the Harper government, as well as prior governments of different political stripes, have repeatedly defended supply management in Canada.¹

Does this desire to participate in the TPP mean that supply management is now really on the table? Can we really, finally, seize this opportunity? It is, after all, hard to imagine countries like the US, Australia and New Zealand not insisting, before we are fully allowed on board, that Canada abandon our supply management regime.

Most economists, think tanks, commentators, consumer advocates (and trade negotiators) have, for quite some time, recommended the dismantling of Canada’s supply management regime — for both domestic economic reasons and for reasons of international trade. Notwithstanding the example provided by the recent, successful dismantling of a similar system in Australia, Canadian politicians still seem stuck. Frustratingly, many of them agree, privately, that it no longer makes sense, that it should be dismantled — but they say that “politically, it’s not possible;” “there are too many votes at stake.” The time, however, may now be ripe. The drastic reduction in the number of farmers involved in the supply-managed sectors, their concentration in certain areas, and changed political and electoral realities mean that politically, it may indeed now be much more possible than has been assumed.

Not only is the perceived political negative not what it used to be, there are potential political positives. There are far more farmers and others in other sectors who support the dismantling of supply management; governments (federal and provincial) can and should engage more effectively with these others, and mobilize their political support. There is an entire country full of consumers — taxpayers and voters — who are paying one and a half to three times more for their milk, other dairy products, chicken and eggs than they should be — amounting to more than $200 more a year per average family. Even with the dairy producers themselves, governments can and should be reinforcing the positive solutions and increased opportunities. Australia, New Zealand — even our own Ontario and BC wine industries — have shown that taking away protection can achieve positive results. Dismantling supply management is NOT something to be feared. The long-assumed political challenges should finally be seen to be what they are — not enough to prevent long-overdue action from being taken.

This paper focuses on dairy — it is the largest of the supply-managed sectors, most of the relevant research has been done on dairy, and the best example so far of deregulation of a supply-managed industry is the dairy industry in Australia. The general principles of our conclusions and recommendations with regard to the dairy industry apply, however, to the others.

¹ On November 23, 2005, a motion supporting supply management was passed unanimously in the Canadian House of Commons.
This paper:
- Summarizes what supply management is and its history in Canada;
- Summarizes the current domestic economics and theories both for and against;
- Examines the problems that our continued support for supply management creates for us as a trading nation — in particular for the non-supply managed agricultural sectors which suffer as a result of reduced access to international markets, but also for the dairy industry itself and the Canadian economy overall;
- Summarizes the successful Australian experience in dismantling their own supply management system;
- Highlights the successes of the New Zealand dairy industry since removing protection;
- Examines — and challenges — the political assumptions behind politicians’ traditional unwillingness to challenge supply management, suggesting that those assumptions are no longer valid, and that the political risks are much smaller than previously assumed; and, finally
- Most importantly, offers concrete suggestions to current decision-makers on how to move forward, based on the Australian model.

WHAT IS SUPPLY MANAGEMENT?

Supply Management is a system of controlled markets that applies in Canada to dairy, poultry (chicken and turkey), and eggs (both table eggs and hatching eggs). It evolved over time, implemented in its current form in the 1970s, primarily to ensure a fair return for farmers and price stability for processors and consumers.

It is not available to any other agricultural activities — beef, pork, grain,2 pulses, oil seeds and their oils — which are, for the most part, subject to the open (and international) market. Different agricultural sectors receive different supports from governments (including Canada), but only dairy, poultry and eggs benefit from the comprehensive controlled market approach of supply management.

As the name suggests, it is a system determined by supply and not, as in most economic activities, demand. Although in practice it gets very complex, the theory is relatively simple: the prices for milk paid to the producers (the farm gate prices) are established based, not by what the market is willing to pay, but primarily on the costs of production; high protective tariffs are in place to prevent competition from outside; and production is controlled through a regulated quota system.

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2 Although not the same as supply management, the last vestige of market control in grain, the mandated single-desk marketing approach of the Canadian Wheat Board, is being dismantled.
How does it work?

**Price-setting:** Producers milk cows and sell the milk. 40 percent of raw milk goes to consumers’ tables (referred to as “table” or “fluid” milk), whether as two percent, whole milk or cream. The rest goes to processors who make butter, cheese, ice cream, yogurt or other dairy products. The prices are set nationally by the Dairy Commission (made up mostly of dairy farmers), by first establishing a target price range. This target price range is then used by the provincial boards to set their own. The Dairy Commissioners arrive at the target price by analyzing production costs, market conditions, other stakeholder input, and what they determine is a fair return to the producers. Other factors include assessments of overall demand for milk and dairy products, and what the current production levels are.

Not only do the authorities set prices based on several different cost and fair return factors, but also exactly the same milk will fetch a different price based on the milk’s ultimate use. There is an entire class system for pricing milk, primarily related to perishability. Highest prices go to fluid/table milk and cream. Next comes milk sold to processors for ice cream, yogurt and sour cream. Next comes cheese, then skim milk powder and then butter. Furthermore, the prices may vary according to the milk’s actual components (butterfat, protein, lactose and minerals). In the end, these are the fixed prices that both consumers and processors must pay.

**Protection from foreign competition:** We live, however, in a global trading environment, and in most cases, the prices set in Canada are significantly higher than what imports of competing products from other countries would cost. To maintain those higher domestic price levels, the Canadian government has to limit competition from outside. First, they simply prevented any imports at all. This was, initially, straightforward, but became more difficult to sustain when faced with increasing international efforts to lower trade barriers, first under the General Agreement on Tariffs and Trade (GATT) and then under the auspices of the World Trade Organization (WTO). Canada is a trading nation, and has generally been a proponent of freer trade — with the glaring exception being its protection of the dairy, poultry and egg sectors. Canada claimed that these sectors were sensitive (an approach grudgingly permitted under the WTO trading rules); it established a tiny quota of allowable imports in these sectors to fulfill minimum access commitments at low tariffs, and then applied exorbitant tariffs to any imports over and above the quota. The allowable quota is so small it doesn’t really affect the domestic market — eight percent of the domestic market for cheese, for example, or one percent in the case of yogurt — as trade negotiator Michael Hart has described it, the equivalent of one rounded teaspoon of yogurt per Canadian per year. The tariff on the over quota (ranging from 168 percent for eggs, 238 percent for chicken, 246 percent for cheese, to almost 300 percent for butter) means that the prices of imports are so high that virtually no one bothers. As intended, the domestic industry remains almost completely protected.

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Control of supply: This is the final piece. With such protection from outside and with guaranteed returns, the dairy business would be extremely attractive to potential new producers or for existing producers to add production. After all, a guaranteed price for your output based on your costs, not on market forces and competition, makes for a no-lose, profitable enterprise. But overproduction would wreak havoc with the scheme, so the government established a quota system — each producer is only allowed to produce his or her quota of milk. This alone has now created a major economic distortion, however: quota is now worth about $28,000 per cow, meaning about $2 million per average farm, for a total quota value in Canada of about $28 billion. This represents double the value of quotas only 10 years ago.5

Whereas the Dairy Commission is responsible for determining milk prices, the national Milk Supply Management Committee is responsible for determining the national production level (with the authority for managing the supply of raw milk for table milk and cream to the provinces).7

The primary goals of price stability and a fair return for farmers were met. It has, however, created distortions in the domestic economy, unfairness vis-à-vis other agricultural producers, and it has caused, and continues to cause, Canada problems as it tries to negotiate trade agreements internationally.

HISTORY OF SUPPLY MANAGEMENT

The history of supply management in the dairy sector in Canada is one of increasingly effective organizational efforts by dairy producers to stabilize and enhance their incomes, together with governmental acceptance of and compliance (federal and provincial) with those efforts during an era of greater enthusiasm for governmental social justice interventions.

The first fully national supply management system in Canada was created in 1970. Dairy was first. Eggs followed in 1972, turkey in 1974, chicken in 1978 and chicken hatching eggs in 1986.

But it did not happen overnight.

Due to pressure from dairy farmers, government involvement began early, with the appointment in 1890 of the first Dominion Dairy Commissioner. This led to various policies and program support for the dairy industry, including an iced butter railway car service (1895); funding for cool cheese curing rooms (1902); cow testing programs (1902); and the grading of butter and cheese for export (1923).8

5 In 1971, when the system was established, quota was allocated free to then-existing producers based on their then-current output. Quota is now transferable, and a cow’s worth of quota now makes each dairy cow in Canada worth approximately $28,000 — not including the cost of the actual cow.
Already in these early years farmers were recognizing the benefits of co-ordinated action and organization. “In 1934, the Canadian Dairy Farmers’ Federation was established as the voice of Canadian dairy producers.”9 It is not coincidental that a year later, in 1935, the government of Canada introduced a temporary subsidy on cheese and butter.

In 1942 the Canadian Dairy Farmers’ Federation was renamed Dairy Farmers of Canada, when the Federation merged with the Producers’ Section of the National Dairy Council. The mandate of DFC evolved to pursue market stability policies and ensure fairer prices for producers.10

Again, not by accident, over the course of the 1940s and 1950s, additional government programs were established to support prices and limit imports. The Agricultural Stabilization Board was created in 1958 (although not just for dairy).

It was in the 1950s and 1960s, however, that dairy producers found it increasingly hard to make a decent and, importantly, stable living. Markets within Canada were volatile, worldwide prices were depressed in the 60s, and revenues varied significantly. This was aggravated by a view that the dairy processors held too much bargaining power and were profiting at the expense of the farmers. The prospect was also looming of the UK joining the European Common Market (which it eventually did in 1973), which would (and did) remove the UK as a major cheese export market for Canada.11

Yet the Agricultural Stabilization Board was not created for, or capable of, dealing with two issues specific to the dairy sector: co-ordinating federal and provincial efforts, and actual control of milk production, understood to be critical for price support. Surplus production was creating challenges.

Early farm organizations were already making moves toward some forms of managed supply, including organizing marketing boards to, for example, set common floor prices which their members respected.12

These groups lacked leverage, however, and therefore turned to provincial governments to create marketing boards.13

Provincially, Ontario and Quebec (the primary dairy producers) had begun to make moves toward some forms of managed supply, but the provincial governments and regional producer groups were only able to implement programs at the provincial or regional level. Their effectiveness was undermined by a lack of regulatory control over marketing that crossed provincial boundaries and national borders. In many instances, despite local management of supply, surpluses from other areas could easily disrupt their orderly marketing and undermine their attempts to regulate prices. This situation led to the call for coordinated marketing plans and national marketing boards.14

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13 Ibid.
14 Ibid.
The 1963 Canadian Dairy Conference was held, which led to the creation of the Canadian Dairy Advisory Committee the same year. In its 1965 final report, this Committee recommended the creation of the Canadian Dairy Commission — which was indeed created under the Pearson government in 1967. Its goals were to provide milk producers with a fair return for their labour and investment, and consumers with a continuous and stable supply of high-quality dairy products. (Note that there is no mention of consumer prices.)

The National Milk Marketing Plan came into being in 1970, with Ontario, Quebec and the federal government the first to sign on. All remaining provinces except Newfoundland entered the Plan by the end of 1974, with Newfoundland eventually signing on in 2001. (The National Milk Marketing Plan’s most important function is to establish the production target for industrial milk in Canada.)

All of this organizational effort coincided with the fact that, in those years, the Canadian government was increasingly inclined to greater social policy intervention — the political appetite was there. It is important to remember, however, that Canada was not alone. This sentiment, this governmental desire to intervene for the public good, was felt around the world. And in Canada, there is no question that, at the time, governmental decision-makers believed that the farmers were suffering from volatile markets, unstable world prices, and a lack of market power. There was also the view that, as farmers were being asked to ensure tougher health and safety standards, they should be compensated for incurring those additional costs. And everyone seemed to agree on the benefits of stable supplies at stable prices, for both consumers and processors, all year long.

These were laudable sentiments at the time, but over the course of several decades, some aspects have proved to be less beneficial economically than intended, and there have been other, unintended consequences. At the same time, for a variety of reasons, the dairy landscape in Canada has changed dramatically from a large number of individual, small family farms to a much smaller number of sophisticated producers.

The goals of supply management were important, and recommending change is not a comment on the worthiness of those goals or even of the structure of the system for the times. But times change, and the system needs changing. There is no shame in learning from past, well-intentioned efforts and realizing that some change is necessary. On the other hand, there is much to be gained, and to be proud of, in making the changes necessary to achieve even better results for all concerned.

DOMESTIC ECONOMICS

This paper does not attempt to re-create the excellent work done by various think tanks and other organizations in analyzing the domestic economics of supply management in the Canadian dairy sector, but rather, based much on their work, summarizes the basics.

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15 Ibid.
16 Conference Board of Canada; CD Howe Institute; Fraser Institute; Montreal Canadian Agri-Food Policy Institute; George Morris Centre; OECD, Montreal Economic Institute; Frontier Centre for Public Policy, and others.
Dairy represents less than half of one percent of Canada’s economy. In terms of agriculture, the dairy industry ranks third behind grains and red meats.\textsuperscript{17}

In 2011 there were only 12,746 dairy farms in Canada,\textsuperscript{18} whereas in 1971 (the beginning of supply management) there were approximately 145,000. Over 40 years, the number of dairy producers has dropped a staggering 91 percent. The number of dairy farms in the non-supply-managed US also dropped dramatically, from 591,870 in 1971 to 67,000 in 2008 (the most recent year for which figures were available) — an 88 percent reduction. One therefore cannot blame supply management for consolidation; on the other hand, it clearly hasn’t protected the small family farm.\textsuperscript{19}

Over the last 30 years we have seen milk production remain relatively constant, albeit from increasingly far fewer producers — larger operations with more cows per farm, with greater economies of scale, and producing more milk per cow.\textsuperscript{20} But this begs a very large question: regular market economics would suggest that in those circumstances prices would have gone down, or at least competed better with inflation. On the contrary, they have risen over the last 30 years, by more than the inflation rate.\textsuperscript{21} The opposite was true in the US, where the consumer prices of dairy products increased by less than the price of all consumer goods.\textsuperscript{22}

As for the prices received by the producers, a report done for the International Dairy Foods Association shows farm gate prices consistently higher in Canada than in the European Union, New Zealand and the United States over the years from 2001 to 2010 — with the difference getting increasingly large in recent years. In January 2010, relative farm gate prices (in US dollars per hundredweight) were approximately $15 in each of New Zealand and the US, $17 in the EU, and a whopping $32 in Canada.\textsuperscript{23}

\textsuperscript{17} Goldfarb, D. 2009. Op. cit. In the 2008-2009 dairy year, the fluid market accounted for approximately 40 percent of total producer shipments of milk, or 33 million hectolitres at 3.6 kilograms of butterfat per hectolitre. The industrial market accounted for the remaining 60 percent, or 49.9 million hectolitres of total producer shipments.

\textsuperscript{18} Canadian Dairy Information Centre. http://www.dairyinfo.gc.ca


\textsuperscript{21} From January 1981 to January 2012, all consumer prices increased by 157.4 percent, whereas consumer dairy product prices increased by 175.7 percent. Statistics Canada, CANSIM series v41690973 and v53385220.

\textsuperscript{22} From January 1981 to January 2012, milk price increased 129.69 percent, whereas the change in all-items CPI for the same period was 160.53 percent. USDL Bureau of Labor Statistics http://future.aae.wisc.edu/data/monthly_values/by_area/312?area=US and ftp://ftp.bls.gov/pub/special.requests/cpi/cpiai.txt

Who suffers?

Consumers: The following table shows the average retail price paid by Canadian and US consumers, respectively, as at each of March 2010, 2011 and 2012. The Canadian and US dollars were, at the times virtually at par so the prices for each jurisdiction are included as reported.

<table>
<thead>
<tr>
<th></th>
<th>Canadian average price for 4 litres of whole milk, $CDN*</th>
<th>US city average price for 3.8 litres of whole milk, $US**</th>
<th>Exchange Rate ($1CDN = $xUS)</th>
</tr>
</thead>
<tbody>
<tr>
<td>March 2010</td>
<td>$6.02</td>
<td>$3.19</td>
<td>$0.98</td>
</tr>
<tr>
<td>March 2011</td>
<td>$6.24</td>
<td>$3.50</td>
<td>$1.02</td>
</tr>
<tr>
<td>March 2012</td>
<td>$6.48</td>
<td>$3.50</td>
<td>$1.00</td>
</tr>
</tbody>
</table>

* Statistics Canada CANSIM series v735169 reports monthly data on the average Canadian price of 1 litre of whole milk. A comparison of data on the average retail price of whole milk in select cities reported by the Canadian Dairy Information Centre (http://www.dairyinfo.gc.ca) shows that the price of 4 litres of milk is typically 2.7 times the price of 1 litre. I apply the 2.7 multiple to the 1 litre price to arrive at an approximate value of the average price for 4 litres of whole milk in Canada.


One often hears the argument that the system involves no government subsidy, and therefore does not cost the government money (other than the cost of the bureaucracy), however the argument simply does not wash. It may not, technically, be a subsidy from the government, but it is quite clearly paid for by taxpayers — the consumers. Based on the table above, a family that buys an average of 4 litres of milk a week will pay close to $150 a year more than they should, just for their milk. Add the much higher prices they also must pay for cheese, yogurt and ice cream, and it is clear that millions of Canadian consumers are paying a major premium to benefit fewer than 13,000 farmers. The Conference Board of Canada estimates that supply management costs an extra $70 per Canadian.24

Worse, it’s regressive. The price burden is relatively higher for those with lower incomes who consume a greater proportion of milk produces — which includes, importantly, single-parent families with young children, the very people for whom basic nutrition should be most accessible.25 Not only are Canadian consumers paying far more, they also have limited choice because so little in the way of imports come in to compete. In virtually every other circumstance this would be viewed as an illegal cartel that limits competition and fixes prices, to the detriment of the consumer.

Processors: On the processing side, those who make products such as cheese, yogurt and ice cream are all paying prices far too high to make them competitive anywhere outside Canada. That may be fine for the captive Canadian market — remember, we have prohibitively high tariffs on these items, so that our processors can be competitive in selling their products in Canada even though they have to pay so much for the milk (even though it is the consumers who ultimately pay the higher prices for their goods). But the Canadian market is tiny compared to global opportunities. Not only are processors dissuaded from expanding their


plants in Canada, let alone from setting up any new ones — on the contrary, processors have
down incentives to take their capital investments, and the jobs that go with those investments,
abroad.26 In 2010, 22,650 people were employed in the dairy processing sector.27 That number
could be, and should be, much higher.

Some efforts have been made to help some processors be competitive with their foreign rivals,
but they are often in the form of Band-Aids, rather than dealing with the underlying problem.
One example of an attempted solution which adds even further distortion: to allow frozen pizza
manufacturers to compete with their US competitors and encourage them not to move away,
they are entitled to pay lower prices for cheese — however pizza restaurants do not get the
same benefit, even though they compete for many of the same customers.28

Another distortion is that quota is based on kilograms of butterfat. Skim milk powder is a joint
product of milk, yet consumer demand is higher for butter fat than for skim milk powder. As a
result, there is a chronic surplus of skim milk powder, which the Dairy Commission buys to
protect the system. As of June 2009, the Commission had 35,500 tonnes (equivalent to more
than 34 million litres, or more than one litre per Canadian of skim milk powder) in storage.29

**Restaurants:** Restaurants, and thus their customers, are paying more than they should. The
Canadian Restaurant and Food Services Association is already vocal in its efforts against
supply management.30

**Dairy farmers themselves:** The system provides higher than average returns for supply
management farmers.31 Indeed, the average dairy farmer is far better off than the average
consumer who, as we have seen, is ironically, the one paying more for that dairy farmer’s
products than he or she should be.32 The incomes of supply-managed farmers are consistently
higher than those in other agricultural sectors.33 However, a system that ensures that the prices
producers receive are calculated on a cost-plus basis, with virtually no competition, provides
little or no incentive, as an industry, to innovate, become more productive or competitive. On
the other hand, the system is unfair to efficient dairy farmers, whose opportunities to expand
and become more productive are hemmed in by the system’s constraints.34 Later in the paper
we look at both the Australian and New Zealand examples, where the dairy industries have, in
a free-market environment, greatly expanded their exports — to the benefit of the dairy farmers
themselves. Canadian dairy farmers are missing out on major global opportunities.

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28 Montreal Economic Institute “Dairy Production — the cost of supply management in Canada.” Feb 2005
http://www.statcan.gc.ca/pub/21-206-x/2012000/tablesectlist-listetableauxsect-eng.htm ; and “CANSIM tables for
Another myth is that the supply management protects and encourages the family farm. On the
contrary, as noted above, the number of producers in Canada dropped from approximately
145,000 at the time the system was implemented to about 30,000 by 1996, then down to a mere
12,746 by 2011.\textsuperscript{35} Indeed, consolidation has been faster and proportionally more significant in
the supply-managed sectors than in non-supply-managed agricultural sectors.\textsuperscript{36}

The high values of quota (which are in addition to the cost of land, cows, barns, and
operations), now about $28,000 per cow, have created a prohibitive barrier to entry as well as a
barrier to achieving economies of scale.\textsuperscript{37} The value of quota has also doubled from only 10
years ago.\textsuperscript{38} It is easy to get out by consolidation, but almost impossible to get in.

The bureaucracy of administration is also incredibly costly, with the focus on regulation,
making adjustments, fighting over provincial quota, fixing loopholes, lobbying politicians and
defending the system against increasing opponents, all of which prevents the necessary effort
and focus on positioning for the inevitable greater involvement in international markets.\textsuperscript{39}

\textbf{All other Canadian enterprises, including the majority of other farmers, who rely on international trade:}
Finally, a focus of this paper which is dealt with in more detail below is the negative effect
supply management has on international market and trade opportunities for the many export-
oriented Canadian industries, including most of our non-supply-managed agricultural sectors,
and thus for the Canadian economy as a whole.

A recent report by the OECD provides a none-too-subtle criticism of the whole system:

\begin{quote}
Nowhere in Canadian agriculture are the distortions greater than in the supply
managed sectors and above all in dairy farming. Not only are dairy farmers’ outputs
protected by prohibitive tariffs that result in retail prices for butter and cheese that
are around two and a half times those in the none-too-free US market, but their
median annual gross income levels have surged to over CAD 250,000, and milk
quota values on their balance sheets have soared to over CAD 26 billion in 2006
(around 2\% of GDP). This represents several million dollars per farm and
CAD 26,000\textsuperscript{40} per cow. Such rents are a blight on the economic landscape and
totally unjustifiable…\textsuperscript{41}
\end{quote}

The ideas behind supply management may have been laudable, in trying to ensure a stable and
fair return to dairy, poultry and egg farmers. And it is true that with stable and predictable
prices (albeit far too high), the producers know what they will get paid, and retailers and
processors know what their costs will be. But the negatives clearly far, far outweigh the
benefits. It is time for change.

\begin{flushleft}
\textsuperscript{36} Government of Canada. “Farm operators by farm type and province (2001 and 2006).” Statistics Canada,
http://www40.statcan.gc.ca/l01/cst01/agrc22a-eng.htm
\textsuperscript{38} Ibid. P 17
\textsuperscript{39} Ibid.
\textsuperscript{40} Note that this number is now about $28,000.
June, 2008. http://www.oecd.org/document/3/0,3343,en_2649_201185_40732867_1_1_1_1,00.html
\end{flushleft}
INTERNATIONAL TRADE IMPLICATIONS

Canada’s continued support for supply management in the dairy, poultry and eggs sectors has hampered Canada’s ability to negotiate free trade or lower tariff trade access to other countries. Simply put, other countries rightly ask why they should open up their markets to competition from Canada when Canada refuses to do so in these areas. This is particularly problematic given that Canada is relatively far more dependent on trade than many other countries. Canadian producers of all manner of goods and services, including almost all of the non-supply-managed agricultural sectors, would benefit from greater market access. The Canadian economy as a whole would benefit as a result, with more jobs in Canada and greater prosperity.

Despite all of the attempted arguments that this is somehow not a subsidy, international trade experts at the OECD, WTO and elsewhere know better. Mandated consumer-paid support distorts trade just as much as any direct government subsidy. Before the WTO Doha round of multilateral negotiations faltered, other countries were clearly frustrated with Canada’s singling out of supply management as being ‘required’ for ‘sensitive’ industries — particularly the many countries that have been reducing their own supports.

The OECD uses the concept of producer subsidy equivalent (PSE) to reflect real support given by governments — whether directly or indirectly through regulation (like supply management). In a report published by the Canadian Agri-Food Policy Institute, the relative PSEs as estimated by the OECD are discussed (based on data from 2006-2008, as a percentage of gross farm receipts). Canada does not compare well. The European Union’s PSE is high (27 percent), due to its Common Agricultural Policy, and this causes the EU significant challenges in its own trade negotiations. But at 18 percent (most of which is attributed to supply management for dairy, poultry and eggs), Canada’s PSE is significantly higher than the US (10 percent), Australia (six percent), New Zealand (one percent), Brazil (six percent), China (nine percent) and Chile (four percent).

Canada’s almost unexplainable insistence on defending supply management, for what is now a mere 12,746 dairy farmers, about 3,000 poultry farmers and fewer than 1,000 egg farmers, has prevented greater access to lucrative export markets for hundreds of thousands of farmers in other sectors, as well as manufacturers and exporters of other goods and services across Canada — and the jobs that they create and maintain.

The irony is that Canadian dairy producers are missing international opportunities as well — they are not exporting a fraction of what they could be. Total dairy exports in 2008 were only about $255 million, a mere five percent of total dairy receipts. The New Zealand experience, discussed below, provides an excellent example of what is possible; since the removal of subsidies, the dairy industry has become New Zealand’s biggest export earner, producing about two percent of total world production. Around 95 percent of its dairy produce is exported.


Closer to home, the removal of protection for the wine industry has had spectacular results, both for Canadian producers and consumers. While under protection, the wines produced in Ontario and BC were of a very poor quality, with a correspondingly small market. However, thanks to pressures under GATT, and the signing of the Canada/USA Free Trade Agreement in 1988, the wine industry could no longer be protected. As with those now under supply management, many wine producers felt threatened. But, importantly, with some transition assistance from the federal and Ontario and BC governments, many Ontario and BC growers undertook a major program to replace the low-quality native grape varieties with European vinifera grapes, not only to comply with trade rules but also to assure more competitive wines in the marketplace. The success of these efforts (notably one of transition cooperation between government and the industry) is clear. The removal of protection prompted major growth in Niagara, the Okanagan, and increasingly in other parts of Canada — and not just in producing high-quality wines, but also in spinoffs for tourism and associated benefits. “Rationalization of the industry has accelerated, productivity has increased, and the industry has become more export-oriented.” “Enterprising vineyards are producing quality wines, some of which have won international awards, and Canadians are consuming increasing quantities, both domestic and imported. Everyone is ahead: farmers, vintners, importers, and consumers.”

No country claims that it has no protection — almost everyone does to one extent or another. But trade negotiations are just that — negotiations — and they often deal not with questions of absolute protection or subsidization, but relative protection or subsidization. Each side looks for the best possible outcome for itself, so the parties engage in give and take, back and forth. Canada’s maintenance of supply management has damaged our credibility, as well as our ability to obtain market access. Each time we are at a negotiating table, we start off with one hand tied behind our back, one major bargaining chip already given up. It means we have to give other concessions or sacrifice other benefits for other industries and markets.

This is clearly problematic with the opportunities presented by the Trans-Pacific Partnership (TPP), currently being negotiated among the United States, Australia, Brunei, Chile, Malaysia, New Zealand, Peru, Singapore and Vietnam. Based on private reports from people directly involved, at least some of the countries have made it clear that Canada’s insistence on maintaining supply management is a major stumbling block — affecting whether we are even welcome at the discussion table, let alone able to join the partnership. Given that New Zealand has no dairy tariffs and is the world’s largest exporter of dairy products, and Australia only 10 years ago dismantled its own supply management system for dairy and is now exporting far more than before, those two alone could make a very good case against Canada. It is hard to imagine some of these countries accepting Canada’s full participation in the TPP without us either abandoning, or committing to abandon, supply management — particularly in dairy.

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48 Ibid. P. 6
49 This is less of a problem, for example, in the current trade negotiations with the European Union, partly because the EU has its own significant subsidies as part of its overall agricultural policy, which make it hard for Europe to point accusatory fingers at Canada. Indeed, the OECD analysis (2006-2008) of producer subsidy equivalent (PSE) shows the EU’s PSE as 27 percent versus 18 percent for Canada. It is harder to throw stones from a glass house. However, private reports from those involved in the negotiations suggest that our supply management is significantly affecting our bargaining power in certain sectors.
Yet it is exactly the growing markets of the Asia-Pacific region that present such opportunities for Canada. From a preventative perspective as well, participating in the TPP is key for Canada, because if Canada is absent, those who do participate will then have greater competitive access to some of those key markets. Not only will not being part of that group prevent Canada from capitalizing on the opportunities, it will hurt its existing competitive position. As a trading nation, this is important to Canada’s future prosperity. So too, for all the same reasons, will be the other bilateral and multilateral trade arrangements that Canada should be entering into, particularly with the large, rapidly-growing emerging economies. Maintaining our heavily protectionist supply management regime will be a recurring problem.

Looking at the agricultural sector alone, by far the majority of farmers in Canada would benefit from the freer international trade that would result from dismantling supply management. In Canada, over 210,000 farmers (92 percent of the total) are directly dependent on export markets; they either export their products or sell them domestically at prices set by international marketplaces. Producers of export-dependent commodities constitute a majority of farms in every province in Canada. Based on 2008 figures, 91.6 percent of all farms in Canada are export dependent, including 88 percent of all farmers in Ontario and 75 percent of all farmers in Quebec, notably the two provinces where the political influence of dairy farmers is assumed to be so strong.

Sales of export dependent commodities account for $25 billion, nearly 80 percent of Canada’s annual farm gate receipts. In all provinces, including Ontario and Quebec, sales of export-dependent commodities constitute a majority of the farm gate receipts.

Canada’s beef sector includes nearly 90,000 primary beef producers as well as value-added processors, and is active in every Canadian province. Collectively, they account for approximately 26 percent of Canadian farms (including 15 percent of farms in Quebec). The Canadian beef industry accounted for $6.5 billion, 20 percent of farm cash receipts in 2006. In 2007, Canadian beef was exported to 62 countries.

Canada has over 6,000 pork producers — approximately 2.6 percent of total farms. Despite their relatively small numbers, in 2006, farm gate receipts from pork producers accounted for over $3.4 billion, or approximately 10.5 percent of Canada’s overall total of $32.4 billion, including a significant portion of farm gate receipts in Quebec. In Quebec, they represent 6.3 percent of all farms.

Canada’s red meat processing industry is the largest sector of the food manufacturing industry, with annual revenues valued at over $16.3 billion and total employment of over 46,000 people in over 400 establishments, often located in rural settings. It is the 11th most important manufacturing sector in the country after such industries as motor vehicles, wood products and petroleum products. The industry is active in virtually every part of the country, with major concentrations of firms found in Alberta, Manitoba, Ontario and Quebec.

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51 Ibid.
52 Ibid.
Over 61,000 farmers (approximately 27 percent of all farmers), produce grains and oilseeds. (This includes 11 percent of all Quebec farms.) In 2006, farm gate receipts from these producers accounted for over $6.8 billion nationally, or 21 percent, of Canada’s overall total farm gate receipts of $32 billion. Canada is a major exporter of grain and oilseeds, ranging from the primary commodities through to fully processed products.

Canada is a key exporter of value-added products such as Canadian canola oil and meal, 75 percent of which is exported. The current value of these exports is estimated at approximately $1.2 billion annually. Canola is heavily dependent on trade and Canadian farmers are dependent on canola. Over 52,000 farmers grow canola and the crop generates between one-third and one-half of their revenues. The oilseeds processed by the industry are produced by 25,000 farmers located in the Prairies, Ontario and Quebec.

In 2007, CAFTA commissioned an analysis of the potential benefits that would flow through a WTO agreement to seven primary export commodities, including wheat, canola seed, barley and soybeans. The analysis, based on 2003-2005 average export levels, looked at the impact of tariff reductions and trade liberalization to determine the potential increases in export values. They found that “Canadian wheat and barley encounter substantial tariff barriers in key markets and around the world. Important markets such as Japan, China, the EU and Korea have substantial bound tariffs on wheat and barley that reduce access. Canadian canola also faces significant barriers to access in India and in China. Increasing access to these key — and growing — markets is essential for Canada’s grain and oilseed producers [emphasis added].”

While the WTO Doha Round still appears stalled, the importance of increased market access continues to grow, and Canada’s opportunities now lie with bilateral and regional multilateral agreements, including the TPP. These opportunities are significant (as are the potential negatives of not participating), but we have to be at the table.

THE AUSTRALIAN EXPERIENCE

Australia was the pioneer in supply management, having implemented it in the 1920s. In the face of both domestic and international market pressures and opportunities, Australia recognized that change was needed, and dismantled the system in 2001 — with considerable success all around. Canada borrowed from the Australians in creating its own supply management system; it can, and should, borrow from the Australian experience once again, this time to dismantle it.

There are differences in the Australian and Canadian situations, both in the actual system mechanics and in the political environment, but there are more than enough similarities for Canada to take a page from Australia’s book.

The reasons Australia implemented supply management in the first place were very similar to the ones in Canada — concerns over volatile markets, inconsistent supply and pricing, and the welfare of farmers.

But, like the concerns increasingly expressed now in Canada about Canada’s being held back internationally, the Hawke government in the 1980s and into the 1990s clearly wanted Australian industries in the sectors that were either affected by or were affecting international trade to face international market realities.  

As with Canada’s provinces, Australia’s state governments have responsibility for market milk (table milk and cream). State bodies had a monopoly on primary-level marketing of milk in their respective states. Prices for milk were set at levels that, as with Canada, were well above export parity. Because of state differences, different approaches were used; in Victoria, for example, because only a small portion of milk produced was for the higher-priced market milk, the state implemented a form of equitable marketing that allocated the large-price premium to all farmers. Other states like New South Wales where market milk was about half of total production, implemented market milk quotas, quota being needed to obtain access to the premiums available for fresh milk. For many NSW dairy farmers, once their quota became tradable in the 1990s, it appreciated in value to the point of, for many, several hundred thousand dollars (Australian). Sound familiar?

Reforms in Australia were begun in the 1980s. The commitment to phasing down assistance for the manufacturing sector of the dairy industry in the Kerin Plan reflected the economic rationalism of the Hawke Labor governments. It was consistent with reductions in protection initiated in other rural industries and in manufacturing. In 1986 the Dairy Produce Act began the phase-out of price support for domestic producers.

Inequalities immediately became apparent, because Victoria produced milk mostly for manufacturing for export, whereas, for example, New South Wales produced more market milk. Yet all states, territories and the Commonwealth Government entered the Competition Principles Agreement (CPA) in 1995, committing to review all laws restricting competition by 2000. Because of the different balances of market versus manufacturing milk and domestic versus export markets, Victoria’s national competition policy review came to a pro-deregulation conclusion, whereas those of NSW and other states with greater market milk balance did not. In the end, however, leadership was shown at the national level, where the decision was made to dismantle regulation.

Just as in Canada, the Australian government faced political challenges — at the time, not everyone thought this was a great idea. Wisely, it asked the Australian Dairy Industry Council for input. They had determined, based to a large extent on Victoria’s competition review, that dismantling the overall support system was inevitable, and the goal was how to do so in an orderly way. This recognition by the dairy industry was important. Those involved realized

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54 Interestingly enough, given the heavily protectionist stance of the Canadian NDP and the Canadian unions, Robert Hawke, Australian prime minister at the time, was a trade unionist, having served a decade as president of the Australian Council of Trade Unions.


56 Ibid. P. 81

that it would be better to participate, and maybe influence the outcomes, than to simply wait to be told what would happen. “While change would affect different parts of the industry in quite different ways, the whole industry was able to unite and develop and present a proactive ‘reform solution’ to government.”

Based on the request made by the industry for support for transition, the government agreed to a total of $1.6 billion in payments under the Dairy Structural Adjustment Program (DSAP). “The average payment to dairy farmers in New South Wales and Victoria under the package is estimated at $143,000 and $72,000, respectively, in 1998-1999 prices. The larger payments per farm in New South Wales reflect the greater importance of the more highly supported market milk outlet for farmers in that state.”

The payments were to be made in quarterly instalments over eight years.

There were also exit payments of up to $45,000 available to farmers who chose to leave dairying, and a Dairy Regional Assistance Program (DRAP) provided $45 million over three years to help dairy-dependent communities affected by deregulation. A smaller, additional package of $140 million was added a year later for farmers and communities most affected.

Key to the whole program was that it was funded, not from government funds (general taxpayers’ money), but by a levy of 11 cents a litre on all retail milk sales for eight years. In present value terms, the adjustment package was equivalent to approximately three recent years of transfers to dairy farmers.

The levy kept dairy prices higher for consumers and processors than international free market prices, true, but they were lower than the previously administered prices. It was, in effect, a smaller price to pay, and for only eight years. After the eight years, consumers and processors began obtaining the full benefit of the lower international prices. “Not counting the new 11 cents-per-litre tax, the decline in real terms has been 18% for brand-name milk and 29% for "no-name" milk. In the first year of the reform, savings to consumers on milk purchased in supermarkets are estimated at more than A$118-million annually.”

Although the package was criticized as inadequate by dairy farmers in some states, especially New South Wales and Queensland, all eventually accepted it. It was clear to the realists that the choice was between deregulation with a package and deregulation without.

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58 Allan Burgess, dairy farmer, Shepparton, Victoria, 2008, from Advancing Agriculture Reform in the EU and Australia. Australian Government, Department of Foreign Affairs and Trade, Department of Agriculture, Fisheries and Forestry, 2008


60 Edwards, G. 2003. Op. cit. P. 87. Edwards describes a number of examples indicating rather lax diligence as to where and on what DRAP money was spent on, but the premise is understood.

61 Ibid.

62 Petkantchin, V. “How Australia got out of supply management — A lesson for Canada: Milk prices fell from 18% to 29%.” National Post, February 8, 2006 P. FP-23.

What happened next?

In the first full year of deregulation, farm returns from milk fell 18 percent in Queensland and 12 percent in New South Wales. However, in the following two years of deregulation, the quantity of farm output increased by 26 percent in New South Wales, 18 per cent in Queensland and 19 per cent in Victoria. In reacting to the new market conditions farmers who stayed in the industry were forced to increase productive performance. Some expanded the number of dairy cows, while others increased their land area. Farmers that did not adjust herd size made changes to improve performance by changing the use of inputs such as fertilizer and irrigation to increase milk yields. Through farm adjustment and exit of the least efficient, yields improved. The end result was that the Australian dairy industry improved its international competitiveness. Total dairy product exports increased 200 percent in the years 1990-2002, correlating with the decline in industry support. Removing protection had a dynamic effect on productivity and reoriented the Australian dairy industry to a globally competitive export industry.⁶⁴

According to some analyses, by dismantling its supply management system, “Australia enabled its dairy industry to remain today one of the most dynamic in the world…Dairy producers acted quickly to compensate for income loss linked to elimination of support prices. For example, almost half of producers expanded their cattle herds; …others enlarged their farms, modernized their equipment or developed other areas of agricultural production. The competitiveness of the industry was thus enhanced.”⁶⁵

According to the Australian government, “As Australia liberalised agriculture, farmers and processors pursued their common interest in the productivity gains that made them competitive, including in growing export markets in Asia. Collaboration of this type was the catalyst for deregulation of the dairy industry — a sector Australians expected to be difficult to reform.”⁶⁶

EXPERIENCE IN NEW ZEALAND

The dairy industry in New Zealand, right next door to Australia, took a very different path from both Australia and Canada. It was farmer-owned and driven through cooperatives from the start, and still is today — all along benefitting from the power of pooled resources. It was also export-focused from the start; the first refrigerated shipment of butter in the world was made in 1871 from New Zealand to Britain.

The first cooperative was formed in that fateful year of 1871, and by the 1930s there were more than 400 dairy cooperatives. Still being export-focused, they had their own Dairy Export Produce Control Board, which later became the New Zealand Dairy Board. Improvements in transportation, technology and processes encouraged consolidation, and by 1995 the number of cooperatives had shrunk to 13.

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⁶⁶ Government of Australia. “Advancing Agriculture Reform in the EU and Australia.” Department of Foreign Affairs and Trade; Department of Agriculture, Fisheries and Forestry. 2008
However, although the export business was doing well, the threat of Britain joining the EU (which it did in 1973) had led the New Zealand Dairy Board to diversify both in terms of markets and products. As part of this effort to encourage more exports to more markets, a system of compensation for costs and support for exports evolved at home, in some cases worth as much as 40 percent of farmers’ incomes. This was not supply management, but rather a simpler system of tariffs and subsidies. A key difference, however, was that the money came from the government purse. Another was that the supports (and their subsequent removal) applied to all agriculture, not just one or two sectors. Over the years, it became increasingly costly to maintain, to the increasing discontent of the taxpaying public.

By 1984, politicians and, interestingly, the producers themselves, realized that these supports were clearly distorting the market, and that there were clear benefits to freeing things up. The supports were seen to be diverting government (and therefore taxpayer) resources away from other areas, and the supports were a disincentive to innovate and find efficiencies. In 1984, the government changed and in relatively short order, virtually all subsidies were eliminated. Not just for dairy, but across all agricultural sectors. “All of this was not achieved without some controversy, and there were a few casualties… It is estimated that around 800 farmers [mostly sheep farmers, as these changes were made to all agriculture] — or 1% of the total number of commercial farmers in operation — were forced to leave the land…those farmers who were heavily in debt at the start of the reform period were hit hard by rising interest rates, and a transition program was negotiated to ease their situation… Overall the ‘transition period’ lasted about six years, with land values, commodity prices, and farm profitability indices stabilizing or rising steadily by 1990.”

It is important to emphasize that although New Zealand provided subsidies to its agricultural industries, it never had supply management as in Canada and Australia. There was no accumulated value for quota, which in Australia did, and in Canada likely will, require a significantly more substantial financial transition arrangement. Also, although supports had developed prior to 1984, they had done so fairly quickly. The New Zealand dairy industry had already had, before supports were brought in, a strong history of open trade and capitalizing on exports. The New Zealand dairy sector is also unique, having successfully maintained its cooperative structure, which has permitted a strong marketing and distribution presence in world markets.

Indeed, more recently, the two then-largest dairy co-operatives amalgamated to form Fonterra Co-operative Group Limited (Fonterra) under the auspices of the Dairy Industry Restructuring Act 2001 (DIRA). As a co-operative, Fonterra is completely farmer-owned (by about 10,000 farmers). It, in turn, owns all the shares in the New Zealand Dairy Board. Two cooperatives, Tatua and Westland remained separate, and there are now several other dairy companies operating in New Zealand, but Fonterra collects and processes over 90 percent of raw milk produced in New Zealand. (DIRA has provisions to protect against the powers of monopsony that Fonterra would otherwise have.)


68 Ibid.
Today, without any trade protections or internal subsidies, but capitalizing on their co-operative structure, the dairy industry is New Zealand’s biggest export earner, benefiting from an efficient farming system, large-scale processing, high research and development investment and creative marketing. New Zealand produces about two percent of total world production — around 95 percent of its dairy produce is exported (compared to a mere five percent for Canada), accounting for about 44 percent of all traded butter, and between 27 percent and 38 percent of traded milk powder. With well over 11,000 dairy herds and about 4.25 million producing dairy cows, dairy is one of New Zealand’s largest industries, contributing approximately 25 percent of total merchandise export earnings (NZ$10 billion in 2008-09).

Of interest to the growing, but still-hampered artisanal cheese sector in Canada, premium speciality cheese products manufactured in New Zealand have increased substantially and there are now over 30 boutique cheese-makers, including prize-winning goats’ milk cheeses.\textsuperscript{69} \textbf{Canada’s producers and processors can compete, too, given the chance.}

New Zealand offers lessons both on the benefits of deregulation and elimination of support, but also on the benefits of cooperative organization, particularly for capitalizing on export opportunities.

\section*{Political Assumptions in Canada}

As we have seen, although implementing supply management was well-intentioned at the time, dismantling it is long overdue. All of the evidence shows that it causes consumers and processors to pay more for dairy products, the bureaucratic burden wastes money and other resources, the system creates all sorts of other economic distortions, and that it continues to seriously hurt Canada’s external trade opportunities, not only for the dairy industry itself, but for all of the other sectors that rely on exports. But despite the evidence, and notwithstanding the successful examples already set by Australia and New Zealand, successive governments have been unwilling to do anything.

Why? Unfortunately, good policy does not always make for good politics. Too often, getting elected takes precedence over policy. Many politicians acknowledge, privately, that supply management should go, but they say that they must continue to support it because there are too many votes at stake. Unfortunately, this perception highlights how one cannot underestimate the power of a good lobby. The well-funded dairy lobby (ironically, paid for by the higher milk prices consumers pay) has for years been extremely effective at leaving Members of Parliament and members of provincial legislatures with the impression (a) that the status quo for dairy farmers is extremely positive, very good for Canada (“supports the family farm”), and (b) (more persuasive to the politicians) that they are so numerous that doing anything to upset them would be political suicide.

But on both counts, this is simply no longer true.

Ironically, even if the numbers were significant from an electoral perspective, thanks to examples in Australia and New Zealand, eliminating supply management should not be something feared by dairy producers, but embraced. And because consensus is always better than unilateral action, politicians should work on those discussions. The last section makes recommendations on how to dismantle supply management in a way that could be reached by compromise with the producers themselves and/or by compromise with the other political parties. Doing so could eliminate, or at least significantly reduce, electoral concerns. Such a win-win solution is possible, and should be the approach taken. Antagonism is neither necessary nor beneficial. In the meantime, however, politicians need to know that, if all efforts at cooperation and persuasion fail, they can still take the necessary action with greater electoral confidence.

First, those long-held assumptions about the electoral strength of the dairy sector are simply no longer valid.

As we have seen, since 1971 (the beginning of supply management), the number of dairy farms has dropped a staggering 91 percent. In 2011, there were only 12,746 dairy farms in Canada.\textsuperscript{70} Not only are they far less numerous, the farms that are left are concentrated in electoral districts so predominantly supportive of one party or another that, even if a proposal to dismantle supply management were received so negatively that some people would change their votes, there are few if any electoral districts where those votes would be enough to change the electoral results.

By superimposing the Canadian federal electoral map of 308 ridings onto a map of Statistics Canada’s agricultural census divisions (Appendix A), and then by analyzing the electoral results of those ridings with a significant number of dairy farms (Appendix B), one can estimate how many votes might be swayed one way or another by the views of the dairy farmers (and those they influence) in each riding — and then consider which ridings, in the worst cases, might actually change hands in a way that would affect overall electoral results. Put simply, if the Conservative government were to take action on supply management in a way worked out with the dairy industry and which was ultimately supported, that would be preferable. But in the worst-case scenario, if the current government were to take action that members of the dairy community still objected to, how many ridings would they in fact be risking?

As it turns out, contrary to most assumptions, not many. Put simply, the dairy farmers, as wonderful as they are, do not represent the same political force that they might once have.

There are only 13 ridings in Canada with more than 300 dairy farms.\textsuperscript{71} And to put things into relative electoral perspective, these are ridings which have an average of 80,000 registered voters each. Eight of these are in Quebec, three of which (based on both the 2008 and 2011 elections) are held comfortably by Conservatives. Three are held by the NDP, two by the Bloc Quebecois, but in four of these, the Conservatives did not even come second, so the situation is not likely to change one way or the other. The other five of this group of 13 are in Ontario, strongly held by Conservatives, each by over 10,000 votes in 2011.


\textsuperscript{71} Based on Statistics Canada’s 2006 agriculture census. Given the continuing rapid reduction in the number of dairy farms, that number is likely now even smaller. Until, however, the next agriculture census is complete, we are unable to determine more current numbers by electoral district.
In summary, the eight Conservative ridings were Conservative in 2008, and then in 2011 went Conservative again, seven of the eight with a plurality of more than 10,000 votes and four with more than a 15,000-vote margin. These are very solidly Conservative ridings.

But what would have happened, in a worst-case political scenario for the government, if dismantling supply management upset the dairy farmers and their supporters enough to change their votes to another party in enough numbers to change the electoral results?

In 2011, the Conservatives won 166 seats, to 142 for all opposition parties combined. If the Conservatives had lost every one of the eight Conservative ridings in this group, the numbers would have been 158 to 150.

**They would still have a majority government.**

More importantly, all of this assumes that even if the dairy community was upset, no one else in these ridings would support dismantling of supply management, but that too is not true. On the contrary, there are many, many people (including many in agriculture) who DO want supply management dismantled and could (should) be encouraged to vote accordingly. We have seen in the section on trade implications the number of other producers of goods and services, including many resident in these ridings, who would benefit from greater market access for their exports. There is significant electoral opportunity in rallying those who would be supportive.

Remember that only dairy, poultry and egg farmers are under supply management. All other agricultural sectors — over 90 percent of all farmers — are not. Most of them, instead, would benefit from greater access to export markets, and therefore would support the dismantling of supply management. Once again, superimposing the federal electoral map onto a map of Statistics Canada’s agricultural census divisions, this time for non-dairy farms, we have determined that in every single one of the ridings in question, there are far more non-dairy farms than dairy (see Appendix A). There are far more farms that would benefit from dismantling supply management, and gaining increased trade, than there are dairy farms.

The political challenge is that they are not as organized as the dairy lobby (otherwise supply management might have already been dealt with). The reality, however, is they represent far more votes across the country, including in every one of these particular ridings, than do the dairy producers. But they need to be mobilized. By better communicating the negative effect supply management has on their trade, particularly their export opportunities, and by emphasizing the corresponding benefits of dismantling it, the policymakers and politicians who understand the need to dismantle supply management can work to improve the electoral support from all of these other groups, who far outnumber the dairy farmers. Although Appendix B shows the numbers for the specific ridings in question, recall from the discussion on trade that, nationally, there are 210,000 farmers in Canada who are directly dependent on trade — more than ten times the number of dairy, poultry and egg farmers combined.

Politicians must also rally the ire of the consumers who pay far more than they should for dairy. After all, they make up most of the average 80,000 voters in each of the ridings in question. Consumers need to better understand that they could be paying less for their dairy products — and that it is the poor who suffer the most. As we have seen, a family that buys an average of four litres of milk a week is paying up to $150 more than in the US, and that
doesn’t include the much higher prices for all other dairy products. The Conference Board of Canada estimates that supply management costs an extra $70 per Canadian. From a political perspective, that alone should be worth far more than the whole variety of family tax credits that have been offered in recent years to encourage votes.

Others who can and should be rallied to the cause include the well over 22,000 people employed in the dairy processing sector. Lower, market-based milk prices would help the dairy processing industry to be more cost-effective and more competitive, more likely to expand in Canada to service global markets, and thus create more jobs for Canadians. The restaurant industry, already vocal in its opposition to supply management, directly employs more than one million people, generates $60 billion in annual sales and accounts for four percent of the national economy.

Many other Canadian businesses rely to a greater or lesser extent on international trade, and would benefit from better access to international markets — particularly the rapidly growing developing economies that beckon via the Trans-Pacific Partnership. There is already considerable support in the various business communities for dismantling supply management, but they should be encouraged to participate more in shifting public opinion.

There are many, many people who could be encouraged to support, with their votes, a government or a party that advocates the dismantling of supply management.

RECOMMENDATIONS

Notwithstanding the electoral analysis, and no matter how few ridings may be affected one way or another, it would be far better to work with the dairy industry to achieve a solution that is accepted, even embraced, rather than forced. Done properly, the dismantling of supply management can be, rather than something that dairy farmers fear, something they can welcome. Indeed, the experience in both Australia and New Zealand suggests that, from the former, dismantling supply management can, in fact, be positive for the dairy producers, and from the latter, that dairy producers, by using their already strong organizational talents, can expand some of the existing cooperatives, and capitalize on much greater export growth opportunities. More importantly for the larger Canadian economy, we can level the field (pardon the pun) for the non-supply-managed sectors domestically, and allow them, other Canadian enterprises and the Canadian economy as a whole to benefit from greater access to much faster-growing international markets.

The time is now: Based on all of the foregoing, the clear recommendation to the federal and provincial governments is to, finally, dismantle supply management in the dairy, poultry and egg sectors. The federal government must make this decision soon, for purposes of trade negotiations where time is now of the essence.

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75 Agropur, one of Canada’s larger processors, is owned by 3,349 member dairy farmers. http://agropur.com/en/profile/
Develop a transition plan based on the Australian model: First, it must be made clear to all concerned that the dairy producers will be compensated and/or provided with transition assistance over time. What time frame (eight years? 10 years?) and what the amount of compensation or transition assistance would be appropriate requires a detailed analysis beyond the scope of this paper, but some transition is critical.

Who will pay for it? It would be extremely difficult in a time of spending cuts to have either the federal government or provincial governments pay compensation or transition costs out of the already limited public purse. However — and this was the brilliance of the Australian model — the system should remove all of the trade and market barriers, but impose a temporary levy per litre of milk, paid for by consumers. True, it would mean prices higher than consumers would pay with a completely free market, but they would be less than what they are paying now, and what they would continue to pay for years to come should the system not change. It would be a win-win approach to raising the necessary funds.

Engage the provincial and territorial governments: Just as there is federal-provincial cooperation in managing supply management, there should be cooperation in dismantling it and dealing with the transition.

Engage the dairy community: Right away, the government must engage in discussions with the dairy producers to assess and address concerns, to educate them on how the Australian approach worked, to help them understand the benefits of opening up the markets, and to ask for their input and ideas on possible transition scenarios — including those to assist the producers in expanding and taking advantage of export opportunities.

It is time for the Canadian federal and provincial governments, and the dairy, poultry and egg industries themselves, to act. Not only is it time to eliminate the domestic economic distortions and the too-high prices for Canadian consumers, the status quo is untenable for a trading nation like Canada, hampered in its trading negotiations by supply management. Opportunities for greater prosperity, both domestically and internationally, including for the dairy industry itself, beckon.
APPENDIX A

ELECTORAL MAP OF CANADA SHOWING THE NUMBER OF DAIRY FARMS PER RIDING.

Dairy Cattle and Milk Production by Federal Electoral District
In the 2011 election, of all 32 ridings with more than 150 dairy farms, in only one non-Conservative riding did the Conservative come second. Of those that went Conservative, most were by a large majority. Most of these ridings are either very Conservative, or very not.

In ALL of these ridings, there are far more farms with crops that would benefit from more trade, and therefore from dismantling of supply management.
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