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MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH

From the Minister

Prime Minister
Another direct approach from Mr Walker before there has been any discussion with the Treasury.
I have told MAFF that this won't do. I suggest we hold fire until we have the Chief Secretary's comments (and Mr Nott's).

What has happened to the reports - distributor's costs? We must have that before considering this

18 July 1980

PRIME MINISTER

[illegible]

Agreed

LIQUID MILK PRICES

I know you will have seen the Press reports that the two sides of the dairy industry have jointly requested us to increase the retail price of milk by $1\frac{1}{2}$p per pint on 3 August. They have argued that this is the minimum that must be done if both sides of the industry - the farmers and the dairy trade - are not to run into severe financial problems.

TL 22/7

I do, however, recognise how crucial it is to the Government in these coming months to keep any increases in the retail price index to the minimum. But I am certain that we must take some action and as quickly as possible, for I think you will see that the attached paper explains that without it there would be this year the most disastrous fall in producers' returns - down in fact to half of the lowest income in the last ten years.

But rather than purely comment upon the implications of giving the $1\frac{1}{2}$p increase on 3 August, I have tried to set out a series of options as to what would actually be available to us if we wished to try and maintain producers' returns at something near their low level of last year.

I hope that you will agree that this should be discussed either in Cabinet or an appropriate Committee.

I am copying this minute and the paper to the members of the Cabinet and to Sir Robert Armstrong.

Peter

PETER WALKER

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MEMORANDUM ON LIQUID MILK PRICES

Background

1. The returns of our milk producers depend upon the prices they receive from the liquid and milk products markets. The latter are determined essentially by decisions taken in Brussels on EEC support prices, but we ourselves fix maximum wholesale and retail prices for liquid milk. Because of the strength of sterling, there is no prospect at present of our improving returns from the products market through a green pound devaluation, so the only way in which we can boost milk producers' incomes this year is to increase the liquid price.

2. The need for such an increase can be seen clearly from the following table showing the net margin per cow in real and money terms since the first year of the last Conservative Government -

Year	£	Index (1970/71 = 100)
1970/71	29.9	100
1971/72	54.6	167
1972/73	61.0	174
1973/74	37.2	96
1974/75	27.4	60
1975/76	78.3	138
1976/77	52.2	80
1977/78	101.7	136
1978/79	95.1	118
1979/80	74.6	80
1980/81	27.0	24 (without taking further action on the price)

It will be seen that if we take no action on prices, the net margin for 1980/81 will be £27. Even in money terms, this would be the lowest figure in the whole of this period; and in real

The increase required to maintain producer returns at a level somewhat lower than that of last year would be:-

$1\frac{1}{2}$ pence on 3 August or
2 pence on 5 October or
$2\frac{1}{2}$ pence on 2 November or
3 pence on 7 December or
1 penny on 3 August and another 1 penny on 7 December or another $1\frac{1}{2}$ pence on 11 January.

The dairy trade and Binder Hamlyn

6. Any final assessment of the dairy trade's position will depend upon the decisions we take later in the autumn following the further work being done by Binder Hamlyn. In the meantime, they have had no increase in their target rate of profit since October 1978, and, on the basis of the system that has operated since January of that year, even the proposal advanced by the industry would leave their measured costs under-recouped by some £30 million. Therefore, unless we take action, they too will be in real difficulties this winter, and the viability of the distribution system, particularly in London, will be seriously at risk.

Scotland and Northern Ireland

7. Although the figures above relate to England and Wales, the position in Scotland and Northern Ireland is broadly similar. It should, however, be noted that in Northern Ireland (where a relatively large proportion of production goes to the less remunerative manufacturing market) the increase proposed in the wholesale price will leave returns there approximately 1.45 ppl or over 10% below those in GB. This is equivalent to over 50% of the net profit margin. If a serious loss of production and employment is to be avoided in Northern Ireland it will be necessary to make public funds available to top up the market returns there.

terms, it would be less than half the next lowest year of 1974/75 and less than one quarter of the average figure during the years of the Labour Government.

3. I do not believe this would be tolerable in political terms, or indeed in the national interest. In June, the dairy herd was some 65,000 head below the equivalent month last year. Applications under the EEC's Non-Marketing Scheme are running at record levels, those received already this year being equivalent to a further 160,000 cows. And, although the increase in the target price that was agreed as part of the recent CAP price package will add £19 million to producer returns in 1980/81, this will be more than offset by the £22 million they will lose from the increase in the co-responsibility levy. There can therefore be no doubt that action is urgently needed.

The options before us

4. The seriousness of the position has led the two sides of the dairy industry to make a joint request for an increase of 1½p per pint in the retail price on 3 August, with the additional revenue being divided equally between producers and distributors. Even this would fall some way short of meeting their needs. It would, for example, still leave the producer net margin 10% below that of 1979/80 (which, together with 1976/77, was the second lowest in real terms in the last 10 years).

5. I appreciate the sensitivity of an increase in the price of a basic commodity such as milk at the present time. However, even if we are merely to retain net margins this year within striking distance of the modest levels achieved in 1979/80, it is clear that an increase of the sort requested by the industry will be necessary. I am sure we will need to provide this. It is also clear that the sooner we act, the smaller the increase that will be needed to achieve any given effect. Thus:-