

## Milking the pricing system

### Despite fluctuations in the farm rate, supermarkets hold on to hefty profits

By Bruce Mohl, Globe Staff, 2/1/2004

The state's largest supermarket chains started charging more for milk when the farm price took a big jump last fall, but now that the federally regulated farm price has fallen, the retailers don't seem in any hurry to lower their prices.

Their reluctance may be understandable. The farm price jumped 24 cents a gallon in September and then another 5 cents over the next two months, but Stop & Shop and Shaw's Supermarkets raised the cost of their store-brand milks by only 10 cents to \$3.09 a gallon. Brand-name milks typically cost even more.

Still, supermarket chains were making hefty profits on milk before the fall run-up in farm prices, as much as \$1 a gallon by one estimate. The increase in the farm price only squeezed their profit margins, it didn't erase them. If the retail price remains at \$3.09 and the farm price keeps dropping, their profit margins would be bigger than ever.

"They kind of took a short-term hit for a long-term gain," said Ronald W. Cotterill, an agricultural economist at the University of Connecticut who has been critical of supermarket milk pricing and has pushed for legislation that would tie the retail cost of milk to the farm price.

Other retailers that historically offered lower prices for milk than the major supermarket chains have already reduced their prices. Costco Wholesale Club and Walgreen's have dropped their prices back to around \$2 a gallon.

A spokeswoman for Stop & Shop issued a statement indicating the chain is trying to decide whether to drop its price. "We're evaluating the numbers, and we'll make a decision shortly," the statement said.

At Shaw's Supermarkets, spokesman Terry Donilon indicated the chain was watching to see what its competitors do. "Shaw's will continue to watch the marketplace," he said, "and we are committed to remaining competitive, understanding the fact that consumers are price conscious."

With many dairy farmers struggling to turn a profit, the seeming disconnect between the price farmers are paid for their raw milk and the price retailers charge for the finished product has been a disputed issue in New England over the last two years.

Retail prices have been remarkably steady over that period. According to surveys conducted by the Massachusetts Department of Food and Agriculture, the retail price of milk at major chains in the Boston area has never gone below \$2.99 a gallon since October 1999. For a brief period in 2001, the price went as high as \$3.39.

By contrast, the federally set price farmers are paid for their raw milk has been extremely volatile. The so-called Class I price, which dairy processors pay to farmers for their raw milk in this area, began 2002 at \$1.33 a gallon and then plummeted to a 25-year low last spring when it reached \$1.13 a gallon. The farm price jumped to \$1.24 a gallon in August and then rose again to \$1.48 in September before peaking at \$1.53 in November. The price for February is back down to \$1.29 and is expected to keep declining.

Erik Rasmussen, the federal milk market administrator in Boston, said spring is typically the time of the year when milk prices are the lowest because supplies tend to be more plentiful.

Dairy processors like Garelick Farms and H.P. Hood are the middlemen between the farmer and the supermarket, but industry officials say the processors operate on negotiated profit margins and pass on to retailers any decreases or increases in the farm price.

To force supermarket milk prices to track swings in the farm price of milk, New York passed an antiprice-gouging law that sets a threshold for retail milk prices that is 200 percent above the farm price. The law bars retailers from selling above the threshold unless they can prove the price is justified as not being "unconscionably excessive."

The New York threshold was \$2.48 a gallon in July and soared as high as \$3.25 a gallon in November when farm prices peaked. The threshold has since subsided, with the February price set at \$2.79 a gallon.

Here in Massachusetts, Secretary of State William F. Galvin has proposed legislation that is similar to the New York law. His bill, which is opposed by the Romney administration and the state's supermarket chains, would require the state commissioner of agriculture to investigate any retail milk price exceeding 200 percent of the farm price and determine whether the price is "unconscionably excessive."

Galvin's bill received a hearing in September but hasn't moved out of committee yet.

Connecticut dairy farmers are also pushing their state to link retail and farm prices for milk. Bruce Grezyk, commissioner of the Department of Food and Agriculture in Connecticut, said his office has concluded that he cannot unilaterally implement retail price controls without legislative approval, which he indicated was unlikely anytime soon.

"There's a lot of work to be done by the industry to reach a consensus," Grezyk said.

## **Rebates galore**

Several companies are trying to build a consumer-friendly Internet shopping business off the customer referral fees paid by retailers. Butterflymall.com and Rebate

share.com are two firms that offer online shoppers cash back if they purchase goods through their sites. The two-step process is a bit of a pain, but a slick idea that will delight penny pinchers. Dan Sondhelm, president of Butterflymall, said it's customary for online retailers to pay referral fees to websites that deliver customers to them. Most websites pocket the fee, but Butterflymall rebates a portion of the money to the customer as an incentive to keep using the site.

Gap.com, for example, pays a 5 percent referral fee and Butterflymall returns 4 percent to the customer, so a \$100 purchase at the Gap costs only \$96 after the Butterflymall rebate.

"Yahoo and AOL get paid the same fee, but they keep it all," Sondhelm said. "We have the same stores. It's just that we give some back to the consumer."

Sondhelm said the most popular destinations for his customers right now are travel sites like Orbitz, Expedia, and Hotwire, and online dating sites like Lavalife and Metrodate. Sondhelm said some consumers have urged Butterflymall to add pornographic websites, but he says he wants to keep it family friendly.

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