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Managing Surpluses by Subsidized Diversion

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Most avocado growers had a branch-breaking crop going into the 1987 crop year. Had there been no January freeze and had we picked it all by October 31st, the crop could have totaled 640 million pounds. As it was, the 1987 crop totaled some 555 million pounds. That supply so overwhelmed the demand we had developed that the average price to growers dropped to about 17 cents per pound. The 1988 crop was only about 40 percent smaller; but the 1988 prices, for those who had fruit, more than tripled the 1987 prices.

The 1987 experience convinced many growers that in addition to programs to expand the total demand, we must be prepared to limit the total supply in an exceptionally big crop year. But how? Eliminating some sizes may be unfair to some growers and damage some markets. We can't trust volunteer withholding. We don't want the complexities and compulsions of citrus-type prorating. We shouldn't overwhelm developed export markets. Regional subsidized promotions might enable resourceful produce men to divert subsidized fruit to normal markets and hurt those prices. Changing the CAC assessment from an ad valorem to a per-pound basis would discourage excess picking, but be especially onerous in a big crop year. As a supplement to the commendable three-year market development program on which the California Avocado Commission is now embarked, it should be persuaded to reserve funds to be used in a very large crop year to subsidize the diversion of some fruit entirely away from regular marketing channels. How?

- Landfill dumping. This would be a last resort, opposed both by humanists and environmentalists. (But when the Israelis had an excessive 270 million pound crop, they dumped 70 million and received good prices for the remainder.)
- Hog food. Some hog feeders have been glad to get cull avocados when they were free.
- Soil conditioner. Dried and ground avocados could be used as a marketable soil conditioner to add organic matter and improve soil tilth. Perhaps the Avocado Society could conduct a small and economical test and demonstration of this use.

Any of these subsidized diversions would undoubtedly be more cost-efficient on a continuous basis throughout a big crop year, rather than done sporadically.

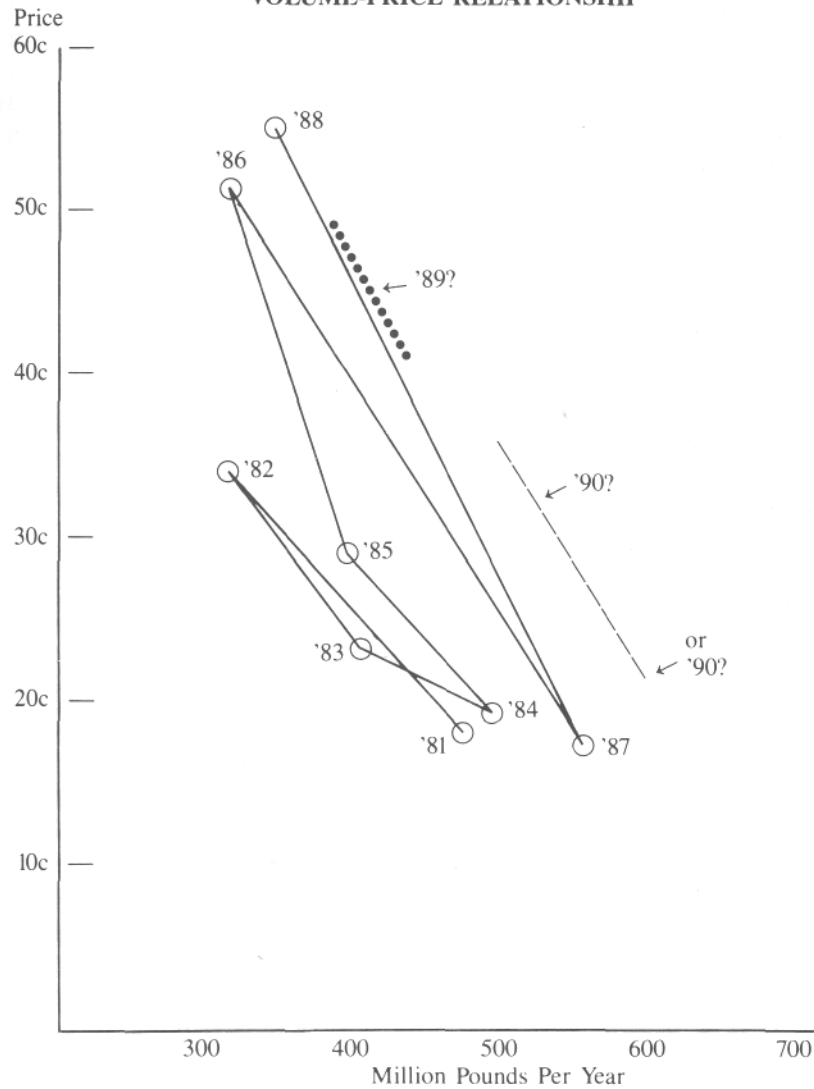
Diverted fruit could include blemished standards, small sizes, thrips-damaged fruit, less-desirable varieties, fruit nearing the end of its storage life, and ungraded fruit containing a normal proportion of culls—as well as glutted prime fruit. It must not include culls resulting from grade-out nor spoiled lots of fruit, either of which would have been dumped in the absence of a subsidy. Obviously, inspection would be required to prevent

payment for fruit in an unmarketable condition. Each shipment must be monitored to ensure that it is diverted in an authorized manner. It must not be exported nor processed into guacamole, oil, or dog food—any use which would compete with developed markets.

How should subsidized diversion be administered? The California Avocado Commission could establish a reserve for that purpose of, say, \$5 million. If 1990 (or a subsequent year) is estimated to have a 575 million pound or larger crop and initial prices portend an average price only in the 18-23 cent range (by Zutanos selling for less than \$6 per 25-pound carton), CAC could commence subsidized diversion. At a rate of \$100,000 weekly, CAC could invite packers to bid for payment increments of \$10,000 by stating the number of pounds they would divert from regular markets in exchange for such payment. (It has been suggested that individual growers should also be permitted to divert fruit for payment. That would require smaller payment increments and complicate inspection, but it is worth considering if CAC "buys" the general concept.) Once commenced, paid diversion should normally be continued throughout that crop year. However, CAC must be able to discontinue the program in the event of a major freeze. It should have the option of suspending the program temporarily (perhaps letting windfall fruit rot on the ground), and it should retain the right to reject all bids in weeks where they prove not cost-effective.

How much fruit would \$5 million divert? The more depressed the market price level, the more pounds each \$10,000 payment would eliminate from the surplus. Remember when packed Hass in August 1987 brought less than \$6 a carton? Earlier in 1987, standard Bacons brought 5 cents to the grower and standard Zutanos brought nothing. If hog feeders or a soil conditioner manufacturer will haul away for nothing, it is reasonable to assume that packers would rid themselves of marginally-marketable fruit in a glut year for an average of 10 cents per pound. A \$5 million diversion program in that event would remove 50 million pounds.

**CALIFORNIA AVOCADOS
VOLUME-PRICE RELATIONSHIP**



The dotted line representing the elasticity of demand predicted for the crop year ending in 1989 and the dashed line representing 1990 were plotted to parallel approximately the average slope of the lines connecting points representing the volumes and prices of the previous years since 1980.

It should be noted that the connecting lines indicate that at the 30 cents price level, the demand has increased by an average of approximately 25 million pounds per year. Reflecting that trend, the dotted slope representing 1989 demand and the dashed slope representing 1990 demand have been plotted to predict similar increases for those years.

What would elimination of 50 million pounds do for the price level? Referring to the accompanying chart, it will be seen that the slopes of the lines connecting high volume/low price years with low volume/high price years are remarkably similar, and

that they tend to move to the right (indicating greater demand at a given price) at a rate averaging approximately 25 million pounds per year. Eyeballing that, we derive a 1990 elasticity of demand indicated by the dashed line. That indicates that if CAC's planning assumption of a 525 million pound crop proves correct, it will average about 32 cents. But if an unfrozen 1987 crop could have totaled 640 million, is it unreasonable to fear the 1990 crop could total 600 million? As of November, trees with freeze-destroyed blossoms in 1988 were lusting to blossom and set in 1989. The demand slope in our graph predicts that a 600 million crop would average only 22 cents. If we could reduce the crop by 50 million pounds to 550 million, it should bring 29 cents. The crop value difference would look like this:

$$\begin{array}{r} 550 \text{ million pounds @ } .29 = \$159 \text{ million} \\ 600 \text{ million pounds @ } .22 = \underline{132} \text{ million} \\ \text{Difference} = \underline{\underline{\$ 27}} \text{ million} \end{array}$$

Not a bad return on a \$5 million investment.

CAC in 1987 spent extra millions on crisis advertising and promotions including support of last-minute "fire hose" promotions intended to reduce inventory glut at retail. Wouldn't it have been wiser to have removed surpluses steadily at the packing house level, before the fruit incurred costs of cartoning, shipping to chainstore warehouses, handling in those warehouses, distributing to stores, stocking store bins, and over-saturating advertising?

CAC's new three-year promotion program carries an \$8 million annual price tag, and it deserves full grower support. But the recent cut in the CAC assessment rate from 5.75% to 4.5% for 1989 regrettably would not provide for a \$5 million subsidized diversion reserve. We growers should press for the creation of such a reserve in future CAC budget decisions. And we should press CAC also for the adoption of the concept of subsidized diversion of portions of crops which, in spite of excellent advertising and promotions, may nevertheless prove to be in price-destroying surplus.