



DPAC's dairy farmer-run board—and additional dairymen representing five states altogether—discussed dairy policy at DPAC's March board meeting and milk pricing workshop in Lancaster,

## DPAC sets priorities at milk pricing workshop

### Part one in a two-part series

*Information is power, and if there was one overarching message from last Thursday's meeting of the Dairy Policy Action Coalition (DPAC), it was to press on from all angles with a primary focus on defining the markets and improving the transparency of them. This was a common thread in DPAC's dairy producer survey results, as well as the comments and insights offered by a panel of market experts during the coalition's milk pricing workshop.*

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LANCASTER, Pa.—Two panels, eight speakers, 20 dairy producers from Pennsylvania, Ohio, New York, Kentucky, and Tennessee along with a handful more on conference call from the East, Midwest and West... DPAC spent five hours distilling a wide range of facts, analysis, ideas and proposals into four achievable goals, while continuing their quest for information on other possible action items during the board meeting and milk pricing workshop here at the Farm and Home Center March 11.

After the fast-paced daylong workshop and board business meeting, a thoughtful outline of forward action emerged. Much ground was covered and much was learned, and at the end of the day, the dairy farmer board members of DPAC elected to put their primary focus on "achievable goals" and to develop a timetable and game-plan to influence not only congressional leaders and decision makers, but also to influence other influencers.

While the coalition's focus Thursday was on developing a unified voice for long term pricing reform, supply management proposals were also presented and discussed.

But as vice-chair Rob Barley said at the outset: "Our focus today is on milk pricing. Supply management is part of that, and we have a panel addressing it here today, but we want this meeting to kickoff the work of our supply management action group as they sift through it."

The milk pricing workshop was organized by DPAC's milk pricing action group chaired by Barley, who served as the workshop moderator. "Our goal today is finding out what we have total agreement on," said Barley. "We want to identify the things we can begin to have Denny Wolff contact the right people to get happening. We also want to identify the things we have consensus on and the things we need more information about."

The DPAC board did conclude the day asking themselves two questions: "Do we believe the pricing system must be addressed before or along with our consideration of some form of growth management?" And, "Do we want to work on 'fixing' the current system or to visualize a brand new system?" After discussion, they agreed unanimously to move forward aggressively on four key components of milk pricing, while they keep working on supply management in committee.

That's just a nutshell of the meeting attended by 15 of the 20 board members in person, along with two participating by conference call. In addition, dairymen from New York, Kentucky and Tennessee made the drive to Lancaster to participate in person:

Bryan Gotham from upstate New York, Jack Fritz from Tennessee and Bennie Sims from Kentucky. By teleconference the board hosted listeners and speakers at different points throughout the day from California, Indiana, Vermont, and Tennessee.

The teleconference hookup also facilitated some of the presenters in the two morning workshop panels.

The board first heard from their government relations consultant Dennis Wolff with an update on short term actions—mainly electronic reporting—which is the cornerstone of long term solutions related to milk pricing.

"We are continuing our dialogue with Adam Tarr at Senator Arlen Specter's office (D-Pa.). They are taking the lead in writing language to get the appropriations for the 2007 Farm Bill section on electronic reporting of dairy products," said Wolff.

"Senator Specter is working with Senator Herb Kohl (D-Wisc.) and Rep. Tim Holden (D-Pa.) on this."

Wolff said the timetable is to get the language for the appropriations written by the end of April so that it can be included in the budget process, which is heavily negotiated toward the end of the year.

"This is a significant segment of the last Farm Bill that will make a significant difference in price reporting," he said.

He also talked briefly about the informal feedback he had received from dairy economists on several pricing and supply management plans the DPAC board had asked them to review.

Preliminary results of DPAC's dairy producer survey were shared by the board's correspondence secretary, who reported that as of March 9th, 334 dairy producers from 23 states, representing 155,531 cows had responded by mail and website.

Survey responses were received from dairy producers milking anywhere from 20 cows to 15,000 cows, and the following

states were represented among respondents: Pennsylvania, Ohio, Maryland, New York, New Jersey, New Hampshire, Virginia, Kentucky, Tennessee, Georgia, Indiana, Michigan, Iowa, Wisconsin, Minnesota, Missouri, Texas, New Mexico, Colorado, Idaho, Oregon, Washington, and California.

Market transparency was ranked by 69% of respondents as one of their top three concerns, with 61% ranking market volatility in the top three and 55% ranking future profitability and market concentration in the top three. By comparison, only 28% ranked over-production of milk as one of their top three concerns.

By a wide margin, the top-ranked priority at 75%—across all regions of the country—was the removal of the influence of the thinly-traded spot market on the Chicago Mercantile Exchange (CME) by taking USDA National Agricultural Statistics Service (NASS) price reporting "to the next level" with daily reporting of more products. Other areas of widespread agreement were the highly favorable responses to evaluate the "make allowances" and yields built into the pricing formulas and the relationship of manufacturing class prices to regional fluid milk prices.

Among pricing concepts, 86% favored changing the make allowance when yield-boosting technologies like imported MPC are used in making cheese. 71% favored reducing the influence of manufactured product prices on the Class I fluid milk price, and 70% favored having a stronger mechanism for promoting regional Class I utilization.

The biggest area of agreement (77%) was for the elimination of traditional product price supports and government support program purchases to be replaced by solutions that encourage innovation and move milk to its highest value use. This distribution of favorable responses held up through all regions of the country. Only 6% of respondents opposed eliminating the price supports, and 16.5% were unsure. (More details about DPAC's producer survey will appear in the final report next week.)

The DPAC board and guests heard from two panels before lunch. The first was a market panel, where each participant gave the "top three things to think about" from their perspective on the dairy markets.

Market Panelists were: Bill Curley, a dairy markets consultant who grew up on a Susquehanna County, Pa. dairy farm, formerly worked for Dean Foods, and is today part owner of Blimling and Associates based in Wisconsin; Marvin Hoekema, a national dairy consultant with Dairy Decisions LLC based in Visalia, California, who grew up on his family's dairy farm in Washington State; Ed Gallagher, vice president of planning and regulatory policy for Dairylea Cooperative Inc. and Dairy Marketing Services (DMS), based in Syracuse, New York; and Kurt

Williams, general manager of Lanco Pennland Quality Milk Producers Cooperative, based in Hagerstown, Maryland.

"The CME is influenceable in the short term, even if it gets it right eventually over a period of weeks or months," said Curley in his market panel discussion of "big picture concerns."

If he had to pick just one thing to get done on dairy policy, it would be to move away from the CME spot market. "It's a real problem for the dairy business," he said. "We would be much better off without it. The CME spot dairy market (cheese, butter, powder) is not a functioning marketplace, and it's not doing buyers or sellers any justice. Unless this is fixed, there will be no meaningful improvement, no matter where we look."

The thinness of the market is the problem. If a couple loads are sold cheap, that drives down the price for 200 loads negotiated off that CME price, and this drops the farm milk price.

Curley said the best way to move away from the CME is to move toward daily reporting of actual negotiated transactions between buyers and sellers.

He also said the current "fixed make allowances stymie creativity in the manufacturing area and contribute to over production" because the make allowances, along with government support price purchases, funnel more milk into commodity production.

"We see a lot of inventory in block cheddar and nonfat dry milk," Curley explained. "The make allowances reduce processing risk dramatically and this creates a system that if a plant can convert milk to these commodities more cheaply than the 'average,' they are guaranteed a profit, which leads to the over supply we concern ourselves with."

An example is the southwest expansion in cheddar cheese production that is coming online, when the last thing the market needs is more cheddar cheese, and everyone's milk price will rise and fall with that.

Curley encouraged the dairymen to think about the current system, which incentivizes over production, but instead of adding another layer of inefficiency, "smartly unwind the system to get the producer more directly aligned with the customer to right-size the supply of milk."

The message here was finding new markets rather than building to blend a price that affects every dairy farm in the country.

The gradual changes to the Federal Orders over time have created pooling rules that reduce the cost of bringing outside milk into an area, by extracting value from that pool.

"The notion that cheddar cheese has a lot to do with what milk costs in the East is an idea whose time has passed," Curley added.

Marvin Hoekema kicked off his comments saying that, "It's important to fix the whole thing, not just a piece of it."

He too supported a roll back of the make allowances "to distribute a greater share of the price risk throughout the supply chain. Right now, the dairy producers have all the risk."

Better NASS reporting was also high on Hoekema's list, and he took the concept of electronic price reporting one step further: "We need to reconcile it," he said. "We need to know how much was sold as fluid and manufacturing."

Hoekema advocated for quarterly milk-flow reconciliation by NASS and the inclusion of 100% reporting on dairy commodity price points, along with a quarterly sources and uses report to know who is selling milk and where it is sourced and dispersed.

He also said the consolidation of pricing power must be addressed, and that it occurred more rapidly after the Federal Orders were consolidated in 2000.

Both Curley and Hoekema talked about the global markets as DPAC board members asked how much influence New Zealand's Fonterra has on U.S. exports?

"Their influence on our exports is 100% because they market 80% of what we export. They are the marketing agency (through a contractual agreement with DairyAmerica)," Hoekema replied. "Fonterra has 70% of the world market. Nearly 50% of those sales are from New Zealand and the other half is remarketing from other parts of the world, including from DairyAmerica."

In 2008, the U.S. powder price gained value before the end of the year. "Then our exports fell off the cliff once powder was sold to the government, and the effect was our powder price went from \$1.25/lb to 85 cents/lb in four weeks," he said.

So the problem is, when they need it, they get it from us, and when the don't need our product, they let it back up into the U.S. market. So DairyAmerica becomes the draw-point and the stockpile. "When Fonterra doesn't have a better date, we're a pretty girl," added Williams.

A few of the panelists referenced the "powder dumps" at the beginning of 2009 as also influencing U.S. milk prices. The government support price actually positions the U.S. as the world balancer.

From Dairylea Cooperative's perspective, Ed Gallagher confirmed that, "More information, faster, is always better, so electronic reporting is where we need to be," he said.

He also acknowledged that the make allowance on Class III offers an automatic margin for big new plants that have a "lower make."

"But those types of things are like taking a room with gray walls and painting it flowery colors," he said. "The bottom line is we would still have the price we have today."

Gallagher focused on fine tuning and income safety net to help control the volatility as the industry grows demand.

He also said that eliminating the price support program would help the U.S. avoid these protein surpluses that hurt demand for U.S. milk.

"Without the price support purchases, the MPC issue goes away," he said. "Right now the supports are a disincentive to making MPC and casein here in the U.S." But he also cautioned that an income safety net is needed to replace the price supports.

Gallagher gave a thumbnail sketch of DFA's Dairy Growth Management Initiative. "It's a supply management program with mandatory contribution to a private entity with a board made up of mostly dairy producers. This would be more flexible and responsive than a government board. The funds could be used for herd retirement, heifer reduction, and authority to use base / excess programs."

Kurt Williams gave his input, noting the number one issue "is defining our markets. We can't value our product without defining our markets," he said. "The CME is not a market. The CFTC acknowledges it's not a market."

Williams added that, block cheddar, a current driver, is diminishing in market importance as fresh cheeses, like mozzarella, grow in market share.

"They all pay Class III, and yet they make a higher value, higher moisture cheese that they don't hold or age," he said, likening mozzarella to the Class I market because it is a fresh product made to order. "You're not getting that value when you look at the return on mmozzarella."

Williams also talked about the Class I mover and location differentials. "Stabilizing the Class I price is important if we're eliminating the price supports," he said. And he encouraged DPAC to "be realistic on what can be accomplished."

To be continued in part two next week