62

Agri-Mark

Mailing Address: P.O. Box 5800
Lawrence, MA 01842
978-689-4442

August 2, 2005

Dear Member:

Cheese prices have weakened in the past two weeks due to concerns that national milk production was up over 5% in June. However, July heat appears to have slowed down milk production and the CWT has also begun subsidizing export sales to strengthen prices. I do expect cheese prices to move back up again, but the peak price may be lower than previously thought, as reflected in milk futures prices. New forecasts are shown on the back of this page. We will be following this closely and keep members informed.

It also appears that there will likely be another small MILC payment for September milk. Any members with large farms who have not yet contacted USDA-FSA to begin their payments for the current fiscal year should do so before August 15th. The MILC program expires at the end of September, but your ALEC Committee is working with others in the industry to get it extended for at least two more years.

In the last check letter it was mentioned that Agri-Mark was having problems involving the Federal Order Class III and IV prices. I thought it might be helpful to explain the situation in more detail:

The problems involving Class III (milk for cheese/whey) and Class IV (milk for butter/powder) prices began when the entire Federal Order pricing system was changed in January 2000. These problems are not unique to Agri-Mark, but effect all dairy product manufacturing plants that use milk pooled under Federal Milk Marketing Orders: they are a significant part of the reason why many Northeast manufacturing plants have closed in the past few years and more are likely to close in the near future. Solutions must be adopted not only to address Agri-Mark's problems, but to assure that all dairy farmers in the Northeast have nearby outlets for their milk.

Beginning first in 2000, Class III and IV milk prices have been determined by a series of pricing formulas never used before. Problems developed right away and hearings were held in 2001 to address those issues. New formulas went into effect in April 2003, but those changes still failed to address all the underlying problems. These continuing problems were brought to USDA's attention immediately, but they were not willing to re-open the issue at that time. However, the problem has gotten progressively worse and caused cheese production capacity to fall dramatically throughout the Northeast.

There are several specific problems with Class III and IV pricing, but the largest issue involves the new "end-product" pricing system. Under this new system, USDA uses a national survey conducted weekly by their NASS (National Agricultural Statistical Service) staff to determine the average price of cheddar cheese, whey powder, butter and nonfat dry milk. USDA then takes the monthly weighted average price of those products, subtracts a pre-set manufacturing cost allowance and adjusts by the yield of each product from 100 pounds of farm milk to finally determine the appropriate class price to be paid for milk.

A simplified example of this calculation would be as follows: If the NASS cheese price was $1.50 per pound, USDA would subtract the cheese manufacturing costs of $0.165 to get a milk value of $1.335 per pound of cheese. Assuming a yield of 10 pounds of cheese from every 100 pounds of milk, USDA multiplies the $1.335 by 10 to get a Class III price of $13.35 per cwt. The actual formulas are more complex and also involve whey powder prices and yields, but the method is still the same.

USDA fixed the manufacturing costs used in the formulas based upon limited plant cost data that is also more than five years old. Those costs also used California plant costs, even though those plants are not even subject to the Federal Order pricing formulas. USDA makes no adjustment for changes in plant costs despite requests during the hearing process from Agri-Mark and others. California formulas, on the other hand, can and do change regularly based on their annual plant costs surveys as energy and other costs have changed. As a result, California cheese plants pay far less for their milk than Agri-Mark and other Federal Order plants ($0.52 per cwt. less in 2004). It is no surprise that our local cheese plants are closing while California cheese production has risen 42% in the last five years!

Agri-Mark has tried to address the higher manufacturing costs in other ways as well. As a member of DairyAmerica, which sells about 80% of the nonfat powder in the U.S., a surcharge on powder prices to our customers was instituted earlier this year to reflect rising energy costs. However, when USDA found out, they insisted that the surcharge be included in the NASS price survey. The surcharge then increased the Class IV price for milk by powder plants, but not one penny went to cover the higher energy costs!

Agri-Mark has already presented information on these problems to USDA staff in several meetings in the past four months. We are seeking to have an emergency hearing so they can quickly consider putting in an annual manufacturing cost adjustment based on actual audited plant cost data. Agri-Mark will also be asking that USDA change two other problems with their Class III pricing formula. One involves a false assumption that whey butter can be sold at the Grade AA butter price, even though it is illegal for whey butter to be sold as Grade AA butter under USDA's own regulations. The other involves a three cent addition to the NASS 640 lb. barrel cheese price based on historical factors that have changed.

<u>If all three changes can be implemented, it will create a fairer price for milk used to manufacture all dairy products and reduce Agri-Mark operational losses by more than $5 million annually.</u> Currently, that $5 million is going into the Federal Order pool and unduly raising the milk prices to all dairy farmers in the Northeast, including those who have no investments in plants and equipment. We are also looking to submit a proposal to raise the Class I price differential to help offset any negative impact the Class III and IV price changes will have on farm milk prices.

As always, if you have any questions about milk prices, the class prices or any other issue, please contact me directly in the Methuen office at 1-800-225-0532. Within Massachusetts, call 1-800-423-4005.

Sincerely,

Robert D. Wellington

Robert D. Wellington
Sr. V.P. of Economics,
Communications & Legislative Affairs

2005	COMPONENT PRICES PER POUND: BUTTER FAT	PROTEIN	OTHER SOLIDS	BOSTON PPD/cwt.	BOSTON BLEND PRICE @3.5 bf	MILC FARM BILL PAYMENT*	CLASS PRICES (NORTHEAST): I	II	III	IV	FUTURES PRICES: III	IV
JAN	$1.733	$2.530	$0.090	$2.17	$16.31	$0.00	$19.90	$13.04	$14.14	$12.52		
FEB	$1.775	$2.661	$0.092	$0.81	$15.51	$0.00	$17.04	$13.36	$14.70	$12.74		
MAR	$1.728	$2.502	$0.095	$1.96	$16.04	$0.00	$18.68	$13.25	$14.08	$12.66		
APR	$1.696	$2.706	$0.102	$0.91	$16.52	$0.00	$17.38	$13.24	$14.61	$12.61		
MAY	$1.548	$2.597	$0.104	$1.58	$15.35	$0.00	$18.05	$12.78	$13.77	$12.20		
JUN	$1.593	$2.574	$0.114	$1.31	$15.23	$0.03	$16.87	$13.06	$13.92	$12.33		
JUL	$1.805	$2.472	$0.124	$1.21	$15.65	$0.00	$17.14	$13.80	$14.41	$13.17	$14.37	$12.90
AUG	$1.770	$2.212	$0.125	$2.26	$15.80	$0.00	$17.69	$13.76	$13.52	$13.07	$13.60	$13.05
SEP	$1.816	$2.445	$0.113	$1.31	$15.64	$0.06	$16.80	$13.94	$14.32	$13.17	$14.16	$13.10
OCT	$1.777	$2.514	$0.109	$1.52	$15.90	$0.00	$17.49	$13.74	$14.36	$13.01	$14.09	$12.80
NOV	$1.727	$2.409	$0.100	$1.87	$15.71	$0.00	$17.66	$13.55	$13.82	$12.67	$13.40	$12.80
DEC	$1.610	$2.416	$0.086	$1.82	$15.19	$0.00	$17.24	$13.02	$13.35	$12.06	$13.40	$12.80
AVG	$1.715	$2.503	$0.104	$1.56	$15.65	$0.01	$17.66	$13.38	$14.08	$12.69		

* capped at 2.4 million pounds of annual milk production

Agri-Mark

Agri·Mark

Mailing Address: P.O. Box 5800 Lawrence, MA 01842 978-689-4442

September 30, 2005

Dear Member;

This week, Agri-Mark economist Robert Wellington submitted his proposal to USDA for an emergency hearing to amend the Class III and IV pricing formulas used in all Federal Orders in order to correct for problems that are causing substantial losses to manufacturers who use such regulated milk. Selected parts of his written testimony are provided below. Interested members can contact the Membership Department or their field representative for a full copy of Wellington's testimony.

"On January 1, 2000, Federal Order Class III and IV pricing provisions began using fixed manufacturing cost allowances to determine the prices of Federal Order regulated milk paid by dairy products manufacturers. Those current cost allowances are set using cost information from two surveys using data from a 1998-2000 time period. Those rates have not been further updated despite rapidly rising energy, medical and other costs over the past five to seven years.

This proposal asks USDA to quickly update the manufacturing cost allowances using the latest data currently being assembled from the same two surveys initially used. While a longer term study to address this issue is being developed by Cornell University, the results of that research and the industry discussion surrounding it will likely take at least two to three years before it can be put into effect in Federal Orders. Several Northeast plants have already closed and the remaining manufacturers can not cover their costs; the situation will only get worse as recent events continue to raise energy, interest and other costs. An effective solution can not wait years!

...Two additional proposals will also be submitted by Agri-Mark for consideration in the same hearing. One reduces the addition to the NASS barrel cheese price used in the Class III protein price formula from three cents to one and one-half cents based upon actual price differences over the past several years. The other adjusts the protein price to account for the fact that whey butter has a lower value than the Grade AA butter price currently, and incorrectly, being used to value that by-product of cheese making.

These proposals are being sought on an emergency basis. Manufacturers using Federal Order milk can not pay the minimum prices for milk required and also cover their production costs under the obsolete allowances currently in place. Dairy product manufacturing plants are crucial outlets for local milk throughout Federal order milk marketing areas and also serve to balance milk supply and demand so Class I needs can be met..."

Cooperatives Working Together (CWT), the economic self-help program conducted by America's dairy producers in an effort to help stabilize farm-level prices, announced this week that it has tentatively accepted 448 bids from farmers to retire their milking herds. There will be approximately 66,000 cows removed, thereby eliminating 1.2 billion pounds of milk, or 0.7% of the nation's annual supply. In the Northeast, bids were accepted by 43 dairy farmers to cull 4,798 cows, reducing milk production by 93 million pounds annually. This represents about 8% of the region's milk production.

This week U.S. Agriculture Secretary Mike Johanns announced a series of Farm Bill Forums that he says are essential to the USDA's commitment to hear concerns directly from rural agricultural and development community leaders and to take into account those concerns when developing the 2007 Farm Bill. The announced meetings in the Northeast to date are:

Maine Farm Bill Forum
October 11, 2005; Time: 3:00 p.m.-6:00 pm. (EDT)
Richard E. Dyke Center, Bangor, Maine
Host: Rural Development Under Secretary Tom Dorr

New Hampshire Farm Bill Forum
October 25, 2005; Time: 9:30 a.m.-12:30 p.m. (EDT)
Manchester Center, Manchester, N.H.
Host: Rural Development Under Secretary Tom Dorr

(over, please)

Rhode Island Farm Bill Forum
October 14, 2005; Time: 9:00 a.m.-12:00 p.m. (EDT)
Coastal Institute, University of RI, Narragansett, RI
Host: Natural Resources & Environment Under Secretary Mark Rey

Vermont Farm Bill Forum
October 26, 2005; Time: 9:30 a.m.-12:30 p.m. (EDT)
Doubletree Hotel, South Burlington, Vermont
Host: Rural Development Under Secretary Tom Dorr

During the forum, the public will be invited to respond to one or more of the following six questions. All participants will be held to a 2-minute response time.

1. How should farm policy address any unintended consequences and ensure that such consequences do not discourage new farmers and the next generation of farmers from entering production agriculture?

2. How should farm policy be designed to maximize U.S. competitiveness and our country's ability to effectively compete in global markets?

3. How should farm policy be designed to effectively and fairly distribute assistance to producers?

4. How can farm policy best achieve conservation and environmental goals?

5. How can Federal, rural and farm programs provide effective assistance in rural areas?

6. How should agricultural product development, marketing and research-related issues be addressed in the next farm bill?

Agri-Mark will be testifying on behalf of members at these meetings, though all members are welcome to testify at their respective meeting if they wish.

Block cheese prices have held up higher than anticipated during the past few weeks, so farm milk prices during the next month or two will be up somewhat from what we previously forecast. We will have a new price forecast in our next check letter.

Also, as a reminder, the Agri-Mark holiday cheese sale is underway for members. Please have your orders in by October 7th.

Sincerely,

Paul P. Johnston

Paul P. Johnston
President and General Manager