



National Farmers Union

Testimony of Joe Logan

**Before the:
U.S. Department of Agriculture**

**Concerning:
Proposal to Amend Class III & Class IV
Make Allowance**

**Wednesday, January 25, 2006
Alexandria, VA**

STATEMENT OF JOE LOGAN

PRESIDENT, OHIO FARMERS UNION ON BEHALF OF NATIONAL FARMERS UNION

HEARING ON PROPOSED AMENDMENTS TO ALL FEDERAL MILK ORDERS

January 25, 2006

My name is Joseph Logan, I serve as the president of Ohio Farmers Union and am here today representing the dairy members of Ohio Farmers Union as well as all the dairy members of National Farmers Union.

Dairy producers and cheese processors are partners, each dependent upon the other. However, both, not just one or the other, must sustain profitability to achieve a healthy dairy industry. Farmers receive no assurance of profitable milk prices under federal orders, why should processors be given special treatment? Farmers Union opposes the proposals outlined by USDA to increase the make-allowance for processors because we believe it gives an unfair advantage to processors and will be economically harmful to producers. Increased energy prices in 2005 have taken a toll on everyone across the country, including dairy farmers, not just the processor segment of our industry.

Producer Income vs. Expenses

USDA has estimated 2005 farm net income to be \$71.5 billion, down \$11.1 billion from the 2004 estimate. This is a 13.5% decrease in net farm income from 2004-2005.

Higher Production Expenses:

- Total production expenses for 2005 are estimated to rise 5.8%, to a total of \$221.9 billion. This includes purchased input costs which increased 5.8% as a result of higher energy costs on fuel and fertilizer.
- The \$12 billion increase in expenses would be the largest annual increase since the \$20 billion rise in 1979.
- Rising costs of energy-based inputs and increasing interest expenses will account for 60% of the increase in 2005 expenses.
- According to ERS, fuel, lube and electricity costs have increased for **Ohio** dairy producers 45.90% in 2005 over 2004.

The Agricultural Marketing Agreement Act of 1937 requires that the establishment of milk prices be conducted according to the following language: “when the national parity price for milk does not adequately reflect the price of feeds, the available supplies of feeds, and other economic conditions which affect market supply and demand for milk in

the marketing area to which the marketing agreement order relates, he shall fix such prices as will reflect such factors, insure sufficient quantity of pure wholesome milk, and be in the public interest.”

We believe the current milk pricing policy being followed by USDA, and the hearing proposals, fails to take into account dairy producers’ production costs as a factor to determine or adjust the value of milk. The scope of public interest concerning the dairy industry today has also taken on a new meaning. Public interest no longer only involves a milk supply for fluid consumption. Dramatic increases in our consumption of processed dairy products show this to be true. America’s consumers rely on manufactured dairy products, as well as fluid milk, to be readily available in the stores at reasonable prices.

A milk pricing system that is balanced requires that dairy product prices, producers' cost of production, and plants' cost of production (make allowance) all be given consideration when determining the value of milk. Each of these items sends signals to one another in a free market environment, so that proper adjustments can be forthcoming. In the current milk pricing system, one of these entities has an unfair consideration; the make allowance is set at a certain level. The make allowance situation allows the processing segment of the industry to be unconcerned with market signals.

A dairy industry that is balanced and market-oriented should be the goal of any milk pricing hearing. However, market signals need to flow to both the producing and processing sectors of the industry for this goal to be realized. Economic and marketing conditions are an important element of this hearing, however, the current USDA Class III and Class IV milk pricing formulas based on dairy product commodity prices lack a full acknowledgement of economic and marketing factors affecting all segments of the industry.

USDA Proposals to Increase Processor Make-Allowance

According to the three scenarios proposed by USDA, all Federal order class and blend prices fall, the U.S. all-milk price falls and dairy product prices increase. With all three scenarios, both producer and consumers are the losers.

Under Scenario #1: Producer revenue falls by \$72 million on average per year.

Under Scenario #2: Producer Revenue falls by \$140 million on average per year.

Under Scenario #3: Producer revenue falls by \$207 million on average per year.

Under NO scenario proposed does producer revenues rise, despite evidence that production costs are increasing in a manner comparable to processors.

Farmers are the only segment of the economy that does not have the ability to pass increased production costs forward. We are price takers, not price makers. While the make allowance for processing may need adjustment, it should not be done at the expense of producers.

Producers should be paid for milk based on the class of product for which it is used, i.e., if milk is turned into non-fat-dry powder but then used to make cheese, the producer should be paid based on the cheese value. USDA may need to implement procedures for further verification as to the use of the milk.

National Farmers Union proposes that the Class III & Class IV make allowances be established in a market-oriented fashion. The cheese, dry whey, butter and nonfat dry milk make-allowances are to have a base make allowance level, set at the weighted average manufacturing costs determined by the USDA Rural Business-Cooperative Service and adjusted on an annual basis. The cheese and whey base allowances are to be adjusted according to the relationship between a cheese-whey powder reference price and producers cost of production. The butter and nonfat milk base allowances are to be adjusted according to the relationship between a butter-nonfat powder reference price and producers cost of product.

This make allowance proposal is directed by market conditions, which the current formula lacks. The current formula forces all market price volatility onto the producer's milk pay price. The challenge for USDA is to develop a system that will link the profits of processors and producers, to give each the proper market signals and incentives to produce a healthful supply of dairy products. Linking the make allowance to producer costs and prices will help USDA ensure a sustainable system for future generations.