

## TESTIMONY OF LAKEVIEW FARMS WITH RESPECT TO PROPOSAL 21

## 2023-24 FEDERAL MILK ORDER HEARINGS

## DOCKET NO. 23-J-0067; AMS-DA-0031

Good morning. My name is Kyle Powell and I am the Vice President of Procurement for Lakeview Farms, LLC. I have been in the food industry my entire professional career. I spent 17 years with the Kroger Co in Cincinnati OH and 3 years with Dairy Farmers of America in Kansas City, KS prior to Lakeview Farms. I have a Bachelor of Science degree in Food / Agri Business from The Ohio State University and a Master of Business Administration (finance) from Miami University (OH). In my current role, I oversee all procurement functions within Lakeview Farms. Lakeview Farms is a food processor with headquarters in West Chester, Ohio and production facilities in Delphos, OH. Lakeview Farms produces Class II end use products such as refrigerated dips, puddings and kefir.

The increase of \$0.86/cwt to \$1.56/cwt will affect how processors purchase dairy milk based products, and most importantly, how retailers pass on new costs to consumers. Dairy costs within Class II are typically passed through to the customer. With the increase in the Class II differential, these costs will move right to the customer. On-shelf retail pricing will reflect the change in the price of farm milk which could significantly impact the omnichannel strategy, specifically, retail and online. While producers may benefit from a greater pool draw, consumers will feel less inclined to buy multiples or become repeat consumers if prices become higher. Class II product sales generally benefit from consumer behavior where multiple purchases are made within a household visit (e.g., yogurt, pudding, cottage cheese, sour cream). Increases in the Class II differential combined with higher premiums due to elevated demand within Class II could limit households consuming these goods.

The increase in farm milk differential has the ability to negatively disrupt the entire dairy supply chain. The extra costs could affect 2 primary aspects of commercial Class II processor production, innovation and domestic dairy usage. During COVID, innovation took a back seat as food and feedstock processors scrambled to keep material moving through the omni-channel. The logjam of innovation continues to lag as some inputs continue to be in short supply and higher costs. Should the differential increase another \$0.86/cwt. (e.g., +200%), processors will accelerate ways to save on costs of goods. Processors are challenged by retail merchandisers every year to cut costs while typically passing on dairy costs. Other fat sources have been used to replace dairy fat in the past with successful commercialization (e.g., palm, soy). Retailers are asking for more oil-based formulations to offset the price volatility of dairy fat. Overall consumer tolerance of substitute dairy fats will cross when the price of non-standard identity dairy products (e.g., dairy dips, dairy dessert) exceeds the value to the customer. Should innovation ramp up without using Class II dairy, US dairy should continue to expect to be left behind on cutting-edge innovations (e.g., coffee creamers, half and half).

Liquid inputs typically are more desirable in spoon able Class II retail product. Mouthfeel and solubility of dry ingredients are sensory traits picked up in the trials. Should dairy inputs be the strategic decision for processors, savvy buyers will arbitrage the market to the best of their availability. Arbitrage opportunities could limit annualized agreements for Class II milk suppliers, leaving them to ship to balancing plants rather than a higher-value Class II sale. Processors will look to pile up on NFDM in times of surplus and purchase condensed skim milk at less than desired premium levels. The possible increased importing of nonfat solids would be a bigger option for processors. The opportunity to arbitrage could lessen the impact of the increased regulated pool value of Class II.

Given the possible paths processors can take, I challenge the increased pool value of \$122M. In AMFB's proposal it does not appear to address new pool benefit as a net value. The possible increased appetite for dairy substitutes should be quantified within overall impact (both near and long term). Further, Class II skim saw an increase of overages of over 30% during Covid-19 due to the incredible demand within the retail space. This is an example of a true premium, allowing the economics of the environment to set price as demand surged. Setting non-market differentials does not set up a healthy supply / demand price relationship.

Class II is one of, if not the number 1, most innovative spaces within the dairy complex. The opportunities for growth are endless if costs are under control and remain competitive with alternatives. We have seen the erosion of natural dairy in end-use products erode over the years (e.g., cheese dips, dairy dessert) due to costs. I urge USDA to keep the current Class II differential with no changes in order to support the growth and innovation of US Dairy.