Agri·Mark FAMILY DAIRY FARMS ®

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Testimony for the USDA Federal Milk Marketing Order Hearing
In Support of NMPF Proposal to Update the Federal Milk Marketing Order Make Allowances
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Thank you for allowing me to speak with you today. I am Catherine de Ronde, Vice President of Economics and Legislative Affairs for Agri-Mark, Inc. (Agri-Mark). I have been with the cooperative for six years; three in my current capacity, and three as the cooperative's economist. My responsibilities include watching dairy market trends, forecasting milk prices, and working on state and federal legislation affecting Agri-Mark members. Prior to joining Agri-Mark I worked as an agricultural economist with the Massachusetts Department of Agricultural Resources. While with the Department, I worked with a variety of agricultural industries, most notably the dairy industry. I have a bachelor's and master's degree in environmental science and resource economics from the University of Connecticut.

Agri-Mark is a dairy cooperative owned by approximately 550 dairy farm families in New England and New York. Our members are pooled in Federal Order 1. Our cooperative has been marketing milk for dairy farmers since 1916 and has headquarters in Andover, Massachusetts and in Waitsfield, Vermont. Our farm families supply more than 3.2 billion pounds of milk annually that we use to make our award-winning Cabot branded cheeses, dairy products, and ingredients. Agri-Mark operates three cheese manufacturing facilities located in Cabot, Vermont; Middlebury, Vermont, and Chateauguay, New York. These are pooled supply plants. In addition to cheese, the Middlebury, Vermont plant also produces valuable whey proteins that are marketed around the world. Agri-Mark also operates a butter-powder facility in West Springfield, Massachusetts that is a non-pooled supply plant. Lastly, Agri-Mark supplies fresh fluid milk to the region's largest dairy processors.

My testimony today is on behalf of Agri-Mark and our 550 farm families. Milk pricing is front and center for our farmers, particularly given the market volatility of the past few years. We thank USDA for granting this hearing and for the opportunity to testify today.

Agri-Mark, along with 15 other dairy cooperatives, served on National Milk Producers Federation's (NMPF) Task Force focused on Federal Milk Marketing Order (FMMO) modernization over the past many months (nearly 2 years now). Agri-Mark is in support of all aspects of the comprehensive NMPF FMMO modernization proposal.

My testimony focuses on our support of Proposal 7 submitted by NMPF, to update the FMMO make allowances in each of the component price formulas.

Of all the modernization pieces the NMPF Task Force reviewed, updating make allowances was by far the most challenging topic. The Task Force spent months evaluating different data sources and methods to update the cost data we had. Despite the challenges, it became apparent quickly that the dairy industry needs a new, consistent, and accurate method to collect robust cost of processing data.

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FMMOs are intended to meet several objectives, including promoting orderly milk marketing. Through end-product pricing, raw milk prices are determined via a series of economic formulas. If any aspect of those economic formulas is not reflective of the marketplace, the resulting calculated prices will be unsuitable, and disorderly marketing may occur. This may be easiest to illustrate using make allowances, which were last updated in 2008 using 2006 cost of processing data. While the FMMO make allowances have remained fixed, actual manufacturing costs have increased over the past fifteen years, resulting in overvalued FMMO prices. Impacted manufacturers are forced to solve for this with individual solutions. However, solving for make allowances at the manufacturing level, versus the FMMO level, creates discrepancies in producer pay prices within the same marketplace. Increased costs of manufacturing must be addressed through FMMO make allowances now and often in the future to correct for cost discrepancies and maintain orderly markets.

Agri-Mark supports NMPF's legislative efforts to provide USDA with the authority to conduct mandatory and auditable costs of processing surveys every two years. Granting USDA this authority legislatively will provide a robust, accurate and timely source of processing cost data for the industry to evaluate. Hearing requests can be made if the survey data suggests make allowances may be unrepresentative of actual processing costs. In the absence of this data, maintaining accurate FMMO pricing is a challenge. With widespread industry support for this effort, we are confident that this authority will be granted.

With published, audited processing cost data derived from mandatory surveys, the industry will be much better positioned to make educated decisions on make allowances in the years to come. However, current make allowances are extremely out of date, and the industry needs an interim fix. We cannot wait. The sense of urgency is widespread, but particularly crucial to cooperatives with Class III and Class IV manufacturing assets. These cooperatives, including Agri-Mark, struggle to maintain profitability while paying members minimum announced milk prices. These cooperative members face financial burdens beyond those without manufacturing assets. An interim fix is required to return to orderly markets.

Agri-Mark supports NMPF's proposal to increase the make allowances incorporated within the component price formulas as follows:

Butterfat	From \$0.1715 to \$0.21 per pound of butter
Nonfat Solids	From \$0.1678 to \$0.21 per pound of nonfat dry milk
Protein	From \$0.2003 to \$0.24 per pound of cheddar cheese
Other Solids	From \$0.1991 to \$0.23 per pound of dry whey

These numbers represent per pound increases of \$0.0385 for butter, \$0.0422 for nonfat dry milk, \$0.0397 for cheese, and \$0.0309 for dry whey.

Agri-Mark supports Proposal 7 submitted by NMPF. Agri-Mark acknowledges, as does NMPF, that from a pure manufacturing perspective, the proposed make allowances are not adequate and will not cover the full increase in costs of processing Agri-Mark and many other Class III and Class IV manufacturers have incurred since 2008. These increased costs, instead of being captured in a make allowance, are transferred to members via lower returns and pay price adjustments. Further, they stymie cooperative's ability to invest in the future. As a cooperative, we must balance the financial needs of our manufacturing assets and member pay price implications. The result from an overdue change in make allowances will be dramatic in and of itself. Agri-Mark views Proposal 7 as the first step in the right direction, providing some financial relief to manufacturers, while ensuring a reasonable producer impact. Paired with a legislative fix to conduct future costs of processing studies, Agri-Mark holds that this two-step approach is the best for the industry at large.

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Other NMPF witnesses have testified to the numerous data sources evaluated by the NMPF Task Force over the last nearly two years. Those include studies by Cornell University, the California Department of Food and Agriculture, and the University of Wisconsin. Each have its limitations, but all show a clear trend. Manufacturing costs of butter, nonfat dry milk, cheddar cheese, and dry whey have increased since 2008. NMPF and others have conducted trend and regression analysis on these costs and have reached the same conclusion.

An analysis of Agri-Mark's cost of manufacturing tells a similar story. Costs of processing across our four plants have increased on average 20 percent since 2008. Increases are found across all cost categories. Most recent and notable are increases in cost of insurance, manufacturing labor and benefits, and repair and maintenance. Agri-Mark has made investments in our plants to improve efficiencies and reduce costs of processing, however these noted increases are in categories that are largely market-driven and outside of our control. For instance, insurance premiums have increased tremendously in response to general conditions in insurance markets. Regarding repair and maintenance, we continue to spend money to upgrade and keep our plants going, however increases in supplies and labor are more expensive. Lastly, labor is critical to our operations and continued investment in our employees is essential. Costs of labor and benefits must be competitive and move with the local markets.

Our three cheese plants produce cheddar cheese, in a mix of 40-pound blocks and 640-pound blocks. Cheese produced is sold as a mixture of branded and commodity cheese, through a combination of retail, private label, and food service channels. Our Middlebury, Vermont plant processes all the whey generated by the three cheese plants, and produces dry whey, whey protein concentrates and whey permeate. Costs of processing vary by plant, based on plant volumes, efficiencies, and product mix. On a weighted average Class III basis, these three plants have seen costs of processing increase 23 percent since 2008.

Our butter/powder plant in West Springfield, Massachusetts produces retail, private label, and food service butter, as well as commodity nonfat dry milk. Cost of processing have increased 17 percent on a Class IV basis since 2008. It is worth noting that our West Springfield facility has a long history of balancing milk in Federal Order 1. In recent years, as the Northeast has become long in milk and Class I utilization has decreased, this dynamic has shifted. Today West Springfield often runs at full capacity. In the future however, as additional capacity comes on, we expect West Springfield to return to its critical function of balancing the Northeast market. While we recognize the essential role this plant has to the region, we also are keenly aware that it is a service that comes at a higher cost of processing to Agri-Mark and its member-owners.

Summary:

In summary, all data sources point in the same direction, i.e., manufacturing costs have increased since 2008. Today's make allowances are inadequate for all four commodities and are leading to disorderly marketing conditions. Agri-Mark supports Proposal 7 submitted by NMPF because it strikes the right balance of addressing the needs of manufacturing plants and producer pay price implications, in a way that minimizes disorder in the marketplace. Agri-Mark is supportive of the two-step approach NMPF has outlined in its proposal to update make allowances:

1. Provide an interim increase to alleviate the acute problems and disorderly market conditions created by the current, clearly insufficient make allowances.
2. Enact the authority for the Department to conduct mandatory, auditable plant processing cost studies, conduct such a study under that authority, and present the resulting data to the industry, which will

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enable interested parties to make requests for further make allowance adjustments on the basis of proper and adequate data.

3. Continue to conduct and report plant processing cost studies regularly and systematically under the same legislative authority and mandate.

The impact of increasing make allowances on producer pay checks is well known. Agri-Mark does not take this impact lightly. Likewise, the financial stress of outdated make allowances on cooperative profitability is well known. Agri-Mark members have invested in their cooperative and manufacturing capacity for over 100 years. We look forward to continuing this legacy.