PR-1947

DREYER'S GRAND ICE CREAM

TRANSMISSION SUMMARY SHEET - (510) 601-4403 (FAX)

TO: USDA - Docket DA-97-12 FAX: (202) 690-3410

FROM: Tom McAlone

DATE: April 30, 1998

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Attached please find the comments of Dreyer's Grand Ice Cream regarding the Federal Order Reform - Proposed Rule.

Sincerely,

Tom McAlone
Director of Materials

Call me at (510) 601-4331 if this transmission is faulty.

cc: John Casella, Trish Corby

MAY 1 1998
RECEIVED

WRITTEN COMMENTS

of
Tom McAlone
on behalf of

DREYER'S GRAND ICE CREAM

Regarding

Docket Number DA-97-12

Comments on The Federal Order Reform Proposed Rule

Areas to be Covered: Our comments will be focused on the proposed price formulas for Class II and Class IV prices.

Introduction: My name is Tom McAlone. I am the Director of Materials for Dreyer's Grand Ice Cream. We are located at 5929 College Avenue, Oakland CA. 94618. I am responsible for dairy forecasting and government relations. Dreyer's is the leading premium ice cream processor selling to the retail grocery trade in the United States under the Dreyer's, Edy's, Portofino and Whole Fruit brand names. We also manufacture and distribute all Healthy Choice and Starbucks ice cream sold in the United States. We employ 3000 people in 5 manufacturing plants, 2 in California and three in Federal Order markets, 30 distribution centers and our home office. We produce over 100,000,000 gallons of frozen dairy desserts annually. Dairy ingredients, milk, cream and condensed, are our largest single purchase. We utilize over 1 billion lb. of milk on a milk fat equivalent basis annually.

Key Principles: We are a member of the IDFA(International Dairy Foods Association) and the IICA (International Ice Cream Association) and support the written comments submitted by the IDFA. As ongoing proponents of increasing the free market orientation of all dairy markets, we feel that the principles outlined below:

(1) Bringing increased market orientation to the regulations is essential

(2) Prices established in California for milk used for butter, nonfat dry milk and cheese should be strongly considered in establishing Federal order prices

(3) Incorrect differences between prices of each class can cause substituting of lower valued products in higher priced classes resulting in unnecessary uses. Therefore, careful attention needs to be given to those products where the proposed Rule fails to recognize the impacts of substitution and end use.

are key to developing a market-oriented final rule which was the challenge set forth in the 1996 FAIR Act.

Overview: We feel that the Federal Order proposed rule for Class II establishes a framework and structure that will result in an excellent final rule provided key inputs and the growing consensus on Class IV pricing are incorporated. Given the divergence of opinion that has characterized debate on these issues for at least 10 years, this is no small feat. We would caution the Department, however, that as written, the proposed rule with its significant price enhancement based on low make allowances would cause significant problems for ice cream processors if adopted as it currently exists in the final rule.

Class IV Prices: Establishing a separate class for milk going into butter and nonfat dry milk, basing the pricing on the end product market place, and using Class IV pricing as a basis for Class II all support the key principles and should result in a excellent final rule. Recognize that the key factors in the pricing formulas (make allowances and yields) need to be adjusted as the factors as proposed would distort current market relationships and unduly enhance producer income. Fortunately from our perspective, both the IDFA and the NMPF(National Milk Producers Federation) , the key producer organization, agree that substantial changes are needed in key factors such as the make allowances and yields. We would urge the USDA to fully incorporate this industry consensus into the final rule. Dreyer's has had a positive experience (both up and down with the non fat dry milk price index in California) where the nonfat dry milk survey price is both mandatory and volume weighted. We would strongly recommend the NASS survey methodology be enhanced to include mandatory reporting and volume weighting.

Class II Advanced Pricing: Again we find ourselves encouraging the USDA to include the industry consensus supporting advanced pricing on Class II milk as represented by both the IDFA and NMPF positions in the final rule. Additionally, by utilizing an end product price series that is as wide as possible and includes contract as well as spot prices, the differences between the immediate impact on Class IV products and the delayed impact of Class II products (with forward prices) should be smoothed out.

Class II Differentials: While we agree that "Because nonfat dry milk may be substituted for fresh milk or wet solids in the production of many Class II products, the Class II price should be determined using Class IV butterfat and nonfat solids prices plus a fixed per hundred weight differential", we feel strongly that the $.70/cwt. differential will not achieve the results the USDA is expecting. First, the cost of converting milk into dry solids is already incorporated in the Class IV prices under the increased make allowances that both the IDFA and NMPF support. Therefore there is no need to incorporate it in the Class II differential. Second, the only costs that will drive the correct substitution behavior are those that directly relate to the buyer such as rehydration costs. Given the fact that the rehydraytion costs are clearly less than drying, a reduction of at least 50% would be in order. We support the IDFA position that the differential should remain at $.30/cwt. RECOGNIZE THAT SETTING THE CLASS II DIFFERENTIAL TOO HIGH WILL RESULT IN BUYER SUBSTITUTION WHICH IS EXACTLY THE BEHAVIOR THE CLASS IV BASE POINTING IS DESIGNED TO ELIMINATE.

Transition Support: As the dairy industry consensus moves the proposed end product prices for manufacturing milk closer to the California values, the need for transition support becomes a larger issue for the final rule. We would suggest that the principles of the "Freedom to Farm" grain portion of the 1996 FAIR act become the model. Their ability to separate out transition support from market distorting artificial price levels is the type of support the dairy industry desperately needs. In attachment I is one such concrete example, Dairy Farm Income Insurance, which was originally developed by Ken Bailey. It is in concept paper form and deserves more study.

I would be happy to answer any questions you may have or provide any additional data. I can be reached by phone at (510) 601-4331, by fax at (510) 601-4403, or by e-mail at tmmcalon@dreyers.com.

Thank you for the opportunity to provide input into this vitally important issue for Dreyer's Grand Ice Cream as well as the entire dairy industry,

Dairy Farm Income Insurance

A Concept Paper for Discussion Purposes

Background

In recent years, the volatility in milk and feed prices has caused large variations in net dairy farmer income. In reaction to this increased volatility, many proposals have been put forward to stabilize prices at artificially high levels through federal or regional price-setting mechanisms. However, such efforts have been shown to reduce consumer demand for milk and increase incentives for overproduction, thereby depressing milk prices and harming the very producers these programs were intended to help.

Therefore, instead of using artificial, market-distorting mechanisms to reduce price volatility, market-oriented programs should be created that provide dairy farmers protection against large fluctuations in income, without distorting markets or inducing overproduction.

Dairy Farm Income Insurance

Dairy farmer income is a function of both milk prices and input costs, particularly the cost of feed. Therefore both factors must be considered when crafting a mechanism to stabilize net dairy farm income.

While the federal government operates a broad array of insurance programs for crop producers, there are very few insurance options available to dairy farmers. Given that the 1996 farm bill phases out the milk price support program, dairy farmers are in need of insurance options to help manage price risk in the face increase price volatility.

One market-oriented income stabilization option would be a Dairy Farm Income Insurance program that would indemnify dairy farmers against declines in the relationship between the milk price and the cost of feed. Farmers would chose the level of protection they would like, by choosing the milk-feed margin below which they would be insured. The higher the margin they choose, the more expensive their insurance premium. The premium level would also depend on the amount of milk production they insure. Farmers may choose to insure part or all of their anticipated production.

In keeping with the monthly changes of regulated milk prices under the federal milk marketing order system, indemnity payments would be made to farmers on a monthly basis, in any month that the local milk price/feed price margin falls below the insured level. The milk price factor used for the purpose of this program would be monthly mailbox prices, as calculated by USDA's regional milk market administrators. The feed price factor would be derived from either USDA/NASS price data or Chicago Board of Trade futures market price data for corn and other dairy feed components.

Similar to crop insurance programs offered by USDA, dairy farmers could be offered a basic level of protection with premiums partially subsidized by the federal government. In addition, farmers would also have the option of increasing their level of protection above the basic level offered by USDA, but would be required to pay the full premium for this enhanced coverage.

Questions for Discussion

1) Should there be an opportunity for states to subsidize the enhanced coverage premiums for their farmers? This would be consistent with the trend of promoting federal/state partnerships. Further, this would give state legislators an ability to participate in helping their dairy farmer constituents, instead of merely deferring to their federal congressional delegations.

2) Is this program biased toward areas of the country that use purchased inputs, instead of growing their own feed? Is there a way to have an additional option that's more applicable to farmers that grow their own feed, such as a "whole farm" approach?

3) Using NASS or CBOT price data will work in determining the corn and soybean parts of the feed price factor for this insurance product. But what data can we use for alfalfa prices?

4) Given the implicit seasonality of both dairy and feed prices, should the guarantee for this insurance product also reflect that seasonality? For example, should farmers simply receive an indemnity payment anytime the milk-feed price margin drops below $7.00/hundredweight, or should the guarantee level be lower in the spring and higher in the fall, following the seasonal trends of both milk and feed crops? If we followed the seasonal-trend approach, the insurance premiums would not be as expensive, but farmers would only be insured against unusually low milk-feed price margins.

5) Is this insurance concept too narrow? By focusing so narrowly on milk prices and feed prices, the cost to the program in the event of a major milk price decline could be quit large. Would the cost be prohibitively expensive, or are there reasonable ways to bring down the cost?

The original concept for this insurance program is based on a paper prepared by Ken Bailey, University of Missouri, entitled "Dairy Farmer Income and Price Insurance Program." In addition, contacts have been made with the following people in discussing this insurance concept:

Allen Rosenfeld, M&R Strategic Services
Terry Frankel, Economist, American Farm Bureau Federation
Ken Olsen, Dairy Specialist, American Farm Bureau Federation
Joe Glauber, USDA, Deputy Chief Economist
Ron Knudsen, Texas A&M
Bob Cropp, University of Wisconsin-Madison
Andy Morton, Senate Agriculture Committee
Otto Doering, Purdue University
Joy Harwood, USDA/ERS
Glenn Daniels, USDA's FCIC/RMA