Agri·Mark

AGRI-MARK'S POSITION ON NATIONAL DAIRY POLICY REFORM

EXECUTIVE SUMMARY

Agri-Mark supports substantial reform in national dairy policy. Dairy farmers must be able to cover their costs of milk production and receive a reasonable return for their labor and investment if their farms are to remain viable.

While Agri-Mark agrees with the general concepts contained within NMPF's "Foundation for the Future" program, it seeks to change some of its specific provisions, including moving forward immediately with a revised version of its national production management program.

The proposed revised production management program is similar to the Marginal Pricing Program (MPP) originally developed by Agri-Mark. When farm milk prices fall to levels that can not adequately cover feed and other costs, the MPP is temporarily triggered. A production base period is determined for each farm based upon their recent milk production levels. All dairy farmers must then reduce their production by a small pre-set amount below that base or else pay a fee on any milk volumes in excess of their adjusted base volumes. The intent of this action is to provide a strong economic incentive for farmers not to produce the small volumes of surplus milk that are depressing farm milk prices. The national sum total of those production reductions will better align supply with demand and move farm milk prices up to a level where farmers can more likely cover their costs and receive a reasonable return for their labor and investment. Once an adequate price level is reached, the MPP ceases until it is needed again. A new production base for each farm is determined each time the MPP is triggered.

The MPP uses the Class III price as the fee per hundredweight on over base milk. Any revenue raised under this program is used to provide additional dairy products to charitable feeding programs such as food banks and soup kitchens. No dairy board is needed under this program.

Agri-Mark supports the Federal Milk Market order Reform provisions in the NMPF program: They should provide greater transparency in price setting. The cooperative is concerned about replacing the Milk Income Loss Contract (MILC) program with an unproven income insurance program and supports producers having the choice to participate in either program. If necessary, Agri-Mark believes these changes can wait until the 2012 Farm Bill goes into effect.

AGRI-MARK'S POSITION ON REFORM

National dairy policy regarding the marketing and pricing of farm milk supplies needs substantial reform in order to address the severe problems of inadequate dairy farm income and increased market price volatility. Proposals for such reform include a comprehensive program by the National Milk Producers Federation (NMPF) and production management programs by several dairy organizations, including Agri-Mark.

The NMPF program called "Foundation for the Future" is a four tiered approach which addresses several issues facing dairy farmers. The program includes revising current milk price and farm income "safety net" programs, changing Federal Milk Order price determination methods and establishing a production management program. The general concepts discussed in the NMPF program were supported by a large majority of member cooperatives and are being positioned to be part of the 2012 Farm Bill.

While Agri-Mark supports the general concepts in the NMPF program, the cooperative would like to see changes in several of the specific parts of the program. The most immediate change needed would be to pursue the enactment of a revised version of its national production management program as soon as possible and well before 2012.

Any national milk production management program must first and foremost balance milk supply with demand. It must effectively eliminate relatively small surpluses of farm milk that drive milk and dairy product prices down below the costs of production and increases price volatility. However, in addition to being an effective program, it must also be acceptable to a vast majority of dairy farms throughout the country as well as have sufficient political support to be passed by Congress. National farmer support may be the most difficult as dairy farmers are each independent business people who do not like the government or others impinging upon the operations of their farms. However, **Agri-Mark members have recognized that severely low milk prices below the costs of production have an even greater impingement upon their operations and as a result, most are willing to accept some type of production management program in exchange for an adequate farm income and reduced price volatility. Agri-Mark believes that dairy farmers will support a relatively simple program that minimizes government involvement, so long as it truly addresses the problem.**

Agri-Mark believes that dairy farmers and their organizations must be aligned behind a common plan if it is to have a reasonable chance of successful approval in Congress. There are currently two plans with a level of national support: the NMPF production management concept and the Costa/Sanders market access bills. The NMPF concept includes several, but not all components of Agri-Mark's marginal milk pricing plan.

The goal of both plans is to better align farm milk supplies with milk and dairy product demand during times when supply outpaces demand. Both plans work to send a revenue signal at the farm level to provide an economic reason for farms to reduce production individually until aggregate national milk production moves into alignment with demand and market prices rise. Agri-Mark does have concerns with various aspects of both programs and is working to address those concerns in its Marginal Milk Pricing Program.

MAJOR PROVISIONS OF AGRI-MARK'S MARGINAL PRICING PROGRAM

PROGRAM TRIGGER: The program triggers in and out based upon the net margin price in the marketplace over two consecutive months. The net margin is calculated as the farm (all-milk) price of milk less feed costs. This is more appropriate than using just the milk price, since volatile feed prices can render even relatively high milk prices insufficient as they did in 2008. Dairy Farmers of America (DFA) first suggested such a trigger and it was embraced by NMPF in its plan. NMPF uses a $6 net margin for two consecutive months to first trigger a 2% reduction from a farm's base milk production. This would have represented about a $14 all-milk price in 2009. For every $1 drop in the net margin, the reduction percentage increases by 1% for a maximum reduction of 4% at net margin of $4 per cwt (about a $12 price in 2009).

Agri-Mark's plan adopts the net margin concept as detailed by NMPF, as well as the percentages suggested in the following table. However, it also allows for a net margin of $7 per cwt. ($15 milk price) to trigger in a 1% reduction. Keep in mind that even just triggering the program at any percentage level will hopefully stop, or at least slow down, production growth on many farms.

Net margin (below)	Milk price (approx)	Percentage decline from base
$7	$15	1%
$6	$14	2%
$5	$13	3%
$4	$12	4%

The program would remain in place for a minimum of three months and trigger out when the net margin price exceeded $7 for two consecutive months.

In order to keep the net margin triggers updated as non-feed related milk production costs change, the trigger levels should be adjusted annually relative to the appropriate changes in the USDA costs of production report.

BASE PERIOD: There are many possible base period milk production calculations, but both the NMPF and Costa/Sanders bills need adjustment. NMPF uses a very current and continuingly updated three month rolling average. This base plan will **not** reduce the incentive for any farm to cut production, since that farm's base would decline progressively further as they reduce. Instead, it will likely provide an incentive to increase production, since any higher production level will quickly become part of a new base.

On the other hand, the Costa/Sanders bills use either the three year average of 2007 through 2009 or the same quarterly period in 2009. Any farm with a large expansion in 2010 or beyond would likely be very much over their base and end up paying substantial penalties.

The Agri-Mark base calculation would differ from either program as it would let a producer choose as his/her base production any three month consecutive period in the 12 months immediately prior to the program triggering. This allows farms which have just expanded or are new entrants to use the most current months. Farms with recent production problems could use the older months for its base and seasonal producers could use their appropriate production months. An average production per day will be determined from whatever three month period is chosen. This base would also give producers the most options and choices, so they have some "buy-in" to the program.

An alternative option would be to have USDA automatically use the three month period with the larger production per day in the past year, so there is no delay waiting for farmers to select their base period. While this may result in a smaller deduction in milk production initially since bases will be larger, keep in mind that it should still effectively freeze a farm's production in place, even without any reduction. U.S. milk production changes due to the combined impact of farms entering or expanding production and farms exiting or shrinking milk production – if the expansion can be curtailed, the exiting and shrinkage will likely continue and will lower total milk production even more.

The base volume will be fixed once the program triggers into effect. When the program triggers out, the base period triggers out with it. A new base is calculated whenever the program triggers back in.

OVERBASE FEE: NMPF uses an over base fee that is equivalent to the blend price of milk received by the individual producer. This was actually Agri-Mark's original suggestion when we first proposed using Federal Order pools. Each producer in the pool was to have the same over base rate and the money would stay in the regional pool. However, in a national program, such a program would likely be extremely controversial as producers in higher priced markets like the Southeast would pay a much larger fee than those in lower priced regions like parts of the West. The problem is further compounded when those over base funds are not distributed back to farmers, as proposed in the NMPF program.

The Costa/Sanders bills set a market access fee on all milk. The rates range from $0.03 to $0.50 per cwt on all of a farm's milk production when the farm exceeds its base production. The actual market access fee rate in place at any given time is tied to the milk-feed price ratio.

The Agri-Mark program uses the actual Federal Order Class III price as the over base fee. This reduces the value of any over base milk by 90% or more and should give producers sufficient incentive not to produce that milk. FOR EXAMPLE: In 2009 Northeast Order producers in received about a $12.29 blend price per cwt. for their milk, while the Class III price that year averaged $11.36. In that year, the over base fee of $11.36 would have reduced the net blend price value of over base milk to less than $1.00 per cwt.

USE OF PENALTY FEE REVENUE: The NMPF penalty fees would be used for demand enhancing activities, while the Costa/Sanders bills would give that money to dairy farmers who kept within their base production. Transferring money between producers would very likely create great animosity from those producers who paid the penalty. If those funds were used to increase demand activities, expanding producers would at least see some positive benefit. It would re-enforce the supply/demand balancing efforts of a production growth management program. **Under the Agri-Mark program, those funds would be used to provide additional dairy products to charitable programs such as food banks and soup kitchens**. Use of this revenue for donations of dairy products should also help get political support from other groups concerned with meeting the food needs of low income consumers.

DAIRY BOARD: The NMPF plan does not use a Dairy Board for its program, but the Costa/Sanders bills do leave many decisions to such a Board. **The Agri-Mark program does not need a Dairy Board, although one could play a role if desired by farmers.**

OPERATION OF PROGRAM: The Costa/Sanders bills create a program that would be in place all the time. **The NMPF program would move in and out as needed. The Agri-Mark program would also move in and out as needed.** This will keep individual farm bases from developing a value (and cost) over time.

OTHER ASPECTS OF THE NMPF FOUNDATION FOR THE FUTURE PROGRAM

REVISED FEDERAL SUPPORT PROGRAMS

The Milk Income Loss Contract (MILC) program has provided significant benefits to small and medium farms during its operation that would be reduced under NMPF's proposed Dairy Producer Margin Protection Program (DPMPP). Rather than replacing both the dairy product price support program and MILC program with the DPMPP, Agri-Mark supports allowing dairy farmers to choose to participate in either program.

FEDERAL MILK MARKET ORDER REFORM

Agri-Mark supports the revisions proposed by NMPF. That plan calls for basing most Federally set minimum milk prices upon a survey of competitive milk prices actually paid to dairy farmers from cheese manufacturers from across the country, rather than the current system which uses NASS cheese prices (often based upon the CME prices) to back into milk prices. This method should provide greater transparency in price setting.