NATIONAL MILK PRODUCERS FEDERATION

Maryland & Virginia Milk Producers Cooperative Association, Inc.

House Agriculture Committee
Field Hearing to Review Dairy Policy

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Chairman Peterson, Ranking Member Lucas and House Agriculture Committee members: thank you for allowing me to testify today about dairy policy on behalf of my cooperative, Maryland & Virginia Milk Producers, and the National Milk Producers Federation (NMPF). Maryland & Virginia markets milk for its 1,500 farmer owners from Pennsylvania to Georgia. Just over 700 of those farmer members dairy right here in the state of Pennsylvania. NMPF develops and carries out policies that advance the well being of dairy producers and the cooperatives they own. The members of NMPF's 31 cooperatives produce the majority of the U.S. milk supply, making NMPF the voice of more than 40,000 dairy producers on Capitol Hill and with government agencies.

My name is Lauren Mosemann and I am from Warfordsburg, PA. My husband Mark and I farm with Mark's family in Misty Mountain Dairy. We milk approximately 375 cows and have about the same number of replacement animals. In fact, my primary job is the care of those replacement heifers and calves. Mark and I have been active participants in the Maryland & Virginia Young Cooperators Program and have also attended YC visits to the Congress coordinated by NMPF. Mark and I were honored to be the Maryland & Virginia Outstanding YC Couple in 2007-2008.

Mark and I have made a conscious decision to raise our children on the dairy farm and we do not rely on any outside income. We have also made a commitment to be involved in our community. Mark is on the local school board and I volunteer with the local Farm Bureau for their Mobile Ag Lab. I have also just signed up to help promote the "Fuel Up to Play 60" nutrition and physical activity program launched recently by the dairy promotion and research checkoff and the National Football League.

Both Mark and I come from long lines of dairy farmers. Mark is the third generation of his family on the home farm and I was the third generation on my family farm that is, unfortunately, no longer in business. Looking back on our decision to dairy, we both had other career options. While today's dairy farm economy naturally creates a second thought or two, this is the decision we made about how we wanted to raise our children.

Mark and I have friends at church with a college age son who would like to return to the farm. That family is debating whether that is an economically viable decision for their son to make. Mark and I see ourselves in that same situation with our children in 15 years or so and we'd like to think that some of the policy decisions we're considering here today will improve that opportunity for our family.

As NMPF and others have testified before this Committee, 2009 presented an unprecedented financial catastrophe for the dairy producer community. Last year, dairy farmers in the United States experienced their worst year financially in anyone's memory. U.S. dairy exports had grown strongly from the equivalent of about five percent of U.S. milk production in 2002 to about 11 percent of production in 2008, peaking, on a monthly basis, at almost 13 percent of production in August of 2008. Then, over the following six months, exports collapsed as the recession deepened worldwide, to a low of less than eight percent of production by January 2009.

Although exports recovered steadily, to average 9.3 percent of production for the year, and domestic dairy product sales were strong despite the economy, this could not counterbalance losing the equivalent of five percent of total commercial sales during the second half of 2008. Milk prices fell far below the costs of production for all dairy farmers, who incurred losses estimated at almost $8 billion last year. Prices recovered gradually during the second half of 2009, as the cumulative effects of removing about 250,000 cows through the voluntary Cooperatives Working Together (CWT) program plus recovering exports slowly began to reestablish a supply-demand balance in the market. Milk prices rose briefly above breakeven around the first of this year, but have subsequently retreated back below cost levels in the past two months, as residual dairy product stocks remain too large to sustain prices above costs at the percent time.

The current dairy and grain futures markets indicate that milk prices will rise again above costs around mid-year and remain there for the remainder of the year, but not to the extent that dairy farmers will make much headway in rebuilding the huge losses of equity in their dairy farms that they experienced last year. Financial recovery may likely prove impossible for many, while some farms are currently in receivership, with their lenders waiting only for the value of dairy cows and the land, their main sources of collateral, to recover equity before they proceed to liquidate them.

<u>A Way Forward:</u>
What has become clear to the dairy producer community from this extraordinary strain is that we need a combination of approaches to deal with the current situation. To address the underlying problems that caused this crisis and the many industry factors that have contributed to its depth and protracted nature, we need to focus on solutions that avoid recurrences of this situation in the future.

Towards that end, last year NMPF created a Strategic Planning Task Force to seek consensus across the dairy producer community and create a solid “Foundation for the Future.” My coop, Maryland and Virginia Milk Producers, has been an integral part of this process. The goal of the Strategic Planning Task Force has been to analyze and develop a long-term strategic plan for consideration by the NMPF Board of Directors that will have a positive impact on the various factors influencing both supply and demand for milk and dairy products. It is extremely important to develop workable and realistic solutions that will garner broad support from dairy producers nationwide in order to unify behind an approach as this committee begins to consider the next farm bill.

As Albert Einstein said, “We can't solve problems by using the same kind of thinking we used when we created them.”

NMPF’s new roadmap for U.S. dairy policy, called the Foundation for the Future, will drastically change many aspects of current policy, some of which have existed for decades. Our existing dairy policies and programs were designed in an earlier time to operate in a relatively closed domestic market. However, today’s market for U.S. dairy farmers’ milk is greatly influenced by global demand and supply, as the record prices of 2008 – and their disastrous plunge in 2009 – clearly demonstrated.

Rather than offering just one solution, the Foundation for the Future program is multi-faceted: it seeks to refocus existing farm-level safety nets; create a new program to protect farmers against low margins; revamp the Federal Order milk pricing system; and establish a way to better balance dairy supply and demand. I would like to touch on each aspect of this approach.

1. <u>Refocusing Current Safety Nets</u>

   Both the Dairy Product Price Support Program and the MILC program are inadequate protections against not just periodic low milk prices, but also destructively low profit margins that occur when input costs, especially feed prices, shoot up. The Price Support Program, in particular, has outlived its usefulness and hinders the ability of U.S. and world markets to adjust to supply-demand signals.

Discontinuing the Dairy Product Price Support Program (DPPSP) would allow greater flexibility to meet increased global demand and shorten periods of low prices by reducing foreign competition. Additionally, shifting resources from the DPPSP toward a new income protection program would provide farmers a more effective safety net.

As this committee may recall, NMPF vigorously defended the importance of the price support program, albeit modified to make improvements in certain respects, in the 2008 Farm Bill process. But at the end of the day, it is clear at this point that the dairy product price support program is not the best use of federal resources to establish a safety net to help farmers cope with periods of low prices and is not the most effective way of achieving this goal.

- **The DPPSP reduces total demand for U.S. dairy products and dampens our ability to export, while encouraging more foreign imports into the U.S.**
  The price support program effectively reduces U.S. exports, by diverting some of our milk flow into government warehouses, rather than to commercial buyers in other nations. It creates a dynamic where it's harder for the U.S. to be a consistent supplier of many products, since sometimes we have products to export, and at other times, we just sell to the government.

- **The Program acts as a disincentive to product innovation.**
  It distorts what we produce, i.e. too much nonfat dry milk, and not enough protein-standardized skim milk powder, as well as specialty milk proteins such as milk protein concentrate, that are in demand both domestically and internationally. Because the price support program is a blunt instrument that will buy only nonfat dry milk – and because that's what some plants have been built to produce, as opposed to other forms of milk powder – it puts the U.S. at a competitive disadvantage to other global dairy vendors.

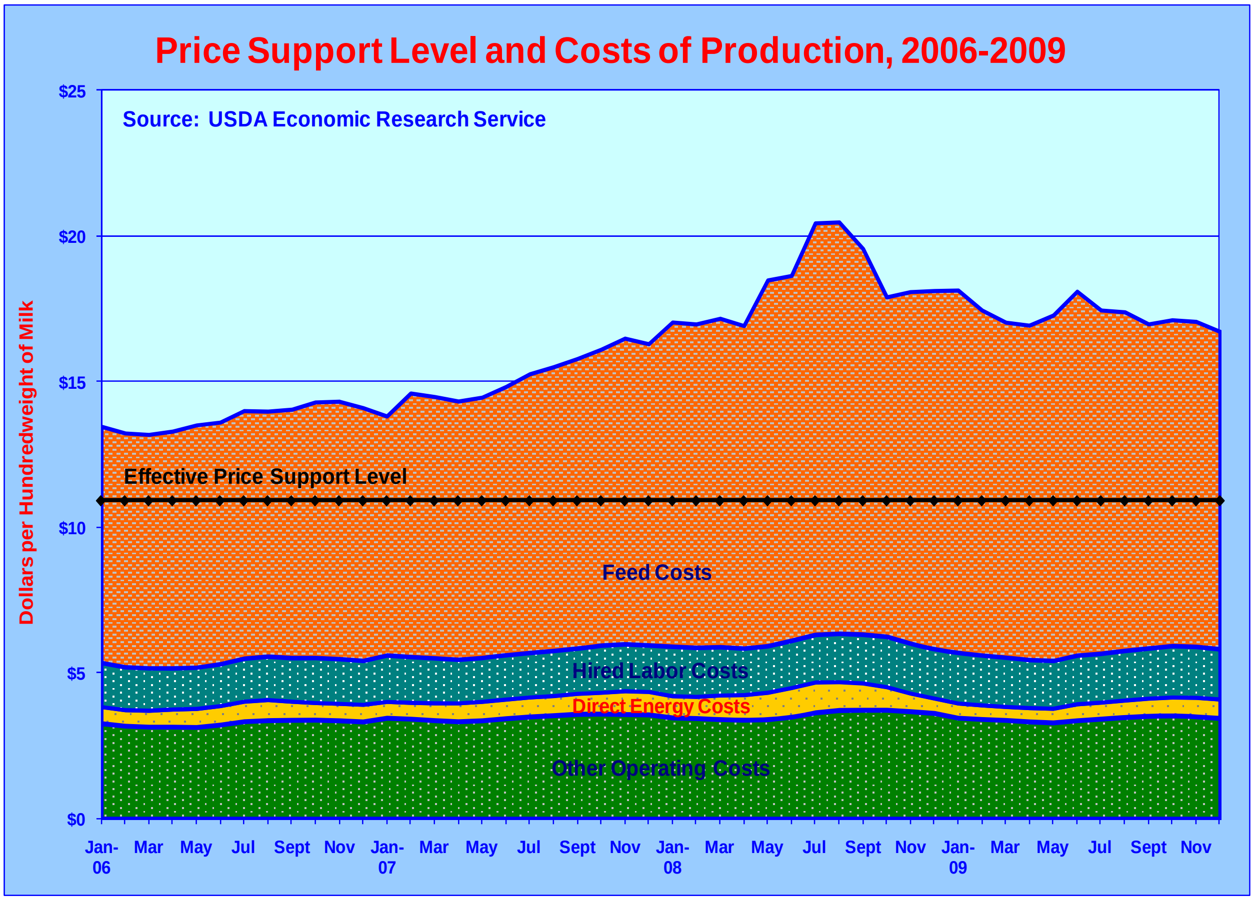
- **DPPSP supports dairy farmers all around the world and disadvantages U.S. dairy farmers.**
  Further aggravating measures, the current program helps balance world supplies, by encouraging the periodic global surplus of milk products to be purchased by U.S. taxpayers. Dairy farmers in other countries, particularly the Oceania region, enjoy as much price protection from the DPPSP as our farmers. Without USDA's CCC buying up an occasional surplus of dairy proteins in the form of nonfat dry milk, a temporarily lower world price would affect our competitors – all of whom would be forced to adjust their production downward – and ultimately hasten a global recovery in prices.

- **The DPPSP isn't effectively managed to fulfill its objectives.**
  Although the DPPSP has a standing offer to purchase butter, cheese and nonfat dry milk, during the past 12 years, only the last of that trio has been sold to the USDA in any significant quantity. In essence, the product that the DPPSP really supports is nonfat dry milk. Even at times when the cheese price has sagged well beneath the price support target, cheese makers choose not to sell to the government for a variety of logistical and marketing-related reasons. We have tried to address these problems, but USDA has to date been unwilling to account for the additional costs required to sell to government specifications. Once purchased, powder returning back to the market from government storage also presents challenges, and can dampen the recovery of prices as government stocks are reduced.

- **The price levels it seeks to achieve aren't relevant to farmers in 2010.**
  Even though the $9.90 per hundredweight milk price target was eliminated in the last Farm Bill, the individual product price support targets: $1.13/lb. for block cheese, $0.85 for

powder, and $1.05 for butter – essentially will return Class III and IV prices around $10/cwt. But in an era of higher cost of production, that minimal price isn't acceptable in any way, shape or form. The chart below depicts the U.S. average cost of production and the effective level of support the program provides for the average price dairy farmers receive for milk in the U.S. As is clear from this graph, this effective price support level is far below today's cost of production.

We believe that with the current funding constraints facing Congress, we are unlikely to see increased support prices. Even if it did, however, we would likely face the same barriers described in the prior point.



In summary, discontinuing the DPPSP would eventually result in higher milk prices for U.S. dairy farmers. By focusing on indemnifying against poor margins, rather than on a milk price target that is clearly inadequate, we can create a more relevant safety net that allows for quicker price adjustments, reduced imports and greater exports. As a result of our DPPSP, the U.S. has become the world's balancing plant. As time marches on, so, too, must our approach to helping farmers. It is because of this that NMPF is now focused upon a transitional process that shifts the resources previously invested in the dairy product price support program, to a new producer income protection program.

2. <u>Dairy Producer Income Protection Program.</u>

As mentioned above, existing safety net programs (the price support program, and the MILC program) were created in a different era. Neither was designed to function in a more globalized market, where not just milk prices, but also feed costs and energy expenses, are more volatile and trending higher. In the future, the solvency of dairy farms will depend more on margins (the difference between input costs and milk prices) than just the milk price alone. In order to address this dilemma, NMPF is proposing a revolutionary new program called the Dairy Producer Income Projection Program (DPIPP). It will help insure against the type of margin squeeze farmers experienced in 2009, and also at other points in the past when milk prices dropped, feed costs rose – or both conditions occurred in tandem.

In developing the Dairy Producer Income Protection Program, a few important principles are being followed:

- Losses caused by either low milk prices or high feed costs need to be covered.
- A farmer's cost for basic protection must be kept low or nonexistent.
- The level of protection available should be flexible, and producers should be able to purchase a higher level of protection if they choose.
- The program should be voluntary, national in scope, and open to all dairy farmers, regardless of size.
- The program should not provide incentives to create artificial over-production.
- The program must be easy to access by all producers through a simple application process or through the assistance of their cooperative.

Essentially, the Dairy Producer Income Protection Program (DPIPP) is intended to be a farm-level safety net program focused on margins, rather than just on prices, in order to create a better tool to deal with global price volatility. DPIPP would offer a combination of a base level of insurance, coupled with voluntary supplemental coverage, will allow farmers of all sizes in all regions to protect themselves from periodic margin squeezes caused both by high input costs and low milk prices.

As a substitute for the other two safety nets, DPIPP would involve two levels of insurance against negative margins. The first would be a base level of coverage, subsidized by the government that covers a portion (but not 100%) of a farm's historical annual milk production, and protects against a modestly negative margin between milk prices and feed costs. The second level would be optional, and allow a farmer to purchase a greater level of coverage, with a portion of that insurance subsidized by the government.

Key elements include:

- **Defining margin as the difference between the national all-milk price and key feed inputs.**
  The all-milk price is the best proxy to define what an average nationwide price is for milk each month. Feed costs are represented by corn, soybean meal, and alfalfa hay, and the cost of those is also tracked monthly by USDA. The difference between the per hundredweight price of milk, and the cost of feeding cows, will establish this program's margin.

- **The government will invest to help defray the cost of a basic level of margin insurance for all farmers.**

A significant portion – but not 100% – of a farm's historic production base will be eligible for coverage. Indemnifying against part, but not all, of that farm's milk volume will ensure that the program does not stimulate overproduction. Once the numerical margin target is established, it will be fixed for the life of the Farm Bill. USDA will calculate actual margins on a monthly basis and make indemnity payments quarterly, as market conditions dictate.

- **Producers will have the option of purchasing an additional level of coverage.**
  For a fee, farmers who wish to insure a higher level of margin protection will have that option, with the premium partially subsidized by the government. The premium will be calculated by the probability or frequency of payments of the specific level of coverage selected. Producers will have a year after implementation of the Farm Bill to sign up for additional coverage.

- **The DPIPP will be equitable and national.**
  This program is designed to have no payment limitations, or production caps, thus ensuring that dairy farms of all sizes will be covered proportionately. The DPIPP will allow for new entrants, i.e. new farming options, but only under strict parameters so the system can't be gamed. The program will be administered by the USDA through the Farm Service Agency (FSA) or the Risk Management Agency (RMA).

This approach is really no different than the concept of private property or auto insurance, where premiums adjust to the coverage desired. But under the DPIPP, the base level of coverage would be the government's obligation to fund, while the supplemental coverage would be a combination of farmer and government cost. And nowhere in here is there a price assurance; the goal is margin insurance, an important distinction. We believe this would provide a much more effective safety net for dairy producers.

3. Federal Milk Market Order Reform

The goal of this effort is to develop a pricing system that compensates producers fairly, reduces price volatility, and creates a more dynamic dairy industry. The key in doing so is to establish a competitive pay price for milk that doesn't depend on the current milk pricing formulas that can distort signals sent both to producers and processors. By revamping Federal Orders, we can encourage the movement of milk to its highest-value uses.

4. Production Management

For the past seven years, NMPF's Cooperatives Working Together (CWT) program has voluntarily helped to address the supply side of the supply-demand equation that ultimately determines milk prices. We need to both revitalize Cooperatives Working Together, and evaluate other approaches that will address the extremes in price volatility impacting producer profit margins. The Foundation for the Future is focused on a program that will trigger, when necessary, a signal to farmers that less supply is needed. This can be blended with elements of the CWT programs. NMPF recognizes that there is considerable interest in action on this point and will be happy to provide greater details on this element to the Committee once it is further developed.

All of these potential changes will ultimately require a new way of thinking about dairy economics. NMPF is not underestimating the size of the shift in attitude necessary on the part of producers to give these proposed programs a fair evaluation. The dairy farmers I know recognize something has to be done before all the farms are gone and if there is one lesson to be learned from the past year, it's that change is needed.

Other Critical Elements Impacting the Dairy Industry:

I have focused the bulk of my testimony on the primary dairy-specific federal policies and particularly those aspects that will most likely be part of the 2012 Farm Bill consideration process. However, there are other issues with significant impact on the dairy industry and I would like to take the time here to touch on each of those key areas.

1. Importance of Dairy in Nutrition Programs

Milk contains a complete nutrient package of nine essential nutrients. In addition to being an excellent source of calcium and vitamin D, it is a good source of Vitamin A, protein and potassium. In fact, milk is the top contributor in our diet for calcium, potassium and magnesium. (All milks- whole, low-fat, fat-free, flavored and lactose-free- contain the same amount of calcium) Bones continue to grow in density and strength until about age 35. After that, drinking milk and eating milk products help prevent further bone loss. Milk provides all five of the five nutrients of concern for children and adolescents: calcium, potassium, fiber, magnesium, and vitamin E.

The Child Nutrition Act, which is scheduled to be reauthorized this year, accounts for more than 5% of the total milk consumed in the United States through the school meal programs. The Healthy, Hunger-Free Kids Act of 2010, approved March 24, by the Senate Agriculture Committee, invests an additional $4.5 billion in child nutrition programs over the next 10 years. The bill both protects milk's current position in several critical child nutrition programs and offers significant opportunities to increase milk consumption by school-age children nationwide. The House Education and Labor Committee should be releasing their draft of the child nutrition bill soon and we are hoping to see a similar positive outcome.

The child nutrition programs play a vital role in helping children, especially those in low-income families, achieve access to quality nutrition, child care, and educational and enrichment activities while improving their overall health, development, and school achievement. These programs are proven to work, but too many children continue to miss out on their benefits because of low participation rates and unnecessary access barriers.

NMPF supports the efforts by the Food Research and Action Center (FRAC), School Nutrition Association (SNA) and the Center for Science in the Public Interest (CSPI) to;

- Expand the Afterschool Meal Program to all 50 states
- Improve the area eligibility test so more communities can operate afterschool, summer, and family child care food programs
- Provide funds for grants to support the start-up and expansion of universal and in-classroom school breakfast programs in low-income schools and provide breakfast commodity support
- Invest in Summer Nutrition Programs by providing funding for start-up, outreach, and transportation grants
- Allow child care centers and homes the option of serving a third meal
- Eliminate unnecessary paperwork that is a barrier to participation through data-based eligibility systems in schools in high-poverty areas and through improved direct certification systems
- Streamline afterschool nutrition rules to allow community-based and local governments in all states the ability to provide meals and snacks year-round through the rules and paperwork of the Summer Food Service Program

NMPF also supports increasing the Special Milk Program and increasing the reimbursement rate for the school meal program. As has been stated over and over, hungry, under-nourished children have difficulty learning.

2. Immigration Reform

Now, more than ever, dairy producers urgently need Congress to act on agricultural immigration reform. Immigrant labor plays a very important role in contributing to the success of America's dairy industry; a large percentage of the hired workers on dairy farms are immigrants. This is true for a great number of dairy farmers across this country, both large and small. NMPF strongly supports the type of broad immigration reform for the agriculture sector that AgJobs (H.R. 2414) contains and the visa program proposed by H.R. 1660, the Dairy and Sheep H-2A Visa Enhancement Act.

Dairy farmers share the concerns of all Americans about securing our borders & protecting this country and they are not willing to sacrifice its security. However, failing to provide for orderly flows of greatly needed workers is creating enormous economic consequences for our industry and do very little to enhance our border protection. We urge members of Congress to join as cosponsors of H.R. 2414 and H.R. 1660 to once and for all address the endemic labor shortage in the dairy farming sector and allow for dairy producers to work within the agricultural visa system.

It is a common misperception in our community and others that immigrant workers take jobs from local workers. It is our experience on my family's farm that this is simply not the case. We've tried to hire local workers and jobs on our farm pay well above minimum wage. Our last job ad resulted in four phone calls. Just one person showed up for an interview but never came back.

3. Estate Tax reform

NMPF supports permanent and meaningful estate tax relief. If estate taxes are allowed to be reinstated at the beginning of 2011 with only a $1 million exemption and top rate of 55 percent, the negative impact on our industry will be significant. We support permanently raising the exemption to no less than $5 million per person and reducing the top rate to no more than 35 percent. It is also imperative that the exemption be indexed to inflation, provide for spousal transfers and include the stepped-up basis.

Family farmers and ranchers are not only the caretakers of our nation's rural lands but they are small businesses too. The 2011 change to the estate tax law does a disservice to agriculture because we are a land-based capital intensive industry with few options for paying estate taxes when they come due. The current state of our economy, coupled with the uncertain nature of estate tax liabilities make it difficult for family-owned farm and ranches to make sound business decisions. We urge Congress to pass permanent estate tax reform now.

As our family works out the partnership agreement, uncertainty about generational transfer of the farm assets is a major factor we must deal with. We strongly support estate tax relief as outlined above, which provides the greatest relief and certainty for agriculture.

4. Climate Change Legislation and Regulation

I thank Chairman Peterson for introducing HJ Resolution 76 disapproving the EPA rule that uses an endangerment finding to regulate six greenhouse gases under the Clean Air Act.

Regulation of GHG emissions should be done only at the direction of the Congress and NMPF supports this attempt to reassert that authority. Agriculture will be one of the industries most affected by climate change regulation and that issue deserves to be fully debated and decided by our elected representatives.

5. <u>Trade</u>

NMPF has been a strong supporter of balanced trade agreements that present net benefits for America's dairy producers. Good examples of agreements that fit this bill are the three pending free trade agreements with South Korea, Colombia and Panama. Of those three, the FTA with Korea offers the greatest prospects for increased U.S. dairy exports, but the latter two agreements would also provide useful new opportunities. As a result, NMPF has strongly supported the passage of all three.

Another good opportunity to expand the market for U.S. dairy products is Chairman Peterson and Representative Moran's Travel Restriction Reform and Export Enhancement Act, H.R. 4645, which NMPF testified in support of before this Committee last month. NMPF believes that efforts to help regain the exports we lost last year are essential to helping farmers and putting the U.S. dairy industry on a firmer footing going forward and H.R. 4645 represents one such positive step in the right direction to increase demand for U.S. dairy products.

A critical threat to the future health of the dairy industry also exists, however, in the prospect of open dairy trade with New Zealand as part of the Trans-Pacific Partnership FTA. Expanded dairy trade with New Zealand offers an entirely one-way street since the FTA would open up no effective new opportunity for the U.S. dairy industry in New Zealand and even the prospect of increasing access to other markets within the TPP is limited. Because of this, producers everywhere throughout the U.S., as well as many leading dairy processors, are seeking the full exclusion of U.S.-New Zealand dairy trade from the TPP.

6. <u>Additional Useful Near-Term Measures</u>

Some measures exist that could be taken prior to the next Farm Bill that are of concern to dairy producers in Pennsylvania and throughout the country. NMPF and most other dairy producers have been supportive of legislation to apply tariff rate quotas (TRQs) to imported milk protein concentrates, casein and caseinates in order to close a major loophole that currently exists in our trade structure. We support H.R. 3674 which would create a path to achieve this important goal.

Additionally, those of us engaged in selling safe and wholesome milk to the marketplace would like to see stronger efforts to discourage the sale of unpasteurized milk. Pasteurization is widely used in the U.S. and around the world because it helps ensure that the final dairy product sold to consumers will be safe. Raw/unpasteurized milk is currently permitted to be sold in many states under certain conditions, but this creates the possibility for consumers to get sick from these unpasteurized products for which appropriate safety measures have not been taken. The last thing the dairy industry needs at this point is a food safety scare.

<u>Closing:</u>

Thank you for the opportunity to testify on the issue of dairy policies here today. My family and I, Maryland & Virginia Milk Producers and NMPF look forward to working with the members of this Committee on issues of critical importance to the dairy industry. I look forward to answering questions from the committee.