MIDWEST DAIRY COALITION

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On behalf of the
Midwest Dairy Coalition

Submitted to the
House Committee on Agriculture
Subcommittee on Livestock, Dairy and Poultry

For a hearing to discuss
"The Economic Conditions Facing the Dairy Industry"

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Chairman Scott, Ranking Member Neugebauer, Members of the Subcommittee:

Thank you for holding this hearing today to discuss the economic conditions facing the dairy industry. My name is Ed Welch and I am the president and chief executive officer of Associated Milk Producers Inc. (AMPI). AMPI is a dairy marketing cooperative with 3,500 member farms, 5.8 billion pounds of milk and $1.7 billion in annual sales. Members operate dairy farms located throughout the upper Midwest states of Wisconsin, Minnesota, Iowa, Nebraska, South Dakota and North Dakota. They own 14 manufacturing plants and market a full line of consumer-packaged dairy products.

I am testifying today on behalf of the Midwest Dairy Coalition, an alliance of dairy cooperatives, associations and state agencies working together to provide an upper Midwest voice on federal dairy policy issues. Members include AMPI, Bongards' Creameries, Cooperative Network, Family Dairies USA, First District Association, Manitowoc Milk Producers Association, Mid-west Dairymen's Company, Milwaukee Cooperative Milk Producers, and the Wisconsin Department of Agriculture, Trade and Consumer Protection.

As suggested by the title of this hearing, the dairy economy is in crisis. Milk prices have fallen farther than expected, and the recovery has been slower than anticipated. In June of

2008, the Class III milk price was $20.25 per hundredweight. One year later, the June 2009 Class III price is $9.97 per hundredweight. Dairy product prices have dipped below support levels repeatedly since January of this year. With milk prices paid to farmers less than half of what they were a year ago, the economic stress in dairy-dependent regions like the upper Midwest is severe. This economic pain is being felt in all regions of the country.

The downturn in dairy is as bad as it has been probably since the depression, primarily because of general economic conditions that drive down both domestic and export demand. The financial crisis also spills over into farm lending in general, and dairy specifically. As the down cycle continues, bankers increasingly hold the key to whether some farmers will be able to continue in business. Consistent anecdotal evidence suggests that dairy farmers are losing about $100 per cow per month. When this happens, dairy farmers either bleed their equity or borrow, which is not currently an option due to financial markets. Literally the milk production infrastructure in the U.S. is at stake. Recovery and TARP monies might be used to make a difference in the short run if bold and innovative solutions are tried.

It is with this background that we offer the following suggestions.

Milk Income Loss Contract (MILC) Program and Dairy Product Price Support Program (DPPSP): Changes Needed to Improve Effectiveness

Without a doubt, the economic safety net provided by the Milk Income Loss Contract (MILC) program has provided significant financial assistance to dairy farmers nationwide during times of low prices. The direct assistance provided the MILC program has benefits community wide, as the dollars multiply throughout dairy-dependent local economies.

The MILC Program was first authorized in the 2002 Farm Bill. The modifications made in the 2008 Farm Bill to add a feed-cost adjuster and restore the original 45 percent payment rate have provided meaningful enhancements to the program. The Midwest Dairy Coalition worked hard for and has strongly supported the MILC program in both the 2002 and 2008 Farm Bill deliberations.

Unfortunately, the current dairy price chasm that we’re experiencing suggests that the MILC program by itself is not sufficient. The price dairy farmers are receiving for their milk is so far below the cost of production that they are losing thousands of dollars a month, even with the MILC program assistance. Congress should consider a temporary increase in the 45 percent MILC payment rate to address the emergency price situation.

As originally envisioned, the MILC program was intended to be a partner to the Milk Price Support Program, which was modified by the 2008 Farm Bill to become the Dairy Product Price Support Program (DPPSP). The two programs working together, in theory, would provide assistance and stability to allow viable dairy producers to weather the storm of low-price cycles. But the theory remains untested, because the DPPSP is not fully functioning, leaving the MILC program to do all of the heavy lifting by itself—a burden it is not able, nor was it designed, to bear.

Therefore, we are urging the U.S. Secretary of Agriculture to take the following immediate, remedial actions to bring the DPPSP back to life and serve its intended purpose:

1) Increase the Commodity Credit Corporation (CCC) purchase prices for butter, powder and cheese.

The 2008 Farm Bill sets minimum CCC purchase prices levels for butter, powder and cheese, but provides flexibility for those prices to be increased above those levels when necessary. We are urging the Secretary to take immediate action to increase the price support levels to reflect the additional costs that dairy product manufacturers face when selling product to the CCC relative to commercial sales.

2) Restore the pre-2009 policy of paying a premium price for consumer-packaged products that are more readily usable in USDA nutrition and food donation programs.

Historically, CCC has paid a premium price under the DPPSP to purchase more consumer-packaged dairy products, such as pasteurized processed cheese in 2- or 5-pound boxes. They are more readily used in USDA nutrition and food donation programs and do not require further processing, as do large cheese blocks and barrels.

However, in January of 2009, just as milk prices were collapsing, the Bush administration issued a notice to dairy product manufacturers informing them that the policy of purchasing consumer-packaged, value-added products was ending. Unfortunately, the current administration has continued this policy.

We are urging the USDA to reinstate its pre-2009 policy of paying a premium price for consumer-packaged, value-added dairy products such as pasteurized processed cheese. This will help stabilize milk prices and the growing needs of food donation programs. If there question about USDA's authority to continue this practice under the revamped statutory authority for the price support program, we believe the DPPSP authority can be married with that of the CCC Charter Act of 1933 to address these concerns.

3) CCC should be an active buyer of dairy products on the Chicago Mercantile Exchange (CME) at established price support levels.

For reasons described below, many dairy product manufacturers are reluctant to sell product to the CCC. We urge the CCC to become an active buyer of dairy products on the CME at the established price support levels, instead of the current practice of being a passive buyer by simply offering to buy product at the established CCC purchase price. Because CME prices are widely used as a benchmark price for off-market dairy product sales, we believe the CCC's active participation in the CME would significantly enhance the DPPSP effectiveness. We believe the Secretary has the authority to buy products for

CCC directly on the CME if, administratively, he waives the CCC product and packaging specifications that are outdated, impractical and costly.

4) Take all practical actions available to harmonize CCC packaging and grading standards with commercial standards set by the CME.

Currently, CCC packaging and grading standards differ from commercial standards established by the CME. Therefore, manufacturers are reluctant to sell product to the CCC because they must change manufacturing procedures in order to address those standards. Because of the discrepancies between CCC and CME standards, and periodic delays in receiving payment from the CCC, there are additional costs associated with selling product to the CCC. We urge USDA to undertake a full review of its dairy product packaging and grading standards, in dialogue with the dairy industry representatives, to investigate practical ways to harmonize CCC standards with those used for commercial sales.

Additional Efforts Necessary to Purchase Cheese for USDA Nutrition and Food Donation Programs

USDA has taken action to use existing CCC stocks of nonfat dry milk for food donation programs. In the long run, this will be helpful in preventing excessive stocks from hanging over the market. We appreciate the Secretary's efforts in this regard. According to food aid organizations such as Second Harvest, food pantry demand is up significantly from one year ago. Dairy products can provide healthful food to children and families in need.

We believe, however, the USDA should take additional action to use all authorities at the Secretary's disposal to purchase cheese products directly off the market for use in USDA nutrition and food donation programs. Direct purchases off the market will have the most direct and immediate affect in stabilizing milk and dairy product prices. <u>They will also help address the humanitarian food needs for low-income populations.</u>

Federal Milk Market Order Reform

The dairy farmers and industry leaders of the upper Midwest have long voiced concerns about the discriminatory pricing policies inherent to the federal milk marketing order system. It is widely documented that the bias of the current system toward Class I (fluid) milk has a downward affect on the value of milk used for manufacturing. For regions like the upper Midwest, where 85 to 90 percent of the milk is used for manufactured dairy products, this discrimination is of great concern. In addition, as Class I utilization percentages nationwide continue to decline, the outdated Class I bias of the federal milk market order (FMMO) system must be revisited. We look forward to working with the committee and USDA to reform the system in favor a more coherent approach to milk pricing.

Trade Issues

We greatly appreciate the Secretary's recent announcement of the Dairy Export Incentive Program (DEIP) allocation for the 2009-2010 marketing year and urge quick action to fill these allocations. The delay in announcement of the 2008-2009 DEIP allocations caused much of this allocation to go unfilled, which is a lost opportunity to help stabilize milk prices. Hopefully, the 2009-2010 experience will be more positive.

In the world of dairy, small imbalances in supply and demand result in large changes in milk prices. We cannot ignore the fact that dairy imports and exports play a role in that overall supply-demand equation. The strong milk prices of 2007 and 2008 were driven in large part by tight supplies of dairy products in the world market and a related surge in U.S. dairy exports. The milk price crash of 2009 was related, in part, to the loss of those markets. The unique, high world market price situation of 2007 and 2008 allowed the U.S. to take advantage of the export market at prices that were profitable to U.S. dairy farmers. The world market dairy prices, however, are often below the U.S. cost of production. While we should look for ways to expand our export opportunities, it defeats the purpose if those markets come at prices that are unsustainable to U.S. dairy farmers.

There have been times in the last decade when dairy product imports have significantly affected domestic price levels. There continue to be dairy product import categories, such as milk protein concentrates (MPCs), for which there are no limits. Whenever U.S. dairy prices start to recover, our market will once again be vulnerable to lower-priced MPC imports from our competitors. The Midwest Dairy Coalition continues to support efforts to establish tariff-rate quotas on MPC imports. This would improve consistency with import rules in place for other dairy products and close loopholes that have encouraged circumvention of those rules.

Long-Term Solutions Needed to Address Wide Price Volatility

While immediate action is needed to address the current milk price crisis, the current situation has sparked industry-wide discussion about long-term solutions to prevent the wide volatility in milk prices. The bottom end of the wide price swings of the last decade has been disastrous for dairy farmers. The high ends of the price cycles are leading dairy product users to seek out alternatives and reduce their use of dairy products, with long-term effects on dairy demand. Indeed, neither side of these wide price swings is beneficial to dairy farmers.

Many plans are being discussed in the industry to institute long-term policies to prevent the type of price crisis we are now experiencing from ever happening again. While there is no national consensus of the best approach to achieve this goal, we strongly urge the committee and the Secretary to assist the industry in developing and analyzing options for the long-term viability of dairy farming in this country.

Thank you for the opportunity to submit this testimony.