Draft of report to committee from sub-committee based on 2 conference calls

10/10/2010

DIAC Mission: The purpose of the Dairy Industry Advisory Committee is to review the issues of farm milk price volatility and dairy farmer profitability and provide a report with recommendations to the secretary on how USDA can best address these issues to meet the dairy industry's needs in the near and long term.

Questions:
Should federal dairy policies take into account policy goals beyond encouraging the least cost for milk production?

Should our recommendations be for the 60,000 + dairy farms or for operations that are able to continue milk production with low average milk-price?

Do solutions proposed by the cooperatives represent the grass roots opinions of the majority of dairy farmers or the opinions of those that supply the highest volume of milk?

Is there a crisis with dairy processors or retailers of dairy products?

"*Although the overall number of milk cow operations has declined since 2001, the number of operations with 500 or more head of milk cows has increased. Since 2001, the number of operations with 500 or more head increased by 20 percent, from 2,795 to 3,350 in 2009 (Graph 1). The largest size group, places with 2,000 or more head, showed the greatest percentage change from 2001, increasing from 325 places in 2001 to 740 in 2009, a gain of 128 percent (Graph 2). While larger operations were growing in number, smaller operations declined in number. Places with less than 500 head went from 94,665 in 2001 to 61,650 in 2009, a decline of over 33,000 operations, or 35 percent." "In 2009, operations with 500 or more head accounted for 5 percent of the total milk cow operations, 56 percent of the milk cows, and 60 percent of the milk production." USDA NAAS*

Different solutions for different time periods:
1. Immediate: 2011
2. Short term: Now to 2014 (implementation of new farm bill programs)
3. Long term: Impact of programs in the new Farm Bill

Where does the crisis lie for dairy farmers?
1. On the production side – impact on business equity and liquidity from 2009 at an unprecedented level that will need many months of higher stable pay-prices to remedy the situation. Many farms have reached the point where there may be no remedy.

2. Those that are under most pressure:
    a. Farms that have to purchase feed
    b. Farms that have highly leveraged assets

    c. Farms that have a business model based on cash-flow needs of short peaks and valleys rather than the protracted tough of 2009.
3. Over 50% of dairy farms under lender supervision either to manage existing debt or use of operational lines of credit.
4. Feed companies are being more pro-active about payment terms and cutting of credit as they can no longer carry the farms that are unable to pay.
5. Major crises in the next 6 months because of:
    a. Increased federal regulation on lenders
    b. Lack of lender confidence
    c. Not enough rebound to repair cash flow deficits and pay down payables
    d. Higher milk prices are being undermined by projected poorer harvests and high grain prices

If we favor/support supply management, what does it mean and what is the goal for it?

1. Canadian system is an extreme: different opinions of effectiveness but not a model for current World market or the USA economy
2. National milk is on the other extreme: safety net, with no stable baseline for production, designed to prevent a prolonged trough within the projected acceptable volatility of an active and growing production
3. What program would limit risk/volatility to prevent a prolonged trough while not masking market signals? What would trigger program to make it the most effective to slow production growth rather than encourage growth to meet cash flow requirements in a depressed market?

What does it need to sustain the 'Family Farm'?

In the way of individual Prosperity:

1. Non-market influence and artificially inflated costs of inputs:
    a. Ethanol mandate and subsidies
    b. Air and water regulations – increasing state, local conservation and federal regulation and oversight
    c. 'Freedom to Farm' within an increasing urban environment
    d. Urban competition for water increases costs and availability
    e. Labor:
        i. Minimum wage
        ii. Immigration
        iii. Competition in the labor market
    f. Disappearance of infrastructure increases parts and service costs
2. Insufficient management time, knowledge, milk volume or available cash flow to employ effective risk management strategies

Use of Secretary's power to set a minimum price either for a specific time period or as part of long-term policy

Increasing milk price could harm the farms that it was designed to help: Any across-the-board (particularly if it is artificial) improvement in milk price will improve overall profitability per unit at any given time. Because the input costs per unit for large farms and/or those with less onerous expenses are generally less than those for small farms and/or those with specific expense disadvantages (ie. environmental pressures, urban encroachment costs, etc), nationwide milk price improvements will enable those farms with a competitive advantage (size or business model) to become even more profitable. This, in turn, enables expansion and more milk supply from those farm demographics that are already generally successful. It is the economics of business, whether you are talking about dairy or any other business. A wholesale increase in milk price will generally not help those dairy farmers who are not already fundamentally well-poised to survive for the long-term.

Solutions:

1. Milk Fortification - Increase demand and supply disappearance in the short term with milk fortification program. There are conflicting claims of the effectiveness to increase demand and the cost to processors but could be an effective medium term measure.
2. Changes to the FMMO to reflect competitive prices, greater transparency and costs of production
3. Counter-cyclical payments
    a. MILC replaced with margin based trigger – adaption of national milk program
    b. Caps based on maintaining family farms most threatened by non-market inflated inputs
    c. Increased counter cyclical payment for environmental practices that address the social, economic and environmental benefits of dairy farm to some communities.
4. Grant based incentives directed specifically at 'at risk' small operations who don't have cash or access to credit to make changes to:
        i. Lower inputs (energy, fuel),
        ii. Change production practices to enable long term lower cost production
        iii. Initiate value-added programs,
        iv. Whole herd buyout for herds under 200 cows with lifetime prohibition on returning to dairy and a 10 year agricultural restriction on development,
        v. Onetime payment to herds under 200 cows to permanently limit production to current levels or a stable pay price fixed to costs of production as defined by USDA tied to a fixed quota of milk entering commerce.