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MCT COMPASS

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Orders on the Line?

Federal Milk Marketing Orders have been a part of the U.S. dairy industry since the late 1930s. Over the years, Federal Orders have been consolidated and reformed but remain firmly entrenched. Still, few outside the inner circle of the USDA's Agricultural Marketing Service's Dairy Division understand what Federal Orders do. The lack of understanding and the level of complexity in even reading Federal Order language has caused many to question their effectiveness.

In the simplest terms, a Federal Order regulates milk marketed within its boundaries. There are 10 Federal Orders that stretch from Washington to Florida and from Vermont to Arizona. In between, there are pockets of unregulated areas or states like Maine and Montana that maintain state milk pricing plans.

Two key functions of a Federal Order are to pool the value of producer milk within the Order and to conduct producer payroll and plant audits. Dairy producers within a Federal Order receive a market average (or pool) price for their milk based on how the milk in their Order was utilized. There are four classes of milk: Class I, fluid milk; Class II, soft products like yogurt and ice cream; Class III, cheese; and Class IV, butter/powder. Each class receives a different price.

If for example, the Class I price was $14.00/cwt and the Class III price was $12.00/cwt, and 50% of the milk within the order was utilized in Class I and the remaining 50% was used in Class III, the market average price for that Order would be $13.00/cwt. A dairy producer in that Order would receive a minimum price of $13.00/cwt regardless of whether the farm shipped 100% of its milk to the fluid milk plant (Class I) or 100% to the cheese plant (Class III).

In addition, Federal Orders audit producer payrolls to assure that producers are paid the minimum price and audit plants to verify how milk was utilized each month.

Unfortunately, that is where simplicity ends and exceptions begin. Not all milk has to be included in the pool; only Class I milk is required to be pooled or regulated. Milk used in the other

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KEN'S CORNER

by Ken Meyers
President
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If the Upper Midwest Federal Order, the largest Order in the program, had been voted out, it clearly would have had a national impact. It would have decoupled the manufacturing milk price from the Class III price in Minnesota and Wisconsin. And that would mean that cheese milk in four of the top-five cheese-producing states (Wisconsin, California, Idaho, and Minnesota) would have been priced independently from the Class III price.

Processor opponents to the Upper Midwest Order would have liked to see it voted out, because it would have enabled them to forward contract for milk and implement pricing formulas that are more reflective of their product mix. Producers who oppose the Order want less federal regulation, which they claim would allow them to compete more freely with their counterparts elsewhere.

But for those of you who support the continuation of the Federal Order program, however, the close vote in the Upper Midwest should serve as a wake-up call for you to get your message out. The Order provides extensive price information and data collection, but what exactly are the benefits of a Federal Order to your business and to your producers? A better understanding of the benefits could result in more industry support. MCT

Skim Support

MCT Forecast					
	Block*	Barrel*	Class III	Butter*	Class IV
Dec	1.3220	1.2860	13.45	1.2386	12.40
Jan	1.3275	1.2975	13.05	1.2450	12.70
Feb	1.2900	1.2700	12.70	1.2500	12.95
Mar	1.2700	1.2500	12.50	1.2750	12.85
Apr	1.2800	1.2600	12.35	1.2950	12.70
May	1.3400	1.3350	12.65	1.3400	12.80

** Block, barrel and butter are monthly averages of CME prices.*

As the industry enters 2007, year-end stocks of butter and cheese are expected to be near last year's levels. Stocks of nonfat dry milk are nonexistent, which sets the stage for higher prices in 2007. The world skim market price is near $1.40/lb and that is expected to support a domestic price of $1.08 to $1.30/lb. Domestic milk production and demand are key factors that will influence CME cheese and butter prices, which are expected to average between $1.35 and $1.45, respectively. MCT

Depooling quandry ...

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classes can be depooled (not included in the market average price calculation) when it doesn't make financial sense to include it. For example, if the Class III price was $14.00 and the Class I price was $12.00, only the minimum amount of milk utilized as Class III would be pooled and the market average price would be closer to $12.00 than $13.00.

Over the past eight decades, a cottage industry of lawyers, economists, and consultants has developed to interpret and debate Federal Order regulations, including pooling requirements, product price formulas for each class of milk, and understanding terms like partially regulated, diversions, and payment dates.

When the industry wants USDA to consider a change to the Federal Order program, a hearing is held. Some hearings are national in scope and apply to all Federal Orders and others pertain to an individual order.

In January 2006, USDA held a national hearing to consider changes in the make allowances used in the pricing formulas. USDA extended that hearing until the fall when more data would be available. In November, USDA published its tentative final decision and gave the producers within the orders 30 days to either vote in favor of the new make allowances or against them, which would eliminate the Order.

That's right. If two-thirds of producers or producers who represent two-thirds of the milk within an Order fail to approve USDA's proposed change, the entire Order is eliminated.

This has occurred. A hearing was held in spring 2002 regarding the Pacific Northwest and Western Orders. A tentative final decision was issued on August 8, 2003, and comments on the decision were requested by October 17, 2003. The polling of producers was completed on October 6, 2003, and producers did not approve the proposed changes by a two-thirds majority.

USDA then extended the comment period from October 17, 2003, to April 1, 2004, and mandated that a referendum be held to determine producer approval of the Western Order as amended. The referendum was completed by December 1, 2003, and failed. The Western Order, which included parts of Oregon, Idaho, Nevada and Wyoming, was terminated effective April 1, 2004

The termination of the Western Order serves as a road map to those in the Upper Midwest and in other areas that question the long-term viability of Federal Orders. In particular, the recent vote on the tentative final decision regarding the make allowance changes was close but prevailed in the Upper Midwest Order. As one observer notes, if the "no's" don't prevail on this attempt, they'll get another chance to kick the can again when USDA releases its decision on the recently held hearing to consider enhancing the Class I and II milk pricing formulas. MCT

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