

Milk Pricing
Senate Ag Committee
February 5th, 2025

In a letter addressed to USDA Secretary Vilsack, dated February 19, 2024, during the hearing process to reform the Federal Milk Marketing Orders (FMMO's), my testimony, as part of that process, underscored the importance of determining the true value of milk through discovery as it pertains to the integrity of those Federal Orders. There were high level meetings convened for the two years preceeding those hearings which involved National Milk Producers Federation (NMPF), its' Member Cooperatives, and others who collectively account for about 85% of the milk produced in the United States, all in preparation for a long overdue federal hearing process to be convened by USDA Secretary Vilsack.

There are four classes of milk; Class I is used as fluid milk, Class II is used for soft products such as ice cream, Class III is largely used for cheese production, and Class IV is for hard products such as milk powders, WMP, SMP, NDM etc. In order to accurately determine the market value of raw milk move one step away from raw milk and use the basic products made from it as the starting point, then back into a milk value by adjusting for yields and conversion costs. In order to remain competitive it is of significant importance to update the conversion formulas used to discover the true value of milk. Having achieved that value, we now have a base from which Class I values are determined. The Class I fluid market pricing is unique to that market, but the function of the FMMO establishes a differential value for Class I based on the competitive value of milk for manufacturing. Today's milk contains higher component levels, which are relevant in manufacturing dairy products, those levels should be updated to reflect the higher component levels in milk. The increased value must then be recognized in the base competitive value the FMMO's used to establish the Class I value. (Credit for this insight goes to Geoff Vandenheuvel, a knowledgeable friend associated with the Milk Producers council of California.)

There are Eleven FMMOs across the United States, it is crucial that the Class I pricing formula results in Class I being the highest Class price most if not all the time. Using the "higher of " price, be it Class III or Class IV, whichever was higher, served the industry well for many years, that pricing formula determined the actual value of milk through price discovery in real time.

Prior to 2019 there was a shift in policy, the "higher of" formula was changed to the "average of" Class III and Class IV plus 74 cents. Today, dairy farmers understand, without question, the "average of" formula, plus 74 cents, DOES NOT reflect the true value of milk through a discovery process, fact is it's a bureaucratic tool which results in price distortion. Furthermore, it calls the entire system into question. Distorting the value of milk misaligns prices and the ability to determine the true value of Class I milk, which subsequently corrupted the entire system.

Touted as revenue neutral at its' inception, the "average of" plus 74 cents pricing formula left dairy farmers grappling with a \$1.2 Billion shortfall in their milkchecks as of February 2024. Using CME futures pricing of February 15, 2024, provided by Dairy Economist Ed Gallagher, the year would end with an additional loss to farmers of \$400.49 Million, based on an annual milk production of 228.2 Billion lbs. There are less than 24,000 dairies remaining in the United States today.