



October 15, 2007

Mr. David Ikari, Chief  
Dairy Marketing Branch  
California Department of Food and Agriculture  
560 J Street, Suite 150  
Sacramento, CA 95814

**RE: October 10-11, 2007 Class 4a, and 4b Hearing -- Post Hearing Brief**

Mr. Hearing Officer and Members of the Panel:

Saputo Cheese USA Inc. appreciates the opportunity to submit the following post-hearing brief to amplify our testimony and address questions raised in Sacramento on October 10th and 11th, 2007.

Cheese Division (USA)

Questions were raised regarding the appropriate coverage of volume by California manufacturing cost allowances and followed a general theme regarding the minimum economic production level to justify an investment in a whey processing facility in the state. Hearing testimony postulated that one million pounds of whey per day was the minimum volume required to justify investment. Further testimony set \$20 million as the investment required for a roughly 2 million pound per day whey drying facility. For illustrative purposes, let's assume that a one million pound per day whey drying facility would cost \$10 million dollars - one half the cost of the aforementioned 2 million pound facility. Let's also assume that such a facility could achieve the same manufacturing cost efficiency contained in the most recent CDFA cost survey. These are very generous assumptions since the plants in the survey are more than double the size of this hypothetical plant and capital costs are generally not linear with respect to capacity. One might consider the attached simplistic model (Exhibit A) to represent the whey processing situation as it exists today in California. It is interesting to note that under the current system, the net result to the plant is the same regardless of the dry whey market. Since 1990 the western dry whey market has averaged \$0.23 and has ranged from \$0.1300 to \$0.8238. It is also interesting to note that the larger the investment, the worse the situation for the processor becomes. While the producer shares in the market price risk, he does not share in the risk that the capital investment will never be returned. If the manufacturing survey cost of \$0.269 (\$0.3099 - \$0.0406 ROI) already encompasses depreciation of the facility, it could be argued that the losses below are overstated by the amount of that depreciation because the debt service figure includes the repayment of principal. With a 30 year life, adding back straight line depreciation of \$333,000 per year on \$10 million and \$667,000 on \$20 million would still result in large net losses for both levels of investment. Our question is: who would invest in whey processing in this environment? The injustice is: if you don't invest, you are still obligated to pay producers as if you had.

Sincerely,

R. Gregory Dryer  
Executive Vice President, Administration & Services  
Saputo Cheese USA, Inc.

Exhibit A



	2007 YTD Market	2006	Market	2005 Market
<b>Statistics</b>				
Milk Per Day to yield 1 million lbs of whey	1,112,149	1,112,149		1,112,149
Class 4b Cheese Yield (3.5% BF/8.7% SNF)	10.084%		10.084%	10.084%
Cheese Per Day	112,149		112,149	112,149
Whey Per Day	1,000,000		1,000,000	1,000,000
Class 4b Whey Yield (5.8 x 8.7/8.8)	5.734		5.734	5.734
% Solids	6.38%		6.38%	6.38%
Whey Solids Per Day	63,772		63,772	63,772
Days Per Year	360		360	360
Whey Solids Per Year	22,957,791		22,957,791	22,957,791
Average Dry Whey Market	\$0.675		\$0.335	\$0.274
CDFA Cost Survey Mfg Cost Per Lb Net of Return on Investment Factor (\$0.3099 - \$0.0406)	\$0.269		\$0.269	\$0.269

**Proforma 1 mil/lb/Day Whey Plant**

Cheese Division (USA)

Whey Value Per Year	\$15,502,822	\$7,685,886	\$6,280,486
Mfg Cost Per Year	\$6,182,533	\$6,182,533	\$6,182,533
Amount due to producers in 4b milk price	\$9,373,092	\$1,556,156	\$150,756
Cash Flow before Debt service	(\$52,803)	(\$52,803)	(\$52,803)
Debt Service 10,000,000 30 yrs @ 8%	(\$888,274)	(\$888,274)	(\$888,274)
Net Cash Flow	(\$941,077)	(\$941,077)	(\$941,077)

	2007 YTD Market	2006	Market	2005 Market
<b>Statistics</b>				
Milk Per Day to yield 2 million lbs of whey	2,224,298	2,224,298		2,224,298
Class 4b Cheese Yield (3.5% BF/8.7% SNF)	10.084%		10.084%	10.084%
Cheese Per Day	224,298		224,298	224,298
Whey Per Day	2,000,000		2,000,000	2,000,000
Class 4b Whey Yield (5.8 x 8.7/8.8)	5.734		5.734	5.734
% Solids	6.38%		6.38%	6.38%
Whey Solids Per Day	127,543		127,543	127,543
Days Per Year	360		360	360
Whey Solids Per Year	45,915,582		45,915,582	45,915,582
Average Dry Whey Market	\$0.675		\$0.335	\$0.274
CDFA Cost Survey Mfg Cost Per Lb Net of Return on Investment Factor (\$0.3099- \$0.0406)	\$0.269		\$0.269	\$0.269

**Proforma 2 mil/lb/Day Whey Plant**

Whey Value Per Year	\$31,005,645	\$15,371,772	\$12,560,973
Mfg Cost Per Year	\$12,365,066	\$12,365,066	\$12,365,066
Amount due to producers in 4b milk price	\$18,746,184	\$3,112,311	\$301,512
Cash Flow before Debt service	(\$105,606)	(\$105,606)	(\$105,606)
Debt Service 20,000,000 30 yrs @ 8%	(\$1,776,549)	(\$1,776,549)	(\$1,776,549)
Net Cash Flow	(\$1,882,155)	(\$1,882,155)	(\$1,882,155)