



December 5, 2011

Sandra Schubert, Undersecretary
California Department of Food and Agriculture
1220 N Street
Sacramento, California 95814

Dear Undersecretary Schubert:

On behalf of the member companies of Dairy Institute, I am writing to request that the Department of Food and Agriculture deny the December 2, 2011 petition received from Western United Dairymen. The Department's August 22, 2011 decision (effective September 1, 2011) made significant changes in the Class 4b whey factor. It acknowledged the need to balance minimum producer prices with the wide range of cheese manufacturing, whey usage and disposal in California.

As proposed, the Western United petition would result in a massive increase in regulated price at a time of continuing historically high milk prices. While feed prices are also at historically high levels, we note that the cost of many feedstuffs have declined from their 2011 highs. Conversely, the economic factors challenging California cheese manufacturers have not abated since the June 2011 hearing. Smaller to mid-size plants have seen their margins erode as their milk prices rose sharply after the hearing decision took effect. At least one small cheese plant has exited the business as a direct result of the higher milk costs incurred because of the last hearing decision. Even larger plants have noted in their reports to shareholders that the decision created a "regulatory challenge" to their operations.

At the same time we understand that the Department was attempting to balance the needs of the industry by increasing the price formula contribution associated with whey and increasing the Class 4b minimum price. Moreover, we acknowledged the importance of such a balance last spring when proposing a sliding scale contribution from whey. But a critical part of our and our members' testimony was that this approach be carefully measured to maintain diversity among cheese manufacturing and not jeopardize plant capacity or investment in California. Calling another hearing so soon after the June 2011 hearing would be unprecedented and unwise. It would undermine business confidence in our state's industry and would jeopardize plant capacity at a time when milk production is increasing. It would increase regulatory

uncertainty and evidence a lack of policy consistency that is crucial for attracting new plant investment.

While we understand producers' desire for higher prices, we believe that increasing the Class 4b price, as proposed by Western United, would be detrimental to the industry. Production of cheese in California is still below the high reached in 2007, and more importantly, there is a very evident lack of new cheese manufacturing capacity in the state. At the same time, California milk production in 2011, will eclipse the previous record milk production seen in 2008 and the state's milk production growth rate (+2.6% year-to-date) is significantly higher than the milk production growth rate for the entire country (+1.6%). Milk cow numbers in the state are increasing and were up by 27,000 head (+1.5%) for the most recently month that figures are available. At the June hearing, both cooperative and proprietary manufacturers testified to concerns about a lack of adequate manufacturing capacity in the state. Those concerns still exist and would be pushed to a higher level if a new hearing were called so soon after the most recent hearing decision was implemented.

The notion that California dairymen are entitled to minimum price levels that are equal to those in federal orders was disputed by evidence entered into the record at the most recent hearing, and this evidence was noted in the hearing panel's report. California's minimum prices must be market-clearing, whereas the federal order pooling rules allow for milk to be sold to manufacturers at prices that are sometimes significantly below the minimum regulated price so that their market clears. The bottom line is that California prices for manufacturing milk classes must balance milk production and plant capacity *in California* and not be set at levels that arbitrarily reference regulated prices in other parts of the country with different supply and demand dynamics.

Given that neither the current nor the previous Class 4b formula has resulted in a rush of new cheese plant investment, it seems clear that the regulated price is not too low, but might in fact be too high. The new Class 4b price formulas were put in place only three months ago. More time is needed to determine if additional changes are warranted. We respectfully request that the Western United petition be denied.

Sincerely;



Rachel Kaldor
Executive Director

Cc Candace Gates