Alliance of Western Milk Producers

Representing California's dairy cooperatives and their producer-owners since 1991

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January 4, 2005

David Ikari, Chief
Dairy Marketing Branch
California Department of Food and Agriculture
1220 N Street
Sacramento, California 95814

Re: Alternative Proposal for February 1, 2005, Hearing to Consider Changes to the California Milk Marketing Stabilization Plans' Class 4b Pricing Provisions

Dear Mr. Ikari:

This alternative proposal for changes to the stabilization plans is being submitted by the Alliance of Western Milk Producers on behalf of its member cooperatives: California Dairies Inc., Dairy Farmers of America and Humboldt Creamery. Together these cooperatives represent approximately 60 percent of the milk producers in California and more than 60 percent of the milk produced in California. It should also be pointed out that two of the three have ownership interests in cheese manufacturing facilities. This proposal has been unanimously approved by the Alliance Board of Directors.

From January 2003 through December 2004 the California Class 4b has averaged 47 cents per hundredweight price below the federal order Class III price. While this difference has ranged from the California 4b price being over four dollars lower to just under two dollars higher, the average difference is significant.

When the federal order commodity values for the January 2003 through December 2004 period are plugged in the California Class 4b formula, it results in an average 4b price that is 28 cents per hundredweight higher than the current average California 4b price. When the current federal order make allowances are plugged into the California 4b formula along with the federal order commodity values the price difference increases to 39 cents per hundredweight.

The key difference between the current California 4b price and the federal order Class III price is the difference in the value of solids not fat. This is due to the Class III formula being a protein and other solids formula while the California 4b formula still does not adequately recognize the value of protein in cheese milk. While the Alliance believes that protein pricing is the where the California 4b formula must go, until the Department has the computer capability to pay producers on a protein basis as well as having processors pay in on protein, the Alliance alternative proposal maintains the current formula structure.

The Alliance alternative proposal modifies the 4b formula as follows:

1. The make allowances used in the formula should be those which cover approximately 80% of cheese and butter production, not on a weighted average basis; for cheese $0.1710 per pound, for butter $0.1570 per pound.

The Alliance has historically supported using the weighted average make allowances because the data indicated that approximately 80% of the product could be produced at or below that level. In its December release adjusted for labor and energy, the Department provided data that showed at what make allowance and below 80% of the cheese and butter could be produced. These are the values used in the Alliance Class 4b proposal.

2. The California price adjuster for cheese would be the 33-month weighted average of $0.0232 per pound. The price adjuster for butter would be the 33-month weighted average of $0.0315 per pound.

The Alliance believes that these price adjusters should be based on weighted averages and not on the simple annual average of monthly weighted averages. In addition, a longer time frame provides a better look at real market conditions.

3. The other solids make allowance remains at $0.1700 per pound of dry whey, however, it is snubbed so that the value of other solids in the formula cannot be less than zero.

The Alliance has serious questions regarding the dry whey manufacturing cost data. Alliance analysis of the Department's cost data indicates that plants included in the survey do not appear to be running at capacity and that one of those plants is a new plant. This is borne out by the very large variation in the non-labor processing costs when compared to the other costs in the dry whey manufacturing cost survey.

The Alliance has also been told by the cost analysis staff that the cheese make allowance includes the costs related to disposing of lactose and minerals from the plants processing whey into whey protein concentrate. It has been indicated that this is equivalent to approximately one cent of the cheese make allowance. No costs related to processing or disposing of whey, or the permeate left over from producing whey protein concentrate should be in the cheese manufacturing cost data since the Class 4b formula now contains a specific whey make allowance. Should the Department decide to increase the dry whey make allowance, the cheese make allowance should be reduced by the one cent now included for disposing of whey processing permeate.

Another factor of importance is the disposition of whey solids produced in California during the cheese making process. Alliance analysis indicates that only about 15 percent of these whey solids are being processed into dry whey. Nearly all of the rest is going into higher value whey protein concentrate products. CDFA has been collecting data on whey protein concentrate (WPC) production in California. Through September, 80 million pounds of WPC has been produced; 49 million pounds of high protein WPC and 31 million pounds of lower protein

content WPC. Therefore, the Alliance proposal includes snubbing the dry whey make allowance so that it cannot be higher than the price at which dry whey is sold. Unless the whey is snubbed, producers are subsidizing a small minority of cheese processors who choose to dry whey when they can't sell it to whey protein concentrate processors.

4. That the factor by which the value of milkfat is multiplied is changed to 3.67 and that the residual nonfat solids value is divided by 8.93 to arrive at a Class 4b solids-not-fat value per pound.

Contrary to the claim made in the Land O'Lakes petition, the purpose of the Class 4b formula is to develop a price for milk going into cheese. That is why the Alliance proposal maintains the cheese yield factor at 10.20 and it is why the Alliance proposes that the milkfat multiplier in the formula be 3.67 and the solids-not-fat divider be 8.93. These numbers are from the data developed by Cal Poly's Dr. Phil Tong when he collected and analyzed milk composition data collected from 13 cheese plants over a 12-month period in 2002-2003. The solids-not-fat number is supported by the Department's cost data that shows milk in the vats tested at 3.94 milkfat and 8.95 solids not fat and resulting in a cheese yield of 10.92 pounds of cheese per hundredweight of milk. Alliance analysis of the Tong data shows that to fully utilize the casein in the milk, milkfat is added to the level in the Department's cost data to achieve the yield.

All other factors in the Class 4b formula would remain the same.

Attached is a stabilization plan modified to reflect the changes proposed by the Alliance. If there are any questions, please don't hesitate to call.

Sincerely,

James E. Tillison
Chief Executive Officer
Alliance of Western Milk Producers

Stabilization Plan Language Changes

(D) The minimum prices to be paid for components used for Class 4a shall be computed as follows:

(1) For all milk fat, not less than the price per pound computed by the formula using the butter price, less an f.o.b. California price adjuster of three and ~~thirty-two~~ fifteen hundredths cents ($0.0315), less a manufacturing cost allowance of ~~thirteen and two-tenths cents ($0.132)~~ fifteen and seven tenths cents ($0.157) and the result multiplied by a yield factor of one and two–tenths (1.2).

(E) The minimum prices to be paid for components used for Class 4b shall be computed as follows:

(1) The Cheese hundredweight price shall be the price per hundredweight computed by the sum of the following:

(a) The price per hundredweight computed by the formula using the Cheddar cheese price, less an f.o.b. California price adjuster of ~~three and twenty-one hundredths cents ($0.0321)~~ two and thirty-two hundredth cents ($0.0232) less a Cheddar cheese manufacturing cost allowance of seventeen ~~and five-tenths cents ($0.175)~~ and one-tenth cents ($0.1710) all multiplied by a yield factor of ten and two–tenths (10.2).

(b) The price per hundredweight computed by the formula using the butter price, less a manufacturing cost allowance of ~~thirteen and two-tenths cents ($0.132)~~ fifteen and seven-tenth cents ($0.1570) less ten cents ($0.10), all multiplied by a yield factor of twenty-seven-hundredths (0.27).

(c) The price per hundredweight computed by the formula using the dry whey price, less a manufacturing cost allowance of seventeen cents ($0.17) the sum of which cannot be less than zero cents ($0.0000), all multiplied by a yield factor of 5.8.

(2) For all milk fat, not less than the price per pound computed pursuant to Subparagraph (D)(1) of this Section.

(3) For all milk solids-not-fat, not less than the price per pound computed by the formula using the Cheese hundredweight price established pursuant to Subparagraph (E)(1) less the product of three and ~~seventy-two~~sixty-seven hundredths ~~(3.72)~~(3.67) multiplied by the Class 4b fat price established pursuant to Subparagraph (E)(2), all divided by eight and eightyninety-three hundredths ~~(8.80)~~ (8.93).