February 6, 2006

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

RE: January 31, 2006 Milk Movement Provisions Hearing -- Post Hearing Brief

Mr. Hearing Officer and Members of the Panel:

Dairy Institute appreciates the opportunity to submit the following post-hearing brief to respond to questions from the panel and to amplify portions of our testimony presented in Sacramento on January 31, 2006. The paragraphs below clarify some of the arguments put forth in our testimony.

The panel asked me to consider the question of whether or not increasing the transportation allowances in Southern California would be an appropriate way to encourage more Southern California milk to move to fluid uses, potentially displacing some of the South Valley milk that is being brought into Southern California and thereby lowering the cost to the pool. After further consideration, I believe that my initial answer to the panel was correct.

Currently, CDFA's hauling cost survey suggests that the local haul cost in the Chino basin is 34.9 cents per hundredweight, while the cost of the haul to Los Angeles is 38.5 cents. These numbers would suggest that a transportation allowance of 3.6 cents per hundredweight would make a producer indifferent between shipping milk to a local cheese plant in the Chino basin and shipping milk to a fluid plant in Los Angeles, all other things being equal. The current transportation allowance in Southern California applicable to Chino-area milk is 9.0 cents per hundredweight

As I mentioned during my testimony, a large cheese plant in Southern California has a considerable portion of the Chino-area milk supply "tied up" so that it is not available to the fluid market. In order to entice milk away from the cheese plant, a fluid plant must be an attractive alternative to producers, taking into consideration not only hauling cost differences, but differences in premiums as well. If the operator of the Chino-area cheese plant were to lose some of its suppliers to Class 1 plants, its next best alternative would be procure milk from Kern County. CDFA data indicate that the haul cost from Kern County to the Chino area (Riverside/San Bernardino) is 88.9 cents per hundredweight, whereas the local haul in the South Valley is 29.7 cents per hundredweight. These numbers suggest that the cheese plant in the Chino area would have to pay at least 59.2 cents per hundredweight to attract milk into its plant from Kern County. Faced with this alternative or the prospect of increasing the premium it pays to Chino-area producers, it would be willing to pay premiums up to 59.2 cents per hundredweight to its current shippers to keep them sending milk to the cheese plant.

In light of the above, it would appear that an increase in transportation allowances from 9 cents to 59.2 cents, at a minimum, would be needed to encourage sufficient quantities of Chino-area milk to move to fluid uses instead of to the cheese plant. However, since this allowance would also be applied to Chino-area milk that is already moving to fluid uses at 9 cents per hundredweight, the total cost of allowances to the pool would likely rise well beyond what it would be under the proposed rate structures of DFA, CDI, or Security Milk Producers. While increasing transportation allowances in Southern California might entice a few independent producers to supply fluid uses, the amount of milk switching would not be enough, in my view, to justify the added cost to the pool.

I was also asked to comment on the transportation allowance's role as a policy tool. Dairy Institute believes quite firmly that transportation allowances should be utilized only where they are necessary to encourage milk to move to fluid uses. The allowances should not be used as a mechanism to equalize hauling costs among producers. Dairy Institute believes that producers have a responsibility under pooling to assure that the Class 1 market is served without processors having to subsidize the haul to their plants. Producers who have no better alternatives than to ship to a Class 1 plant do not need to receive transportation allowances because they will ship their milk to a fluid plant without them. Furthermore, we do not believe producers are entitled to receive transportation allowances simply because their fellow producers in other areas are eligible to receive them.

Dairy Institute appreciates the opportunity to submit this post-hearing brief, and we appreciate the hearing panel's consideration of our view.

Sincerely,

William Schiek
Economist