
LEPRINO FOODS COMPANY'S POST-HEARING BRIEF

In the Matter of:

Proposed changes in the Class 4b price formula as provided in the Consolidated Stabilization and Marketing Plan considered at the April 11, 2016 Hearing held by the California Department of Food and Agriculture in Sacramento, California.

Pending before the Secretary of the California Department of Food and Agriculture ("CDFA" or "Department") are proposed amendments to the Consolidated Stabilization and Marketing Plan concerning changes in the Class 4b price formula. The hearing on this matter was held April 11, 2016 in Sacramento, California. In accordance with California Food and Agricultural Code § 61903, Leprino Foods Company ("Leprino") is submitting this Post-Hearing Brief to clarify its testimony and respond to other testimony and questions asked by the panel during the hearing.

Use of WPC-34 vs. whey as commodity price index.

Dairy Institute's proposal to value whey at its liquid WPC-34 value is superior to the current price reference to sweet whey. As noted in my testimony, the WPC-34 price index is the most common reference used for the sale of liquid concentrated whey by cheese plants that do not have the scale to make full whey processing economically feasible.

The panel asked several witnesses about the correlation between WPC-34 prices and WPC-80 prices. Leprino Foods produces and markets both WPC-34 and WPC-80. The WPC-80 market tends to lag the WPC-34 market. WPC-34 prices typically move weekly whereas WPC-80 prices tend to be negotiated in advance and set quarterly. We analyzed the price relationship and found that our WPC-80 pricing has a 0.85 correlation co-efficient with WPC-34 prices six months back.

The witness from Milk Producers Council also argued that, if sweet whey is discarded in favor of WPC-34 as a product to which whey value is indexed, it may be more appropriate to value cheese relative to mozzarella rather than cheddar since mozzarella production now exceeds cheddar production in California. This logic is not sound. Sweet whey does not represent the most generic form of whey revenue generation; liquid whey priced relative to WPC-34 does.

Additionally, once mozzarella production is narrowed to a uniform specification for which prices received, manufacturing costs and yields can all be matched, the volume is far less than cheddar. Cheddar cheese has formed the basis of regulated cheese milk end product price formulas since California developed a separate Class 4b milk price formula in 1989. The specifications for Cheddar cheese are clearly identified in FDA's standard of identity and large volumes of bulk cheddar cheese continue to be produced.

In contrast with cheddar cheese, mozzarella specifications vary significantly in order to optimize the performance within a customer's application. FDA's standard of identity breaks the mozzarella category into eight products. To satisfy the need to have a clearly specified product in the Class 4b price formula, one product, such as low moisture part skim mozzarella, would need to be selected from within the

broader mozzarella group.

The next filter that would need to be applied to the eligible product definitions is form. The product form is intended to be bulk and not differentiated with value added processes. This eliminates the inclusion of retail product and shredded product as well as other value added processes. After narrowing the mozzarella that would be eligible for reporting to low-moisture part skim mozzarella that is sold in unshredded form of bulk size, the eligible volume is much smaller than that represented in the bulk cheddar category. We reviewed our California production and identified the proportion that would be ineligible for reporting during our FY14 fiscal year. That volume represented in excess of 80% of our California mozzarella production. I do not have visibility to our competitor's production profile, but expect that much of their mozzarella is similarly sold in shredded form given the nature of the mozzarella market. If that is the case, the volume of mozzarella that would be reportable is roughly 60% of the volume of cheddar cheese production in California within the same period. Cheddar remains the dominant form of uniform bulk cheese produced in California.

Bulk cheddar remains the best product upon which to build the Class III price formula. The price for most commodity cheeses produced within the US is referenced to the price of spot cheddar cheese traded at the Chicago Mercantile Exchange (CME).

Milk supply as only consideration in plant siting.

Contrary to the DFA witness's assertions, milk supply is not the only factor considered when making a plant investment decision. The decision to invest in new plant capacity involves several factors in addition to supply certainty. The combined plant operating costs and milk costs must be competitive with alternative supply sources on a landed basis in target markets.