NAJ Equity Newsletter April 2018

Vol. XLIV, No. 4

Multiple Component Pricing

FMMO 5 and 7

Since the inception of National All-Jersey Inc.'s (NAJ) Project Equity in 1976, its primary goal has been to secure equitable milk pricing in all regulated milk pricing systems. NAJ took another step towards achieving that goal on April 3. Together with 14 milk cooperatives and three state-wide producer organizations, NAJ coordinated the filing of a formal hearing request with the United States Department of Agriculture-Agricultural Marketing Service (USDA-AMS) to convert the Appalachian and Southeast Federal Milk Marketing Orders (FMMOs 5 and 7) to multiple component pricing (MCP) from their existing skim-butterfat pricing. If successful, eight of the ten FMMOs will utilize multiple component pricing with only the Florida and Arizona orders retaining skim-butterfat pricing.

Proponent cooperative associations:

- Cobblestone Milk Cooperative, Inc.
- Cooperative Regions of Organic Producer Pools
- Dairy Farmers of America, Inc.
- Erie Cooperative Association, Inc.
- Foremost Farms USA
- LANCO-Pennland Quality Milk Producers Assoc., Inc.
- Lone Star Milk Producers, Inc.
- Maryland and Virginia Milk Producers Cooperative Association, Inc.
- Michigan Milk Producers, Inc.
- Prairie Farms Dairy, Inc.
- Premier Milk, Inc.
- Scioto Co-Operative Milk Producers Association
- Southeast Milk, Inc.
- White Eagle Cooperative Association

Supporting producer trade associations:

- National All-Jersey Inc.
- Kentucky Dairy Development Council
- Georgia Milk Producers
- North Carolina Dairy Producers Association

The difference between skim-butterfat pricing and multiple component pricing lies in how the skim portion of milk is priced. Skim-butterfat pricing assumes all producer milk contains 2.99% true protein and 5.69% other solids. Producers are paid for their milk and Class II, III and IV processors buy skim based on those default component levels. Producer milk with higher components is under-valued, and milk with lower components is over-valued.

Data requested from the Market Administrator offices prior to drafting the hearing request supported six strong reasons to implement multiple component pricing in Federal Orders 5 and 7.

1. Increase hauling efficiencies

Above-average protein milk in the states on both sides of the border of Orders 5 and 7 is being hauled longer distances to be delivered to processing plants in the multiple component pricing orders to realize its protein value. If this milk was delivered to processing plants in Orders 5 and 7, it would lose value because the existing skim-butterfat pricing does not factor its protein into its regulated price. The protein value realized from the MCP orders more than offsets the cost of the additional hauling. However, if Orders 5 and 7 utilized multiple component pricing, milk hauling could be made more efficient while realizing the added value from protein. Furthermore, data suggests that below-average protein milk produced outside of Orders 5 and 7 is being trucked into the

National All-Jersey Inc. 6486 East Main Street, Reynoldsburg, OH 43068 www.usjersey.com
614-861-3636 VOICE naj@usjersey.com 614-861-8040 FAX

southeast to minimize its price discount from having below standard protein.

2. Eliminate transaction losses

When supplemental milk for Order 5 and 7 Class I plants needs to be purchased from the surrounding FMMOs, that milk is purchased using multiple component pricing and sold in the southeast using skim-butterfat pricing. Often these transactions result in a loss to the handler because the milk has greater value when priced using MCP. These transaction losses would not occur if Orders 5 and 7 utilized multiple component pricing.

3. Increase regulatory uniformity for manufacturing milk

Currently Class II, III and IV milk costs are different in the MCP orders than the skim-butterfat orders. Manufacturing plants in the southeast pay the same price for the skim portion of their milk regardless of its protein or solids-not-fat content. Manufacturing plants in the surrounding MCP orders pay for the solids in the skim. Therefore, milk that contains above- or below-average skim solids will carry a different cost for manufacturers located in Orders 5 and 7 compared to their counterparts located in the MCP orders. Manufactured products compete for markets regionally and even nationally. Having different milk costs creates an uneven starting point for processors located in different orders.

4. Provide better price signals to producers

Consumers value dairy products for their component content, both butterfat and protein. Historical data shows that producers in MCP orders have increased the protein content of their milk over time due to FMMO prices including value for protein.

5. The SCC adjustment will incent improved milk quality

Four of the six MCP orders include a small price adjustment based on whether producer milk is above or below 350,000 SCC. Historical data shows that producers in those orders have reduced their SCC levels over time. SCC levels in producer milk is also a global trade issue.

6. Increase the value of pooled milk

While the pooled value of Class I milk will not change with the adoption of MCP, the value of Class II, III and IV milk is expected to increase. The Market Administrators have estimated the change in value of Class II, III and IV skim solids pooled in Orders 5 and 7 from January 2008 through December 2017. According to their calculations MCP would have added nearly $83 million to pooled revenues during that 10-year period.

Now that the hearing request has been filed, USDA has 30 days to either:

- Issue an action plan to complete the hearing within 120 days, or
- Request additional information, or
- Deny the request.

In short, the absence of multiple component pricing for the Southeast and Appalachian markets (Orders 5 and 7) creates and perpetuates marketing inefficiency, lack of uniformity for manufacturing milk prices, inequitable marketing or procurement costs to handlers, and understated revenue to producers.

In 1988 the Great Basin Federal Order became the first FMMO to adopt MCP. NAJ was at the forefront of that historic change coordinating producer organizations and processors through the hearing process. Thirty years later NAJ is reprising its facilitator role to bring equitable milk pricing to another region of the U.S. dairy industry.

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