TESTIMONY OF ROBERT D. WELLINGTON
SR. VICE PRESIDENT & ECONOMIST*
AGRI-MARK DAIRY COOPERATIVE
AT THE
MASSACHUSETTS DEPARTMENT OF AGRICULTURE RESOURCES
PUBLIC HEARING IN BOSTON, MA
MARCH 20, 2007

Thank you for this opportunity to submit testimony on behalf of Agri-Mark Dairy Cooperative and its Massachusetts dairy farm families who produce the majority of fresh, wholesome farm milk in the state.

SEVERE ECONOMIC CONDITIONS ON DAIRY FARMS

Massachusetts dairy farmers, as well as their farm neighbors throughout the region have faced severe financial conditions throughout the past decade. Farm milk prices have fluctuated dramatically during this period. Even when farm milk prices seemed to recover for a brief period, the recovery was never long enough or prices high enough to compensate for losses accumulated in the years preceding recovery. A brief period of high market prices would quickly spur milk production on huge factory dairy farms in states out west. National farm milk prices would then plunge again, driving local Massachusetts and New England farm milk prices down with them.

This destructive farm financial cycle reached its worse point in 2006 when huge milk production increases in states like Texas, California, Idaho and Colorado (Table 1) collapsed market prices at the same time that energy costs skyrocketed driving farm milk production costs to record high levels. Farm milk prices fell below even those levels experienced by farmers 25 years ago (Table 2)!

At the same time that farm milk prices were collapsing, milk production costs were skyrocketing. On the milk production cost side, keep in mind that dairy farms use large amount of energy products to milk and tend the cows, cool and transport their milk to market every day, and plant and harvest crops to feed their herds. In addition, high energy prices also drive fertilizer prices up substantially.

Farm Credit Bank information showed that by last summer, the average Massachusetts dairy farm, which milks about 120 cows, was losing over $5,000 per month even before allocating no money toward family labor and return on investment. Just when energy prices finally appeared to be falling in the autumn and offering some financial hope to farms, corn prices began jumping up due to ethanol production plants. This added even more financial stress to farm families.

Farm milk prices are expected to rise in 2007 as more farms are forced out of business and milk production falls, However production costs are rising faster than milk prices, leaving dairy farms in even a worse net income situation. Supplemental feed purchases to get herds through the

winter now cost record amounts. As dairy farms look toward this spring, they see energy prices rising again. In addition, the costs of seed and all crop inputs are rising substantially as Midwest farms increase their demand for crop growing inputs in order to meet the record corn production expected this year. In the past, record volume corn crops usually meant cheap feed available for cows, but this year (and for the foreseeable future), corn prices will remain at record high levels in response to the huge demand from ethanol producing plants. All this further threatens the financial livelihood of Massachusetts dairy farms.

SUPPLY AND DEMAND FOR MILK

The political boundaries of the State can be considered a rational market definition for purposes of this petition. The costs side of dairy farmers' ledgers are peculiarly state based in terms of tax rates, input costs, regulatory burdens, and other legal compliance. While milk does flow outside and inside the state, the majority of the milk produced in Massachusetts is delivered within the state, consumed within the state, and priced according to the Federal Milk Marketing Order system.

The supply of fresh, local Massachusetts milk to the Commonwealth at a reasonable price, and with minimal supply disruption potential, is at risk. The consumer population growth continues to outpace the milk supply of Massachusetts, New England and New York milk. The Northeast region already does not produce enough milk to satisfy the dairy consumption needs of its population. Western and Midwestern milk can be shipped into the region, but at high costs to consumers, the environment, and our energy security.

There is, thus, a substantial disconnect between national supply and demand, and local supply and demand. The cost of shipping milk is at least 3 cents per retail gallon per hundred miles. Milk is a bulky product. Shipping milk from Eau Claire, Wisconsin to Boston, a 1300 mile journey, adds at least 39 cents per gallon to the cost. Shipping milk from Boise, Idaho to Boston, a 2700 mile journey adds 81 cents per gallon. Shipping milk from Fresno, California to Boston, a 3100 milk journey, adds 93 cents per gallon.

Distant supplies place our citizens at risk from supply disruptions. Terrorist attacks, food safety events, transportation or energy shocks, and other factors place our state's consumers at risk.

None of the problems faced by Massachusetts dairy farms were caused by their own actions nor can be corrected by any action they take now or in the future. Farm milk prices are set nationally by USDA and react to national supply and demand conditions, which are not necessarily relevant to local/regional supply and demand. Western farms often milk thousands of cows each, and sometimes even tens of thousands of cows each (28,000 cows at one operation alone). These factory farms expand the national milk supply and drive all farm milk prices down. For example Idaho has grown so rapidly that it is now the fourth largest milk production state in the nation, passing Pennsylvania this past fall. California passed Wisconsin a dozen years ago and now produces far more milk than the self-proclaimed "dairy state". New Mexico produces far more milk than all of New England combined and even Colorado passed Vermont in milk production this past fall! (Table 1)

TRUE VALUE OF MASSACHUSETTS DAIRY FARMS

The contributions of dairy farms to the economy and character of Massachusetts can not be measured in pounds of milk alone. Farm income is mostly spent in the local communities, multiplying the impact of each dollar several times. When the amount of dollars to spend falls by literally tens of thousands of dollars per farm, as it did in 2006, entire communities suffer.

Farm milk fuels an economic engine as it travels to plants that process it into everything from fresh drinking milk to cheese, butter, ice cream, yogurt or dozens of other products. These plants generate hundreds, and likely thousands of jobs and millions of dollars of investment in the state. It has been estimated that a single cow generates $13,000 of economic activity each year. That means that the average Massachusetts dairy farm milking about 100 cows generates $1.3 million dollars in economic activity! This can be verified when one considers that the average farm generates between $300,000 and $400,000 in milk, cow, crop and other sales with that money having a multiplier of 3 to 4 times when all money movements in the local communities as well as all the money spent at the plants who use the milk is considered.

The existence of dairy farms affects the very character of the state. They create a diverse working landscape for the recreational and scenic enjoyment of all Massachusetts citizens and visiting tourists. Dairy farms own or rent the most of the 518,570 acres of agricultural land in the state used for farming. Their economic support of farm input businesses allow those businesses to be available for other agricultural operations in the state. If dairy farmers go out of business, it will increase the stress on farm service providers and thereby all types of remaining farm operations.

In all honesty the only people who truly care about the importance of dairy farm to the state are government officials like yourself, legislators and other citizens of Massachusetts as well as cooperatives such as Agri-Mark who only have members in the local region. As far as national milk supplies are concerns, milk production INCREASES in 2006 individually in such states as California, Idaho and Texas was several times greater than the TOTAL MILK produced by all Massachusetts dairy farms. Nationally, every dairy farm in Massachusetts could have been forced out of business in 2006 and US milk production would have still shown a substantial increase from the year before.

STATE LEGISLATIVE ACTION NEEDED

The solution for keeping the Massachusetts dairy industry viable must come from the state itself for the most part. Regional efforts like the former Northeast Dairy Compact were great but need Congressional approval that has been denied for the past six years by legislators in other areas of the country. In order for Massachusetts to be assured of receiving all the benefits of a vibrant dairy industry, action is needed to offset the severe financial losses incurred by dairy farms in 2006 and so far in 2007. Legislative efforts mandating direct payments similar to what several neighboring states have already done is needed. Unfortunately just setting a higher price for Massachusetts produced milk would not work in the marketplace because milk buyers can then buy less expensive milk in nearby states and local producers would not have markets for their milk.

NEIGHBORING STATES ARE ASSISTING THEIR DAIRY FARMS

Vermont allocated $8.6 million in state funds to pay its dairy farmers beginning last summer and has just approved an additional $3 million payment to be made at the end of this month. Combined with other type payments, Vermont has given more than $12 million to its dairy farmers in the past year.

Connecticut allocated $2 million last summer for direct payments which were made in August as well as another $2 million in loans that will likely be forgiven if the farms remain in business over the next two years. In addition, the Connecticut legislature is considering another $4 million direct payment to farmers as well as a long term price safety net program similar to Maine's.

Maine has a state milk handling fee program which was passed in 2005 and collects a fee of from zero to twelve cents per gallon on packaged fluid milk sold in the state. It is collected on container sizes from one quart up to, but not including, 20-quart containers. The Maine fee rate depends upon the Class I price level in place during the month. When Class I prices are at or above $18.50 per cwt ($1.59 per gallon), the fee falls to zero. The maximum fee of twelve cents per gallon is reached when Class I prices are below $16.00 per cwt. ($1.38 per gallon).

A separate law is also in place in Maine which creates a dairy (farm) stabilization program that assures a target price is paid to the state's dairy farmers based upon actual cost of farm milk production information. Those payment rates were last updated to reflect higher farm costs through July 2006. There are three payment tier rates under the program. The first 2.1 million pounds of annual production receives a price of $18.68 per cwt. Production between 2.1 million and 4.9 million pounds receives $16.23 per cwt. Annual production at a large farm in excess of 4.9 million pounds (above approximately 250 cows) receives $15.43 per cwt. The Maine program also takes in consideration the current MILC Federal payment program. The Maine program has made a substantial difference in maintaining the dairy industry in that state.

The following comments are from the rule adopted by the Maine Milk Commission on September 1, 2006 relative to the costs of producing milk in the state:

III. CONCLUSIONS OF THE STUDY OF PRODUCING MILK IN MAINE

This project has derived a representative cost of production estimate for Maine dairy farmers. This estimate is based upon responses from the 2004 Cost of Production survey implemented by the University of Maine and the Maine Milk Commission. This survey was used to develop typical farm units to represent the dairy farming population as a whole. From these characteristic farms, economic engineering budgeting approaches were applied to value all factors used in dairy production following best practice budgeting approaches.

Overall, when all factors of production are accounted for, including variable operating expenses, overhead, depreciation and interest, the average long-run cost of producing milk is estimated at $25.71/cwt for Maine dairy producers. When depreciation and interest are omitted, the short-run cost of production is $17.66/cwt.

Several factors contribute to the higher cost of production of Maine producers over Northern Crescent producers[1] as a whole. The total cost of production for the Northern Crescent farm was $21.86/cwt. The "average" Maine farm budget includes additional costs that are not captured in the USDA budget[2]. When the Maine and the USDA budget are aligned, the total cost of production for Maine is $23.40/cwt and $21.76/cwt for the USDA Northern Crescent region. The difference of $1.64/cwt is largely accounted for by higher fuel, lube and utility costs, repair costs and property taxes of Maine producers. Dairy producers operate under set rules and regulations that are generally beyond their control. Producers do have control over repair expenses but in order to reduce this cost, investment in new equipment is required. Under current price conditions in the dairy sector, capital formation for these purchases will be difficult making cost savings in this component difficult to realize.

Based on information provide at public hearing on July 21, 2006 and based on the most recent updates to the 2004 University of Maine cost of producing milk in Maine study, the Commission hereby adopts the following 3 levels of target prices, each representing a range of annual production. These are based on the findings of the most recent study conducted in accordance with 7 M.R.S.A. Section 2953 to estimate the short-run break-even point within each tier. These short-run breakeven target prices have been updated to reflect higher costs through July 2006.

Tier:	***Annual Production Range:***	***Target Price:***
Small Farm	***0 – 21,355 hundredweight***	***$18.68***
Medium Farm	***Over 21,355 to 49,079 hundredweight***	***$16.23***
Large Farm	***Over 49,079 hundredweight***	***$15.43***

At current milk prices[3], the returns to farm labor are negative indicating that dairy producers will be forced to reduce inventories or liquidate farm assets to remain in operation. Based upon the results of these budgets, this situation will only become more exacerbated, as petroleum prices are higher now than when the survey data was collected.

COSTS OF PRODUCING MILK IN MASSACHUSETTS

The costs of producing milk in Massachusetts are very similar to that in Maine. In fact Massachusetts costs are likely even higher than those in Maine due to the fewer number of dairy farms in Massachusetts (about 180 farms) versus Maine (about 360 farms). Fewer farms mean

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[1] *The "Northern Crescent" region includes all of the Northeast, portions of Pennsylvania, Maryland, Minnesota and Ohio plus all of Michigan and Wisconsin.*

[2] *The Maine budget includes capital recovery over the whole herd of animals while the USDA budget only includes breeding stock. The opportunity cost of land is also computed differently so this component is also removed from the comparison.*

[3] *E.g., The Federal Order minimum producer price (statistical blend) effective for June 2006 was $12.66*

fewer support service providers that usually results in less competition and higher prices. Wage rates also tend to be higher in more urbanized Massachusetts than in Maine. In addition, the Maine costs estimated last summer does not include the much higher corn and other cropping costs that exist today.

Massachusetts dairy farms average less than 2.1 million pounds of milk annually and their costs are at least the $18.68 set by the Maine Milk Commission for dairy farms in that size range. Keep in mind that that cost estimate excluded interest and depreciation and is essentially the short-run costs of production.

The public at large receives many benefits from Massachusetts dairy farmers. These include open space, working landscapes, quality of life, agrarian culture, and a highly attractive backdrop for tourism. The public receives these benefits free of charge. However, if the market does not cover the short run costs of the economic product, milk, produced by farms, then the state should consider whether to pay for these benefits to the extent producers are not compensated from the marketplace. The Department may wish to explore its powers to provide a Green Payment program to farmers, and a method of funding it. The Department may also wish to recommend legislation accomplishing this Green Payment goal. Essentially, as the price of farm milk goes down below cost of production levels, the Green Payment program would kick in to pay for the public services provided by farms. If the farm milk price is high, the public services will come free to the state in the form of dairy farms continuing their businesses. A fee at some level in the dairy marketing channel could be considered to offset these added expenditures.

Given that information, Massachusetts dairy farmers must receive at least $18 per hundredweight in the short-run or they can not cover their immediate costs. This is an extremely conservative cost figure. Any program involving state payments to farmers should use an $18 price as a target payment.

MASSACHUSETTS CAN AND SHOULD ACT

Neither the Maine program nor the Green Payments program would affect the competitiveness, efficiency or markets of producers or processors in other states. The federal marketing order makes supply and demand virtually irrelevant to proper market signals in Massachusetts. Dairy farm stabilization in Massachusetts will not burden other states because the state is such a small player in the national market, that any supply stabilization will have no market impact. Farm decisions in other states are affected by far more direct factors than any Mass dairy stabilization efforts could have. These included input costs, taxes, regulatory costs, and other factors. Also, consumers will not be harmed by a state price stabilization program, because the retail price of milk rarely falls significantly when the farm price falls. Retail milk prices are far more directly affected by other factors such as competition among retailers, transportation costs, labor costs, energy costs, community income, etc. On any given day, the price spread for milk within the same community can vary by a $1.00 per gallon or more.

Assuming consumers paid 10 cents per gallon more to keep the state dairy farmers going at current levels, and assuming the 20 gallon per capita consumption of milk found by USDA, the annual cost per consumer for a truly effective long term solution is at most $2.00. If milk has to be shipped from the high growth regions, such as Idaho at 81 cents per gallon transportation

costs, then the annual consumer cost could eventually rise by as much as $16.20 per year at 20 gallons per capita consumption.

BEWARE OF PROPOSED PROGRAMS THAT WILL NOT WORK

We have heard that some non-farm groups are proposing a dairy farm income insurance program similar to a national crop insurance program so state programs will not be needed. We disagree with those proposals. The farmers I speak with do not view that as an acceptable alternative and usually have little positive to say about the current ineffective crop insurance programs.

Insurance only works when a relatively few members of a large group experience a relatively rare occurrence. For example, home fire insurance works and is usually inexpensive to purchase because fortunately, few homes burn down each year. However, what would that insurance cost is ALL homes burned down on a regular basis every two or three years? This is effectively what happens in the dairy industry. This repeating, destructive low milk price problem is what Massachusetts dairy farmers have faced so many times that such an insurance programs would cost farmers more in premiums than they would gain. We are concerned that discussion of such ineffective income insurance programs is merely a way to distract well meaning dairy farm supporters in the legislature and elsewhere.

Thank you for this opportunity to express our comments.

* I can be reached at 1-978-687-4934 or at rwellington@agrimark.net if you have any questions. My background and experience are as a professional dairy economist with graduate and undergraduate degrees in agricultural economics from Rutgers University. I spent the first eleven years of my career at the USDA-Milk Market Administrator's Office in NYC serving as senior economist and chief of research and market information. In 1989 I became Sr. Vice President for Economics, Communications and Legislative Affairs for Agri-Mark Dairy Cooperative, serving our farmer member/owners in Massachusetts, the five other New England states and New York State. I have served on many national and state economic advisory committees during my career (list available opon request).

TABLE 1:

Milk Cows and Production: By State, United States, and Puerto Rico, 2005-2006

State	Milk Cows 1/		Milk Per Cow 2/		Milk Production 2/		Change From 2005
	2005	2006	2005	2006	2005	2006	
	--- 1,000 Head --		---- Pounds ----		-- Million Pounds --		Percent
AL	16	14	14,000	14,500	224	203	-9.4
AK	1.1	0.8	12,273	12,250	13.5	9.8	-27.4
AZ	165	173	22,679	22,855	3,742	3,954	5.7
AR	22	20	13,545	13,250	298	265	-11.1
CA	1,755	1,780	21,404	21,815	37,564	38,830	3.4
CO	104	110	22,577	23,155	2,348	2,547	8.5
CT	20	19	19,200	19,316	384	367	-4.4
DE	7.4	7.0	17,662	17,429	130.7	122.0	-6.7
FL	137	132	16,591	16,417	2,273	2,167	-4.7
GA	81	77	17,259	18,234	1,398	1,404	0.4
HI	5.4	4.3	12,889	13,256	69.6	57.0	-18.1
ID	455	488	22,332	22,326	10,161	10,895	7.2
IL	104	103	18,827	19,204	1,958	1,978	1.0
IN	156	165	20,295	19,994	3,166	3,299	4.2
IA	195	205	20,641	20,146	4,025	4,130	2.6
KS	111	112	20,505	20,920	2,276	2,343	2.9
KY	106	98	12,896	13,276	1,367	1,301	-4.8
LA	35	32	12,400	12,375	434	396	-8.8
ME	33	32	18,030	17,938	595	574	-3.5
MD	71	64	15,986	17,078	1,135	1,093	-3.7
MA	17	16	17,059	17,375	290	278	-4.1
MI	312	320	21,635	22,188	6,750	7,100	5.2
MN	453	450	18,091	18,587	8,195	8,364	2.1
MS	25	23	15,280	14,826	382	341	-10.7
MO	117	115	16,026	16,000	1,875	1,840	-1.9
MT	19	19	19,579	18,632	372	354	-4.8
NE	60	61	17,950	18,328	1,077	1,118	3.8
NV	25	27	21,680	20,667	542	558	3.0
NH	16	15	18,875	19,533	302	293	-3.0
NJ	12	11	16,000	16,182	192	178	-7.3
NM	328	355	21,192	21,515	6,951	7,638	9.9
NY	648	638	18,639	18,879	12,078	12,045	-0.3
NC	54	51	18,741	18,510	1,012	944	-6.7
ND	33	32	14,182	14,688	468	470	0.4
OH	270	274	17,567	17,737	4,743	4,860	2.5
OK	75	73	16,480	16,630	1,236	1,214	-1.8
OR	121	118	18,876	19,000	2,284	2,242	-1.8
PA	561	554	18,722	19,390	10,503	10,742	2.3
RI	1.1	1.1	17,000	17,273	18.7	19.0	1.6
SC	18	17	16,000	16,353	288	278	-3.5
SD	81	81	17,741	18,580	1,437	1,505	4.7
TN	70	67	15,743	15,657	1,102	1,049	-4.8
TX	320	335	20,131	21,328	6,442	7,145	10.9
UT	88	86	18,875	20,291	1,661	1,745	5.1
VT	143	141	18,469	18,383	2,641	2,592	-1.9
VA	105	102	16,990	17,363	1,784	1,771	-0.7
WA	241	237	23,270	23,055	5,608	5,464	-2.6
WV	13	13	14,923	15,385	194	200	3.1
WI	1,236	1,243	18,500	18,824	22,866	23,398	2.3
WY	4.9	6.7	14,878	17,612	72.9	118.0	61.9
US 3/	9,043	9,112	19,565	19,951	176,929	181,798	2.8
PR4/	91	90	8,154	8,222	742	740	-0.3

1/ Average number during year, excluding heifers not yet fresh.
2/ Excludes milk sucked by calves.
3/ May not add due to rounding.
4/ Puerto Rico is not included in the U.S. total.

TABLE 2:
FEDERAL ORDER BLEND PRICE FOR FARM MILK, CENTRAL MASSACHUSETTS ZONE

	1981	2006	Difference
		dollars per hundredweight	
JANUARY	$14.45	$14.53	$0.08
FEBRUARY	$14.45	$14.00	($0.45)
MARCH	$14.19	$13.18	($1.01)
APRIL	$14.06	$12.39	($1.67)
MAY	$13.85	$12.36	($1.49)
JUNE	$13.82	$12.41	($1.41)
JULY	$14.29	$12.53	($1.76)
AUGUST	$14.60	$12.81	($1.79)
SEPTEMBER	$14.78	$13.18	($1.60)
OCTOBER	$14.86	$13.79	($1.07)
NOVEMBER	$14.65	$13.96	($0.69)
DECEMBER	$14.39	$14.17	($0.22)
AVERAGE	$14.37	$13.28	($1.09)