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# A Losing Proposition

By RINKER BUCK
Courant Staff Writer

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CORNWALL -- With the supermarket price of milk poised to climb to $4 a gallon this month, consumers might have a hard time finding sympathy for the plight of dairy farmers.

But if you want to understand the story behind skyrocketing milk prices, one place to start is Buddy and Irene Hurlburt's Hautboy Hill Farm.

The Hurlburts and their six children work 200 acres on a hill overlooking Cornwall Hollow, just above the picturesque cemetery where Civil War Gen. John Sedgwick is buried with his men.

Hurlburts have been farming on Hautboy Hill since 1748, and when he took over the farm from his father in the 1970s, Buddy, now 48, did exactly what economists say small farmers must do to protect their income from the perilous economics of dairy farming.

He diversified.

In addition to milking 90 Jersey and Holstein cows, the Hurlburts raised and packaged their own brands of beef and pork, kept a flock of chickens for eggs and sold sand off a small lot they'd opened up for stall bedding for their cows.

But then what some dairy economists have called a perfect storm of negative financial news did in the Hurlburt herd.

In 2002 and 2003, foreign imports of whey and cheese products and flat domestic consumption of milk kept the federal adjusted milk price in the $12 to $13 range per hundredweight. (A hundredweight is equal to 100 pounds, or 11.63 gallons.) This bulk price is well below the $15 per hundredweight that most Northeastern farmers need to cover their costs.

In response to the prolonged price slump, dairymen from powerhouse dairy states such as California and Wisconsin added to their herds and hiked production to shore up their revenues, quite literally flooding the market and further restraining prices. Smaller producers such as Hurlburt - without access to the capital and economies of scale of the big Western and Midwestern producers - were trapped in a classic squeeze.

"For those two to three years that we were stuck with $12 and $13 hundredweight prices for our milk, we were losing $70,000 or more annually on our dairy," Hurlburt says. "The profits from our beef, pork and chicken operation, essentially, were being used to prop up a losing dairy business."

So, in February, after much anguish and a long, revealing analysis of his costs with his banker, Hurlburt sold off most of his herd and went into the business of selling specialty bottled milk directly to consumers and local stores.

That decision became more symbolic than the Hurlburts realized at the time. Over the winter, another perfect storm was forming to drive milk prices up again. Farm closures, herd sell-offs and rising grain prices have drastically curtailed milk production. Supplies were also reduced by a ban on the import of cheaper, high-production cows from Canada because of mad cow disease, along with quality control problems with the growth hormones injected into cows to boost production.

The result was a classic swing of supply and demand. In March and April this year, the federal adjusted price for milk began climbing toward $16 per hundredweight, and for May the price will be slightly over $18, a historically high price that is expected to push supermarket prices up to $4 for a gallon of milk. The price increases probably will show up in supermarket coolers as early as this week.

Most dairy economists expect high milk prices to remain through the summer, after which the higher production rates of the warmer months gradually will return supply to more normal levels, moderating prices by late fall.

The Hurlburts' fate, and that of farmers like them, typifies a business that many farm economists say has been heavily weighted in favor of processors and supermarkets for years. In Connecticut alone, according to figures prepared by the department of agriculture at the University of Connecticut, the number of dairy farms fell from 357 in 1989 to 192 in 2002 - a drop of nearly half in only 13 years.

Ronald W. Cotterill, an agricultural economist at UConn and the director of its Food Marketing Policy Center, has completed several exhaustive studies of pricing structures in the dairy industry and predicts that Northeast farms will continue to fail until states address a national system that returns higher prices to Midwestern and Western producers.

"What we've found was that farmers were getting about $1 a gallon to produce the milk, and processors were charging about 60 cents to bottle and deliver that gallon to the supermarkets," Cotterill says. "The supermarkets were then getting about $3.10 at retail per gallon. Our analysis is that this represents at $1 per gallon [in the final price] too much. The supermarkets have had huge margins for years."

Capturing these middleman and retail margins by bottling their own specialty milk had long been a dream of the Hurlburts. Cornwall lies in the heart of the prosperous Litchfield County second-home market, where specialty cheeses, baked goods and organic products have made gourmet food stores a growth industry. Two years of low prices for commercial bulk milk finally forced the Hurlburts to act.

At the urging of his banker, Buddy Hurlburt drew up a business plan showing that, with just six to eight cows, he could produce 35 gallons of "creamline" whole milk a day. (Old-fashioned creamline milk, which is pasteurized but not homogenized, has to be shaken to mix in the heavier cream at the top.)

At the specialty prices charged by local stores, he could sell this for $6 a gallon, which would earn him more than $1,400 a week in gross proceeds, or about $75,000 a year. With the cash from selling off his herd earlier in the year, Hurlburt had enough to invest in pasteurizing and bottling equipment. Eleven local stores agreed to take on his new Hautboy Hill Farm brand, which the couple will begin selling at their farm stand in Cornwall in a few weeks.

"We were amazed once we ran the numbers," Buddy Hurlburt says. "Grossing $75,000 a year direct to us was better than we were doing running 90 milk cows in a commercial operation. We realized that running a big commercial dairy was just a money-laundering operation - moving the money around but not returning the profits of milk to us."

Other economies will make a big difference in the Hurlburts' operation. Instead of raising more than 100 acres of corn and "losing money on it by feeding it to cows," Hurlburt said, he will graze his smaller herd on grass and feed them a small amount of grain supplements every day. His corn fields will be converted to a cash hay crop.

Bills of $3,000 a month for supplementary grain for a big herd, and $1,000 a month in electric bills to run milking machines for 90 cows, are a thing of the past.

"When you have a big cow operation, the expenses are horrendous and just swamp you," Irene Hurlburt says. "Tractors don't break down and require a $130 part. They break down and require a $1,300 part. It's a huge relief to be moving onto something new."

Adds Buddy: "What's ironic about all this is that we're actually regressing to a model of farming from the 1800s, when farmers sold their milk directly to customers. That's what the modern farm economy has done to us."

David Jacquier, 54, a director of the huge New England dairy cooperative Agri-Mark, has no immediate plans to change the business model of his dairy operation. But the 375 cows on his Elm Knoll Farm in East Canaan produce 10 million hundredweight of milk a year, resulting in devastating losses when prices stay low.

Until prices began spiking upward this spring, Jacquier says, he was losing $1.50 per hundredweight. "I lost more in the last two years - almost $700,000 - than I gained in equity in the last 32 years," Jacquier says. "Essentially, I lost my retirement."

Adjusted prices now in the $16 to $18 range per hundredweight will help him recoup this summer, Jacquier says, but rising fuel and grain costs have already increased his break-even point this year about $1, to more than $14 per hundredweight.

If, as expected, prices this winter drop back down to $14 or $15 per hundredweight, "we'll be right back where we were before, losing money because the basic price doesn't support our costs."

But the three generations of Jacquiers who have farmed in East Canaan may already have reached their end.

"For 10 years I had the best partner you could have in this business, my son," Jacquier says. "Then we invested $1.2 million in a new dairy building and faced these two years of low milk prices. I bought my son out and now he drives a truck, working the gravel pits, and he's making a better living than he did in dairy."

Jacquier is planning to give dairy farming five or 10 more years to see if price trends improve.

"If they don't, I guess I'll quit and build houses for a living," he says. "That will be my last crop."

Meanwhile, down in Cornwall, Buddy and Irene Hurlburt are busy making the last improvements to their creamery while they await delivery of their new glass bottles, and preparing the farm stand beside their house for its spring opening. They're looking forward to bottling their first batch of milk and beginning delivery to stores.

Parting with his herd over the winter was difficult, mainly because the Hurlburts had raised them all from calves and each had a name. The patterns of life on their hill will change in other ways.

"I did all of my best thinking of the day during milking, and, you know, it usually took about six hours," Buddy Hurlburt says. "But now I'll be done milking and bottling in just a couple of hours. I guess I'll just have to learn to think quicker."

*A discussion of this story with Courant Staff Writer Rinker Buck is scheduled to be shown on New England Cable News each half-hour today between 9 a.m. and noon.*