TESTIMONY OF THE KROGER CO.

FEDERAL MILK MARKET ORDER HEARING

7 CFR PARTS 1005, 1006, AND 1007

DOCKET NO. DA-07-03

MILK IN THE APPALACHIAN, FLORIDA AND SOUTHEAST MARKET

My name is John Hitchell. I am employed by The Kroger Co. Manufacturing Group as the General Manager of Raw Milk Procurement. I am appearing today in opposition to the proposed Class I differentials in proposal number one.

The Kroger Co. operates four fluid distributing plants that are regulated handlers in the Federal Orders under discussion at this hearing. Winchester Farms located in Winchester, Kentucky and Westover Dairy located in Lynchburg, Virginia are regulated in Federal Order #5. Heritage Farms Dairy located in Murfreesboro, Tennessee and Centennial Farms Dairy located in Atlanta, Georgia are regulated in Federal Order #7.

The Kroger Co. believes that the implementation of the proposed Class I differentials will disrupt traditional pricing relationships dating back to the Class I differentials mandated in the 1985 Farm Bill and re-established during Federal Order reform in 1999 between fluid handlers located inside and outside Order #5 and Order#7 and place our dairy plants in an unacceptable competitive situation.

Winchester Farms has operated since 1982 and the plant has serviced the Cincinnati markets and part of West Virginia within Federal Order #33 and the Louisville/Order #5 market since it's inception. The Order #33 sales represent approximately 53% of the plant's sales and the sales in the Order #5 area represent 44%.

EXHIBIT

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The price relationship between Winchester Farms and their competitors located in Louisville and the Cincinnati market has remained unchanged since the increase in the differentials mandated in the 1985 Farm Bill and the adjustment in the Class I differentials implemented in 2000 with the conclusion of the Federal Milk Order Reform process in 1999.

The proposed increase in Class I differentials contained in this hearing would the raise the differential at Winchester \$.40/cwt. The Louisville differential would be increased only \$.10/cwt. and the differentials in the Cincinnati market are untouched by this proposal.

Implementation of these differentials would place Winchester Farms in an unacceptable uncompetitive position compared to their fluid competitors located in Order #33 and Louisville. The Kroger Co. is requesting that the Class I differential for Winchester Farms and Louisville, Kentucky remain at the current level of \$2.20/cwt. in order to maintain the traditional spread in Class I differentials between Winchester and their competitors in Cincinnati, West Virginia and Louisville. At a minimum The Kroger Co. requests that the Class I differential increase at Winchester, Kentucky be no greater than the proposed Class I differential increase at Louisville of \$.10/cwt.

The proposed increase in the Class I differential at Westover Dairy is \$.40/cwt. Westover has serviced a Class I fluid customer located in Order #1 for over 6 years. Implementation of these proposals would place Westover in an uncompetitive position compared to fluid processors located in Order #1 which is not being addressed at this hearing and will not be receiving an increase in Class I differentials.

In addition dairy farmers located in the Mid Atlantic States produce the majority of the raw milk supplied to Westover Dairy. The current pricing structure is generating a sufficient income to dairy farmers to supply the majority of Westover's raw milk requirements.

Implementation of the proposed differential at Westover Dairy will place the plant in an uncompetitive situation compared to fluid processors located in Order #1 who are in a position to service their customer. In addition, the current pricing structure has maintained a local milk supply for the plant. For these reasons The Kroger Co. requests the Class I differential remain at the current level of \$2.80/cwt.

The Kroger Co. has operated Heritage Farms Dairy since 1980. When Heritage Farms opened the plant serviced the Atlanta market. The sales within the Atlanta market continued to increase to a level that justified The Kroger Co. making a significant capital investment in 1996 when we opened Centennial Farms Dairy. Part of the justification for the facility was based on the traditional spread of Class I differentials between Murfreesboro, Tennessee and Atlanta, Georgia of $.50/cwt.

The proposed increase in the Class I differential at Heritage Farms Dairy is $.30/cwt. The proposed increase in the Class I differential at Centennial Farms Dairy is $.70/cwt. If adopted as proposed the spread in Class I differentials between Heritage Farms and Centennial will increase from $.50.cwt. to $.90/cwt.

An increase in the spread of the Class I differentials of this magnitude between Murfreesboro, Tennessee and Atlanta, Georgia will call into question the efficacy of The Kroger Co. original capital investment in a fluid milk plant in Atlanta. I can assure you that there is a question as to whether we would have made the decision to make that investment and generate the economic opportunities that Centennial provides the Atlanta area.

The implementation of the proposed Class I differential increase at Heritage Farms and Centennial Farms will inflate the historical spread between these two markets. The Kroger Co. requests that the Class I differentials be unchanged and maintain the historic spread between Murfreesboro and Atlanta.

As we have attempted to illustrate increasing Class I differentials in the Southeast in isolation will generate competitive discrepancies with the surrounding markets. In addition the Class I differential increases as proposed will distort historical price levels between plants regulated in Order #5 and Order #7 and produce competitive inconsistencies where none exist today.

For these reasons The Kroger Co. requests that the Secretary not adopt the proposed changes in Class I differentials in Order #5 and Order #7.