Saputo

January 22, 2007

Hearing Clerk
Stop 9200-Room 1031
United States Department of Agriculture
1400 Independence Avenue, SW
Washington, D.C. 20250-9200

Re: Docket no. AO-14-A74, et al.; DA-06-01: Milk in the Northeast and Other Marketing Areas; Tentative Final Decision on Proposed Amendments and Opportunity To File Written Exceptions to Tentative Marketing Agreements and Orders.

Subject: Saputo Cheese USA Inc. Comments on USDA Tentative Decision on Make Allowances

Testimony at the hearings substantiated significant manufacturing cost increases that have taken place since the current make allowances were established. Manufacturers do not have the ability to recoup these cost increases under the current system. The interim decision appears to have largely ignored these facts. Establishment of a base manufacturing milk price enables the market to adjust when prices are too low by the payment of premiums above the minimum. Establishing too high a minimum price based on unrealistic manufacturing cost data can permanently damage the industry's infrastructure. That generally describes what has in fact been taking place in the industry over the past several years.

Dr. Stephenson clearly testified that his cheese cost sampling methodology was stratified and heavily weighted toward the largest of plants. He indicated an adjustment was required to make his sample representative of the universe and in fact testified as to the extent of adjustment required. In the decision, USDA contends that Stephenson's cheese adjustment can not be incorporated because a similar adjustment was not presented for the other applicable products. This conclusion is clearly flawed since Stephenson's sampling techniques for those products were not stratified to begin with.

Cheese and whey operations typically share many services and their related costs. Determination of cost attributable to either process is by its nature somewhat arbitrary. One company may attribute relatively more cost to its cheese process and less to whey processing, while another may do the opposite. The combined costs, however, should be verifiable and indisputable. California cost studies have led to a relatively low cheese

Cheese Division (USA)
Saputo Cheese USA Inc.
25 Tri-State Int'l Office Center
Suite 250
Lincolnshire, Illinois
US 60069
Tel: (847) 267-1100
www.saputo.com

make allowance of 17.8 cents (low but still higher than the USDA tentative decision of 16.82 cents) and a relatively high whey make allowance of 26.7 cents. When weighted by the proportionate volumes of the two product streams, these numbers in combination come remarkably close to the combined 20.77 cents for cheese and 20.32 cents for whey that Dr. Stephenson testified to after taking marketing costs and updated energy costs into account. When USDA decided to ignore the high California whey make allowance but to consider the relatively low cheese make allowance in isolation, an injustice occurred because of the aforementioned interdependency. USDA was wrong to have arbitrarily chosen which costs to selectively include or exclude in this case.

Finally, serious flaws exist in the calculation of return on investment, or capital cost, or depreciation and interest, or whatever one chooses to label the factor that represents amount required to pay for the facility and equipment necessary to generate the volume of product represented by these cost studies. In Dr Stephenson's case, he reports an ROI factor of $0.0085 per pound of cheese for eight low cost plants that generate on average, 88.7 million pounds of cheese per year. It appears he employs a bond index factor of somewhere near 7%. 88.7 million pounds at $0.0085 per pound yields just over $750,000 per year. If money costs 7% and the $750,000 represents interest alone with no return of capital or depreciation, then the plant would cost just under $11 million dollars (much less if you include depreciation). Clearly, a plant capable of generating that volume of cheese would cost or be worth at least 5 or 10 times that amount. In other words, there are serious shortcomings in the factor used to represent capital cost or return on investment in both the California and the Stephenson studies. This underestimation, when coupled with aforementioned increases in manufacturing costs, has impaired many processors' abilities to attain acceptable margins.

We request that USDA revise the interim decision to incorporate the California whey make allowance data and to utilize a cheese make allowance which encompasses Dr. Stephenson's adjustment for the stratified sample.

Very truly yours,

R. Gregory Dryer

R. Gregory Dryer
Executive Vice President - Administration & Services
Saputo Cheese USA Inc.

DD:ba