United States Department of Agriculture

Before The Secretary of Agriculture

In re: [Docket No. 23-J-0067; AMS-DA-23-0031]

Milk in the Northeast and Other Marketing Areas

Hearing beginning August 23, 2023

Testimony Presented By:
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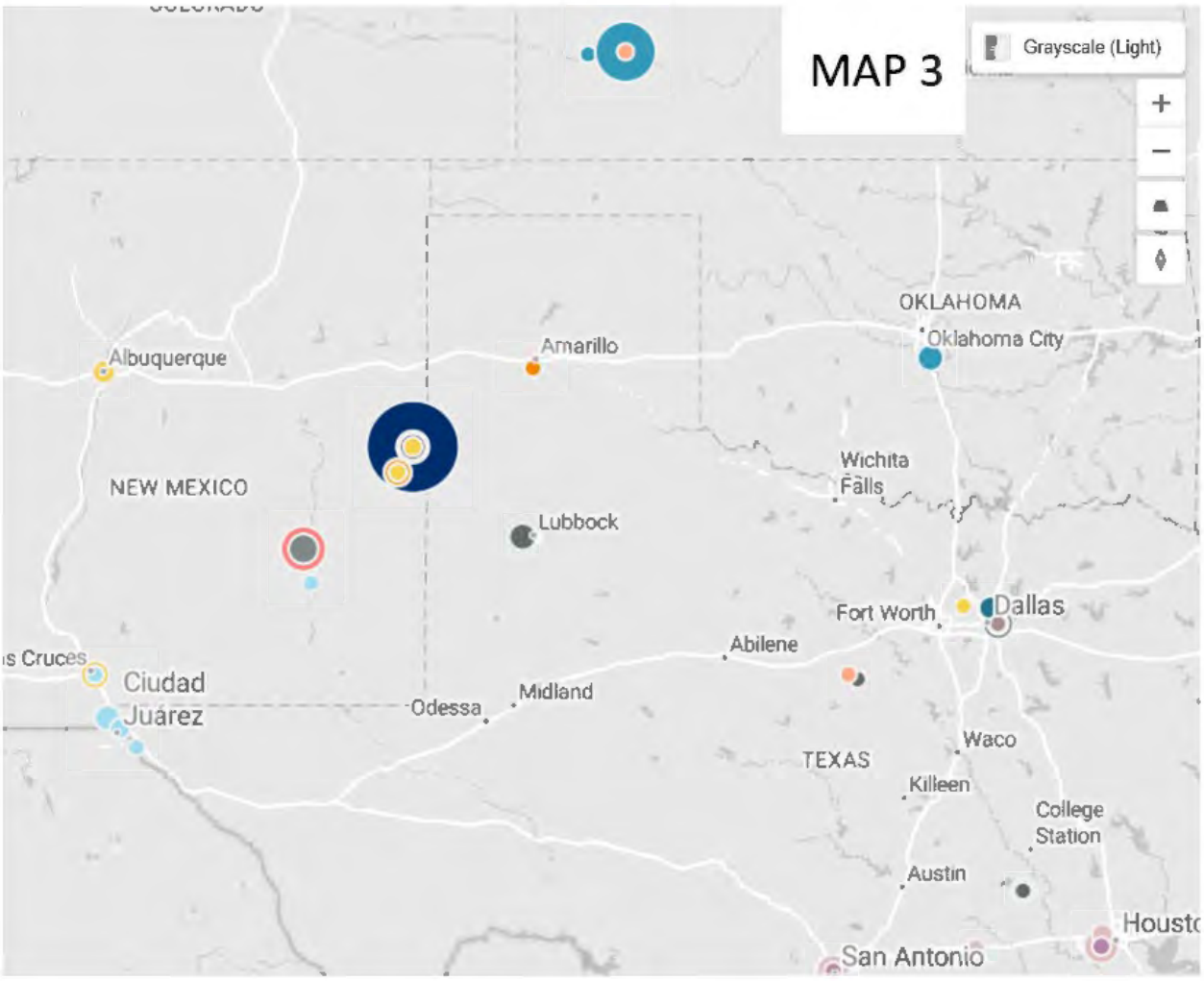
Hearing Subject Area: Class I and Class II Differentials

My name is John Kang, and I am the Director of Sales and Marketing with Dairy Farmers of America (DFA)'s Southwest Area. I attended the University of Texas with a major in Communications and Marketing. The primary reason I applied to DFA is because of their support for family-operated businesses. I have been working for DFA for 8 years and involved in marketing milk across 4 geographical areas within our Cooperative. I serve as the customer interface for all the customers in the Southwest Area and have been involved in Federal Order pooling for more than 5 years. My office is in Grapevine, Texas.

Today, I am testifying in support of Proposal 19, submitted by the National Milk Producers Federation (NMPF), to update the Class I pricing surface. The update would further the goals of ensuring adequate supplies to Class I plants and encourages the efficient movement of milk.

I would like to focus on the marketing conditions in my region which encompasses Federal Order 126. The Southwest Federal Order's milk supply has dried up in areas where most of our Class I plants are located. Between 2010 to 2023, the Southwest Area has lost 43 percent of its milk shed. This loss has forced milk to stair step into

areas where the majority of Class I plants are located. For example, the Stephenville, Texas milk shed will supply the Class I plants in the southern region of Texas and the Dallas-Fort Worth Class I plants are then supplied by the Texas Panhandle. Several years ago, a large supply of milk in south Texas supplied the South Texas demand. That left a larger local supply to fulfill the Dallas-Forth-Worth (DFW) Metroplex and created less milk movement from the Texas Panhandle. Unfortunately, the southern milk shed is now close to nonexistent, and milk must be stair stepped south from further distances. Please refer to Map 3.

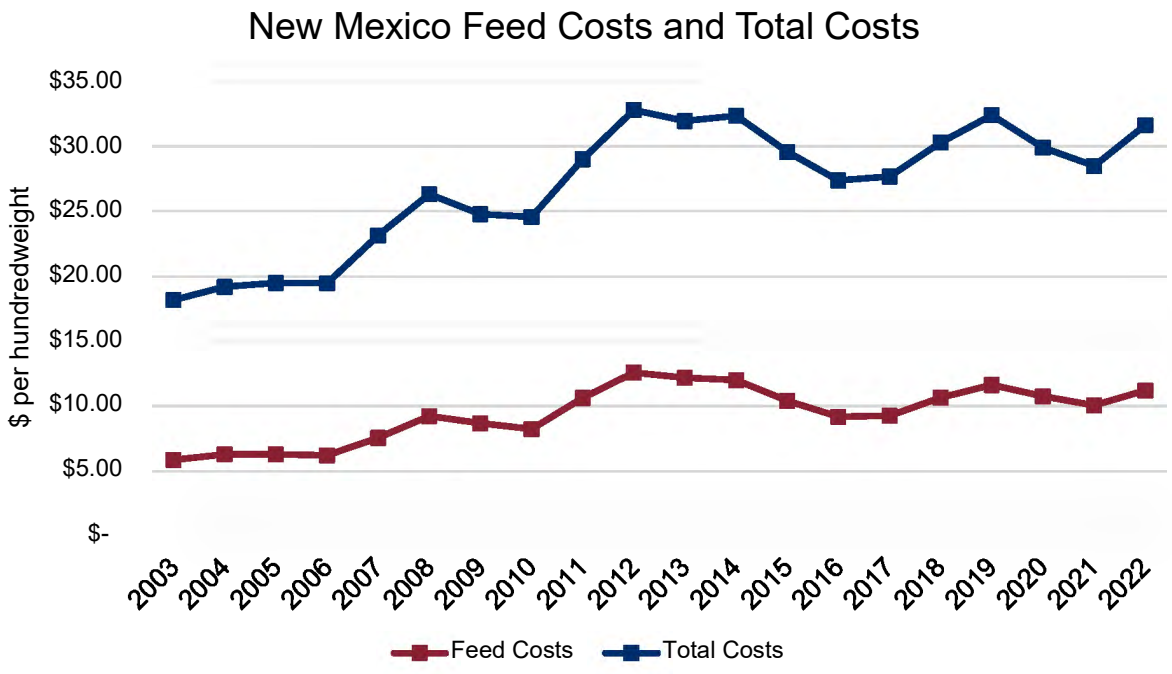


Nonetheless, as the market and economics have continued to change, the price surface has remained the same. In order to supply Class I plants, dairy farmers are being forced to subsidize the haul cost that is increasing in distance and cost. This has put dairies and handlers in an economic predicament. The NMPF proposal is designed to address the need for the greater movement of milk and take some of the burden off of dairy farmers.

In addition to the impact of increased hauling costs impacting farmers' pay price, feed prices have seen a drastic increase over the past 5-10 years and dairies are suffering from it. Please refer to Graph 1 and Graph 2.

Summary of Frazer, LP Dairy Farm Operating Trends Data, Annual[1]

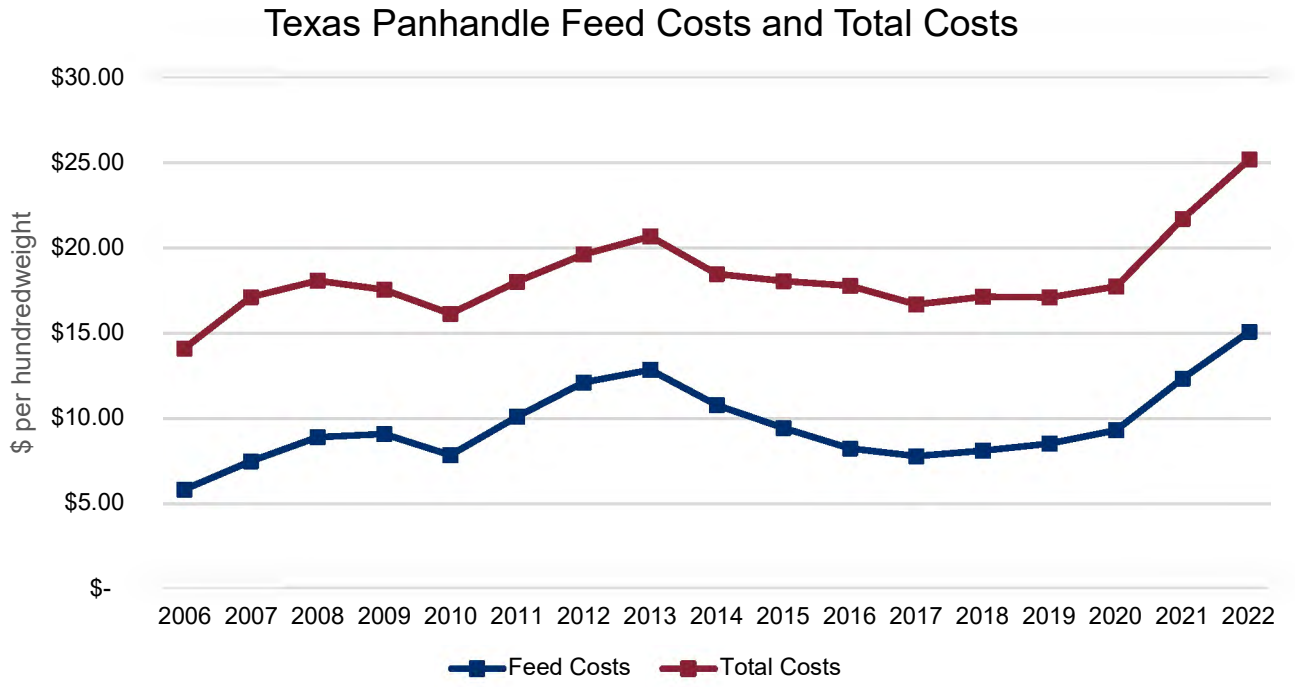
Graph 1



[1] Frazer, LLP Dairy Farm Operating Trends, reports dated December 31, 2022, December 31, 2015 and December 31, 2009

Summary of Frazer, LP Dairy Farm Operating Trends Data, Annual[2]

Graph 2



The Southwest Area dairy farmer is facing two haul costs that are increasing in cost per mile and in the mileage itself: one for the milk pickup and the other to haul silage and alfalfa for feed has created only financial hardships. A large portion of the raw milk production in the DFA Southwest Area is in the Texas Panhandle and New Mexico. Unfortunately, it is one of the driest areas in the Southwest Area. Droughts have made it difficult for dairies to grow their own alfalfa and silage. When farmers cannot grow their own feed locally, they must pay to source it from further distances. Given the substantial competition for feed and the increased cost to haul it, we do not expect the cost to operate a Southwest Area dairy to get any cheaper and the current price surface is modeled after a market that no longer exists. If we can adjust the location differential,

[2] Frazer, LLP Dairy Farm Operating Trends, reports dated December 31, 2022, December 31, 2015 and December 31, 2009

we can assist in making sure dairies are able to operate optimally and efficiently, so they can send Grade A product to Class I plants, which in turn benefits consumers.

The Southwest Area is located mainly in Federal Order 126, but there are instances when milk flows across other Federal Order boundaries. Updating the Class I surface pricing will help supply Class I plants when their own local production is lower. However, the current price surface creates an economic problem. The benefit to shift milk across federal order boundaries has decreased every year because the total return is not attractive (Class I differential and haul cost). Maximizing the value of milk back to the dairy and supplying a Class I market when its local production declines, is the main focus. By raising the price surface per the NMPF proposal, it will increase the incentives to have Southwestern milk move out of Order 126 to Class I plants elsewhere.

Throughout the year, the ups and downs with supply and demand impacts areas that are heavily populated with people and Class I plants. To keep milk flowing to these Class I markets, the Southwest Area ships milk from Southwest Kansas and the Texas Panhandle to locations such as Arkansas and Missouri. Current Class I differentials in Arkansas are lower than the Dallas-Forth-Worth (DFW) Metroplex. Thus meaning, the Southwest Area farmers are incurring additional freight to fulfill a Class I demand in a market with a lower return. Supplying Class I plants with a deficit local supply from Southwest Kansas and the Texas Panhandle should be encouraged and not hurt the farmers financially. The proposed changes from NMPF will support the movement of milk from Western Kansas into those Class I plants. Please refer to Table 1.

It is important to maintain equitable pricing in Western Kansas compared to the current pricing model that exists today. Mr. Gallagher’s testimony will cover that. The price surface should be designed to help milk flow west to east, but the current model economically discourages it. Supplying a deficit market east of the Southwest Area should be incentivized with a higher differential that will keep milk flowing in the proper direction while covering some of the additional haul cost.

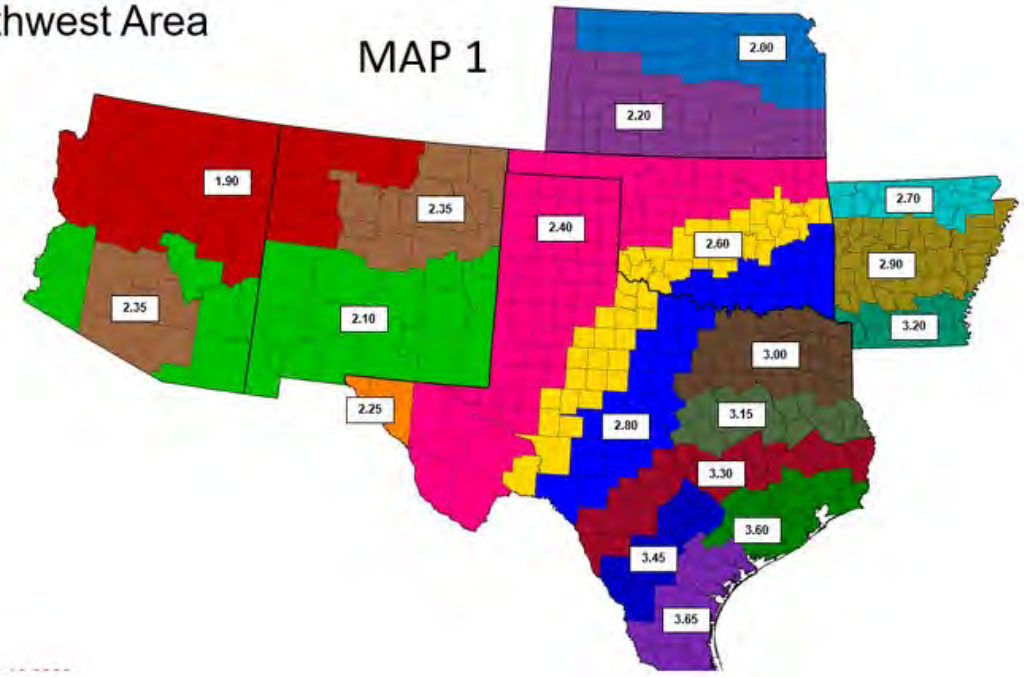
Table 1

	Current	Proposed	Difference
Garden City, Kansas	$2.20	$3.00	$0.80
Amarillo, Texas	$2.40	$3.00	$0.60
Kansas City, Missouri	$2.00	$3.35	$1.35
Wichita, Kansas	$2.20	$3.85	$1.65
Norman, Oklahoma	$2.60	$3.85	$1.25
Chandler, Oklahoma	$2.60	$3.85	$1.25
Fayeteville, Arkansas	$2.70	$4.00	$1.30
Fort Smith, Arkansas	$2.90	$4.00	$1.10
Little Rock, Arkansas	$2.90	$4.60	$1.70

Current Class I differentials are outdated as supply has shifted and operating costs have gone up. Dairies are spending more money every year to supply Class I plants and the NMPF proposal helps alleviate financial burden to the dairies and keeps Class I plants full. Previous testimonies on hauling cost match what the Southwest Area is aware of in the marketplace and believes the proposal properly aligns Federal Order 126 and Federal Order 7. Also, please refer to Map 1 and 2 for the current price surface versus NMPF's proposal. Thank you for allowing me to testify today in support of this proposal.

Current
Southwest Area

MAP 1



NMPF Proposed
Southwest Area

MAP 2