

Pennsylvania Milk Marketing Board

March 8, 2019

Testimony by Rob Blaufuss

**On behalf of Dean Foods and the Pennsylvania Association of Milk Dealers in
Support of the Proposal on the PMMB Over-Order Premium Increase**

My name is Rob Blaufuss and I am currently employed by Dean Foods as the Director of Dairy Procurement and Risk Management. My business address is located at 2711 North Haskell Ave, Dallas, Texas, 75204. Dean Foods owns and operates four distributing plants located in the Commonwealth of Pennsylvania.

I am here today in support of the Cooperatives proposal to increase the Pennsylvania Milk Marketing Board's Class I over-order premium by \$0.25/cwt to \$1.00/cwt for April through September 2019. While Pennsylvania may be on the leading edge in discussing a premium increase, we feel the market should be able to bear the proposed premium increase proposed by the Pennsylvania Association of Dairy Cooperatives (PADC) without putting undue competitive pressure on Pennsylvania Class I plants.

Pennsylvania Milk Supply Conditions

Pennsylvania milk production experienced year-over-year production declines during the second half of 2018. As highlighted in **Exhibit 1**, Pennsylvania's year-over-year milk production decline has been particularly acute between August and December. During this time period, year-over-year milk production in the Commonwealth declined by a combined 210 million pounds, or 4.7%.

In what could portend the potential for further milk production declines, the number of dairy cows on farm in Pennsylvania declined by 20,000 head year-over-year in December 2018. The total monthly dairy cows on farm for Jan 2016 through December 2018 can be found in **Exhibit 2**.

Milk Supply Dynamics in Areas Near Pennsylvania

Milk supply dynamics are also changing in areas near Pennsylvania. Milk production has declined in states such as Vermont, New York, Ohio and Michigan in 2018, albeit at a much smaller level than Pennsylvania. Total combined milk production in New York and Vermont experienced a modest decline of 59 million pounds, or ~0.3%, compared to year prior levels in Calendar Year 2018. The combined monthly milk production volumes in those two states stabilized as 2018 progressed with the year-over-year decline in production between Jan and May being partially offset by an increase in

production between June and December. The monthly combined milk production levels for New York and Vermont can be found in **Exhibit 3**.

Michigan and Ohio also both saw a reduction in their milk supplies in 2018. Their total combined milk production declined by a combined 1.2%, or 208 million pounds, year-over-year in 2018. Michigan and Ohio's combined monthly milk volumes for 2016 – 2018 can be found in **Exhibit 4**

Improved Dairy Price Outlook for 2019

Domestic dairy product prices are expected to improve in 2019. As Mr. Hollon indicated in this testimony, milk prices are expected to increase during the April – September 2019 period on both a year-over-year basis and compared to October 2018 – March 2019 prices (using both actual and estimated prices). As of market close on February 19, 2019 CME futures prices for Class III and Class IV for April through September are trading at levels that are significantly higher than the prices paid over the same period in 2018. Class III and IV prices are used to directly set Class I mover prices while Class IV formulas are used to set Class II prices. While futures prices at the CME today by no means guarantee actual market prices at the time those futures contracts settle, they do indicate what buyers of those products are willing to pay under current supply and demand conditions.

The Class III and IV prices on **Exhibit 5** represent the actual prices paid, by time period, between April 2015 – January 2019, while prices for February 2019 – September 2019 reflect CME prices as of market close February 19, 2019. As the data shows, the Class III futures price average of \$15.49/cwt for April – September would represent a \$1.09/cwt increase compared to the October 2018 – March 2019 period and would be \$0.49/cwt higher than the same period last year. Increased nonfat dry milk prices are expected to help lead to noticeably higher Class IV prices in 2019. Class IV futures prices for April – September 2019 averaged \$16.48/cwt as of market close February 19th. Should these values come to fruition, they would represent a \$1.10/cwt increase compared to the previous six-month period and a \$2.06/cwt increase compared year prior levels. The monthly Class III and Class IV actual and estimated prices can be found on **Exhibit 6**

The most recent Farm Bill included a provision that will reform the Class I price formula. Since Federal Order reform, Class I mover prices have been set using the 'higher-of' the advanced Class III or Class IV skim price. As stated in the Farm Bill, the Class I mover prices will be calculated using the simple average of the advanced Class III and IV prices plus \$0.74/cwt. While USDA has not released an official date in which the new formula will become effective, current industry expectations call for the change to be reflected starting with the June 2019 price announcement. The Class I prices on the previously mentioned **Exhibit 5** are reflective of April 2015 – March 2019 actual announced Mover prices. Class I price estimates for April 2019 and May 2019 are calculated using the 'higher-of' the month prior Class III or IV CME futures prices (i.e. February Class III/IV price for March Class I price). June – September 2019 Class I price estimates are the function of month prior Class III and IV futures prices and the new Class I price formula previously discussed. As the data shows, the Class I mover price estimates call for an average of \$16.46/cwt for April – September 2019. This Class I mover represents a \$0.91/cwt increase compared to the previous six-month period and is \$1.77/cwt higher than year prior levels. The monthly actual and estimated Class I mover prices for January 2015 – September 2019 can be found on **Exhibit 7**. It's worth noting that the new Class I formula that will be implemented later this year would mean modestly higher Class I mover prices compared to the current price formula given current Class III and IV futures prices.

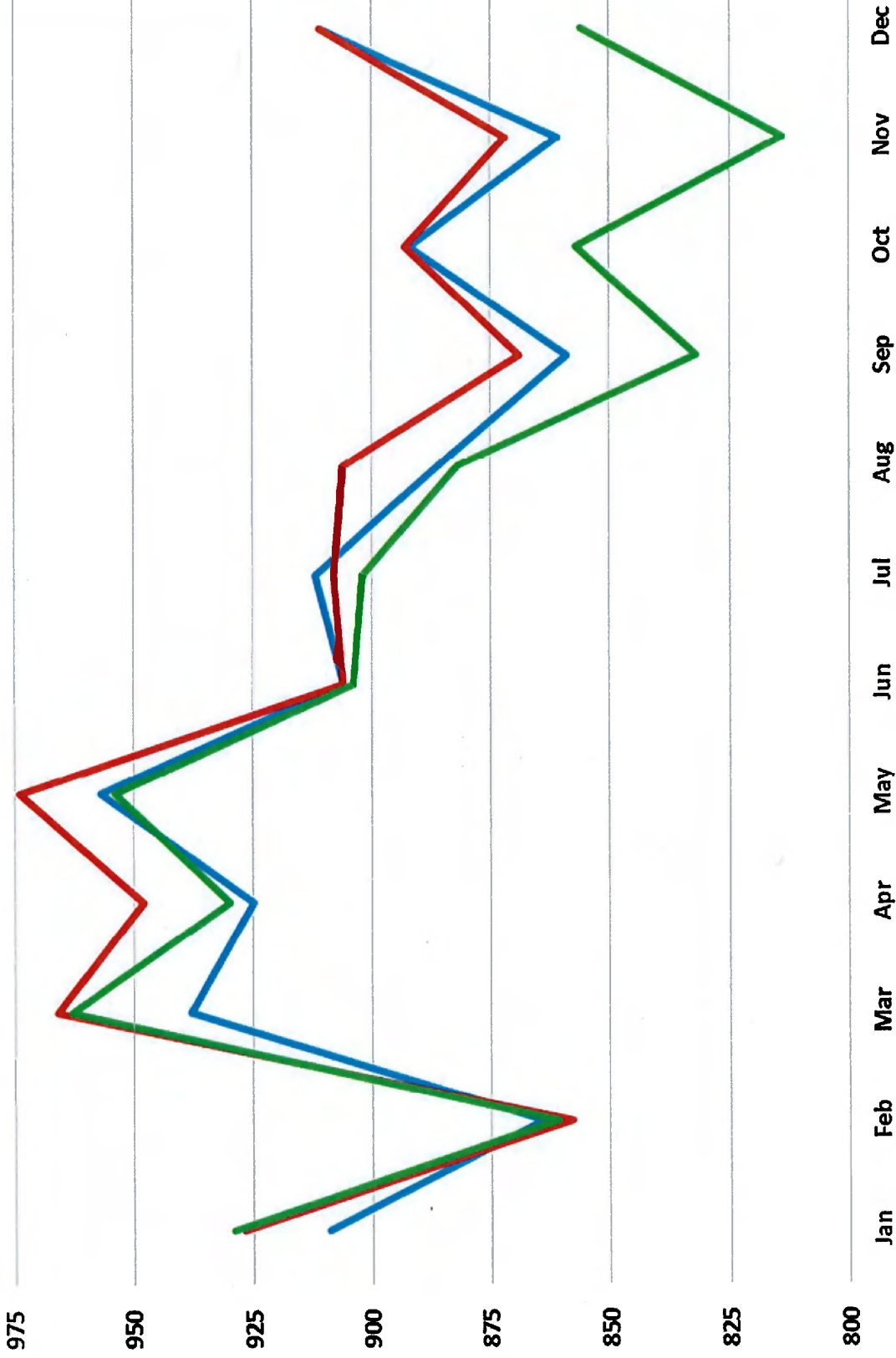
Conclusion

It is Dean Foods' viewpoint and the viewpoint of the Pennsylvania Association of Milk Dealers that the Class I over-order premium in Pennsylvania be set at a level that is both reflective of market fundamentals and competitive with prevailing premiums in areas surrounding the Commonwealth. Given market conditions, we believe that an increase of 25-cents per cwt will help the Pennsylvania dairy farmers and not create an undue threat to PA Class I plant competitiveness. Therefore, Dean and the Pennsylvania Association of Milk Dealers support the request of the PADC

Thank You for allowing me to testify before the Board today.

Pennsylvania Monthly Milk Production

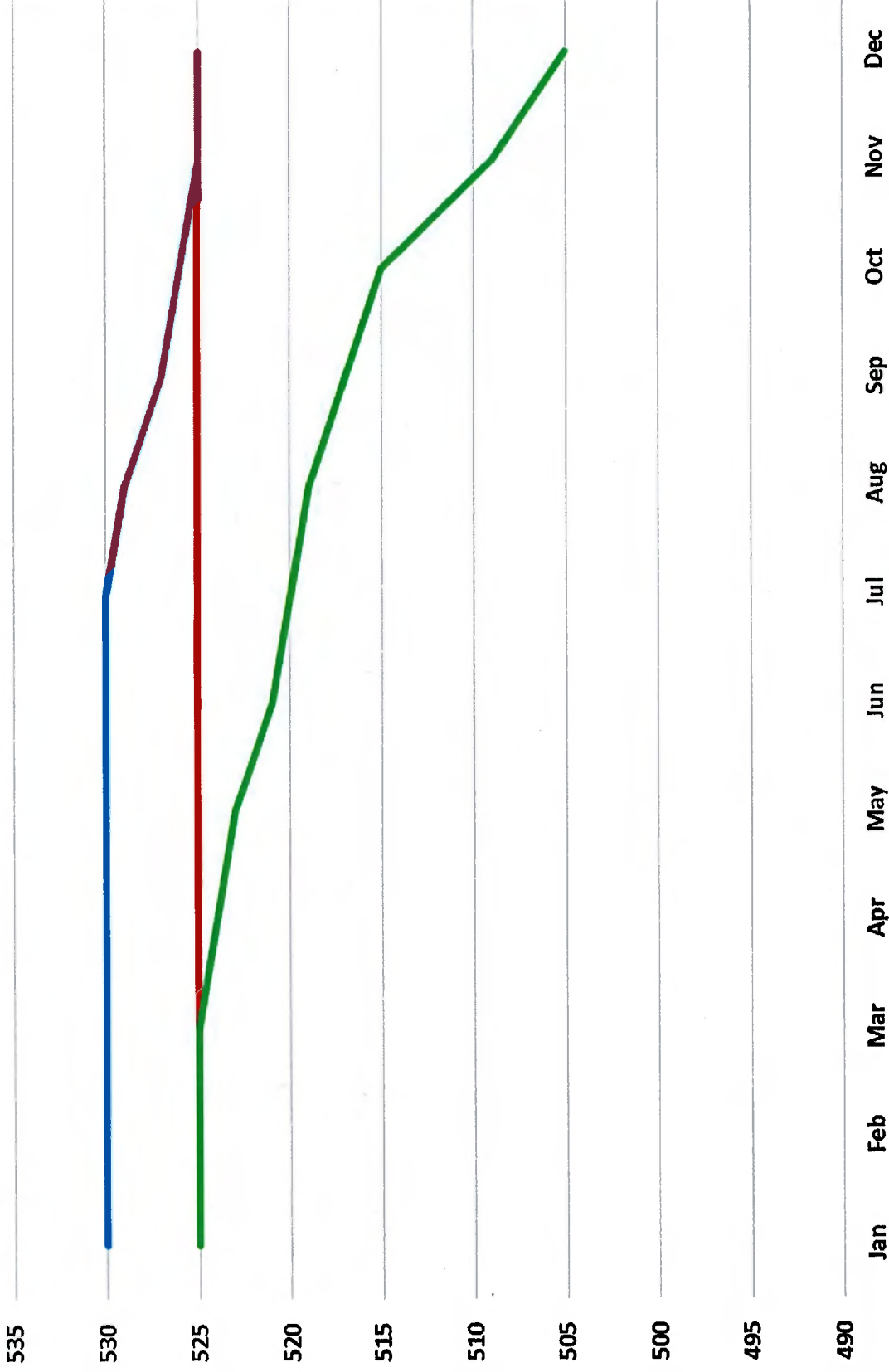
Pounds (in millions)



Source: USDA-NASS

Pennsylvania Dairy Cows on Farm

Head (in thousands)

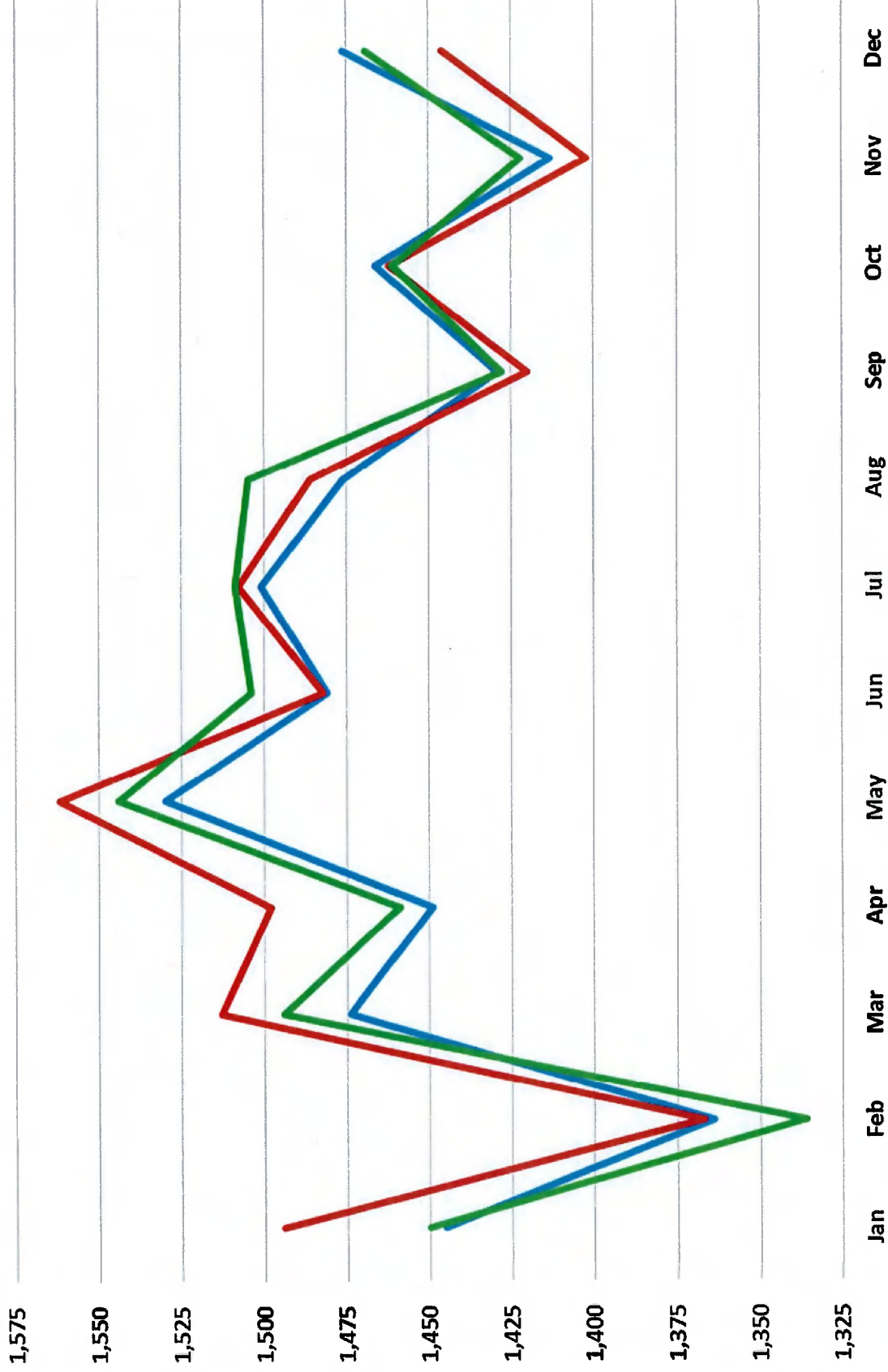


2016 2017 2018

Source: USDA-NASS

Total Monthly New York and Vermont Milk Production

Pounds (in millions)



Source: USDA-NASS

Total Monthly Michigan and Ohio Milk Production

Pounds (in millions)

1,500

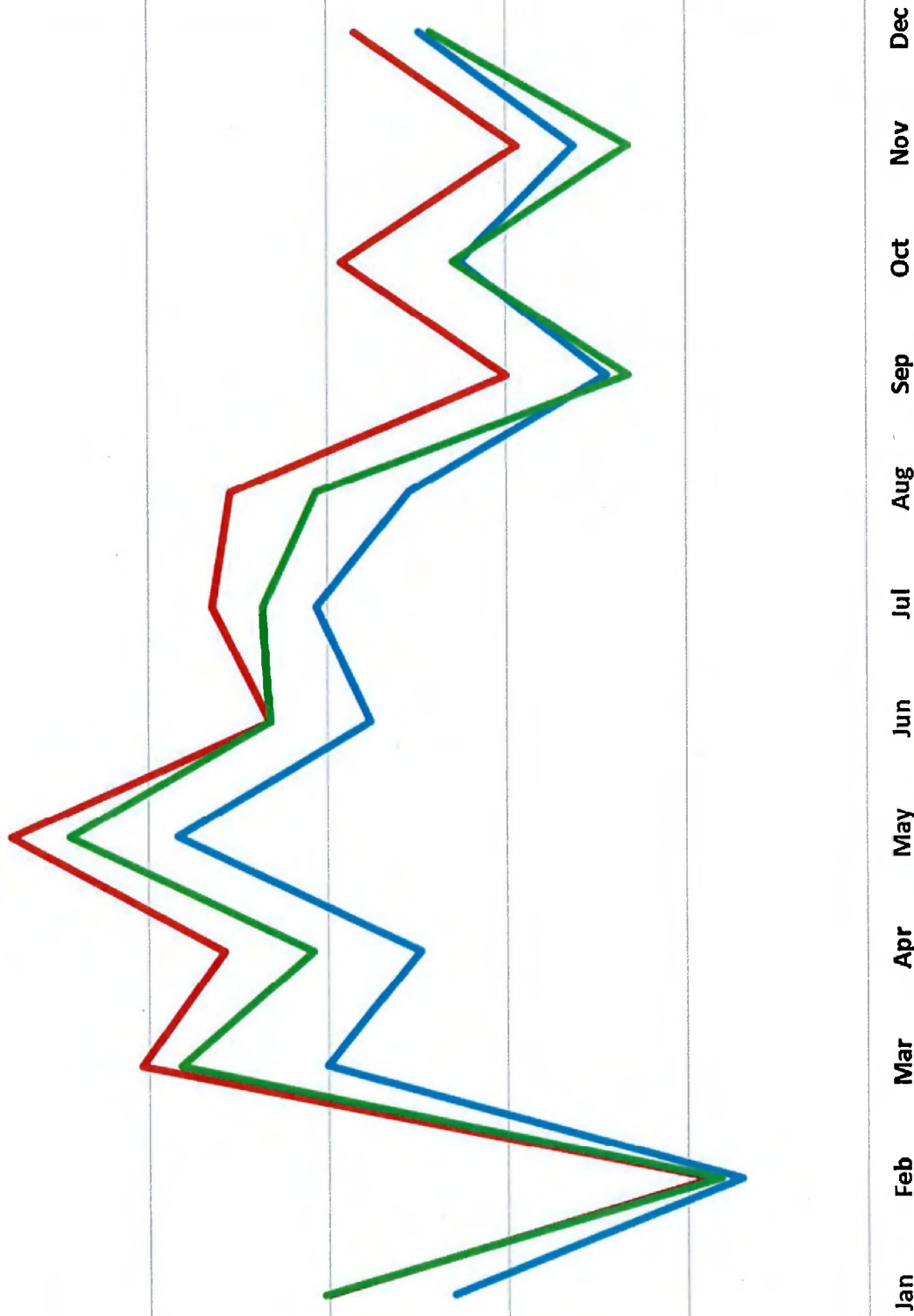
1,450

1,400

1,350

1,300

1,250



2016 2017 2018

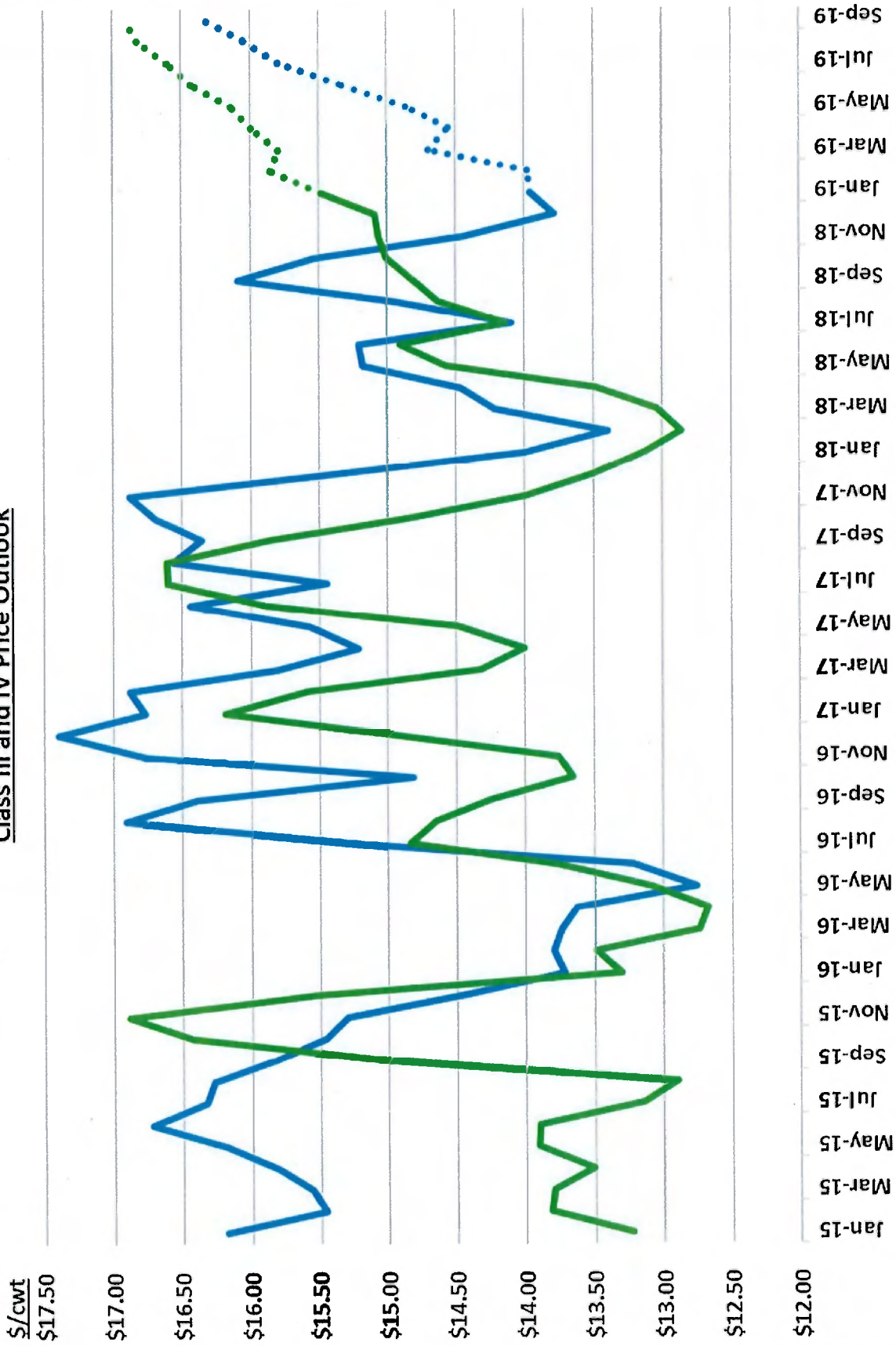
Source: USDA-NASS

Dairy Price Outlook: April 2015 – September 2019

Time Period	Class III	Class IV	Class I Price
Apr 15 - Sep 15	\$ 16.19	\$ 13.74	\$ 16.10
Oct 15 - Mar 16	\$ 14.41	\$ 14.73	\$ 15.42
Apr 16 - Sep 16	\$ 14.69	\$ 13.88	\$ 14.32
Oct 16 - Mar 17	\$ 16.41	\$ 14.75	\$ 16.56
Apr 17 - Sep 17	\$ 15.94	\$ 15.58	\$ 16.10
Oct 17 - Mar 18	\$ 15.11	\$ 13.57	\$ 15.46
Apr 18 - Sep 18	\$ 15.00	\$ 14.42	\$ 14.69
Oct 18 - Mar 19	\$ 14.40	\$ 15.38	\$ 15.55
Apr 19 - Sep 19	\$ 15.49	\$ 16.48	\$ 16.46

Source: USDA-AMS, CME Group and Dean Foods Calculations

Class III and IV Price Outlook



Class I Mover Price Outlook

