Testimony for Pennsylvania State Senate Agriculture and Rural Affairs Committee Over Order Premium Hearing
Submitted by Zach Myers, Risk Education Manager, Center for Dairy Excellence

Chair Vogel, Minority Chair Schwank, and Other Distinguished Members of the Agriculture and Rural Affairs Committee, thank you for the opportunity to come before you on behalf of the Center for Dairy Excellence and Pennsylvania's dairy farm families. As a public:private non-profit in Pennsylvania, the Center for Dairy Excellence (Center) is grateful for the financial support provided by the Pennsylvania legislature and administration. Each Center staff member is passionate about the dairy industry and diligently uses those resources to meet both the Mission: Empower and support Pennsylvania dairy families and businesses to thrive, and the Vision: Serve as a catalyst for a vibrant Pennsylvania Dairy Industry. While it is not the scope of the Center's responsibilities to offer policy recommendations, it is the Center's responsibility to make sure those involved in policy decisions have the best information available to make the most informed decision when considering policy changes. The goal of my testimony today is to provide a snapshot of the current Pennsylvania dairy industry and outline the challenges Pennsylvania's dairy farm families face and opportunities that exist that could improve the state's dairy economy.

According to finalized USDA National Agricultural Statistics Service (NASS) data, Pennsylvania ended 2022 with 5,000 licensed dairy farms. This represents a reduction of 3.8% or 200 dairies compared to 2021. Since I began working at the Center in December 2018, Pennsylvania has lost a total of 1,200 dairies. This is a near 20% drop in the number of dairy farms over four years. Cow numbers also saw a decline through 2022, ending the year with 468,000 mature dairy cows. This was a 6% decline, or 7,000 cows, relative to 2021. This is not a recent trend, with dairy cow numbers declining each year over the same period. Since 2018, cow numbers have decreased by a total of 51,000 head, or 10%. As a result of the continued loss of dairies and cows, total milk production has also been declining. There was a total of 9.949 billion pounds of milk produced across the Keystone State in 2022, representing a 1.6% decline, or a drop of 265 million pounds compared to 2021. Total milk production during 2018 equaled 10.893 billion pounds. Since then, Pennsylvania milk production has declined 944 million pounds, a total of 9%.

However, it is not all bad news. Although total milk per cow declined in 2022 compared to 2021, the general trend since 2018 has been improved efficiency year-over-year. Pennsylvania's average cow produced 79 pounds of milk less in 2022 than she did in 2021, but the multi-year trend is net positive. At 21,259 pounds of milk per cow in 2022, milk production per cow has increased by 710 pounds since 2018 which represents a 3% increase. One factor constraining total milk production in Pennsylvania is the supply management programs that have restricted growth on many dairy farms in Pennsylvania since 2019.

Even with recent declines in dairy farm numbers, milk cows, and total production, dairy farming is an economic driver for the Commonwealth. The state's dairy industry contributes $11.8 billion in annual economic revenue and supports 47,000 jobs. For each $1 on the farm, $2.50 in economic revenue is generated across the industry. Pennsylvania continues to be a national leader. Pennsylvania ranks second in number of dairy farms, fifth in number of dairy cows, and eighth in total milk production. Pennsylvania is also a national leader in butter, ice cream, and ice cream mix production.

Pennsylvania's dairy industry is truly unique. Ranking second nationally in dairy farm numbers and fifth in dairy cows means that the average herd size across the Commonwealth is small. The average herd size across the country in 2022 was 337 cows. In Pennsylvania, the average dairy farm is only 94 cows per dairy. In fact, this herd size average is the fourth smallest in the nation. Dairies in Pennsylvania do not have the cost efficiencies that larger dairies in other states have.

Historically, feed costs in Pennsylvania have also been higher than many of the other top dairy states in the Northeast, Mideast, and Midwest as we are a net importer of feedstuffs to meet the demands of the dairy industry. Having to go further away for feed commodities increases the freight cost of those ingredients, increasing the cost of purchased feeds in Pennsylvania. Higher land values in Pennsylvania increase the cost of homegrown feeds. Both factors further stress Pennsylvania dairies' cost of production. In fact, data from Farm Credit Northeast and Horizon Farm Credit shows that the cost of production in Pennsylvania is typically 75 cents to $1.00 per cwt higher than New York dairies.

Also, Pennsylvania is known for its conservative Amish and Mennonite communities. Dairies in these communities, in many cases, cannot participate in the state and federal programs that other dairy farms can and are at the mercy of dairy markets. Without economies of scale that help to reduce cost of production and lack of ability to participate in government programs, many Pennsylvania dairy farmers rely on premiums in the marketplace for their financial success. Unfortunately, many of the premiums in the marketplace either do not exist anymore or are not as high as they once were. Quality premiums are an example of a premium that looks different than it did a few short years ago. Dairy farmers have made excellent strides in improving milk quality over the last decade with the help of milk quality incentives offered by processors and milk handlers across the state and country. However, now that milk quality is not much different from milk handler to milk handler, there is not as much desire on the processor or milk handler side to offer as high of an incentive, or in some cases, any incentive at all.

Federal dairy policy has also affected premiums over the last several years. Make-allowances are credits to the processor to cover the theoretical costs associated with processing raw milk into final products. Each manufactured product like cheese, butter, or milk powder has a make-allowance, set by the USDA, that is used to compute the final price paid to dairy farmers. The make-allowance is a deduction to the final farmgate pay price. Make-allowances have not been updated in over 10 years and are no longer believed to cover the theoretical cost of manufactured dairy products. Dairy processors have lowered or eliminated the marketplace premiums they are willing to pay to help recoup expenses that make-allowances do not cover in order to maintain their margins.

The current federal Farm Bill cycle ends this year. The programs developed, appended, removed, or kept in the next Farm Bill will have a significant impact on Pennsylvania's dairy farm families. Programs like Dairy Margin Coverage, Dairy Revenue Protection, and Livestock Gross Margin for Dairy are Farm Bill programs that have provided many Pennsylvania dairy farm families with a much-needed safety net to remain successful in an ever-changing, increasingly volatile dairy market.

This year is also the first time in more than 10 years that the Federal Milk Marketing Order Reform mechanism has been activated. The International Dairy Foods Association (IDFA), the dairy processor lobbying arm, submitted a proposal to the USDA asking to grant a hearing on increasing the make-allowances previously described. Changing make-allowances alone would result in further milk price degradation to the nation's dairy farmers. The National Milk Producers Federation (NMPF), the dairy farmer and cooperative lobbying arm, does not support this proposal and is asking USDA to reject the IDFA proposal and instead consider their more comprehensive Federal Milk Marketing Order Modernization proposal, which includes returning to the "higher of" Class I mover, removing barrel cheese from the protein component price formula, extending the reporting limit to 45 days on forward priced sales on nonfat dry milk and dry whey to capture a better representation of export sales, updating component factors for protein, other solids, and nonfat solids in the Class III and IV skim milk price formulas, and updating the Class I differential price system to better reflect the cost of delivering milk to fluid processing plants. Updating these factors will, theoretically, result in a net increase in farmgate price. The NMPF proposal also addresses the IDFA's concern about make-allowances by including a request to update make-allowances to better reflect current processor input prices and developing a system whereby make-allowances are more regularly reviewed by the USDA by conducting mandatory plant-cost studies every two years. Although changing make-allowances results in a reduction in farmgate price, the net effect of NMPF's proposed changes will result in a higher pay price for dairy farmers across the country. It is my understanding that NMPF will submit its proposal to the USDA by the end of this week.

In preparation for this testimony, I compared the U.S. all-milk price to the Pennsylvania all-milk price from 2008 to 2022. The U.S. all-milk price is the average price paid to dairy farmers across the nation, and the Pennsylvania all-milk price is the average price paid to all dairy farmers in the Commonwealth. Both numbers are published by the USDA in its monthly *Agriculture Prices* report. The milk price that dairy farmers receive is calculated on every one hundred pounds – or about 11.6 gallons – of milk produced on the dairy farm.

Historically, Pennsylvania dairy farmers receive a price that is higher than the average U.S. dairy farmer. However, over the last 15 years the gap between Pennsylvania's milk price and the U.S. milk price has narrowed. From 2008 to 2012, the difference between Pennsylvania's average price and the U.S. price was +$1.73 per hundredweight (cwt) and, from 2013-2017, it was +$1.29 per cwt. Over the last five years (2018 to 2022), the gap between the Commonwealth's average price and the national average price narrowed to just 49 cents per cwt. During the height of the pandemic in 2020, the average Pennsylvania price was 18 cent per cwt less, on average, than the U.S. all-milk price. This was the only year over the 15-year span that Pennsylvania's average price was less than the U.S. average. I am sure there are several factors they played into this decreased gap in prices, not over order premiums alone. An economic analysis would be required to determine the exact contribution that declining premiums made to the narrowing of this gap. However, it would be safe to say that it has played a part.

Unfortunately, all current Pennsylvania dairy issues cannot be fixed by increasing the amount of marketplace premiums alone. According to information received from the Pennsylvania Milk Marketing Board in 2022, about 80% of the milk produced in Pennsylvania is marketed through cooperatives. Earlier, I referenced the supply management programs put in place by these cooperatives, as well as independent processors, that have limited or prevented Pennsylvania dairy farmers from expanding. I also spoke about how economies of scale help reduce production cost. Without the ability to expand, greater economies of scale cannot be realized, and cost of production remains high. Milk production limitations prohibit those operations that do have the land base and financial ability to expand from helping to grow the Pennsylvania dairy industry through expansion.

Cooperatives have reason to implement and enforce supply management programs, as they are meant to reduce the likelihood of over-supply conditions. This allows supply to better coincide with processing capacity and sales, which helps to bolster farmer pay price since reduced prices occur with over-supply situations. Again, an economic analysis would have to be conducted to see the exact effect of supply management programs on pay price, but it makes economic sense that in recent years, suppressing milk supply has helped to maintain a higher milk price than would have occurred in an over-supplied market. In conversations with some cooperatives implementing these supply management programs, they expressed that if they had a market for the milk, they would restructure or cancel their supply management programs and allow their member owners more freedom to grow. One issue restricting expansion in Pennsylvania is milk processing capacity. More processing capacity would provide new markets for milk production growth within Pennsylvania. There has been no major investment in new processing capacity and little reinvestment to improve current capacity in Pennsylvania. The Center is currently working with Dr. Christopher Wolf, E.V. Baker Professor of Agricultural Economics in the Dyson School of Applied Economics and Management at Cornell University, to identify what is discouraging investment and reinvestment into processing capacity in Pennsylvania and the Northeast. Results from this research will provide insight into what limitations to processing capacity growth exist and could serve as a basis for developing state or regional programs that encourage new or re-investment to improved processing capacity.

Dairy Farmers are “price takers” not “price makers,” therefore, they rely on a fair and equitable system to be able to succeed and thrive in this great dairy industry. Every dollar or cent per cwt is important. I will reiterate that it is not the Center’s responsibility to take a position on federal or state policy issues. However, the Center acknowledges that there are concerns from the Pennsylvania dairy community about the Pennsylvania Milk Marketing Board’s current Over Order Premium structure. Although I have not provided an opinion nor implied a solution to the current situation, it is the Center’s opinion that any state program should meet the objectives for which it was designed, be fair, equitable, and transparent to both dairy farmers and dairy consumers.

Thank you for your time.

Respectfully Submitted,

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