

Breakout 3C – Growing the Dairy Industry, A Working Session

Moderator Sheila Harsdorf, Agriculture Commissioner for the State of Wisconsin, opened the meeting and introduced the two panelists, Dr. Mark Stephenson from the University of Wisconsin Director of Dairy Policy Analysis, and Dr. Scott Brown, Assistant Extension Professor in the Department of Agriculture and Applied Economics from University of Missouri.

Sheila began by noting that this breakout was not a normal presentation and Q&A session, but a working session to investigate the problems and solutions to the problems facing the dairy industry today.

The discussion was opened. Scott Brown began with talking about two things. Relating to the Farm Bill, the 2018 Farm Bill is potentially in the works now at the start of the year, with a lot of language already written on the House side. From a dairy perspective, MPP is a problem now and there are not many changes to the program being proposed. Premiums could go down for smaller operations, and perhaps an opportunity to buy up as well. But the changes on the House side are related to those producing less than 4 million pounds on an annual basis. The program for the larger operations will remain unchanged. The Senate version is unclear. Budgets are a problem.

If there is no passage of the 2018 Farm Bill, MPP will remain as is, and many dairy farmers will remain without a safety net. Relating to policy in Missouri, the last legislative session, they ended up with \$600,000 appropriate to pay up to 75% of the premiums producers had paid under the MPP program. When a state loses too much of its dairy farms, it is hard to keep the necessary infrastructure for the remaining farms.

The structure of the industry from a U.S. perspective is very different than it was in the past. In periods of good milk prices more milk is produced and more investment happens. When prices fall, nothing changes. This is the crux of what we have to face in terms of the state of the industry today. Demand has to pick up, but until then we keep producing more milk. Trying to find the infrastructure for all that milk is going to continue to be more and more important.

Mark Stephenson followed on by saying that when you get down into the time periods when things are intensely happening sometimes you're so close to the smoke it's hard to see what's going on. But he thinks some of the structural change is going to become apparent several years from now. He thinks it is happening right now in a serious way. There are very much regional differences in what is happening. We still produce milk in all 50 states. We are intensifying milk production into regions within states.

Over the last decade California has had one of the largest concentrated growths of dairy farms in the central region, and the biggest region of contraction from the Imperio Valley region. We see either specializing into or out of dairy. There's a lot more of dairy that seems to be moving – either by plan or by default – into some of the more northern states and regions. This is coming due to a collision of a couple of trends.

One of them is the perpetual trend toward more and more productivity, or milk per cow. A cow that produces 20,000 pounds of milk versus one that produces 30,000 pounds of milk has about 30% more body heat to dissipate. We can do that at lower levels of production in all 50 states. We can't do that anymore. Michigan has the highest productivity milk per cow – about 26,000 pounds. And southeastern states are down around 13,000 pound average. These states are contracting. They are facing loss of infrastructure to support dairy, so it just gets more and more expensive and difficult.

The northeast has been a traditional dairy area. It's grown in milk production over the last few years. But this has put stress on processing in the area, because there has not been an adequate processing home for some of this milk. So we see headlines of milk being dumped. New York, Michigan and Wisconsin have added about 15 million pounds of milk per day. That requires three large dairy processing plants to handle the volume. We don't have that capacity.

The question isn't capacity or building of plants. It's 'Who is the customer for this product?' The other trend that they're colliding with is the somewhat warmer global atmosphere that we have, which tends to provide more heat in the west, which is a problem. If you look at the difference in trends of the top four dairy states, the milk productivity per cow in Idaho and California is trending slightly up, but almost flat. New York and Wisconsin is trending up at a much steeper rate. He thinks we're hitting the limit of what cows want to do in these kind of climates.

These things are going to be issues to deal with, and you can't solve them by the swipe of a pen. The dairy industry is going to be driven by some of these big movers.

The other thing to throw into the mix which has been a little under the radar for a lot of people but the last ag census showed that 53% of the milk was being produced on less than 3% of the largest farms in the country. That trend has not slowed down a bit. By the time we get the 2017 census, he believes we'll find it is significantly higher than that. The slow price that we're in right now has been a real problem, but we have a number of farmers that have cash flowed through the whole thing. And other farms are bleeding cash. So it's been a slow scrape rather than a deep cut.

The background of the speakers complete, Sheila opened the floor to discussion. She started up by asking what they think the biggest challenges are that face the dairy industry. Scott Brown answered by saying lack of adequate processing capacity is a major problem. Most new processing coming on line has been funded in part by the producers who have seen the need for expansion. The coordination is really important. The market is extremely inelastic. Growth comes from the international marketplace and just what the rest of the world wants from the U.S. in terms of dairy products. Trade policy is critical, and exchange rates are important as well.

Mark agreed. The domestic demand is growing per capita, but slowly. We have an excellent domestic market. But we've stumbled into export markets. We're still new to the international marketplace, and we need to identify the customers.

A question was asked about the growth of international milk production. Pasture based locations are limited by their resources. Our biggest competitors are the EU, whose quotas are not off, resulting in significant increases in production.

Scott mentioned the ability to export our technology is not that difficult anymore. That competition might get even stiffer. Being closer to the markets gives some of these countries an advantage, i.e. the countries in the EU.

Some of the questions centered on resistance by neighbors and municipalities to new dairies being built, especially large farms. Quotas were also discussed. Competition for the land was explored. Rebuilding after a serious drought was discussed, as were EPA rules and regulations as they impact the relocation of farms. Groundwater, the aging of the farming population, cyclical demand, the FMMO were discussed as well.

Sheila posed the question – How do we deal with overproduction? She mentioned the Canadian system, and noted that people are currently having this discussion. The USDA long term projections does not show milk prices getting back about \$18 cwt in the U.S. until 2026. There is a number of

more efficient operations in some parts of the country who don't get rich on that number but who can survive. The question is how bad does it have to get in order to get the supply response we need, or does the demand side grow enough that we come out on the other end?

As some parts of the industry get bigger, we see distribution of production costs narrow a lot, which means we don't lose the low end as easily as we once lost it. This makes aggregate response more difficult. Adding to this, many times in commodities, the processor likes to do business with fewer suppliers. It adds to their efficiency and costs less.

Possible solutions – get more ag lenders, diversify dairy products, find more markets, consolidate. Perhaps create another class of milk for small producers, which would explicitly say we take money from one group and give it to another. One must look at social engineering – what's desirable? What do we as a nation want to do? Find the best way to achieve the best outcome for all. If there aren't intentional strategies now, twenty years from now our dairy industry will look completely different than the one we know. Changing the Federal Orders will have to be done administratively. Congress is not likely to bring this up again after the difficulties of the negotiations from the last change in the late '90s.

Overproduction is the nature of a commodity, which has an uncoordinated supply chain. There is no communication to determine what would be the best for every producer. But the supply chain will become coordinated once we have a smaller number of operations.

For smaller producers, any federal regulation tends to hurt them more than the larger operations. Therefore larger producers support increased regulation that they can easily comply with, at the expense of smaller farms. It was suggested that we do away with some of the regulations for smaller farms, as long as the safety of the product is not impacted. There is a market for locally produced and artisanal products. However, we will continue to lose farms if we do not relax the regulations on the smaller ones.

When there are new markets for dairy products, you have to make sure that you are good marketers as well. Some do it well, and so don't do it so well.

The discussion was brought to a close due to lack of time. The speakers were thanked for their participation.