

The Market Administrator's Bulletin

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Federal Order No. 2

New York–
New Jersey
Milk Marketing
Area

Volume 58

July

1998

Court Rules Class I Differentials Legal

The United States Court of Appeals for the Eighth Circuit (Appeals Court) issued a ruling on August 13, 1998. The decision in *Minnesota Milk Producers et al. v. Dan Glickman* reversed a lower court ruling that the Class I differential system used under the federal milk marketing order program is unlawful. The Appeals Court stated that the Secretary of Agriculture's decision to maintain the current system for pricing Class I milk was within his discretion and he may continue to enforce the existing Class I pricing system.

The complete ruling can be found on the internet at: <http://ls.wustl.edu/8th.cir/opinions.html>. ♦

Federal Order Reform Continues

USDA is currently reviewing nearly 4,500 comments received regarding the January 1998 proposed rule. After analyzing the comments and additional information, USDA will issue a final rule detailing proposed changes for the federal milk order program. Information on the final rule will be provided to producers to determine approval. Each approved milk marketing order will become effective no later than April 4, 1999. ♦

Order No. 2 Web Site Now On-line

A World Wide Web site for Order No. 2 is now on-line, providing electronic access to federal order information released by this office. Price announcements, including uniform and class prices, the *Bulletin* and most other reports and publications currently released by this office will be available on the site. A "quick facts" summary section, reporting comparable price information for the three Northeast Federal Milk Marketing Orders (New York–New Jersey, New England, and Middle Atlantic) together with the Western New York State Milk Marketing Order, has been created. Price information posted on the site will be updated on the same day that the applicable price announcement or report is required to be released. Links to USDA Dairy Programs web sites and web sites of other Federal Milk Marketing Orders also are included. The address for Order No. 2 is <http://www.fmmone.com>. E-mail comments or messages can be sent to this office at MA_Albany@fmmone.com. ♦

July 1998 Pool Highlights

- The July 1998 uniform price equaled **\$13.53**, an increase of \$0.12 from last month and \$1.86 higher than last year.
- All class prices were above last year's. The Class III-A price was \$3.53 higher than last year's, but only added \$0.01 to the uniform price because of low utilization.
- Producer receipts totaled 1,014.5 million pounds, a decrease of 1.4 percent from last year.
- Class I receipts totaled 390.9 million pounds, a decrease of 0.9 percent from last year.
- Daily deliveries per producer (DDP) equaled 3,368 pounds, a year-to-year increase of 206 pounds (6.5 percent). This was the largest DDP increase this year.
- For the second month, the Emkay Trading Corp. plant located in Arcade, NY, was a temporary pool plant under Order No. 2. ♦

Order No. 2 Prices and Utilization for July

	1997	1998	Percent change
Prices*			
	dollars per cwt		
Uniform	11.67	13.53	15.9
Class I	13.12	13.30	1.4
Class II	11.00	11.18	1.6
Class III	10.89	14.80	35.9
Class III-A	12.09	15.62	29.2
Utilization			
	million pounds		
Class I	394.3	390.9	(0.9)
Class II	162.9	156.2	(4.1)
Class III	438.0	448.8	2.5
Class III-A	33.2	18.7	(43.6)
Producer Receipts#	1,028.5	1,014.5	(1.4)

* For bulk milk testing 3.5 percent butterfat in the 201-210 mile zone.

Totals do not add due to rounding.

U.P. Forecasted to Increase

The uniform price **forecast** for **August 1998** is **\$14.99** per hundredweight of bulk milk testing 3.5 percent butterfat in the 201-210 mile zone. This is an estimate. ♦

Forecasting the Uniform Price

Around mid-month the New York–New Jersey Market Administrator's Office estimates the uniform (blend) price for that month. This dollar amount is shown in the lower right-hand corner on the front page of the monthly *Bulletin*.

The July estimate raised many questions by producers and handlers. In this article, we will explain how we calculate our estimate.

The uniform price is a weighted average of the prices for each class of milk based on their prospective usage. The first thing we estimate is how much milk will be pooled under Order No. 2. We do this by predicting the number of producers and the average daily delivery per producer (DDP) for the month. Current and historical information is combined to estimate these factors. Multiplying the number of producers times DDP times the days in the month equals total pooled receipts.

The next step is to estimate utilization in each class. Again, historical data and current information are analyzed. A main element in estimating class usage is the seasonality effect, such as school closings in summer decrease Class I usage. Estimating the amount of milk to be used in each class gives us the weights for our weighted average.

Class I and II prices are determined 2 months in advance. For example, the July Class I and II prices were based on the May basic formula price (BFP):

<u>BFP</u>		<u>Class Differential</u>		<u>Monthly Price</u>
(2nd preceding month)		(202-210 mile zone)		(July)
\$10.88 (May)	plus	\$2.42 (Class I)	=	\$13.30
		\$0.30 (Class II)	=	\$11.18

The Class III and III-A prices are estimated using many factors. The Class III price is the BFP for the current month adjusted slightly each month by a seasonal adjuster. For the year, the annual average Class III price equals the annual average BFP.

The BFP is comprised of two parts: the base month price and the change in product prices from the previous month. The base month price is reported by USDA's National Agricultural Statistics Service. It is the survey portion of the BFP calculated from prices reported by cheese, butter, and powder plants paying for Grade B milk in Minnesota and Wisconsin.

The change in product prices is more straightforward. By watching the weekly markets for the component products, this part of the formula can be estimated fairly accurately. The component prices are Grade AA butter on the Chicago Mercantile Exchange, nonfat dry milk and dry buttermilk in the Western States, 40-pound block Cheddar reported on the National Agricultural Statistics Service survey, and the Grade A butter equivalent price (CME Grade AA less 9 cents). The Central States nonfat dry milk price is needed

to calculate the Class III-A price. Each month when our office calculates that month's estimated blend, we have about half of the weekly prices needed to calculate monthly product price averages.

Using our methodology, we estimated a base month price for June of \$12.97 at 3.5 percent butterfat. Estimating product prices for July gave us a monthly change of \$1.54. Adding this change to the base month equals the current month's BFP estimate (see below). The actual BFP for July was \$14.77 per hundredweight at 3.5 percent butterfat.

	<u>Estimate</u>	<u>Actual</u>
	<u>(\$ per cwt)</u>	
Base Month Price	12.97	13.17
Change in Product Prices	+ 1.54	+ 1.60
BFP	14.51	14.77

Using our BFP estimate plus the July Order No. 2 seasonal adjuster of \$0.03 equaled a July Class III price of \$14.54. Our estimated Class III-A price was \$15.56 per hundredweight.

To get the estimated blend price, we take the anticipated class utilizations discussed earlier and multiply each class utilization percentage times each class price. To this number we make adjustments for cooperative payments, transportation, and inventory reclassifications. Monthly, this adjustment is usually a deduction of \$0.16 per hundredweight. See example:

	<u>Utilization</u>		<u>Price</u>		<u>Dollar Value</u>
Class I	39.2	x	13.30	=	5.21
Class II	16.6	x	11.18	=	1.86
Class III	41.7	x	14.54	=	6.06
Class III-A	2.5	x	15.56	=	<u>0.39</u>
			Subtotal:		13.52
			Less adjustment:		<u>(0.16)</u>
			Estimated Price for July:		13.36

When the actual BFP was announced at \$14.77 for July, our uniform price estimate was revised upward. In addition, the Class III-A price was higher, again positively affecting the blend.

Keep in mind the 2-month lag in the Class I and II prices; the July prices were based off of the May BFP of \$10.88. Note that the August Class I and II prices are considerably higher than July's due to the record \$2.22 increase in the June BFP.

Also, a phenomenon occurred during July. The Class III price was higher than the uniform price; this is the first time this has ever happened under Order No. 2. Because of the lag in prices combined with the record-setting increase in the BFP, the Class I and II prices actually lowered the blend price for July. ♦

In-Area Sales Continue to Decline

For the first 6 months of 1998, total sales of packaged fluid milk products in the New York–New Jersey (Order No. 2) milk marketing area declined 1.5 percent compared to the same period in 1997. The accompanying table shows in-area sales for the January–June period of 1996–1998. Comparisons for 1996 have been adjusted for leap year. Data for 1998 is preliminary.

In November 1997, the Food and Drug Administration eliminated the standards of identity on lowfat dairy products to allow labeling in accordance with the National Labeling and Education Act of 1990. As a result, new descriptions have been given for certain products: 2% milk is now referred to as reduced fat; 1% milk is now called lowfat; and skim milk is fat free.

Of the aforementioned categories, only fat free milk experienced an in-area increase in sales. Sales grew 3.7 percent during the first half of 1998, increasing fat free's market share to 14.6 percent of total sales. Flavored milk and drinks increased slightly. The influence of lower fat products continues in this category shown by the decrease in average butterfat test for the years shown in the table. Buttermilk sales increased 4.9 percent in 1998 but only

Sales of Packaged Fluid Milk Products Inside the NY–NJ Marketing Area, January–June, 1996–98

Product	1996	1997	1998	Year-to-year change	
				1996-97*	1997-98
	million pounds			percent	
Whole	1,104.6	1,067.4	1,039.1	(3.1)	(2.6)
Reduced Fat	391.4	377.9	363.7	(3.2)	(3.8)
Lowfat	296.4	290.5	288.7	(1.7)	(0.6)
Fat Free	289.5	296.0	306.9	2.5	3.7
Flavored	88.4	90.7	91.6	2.9	1.0
Buttermilk	7.5	7.0	7.3	(6.4)	4.9
Total	2,177.8	2,129.5	2,097.3	(1.9)	(1.5)

* Adjusted for leap year.

accounted for 0.3 percent of total sales, unchanged from the past two years.

Whole milk sales declined 2.6 percent during the first half of 1998, lowering its share of total sales to 49.5 percent. This is the first time whole milk sales have been below 50 percent of the total. Even though lowfat sales (1% milk) dropped slightly, their share of the Order No. 2 market increased 0.2 percentage points.

On a monthly basis, sales during the first 6 months of 1998 have been below the previous year for every month except June. ♦

Dairy Commodity Markets Remain Bullish

Through the second week in August, wholesale market prices for cheese and butter have remained at record levels after bottoming out in early May. In turn, the basic formula price (BFP) for June and July was significantly above the May BFP, and the possibility exists for a near record BFP being attained in August. The BFP, which is used to determine Class I, II and III prices under federal orders, is a calculated price. It combines an estimate of the value manufacturing plants buying Grade B milk in Minnesota and Wisconsin pay dairy farmers (base month price) together with a monthly average of wholesale market prices for Cheddar cheese, butter, and dry milk powder (change in product prices). See "Forecasting the Uniform Price" article for related information.

Prices Have Risen

The wholesale price of Grade AA butter on the Chicago Mercantile Exchange (CME) has risen 16.75 cents per pound to \$2.1525 (as of August 14) since we last reported on record butter prices on July 17. Prices for 40-pound block Cheddar cheese on both the CME and the National Agricultural Statistics Service (NASS) survey also have risen since last month, although to a lesser degree. The CME price has remained at \$1.6575 per pound for three consecutive trading sessions after jumping 5 cents on July 24. Of possible future concern, the CME price for barrel cheese, which is not used in the BFP formula, has

been falling and currently is \$1.4875. Typically, the spread between block and barrel prices is within 5 cents with barrel prices below block's. The current spread has barrels 17 cents lower than blocks.

The NASS survey cheese prices (used in the BFP formula) also have increased. For the week ending August 7 the NASS price was \$1.6200; 3.75 cents below the equivalent CME price.

BFP Futures Prices

Both the CME and the Coffee, Sugar and Cocoa Exchange (CSCE) trade BFP futures contracts. BFP futures contracts for a given month can be purchased on either exchange up until the day before the BFP for the particular month is announced by USDA. Although futures prices fluctuate considerably in the period before the actual BFP is announced, perhaps they do serve as an indicator of what industry buyers and sellers think the announced BFP will be. As of August 14, August BFP futures contracts settled on the CME at \$15.30 per hundredweight; the CSCE settling price was \$15.29. Looking ahead a few months to December, when uncertainty about weather, milk production, crops, and other factors that can affect the future availability of milk are much greater, CME and CSCE BFP futures are \$12.50 and \$12.55 per hundredweight respectively. As comparison, the actual BFP for May 1998 was \$10.88 per hundredweight. ♦

Determination of Uniform Price of \$13.53 for July 1998

Per hundredweight of milk testing 3.5 percent butterfat received in bulk from farms in the 201-210 mile zone

TOTAL VALUE OF POOLED MILK							
Class	Milk pounds	Per-cent	Minimum price	Value at minimum price	Transportation differential dollars	Total value	Contribution per cwt of receipts
I-A	375,958,942	37.1	13.30	50,002,539.26	112,710.34	50,115,249.60	4.940
I-B	14,918,838	1.5	13.30	1,984,205.44	2,181.30	1,986,386.74	0.196
II	156,150,625	15.4	11.18	17,457,639.90	18,552.03	17,476,191.93	1.723
III	448,802,349	44.2	14.80	66,422,747.69	42,172.37	66,464,920.06	6.550
III-A	<u>18,716,667</u>	<u>1.8</u>	15.62	<u>2,923,543.38</u>	<u>2,760.44</u>	<u>2,926,303.82</u>	<u>0.289</u>
Reported receipts	1,014,547,421	100.0		138,790,675.67	178,376.48	138,969,052.15	13.698
Adjustments:	<u>Product pounds</u>		<u>Dollars*</u>				
Sec. .60(d)(6) I	2,606,047		8,411.17				
Sec. .60(d)(6) II	4,571,849		(82,750.46)				
Total Sec. .60(d)(2) thru (6)	7,177,896		(74,339.29)			74,339.29	(0.008)
Total adjustments	7,177,896		(74,339.29)				
Total pool milk classified	1,014,547,421						
Handlers must pay			(74,339.29)	138,790,675.67	178,376.48	138,894,712.86 **	13.690
COMPUTATION OF UNIFORM PRICE							
	<u>Milk pounds</u>			<u>Dollars</u>		<u>Dollars per cwt of receipts</u>	
Total value of pooled milk				138,894,712.86		13.690	
Less: Cooperative payments	651,710,637		260,684.25			0.026	
Reserve			898,671.75			0.088	
Transportation credit	1,014,547,421		1,521,821.14	<u>(2,681,177.14)</u>		<u>0.150</u>	<u>(0.264)</u>
Value of pooled milk less subtractions				136,213,535.72		13.426	
Add: Freight adjustment to 201-210 mile zone			154,681.51			0.015	
Unreserved cash in producer settlement fund			<u>900,048.83</u>	<u>1,054,730.34</u>		<u>0.089</u>	<u>0.104</u>
Uniform Price	1,014,547,421			137,268,266.06		13.530	

* Includes transportation and other applicable differentials.

** In addition handlers must pay \$98,042.49 for butterfat in excess of 3.5 percent.

Note: The average butterfat test of milk delivered was 3.504334 percent. The butterfat differential was \$.223 for each one-tenth of one percent of butterfat.

Comparative Price and Other Descriptive Statistics

	JULY 1997	JUNE 1998	JULY 1998
Order No. 2			
Handlers (with producer milk)	37	32	32
Bulk Tank Units	100	94	97
Producers	10,493	9,764	9,718
Daily Deliveries Per Producer (pounds)	3,162	3,449	3,368
Price Factors, Monthly Averages (dollars)			
Basic Formula Price, 3.5% butterfat, per cwt	10.86	13.10	14.77
Cheddar Cheese, 40-lb blocks, per lb, NASS	1.1767	1.4038	1.5656
Butter, Grade A, per lb#	1.0184	1.8468	1.9185
Nonfat dry milk, Central States, per lb	1.0765	1.0289	1.0297
Uniform Prices (dollars per cwt, 3.5% butterfat)			
Order No. 1, Zone 1 (Boston)	12.69	14.40	13.86
Order No. 2, 1-10 mile Zone* (New York City)	12.54	14.28	14.40
Order No. 4, Philadelphia¶	12.48	14.18	13.56
Class I Utilization Percentage			
Order No. 1	44.2	42.9	53.2
Order No. 2	38.4	37.7	38.6
Order No. 4	42.5	39.6	43.4

CME through May 1998; Grade A equivalent price effective June 26, 1998.

* Includes 15-cent transportation credit.

¶ Includes 6-cent direct-delivery differential.

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