

conjunction with a product price formula updater. This price would be available on or before the 5th day of the month and would be based on the price for the second preceding month updated by the change in a product price formula for the preceding month.

The witness representing the MIF/IICA testified that a basic formula price, based on an expanded, unregulated competitive pay price for Grade B milk in Minnesota and Wisconsin, would best reflect the supply and demand conditions for all major uses of manufactured dairy products and would provide the industry with a reliable price series. The witness stated that the base month M-W price survey represents about 60 percent of all Grade B milk in Minnesota and Wisconsin and incorporates a representative sample of both twice-a-month pay plants, as in the current M-W price, and once-a-month pay plants. Because the base month M-W price available on or before the 5th day of the month is for the second preceding month, the witness stated the need for a product price formula to update the base month M-W price. The MIF/IICA proposed adopting a butter/powder/cheese formula using annual product yields and Minnesota and Wisconsin product weights to update the base month M-W price. This formula was utilized in the Department's study to update the Agricultural Prices M-W. For example, the use of an updating formula would result in the price announced on March 5th being based on January pay prices updated by changes in product prices between January and February.

The witness testified that this proposal would be essentially revenue-neutral when compared to the current M-W price. Their comparison of these two price series from January 1988 through April 1992 resulted in an updated base month M-W price that averaged only five cents per hundredweight higher than the current M-W price.

A witness representing Country Fresh, Inc., the Morningstar Group, Inc., and Oak Farms Dairy (Country Fresh, et al.) also testified in support of the adoption of the updated base month M-W price as a replacement for the current M-W price. The witness supported this proposal for four main reasons: (1) It uses actual Grade B milk prices in Minnesota and Wisconsin, thus linking Federal order prices to the competitive markets; (2) it expands the Grade B survey to alleviate NASS' statistical concerns; (3) prices remain relatively equal to current M-W prices; and (4) the proposal provides the same amount of

advance pricing currently available under the Federal order program.

Kraft also supported the adoption of the base month M-W price as the replacement for the current M-W price. However, Kraft's proposal does not include an updater. Thus, the price announced on the 5th of each month would be the price for the second preceding month. For example, the price announced on March 5th would represent January pay prices. The witness representing Kraft testified that the adoption of the base month M-W without an updating adjuster would accomplish the following objectives: (1) Eliminate the use of estimated prices; (2) Keep the M-W price determined in a non-regulated market; (3) Reflect competitive conditions for milk rather than products; (4) Result in a more competitively determined price; and (5) Remain free from fine tuning.

The Kraft witness testified in opposition to the use of an updater in conjunction with the base month M-W price for two reasons. First, although he agreed that product prices and milk prices are related, he stated that changes in competitive milk prices do not correspond exactly with changes in product prices. Secondly, the witness asserted that product price formulas are subject to controversy based on which product prices, product yields, and weight factors are used.

The Kraft witness acknowledged that the additional lag created by Kraft's proposal may affect the way the industry conducts business, as the lag may create month-to-month differences in processor margins. However, the witness contended that over time this proposal does not change the competitive value of milk to either producers or processors.

Opposition to the adoption of the base month M-W price was presented by witnesses representing NFO, TAPP/FUMMC, and the United States Cheese Makers Association, the American Producers of Italian Type Cheese Association, the Ohio Swiss Cheese Association, and the Wisconsin Cheese Makers Association (Cheese Makers) and in briefs filed on behalf of these organizations and WFBF/MMPA. The witnesses for these organizations objected to the adoption of the base month M-W price for two primary reasons. First, the decline in the amount of Grade B milk production raises uncertainty about the statistical reliability of any survey based only on Grade B milk. Secondly, a Grade B only survey does not reflect the true value of milk used for manufacturing purposes.

The opposition recited statistics regarding the decline in Grade B milk

producers and processors that they claim has resulted in a lack of competition for the Grade B milk supply and an increased competition for the Grade A milk supply. The opposition further contended that as manufacturers shift money away from the Grade B supply, they can use this money to attract the Grade A milk supply. This results in Grade B prices which do not truly reflect the value of milk used for manufacturing purposes. The opponents argued that merely enlarging the sample size would neither affect the amount of competition nor the value of the milk.

The Cheese Makers also argued that the continued use of a Grade B survey results in the extended use of an untimely price announcement, announcing the price for the milk after it has been manufactured into products. The witness stated that the dairy industry is one of the last industries to engage in the receipt of a raw commodity, manufacture it into finished products, and price and sell these products before knowing the cost of the raw ingredient. This, according to the witness, is resulting in an unstable market.

To follow through on the argument presented by the Cheese Makers regarding the untimeliness of a Grade B survey, several witnesses opposed the additional lag in pricing created by Kraft's proposal. In fact, most witnesses who supported the adoption of a competitive pay price series advocated the use of a product formula for updating purposes. One witness for the Central Milk Producers Cooperative (CMPC) stated that the industry has long recognized one problem with the current M-W price being the time lag between changes in product markets and milk prices both on the upside and downside of the market. The combination of the M-W price lag and the forward pricing used in the Federal order program further complicates the timing problem and any additional lag would be unacceptable. In its brief, CMPC further asserted that an additional lag could create an opportunity for exploitation of the market by manufacturers.

The witness for Country Fresh, et al., stated that these organizations strongly oppose any reduction in the amount of forward notice the industry currently receives on its raw milk costs. This point of view was further addressed by the National Milk Producers Federation witness who stated that Federal order prices should, to the maximum extent possible, reflect current market conditions. The brief filed on behalf of AE/SFG stated that although we "understand Kraft's proposal \* \* \* less