

Testimony Submitted on Behalf of
Northeast Farm Credit Associations
Federal Marketing Order Hearing on Class I Differentials
December 12, 2006

Northeast dairy farmers have experienced very difficult operating conditions for the entire 2006 operating year. Farm milk prices plummeted to levels well below cost of production. Also, cost of production itself has been under substantial upward pressure as a number of costs including anything closely related to the energy complex such as trucking and utilities, interest costs and now feed costs have seen substantial upward pressure. In addition to these market adversities, some regions within the Northeast have also experienced cropping adversity with heavy late spring rains delaying and even prohibiting corn planting and interfering with early summer forage harvesting. All of this adversity speaks to the need to reconsider Federal milk marketing order price formulas as to any possible ways to update them to the benefit of dairy producers.

I am representing the CoBank Northeast Regional Council and more specifically the four Farm Credit associations who collectively serve the eight states of the Northeastern United States:

- Farm Credit of Western New York
- First Pioneer Farm Credit
- Yankee Farm Credit
- Farm Credit of Maine

Collectively these four associations provided nearly \$1 Billion of credit to approximately 4,500 dairy farmers in our region as of December 31, 2005 and this accounts for more than half of the total credit used by dairy farmers. In addition, we provide a variety of other services to dairy producers including farm accounting services, business consulting, leasing, crop insurance and property appraisal.

I am currently employed by Farm Credit of Western New York as its Chief Operating Officer, a position I've held since 1998. I have spent 30 years working with farm credit and farmers in the Northeast as a loan officer, credit analyst, credit manager and chief credit officer. I am a past president of the Northeast Cooperative Council and currently serve as a member of the Northeast Dairy Leadership team; a team of dairy leaders from NY, PA. and VT formed to collaborate on Dairy issues facing each state and the Northeast milkshed collectively as dairy policy is considered in the future. In my current capacity I serve as Chief Financial Officer and Chief Credit Officer as well as providing operational leadership for all financial services for Farm Credit of Western New York. In this capacity I have substantial daily insight into our dairy farm customers' actual farm operating conditions.

Exhibit	18
Witness	
Date	Rptr.
Powers Garrison & Hughes	

Starting in 1978, our Associations have annually prepared a detailed report on farm operating conditions called the *Northeast Dairy Farm Summary*. This is a statistical summary of actual farm accounting records submitted by several hundred of our customers for tax and credit purposes. Our staff works closely with participating producers to obtain balance sheets and income statements, to reconcile the data, to obtain additional data such as average number of cows and to otherwise prepare the data for use in our annual summary.

Our 2005 producer sample consisted of 539 farms from across seven of the Northeast states. The average characteristics of these farms were:

- 232 cows average size
- 577 crop acres
- 5.0 worker equivalents including the family operators
- 21,593 pounds of milk sold per cow
- Milk price of \$16.12 per cwt.
- \$590,000 of debt, or \$2,543 per cow
- 72% net worth

This is a representative sample of our Northeast dairy farm industry that is very useful for studying year-to-year trends and differences in profitability and cost factors among individual farms. It is not intended to be a complete analysis nor a random sample of all dairy farms in the Northeast, although we believe that this data is the most indicative set of data available for studying Northeast dairy farms over a long period of years.

For purposes of this testimony, we will present data from 1990 to present, including our best estimate of 2006 annual results as estimated by my colleague, Mr. James Putnam, II, Senior Vice President of First Pioneer Farm Credit. In showing these 17 years, it is our intention to provide a broad historical context for the numbers that includes the 1996-98 baseline period used in the 2000 Federal Order changes.

There has been substantial cost inflation being experienced by dairy farmers in 2006, and for that reason, it is critical to include estimated 2006 results as we have done here. Our estimation procedure for 2006 is basically:

- Use actual **2005 Cost of Production** broken down by the 18 individual cost categories from our *Northeast Dairy Farm Summary* as our base.
- Change each individual category by the percent change in the relevant input cost index as published in the US Department of Agriculture's monthly *Agricultural Prices* statistical report.
- Adjust each individual cost category for the increase in milk production per cow during 2006, as reported by the US Department of Agriculture in its monthly publication called *Milk Production*. For the first three quarters of 2006, milk production per cow is reported to be up by 1% per cow in our 8-state region, which has the effect of offsetting cost inflation by that same amount.

From our data, we then constructed a cost series that we are calling *Labor, Resource and Utility* expenses which attempts to track costs of Grade A milk production referenced in the 2000 Federal Order proceedings as well as testimony submitted by proponents of the present petition. This series includes the following cost categories from our data set:

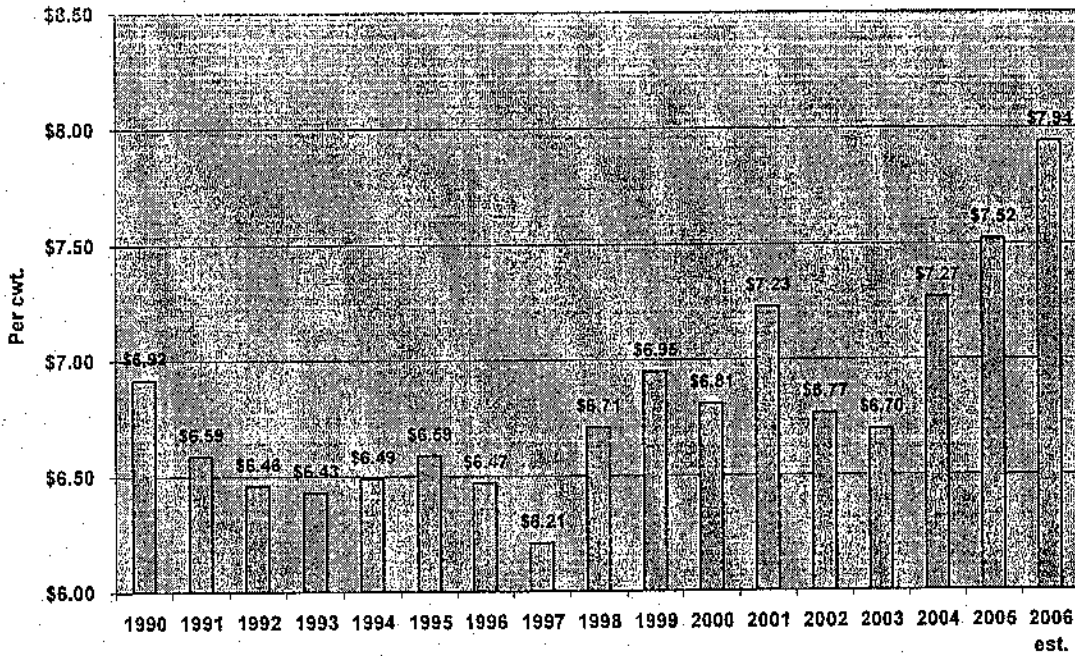
- Hired labor
- Insurance
- Interest on debt
- Repairs
- Supplies
- Taxes
- Utilities
- Veterinary
- "Other" expenses not specifically categorized

This series is shown in the graph at the top of the next page for the 1990 to 2006 period, and then as a percent change in the graph on the lower part of the page.

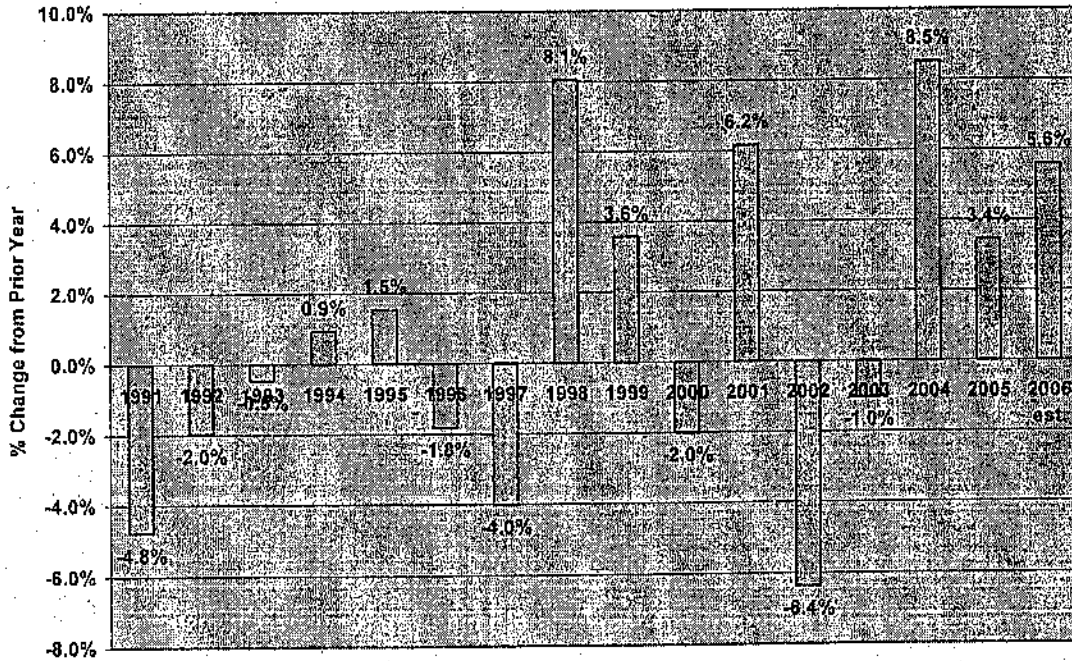
Based on what this data is telling us, we make the following conclusions about *Labor, Resource and Utility* expenses:

1. This combination of expenses accounts for 55% of total cash operating expenses in both 2005 and 2006. It has accounted for an average of 54% of total expenses since 1990.
2. This general category of non-feed, non-crop production costs does not show a steady year-to-year upward progression, but rather fluctuates quite a bit from year to year. This is not a surprise as dairy farmers are continually challenged to manage around a large array of external factors that constantly influence their cost of production.
3. The general trend within this price series has been upward, dampened considerably by continual increases in milk production per cow which have the effect of offsetting pure input cost increases to some extent.
4. Comparing 2006 estimated *Labor, Resource and Utility* costs of production with the average for 1996-98 shows a 23% total increase.
5. Looking just at the change since 2003 shows that cost inflation to dairy farmers has accelerated in the past three years, increasing 18% just since 2003.

Labor, Resource and Utility Expense Per Cwt.
for Northeast Dairy Farms, 1990 - 2006



Labor, Resource and Utility Expense for Northeast Dairy Farms,
Percent Change from Prior Year

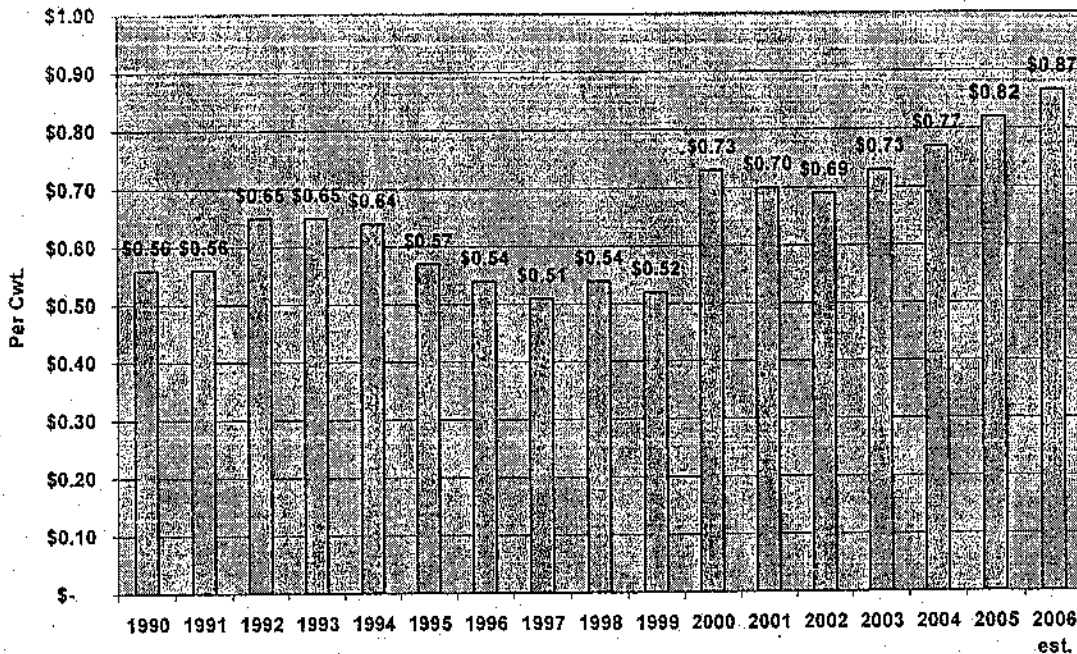


The trend over time has been for *Labor, Resource and Utility* costs to increase with general inflation. There have also been periods, such as 2002 and 2003, when this category of expenses declined a bit. So what might we anticipate in 2007 and 2008? Our view is that there continues to be substantial upward pressure on this category of costs which will likely keep it at 2006 estimated levels and probably modestly higher in the next couple of years. Our rationale is:

- Labor, the largest component of this cost category, is likely to continue to rise along with prevailing wage rates in the economy. Several Northeast states have already raised the minimum wage and there seems a fair likelihood of a Federal increase when the new Congress takes over.
- Interest rates were at historically low levels in 2002 and 2003 as the Federal Reserve Board tried to manage recession and the impact of the 9/11 terrorist attacks. While rates may have peaked out in the current cycle, no one that I know of is forecasting a near or sharp reduction in interest rates in the coming year. Most dairy farmers have drawn extensively on their operating lines of credit this year to help pay bills and so the prospect is that they are entering 2007 with higher levels of debt on which interest is incurred.
- Energy costs have backed off somewhat in the last 6 months and this is reflected in the USDA cost indices. Again, no one that I know of is forecasting a return to \$1.35 gasoline and diesel. Today's energy-driven costs are here to stay and have a substantial impact on dairy farmers' cost structure in such areas as utilities and other services.

We also looked at hauling costs paid by dairy farmers which are a separate category in our overall cost accounting approach. Given the hyperinflation of fuel costs in the last couple of years, it should come as no surprise that Northeast dairy farmers have experienced substantial inflation in this category as well – up 63% between the 1996-98 base period and 2006. Since this cost is on a per cwt. basis and is passed back to the producer with basically no opportunity for cost control, it is not surprising to see this trend. The data is shown in chart form on the next page.

Hauling Cost Per Cwt.
for Northeast Dairy Farms, 1990 - 2006



In summary, Northeast dairy farmers have experienced substantial cost inflation in their businesses during the past three years. We calculate this to be a 23% increase in the specified *Labor, Resource and Utilities* cost category since the 1996-98 base period and 18% in just the past three years. This would have been a substantially larger percentage increase had it not been for the continuing gains in efficiency that our producers have been achieving. We support all efforts to update the pricing provisions of the Federal marketing orders to properly reflect today's cost realities back to dairy producers. Thanks for hearing us on this important matter today.

December 11, 2006

Analysis and Narrative

- James Putnam, II, Senior Vice President, First Pioneer Farm Credit, ACA
- Scott Herring, Chief Operating Officer, Farm Credit of Western New York, ACA
- Joanna Samuelson, Director of Knowledge Exchange, First Pioneer Farm Credit, ACA

	Cost of Production		COP + Return on Equity	
1990	\$ 14.56	1.60	\$ 16.16	0.32
1991	\$ 13.33	1.50	\$ 14.83	0.30
1992	\$ 13.28	1.40	\$ 14.68	0.28
1993	\$ 13.32	1.40	\$ 14.72	0.28
1994	\$ 13.51	1.40	\$ 14.91	0.28
1995	\$ 13.07	1.80	\$ 14.87	0.36
1996	\$ 14.36	1.20	\$ 15.56	0.24
1997	\$ 14.00	1.15	\$ 15.15	0.23
1998	\$ 13.82	1.15	\$ 14.97	0.23
1999	\$ 13.67	1.20	\$ 14.87	0.24
2000	\$ 13.16	1.30	\$ 14.46	0.26
2001	\$ 14.51	1.25	\$ 15.76	0.25
2002	\$ 12.89	1.25	\$ 14.14	0.25
2003	\$ 12.12	1.30	\$ 13.42	0.26
2004	\$ 14.53	1.40	\$ 15.93	0.28
2005	\$ 14.55	1.50	\$ 16.05	0.30
2006 est.	\$ 15.84	1.50	\$ 17.34	0.30

1996-98 Avg.	\$ 14.06	\$	15.23
<u>% Change:</u>			
96-98 to 2006	12.7%		13.9%
2003 to 2006	30.7%		29.2%

The Cost of Producing Milk

	<u>2005</u>	<u>2006</u>
Adj. Cash Operating Exp.	15.08	15.73
+ Depreciation	1.27	1.32
+ Family Living	0.89	0.91
Total Costs	17.24	17.96
- Nonmilk Income	2.69	2.69
Net Cost of Production	14.55	15.27

	Chemicals	Custom	Feed	Fertilizer	Freight	Fuel	Insurance	Interest
1990	0.15	0.15	4.40	0.61	0.56	0.46	0.35	1.02
1991	0.14	0.13	3.65	0.48	0.56	0.41	0.35	1.05
1992	0.18	0.14	3.89	0.48	0.65	0.39	0.35	0.87
1993	0.18	0.17	3.86	0.44	0.65	0.38	0.38	0.77
1994	0.20	0.17	3.92	0.44	0.64	0.36	0.38	0.77
1995	0.20	0.14	3.59	0.42	0.57	0.31	0.37	0.94
1996	0.19	0.17	4.72	0.45	0.54	0.34	0.30	0.84
1997	0.20	0.18	4.56	0.49	0.51	0.35	0.28	0.83
1998	0.23	0.22	4.24	0.53	0.54	0.30	0.27	0.87
1999	0.21	0.27	3.76	0.51	0.52	0.29	0.27	0.77
2000	0.16	0.33	3.85	0.44	0.73	0.43	0.26	0.85
2001	0.18	0.47	4.23	0.48	0.70	0.40	0.25	0.76
2002	0.16	0.41	3.93	0.42	0.69	0.34	0.24	0.54
2003	0.16	0.39	4.19	0.41	0.73	0.43	0.24	0.52
2004	0.18	0.50	4.76	0.44	0.77	0.52	0.25	0.49
2005	0.21	0.49	4.23	0.48	0.82	0.66	0.26	0.60

2003 est.

Components as % of Total Cost

	Chemicals	Custom	Feed	Fertilizer	Freight	Fuel	Insurance	Interest
1990	1%	1%	31%	4%	4%	3%	2%	7%
1991	1%	1%	29%	4%	4%	3%	3%	8%
1992	1%	1%	30%	4%	5%	3%	3%	7%
1993	1%	1%	30%	3%	5%	3%	3%	6%
1994	2%	1%	30%	3%	5%	3%	3%	6%
1995	2%	1%	28%	3%	5%	2%	3%	7%
1996	1%	1%	35%	3%	4%	2%	2%	6%
1997	2%	1%	34%	4%	4%	3%	2%	6%
1998	2%	2%	31%	4%	4%	2%	2%	6%
1999	2%	2%	28%	4%	4%	2%	2%	6%
2000	1%	2%	29%	3%	5%	3%	2%	6%
2001	1%	3%	29%	3%	5%	3%	2%	5%
2002	1%	3%	29%	3%	5%	3%	2%	4%
2003	1%	3%	31%	3%	5%	3%	2%	4%
2004	1%	3%	31%	3%	5%	3%	2%	3%
2005	1%	3%	28%	3%	5%	4%	2%	4%

Labor	Rent	Repairs	Seed	Supplies	Taxes	Utilities	Vet	Other
1.93	0.42	1.16	0.23	0.69	0.43	0.45	0.47	0.42
1.78	0.38	0.87	0.21	0.57	0.42	0.44	0.47	0.64
1.78	0.37	0.98	0.24	0.60	0.41	0.44	0.50	0.53
1.82	0.38	0.90	0.22	0.61	0.42	0.43	0.51	0.59
1.78	0.41	0.93	0.23	0.64	0.40	0.44	0.57	0.58
1.65	0.38	0.84	0.21	0.65	0.41	0.43	0.54	0.76
1.82	0.37	0.96	0.21	0.69	0.33	0.45	0.59	0.49
1.79	0.42	0.90	0.22	0.70	0.31	0.42	0.57	0.41
1.93	0.40	1.08	0.24	0.84	0.31	0.39	0.61	0.41
2.12	0.48	1.14	0.25	0.90	0.29	0.38	0.65	0.43
2.20	0.37	1.00	0.22	0.86	0.29	0.38	0.61	0.36
2.47	0.41	1.07	0.23	0.98	0.27	0.39	0.69	0.35
2.46	0.36	0.93	0.21	0.93	0.27	0.38	0.69	0.33
2.52	0.31	0.86	0.22	0.91	0.27	0.40	0.67	0.31
2.70	0.33	1.13	0.25	0.93	0.28	0.41	0.73	0.35
2.72	0.30	1.15	0.28	1.00	0.29	0.43	0.76	0.31

Labor	Rent	Repairs	Seed	Supplies	Taxes	Utilities	Vet	Other
14%	3%	8%	2%	5%	3%	3%	3%	3%
14%	3%	7%	2%	4%	3%	3%	4%	5%
14%	3%	8%	2%	5%	3%	3%	4%	4%
14%	3%	7%	2%	5%	3%	3%	4%	5%
14%	3%	7%	2%	5%	3%	3%	4%	4%
13%	3%	7%	2%	5%	3%	3%	4%	6%
13%	3%	7%	2%	5%	2%	3%	4%	4%
13%	3%	7%	2%	5%	2%	3%	4%	3%
14%	3%	8%	2%	6%	2%	3%	4%	3%
16%	4%	9%	2%	7%	2%	3%	5%	3%
16%	3%	7%	2%	6%	2%	3%	5%	3%
17%	3%	7%	2%	7%	2%	3%	5%	2%
18%	3%	7%	2%	7%	2%	3%	5%	2%
18%	2%	6%	2%	7%	2%	3%	5%	2%
18%	2%	7%	2%	6%	2%	3%	5%	2%
18%	2%	8%	2%	7%	2%	3%	5%	2%

	<u>2006</u>	I	II	III	Total	<u>2005</u>	I	II	III
CT		20	19.5	19	19.5		20	20	20
ME		32	32	32	32.0		33	33	33
MA		16	16	15.5	15.8		17	17	16
NH		15.5	15	15	15.2		16	16	16
NJ		12	11.5	11	11.5		12	12	12
NY		650	649	643	647.3		649	646	648
RI		1	1.1	1.1	1.1		1	1	1.1
VT		143	142	141	142.0		143	144	143
Total					884.4				
CT		97	95	86	278		99	101	92
ME		140	147	145	432		147	155	151
MA		72	73	68	213		73	76	72
NH		77	76	71	224		75	79	74
NJ		48	47	41	136		49	50	47
NY		3060	3130	3049	9239		2935	3116	3053
RI		4.6	4.9	4.7	14.2		4.6	5	4.7
VT		663	672	636	1971		655	688	656
Total					12507.2				
					14142.02				
New England					25%				

Total

20.0

33.0

16.7

16.0

12.0

647.7

1.0

143.3

889.7

292

453

221

228

146

9104

14.3

1999

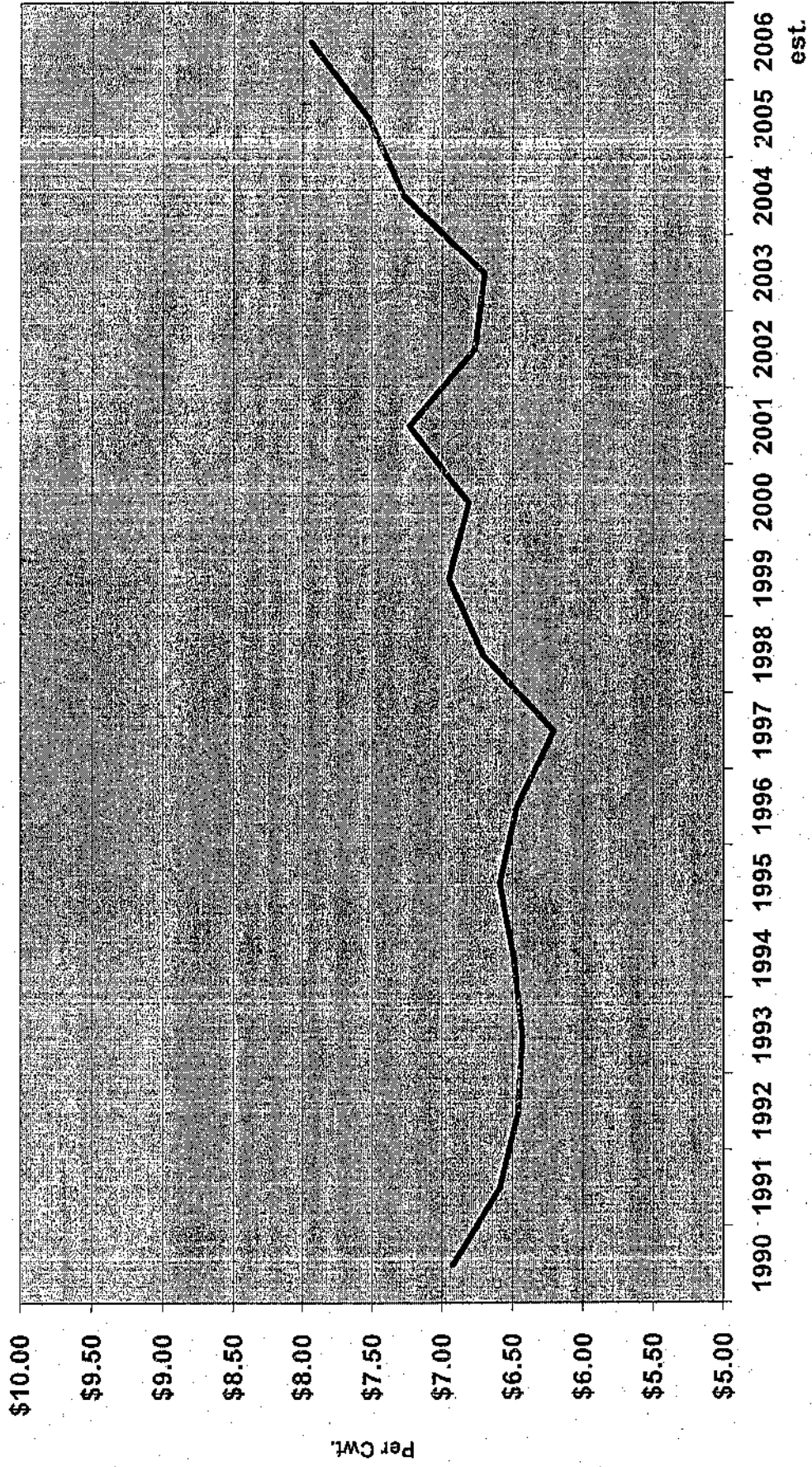
12457.3

14001.69

1.0%

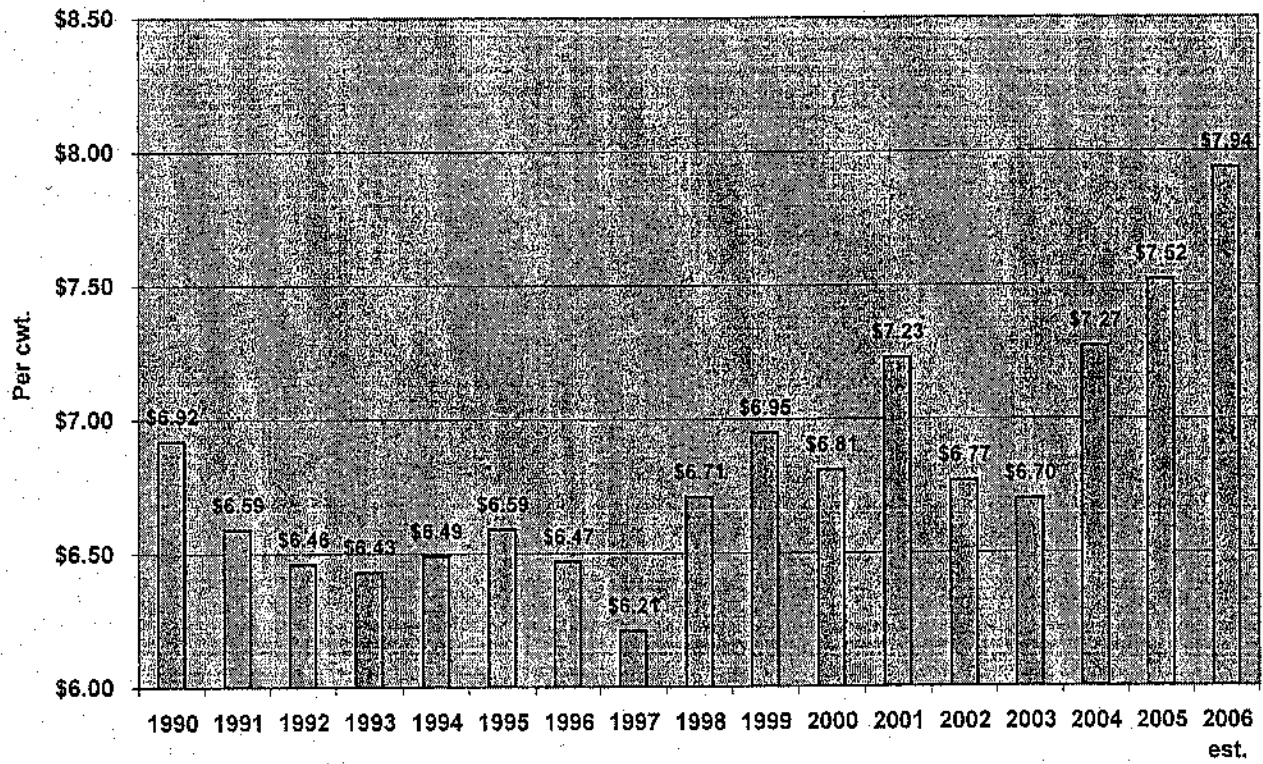
26%

Labor, Resource and Utility Expense Per Cwt.
for Northeast Dairy Farms, 1990 - 2006

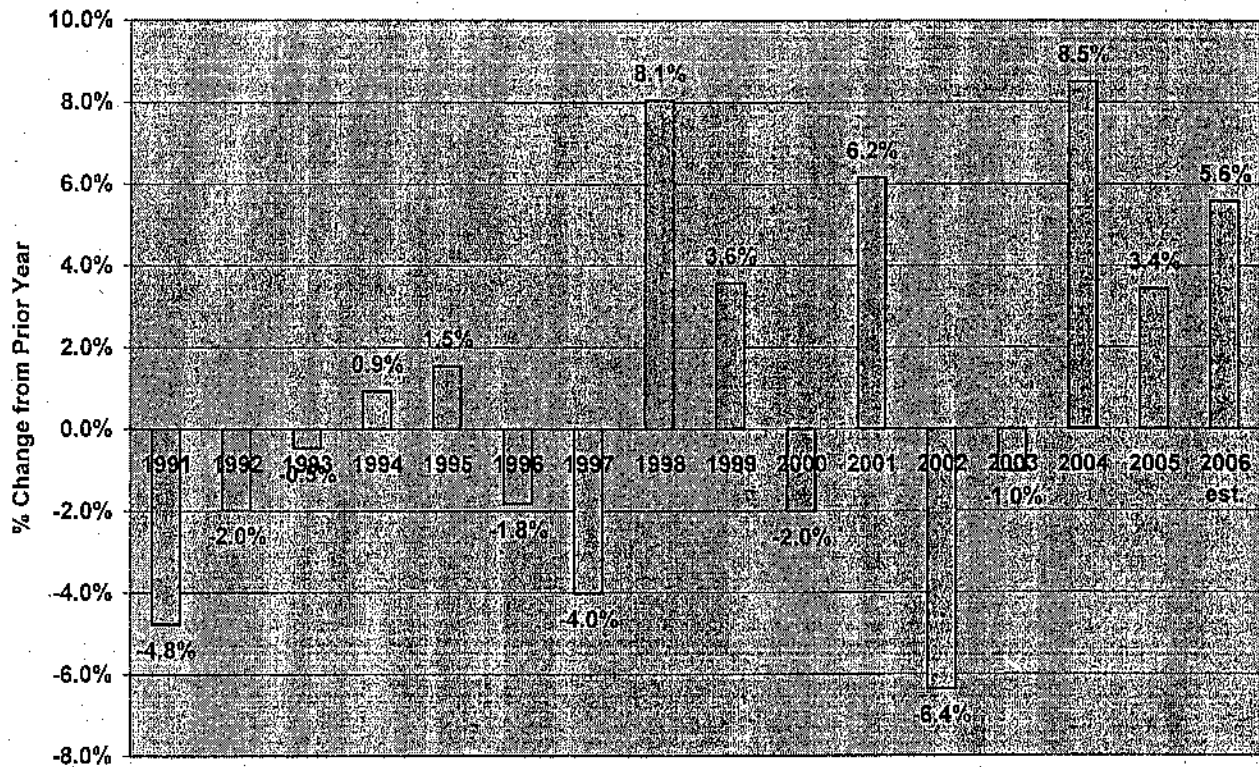


est.

Labor, Resource and Utility Expense Per Cwt.
for Northeast Dairy Farms, 1990 - 2006



**Labor, Resource and Utility Expense for Northeast Dairy Farms,
Percent Change from Prior Year**



Year	Chemicals	Custom	Feed	Fertilizer	Fuel	Insurance	Interest	Lab	Rent	Repairs	Seed	Supplies	Taxes	Utilities	Vet	Other	Cows	Cash Op. Exp.	Labor, Resources & Utility	Family Living	Depreciation	LRU % Change	
1990	0.15	0.19	4.40	0.81	0.86	0.46	0.35	1.02	1.93	0.42	1.16	0.23	0.69	0.43	0.47	0.42	0.22	14.12	\$ 8.92	1.43	1.33	-1.8%	
1991	0.14	0.18	3.65	0.48	0.56	0.41	0.35	1.05	1.78	0.38	0.87	0.21	0.57	0.42	0.44	0.47	0.18	12.73	\$ 6.59	1.35	1.32	-4.8%	
1992	0.18	0.14	3.88	0.46	0.65	0.39	0.35	0.87	1.78	0.37	0.98	0.24	0.60	0.41	0.44	0.50	0.24	13.04	\$ 6.46	1.31	1.26	-2.0%	
1993	0.20	0.17	3.66	0.44	0.65	0.38	0.38	0.77	1.82	0.38	0.80	0.22	0.61	0.42	0.43	0.51	0.23	12.94	\$ 6.43	1.20	1.36	-0.5%	
1994	0.20	0.14	3.92	0.44	0.64	0.36	0.38	0.77	1.78	0.41	0.84	0.23	0.64	0.40	0.44	0.57	0.21	13.07	\$ 6.49	1.12	1.33	0.8%	
1995	0.18	0.17	4.72	0.45	0.54	0.34	0.37	0.94	1.65	0.38	0.84	0.21	0.65	0.41	0.43	0.54	0.19	12.60	\$ 6.59	1.12	1.22	1.8%	
1996	0.20	0.18	4.90	0.49	0.51	0.35	0.28	0.83	1.79	0.42	0.90	0.22	0.70	0.31	0.42	0.57	0.17	13.63	\$ 6.47	1.07	1.14	-1.8%	
1997	0.22	0.22	4.24	0.53	0.54	0.30	0.27	0.87	1.93	0.40	1.08	0.24	0.84	0.31	0.39	0.61	0.17	13.30	\$ 6.21	1.07	1.12	-0.5%	
1998	0.18	0.33	3.76	0.51	0.52	0.29	0.27	0.77	2.12	0.48	1.14	0.25	0.80	0.29	0.38	0.65	0.16	13.58	\$ 6.71	1.04	1.12	8.1%	
1999	0.18	0.33	3.65	0.44	0.73	0.43	0.26	0.85	2.20	0.37	1.00	0.22	0.86	0.29	0.38	0.61	0.16	13.40	\$ 6.96	1.06	1.21	8.1%	
2000	0.18	0.41	4.23	0.48	0.70	0.40	0.25	0.76	2.47	0.41	1.07	0.23	0.80	0.27	0.38	0.69	0.16	13.50	\$ 6.81	1.08	1.19	3.6%	
2001	0.16	0.39	4.19	0.41	0.73	0.43	0.24	0.54	2.46	0.36	0.93	0.21	0.83	0.27	0.38	0.69	0.13	14.54	\$ 7.23	0.95	1.15	2.0%	
2002	0.18	0.39	4.19	0.41	0.73	0.43	0.24	0.52	2.52	0.31	0.86	0.22	0.81	0.27	0.40	0.67	0.13	13.67	\$ 6.77	0.96	1.14	6.2%	
2003	0.18	0.39	4.19	0.41	0.73	0.43	0.24	0.52	2.52	0.31	0.86	0.22	0.81	0.27	0.40	0.67	0.13	13.67	\$ 6.70	0.96	1.14	-1.0%	
2004	0.18	0.39	4.19	0.41	0.73	0.43	0.24	0.52	2.52	0.31	0.86	0.22	0.81	0.27	0.40	0.67	0.13	13.67	\$ 6.70	0.96	1.14	-1.0%	
2005	0.21	0.48	4.23	0.46	0.82	0.68	0.25	0.60	2.72	0.30	1.15	0.28	0.93	0.28	0.41	0.73	0.35	15.14	\$ 7.27	0.89	1.22	8.5%	
2006 est.	0.22	0.50	4.51	0.51	0.87	0.70	0.26	0.87	2.78	0.31	1.17	0.30	1.02	0.28	0.45	0.77	0.31	15.96	\$ 7.94	0.89	1.27	3.4%	
2006 est.																							5.6%
1996-99 Avg. % Change	0.21	0.19	4.51	0.49	0.69	0.33	0.28	0.85	1.85	0.40	0.98	0.22	0.74	0.32	0.42	0.59	0.44	13.50	6.48				
96-98 to 2006	5.1%	63.0%	0.0%	3.6%	11.3%	-8.8%	3.9%	50.8%	-21.5%	19.2%	34.4%	36.7%	-7.9%	8.2%	30.9%	-27.9%	-32.0%	18.2%	22.9%				
2003 to 2006	35.8%	21.8%	7.6%	23.6%	82.2%	10.0%	69.2%	10.5%	0.4%	35.8%	36.5%	11.6%	8.0%	13.6%	15.2%	1.6%	-12.8%	16.7%	18.5%				
2006 Factor	1.045	1.026	1.076	1.068	1.067	1.026	1.472	1.034	1.048	1.028	1.063	1.026	1.016	1.067	1.026	1.026	1.026	1.031					

1.031

Hauling Cost Per Cwt.
for Northeast Dairy Farms, 1990 - 2006

