

PFB EXHIBIT 1

**Testimony Offered for
Pennsylvania Farm Bureau
Before the Pennsylvania Milk Marketing Board
Regarding the Level and Duration of
the Class I Over Order Premium**

September 2, 2015

**Presented by Michael Evanish
Manager, MSC Business Services
PFB Members' Service Corporation**

Introduction

This testimony is offered at the request of Pennsylvania Farm Bureau, which represents over 61,400 farm and rural family members in 63 counties. Dairy farmers comprise the largest segment of agricultural producers who are members of Farm Bureau.

I am Michael Evanish. I currently serve as manager of MSC Business Services, a division of PFB Members' Service Corporation (an affiliate company of Pennsylvania Farm Bureau), and have served in this position since 1997. MSC Business Services provides an array of services to assist farmers economically manage their farm operations. The services provided include income tax planning and preparation, business and tax accounting, payroll services and recordkeeping, business analysis and benchmarking, and business consultation.

I am responsible for overseeing the operation of the division's approximately 4,400 contracts and the supervision of its 35 accountants, known as Account Supervisors, and 25 support staff. I have been employed by MSC Business Services since 1976. Until January 1989, I served as an Account Supervisor, working with members in Butler, Beaver and Lawrence Counties. From 1989 through 1997, I served as Director of Training. In this capacity, I was responsible for educating and training all staff, including Account Supervisors who work with MSC's clients.

Other features of my work experience and educational background are contained in Appendix 1.

In my capacity as Manager of MSC Business Services, it is imperative that I have a working knowledge and understanding of existing economic and financial conditions in Pennsylvania's dairy industry and the likely financial impacts these conditions will have on the current and future operation of the dairy farms. To maintain this working knowledge I am in daily contact with Account Supervisors who share the conditions their clients are experiencing, including prices received for their products.

As I mentioned earlier, an important service that MSC Business Services provides is business consultations. As part of this service, we are often asked to develop budgets and make cost of production projections. I personally review and approve all consulting reports produced by MSC Business Services. Other features of my work experience and educational background are contained in Appendix 1.

To provide our clients with insights into their relative financial health, we prepare comparisons of their operations to all-client averages. One key measurement is how they compare with other MSC dairy clients of similar size and make-up. For the past several years, each dairy farm has received a *Dairy Profitability Comparison* that provides a side-by-side comparison of their income

and costs with the same from “comparably sized” dairy farms and the “top 10% farms” serviced by MSC.

In testimony I offered at last year’s over-order premium hearing, I presented to the Board aggregate annual averages of income and costs experienced by our dairy farms for the years 2008 through 2013.

Table 1 is the same table I offered at the Board’s hearing last September. It displays the annual average incomes, costs and net margins per hundredweight of milk sold by MSC-client dairy farms.

There is little doubt that the prices received by Pennsylvania dairy farmers in 2013 and 2014 have helped them recover significantly from the devastating financial effects of 2009 and 2010. But that two-year period of economic gloom was a serious financial setback, and can’t be ignored, even today. As shown in Table 1, MSC client dairy farms lost, on average, <\$2.53> for every hundredweight of milk produced in 2009. And losses continued, throughout 2010, averaging <\$0.12> per hundredweight. Such losses, for such a prolonged period of time, have a depressing impact on subsequent business decisions and enthusiasm about the future. Without enthusiasm for the future, owners are far less likely to take on the additional financial risk necessary to modernize their operations. They are also far less likely to promote dairy farming as a career to the next generation, placing the future of dairy farming in Pennsylvania in greater jeopardy.

As I indicated in my testimony last September and as shown in Table 1, MSC client dairy farms experienced, on average, modest profits of \$1.04 per hundredweight in 2011 and \$1.41 in 2013, and essentially broke even in 2012. The modest returns did little more than offset the financial losses incurred by MSC-client farms in 2009 and 2010.

For the six-year period of 2008 through 2013, the net margin realized on MSC-client dairy farms averaged a meager \$0.06 per hundredweight. To put it another way, our dairy farmers had little profit to show for these six years of operation.

To help demonstrate just how meager profits were during this period, I added the “Yearly Net Margin” dollar amount to the bottom of each column. The total of all six years was only \$21,660 or an average of \$3,610. I ask that the Board keep in mind that the level of premium established by the Milk Marketing Board for this six-year period was at or above the level of over-order premium mandated in the Board’s current order.

Table 2 indicates the averages of incomes, expenses and net margins per hundredweight for MSC client dairy farms for the period of 2008 through 2014. It essentially is a restatement of Table 1, with an additional column to include the 2014 numbers. The average figures in the last column in Table 2 have been updated from Table 1 to reflect the addition of 2014 information. Again, the “Yearly Net Margin” dollar amounts have been added to the bottom of each column. The total of all seven years is \$144,420 or an average of \$20,631.

2014 brought significant and welcome financial returns to Pennsylvania dairy farms. On average, MSC-client dairy farms experienced an unprecedented net margin of \$3.58 per hundredweight. These returns were predominantly a reflection of the level of prices received for milk in 2014, which were the highest on record.

As many expected, producer prices in 2015 have been much lower than 2014’s record setting prices. And, given the degree to which milk prices have fallen in 2015, based on conversations with Account Supervisors and available data, it is safe to say that 2015’s net margins will be considerably reduced.

Beyond the reduction in the price received for milk, I would point out the trend of increased costs of production that Pennsylvania dairy farmers have experienced in recent years. Looking at Table 2, annual costs of production have increased substantially from 2009’s average of \$19.50. In 2010, the average cost

of production increased to \$20.64, and jumped to over \$23.00 per hundredweight in years 2011, 2012 and 2013. And in 2014, the average cost of production increased by another \$2.00 to \$25.14 per hundredweight.

At past hearings, I have testified on the recent trend for dairy farmers to devote a greater portion of their milk income toward purchases of feed and for the production of feed crops. Table 3 shows the percentage of milk income that was utilized on average for purchased feed and for crop expenses (seed, fertilizer, chemicals and fuel). Keep in mind that these costs are out-of-pocket costs for MSC-client dairy farms.

My prior testimony highlighted for the Board the increased drain on farmers' income to meet expenses related to feed purchases and production of feed. From 2008 to 2013, that percentage of milk income needed to purchase feed and feed crop production inputs averaged over 44% and well above the average of 30% that dairy farms had traditionally experienced prior to 2008. Even with 2014's milk price of \$25.57, the percentage of milk income needed to purchase feed and crop expenses was over 38% on average. Again, much higher than the traditional 30% level.

The need to set aside a greater portion of milk income for the purchase of feed and feed crop production inputs has become the norm on today's dairy operations. Milk income that was previously available to finance other costs must

now be diverted toward feed and crops. In 2014, the high milk price provided relief, while 2015 has seen a significant reduction in milk price without a corresponding reduction in the cost of feed and crops.

Conclusion

2014 was a very positive financial year for Pennsylvania dairy farms. But most experts in the industry predicted that the record-high prices could not be sustained. We have already seen prices drop to dismal levels. Reports from Account Supervisors indicate a 2015 milk price reduction that is greater than that experienced from 2008 to 2009. Only time will tell if this becomes the story line for all of 2015.

Looking to the future, the Board must consider the costs of production trend line and how that will interact with the current price depression. Is 2015 a replay of 2009? Or will Pennsylvania's dairy farmers experience relief in the second half of the year? No one can be sure. The only sure thing is that the current price being received for milk will not support reasonably expected costs of production.

On the basis of the testimony I offer today, I can make no other recommendation but that the over-order premium be continued at least at the current levels for another six months.

I would like to thank the Pennsylvania Milk Marketing Board (PMMB) for the opportunity to offer testimony today.

TABLE 1

**MSC Business Services
Key Dairy Benchmarks per CWT**

	2008	2009	2010	2011	2012	2013	Avg
Income							
Milk	\$19.84	\$13.91	\$18.05	\$21.87	\$19.77	\$21.40	\$19.14
Livestock Income*	\$0.93	\$0.92	\$1.11	\$1.20	\$1.50	\$1.48	\$1.19
Other	\$1.28	\$2.14	\$1.36	\$1.35	\$2.06	\$1.59	\$1.63
Total Income	\$22.05	\$16.97	\$20.52	\$24.42	\$23.33	\$24.47	\$21.96
Expenses							
Management Labor	\$2.24	\$2.17	\$2.14	\$2.22	\$2.20	\$2.10	\$2.18
Feed*	\$5.53	\$5.13	\$5.72	\$7.07	\$6.60	\$6.20	\$6.04
Hired Labor	\$1.64	\$1.54	\$1.56	\$1.70	\$1.84	\$1.97	\$1.71
Interest	\$0.85	\$0.78	\$0.77	\$0.79	\$0.69	\$0.63	\$0.75
Rent	\$0.54	\$0.53	\$0.56	\$0.59	\$0.69	\$0.77	\$0.61
Milk Marketing	\$1.00	\$1.01	\$1.02	\$1.06	\$1.09	\$1.11	\$1.05
Dairy Expenses	\$2.21	\$1.98	\$2.05	\$2.21	\$2.30	\$2.23	\$2.16
Crops (Seed, Chem, Fert, Fuel)	\$2.45	\$1.89	\$1.97	\$2.43	\$2.85	\$2.74	\$2.39
Depreciation	\$1.43	\$2.17	\$1.49	\$1.53	\$1.63	\$1.55	\$1.63
Other	\$3.62	\$2.30	\$3.36	\$3.78	\$3.43	\$3.77	\$3.38
Total Expenses	\$21.51	\$19.50	\$20.64	\$23.38	\$23.32	\$23.07	\$21.90
Net Margin	\$0.54	-\$2.53	-\$0.12	\$1.04	\$0.01	\$1.41	\$0.06

*Adjusted for Inventory Change (Livestock Inventory for Livestock Income and Crop Inventory for Feed)

Avg # Cows	124	119	127	132	134	149	
Milk Sold per Cow	20,113	19,750	20,061	19,992	20,036	20,466	
Yearly Net Margin	\$13,468	<\$59,461>	<\$3,057>	\$27,445	\$268	\$42,997	Total Avg. \$21,660 \$3,610

TABLE 3

MSC Business Services

Key Dairy Benchmarks – Purchased Feed and Crop Expense to Milk Price

<u>Year</u>	<u>Purchased Feed and Crop Expense (Per Cwt.)</u>	<u>Average Milk Price (Per Cwt.)</u>	<u>Percentage of Feed and Crop Expense to Milk Price</u>
2008	\$7.98	\$19.84	40.2%
2009	\$7.02	\$13.91	50.5%
2010	\$7.69	\$18.05	42.6%
2011	\$9.50	\$21.87	43.4%
2012	\$9.45	\$19.77	47.8%
2013	\$8.94	\$21.40	41.8%
2014	\$9.86	\$25.57	38.6%

APPENDIX 1

Michael Evanish, Manager MSC Business Services

Michael Evanish is Manager of MSC Business Services, a division of PFB Members' Service Corporation (an affiliate company of Pennsylvania Farm Bureau). MSC Business Services employs approximately 60 professional and support staff providing services to members consisting of income tax planning and preparation, write-up and computerized records services, payroll preparation, business analysis and benchmarking, and consulting services. All services are provided under contracts numbering in excess of 4,400.

Michael has been with PFB Members' Service Corporation since 1976. He served clients in Butler, Beaver and Lawrence Counties in Western, PA until January 1989 when he became Director of Training. As Director of Training, Michael was team leader for the electronic recordkeeping program currently used by about 700 PA farms, and the rewrite in 1990 & 2006 of the Business Analysis program and meeting the training needs of all staff. In 1997, Michael became Manager of MSC Business Services.

Michael has degrees in accounting and marketing from Clarion University. He is an IRS Enrolled Agent and has passed the CPA exam. For three years he was a member of the IRS Commissioner's Advisory Committee where he chaired the Small Business/Self-Employed Subcommittee. He also served on the PA Department of Agriculture's Dairy Task Force and PA Dairy Leadership Council. The publication of the annual *Dairy Profitability Comparison* is his responsibility.