

# The Milkweed



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The farmer's milk marketing report

## Antitrust Investigators Study Taking Apart DFA

by Pete Hardin

Remember "Ma Bell"!

Federal Antitrust actions that broke up telephone powerhouse AT&T into regional units could be a useful precedent for the fast-moving, federal/state Antitrust investigation into widespread allegations of misbehavior against the nation's largest dairy farmers' cooperative.

The Antitrust Division of the U.S. Department of Justice—currently conducting a nationwide, federal/state investigation of Dairy Farmers of America (DFA)—has hired academics to recommend how to take apart the nation's largest dairy cooperative.

This latest move shows how fast and how far Antitrust's investigation into DFA's alleged misdeeds has progressed in just a few short months. About 15 states are participating in the coast-to-coast Antitrust probe of DFA, the first of its kind in the history of the dairy industry. Investigators seem convinced that DFA's misdeeds have violated protections provided to agricultural cooperatives under the 1922 federal Capper-Volstead Act.

Also at issue: possible violations of a 1977 Consent Decree that was instituted against DFA's predecessor — Mid-America Dairymen.

*The Milkweed* foresees significant action by federal/state Antitrust investigators to severely rein in DFA ... sometime in 2005.

### Demands for info from co-ops, super pools

Antitrust investigators have hit DFA, as well as many other dairy cooperatives and regional "super pools" (common marketing agencies), with lengthy lists of questions about how co-ops are structured and operate, testing procedures for farm milk, etc. These formal requests for information are known as "Civil Investigative Demands." Observers believe that Antitrust officials are "fishing" for understandings about how other dairy co-ops operate, to develop a "benchmark" for evaluating DFA's actions.

The same concept is believed at work in regard to regional dairy co-op "super pools." A "super pool" is a common marketing agency involving two or more co-ops, operated regionally.

Antics of the Southeast Marketing Agency

(SMA—a regional "super pool" controlled by DFA) have been the target of many complaints and inexplicable milk pricing actions. SMA has failed to charge milk buyers in federal orders #5 (Appalachian) and #7 (Southeast) enough money to cover costs of serving the market. SMA's member co-ops have resorted to big reblands (underpayments) against farmers' milk checks to compensate for losses.

### DFA's key concern: keeping lenders' happy

Short-term, the biggest challenge for DFA may be to pacify any emerging worries from the co-op's lenders. A big Antitrust investigation that threatens to break apart the massively-indebted cooperative could spook lenders. DFA's acknowledged debts exceed one billion dollars. That figure is roughly twice the monthly milk revenue of DFA's members.

DFA officials have repeatedly denied that the co-op has used money due to members for unremunerated milk sales as collateral for the cooperative's borrowings. However, a March 4, 1999 news release by Moody's Investors Service clearly stated that DFA's Bylaws specified that creditors claims superceded payments due to members for their milk.

If the Antitrust probe hits DFA hard ... perhaps breaking apart the co-op into its regional operating units ... lenders' ability to cover over \$1 billion of DFA's debt could be impaired. Any perception by DFA's creditors that the co-op is in danger of getting smacked hard by the Antitrust investigation could panic lenders into seizing DFA's assets.

### Will the ship go down with Hanman???

DFA is truly the creation of CEO/President Gary Hanman. Hanman has headed DFA and its predecessor cooperatives since 1974. Along the way, he has hand-picked and custom-fertilized the vast majority of DFA's board of directors, as well as senior- and middle-level management. Loyalty to Hanman is a must at DFA. His power is near absolute.

As Antitrust tightens the vice, questions must arise about how long it will take for the co-op's board of directors to conclude that Hanman's leadership is sending DFA to potential ruin. Hanman's executive compensation is unknown. Questions focus on an

alleged, multi-million dollar bonus he was paid. Further, directors' personal financial assets could be legally challenged if it's proven in court (by creditors or dissident members) that the board of directors failed its mandate to guide the co-op judiciously.

### Massive impact on U.S. dairy industry, if ...

DFA is the nation's largest dairy farmer co-op. *The Milkweed* estimates that, when including DFA members' milk and non-member milk marketed through joint ventures (such as Dairy Marketing Services) and some "super pools," DFA could control as much as 40% of the monthly milk income paid to U.S. dairy farmers. If Antitrust investigators break up DFA ... or if the co-op's lenders get nervous and pull in assets ... the co-op faces some very serious challenges to survival. Prepare for a crash.

Available liquid assets cannot satisfy claims by creditors, suppliers and members' outstanding payments for milk deliveries.

Recent comments by Hanman claimed no wrongdoings and promised to "vigorously defend" the co-op against alleged misbehaviors. Are DFA members' interests served by paying legal bills for Hanman and corporate directors who have misguided the co-op?

## October Class III \$14.16; No Decline for November

USDA announced the October federal order Class III (cheese milk) price at \$14.16/cwt., down 56 cents from June. This decline reflected the downward blip in cash Cheddar prices seen in late September-early October at the Chicago Mercantile Exchange.

That extremely brief, and probably artificial, drop at CME was followed by a return to cash Cheddar prices similar to those seen in August and September.

The November Class III price, which is based on USDA-NASS price surveys that lag CME moves by a couple of weeks, will thus likely rise slightly from the October level.

USDA announced the October federal order Class IV (butter-powder) value at \$12.81/cwt., down 19 cents from September.

The federal order Class I base price for October is \$14.78/cwt., and the November Class I base will drop to \$14.29.

## U.S. a Deficit Milk Producing Nation

by John Bunting

### Supply

The United States is a DEFICIT MILK-PRODUCING NATION.

The latest USDA estimate for federal fiscal year starting October 1, 2004 shows farm milk marketings 3.7% **BELOW** estimated consumer demand.

Proof of that fact is found in the October 12, 2004 "World Agricultural Supply and Demand Estimates" produced by USDA's Economic Research Service (ERS).

ERS projects total U.S. farm milk production for October 1, 2004 through September 30, 2005 at 173.3 billion pounds. If milk used on the farm and not sold is subtracted from this total, 171.3 billion pounds of U.S.-produced milk will be available to consumers this year.

USDA/ERS estimates that "Commercial Use" of dairy products for this federal fiscal year will total 177.9 billion pounds.

This supply-demand gap is obviously being filled by imports — including milk protein concentrate and caseins that are not included in these USDA/ERS calculations.

The 173.3 billion pounds of domestic production amounts to an increase of 3.3 billion pounds (1.94%) from the 2003-2004 fiscal year that concluded September 30. Just where that increase is supposed to come from is not known. It's important to note that ERS lists 2.0 billion pounds of the current year's farm milk supply as "farm use." In other words, some 2.0 billion pounds of this year's 173.3 billion pounds of farm milk will be fed to calves, dumped, etc. Thus, only 171.3 billion pounds of U.S.-produced milk will be available for sale.

Imports are a key element in the milk supply estimate. For this year, ERS projects that 5.2 billion pounds of dairy imports will enter the country for commercial use, down 0.5 billion pounds from the estimated total for the last fiscal year.

HOWEVER ... ERS uses a "milk equivalent, milkfat basis" for estimating dairy imports. That estimate is held faulty by some sources, because it fails to account for the high volume of milk protein powders imported into the U.S.

ERS does not include imports of either casein

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