PA Milk Marketing Board
How USDA Prices Milk – Part 2

This second in a series of four articles discusses how milk *component* prices combine with other factors to formulate *Class* prices. Remember from Part 1 that the "Three Cs" are what make up the process of milk pricing: commodity, component, and class. *Components* are the particles contained in fluid milk that are used in pricing, specifically, butterfat, proteins, and other milk solids. Once protein, butterfat, and other solids prices are calculated, they are added to the following:

- Average of Class III Skim and Class IV Skim Pricing Factor – Calculated from prices and volumes (yield) reported from most recent two-week period with additional $0.74/cwt added.
- Advanced Butterfat Pricing Factor – [Two-week average butter price] – [make allowance (USDA estimate of extra cost to produce butter)] + [yield factor (USDA estimate of cost to convert butterfat to butter)].
- Class 1 Differential – An amount added (usually) as an incentive to move milk from areas of high supply to areas of low supply - often county-specific and depends on delivery location.

The four milk class prices are then calculated in the following way:

- Class 1 (milk and milk beverages): Average of Class III Skim and Class IV Skim Prices Pricing Factor + Advanced Butterfat Pricing Factor + Class 1 Differential
- Class 2 (cottage cheese, yogurt, etc.): (Class 2 Skim price x 0.965) + (Class 2 Butterfat price x 3.5)
- Class 3 (hard cheeses): (Class 3 Skim price x 0.965) + (Butterfat price x 3.5)
- Class 4 (butter and dry products): (Class 4 Skim price x 0.965) + (Butterfat price x 3.5)

Processors may pay different prices for milk depending the class, but FMMO pricing includes the pooling concept. Pooling results in all dairy farmers being paid the same base price for their milk regardless of where it is sold (in the FMMO). This allows even distribution of money from milk sales to farmers and helps avoid destructive competition between farms.

Part 3 will look at how the PA Milk Marketing Board uses FMMO class pricing to establish prices in Pennsylvania.