

CIAB News

Information from the Cherry Industry Administrative Board

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Mother Nature is Far Kinder in 2013

THE RESURGENCE OF CHERRIES IN 2013

Contrary to last year, Mother Nature has been much kinder to the tart cherry industry in 2013. Winter held on longer than usual and Spring progressed rather slowly. All of this set up conditions for a much needed decent, if not good, crop of tart cherries for 2013.

Growers and handlers in most of the mid-West suggested a good crop potential. In MI the Northwest and Southwest districts indicated that they had good blooms, good pollination conditions and a good fruit set. The same held true for NY and WI.

Unfortunately, WC MI did suffer some freeze damage in mid-May just as the cherries were in bloom. The temperatures dipped quite low, and Mother Nature took some of the cherries from the crop. Nonetheless, estimates were for better than an average crop.

UT and WA had quite good harvests in 2012, but it is expected that they will have average to smaller crops in 2013. WA did experience some colder weather and might be a bit lower than average in 2013.

CROP ESTIMATES FOR 2013 - A GOOD CROP

The crop for 2013 is expected to be larger than average for the United States. This is a good thing since the industry's inventories are quite low following 2012. This will provide handlers the opportunity to refill their inventories while recapturing sales opportunities.

Crop estimates for 2013 were presented at the MFFPA Guesstimate and at the CIAB meeting the following day. The results of those estimates are posted in the table below.

While the NASS, USDA usually prepares and presents its estimate of production for the cherry crop during the CIAB's June meeting, it did not do so this season. Due to the effects of sequestration at the Federal level, the NASS did not to make a crop estimate for cherries or for many other agricultural commodities. As of this moment, the NASS will also discontinue publication of various reports and surveys including the Non-citrus Fruit, Nut and Vegetable Report that it has published for so many years.

The estimates of production from the Guesstimate and the CIAB were the same. The estimates were:

Crop Estimates and 3 Yr. Average Production

| District | MFFPA | CIAB | Average | 3 Yr. Avg. '10-'12 |
|---------------------|--------------|--------------|--------------|-----------------------|
| NW MI | 125.0 | 125.0 | 125.0 | 53.4 |
| WC MI | 60.0 | 60.0 | 60.0 | 37.7 |
| SW MI | 23.5 | 23.5 | 23.5 | 10.0 |
| NY | 9.0 | 9.0 | 9.0 | 5.1 |
| OR | 2.0 | 2.0 | 2.0 | 1.8 |
| PA | 2.0 | 2.0 | 2.0 | 2.8 |
| UT | 25.0 | 25.0 | 25.0 | 32.5 |
| WA | 20.0 | 20.0 | 20.0 | 20.4 |
| WI | 9.3 | 9.3 | 9.3 | 4.5 |
| Total Crop | 275.8 | 275.8 | 275.8 | 168.2 |
| Unrestricted | 22.3 | 22.3 | 22.3 | 14.2 |
| Restricted | 253.5 | 253.5 | 253.5 | 154.0 |

It must be noted that NY and WI, like OR and PA, are unrestricted districts since they have fallen below the 6 million pound threshold for being restricted. NY and WI's three year averages are 5.1 and 4.5 million pounds respectively. These districts will become restricted again when their averages exceed 6 million pounds of production.

CIAB ASKED THE USDA HOW TO HANDLE CROP YEAR 2012/13 UNDER THE ORDER

The crop failure of 2012 presented some concerns that the industry had not faced before. We did have the crop failure of 2002 before, but that crop loss did not alter which districts were subject to restriction.

2012, on the other hand, did have significant impact on what districts were restricted. If the three (3) and five (5) year production averages for a district were deemed to include 2012, then NW and WI would not be restricted because their production was less than 6 million pounds on average. On the other hand, if 2012 were to be considered an anomaly and an outlier and, therefore, not included in the calculation of the average production levels, NY and WI would have been restricted districts.

Members of the Executive Committee met with representatives of the USDA to discuss this situation, to state the case for each side of the matter and to get resolution of the question prior to the June meeting. The bases of the positions for the two sides were legal and equitable. The legal argument was that the order is written to account for crop variability and crop failures, the threshold limit is six (6) million pounds and the terms of the order should apply as written.

The counter argument was based in equity. It was that all producers and processors in the mid-West were hurt in the same fashion in 2012, the producers in all of the districts harmed by 2012 should be treated similarly in 2013 and that the states of NY and WI should not receive a benefit, i.e. not being restricted, that producers and handlers in MI do not receive. The recommended solution given this point of view was to not consider crop year 2012 as pertinent to the order and to not use it in calculating the three and five year averages.

The USDA made the decision that there was no underlying authority in the order or the Act to allow for the equitable argument to be adopted. They ruled, therefore, that crop year 2012 would be included for all purposes under the order and, specifically, for calculating the three and five year averages.

The outcome of this decision, then, is that NY and WI are not restricted districts under the order. NY's three year production average is 5.1 million pounds and WI's three year production average is 4.5 million pounds. These districts will be restricted again only after their three year production average exceeds 6 million pounds.

INDUSTRY INVENTORIES VERY LOW; CARRY-IN AT AN ALL TIME LOW

The amount of fruit carried forward from crop year 2012 into crop year 2013 is at an all-time low. This is the outcome of the very small crop and the ongoing marketing efforts of the industry.

The products held by handlers at the conclusion of May 2013 were:

| | Millions | Percen |
|--------------|------------|--------------|
| Frozen | | |
| 5+1 (30) | 7.6 | 43.7% |
| Drying Stock | 0.9 | 4.9% |
| IQF (40) | 1.0 | 5.7% |
| Other | <u>0.1</u> | <u>0.3%</u> |
| ST: Frozen | 9.4 | 54.7% |
| Waterpack | 0.2 | 1.1% |
| Piefill | 0.7 | 3.9% |
| Puree | 0.3 | 2.0% |
| Juice | 2.1 | 12.2% |
| Dried | 1.7 | 10.1% |
| Other | 2.8 | <u>16.1%</u> |
| ST: | 7.8 | 45.3% |
| Grand Total: | 17.3 | |

THE OPTIMUM SUPPLY FORMULA AND CALCULATION OF RESTRICTION

The crop for 2013 was estimated to be fairly large by recent measure, but it is certainly not as large as people had earlier thought it might be. Given the estimates presented at the meetings, it was determined

that there is likely to be some restriction this year. However, given the uncertainty of the estimates that were presented, much will depend upon the actual production for the year.

The process of calculating and the amount of restriction is quite different now than it was before. Please recall that the CIAB made some adjustments to how items are to be handled under the OSF and the industry amended the order with respect to grower diversions, aka "bottom line credits". These were done before crop year 2012, but they did not come into play in 2012 because of the crop failure last year. These changes require that the CIAB look at the restriction process somewhat differently than before.

The basic premise of the OSF remains the same. That is to say, when the current crop exceeds the projected demand in the domestic market, also known as the "free" market, a crop restriction is required. On the other hand, if the supply is less than the demand in the "free" market, no restriction is required. It is how we define the elements in the equation that are a bit different.

Carry-in Inventories in 2013 - All of it is "Free"

The CIAB reviews various items when making the OSF analysis. Carry-over is one factor and is an important part of the OSF. It is added to the estimated production for the year to define "supply" for the calculation.

Given the crop disaster of 2012, all production was "free". Also, all inventories carried into 2012 were released to the handlers as "free" tonnage. Therefore, all inventories in handlers' possession carried from 2012 to 2013 are "free". The 17.3 million pounds of carry-in is "free".

Optimum Supply Formula

The underlying idea of the Optimum Supply Formula (OSF) is to properly supply the U.S. domestic market, the "free" market. Production in excess of the "free" market volume is "restricted" and must either be held in reserve inventory or sold into "secondary" markets. Secondary markets include export sales and new market development projects.

To calculate the "free" and "restricted" percentages under the OSF, a number of elements must first be calculated.

Demand - 3 Year Average

To determine the current season's restriction, if any, the supply of cherries is compared to the demand for tart cherries in the "free" market. The average of such sales over the past three seasons is used as "demand" for the OSF.

To determine the 3 year average of sales, the CIAB must first calculate sales for 2012. Recall that since there was no restriction in 2012, all sales in 2012 were "free sales". Unfortunately, given the small crop and

the reduced inventories, total sales for 2012 were not very large.

Sales in 2012/13

Calculating the year's sales is done by comparing inventory levels at the beginning and the end of the crop year. The CIAB formula to calculate gross sales, stated in millions of pounds, is:

| | |
|--------------------------------|------------|
| Inventory Beginning of Year | 56 |
| Pack | 85 |
| - Total Inventory, End of Year | <u>17</u> |
| Total Sales | <u>123</u> |

3 Year Average of Sales and Adjustment

Calculating "demand" requires that the CIAB look at the last three years of "free" sales. Previously this figure had been adjusted by the volume of diversion credit activities. This is still the case, but, with the recent changes to the CIAB's processes, this calculation is somewhat different. Under the revised process, export sales activities are the only thing that is subtracted from the gross sales to calculate "free" sales.

This change in the calculation comes from the procedural changes made by the CIAB in the past few seasons. Such things as USDA sales, market expansion activities and exports previously earned diversion credits for handlers. Since they were "secondary" market sales, they reduced the volume of "free" sales which effectively increase restriction under the OSF.

Now restriction percentages will be reduced under the new calculations. The CIAB's procedures will result in an increase to the "free" sales. This, in turn, will increase the average demand in the "free" market under the OSF. Consequently, restriction in any given year will be lower since the "free" demand is greater.

The average free sales posted in millions of pounds is calculated as follows:

| | Gross | Exports | Free Sales |
|-----------|------------|-----------|------------|
| 2010 | 268 | 17 | 251 |
| 2011 | 264 | 14 | 250 |
| 2012 | <u>123</u> | <u>0</u> | <u>123</u> |
| 3 Yr Avg. | <u>266</u> | <u>16</u> | 208 |

The CIAB was concerned with the industry's ability to recapture sales lost from the 2012 crop failure. "Free" sales in 2010 and 2011 averaged about 250 million pounds. The CIAB concluded that it was important for the marketers to have enough "free" cherries to at least meet the "free" sales seen prior to the crop failure. Therefore, the CIAB adjusted and increased the 3 year average of free sales by 42 million pounds. This increased the demand side of the OSF and reduced the amount of restriction calculated in the OSF. If this adjustment had not been made, the

restriction percent would have been bigger by 16 percentage points.

Preliminary Restriction Percentage Determined

Shown below is the result of the OSF for the 2013 given the crop estimates made at the meeting.

OSF

Crop Year 2013 - 14 Using the CIAB Crop Estimate (1,000,000's of Pounds)

| | | |
|---|--------------------------|--------------|
| Estimated in-orchard diversions | | 0 |
| SUPPLY | | |
| | Restricted | 253.5 |
| + | Unrestricted | <u>22.3</u> |
| | ST, Processed Prod.: | 275.8 |
| + | Carry-in | 17.3 |
| | Orchard Diversions | <u>0.0</u> |
| | ST, Supply: | 293.1 |
| DEMAND | 3-Year Avg. Sales | - 208. |
| | MGF | 21.0 |
| | Adj. to sales | 42.0 |
| | Other factors | |
| | Carry-out | 20.0 |
| | Other | <u>0.0</u> |
| | | <u>291.0</u> |
| SURPLUS / (SHORTFALL) | | 2 |
| RESTRICTED and FREE % and Pounds | | |
| | FREE % | 99% |
| | Free Pounds | 251 |
| | Restricted % | 1% |
| | Restricted Pounds | 2 |

Whether or not to restrict in 2013

Using the crop estimates shared at the meeting, the application of the OSF resulted in a very small restriction percentage. There was much discussion about whether the CIAB should announce a preliminary restriction or suspend operation of the OSF for the season. Ultimately it was decided to accept the preliminary restriction percentage as calculated and to operate under this determination. As is always the case, reconsideration of the restriction decision will be done in September based on actual production.

If the situation in September warrants change of the restriction determination, the CIAB will decide accordingly. By definition, if the crop picks long of the estimate, the restriction percentage increases under the OSF. If the crop does not increase significantly or if the restriction remains minimal as it presently is, the CIAB could recommend that the OSF be suspended for 2013. If the crop pick short of the estimates, there would not be any restriction under the OSF.

The CIAB's decision regarding the OSF preserves harvest time options for growers and handlers. Growers will be able to do in-orchard diversions if they need to do so and earn diversion credits. Similarly, handlers will be able to undertake at-plant diversions during the harvest and earn diversion credits. Had the CIAB

decided not to have restriction in June, these options would not have been available to growers and handlers.

Growers and handlers must realize, however, that harvest time diversion decisions must be made carefully. Keep in mind that diversion credits will be valid only if there is a restriction under the OSF as determined in September. If there is no restriction under the OSF, diversion credits will not be needed by handlers. This outcome will render meaningless any diversion credits issued during harvest. Please make your decisions carefully.

FINAL RESTRICTION TO BE SET IN SEPTEMBER

As everyone knows, the percentages set by the board in June are “preliminary”. The board is required to meet in September to review the actual production figures and to recommend the final percentage regulation to the Secretary.

RECAPTURING SALES IN 2013

It is the position of the CIAB that the industry must do its utmost to return to the sales volumes seen before 2012, and it must do this as quickly as possible. It is important that the industry be well positioned to recover more quickly after 2012 than it was following 2002. This dictates that marketers have enough fruit to sell. Much of the discussion at the meeting and about the OSF was how to support this effort.

Adequate supply and an adjustments to sales

As noted earlier, the board made an adjustment to the calculated 3 year average of “free” sales. This adjustment was to provide industry marketers with an adequate amount of inventory to supply the “free” portion of sales seen in 2010 and 2011.

The free sales in 2010 and 2011 averaged 250 million pounds as calculated under the CIAB’s revised process. However, the average of “free” sales for the years 2010 through 2012 were only 208. If the OSF had used this volume of sales, it would have under-supplied the industry, and it would have made the recovery for the industry more difficult.

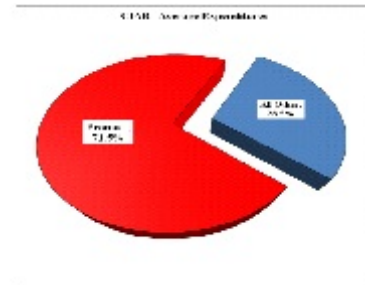
The CIAB decided that it was best to adjust the free sales in the OSF by enough pounds to get back to the 250 million pound average. It is intended that this will make sales more likely and accelerate the return of the tart cherry industry to its previous sales levels.

Promotion activities

Through the promotional campaign of the CIAB and the CMI, the tart cherry industry will move aggressively to rebuild sales opportunities. The promotion agency, Weber Shandwick, kept the program going through 2012. It has prepared a very strong campaign for 2013 to bring tart cherries to the

forefront of the minds of consumers and food manufacturers this Summer.

At the June meeting Mr. Ray Rowley, Chairman, Promotion Task Force, shared some facts about the CIAB’s promotional activities through the years. The CIAB’s contributions to the promotion program have averaged \$1.15 million per year. In fact, on average the promotional expenditures represent 71.5% of the CIAB’s expenses.



The CIAB’s total contributions to the promotional effort exceed \$6.9 million since the start of the program. These funds have combined with the funds from the CMI to make the industry’s promotion program much stronger allow it to have a broad reach to consumers and to business-to-business clients.

BOTTOM LINE CREDITS

Please recall that the industry recently approved the amendment for Bottom Line In-orchard Diversion Credits and that the CIAB made other changes to the operation of the OSF. These changes were done to make the OSF operate more effectively, to lessen the burden of restriction and to make compliance with restriction easier.

WEEKLY RAW PRODUCT REPORTS DUE

The Weekly Raw Product Report (Form 1) is due from processors by the close of business each Monday during harvest. The information is tabulated and distributed to the industry via the website and a postcard mailing.

CALENDAR OF EVENTS - JULY TO SEPTEMBER

- July 10 Form #3 Sales and Inventory Report (for the period ending June 30)
- July 1, 8, 15, 22, 29 - Form #1 Weekly Raw Product
- Aug. 5, 12, 19, 26 - Form #1 Weekly Raw Product
- Sept 12 CIAB meeting to set Final Restricted Percentage, if any
- Sept 17 Cherries Acquired from Producers (Form 2) due to CIAB