U.S. dairy markets and policy update

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Dairy Policy Update: Margin Protection Program (MPP)

On December 5, 2014 the nation's dairy farmers will vote in a referendum on the new Farm Bill dairy safety net program. Passed after much debate and made operational on August 28, 2014, USDA Secretary Vilsack officially announced the start of the new Margin Protection Program (MPP). For the first time in the history of U.S. dairy policy, dairy farmers will have a program that allows them to take a stake in the own national safety net policy. For the first time they are given the opportunity to individually select a level of financial support and to pay a modest amount for their selection. Make no mistake – this is a watershed event and those in leadership and policy positions, and in Washington D.C., will be watching very carefully. Will dairy producers sign on to this new program in sufficient numbers to call this program a success? In case you missed it, here are a few of the key details defining the Margin Protection Program.

Item 1: If you elect to participate you will be required to establish a production history (PH) based on the highest annual production from the calendar years 2011, 2012 or 2013. Once established, your production history will be increased each year by the U.S. average production growth. There is no penalty for increasing production over this level other than the stipulation that extra production will not be eligible for the coverage under the MPP.

Item 2: Selecting coverage above the lowest level of $4 will require you to pay a premium. Premiums follow a two tier schedule. For a production base at 4 million pounds or less there is one schedule and for those farms with a production history over 4 million pounds there is a second more expensive schedule for production over 4 million pounds.

Item 3: Producers whose annual production is at or below 4 million pounds the cost of coverage all the way up to $6.50 remains very reasonable, only becoming more expensive at the $7 to $8 levels. For a producer whose annual production base is above 4 million pounds, the cost is still modest up to the $5 level, but then increases rather significantly above that point.

Item 4: You will not be allowed to simultaneously use Livestock Gross Margin Insurance and this MPP program. There are rules in place that spell out very clearly how MPP and LGM-dairy will coexist. You can continue to use all other tools, such as futures and options and forward pricing through your cooperative to provide price risk management.

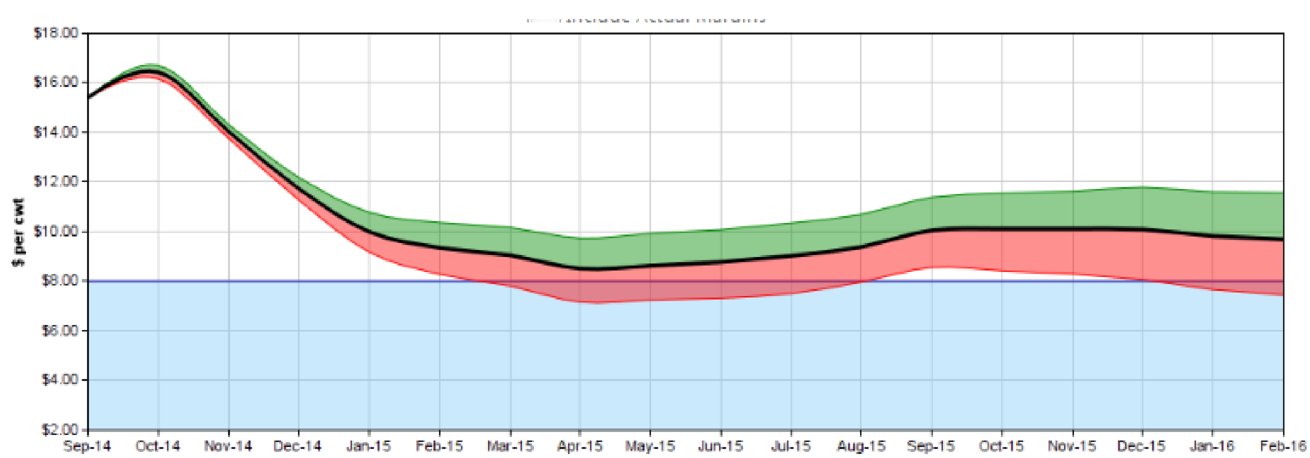
Item 5: To participate you must register with your local USDA Farm Services Agency and complete forms CCC-781 to establish eligibility and production history and also form CCC-782 make program selections for 2014 and 2015. You must complete and submit these signed forms at your FSA County Office no later than end of business November 28, 2014.

Item 6: At the time of registration you will be able to elect a coverage percentage (25% to 90%, 5% increments) and a coverage level ($4 to $8, 50 cent increments). During this initial period, you will be able to make this selection for the remainder of 2014 and all of 2015. A producer does not have to make this decision now but can wait until the following registration period. However, once the decision is made to register and participate in the program, you are obligated to pay the $100 administrative fee each year through 2018. Election of coverage percentage and coverage level are made each year and can be changed during the enrollment period for each year. After November 28, 2014 the enrollment period will occur from July through September for calendar years 2016, 2017 and 2018.

National U.S. Dairy Margin Update

At the time of this writing the concern looking forward is the falling U.S. cheese, butter and skim milk powder prices and the likely impact on the dairy farm financial viability in the coming year. At the end of 2014 U.S. dairy commodity prices are making a significant realignment with lower world prices and it is natural to assume that this realignment will result in dramatically lower IOFC margins for 2015. To pull the U.S. All Milk Price low enough to trigger significant MPP payments, my analysis suggests that Class 3 and Class 4 prices would have to fall by at least $1.50 per cwt. over what the futures market is currently forecasting for 2015. This would require U.S. dairy commodity prices falling below world prices quite early in 2015.

A look at the current MPP margin forecast based on the futures market prices as of November 2014 shows the margin to stay above $9.50 / cwt. through the next 15 months.



The colored bands show the middle 50% probability interval for forecast margins. There is a 25% chance that the margin could be above the green band and a 25% chance that the margin could be below the red band. The graph data and probabilities are calculated from futures market data available on 11/21/2014.

If you would like to read or hear more about the MPP program, link into the Dairy Markets and Policy website (http://dairymarkets.org/MPP/) where you will find a wide assortment of support information on this new program.