

Risk Management Tools

Earl D. Biggers

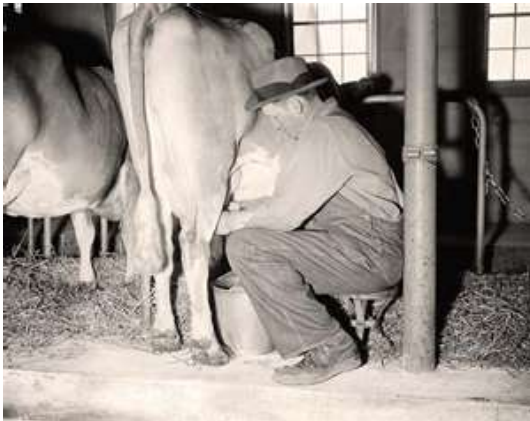
Manager, DFA Risk Management

One way to handle risk – just sit it out!



Why is milk marketing so complicated?

- In times past, the dairyman received whatever the local creamery was paying



- Virtually every aspect of farming has changed



Sample milk check from a multiple component Federal Order, "northern" Missouri

Pay Period Totals:	WEIGHT	1,603,200	GROSS		265,794.04	DEDUCTIONS				
TANK WEIGHTS			COMPONENTS		QUALITY TEST RESULTS					
01 thru 30			B.F.	PROT	OTS	SOMATIC CELL	BACTERIA	FRZPT	INHIBITOR	SED TEMP
TOTAL	1,603,200	AVG	3.68	3.07	5.76	322,000				

*****PRICING INFORMATION*****

BUTTERFAI PAYMENT	3.68	BF AVG	59,001.72	1.6964	100,090.52
PROTEIN PAYMENT	3.07	PROT AVG	49,183.22	2.7055	133,065.20
OTHER SOLIDS PAYMENT	5.76	OS AVG	92,283.17	0.1020	9,412.88
PROD PRICE DIFF			1,603,200	0.0400	641.28
SOMCELL ADJ	322,000	SCC RATE .00280	1,603,200	0.0800	1,282.56
QUALITY			1,603,200	0.1000	1,603.20
VOLUME			1,603,200	1.2000	19,238.40

GRADE A PAY PRICE ***** \$ 16.55028

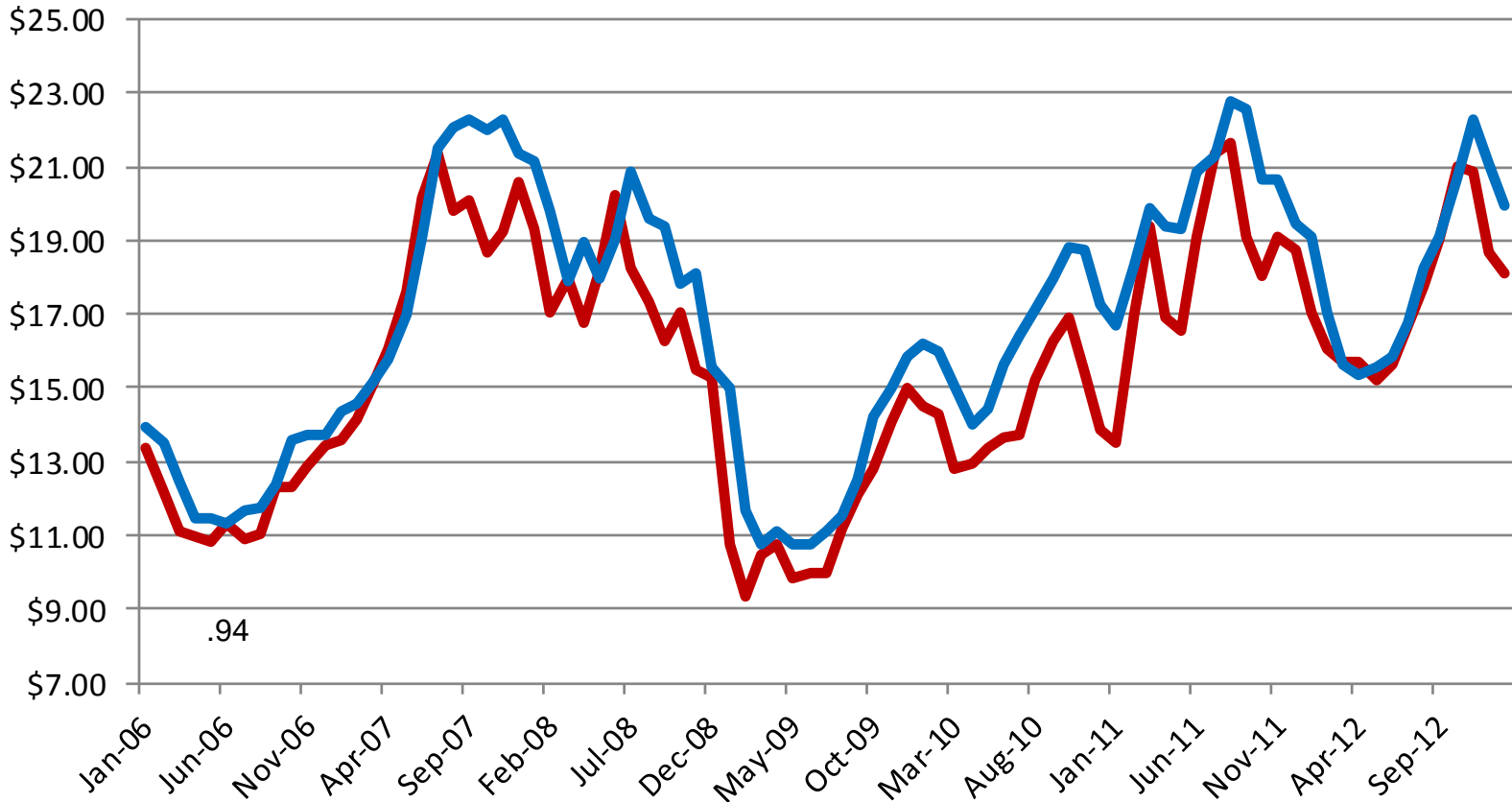
-----FORWARD CONTRACTING PRICING INFORMATION-----

	WEIGHT	MIN PRICE	PREMIUM	CONTRACT PRICE	ANNOUNCED PRICE	ADJ	AMOUNT
FIXED CLASS III	200,000			\$ 12.50	\$ 12.29	\$ 0.21	\$ 420.00
FIXED CLASS III	200,000			\$ 12.00	\$ 12.29	\$ (0.29)	\$ (580.00)
MINIMUM CLASS III	200,000	\$ 13.00	\$ 0.40	\$ 12.60	\$ 12.29	\$ 0.31	\$ 620.00
FORWARD CONTRACT SUBTOTAL							\$ 460.00
PAY PRICE ADJUSTED BY FORWARD CONTRACT PRICING *****							\$ 16.57897



S Missouri Mailbox Price Compared to Class III

— Class III — S Missouri Mailbox



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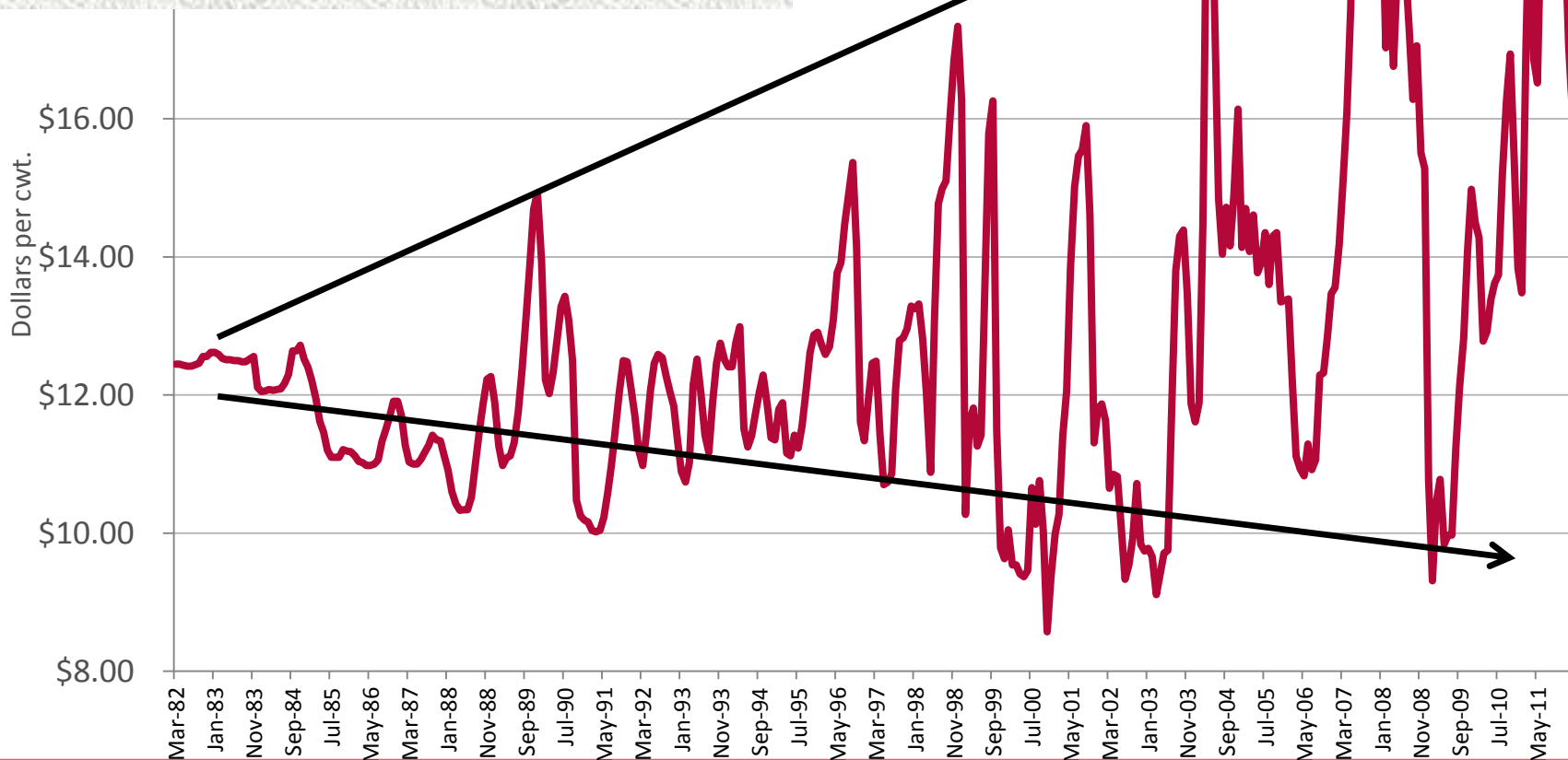
Volatility!

A 30 Year Class III History

\$20.00

Why volatility may be here to stay

BY Jurrien Timmer, Director of Global Macro and Co-Manager of Fidelity® Global Strategies Fund, Fidelity Viewpoints — 10/24/11



DFA Risk Management

. . . So Why Forward Contract?

1. To decrease price volatility
2. To aid in cash flow, to make your debt obligations
3. To create a price floor (Min Price Contract)
4. To shift price risk to somebody else

IT'S NOT TO BEAT THE MARKET!



What is “Beating the Market”?

KEY POINT!



- Forward contracting is **NOT** being “smart enough” to consistently out guess the market and thereby get a higher price –
- It’s about transferring risk and/or decreasing volatility of prices.



This is NOT forward contracting!



Wise Guy



**Placing Order With
Earl in KC**



Hit the Jackpot



“Basis”

**an important
concept even if you
never contract**



Your Farm Gross Milk Price =

Announced Class III

**Class III
BASIS**



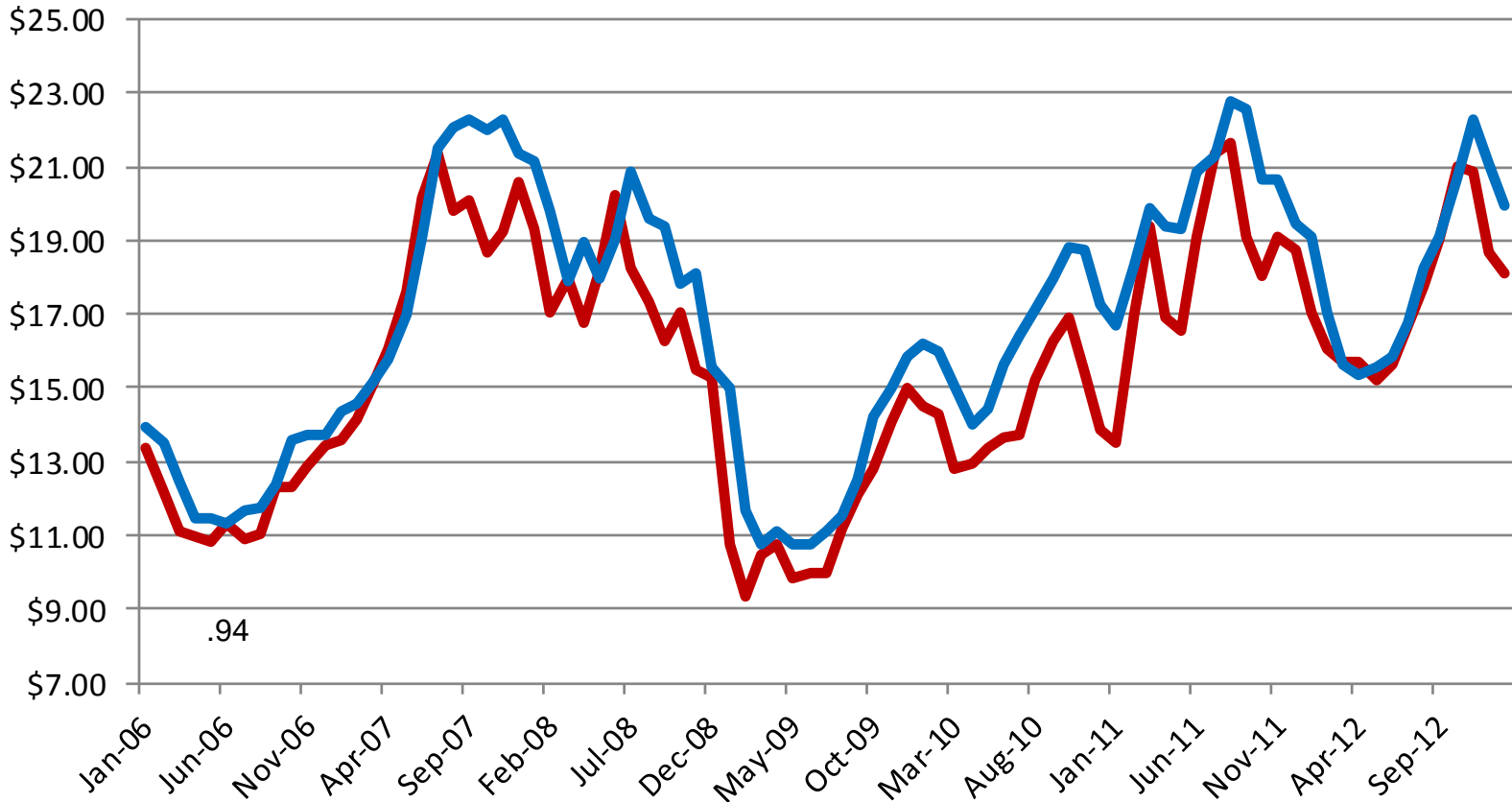
- +/- your actual test %
- +/- bacteria quality (SPC, PI, LPC, etc)
- +/- your SCC
- +/- any other premium (rBST, vol, etc)
- +/- the value brought by CI I, CI II, & CI IV sales

= Your farm's specific, gross pay price



S Missouri Mailbox Price Compared to Class III

— Class III — S Missouri Mailbox



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Contracting Tools



Two Main Distinctions:



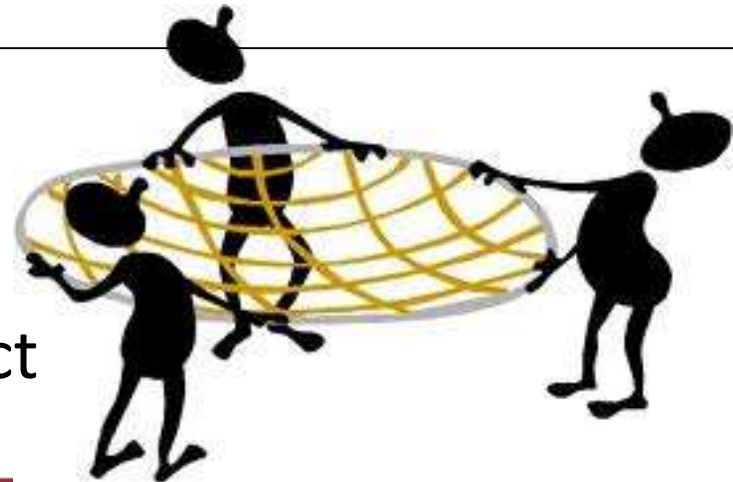
There are forward contracts that are **fixed**:

- Fixed Class III
- Fixed Class IV
- Target Blend

Other forward contracts act like a

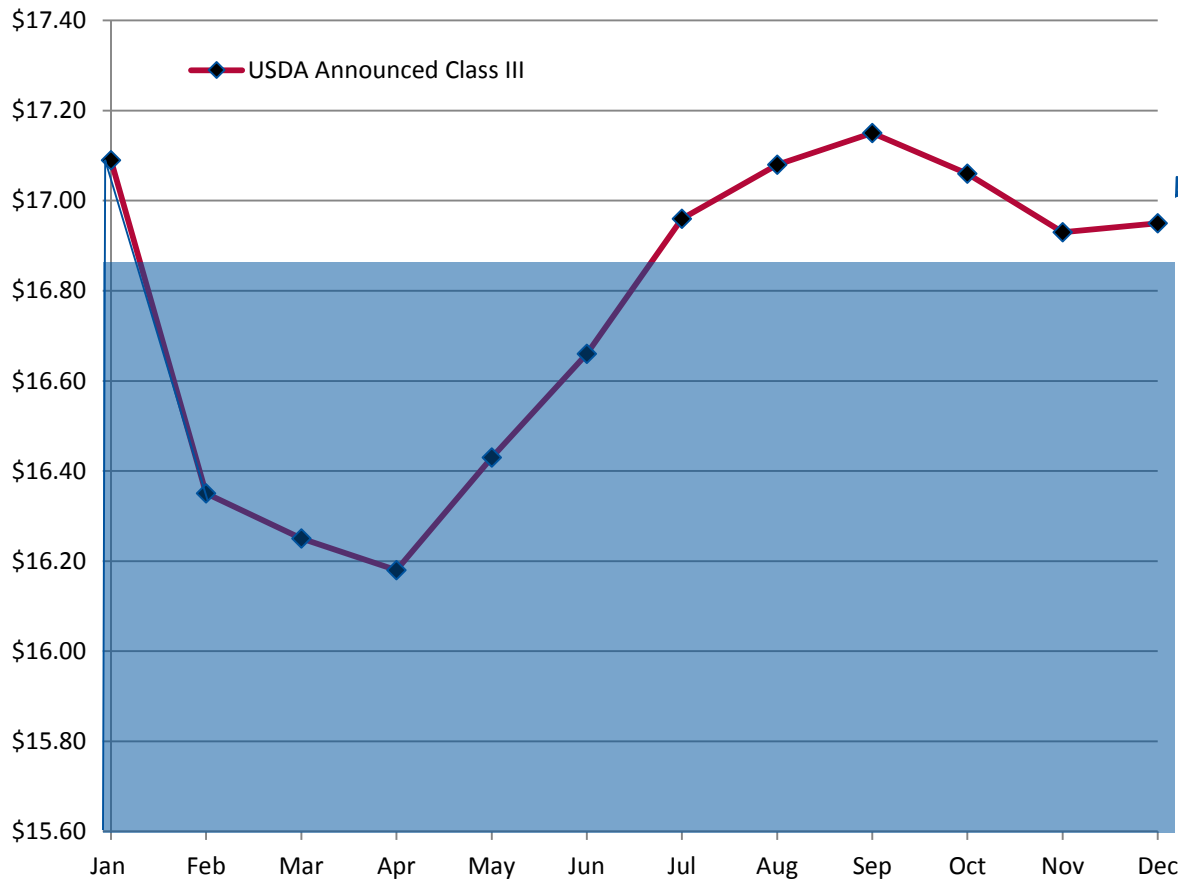
safety net:

- Min Price (buying a “put”)
- Min/Max Price forward contract
- Upside Rider (buying a “call”)



Fixed Price, Class III* Example

12 Month, Average Price, Fixed Forward Contract



Example IF
Class III then
Averaged
\$16.76

\$16.85 Contracted
For 2014 on
11/21/2013

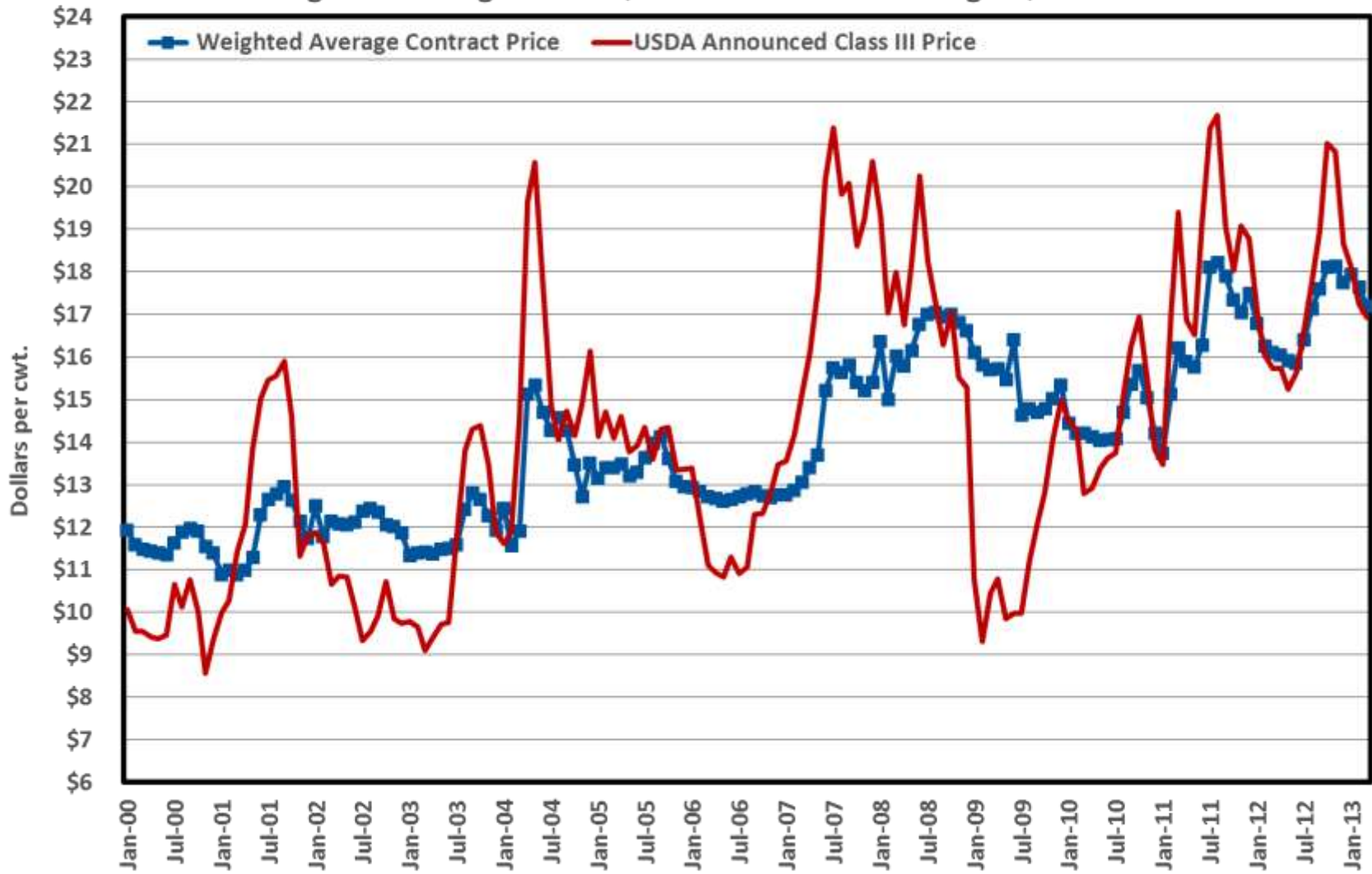
* Class IV works
the same way



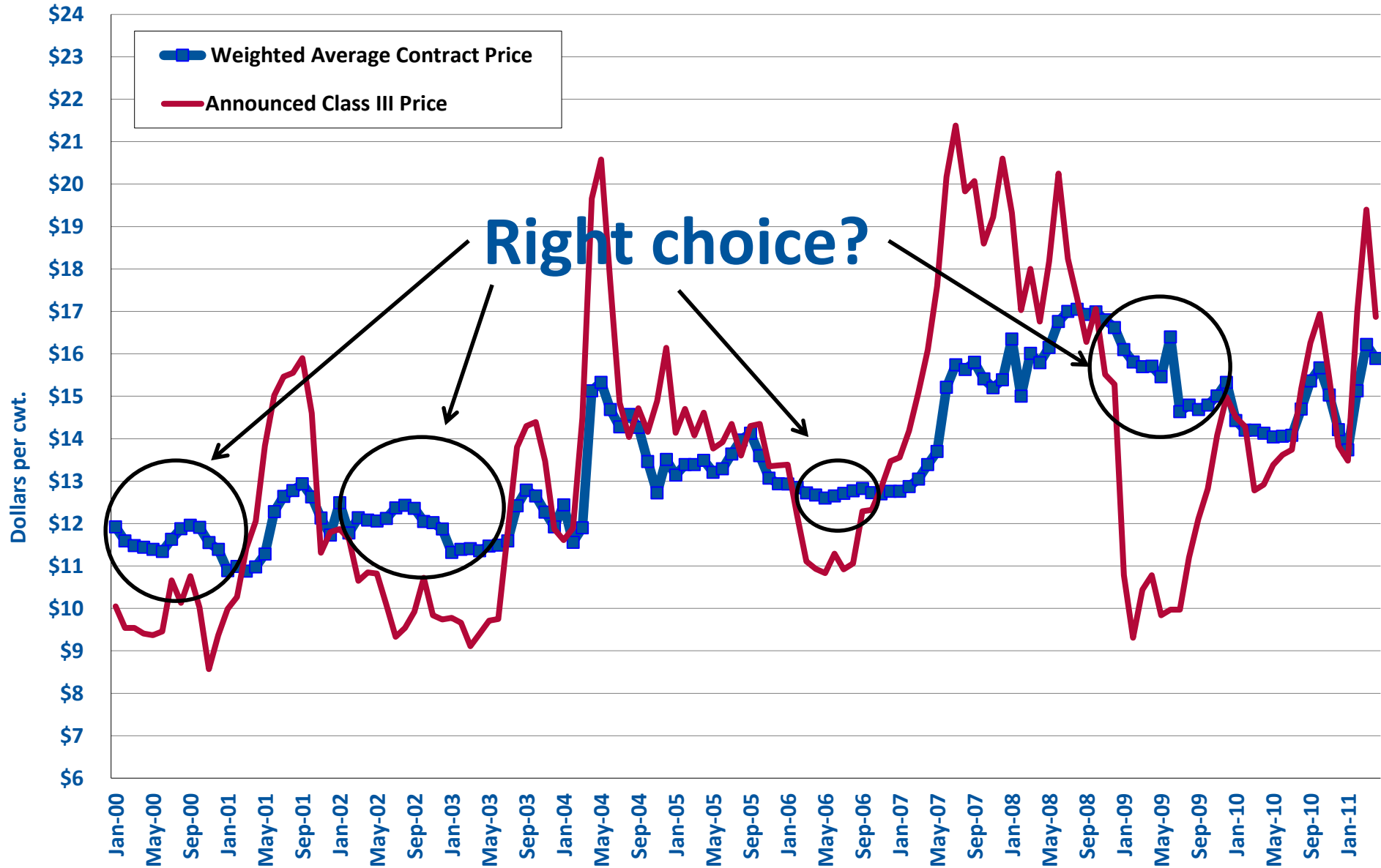
How fixed contracts work over time



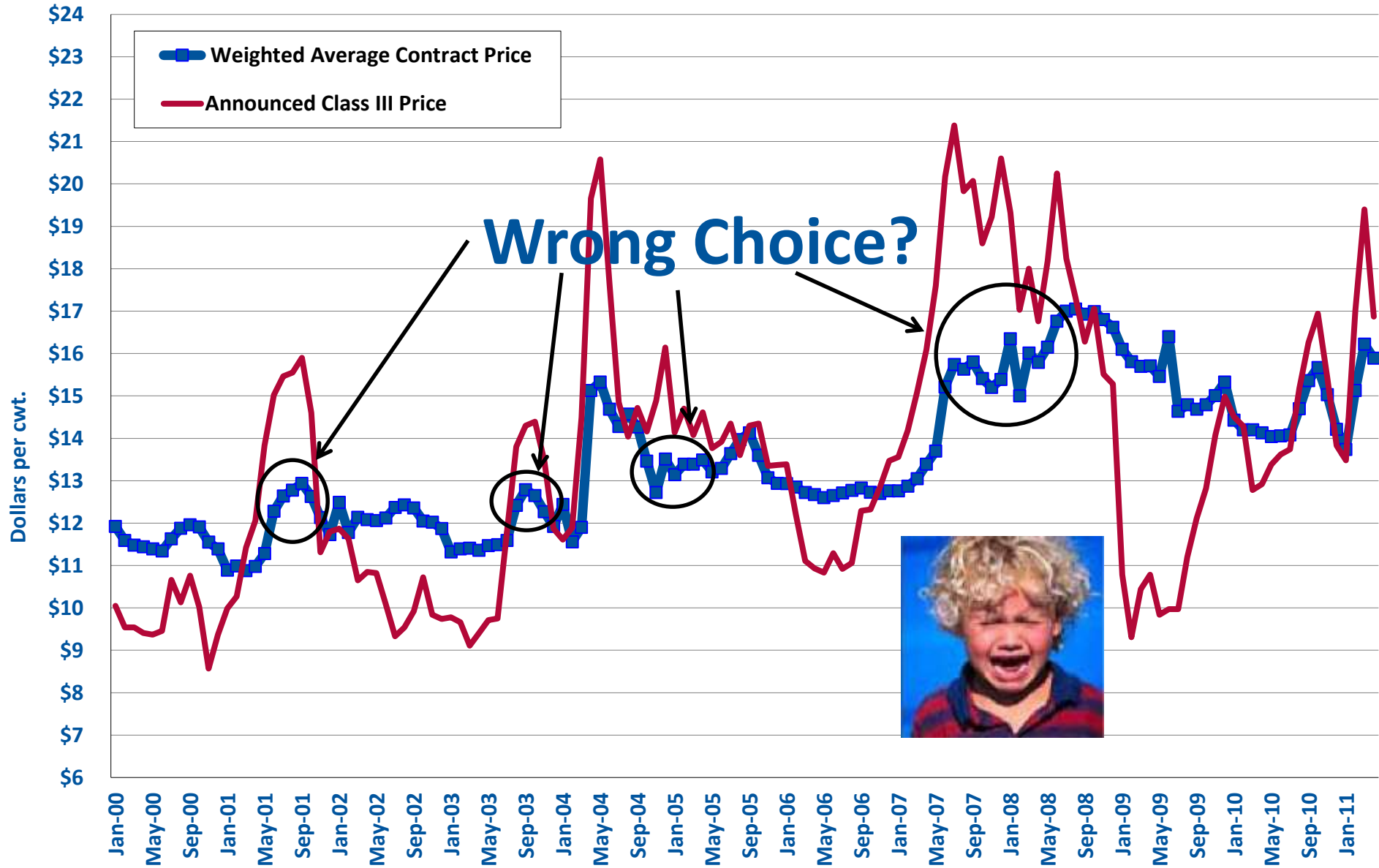
DFA Risk Management Weighted Average Contract Prices
vs. USDA Announced Class III Prices thru Feb 2013
Weighted Average Value - \$14.04 vs. Class III Average - \$14.14



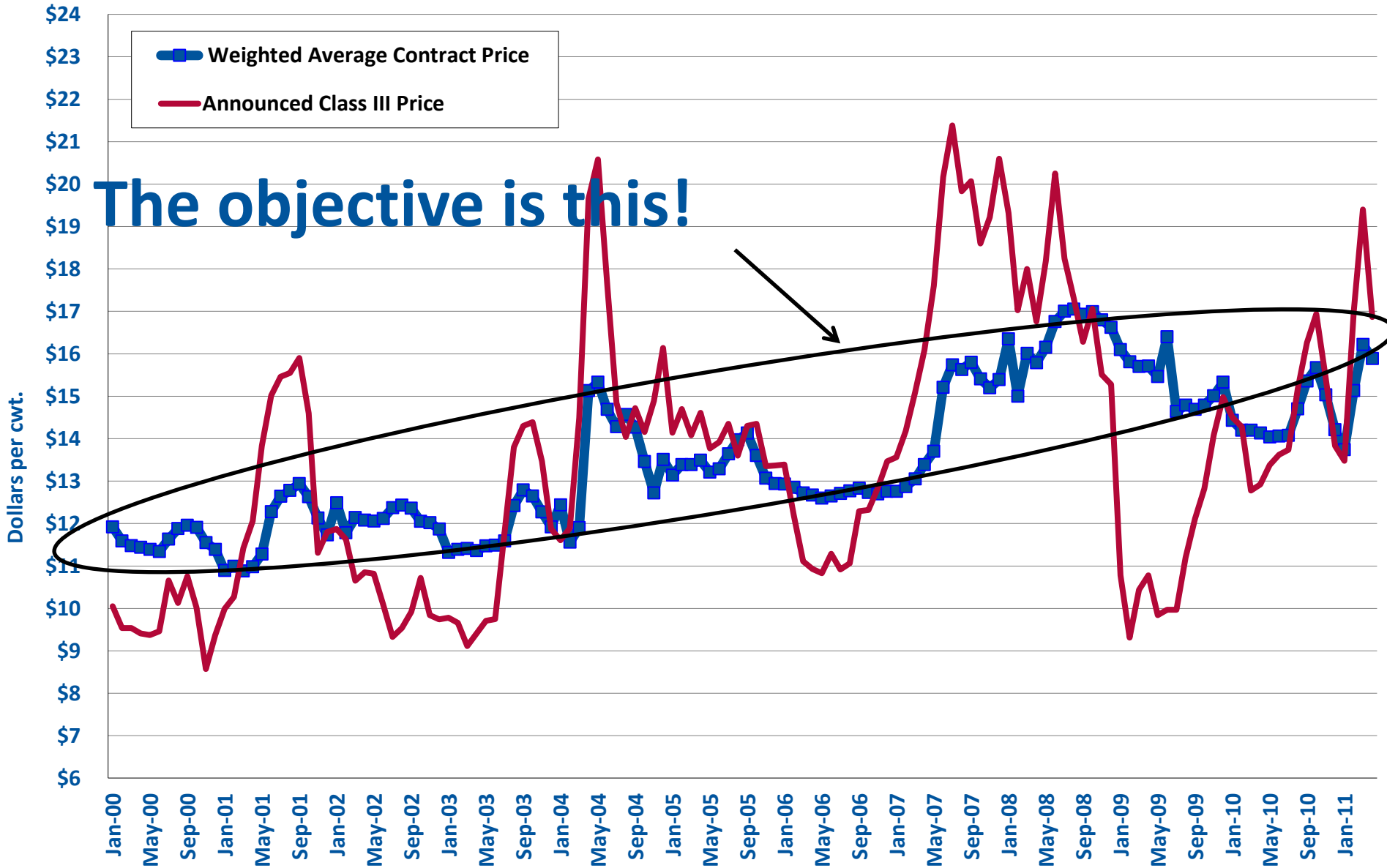
How do you measure success?



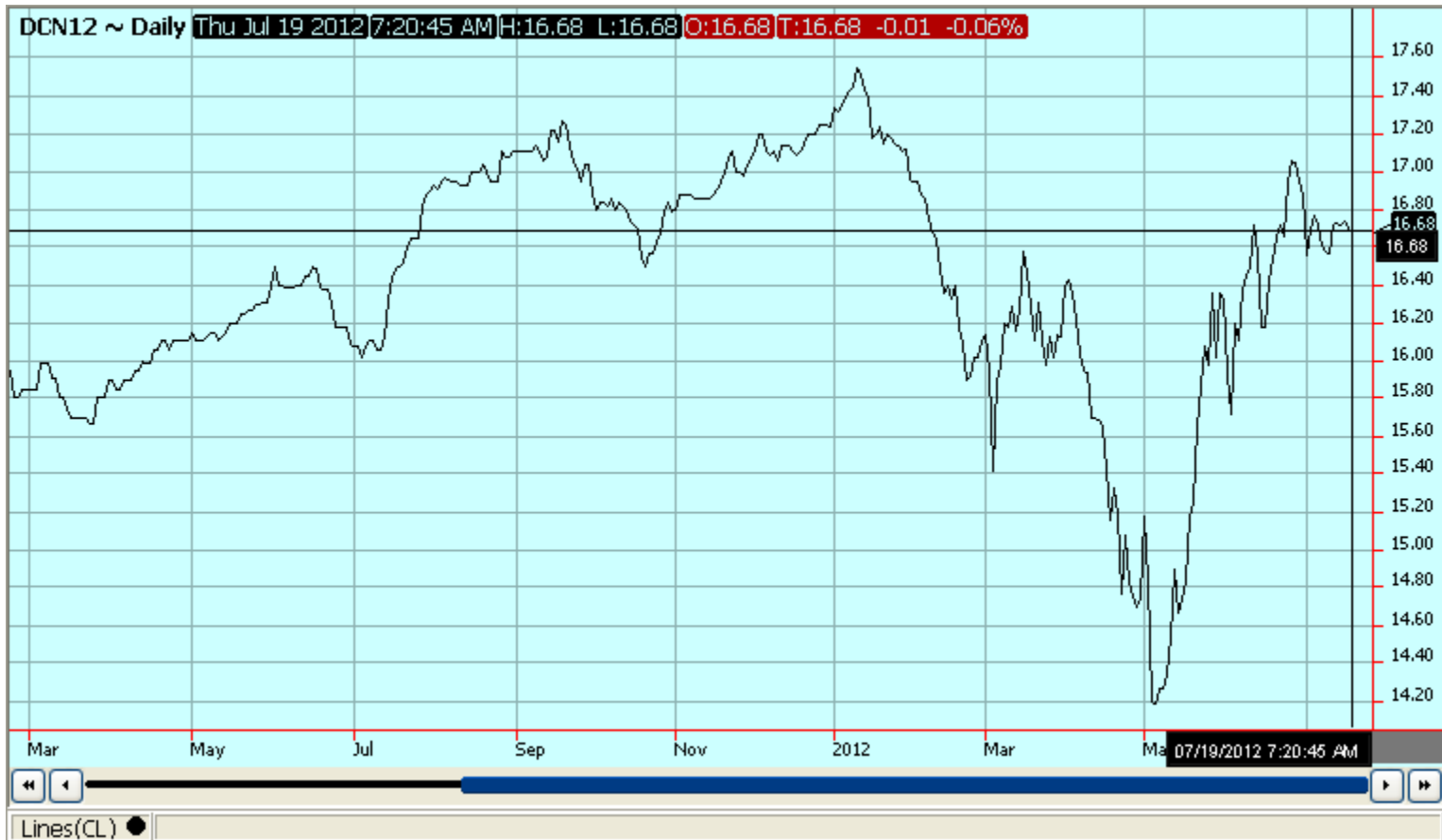
How do you measure success?



How do you measure success?



16 Month Price History for July 2012



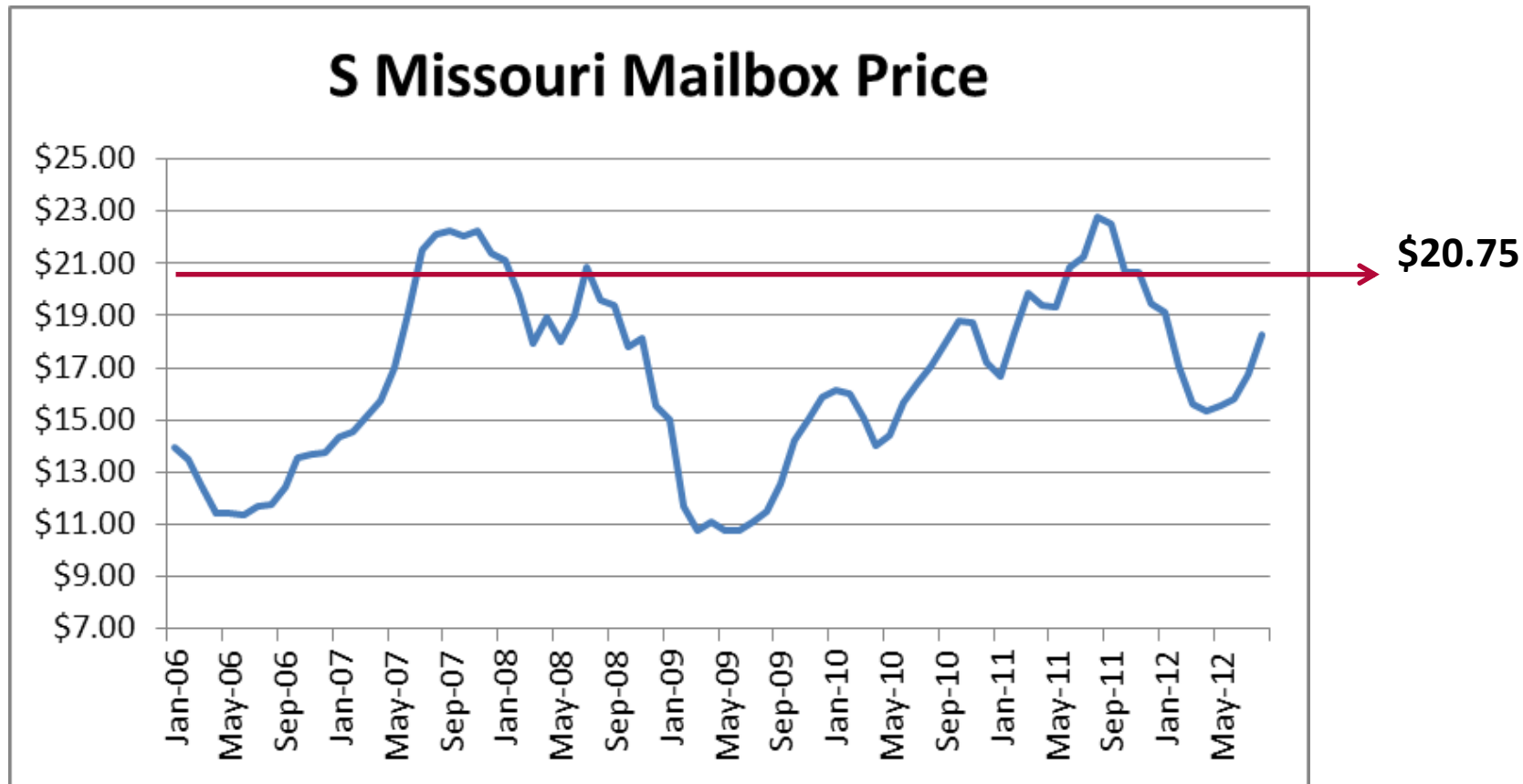
Target Blend, Another Fixed Price Example

- Uses a combination of Class III and Class IV
- Creates opportunities to contract prices that are closer to actual farm price than Class III alone
- Reduces price swings traditionally associated with major changes in “Blend Basis”
- Protects from significant declines in both Class III and Class IV
- **6 month minimum**



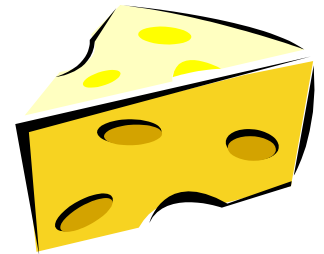
Fixed Target Blend Price

Target Blend for All 2014 (as of 11/21/2013): \$20.75 compared to the historic S Missouri mailbox price



Target Blend Contract Availability

- Class IV futures volume is limited
- May be opportunities to contract Class IV with processor customers
 - processor offers now include calculation for Target Blends
- **Ability to write Blend Contract will depend on availability of Class IV contract interest**
- DFA Risk Management can also do just a mix of Class III & IV too



Two Main Distinctions:



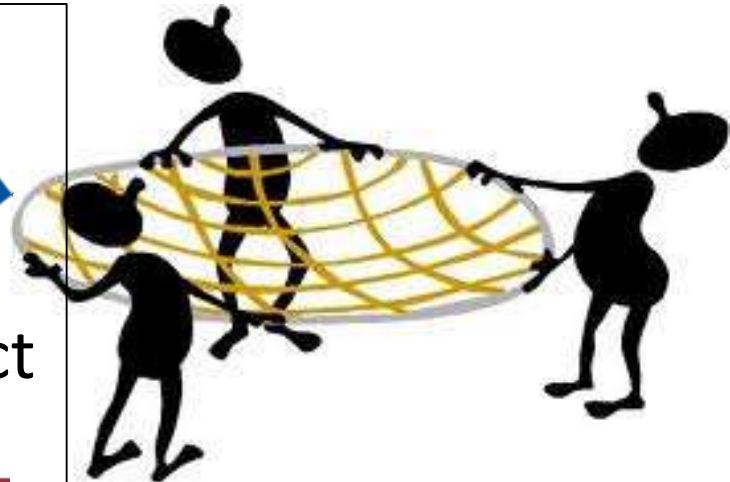
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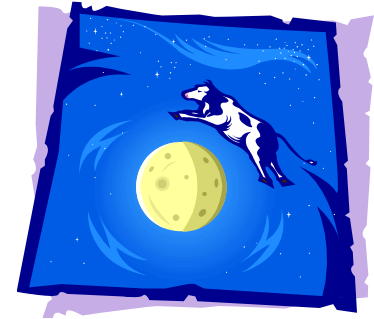
Other forward contracts act like a

safety net:

- Min Price (buying a “put”)
- Min/Max Price forward contract
- Upside Rider (buying a “call”)



Minimum Price Contract (buying a put)



- Protects against a declining market
- Sets a floor for Class III (or IV) price
 - You set the floor price (.25 increments)
- Market prices higher than floor are paid
- Monthly premium per cwt contracted
 - Premium cost fluctuates daily on the CME
 - **Through the co-op, no “up front” charges**



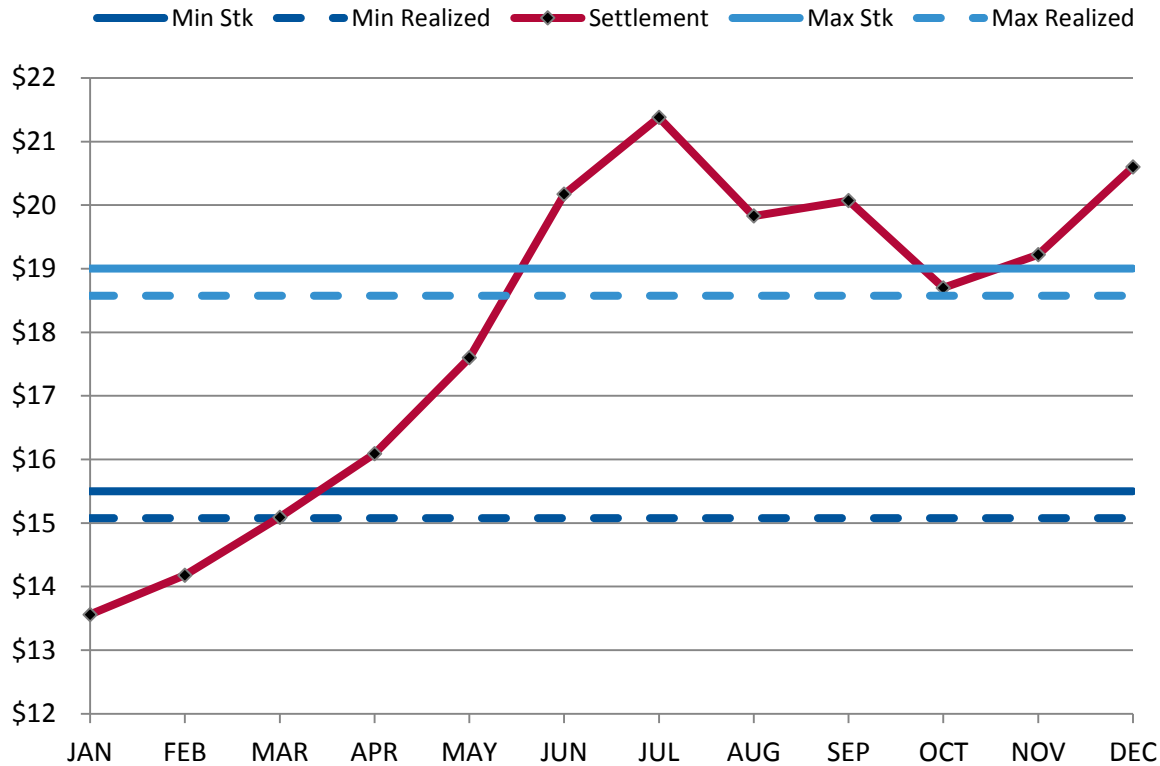
Min/Max Forward Contract



- **Set a floor and ceiling for Class III price**
 - The “ceiling” helps lower the cost
- **Creates a price window (collar, fence)**
- **Can be a lower cost alternative to Minimum Contract**
- **You “give up” any prices above the Maximum**
- **Can consider using an Upside Rider with this program**



Safety Net Example: Min/Max Forward Contract



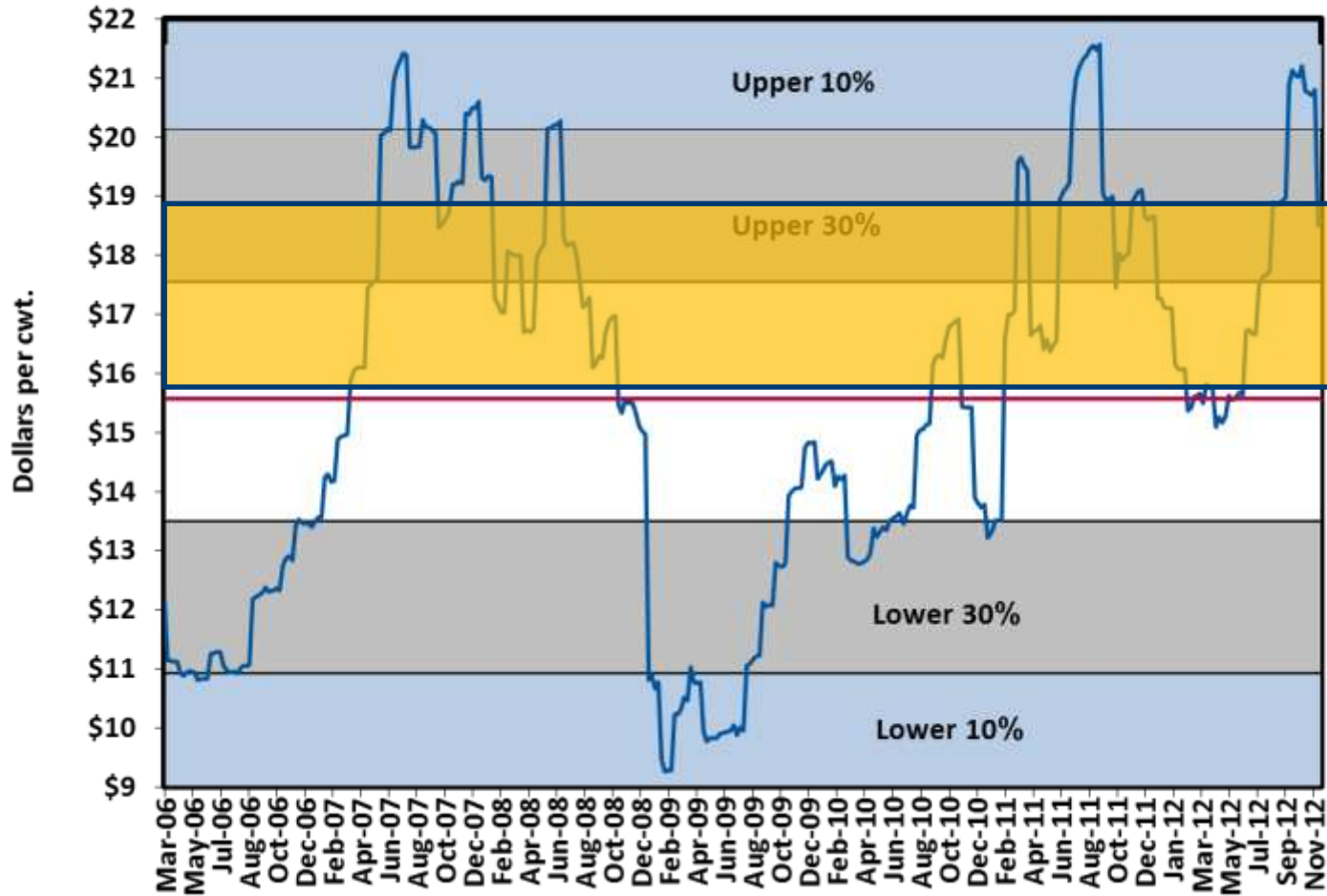
Example:
\$15.50/\$19 Min/Max
Costing \$.15 for CY 2014



Safety Net Example: Min/Max Forward Contract

CME Class III Milk Futures with Percentiles

— Class III Milk Futures — Average

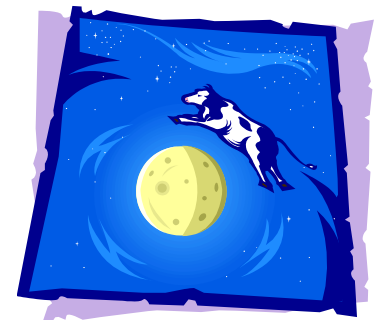


Example:
\$15.50/\$19 Min/Max
Costing \$.15 for
Jan 14 – Dec 14



“Safety valve”: Upside Rider (buying a call)

- **Generally used as an amendment to an existing contract**
 - For example, you have a \$17 Fixed Contract for 2014 and then you could have bought a \$19 Upside Rider (call) for an additional \$.31 (as of 11/21/2013)
 - Can also be used with Min/Max
 - Rising prices increases cost



Other Risk Management Tools . . .



DFA Risk Management Feed Riders

Your Feed Source will Impact your Milk Hedging Strategy

GROWN

- Crop Insurance
- Pre-purchase inputs



or

PURCHASED

- Contract with suppliers
- Hedge with DFA/RM



Milk-Feed Margin Program

- Secure the margin between a Class III milk price and primary feed costs
- **Done as single months only**
- Shown daily in DFA Today and on the MyDFA website
- It's like selling your milk today and buying the feed today



Your Source for Watching Margins



Daily Market Update

Dairy

- The CME cash cheese market experienced activity in the barrels with six loads traded with the price moving 1/2 cent lower. This is the sixth consecutive day that the barrel price has been unchanged or lower.
- CME Group Class III milk futures closed mixed with little fresh news in the market. The volume of barrel cheese brought to the market by sellers added a weaker tone to the Class III milk futures market.
- The lack of direction from the CME cash cheese market has resulted in the 2013 coverage Class III milk futures settling 10 cents lower since the beginning of the year.
- CME wheat futures provided further downward pressure to Class III milk futures, with the majority of months settling lower on the day.

Grains

- USDA officials will release the January Crop Production report at 11 a.m. CST tomorrow versus the previous release time of 7:30 a.m. CST.
- The focal point for today's grain and oilseed complex activity was the adjustment of positions prior to tomorrow's USDA report. The complex closed mixed on the day with little movement in either direction.
- CME corn futures settled slightly higher as the market priced in an expectation of slightly lower revisions to the final 2012 U.S. corn production in tomorrow's report.
- CME soybean and soybean meal futures closed mixed within a relatively narrow range. The market weighed expectations of higher 2012 soybean production estimates with continuously strong international export demand.

Prepared by **DFA** Risk Management

MILC program update

The recent extension of the Farm Bill, signed by President Barack Obama last week, reinstated the Milk Income Loss Contract (MILC) program through August 31, 2013, at a payment rate of 45 percent, covering 2.985 million pounds of milk per year with a feed adjuster of \$7.35 per hundredweight.

The extension provides for retroactive MILC payments for the September 2012–December 2012 timeframe at the above stated rate. While details and sign-up timelines have not been finalized, an announcement regarding the 2012–2013 MILC sign-up period is expected soon. USDA officials have stated they are committed to making the process farmer friendly. To view projections for possible MILC payments, visit www.nmpf.org/milk_pricing/milc_payments.

Dairy cow slaughter declines

Today, U.S. Department of Agriculture (USDA) officials released Cow Slaughter Under Federal Inspection By Region and U.S. Total report. For the week ending December 29, there were 43,100 dairy cows culled. This is 8,400 head (16.3 percent) less compared to the previous year, marking the first time in 34 weeks that cow slaughter has declined from last year. Year to date, 3.1 million dairy cows have been culled, up 177,500 head (8.1 percent) from the same period last year.

For states east of the Mississippi River, culling totaled 21,300 head, down 5,100 (22.3 percent) from the previous year. The states west of the Mississippi River culled 21,800 head for the week ending December 29. This is 2,300 head (9.6 percent) less compared to the same period last year.

Dairy			Dairy			Grains			Other Markets		
Cash Markets			Spot/Barrel Cheese Price			Corn			Energy (weekly contract)		
Commodity	Today	Change	Monthly	Today	Change	Monthly	Today	Change	Commodity	Today	Change
Blocks	\$1,730	↓ 1/2	Jan-13	\$1,760	↓ 1 1/2	Mar-13	\$6.975	↓ 4.5	Crude Oil	\$83.82	↓ \$8.72
Barrels	\$1,680	↓ 8.5	Jan - June 13	\$1,900	↓ 0.15	May-13	\$6.975	↓ 3.75	Heating Oil	\$2,954.3	↓ 1.65
Butter	\$1,447.5	↓ 0.25	Jul-13	\$6.955	↓ 2.25	Jul-13	\$6.955	↓ 2.25	Natural Gas	\$2,193	↓ \$4
Class III Futures			Milk Feed Margin Prices			Soybeans			Dollar & Stock Markets		
Monthly	Today	Change	Monthly	Today	Change	Monthly	Today	Change	Monthly	Today	Change
Jan-13	\$19.07	↓ 1/4	Jan-13	\$5.71	↓ 8	Jan-13	\$14,755	↓ 2.25	Dollar Index	79.877	↓ 0.060
Feb-13	\$17.15	↓ 1/4	Jan - June 13	\$5.82	↓ 2	Mar-13	\$13,707	↓ 5.75	DJIA	13,471	↓ 81
Mar-13	\$17.91	↓ 3/4	Jul - Dec 13	\$6.73	↓ 2	May-13	\$13,210	↓ 3.75	S&P 500	1,472.83	↓ 11.68
Apr-12	\$19.07	↓ 1/4	Dairy Cattle			Soybean Meal			Live & Feeder Cattle		
May-13	\$18.26	↓ 4	Commodity	Today	Change	Monthly	Today	Change	Commodity	Today	Change
Jun-13	\$18.48	↓ 1/2	Cheese	\$1,750	↓ 0.8	Jan-13	\$493.79	↓ \$2.80	LC - Feb-13	\$121.53	↓ \$0.300
Jul - Mar 13	\$17.91	↓ 2	Butter	\$1,530	↓ 0.7	Mar-13	\$493.48	↓ \$4.30	LC - Apr-13	\$136.59	↓ \$0.275
Jan - Jun 13	\$19.09	↓ 1	Dry whey	\$0,627.5	↓ 0.005	May-13	\$493.79	↓ \$2.30	FC - Jan-13	\$168.68	↓ \$0.850
Jan - Dec 13	\$19.26	↓ 1	DFWM	\$1,545	↓ 5	Jul-13	\$296.65	↓ \$2.20	FC - Mar-13	\$152.63	↓ \$0.925

For more DFA Risk Management, call 1-877-424-3343 or visit www.dfariskmanagement.com. If you would like to receive DFA Today, please visit www.dfa.com or stop receiving DFA Today, send your name, membership number and the number of email address to marketing@dafa.com or fax to 510-601-6415.

MILK / FEED MARGIN SETTLEMENTS

CME Group Settlements as of Thursday, January 10, 2013

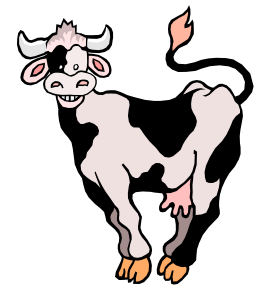
Class III Contract Month	Class III Price (\$ per cwt.)	Corn Month	Corn (\$ per bu.)	Soybean Meal Month	Soybean Meal Price (\$ per ton)	Primary Feed Value (\$ per cwt.)	Non-Primary Feed Margin (\$ per cwt.)
Dec-12	\$17.97	Mar-13	\$7,527.5	Jan-13	\$434,9000	\$ 13.29	\$4.55
Jan-13	\$18.04	Mar-13	\$6,9850	Mar-13	\$419,4000	\$ 12.50	\$5.41
Feb-13	\$18.25	Mar-13	\$6,8900	Mar-13	\$409,2000	\$ 12.28	\$5.94
Mar-13	\$18.31	May-13	\$6,8750	May-13	\$401,6000	\$ 12.18	\$6.00
Apr-13	\$18.29	May-13	\$6,8750	May-13	\$401,6000	\$ 12.18	\$6.04
May-13	\$18.26	Jul-13	\$6,7850	Jul-13	\$397,3000	\$ 12.03	\$6.36
Jun-13	\$18.67	Jul-13	\$6,7850	Jul-13	\$397,3000	\$ 12.03	\$6.42
Jul-13	\$18.65	Sep-13	\$5,9675	Aug-13	\$389,6000	\$ 11.00	\$7.45
Aug-13	\$18.53	Sep-13	\$5,9675	Sep-13	\$377,8000	\$ 10.88	\$7.45
Sep-13	\$18.30	Dec-13	\$5,7450	Oct-13	\$363,7000	\$ 10.47	\$7.63
Oct-13	\$18.21	Dec-13	\$5,7450	Dec-13	\$362,5000	\$ 10.46	\$7.55
Nov-13	\$18.10	Dec-13	\$5,7450	Dec-13	\$362,5000	\$ 10.46	\$7.39
Dec-13	\$18.04	Mar-14	\$5,8450	Jan-14	\$363,1000	\$ 10.58	\$7.21
Jan-14	\$17.90	Mar-14	\$5,8450	Mar-14	\$366,3000	\$ 10.62	\$7.03
Feb-14	\$17.30	Mar-14	\$5,8450	Mar-14	\$366,3000	\$ 10.62	\$6.43
Mar-14	\$17.13	May-14	\$5,9175	May-14	\$367,7000	\$ 10.72	\$6.11
Apr-14	\$18.16	May-14	\$5,9175	May-14	\$367,7000	\$ 10.72	\$5.14
May-14	\$16.07	Jul-14	\$5,9550	Jul-14	\$371,0000	\$ 10.79	\$4.98
Jun-14	\$16.00	Jul-14	\$5,9550	Jul-14	\$371,0000	\$ 10.79	\$4.91
Jul-14	\$15.77	Sep-14	\$5,7400	Aug-14	\$370,4000	\$ 10.54	\$4.93
Aug-14	\$15.77	Sep-14	\$5,7400	Sep-14	\$370,4000	\$ 10.54	\$4.93
Sep-14	\$15.42	Dec-14	\$5,6200	Oct-14	\$370,4000	\$ 10.40	\$4.72
Oct-14	\$15.26	Dec-14	\$5,6200	Dec-14	\$353,6000	\$ 10.22	\$4.74
Nov-14	\$15.18	Dec-14	\$5,6200	Dec-14	\$353,6000	\$ 10.22	\$4.66

Primary Feed Value = (corn price per bu. X 35.71 X .03244) + (soy price X .01050)

Non-Primary Feed Margin = Class III - Primary Feed Value

Prices listed above are based on published CME prices for the date listed and are not actual contract offers. DFA does not make, and expressly disclaims, any express or implied guaranty, representation, or warranty regarding any opinions or statements set forth herein. DFA is not acting as your consultant or advisor, or in a fiduciary capacity, for any purpose, and is not providing advice regarding the value or advisability of trading in commodity interests, including swaps, futures contracts and commodity options or any other activity which would cause DFA or any of its affiliates to be considered a commodity trading advisor under the Commodity Exchange Act. None of the information contained herein should be construed as trading or risk management advice. Before undertaking any trading strategy, you (and your customers or members) should consult your own independent advisors if you are interested in forward contracting with DFA RM, please call 1-877-424-3343 to discuss current offerings.





How do I get started?

- DFA members can call DFA/RM and we will send you a *Master Agreement* (or you can establish a relationship with a broker)
- Return signed *Master Agreement* to DFA/RM
- Once you're in the system, just call DFA/RM to place and order
- Orders can be revised/cancelled as long as they have not been "filled"



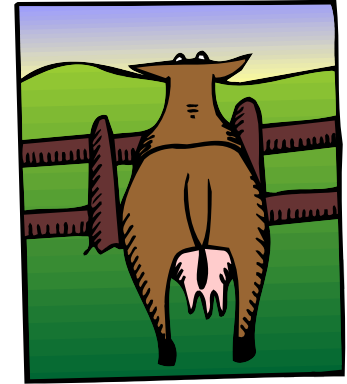
Milk Contracting Details

- **Forward contracts can be for Class III, Class IV, options, and a variety of combinations**
- **Can be for one month or up to 24 months***
- **Can place multiple, single month orders – or - groups of months, done as an average**
- **Some producers have several contracts in any given month, resulting is several different prices**
 - A CME contract is 200,000 pounds
 - DFA/RM Minimum = 20,000 pounds and in 5,000 pound increments

* More distant months may have limited activity



Your Obligation



- Your forward contract is an agreement to deliver a stated volume of milk for the agreed upon month(s) at the agreed upon price plus applicable basis and agreement by your coop to market your milk, provided it meets the required quality and delivery requirements.




Information Sources:

DFA Today

Wednesday, May 25, 2011

Fuel Prices Decrease

According to U.S. Energy Information Administration officials, the average gasoline price throughout the United States decreased



Dairy Commodity Markets & Industry News

CME Daily Cash Prices				
	Today	Previous	Change	Trades
Blocks	\$1.7800	\$1.7400	4.00 ¢	1
Barrels	\$1.7550	\$1.7400	1.50 ¢	0

WEEKLY Pricing Update


Friday, April 27, 2012

Market Headlines

- Spot blocks ended the week 1 cent higher while the cash barrel market declined 3.5 cents.
- Cattle futures recovered late in the week as concerns over the recent case of BSE begin to subside.
- Grains rallied this week supported by the surge in cash prices, coupled with news of strong Chinese export demand.

DFA Risk Management

Weekly Chart Spotlight



Minimum/Maximum Contracts

(monthly per net cost to establish a floor, give up some upside opportunity to reduce cost)

May - December 2012 Class II Min/Max Table					July - December 2012 Class II Min/Max Table						
Maximum	\$14.00	\$14.25	\$14.50	\$14.75	\$15.00	Maximum	\$14.00	\$14.25	\$14.50	\$14.75	\$15.00
\$17.00			(0.10)	(0.20)	(0.30)	\$17.50			(0.10)	(0.20)	(0.30)
\$17.25		(0.10)	(0.20)	(0.30)	(0.40)	\$17.75		(0.10)	(0.20)	(0.30)	(0.40)
\$17.50	(0.10)	(0.10)	(0.20)	(0.30)	(0.40)	\$18.00	(0.10)	(0.10)	(0.20)	(0.30)	(0.40)
\$17.75	(0.14)	(0.10)	(0.20)	(0.30)	(0.40)	\$18.25	(0.14)	(0.21)	(0.31)	(0.38)	(0.48)
\$18.00	(0.17)	(0.25)	(0.32)	(0.40)	(0.50)	\$18.50	(0.18)	(0.25)	(0.34)	(0.47)	(0.55)

Fixed Price Contracts

Months	Class II (\$ per cwt.)	Weekly Change	Class IV (\$ per cwt.)	Weekly Change	Milk-Fed Margin	Weekly Change
May12-Jul12	14.40	↓ (0.40)	13.80	↓ (0.80)	2.87	↓ (0.77)
May12-Dec12	15.21	↓ (0.20)	14.50	↓ (0.71)	4.40	↓ (0.71)
Jul12-Dec12	15.50	↓ (0.34)	14.75	↓ (0.75)	6.97	↓ (0.73)

Minimum Price Contracts

Months	Class II	Class III	Class III	Class III
May12-Jul12	(0.34)	(0.81)	(0.70)	(0.70)
May12-Dec12	(0.34)	(0.48)	(0.70)	(0.70)
Jul12-Dec12	(0.30)	(0.52)	(0.70)	(0.70)

Target Hauls

Months	Central Area	Midwest Area	Northeast Area	Southeast Area	Southwest Area	Colorado State
May12-Jul12	15.02	15.22	15.75	16.07	16.63	15.02
May12-Dec12	15.70	15.94	16.82	17.00	16.36	15.70
Jul12-Dec12	15.78	15.93	16.48	17.37	16.34	15.78

Feed Contracts


Months	Com Rider (\$ per bu.)	Weekly Change	Soymeal (\$ per ton)	Weekly Change	Feed Rider (\$ per cwt.)	Weekly Change
May12-Jul12	6.11	↓ 0.17	428.90	↓ 16.17	11.50	↓ 0.37
May12-Dec12	5.78	↓ 0.10	399.26	↓ 10.98	10.78	↓ 0.23
Jul12-Dec12	5.06	↓ 0.05	387.88	↓ 6.47	12.43	↓ 0.15

Upside Riders

Months	Class II	Class III	Class III
May12-Jul12	(0.14)	(0.16)	(0.14)
May12-Dec12	(0.00)	(0.04)	(0.44)
Jul12-Dec12	(0.00)	(0.04)	(0.44)

Want more information on how DFA Risk Management can help you? Call 1-877-424-3343

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DFA Risk Management

- www.dfariskmanagement.com, your basis report, links to the CME, cool tools, and more!
- DFA Today: free, daily e-mail or fax
- DFA/RM Pricing Update: free, weekly summary e-mail or fax
- Twitter feed for daily cheese market results to your cell.
- Mobile website too
- CME has an extensive website

Additional thoughts:

- Don't need to do all at once, you can have multiple contracts for any given month; “The only way any of us will ever be 100% right or wrong is to sell everything in one day. Don't do it!” The Brock Report, 1/6/2012



- In my opinion, forward contracting should be an on-going activity; stay informed on current market conditions

Questions?

- **Why don't my *target orders* fill?**
 - Offering above current levels?
- **What is a *margin account*?**
- **Why can't I get *high of the day*?**
- **What's the difference between doing months *individually* or as an *average*?**





Thanks!

Any Questions?

ebiggers@dfamilk.com

DFA Risk Management 877-424-3343

www.dfariskmanagement.com



DFA Risk Management

- **Following slides are just additional material**



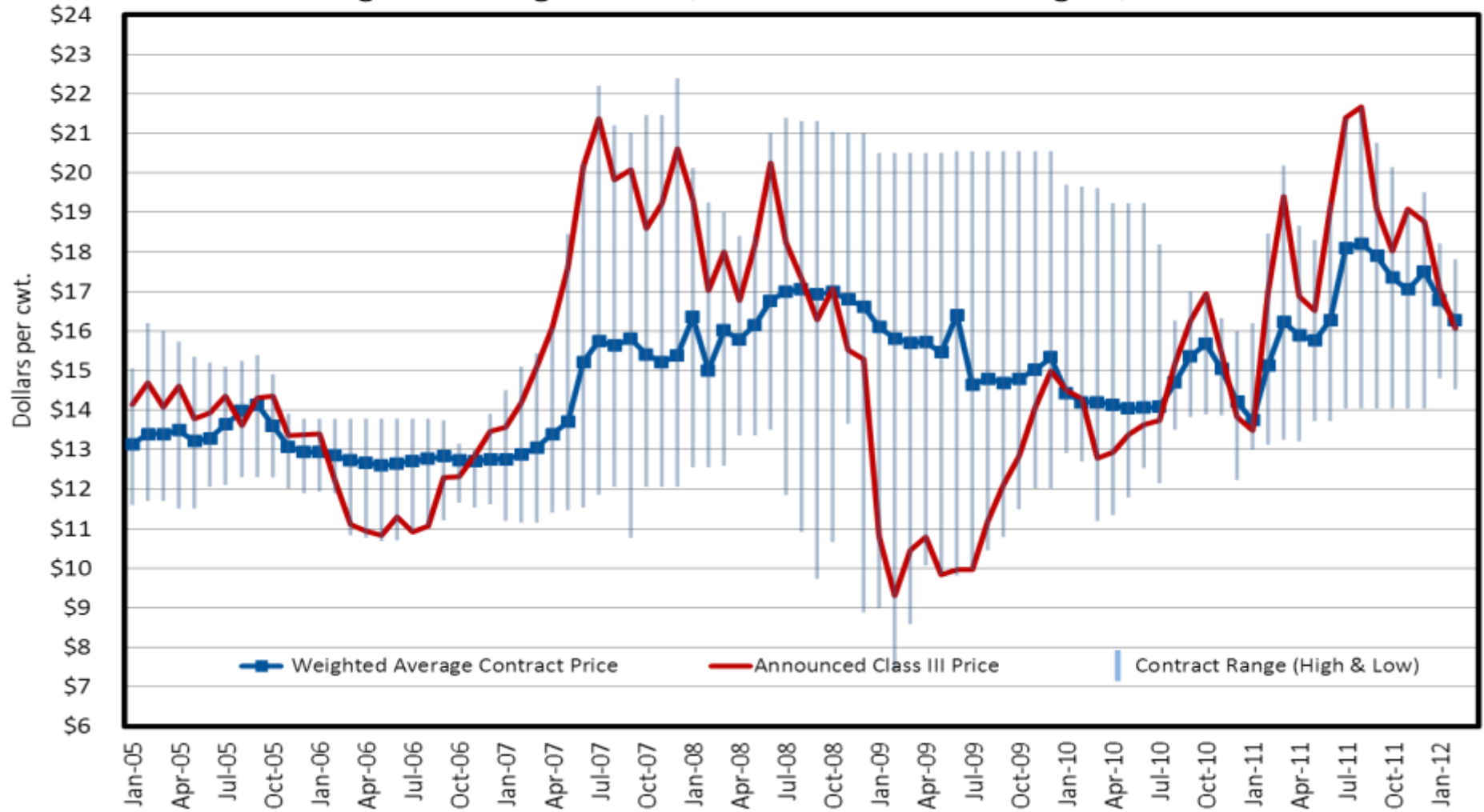
Feed Rider Forward Contracts

- **Done as single months only**
- **Members can select corn and/or soybean meal quantities to hedge**
 - There are quantity limits though (1,100 bu corn or 10 tons soybean meal per 100,000# milk)
- **DFA/RM now offers price protection on corn and soybean meal**
 - Fixed Price
 - Maximum Price



DFA's Risk Management Weighted Average Contract Prices vs. USDA Announced Class III Prices

January 2005 through February 2012 - Contract Ranges Reflected
 Weighted Average Value - \$13.78 vs. Class III Average - \$13.85



Understanding Basis Variability

- It's not Basis Variation that will hurt you but it's the lack of understanding and an unrealistic expectation of what your basis will be:
- \$19 contracted + \$4 expected basis = \$23
... however ...
- \$19 contracted + \$2 actual basis = \$21!

