

Prospects for Dairy Policy in 2013

USDA Ag Outlook

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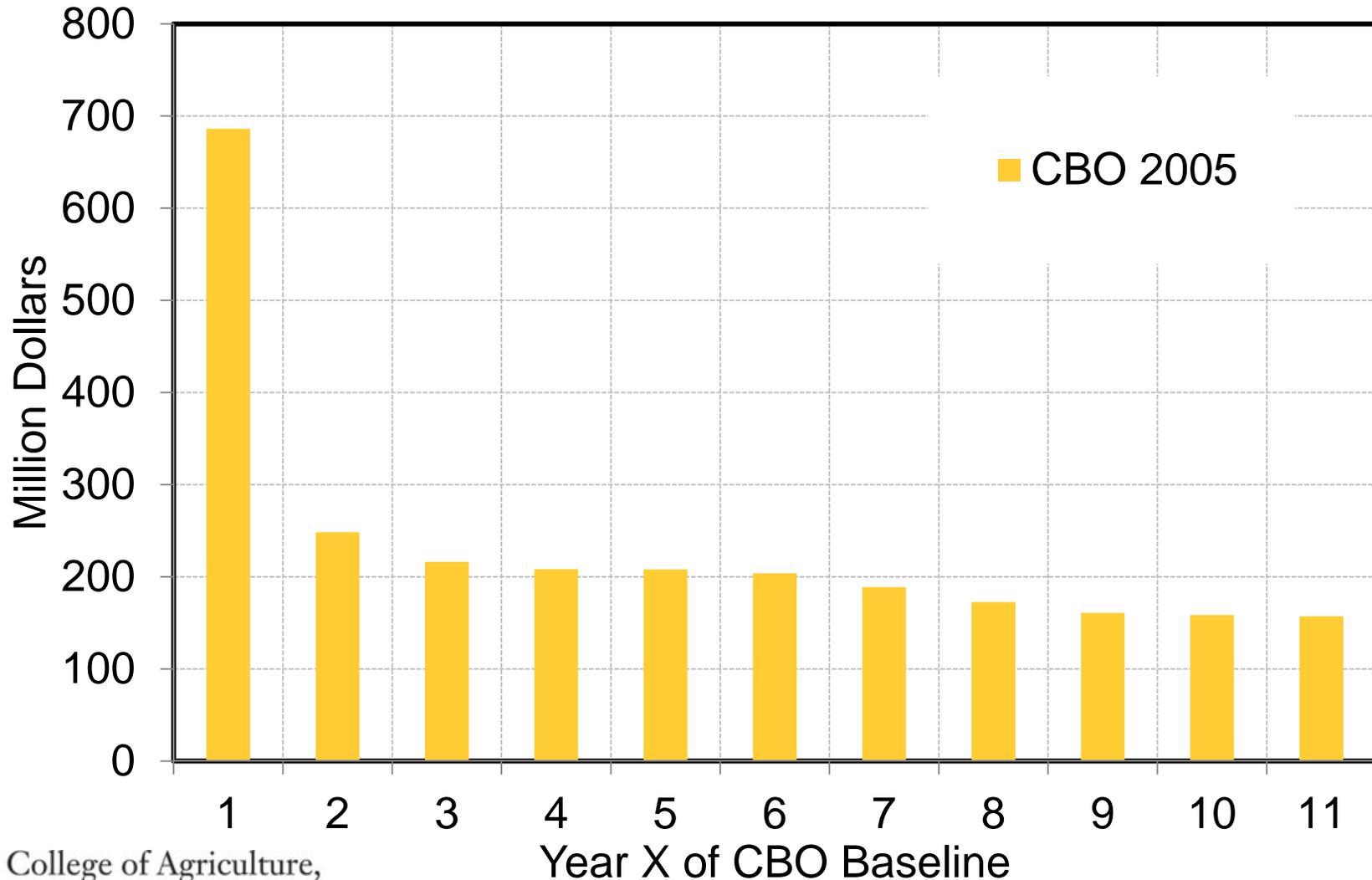
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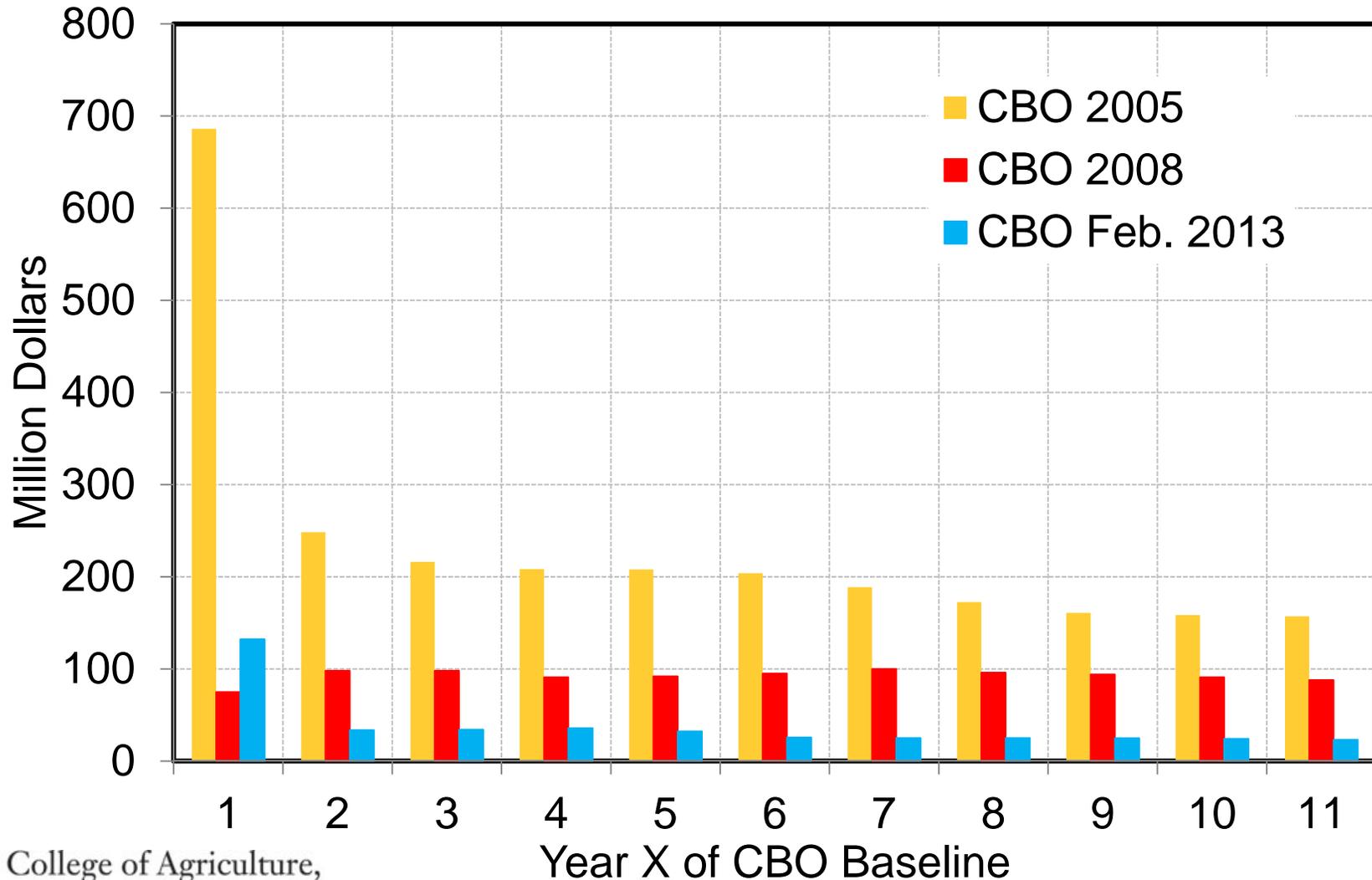
New Dairy Policy in 2013?

- It is too early in 2013 to have a good sense of where dairy policy might come out
- Once some of the budgetary issues become clearer, farm bill debate may begin again
- Projected CCC outlays for current dairy decline yet again
- In a period of rapidly growing feed costs interest has turned to a margin insurance approach

Dairy Baseline Declining Over Time With Higher Input Costs Raising Milk Prices



Dairy Baseline Declining With Higher Input Costs Raising Milk Prices

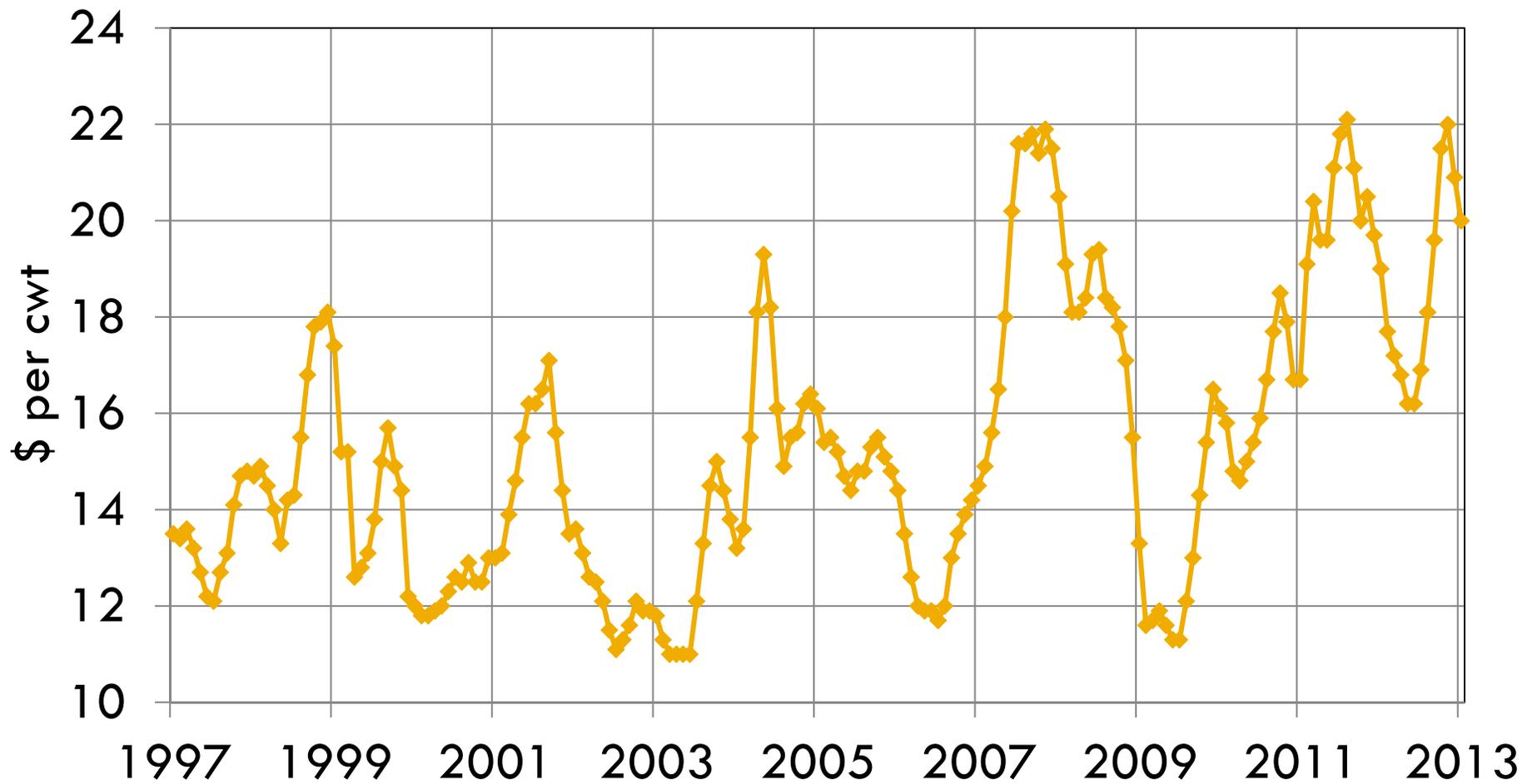


Let's Put This In Perspective

- USDA currently estimates 2012 dairy cash receipts at **\$37.0 billion**
- CBO Feb 2013 baseline spending on dairy programs average over the FY14 to FY23 period **\$28.4 million**
- **0.08%** is dairy spending relative to dairy cash receipts
- It is hard to construct an “effective” program with such small annual outlays



Monthly U.S. All Milk Prices

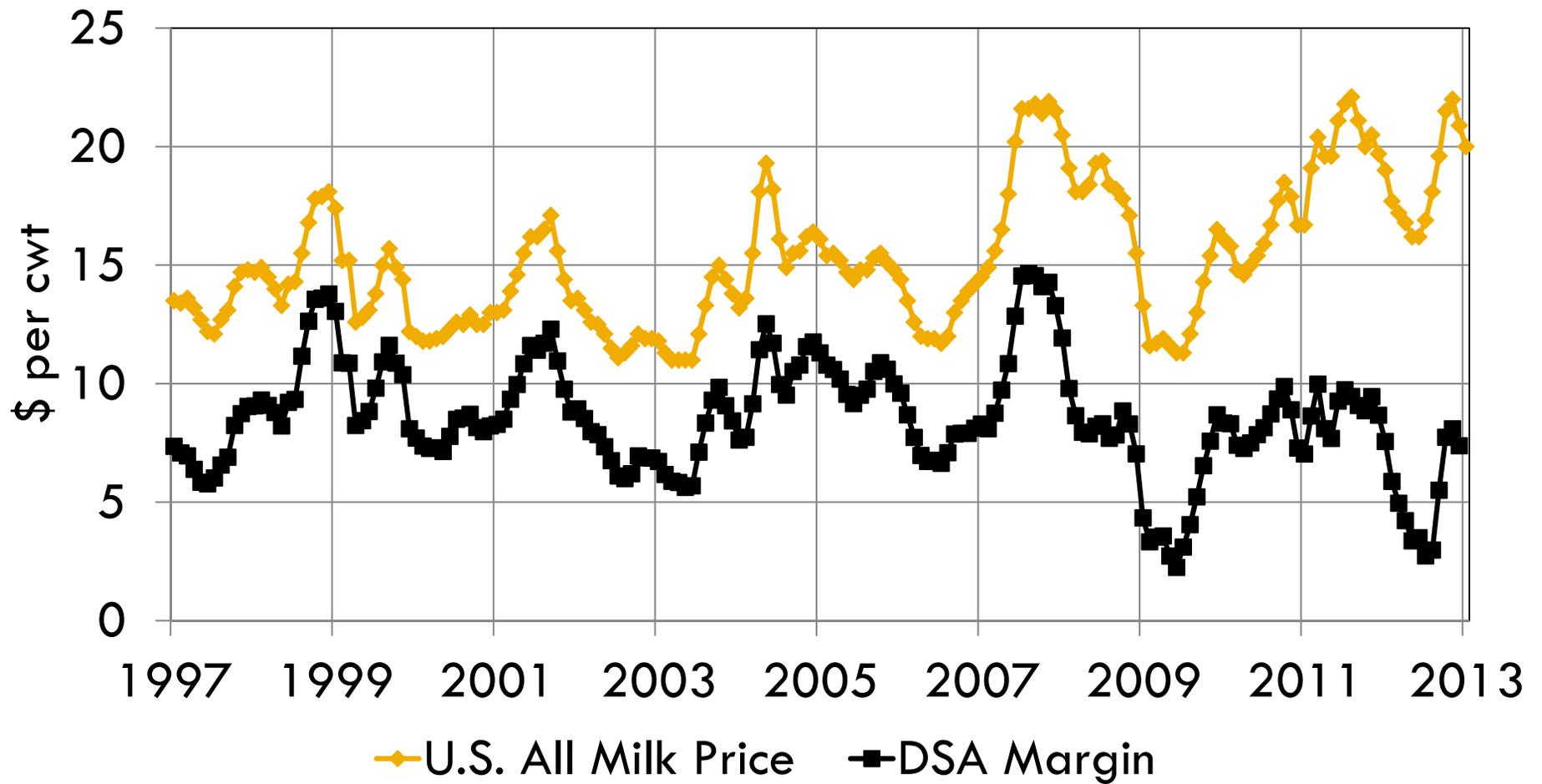


Margin Protection (Milk Price Less Feed Costs) Has Been The Focus

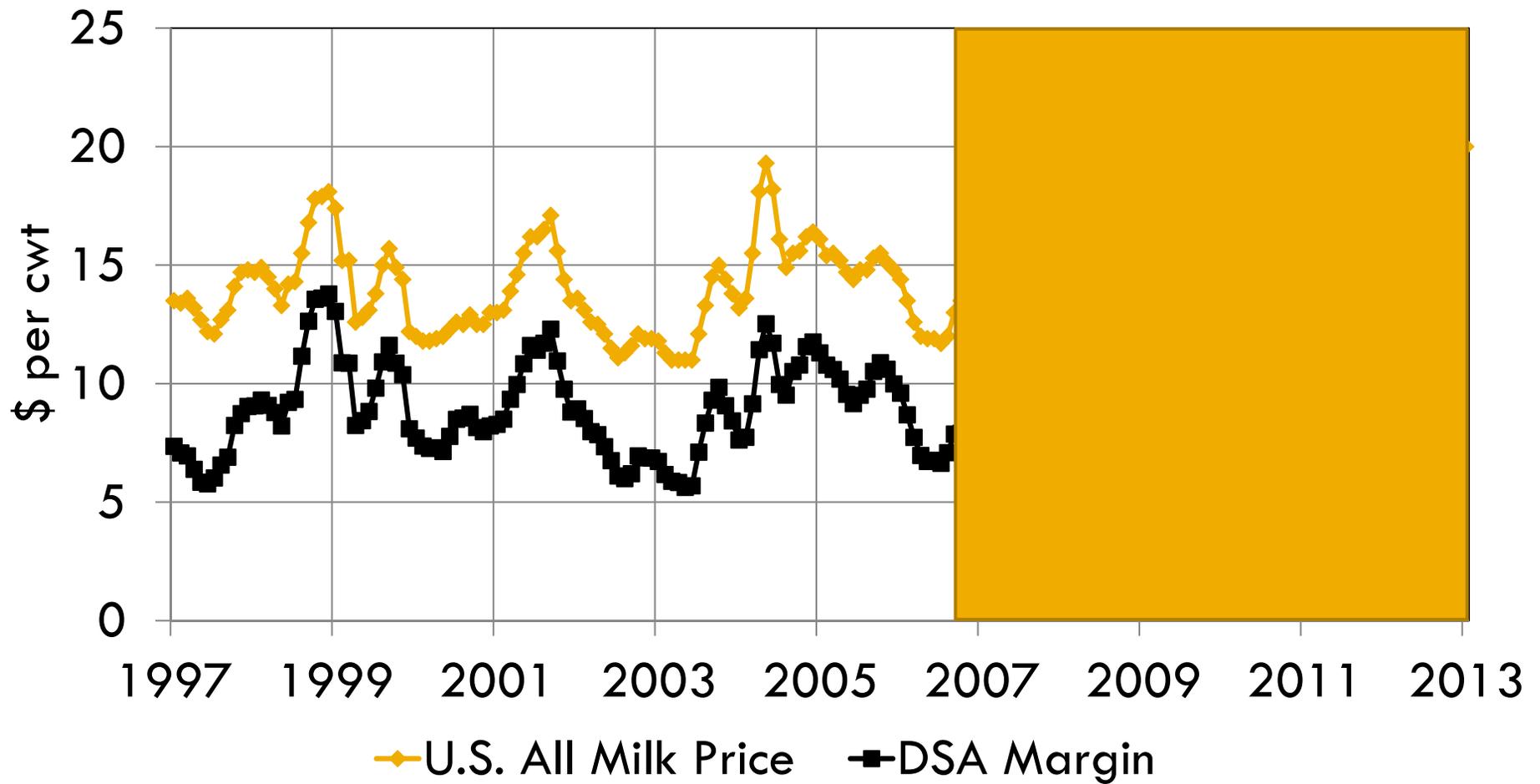
- The combination of high feed costs and price volatility has led the discussion of margin protection
- Protecting margins instead of just milk prices helps on government outlays because milk prices and feed costs are negatively correlated
- This margin is what producers have available to pay for all other costs besides feed costs
- There has been inflation in these other costs over time
- Producer response to margin risk reduction



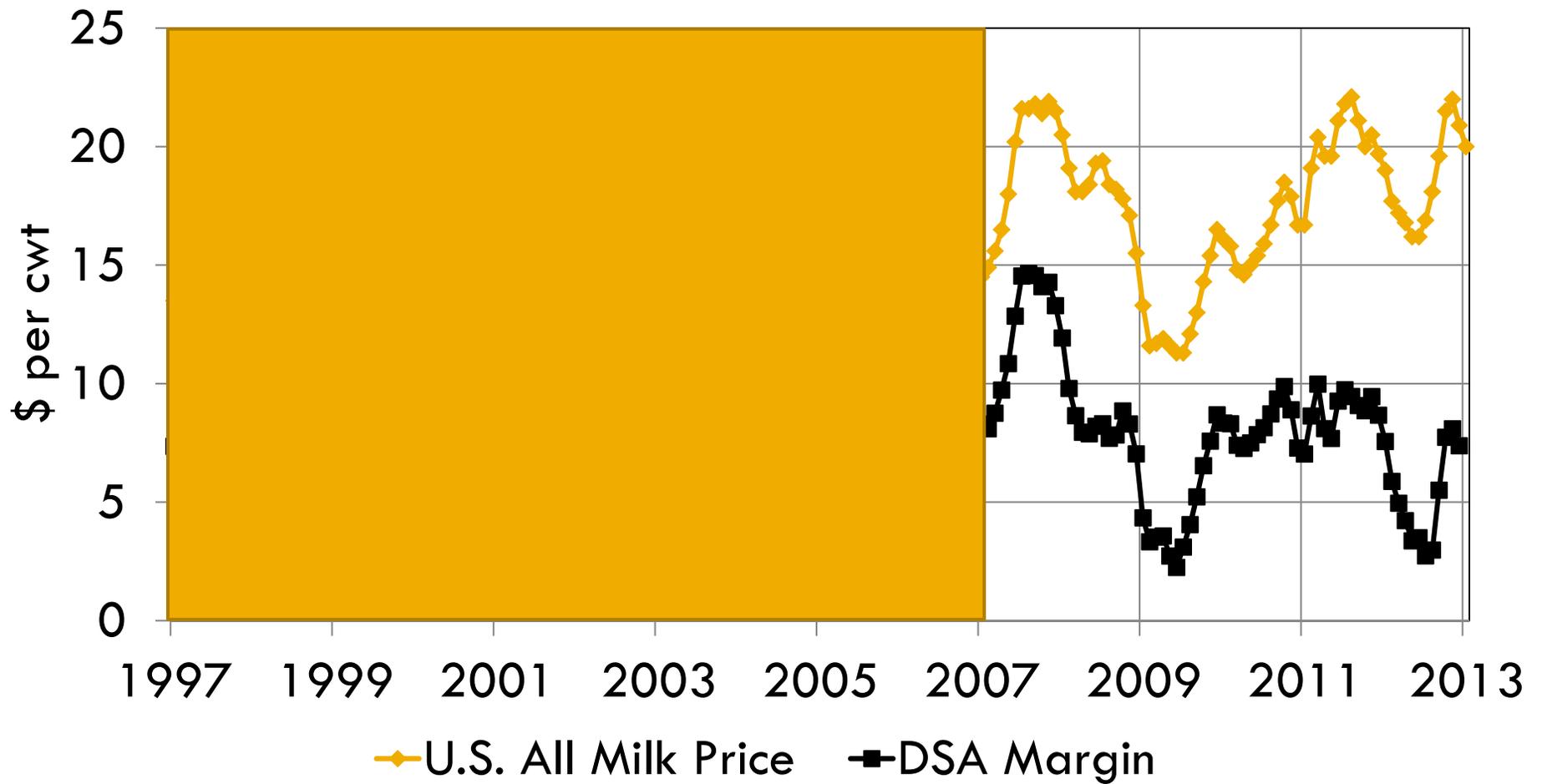
Dairy Industry Facing Milk Price and Margin Volatility



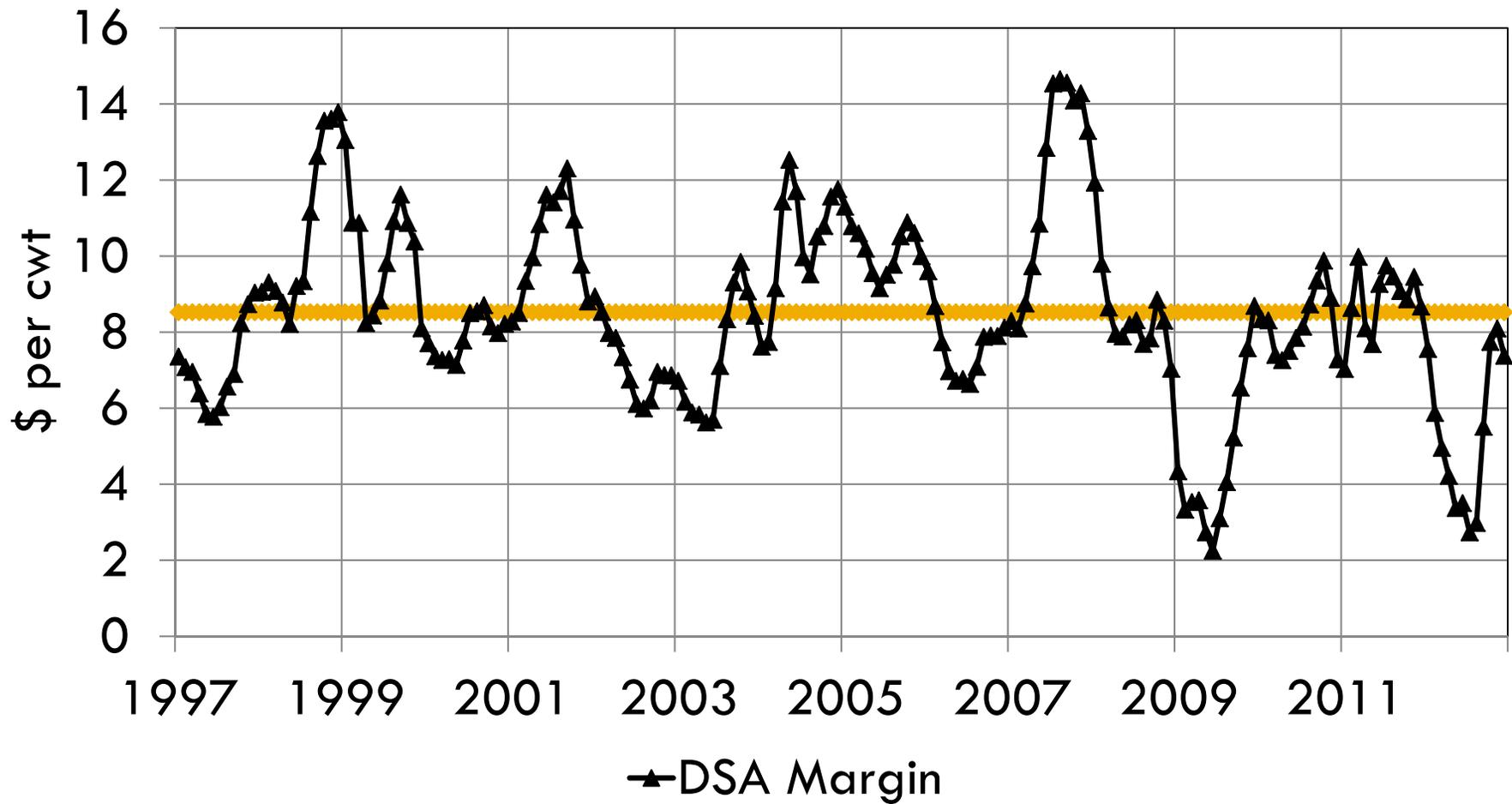
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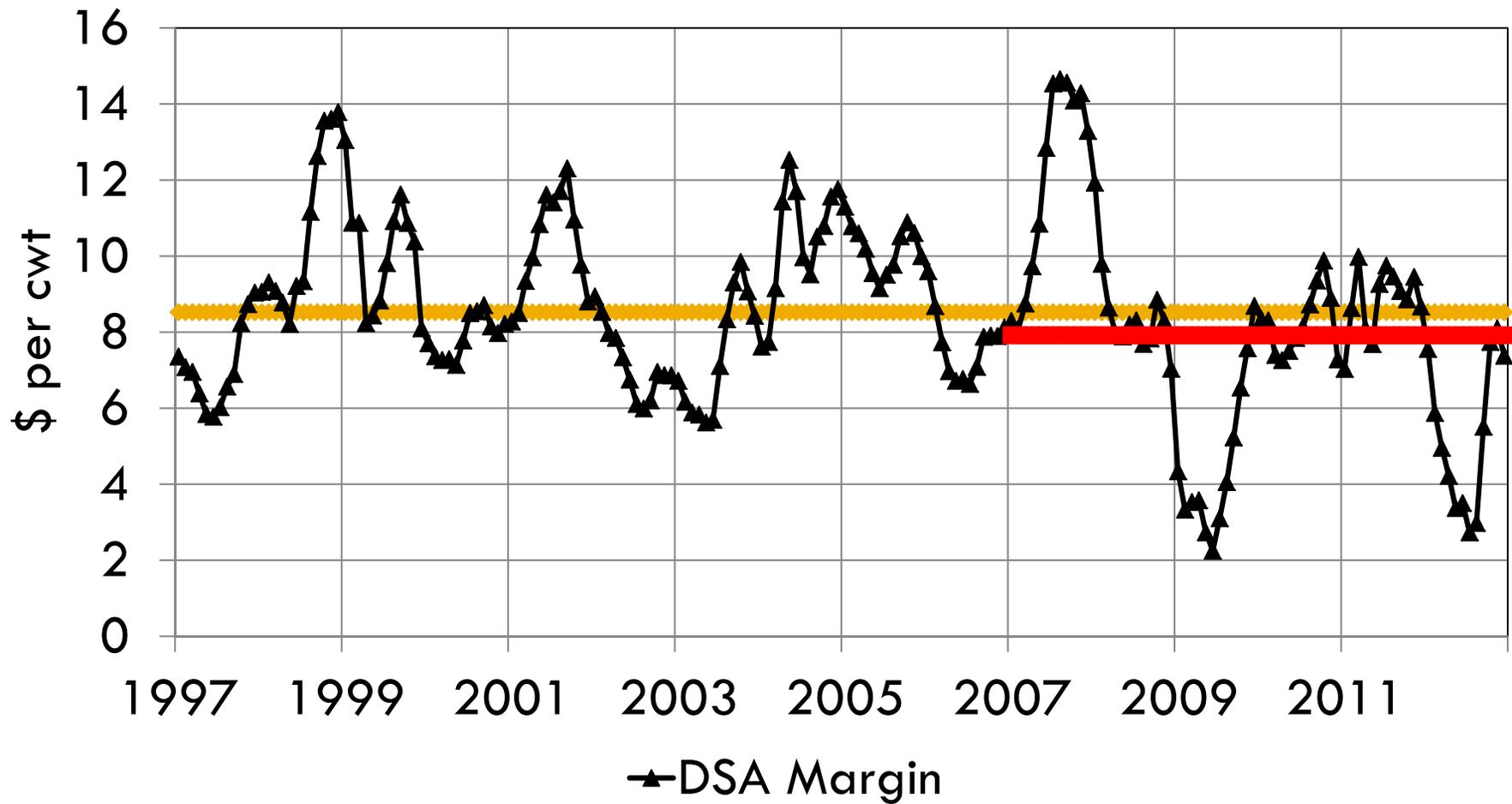
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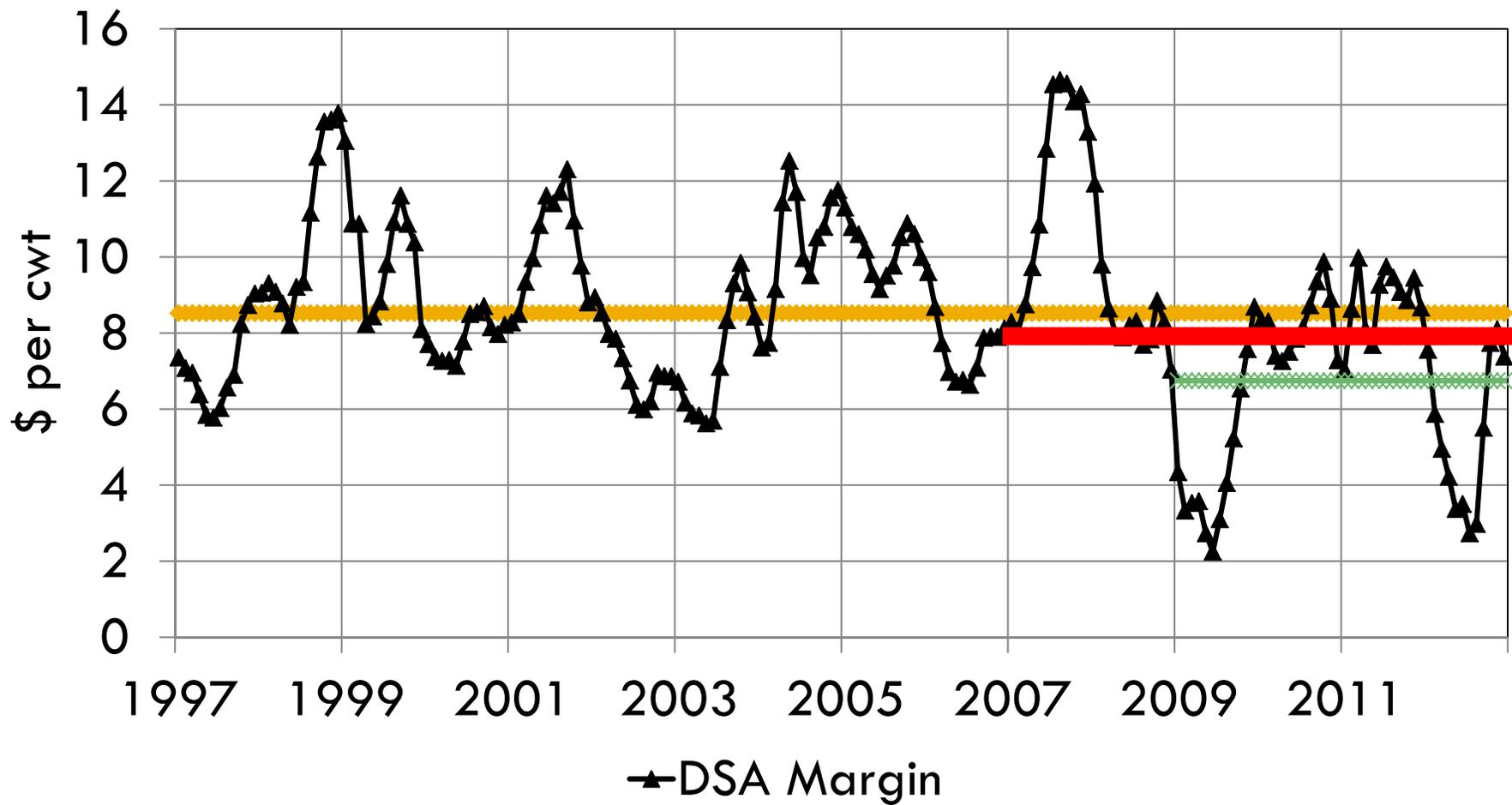
My Largest Concern? An Adequate Safety Net – Not Too Good Or Bad



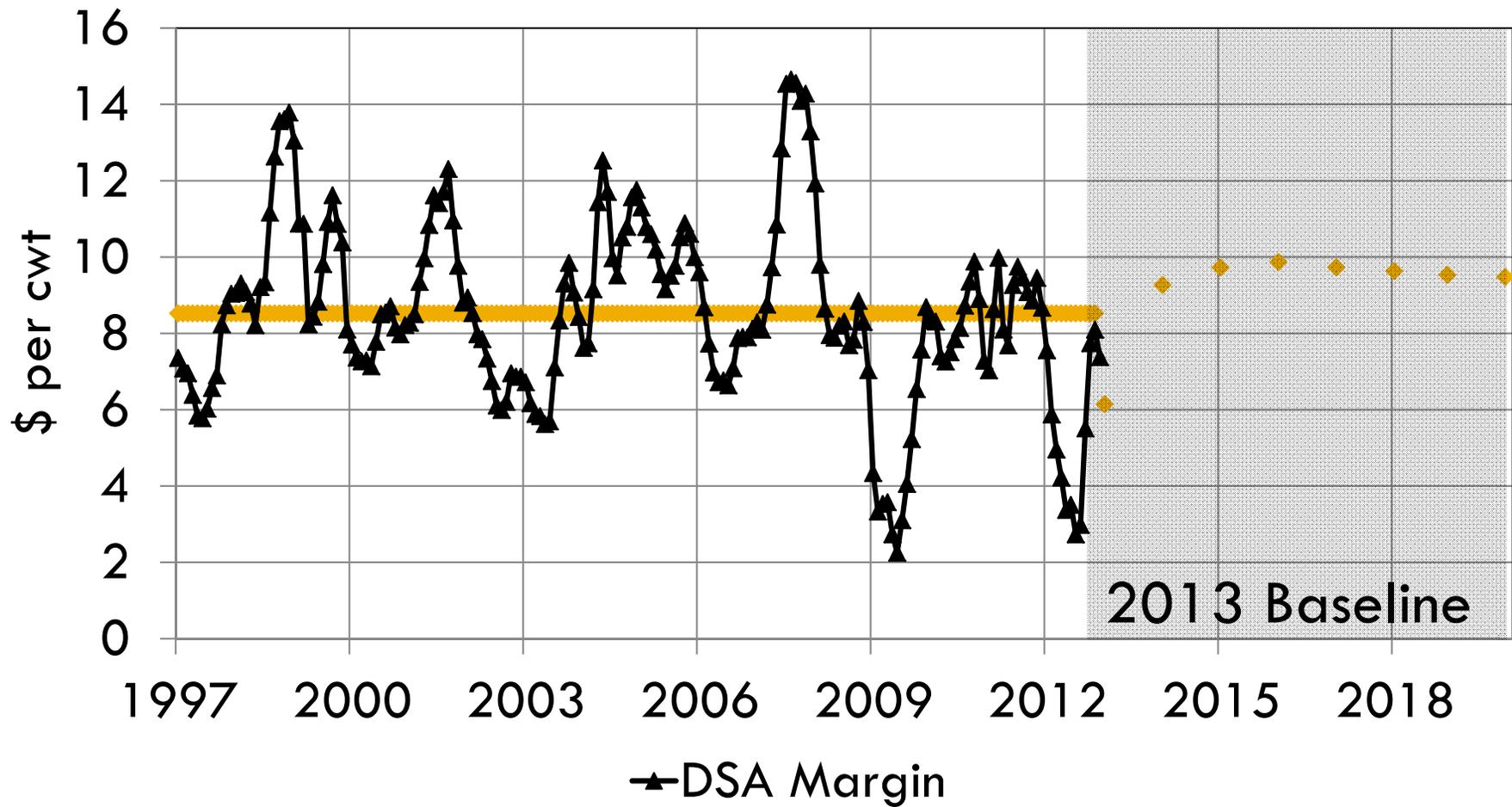
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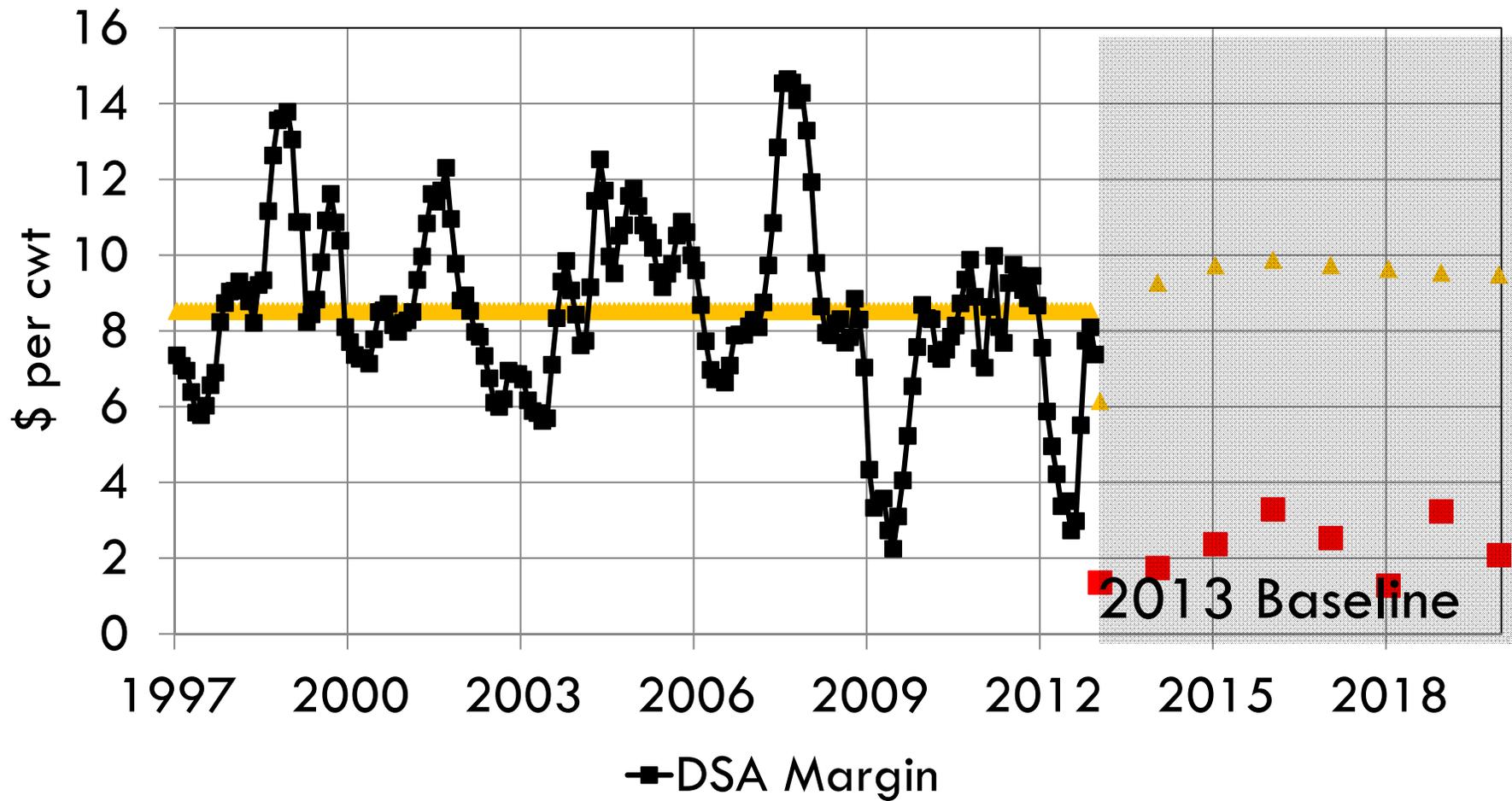
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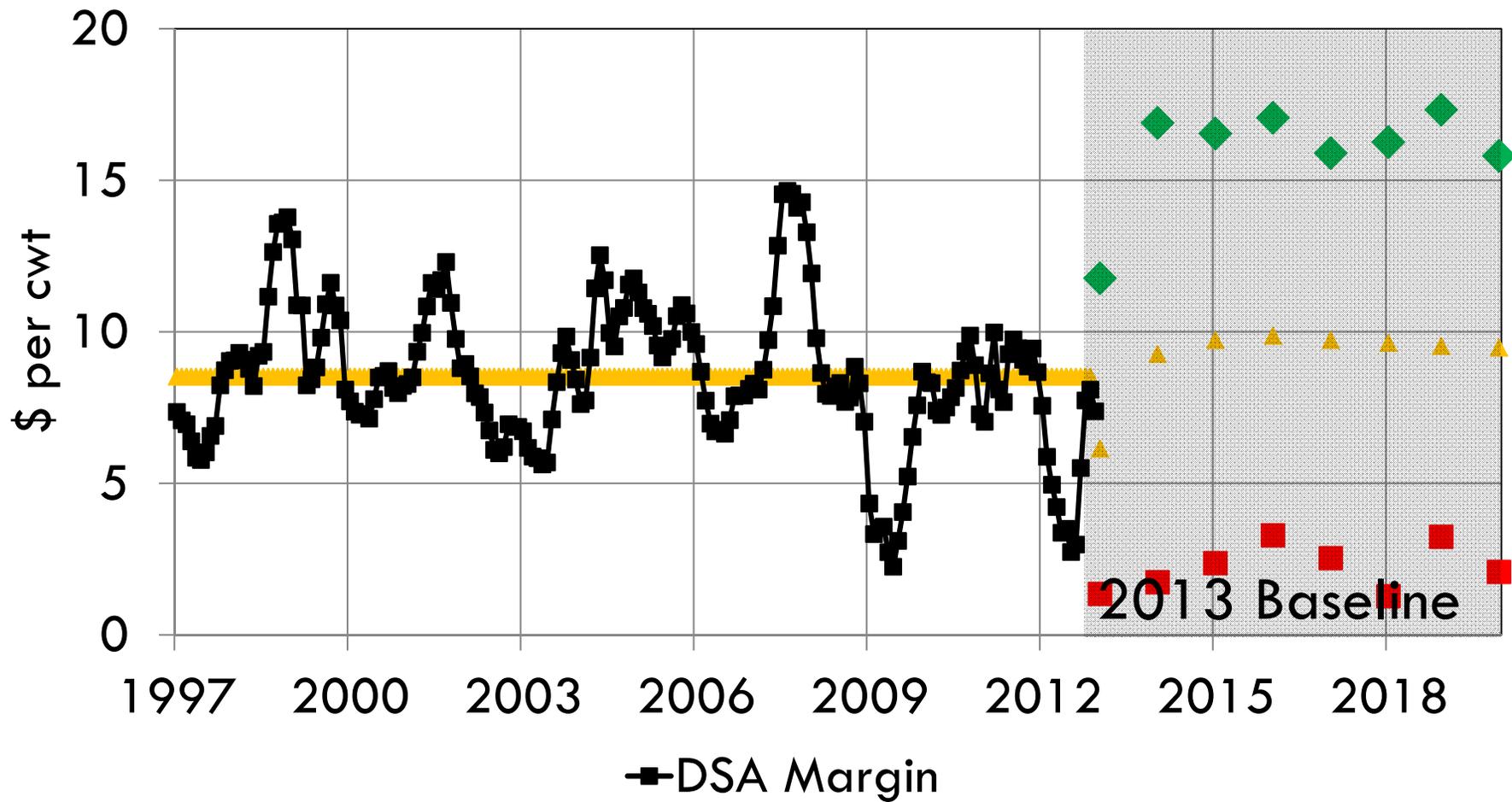
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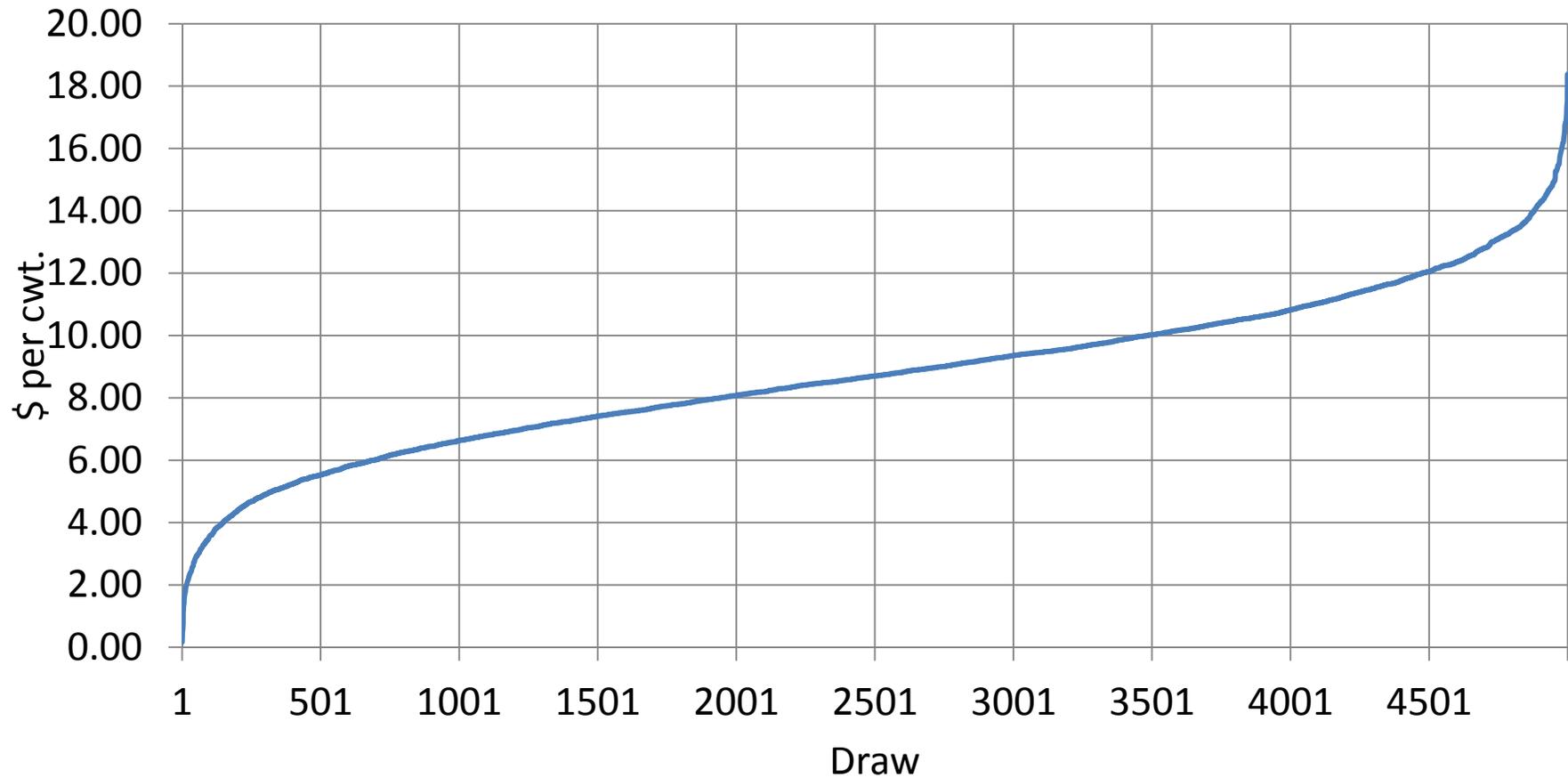
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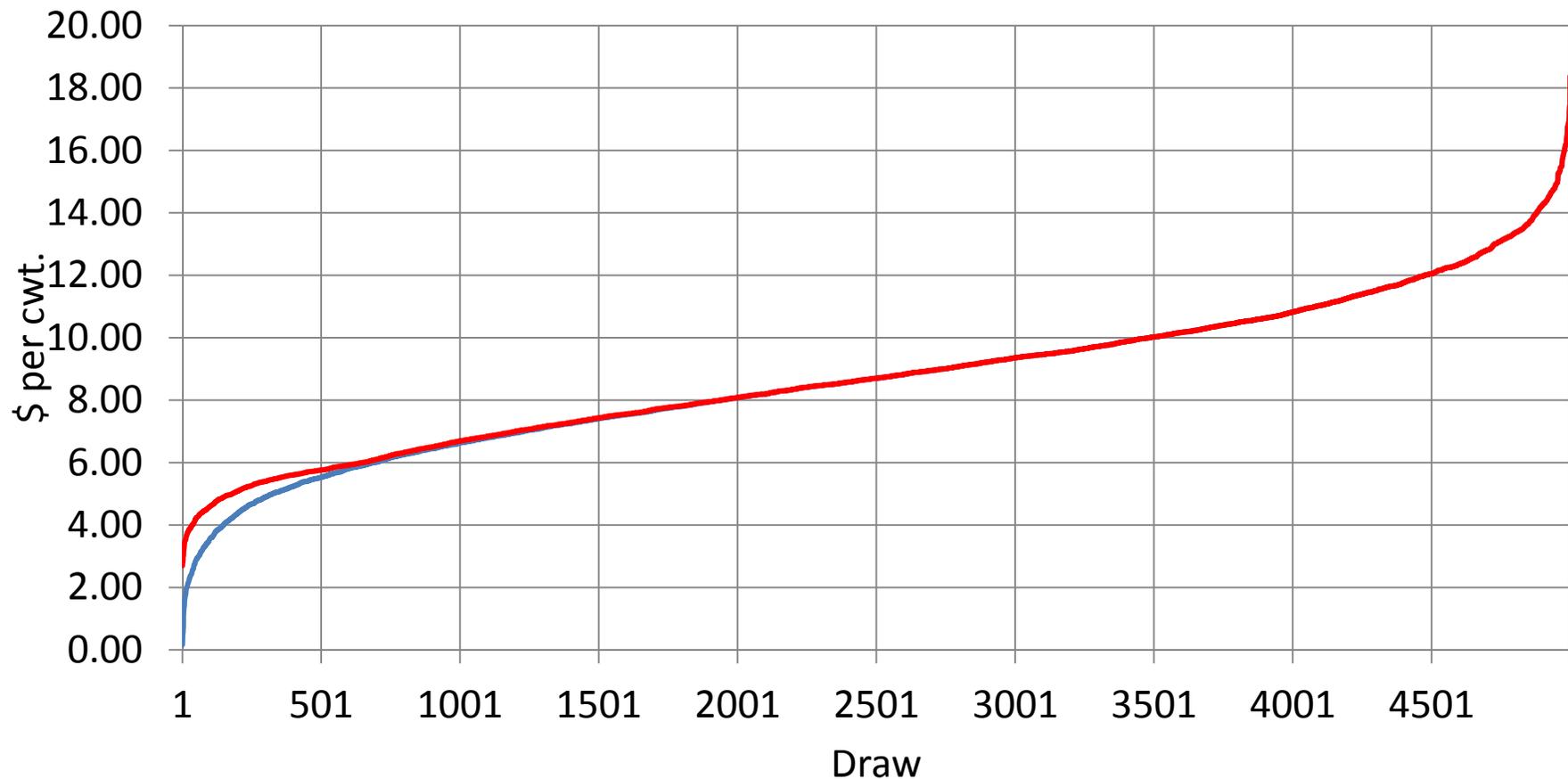
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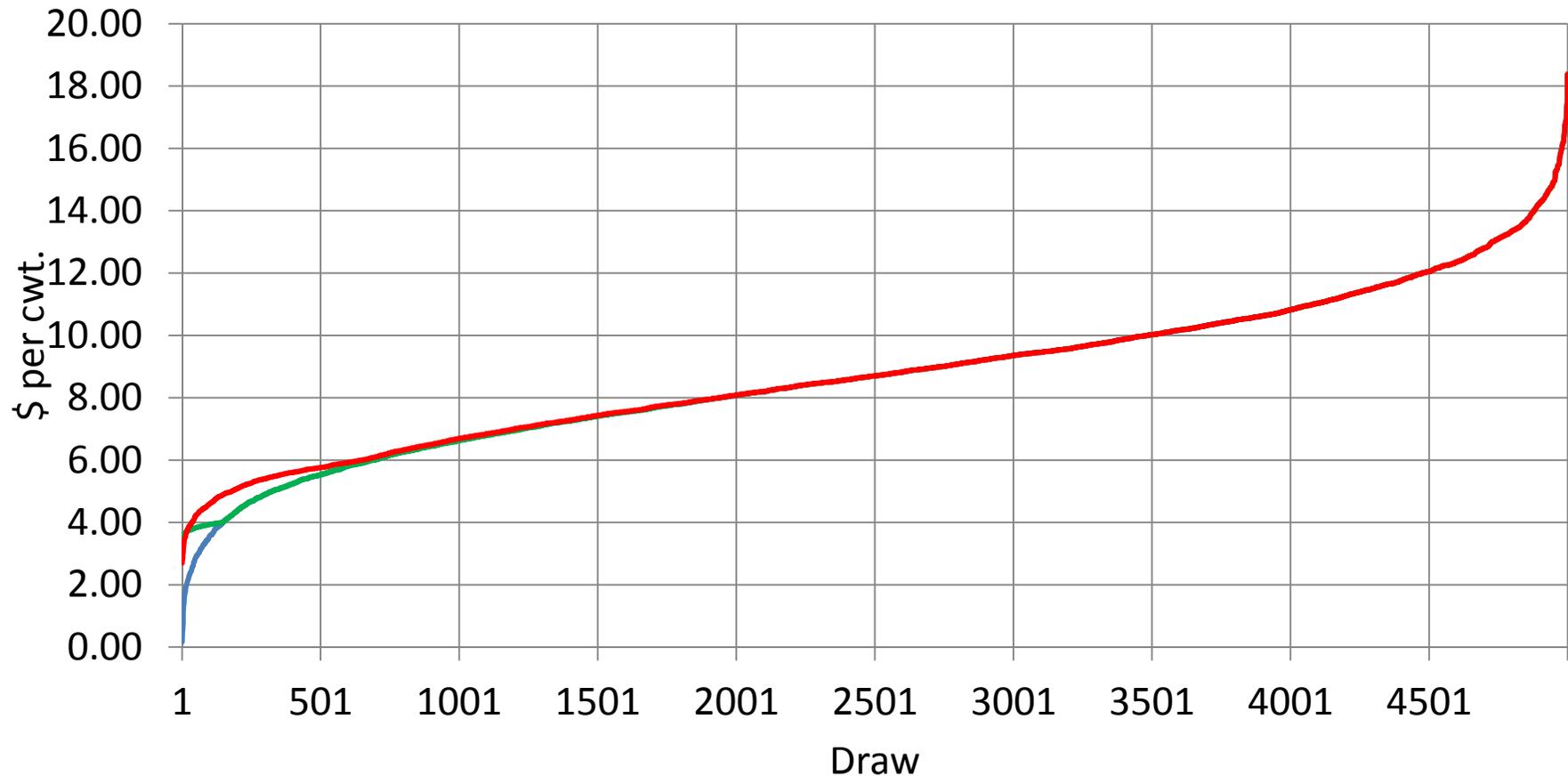
Distribution of DSA Margin Outcomes



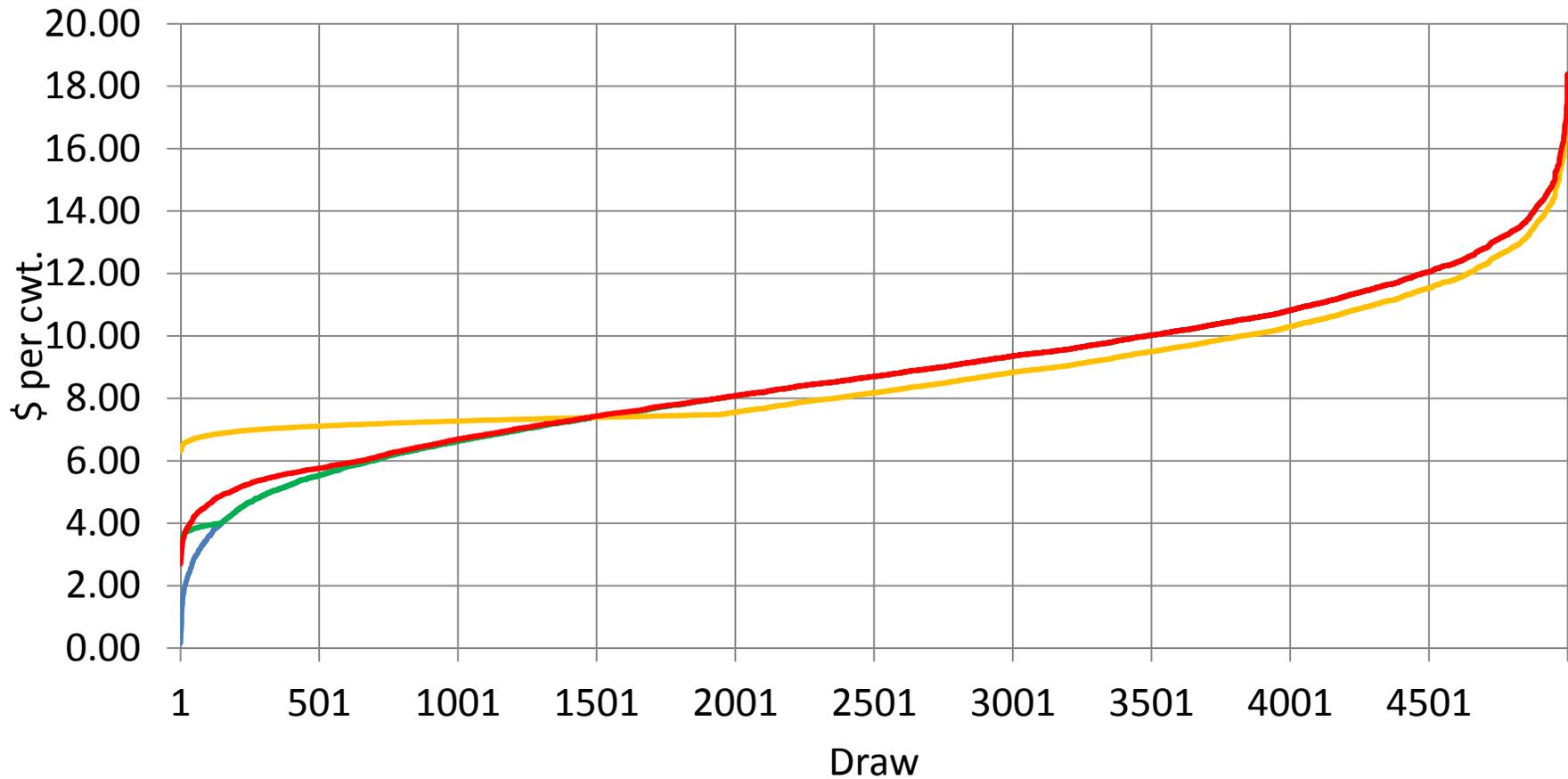
What Does the MILC Program Do?



What Coverage Does the Base Program Provide?



And Adding Supplemental Coverage to the Mix?



So Let's Summarize This

- First, the likelihood of making payments is low given the baseline distribution
- However, if we get low margin outcomes government outlays could become very large
- The average effects show little program payments
- It is a fine line that must be walked in setting these program provisions
- If those of us modeling this are wrong:
 - ▣ No participation
 - ▣ Large government outlays
- What options are available to combat this?

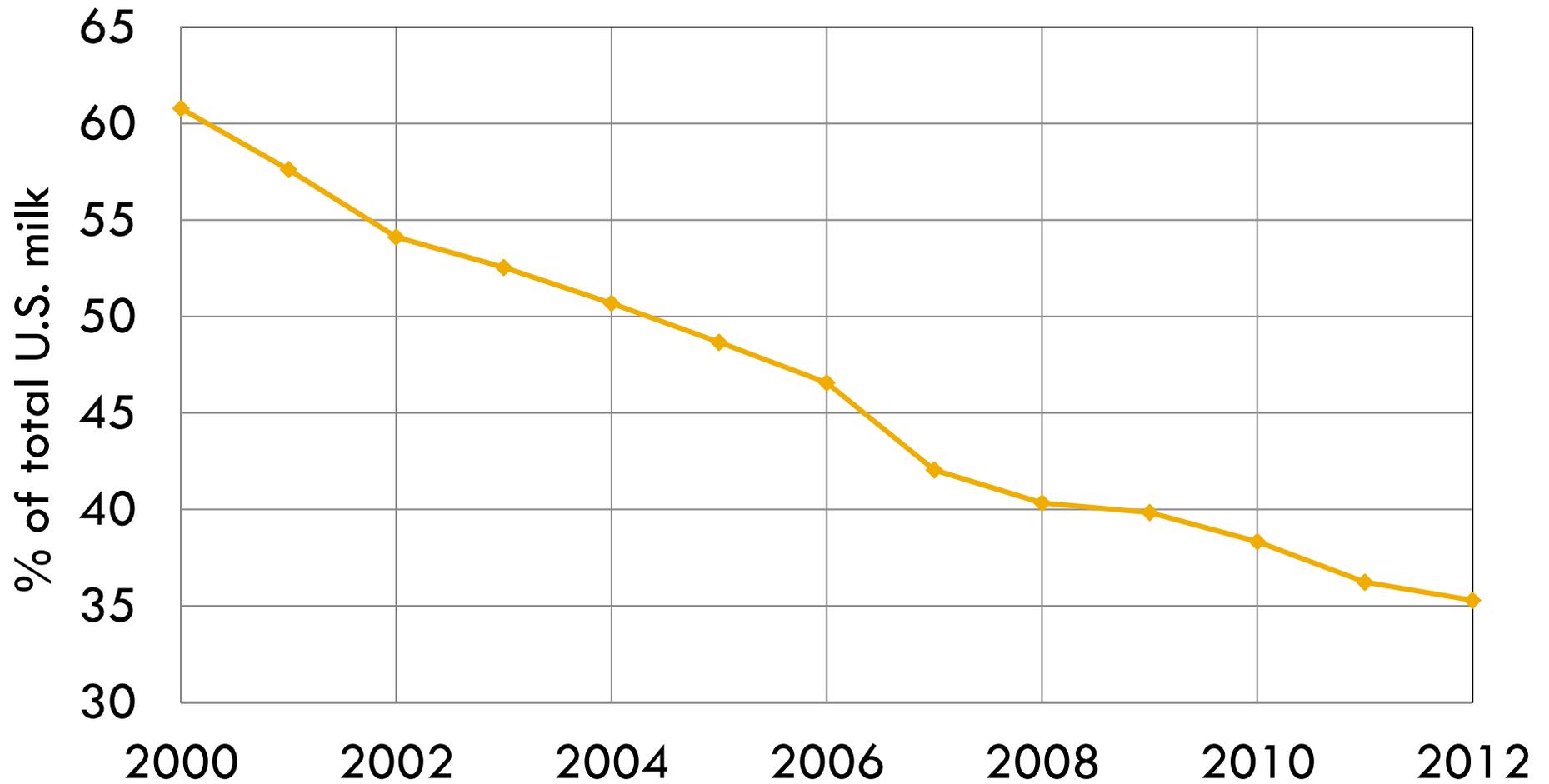


Base Determination Important to Program Effects

- A historically fixed base:
 - ▣ Helps limit government outlays
 - ▣ Reduces support over time for producers who grow
- A base that adjusts through time
 - ▣ Could result in producer expansion
 - ▣ Keeps support at the same proportion for an individual producer
- MILC provides a good perspective



Eligible U.S. Milk Production With a 2.985 Million Pound Cap



Trigger Levels Matter Greatly!

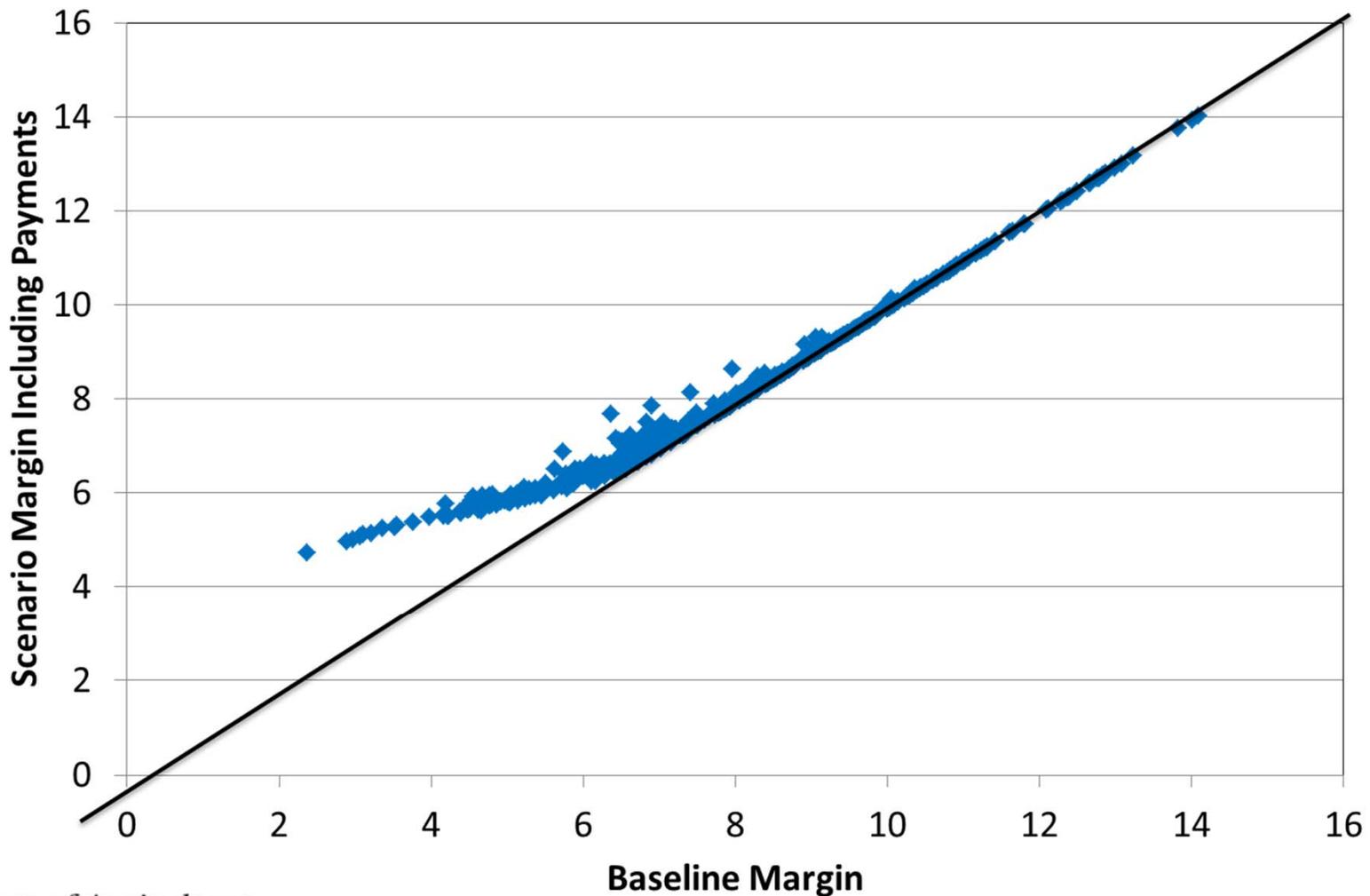
- Let's compare MILC and DSA
 - A \$0.10 increase in corn price means
 - DSA margin decreases by 0.11 per cwt
 - MILC payment rate increases by 0.04 per cwt
 - A \$1 increase in alfalfa price means
 - DSA margin decreases by 0.014 per cwt
 - MILC payment rate increases by 0.0095 per cwt
 - A \$0.10 decrease in milk price means
 - DSA margin decreases by 0.10 per cwt
 - MILC payment rate increases by 0.045 per cwt
- Remember bases differ
 - MILC 2.985 (2.4) million pounds
 - DSA 80% of historical base for base program, up to 90% of previous year's marketings for supplemental payments



Flexibility Offered Allows Producers to Choose Coverage

Coverage Level	Supplemental Premium Rate		
	First 4 million lbs	Above 4 million lbs	
\$4.50	\$0.010	\$0.015	
\$5.00	\$0.025	\$0.036	
\$5.50	\$0.040	\$0.081	
\$6.00	\$0.065	\$0.155	\$0.075
\$6.50	\$0.090	\$0.230	
\$7.00	\$0.434	\$0.434	
\$7.50	\$0.590	\$0.590	\$0.332
\$8.00	\$0.922	\$0.922	

Baseline Versus H.R. 6083 Margin Comparison



Summary

- The 2012 dairy policy debate will surely provide the framework for the 2013 dairy policy debate
- It should not be lost that this is a time where major policy change is being attempted in the dairy industry
- Policy change of this magnitude will be hard
- We should not lose sight that an adequate safety net is our goal

