

WESTERN UNITED DAIRYMEN RISK MANAGEMENT SEMINARS

December 2010

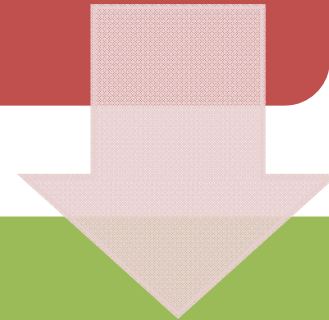


WHO WE ARE

- **Blimling and Associates, Inc. is a widely respected consulting and research firm based in Cottage Grove, Wisconsin with branch offices in Pennsylvania, Nebraska and California**
- **Producer-focused research and risk management consulting**
 - **Market news/commentary; milk-price forecasts updated weekly**
 - **Provide a broader view than just the supply-side or US perspective**
 - **Avoid blanket recommendations and solicitations**

TODAY'S TOPICS

What's Changed

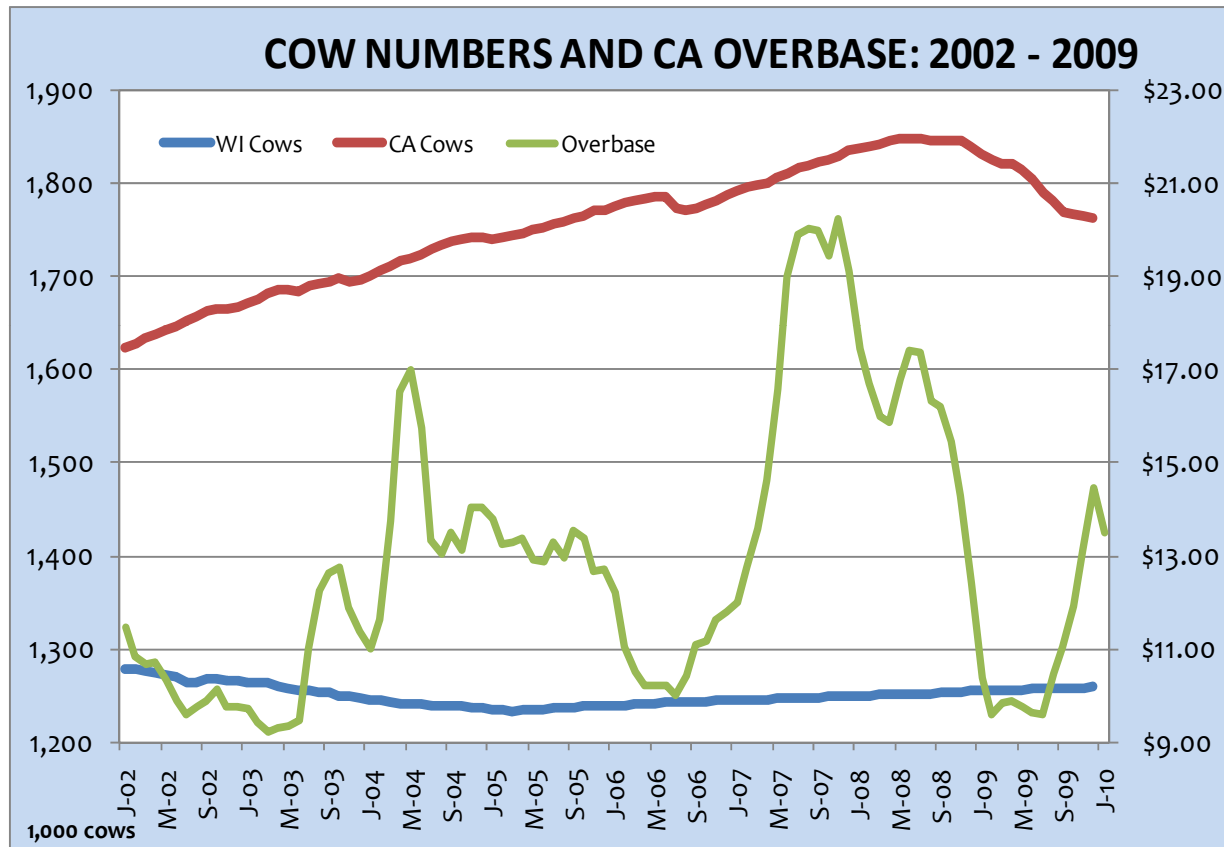


Current Thoughts on
Hedging

THINGS ARE DIFFERENT

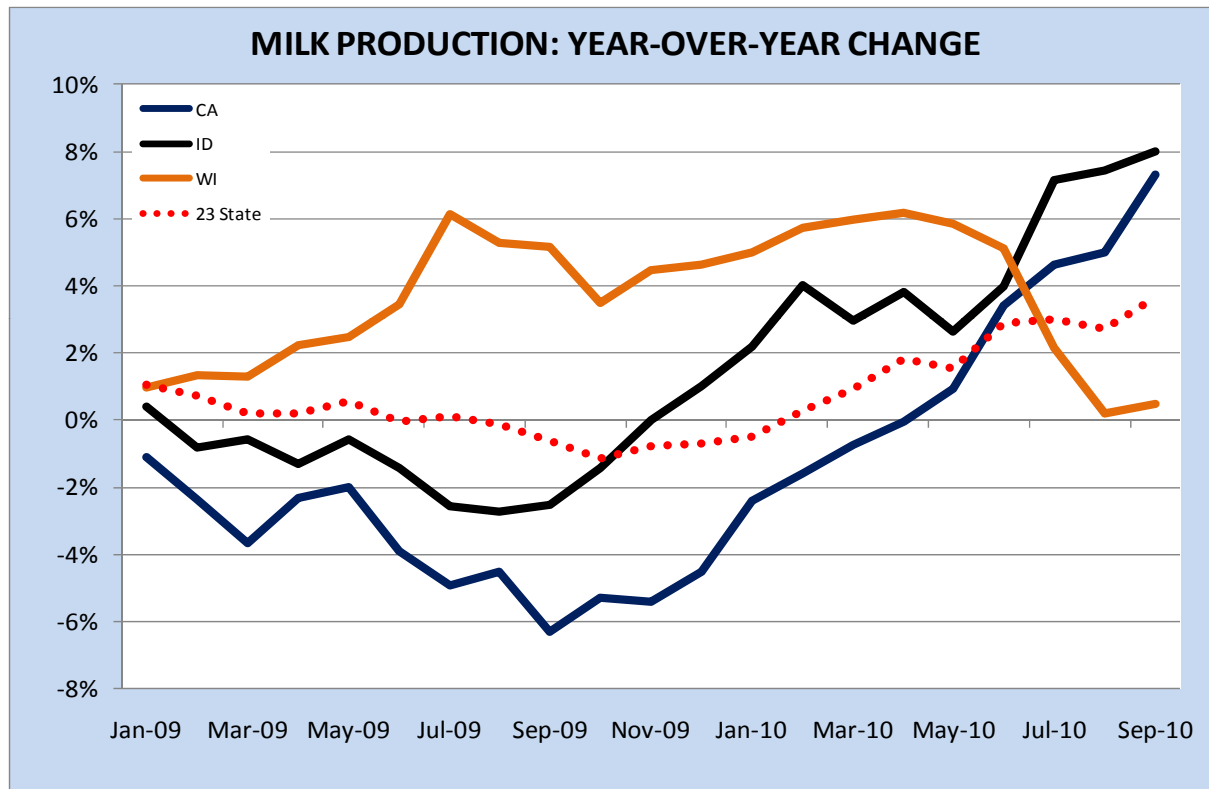
- The US dairy industry in general and Western producers in particular are experiencing profound change that requires new ways of thinking and the need to manage risk to their revenue stream.
- What seemed automatic not so long ago is no longer assured – such as inevitable growth and ‘guaranteed’ profitability in the West.
- While no one can be sure how everything will “turn out” in 3, 5, or 7 years, most market participants believe volatility will persist – income volatility as well as margin volatility.

SOME HISTORY



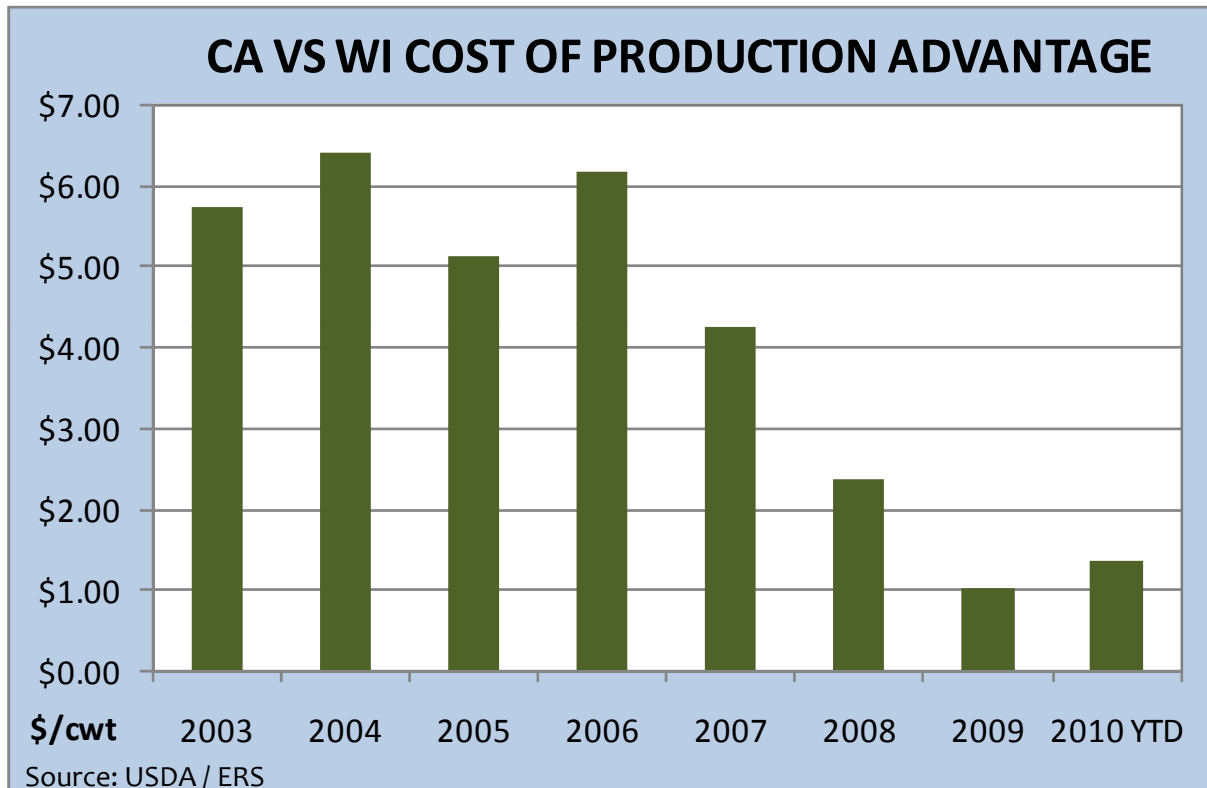
- In day's gone by, Western producers could largely settle back and watch events unfold...
 - Markets could not get low enough for long enough to wreck long-term financial prospects
 - Managing the margin was not an imperative: why give up opportunity at the highs when one could survive the lows?

A CHANGING LANDSCAPE



- The pain of 2009 was felt most acutely by Western dairymen
- Due to a different model, producers in the traditional dairy areas did not suffer as greatly
 - 50+ CAFO permits are pending in Wisconsin and processors are expanding

WHAT CHANGED?



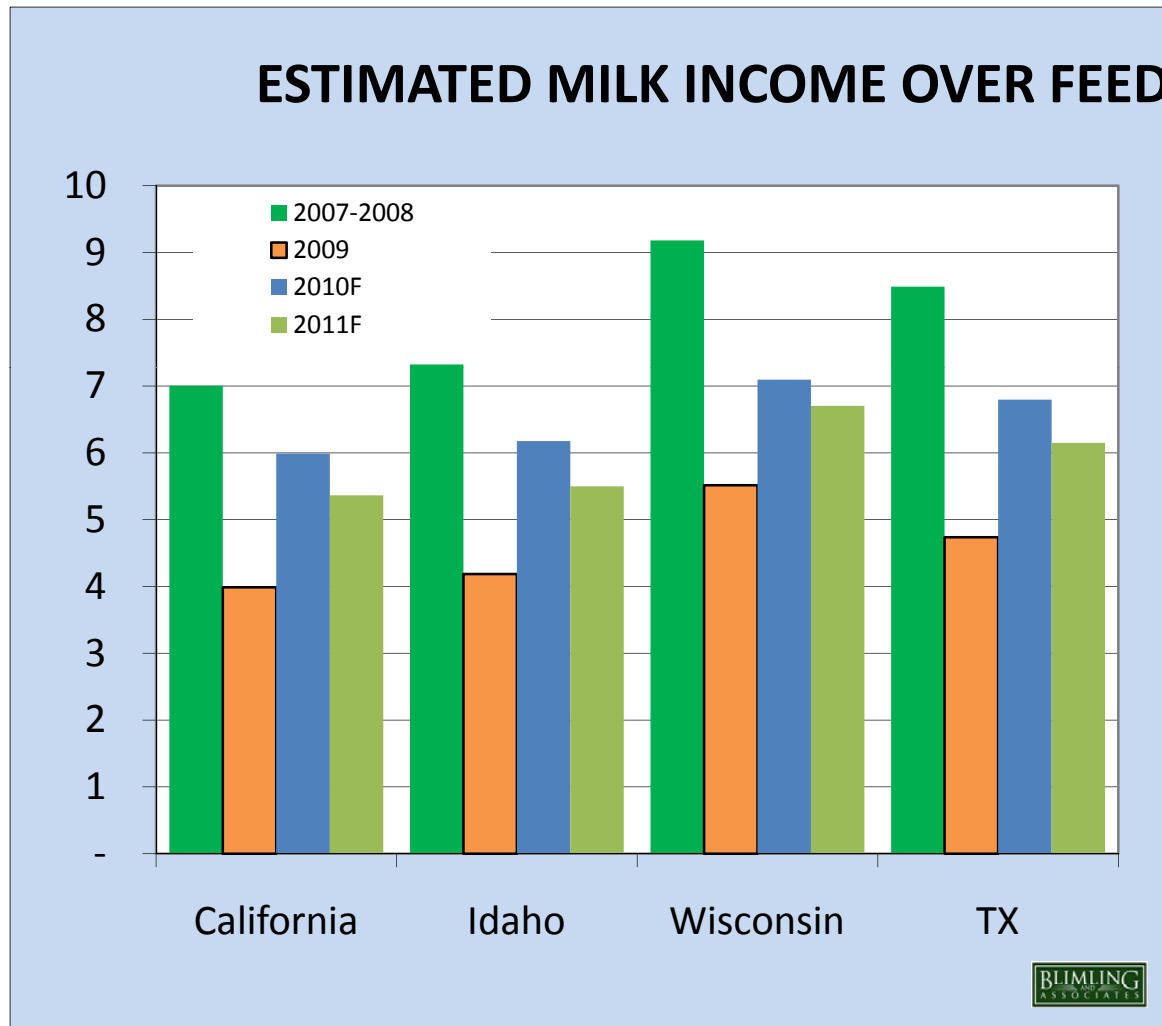
- With such an advantage, in low milk price periods, contraction came from the traditional dairy areas
- Today, a more level playing field exists among the regions, putting greater pressure on Western operations

TODAY'S REALITY

	C.O.P.		less WI pay		
	Advantage	less MILC	diff	Net CA Adv	
2003	\$ 5.74	\$ (1.09)	\$ (1.14)	\$ 3.51	
2004	\$ 6.42	\$ (0.22)	\$ (1.80)	\$ 4.41	
2005	\$ 5.14	\$ (0.01)	\$ (1.48)	\$ 3.65	
2006	\$ 6.18	\$ (0.61)	\$ (1.79)	\$ 3.77	
2007	\$ 4.27	\$ (0.01)	\$ (1.44)	\$ 2.82	
2008	\$ 2.36	\$ -	\$ (2.46)	\$ (0.10)	
2009	\$ 1.03	\$ (1.15)	\$ (1.85)	\$ (1.97)	
2010	\$ 1.38	\$ (0.04)	\$ (1.77)	\$ (0.42)	

- In this context, it is not surprising that CA cow numbers were down 78,000 head in 2009, while WI grew by 4,000
- Feed prices provided some relief in early 2010, but that may have been fleeting
- This environment requires a different approach to managing risk

OUR CONCERN FOR TOMORROW



A real possibility for margin squeeze in 2011 with high feed costs and softening milk prices.

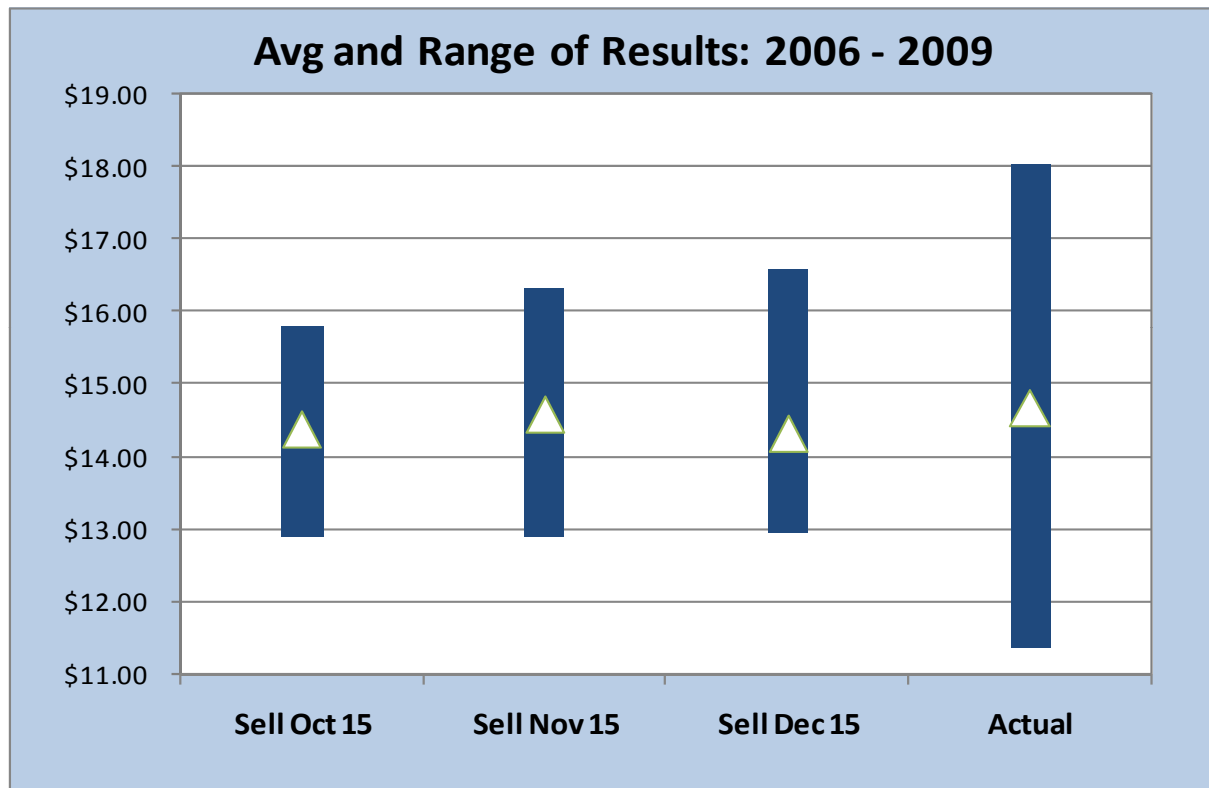
States will be impacted differently.

These figures assume current futures prices. Our outlook later today suggests futures may be overvalued in places.

NEW TOOLS ARE REQUIRED

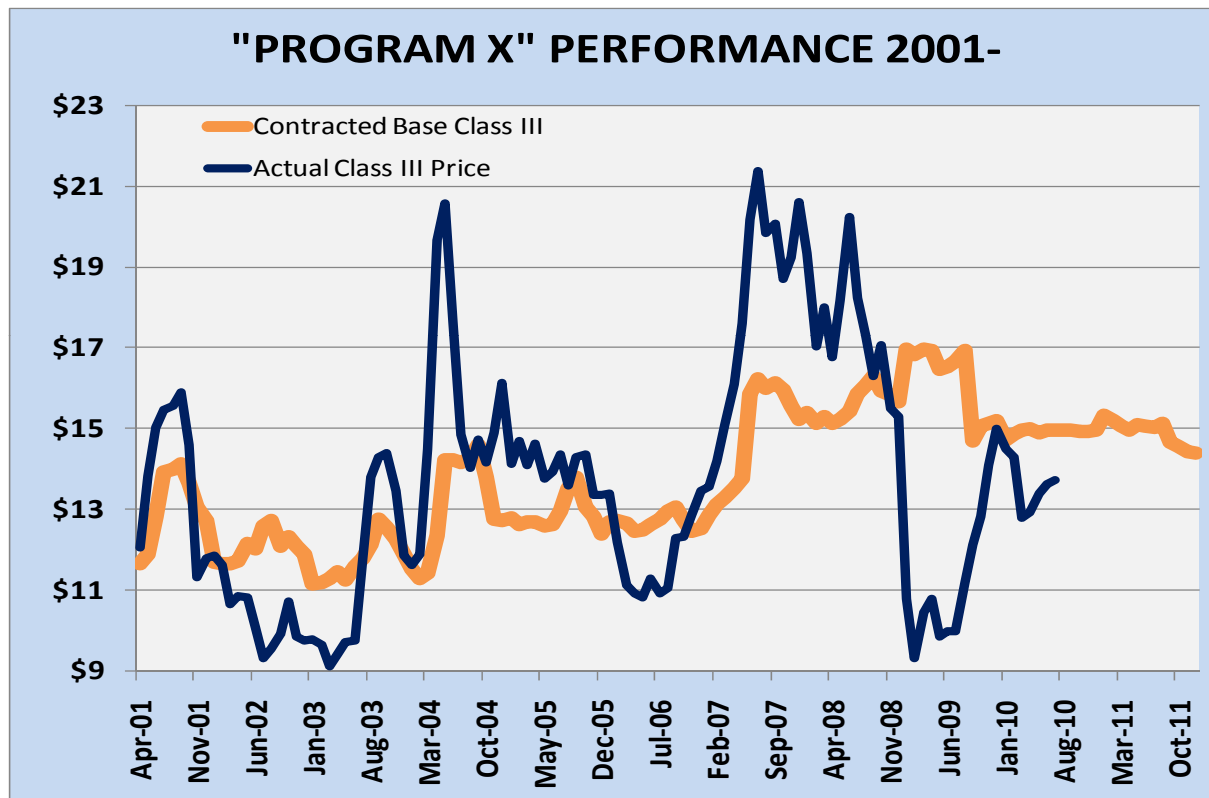
- If we believe that costs are going to be *more variable* and income is going to be *as variable* going forward – in a more competitive environment – then managing margins becomes a critical objective for dairy producers.
- Ultimately this is the objective of most businesses – protecting and growing the bottom line.
- Managing margins – for the first time – is becoming a concept that producers – and their lenders – are starting to embrace.
- Risk management doesn't guarantee profitability but is another tool in the toolkit that more and more Western producers are considering

TRANSFER OF VOLATILITY



- Assumes 'locking' in a price for the next calendar year on Oct, Nov and Dec 15
- Averages are pretty comparable . . .
- But, ranges are dramatically different
- If volatility or low prices are an issue, risk management helps

WHAT ABOUT REAL LIFE?



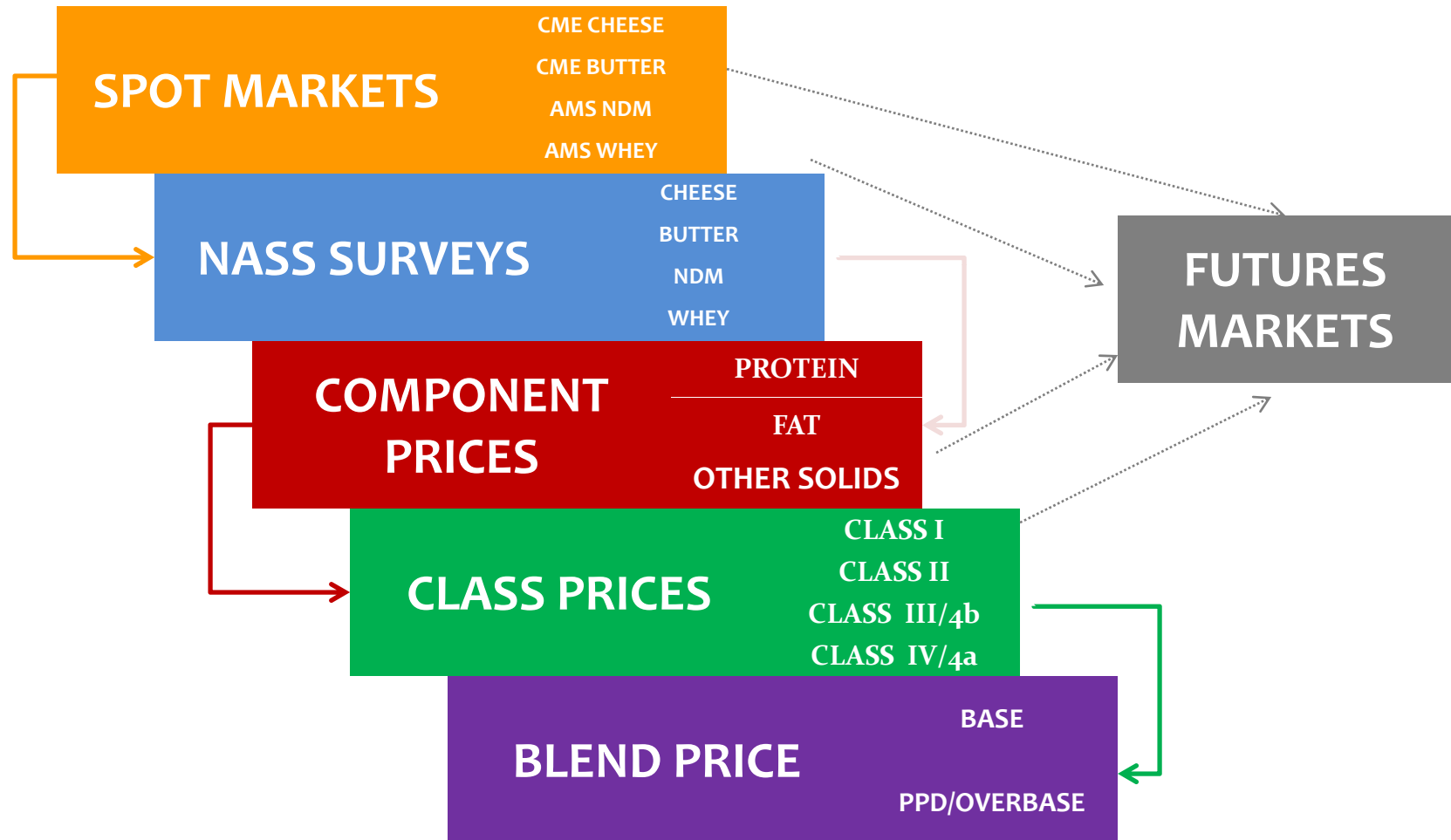
- Examined data from one active farmer program we manage
- From April 2001 through July 2010:
 - Contracted milk: \$13.67 average with \$16.96 high and \$11.14 low
 - Market milk: \$13.76 average with \$21.38 high and \$9.11 low
- Huge difference: \$5.83 high/low spread versus \$12.27

IF ONLY HEDGING MILK WAS THIS EASY

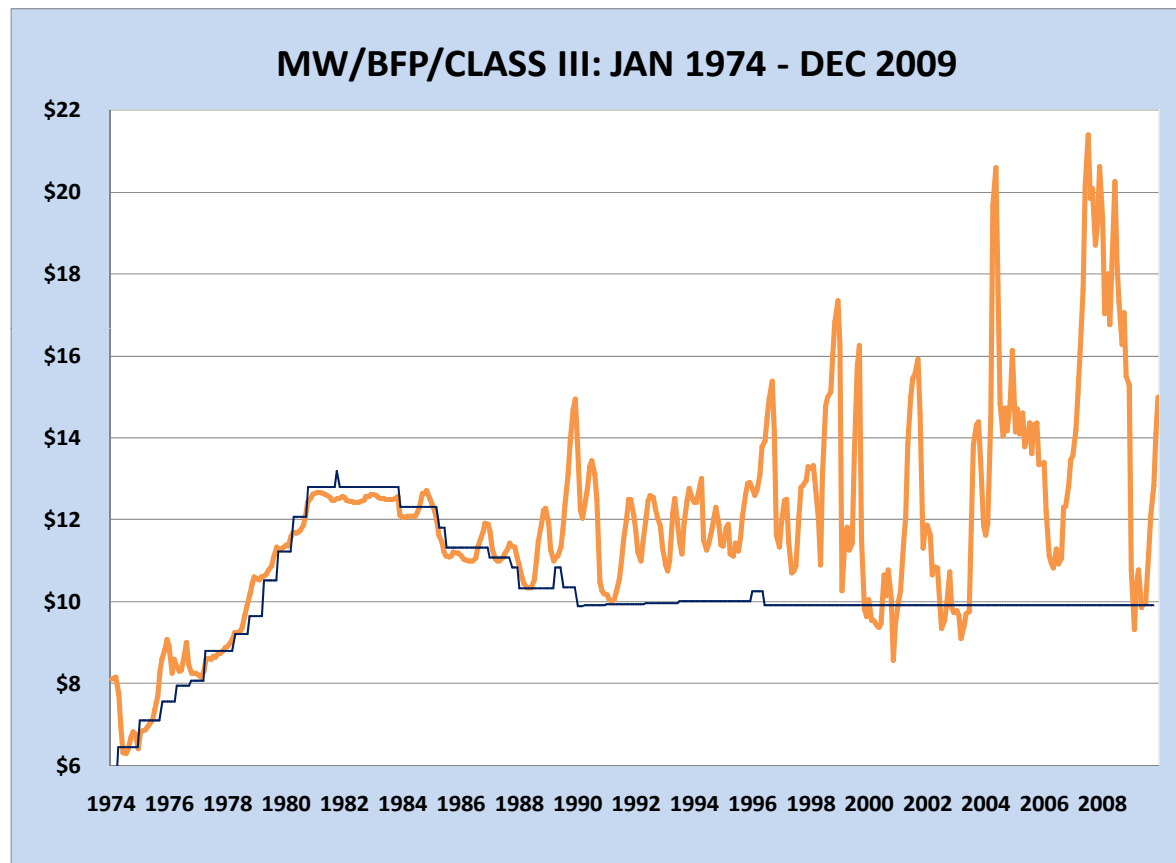
THE CORN MODEL

**FUTURES
MARKET**

INSTEAD . . . WE GET THIS



STILL A COLLECTIVE LEARNING PROCESS



- Compared to other markets, volatility is a relatively new concept in dairy.
- This is not just a reality for producers, but end-users as well.

THANKS FOR YOUR PARTICIPATION

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