8-18-1999

Dairy Options Pilot Program

Rama S. Valluru

University of Nebraska-Lincoln

Valluru, Rama S., "Dairy Options Pilot Program" (1999). *Cornhusker Economics*. 855.
http://digitalcommons.unl.edu/agecon_cornhusker/855

Cornhusker Economics

Dairy Options Pilot Program

Market Report	Yr Ago	4 Wks Ago	8/13/99
Livestock and Products, _Average Prices for Week Ending_			
Slaughter Steers, Ch. 204, 1100-1300 lb Omaha, cwt..	$60.63	$63.83	$65.04
Feeder Steers, Med. Frame, 600-650 lb Dodge City, KS, cwt.	69.88	86.50	*
Feeder Steers, Med. Frame 600-650 lb, Nebraska Auction Wght. Avg.	*	*	90.20
Carcass Price, Ch. 1-3, 550-700 lb Cent. US, Equiv. Index Value, cwt..	97.07	98.84	101.26
Hogs, US 1-2, 220-230 lb Sioux Falls, SD, cwt.	36.35	29.50	34.75
Feeder Pigs, US 1-2, 40-45 lb Sioux Falls, SD, hd.	*	*	21.56
Vacuum Packed Pork Loins, Wholesale, 13-19 lb, 1/4" Trim, Cent. US, cwt. . . .	111.60	109.30	122.80
Slaughter Lambs, Ch. & Pr., 115-125 lb Sioux Falls, SD, cwt.	80.43	81.50	88.07
Carcass Lambs, Ch. & Pr., 1-4, 55-65 lb FOB Midwest, cwt.	162.50	172.00	183.50
Crops, _Cash Truck Prices for Date Shown_			
Wheat, No. 1, H.W. Omaha, bu.	2.67	2.60	2.80
Corn, No. 2, Yellow Omaha, bu.	1.79	1.60	1.71
Soybeans, No. 1, Yellow Omaha, bu.	5.34	3.93	3.23
Grain Sorghum, No. 2, Yellow Kansas City, cwt.	3.26	2.76	4.22
Oats, No. 2, Heavy Sioux City, IA , bu.	*	*	1.12
Hay, _First Day of Week Pile Prices_			
Alfalfa, Sm. Square, RFV 150 or better Platte Valley, ton.	*	87.50	57.50
Alfalfa, Lg. Round, Good Northeast Nebraska, ton.	55.00	*	*
Prairie, Sm. Square, Good Northeast Nebraska, ton.	70.00	*	57.50

* No market.

Dairy producers are more prone to production, marketing and financial risks than ever because they have few marketing alternatives, despite the highly volatile milk prices. Considering the precarious situation that dairy farmers face, USDA's Risk Management Agency (RMA) has launched a novel cost-share program in select states and counties across the nation that allows farmers to try and use futures and options markets. The program, Dairy Options Pilot Program (DOPP), at a cost of $11 million is a first of its kind. Launched under the 1996 FAIR Act, it was first announced on June 8, 1998 by the Secretary of Agriculture, Dan Glickman. The program helps dairy producers to create their own financial safety net by purchasing exchange-traded options on the price of their milk.

Eligibility: Any producer who operates a dairy farm in the selected counties where the program is implemented and produces at least 100,000 pounds of milk over a six-month period is eligible to participate in the program. Apart from the producers, licensed brokers who are in good standing with the National Futures Association (NFA) are eligible for participation.

Program Details: The program is covered for a period of 6-8 months for each producer, during which time each producer will purchase options up to a maximum of 600,000 pounds of milk. The option contract works like a price insurance, i.e., when the milk prices fall below the floor/strike price purchased, the option contract increases in value and the producer gains. This helps the producer cover the price risks in the periods of prolonged low prices that hamper the

cash flow on a farm. The program is highly subsidized by the Department of Agriculture. During the program participation the producer is responsible for 20% of the premium cost of each option and the other 80% of the premium, as well as the broker fee ($30 per option) is picked up by USDA. The program also mandates a 4-hour training program in each county that gives an overview on options, broker selection, dairy market analysis and negotiation of commissions.

The counties and states selected for the first phase of implementation are based on dairy concentration and diversity in operations. The first phase of implementation was done in California, Minnesota, New York, Pennsylvania, Wisconsin, Vermont and Texas. In the second round, 25 other states have been included and the program has been extended to other counties in the states. The first phase has been implemented in Gage county in Nebraska, and has been scheduled for implementation in the second round.

References:

"Announcing the Dairy Options Pilot Program," brochure published by the United States Department of Agriculture, Risk Management Agency, October 1998.

"DOPP Performance Statistics," fact sheet from the United States Department of Agriculture, Risk Management Agency, St. Paul Regional Service Office, July 1999.

S. Rama Valluru, (402) 472-8480
Research Analyst
Dept. of Agricultural Economics

Performance Statistics for First Phase of Implementation (As of July 23, 1999)

State	Active Brokers	Active Producers	Options Adjustments	Options Purchased	Broker Fees $	Producer Subsidies $
CA	4	34		141	4,230	61,744
MN	9	124		542	16,260	209,360
NY	3	35	1	136	4,080	55,936
PA	6	90	5	399	11,970	165,372
TX	2	10		27	810	17,424
VT	1	13		69	2,070	25,216
WI	9	122	1	386	11,550	159,452
TOTAL	**34**	**428**	**7**	**1,700**	**50,970**	**694,504**

Source: Risk Management Agency, USDA (St. Paul Regional Service Office)