MITIGATING RISK IN THE DAIRY SECTOR
2011 USDA OUTLOOK FORUM
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MITIGATE RISKS – THE ISSUES…….

- Price of feed (corn and proteins)
- Dairy exports / dollar valuation
- Global economies / dairy exports
- Debt / leverage
- Liquidity / bank valuations
- Increasing costs (insurance / supplies / energy / etc.)
- Regulations (environmental / regulatory / etc.)

- What can we do to mitigate our risks…….
MITIGATE RISKS – OUR MISSION

+ As a dairy farmer, we (our family) are.....
  ✖ Engaged in the production of high quality milk
  ✖ Develop and maintain a sustainable model to move forward in today’s agricultural climate
  ✖ Understanding challenges of today’s dairy industry
  ✖ Embrace technology
  ✖ Mitigate and minimize risks!!!!

+ We are proud to be dairy farmers.....share with you our farms....
DAIRY FARMS – OVERVIEW

- Northside Farms - Conventional
  - Milking Cows: 5400
  - Ship to Select Milk Producers Inc.
  - Doubled in size in 2002 by moving Central Texas operations to the Texas Panhandle.
  - Strategic move – environmentally friendly area!

+ Mitigate Risks.....Diversify
Dairy Farms – Overview

Diversify - Organic Milk Production

- Natural Prairie Dairy Farms – Organic
  - Milking Cows: Large Scale
  - Build relationship with buyers
  - “Contract Producer”
    - Only produce what is contracted
    - Expansion – 1 year minimum lead time
+ Organic Milk Production
  ❌ Began in 2005 and has consistently grown
  ❌ Demand for product
  ❌ All milk is contracted
  ❌ Regulations / NOP Rules “tedious at best”
  ❌ Major financial investments

❌ Have created a model that is sustainable!!
MITIGATE RISKS - SUPPLIERS

+ Producing a wholesome, fresh product for the consumer is critical
+ Cooperatives strategy
+ Partner with suppliers to know what they want
+ Keeping suppliers happy is key to success for longer term

Natural Prairie Dairy Farms - Supplier of the Year
Northside Farms 1st in Quality (3 years standing)
MITIGATE RISKS – VERTICAL INTEGRATION

Grow as much of your own feed as you can.....

Conventional Farms:
¬ Corn (silage), wheat, alfalfa, sorghum
¬ 5,042 Irrigated Acres

Organic Farm:
¬ Corn (silage and grain), wheat (silage and grain), alfalfa, sorghum, oats, grazing acres (Bermuda/fescue/clover)
¬ 20,059 Irrigated Acres
Grow your own heifers.....

- Better genetics
  - Lower cull rates
  - Better milk production
- Lower cost of replacements
- More control / better management
- Use of sexed semen - more heifers in the system

We grow our own heifers for both conventional and organic operations on two separate heifer raising operations. A total of 17,000 head for the two operations.
MITIGATE RISKS – MANAGEMENT IS KEY!

- Creation of a centralized management company called: AgriVision Farm Management
- Dairy Management
- Farm Management
- Businesses are De Jong family owned/operated
Management is KEY to successful operations – Having the right people in the right positions.

- CEO - Operations
- CFO – Finance
- Farm Managers (2)
- Risk Manager / Feed Purchasing (2)
- Accounts Payable Manager
- Office Manager
- Efficiency/Purchasing Manager
- Human Resource Director
- Interns during summer
- Dairy managers and supervisors – TEAM approach!
Creation of risk management company: Pedestal Commodity Group

- Seeks to manage margins for a dairy entity
- Helps minimize some volatility to bottom line
- Hedging via futures & options on CME
  - Farming (crops)
  - Dairy (milk)
  - Dairy (inputs)
- Cash commodity purchasing and logistics
- Hedging Line of Credit
Business: Supplies and Parts......

- Dairy / farm supplies – bulk ordering of ALL dairy and farm supplies (semi-loads of teat dip..../sprinkler nozzles, etc.)
- Two full time mechanics – loaders, tractors, irrigation pumps, etc.
- Parts hunter/order for equipment parts
- Developed internal software / Equipment # / tracking of all maintenance and repairs.

Make better decisions regarding equipment purchases and when to sell!
MITIGATE RISKS – VOLATILITY

Average annual mailbox price:

- 2007: $17.81/cwt
- 2008: $16.63/cwt
- 2009: $11.36/cwt
- 2010: $15.10/cwt
DAIRY ECONOMICS

Advantage of Feed Coverage in Volatile Markets

- **Covered**
  - Feed: $901,458.00
  - Herd Replacement: $330,480.00
  - Fixed Costs: $438,576.00
  - Principal & Interest: $202,561.25
  - Total: $202,561.25

- **Uncovered**
  - Feed: $1,100,000.00
  - Herd Replacement: $330,480.00
  - Fixed Costs: $438,576.00
  - Principal & Interest: $202,561.25
  - Total: $202,561.25

- Income at $15/cwt: $901,458.00
- Income at $12/cwt: $330,480.00
- Income at $10/cwt: $202,561.25

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Covered vs Uncovered costs under different income scenarios for feed coverage in volatile markets.
MITIGATE RISKS – OUR PHILOSOPHY

- Strategies for long term viability
  + Maintain cash
  + Culling – milk per cow efficiency
  + Interest only real estate notes
  + Create tools to evaluate and project financial expectations
  + Continuously evaluate budget / actual
  + Evaluate equipment repairs / purchasing
  + Don’t ignore the inevitable
Feed costs very high – continuing to rise / many not hedged or positioned adequately
More dairies are filing for bankruptcy
Dairy lenders are “cutting loose” those that have been in special assets for lengthy time period
Not a lot of lending options
Some dairymen are not looking at long term viability
MITIGATE RISKS – FUTURE CHALLENGES

- Health care – increased costs
- Activist groups
- Immigration
- Increased regulation
- Taxes
- Banking/Liquidity in business
  - Will dictate spending/saving on farm
  - Mandated revenue insurance or hedging??
MITIGATE RISKS – FUTURE

Why do dairy farmers do what they do??

- Way of life
- Great lifestyle to raise a family
- Values
- Rural life

Future Generation – We must be an operation that is sustainable in order to be here for the next generation!