

# Rice Dairy LLC

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## About Rice Dairy



## Rice Dairy

- Boutique brokerage firm specializing in dairy
  - GUIDANCE
  - ANALYSIS
  - EXECUTION SERVICES
- Five exchange members executing trades on behalf of the firm's clients
- Along with Chief Market Analyst Jerry Dryer, Rice Dairy publishes **daily** and **weekly reports, periodic price forecasts, and pre-USDA report estimates**

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## How can Rice Dairy help your Farm?

- We help develop and then execute risk management strategies
  - Milk
  - Milk – Feed Margin

**Create a plan that protects your business**

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# Risk Management is for Everyone

Futures/Options trading **is not** for Everyone

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## Various Risk Management Strategies

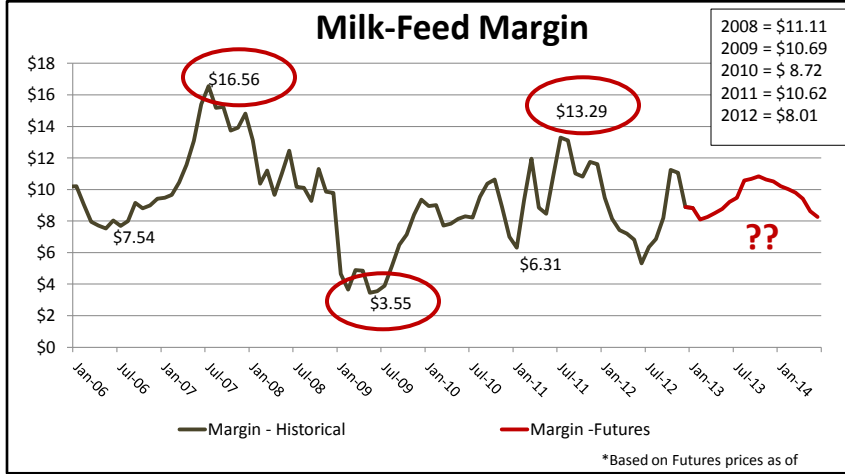
- Futures/Options trading
- Hedging through your coop
- USDA's LGM insurance
- Excellent equity position to 'self-insure'

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# Why Risk Management



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# Some of the Basics

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## What is Basis

**Basis = Farm Price – Class III Price**

- \$2.73 Average for Appalachian Area 2008-2012

Example:

Farm Price	\$20.75
- Class III	\$18.00
<b>= Basis</b>	<b>\$2.75</b>

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## Risk Management Basics

- Futures and Options Markets
  - Each month has a unique price
  - Can book up-to 24 months
    - As little as one month
  - 200,000 lbs of milk per month

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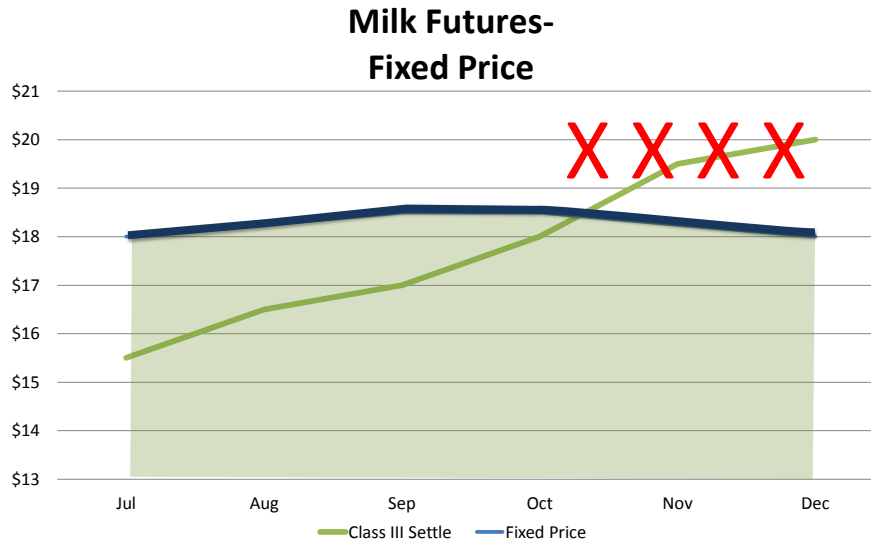
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# Popular Risk Management Strategies



## Futures





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## Margin Account Funding

### Futures

- Initial Margin =
  - Around \$2,000 per contract (200,000 lbs)
    - 6 months, 200,000 per month = \$12,000
- Maintenance Margin =
  - Prices move higher – you owe
  - Prices move lower – credit your account
  - Plan for \$2.00/cwt
    - 6 months, 200,000 per month = \$24,000

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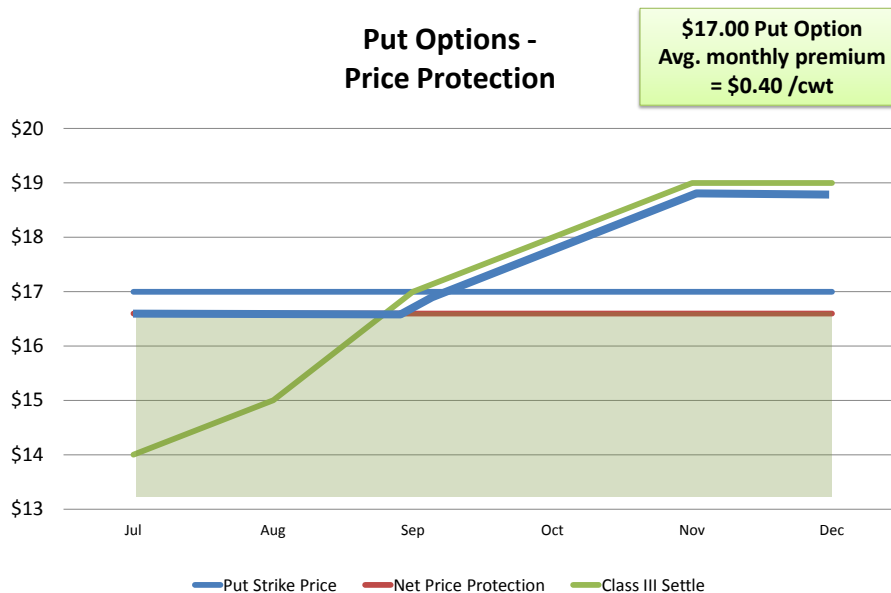
# Options



# Put Options







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## Margin Account Funding

### Buying Put Options

- Initial Margin =
  - Premium Amount
    - 6 months, 200,000 per month @ \$0.45 = \$5,400
- Maintenance Margin = NONE
  - Prices move higher – you owe nothing
  - Prices move lower – credit your account

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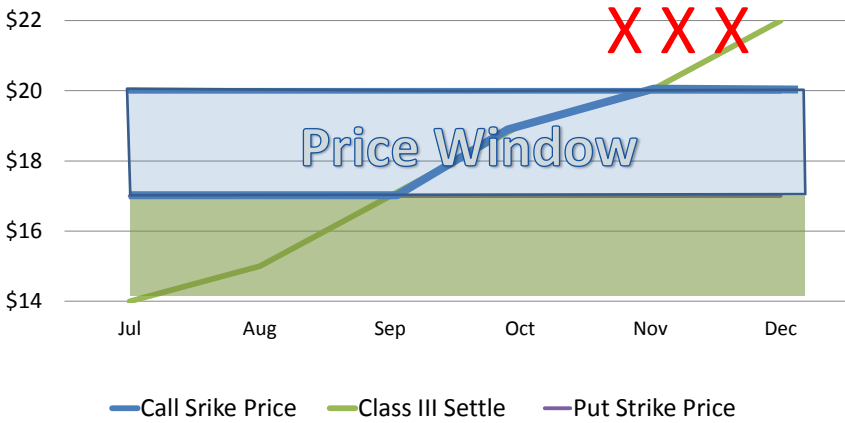
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# Put and Call Option



**Put & Call Options -  
Price Protection & Price Ceiling**

**\$17.00 Put & \$20.00 Call  
Avg. monthly premium  
= \$0/mo**



## Margin Account Funding

### Buy Put & Sell Call

- Initial Margin =
  - Around \$1,500 per contract (200,000 lbs)
    - 6 months, 200,000 per month = \$9,000
- Maintenance Margin =
  - Prices move higher – you owe
  - Prices move lower – credit your account
  - Plan for \$2.00/cwt
    - 6 months, 200,000 per month = \$24,000

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## Milk – Feed Margin

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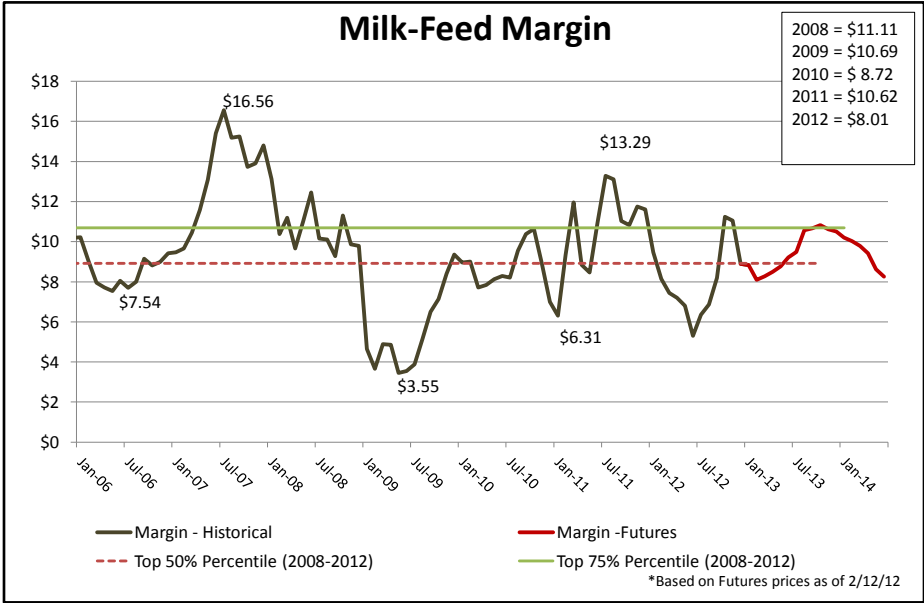


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# Milk-Feed Margin

- Default established from several ‘typical’ rations
- Computed energy and protein in entire ration into corn and soybean meal equivalents
  - Backed out hay
  - Hedge protein and energy
- Can easily create specific margin for your farm

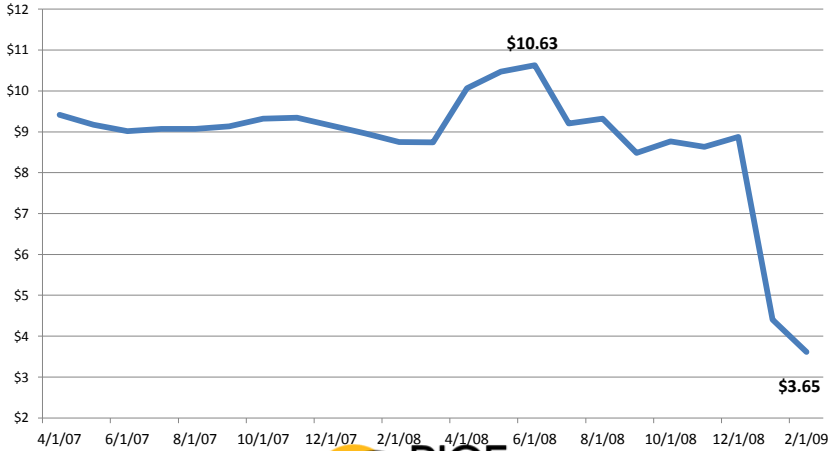
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# Historical Perspective

Feb '09 Margin Trade Data



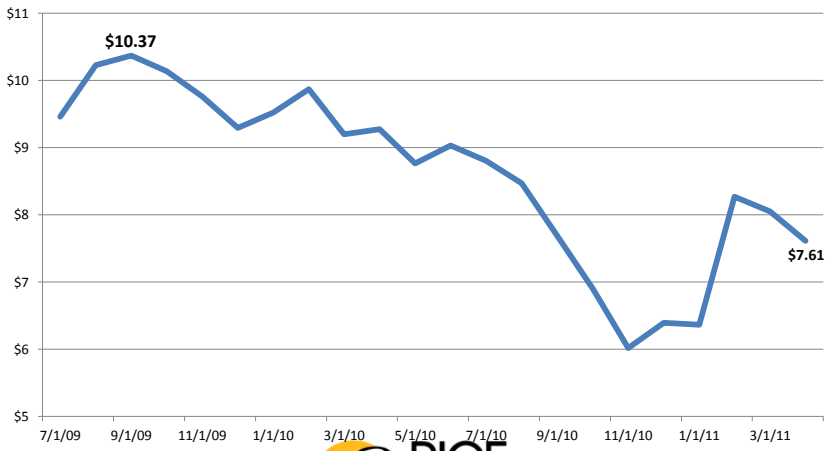
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# Historical Perspective

May '11 Margin Trade Data



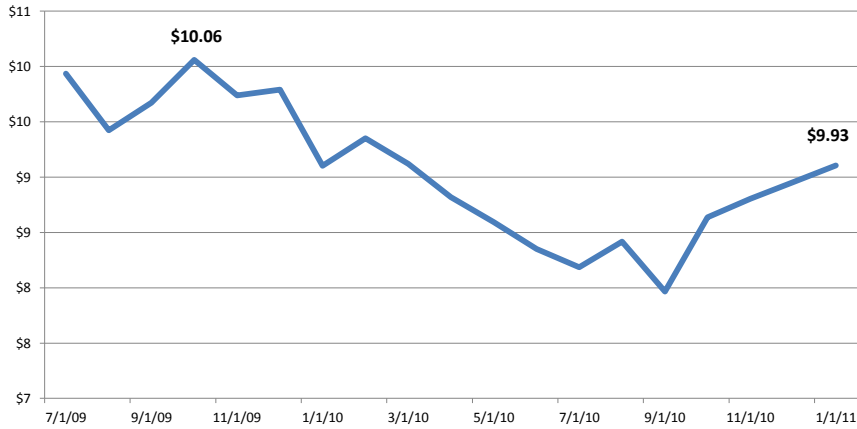
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# Historical Perspective

Oct '11 Margin Trade Data



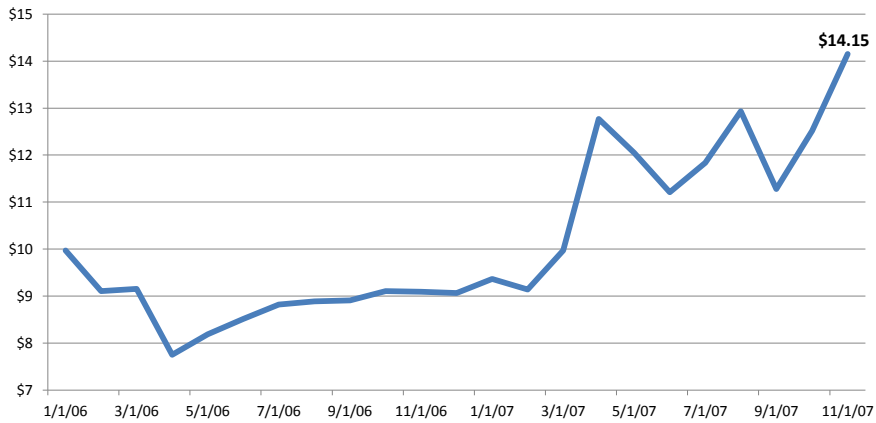
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# Historical Perspective

Dec '07 Margin Trade Data



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# September 2013 Margin



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## Some words of caution...

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## Be Consistent

You can't beat the market.

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## Avoid **Fear** and **Greed**

**Fear** will make you hedge when you shouldn't  
**Greed** will make you not hedge when you should

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# Avoid Price Projections

They are not guarantees  
They will not protect your business

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## Disclaimer

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# Our Goal is to Protect Your Business

Questions/Discussion

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## Trading on the CME

### Pros

- Work with a broker
  - Get advice
- Flexibility to get in and out of the market
- Can contract 100+ percent
- Broker fees

### Cons

- Contract size set by CME
- Must fund margin account
- Broker fees

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## Cooperative or Milk Plant

### Pros

- **No money upfront**
  - No margin account
- Contract size is flexible
  - Great for smaller dairies
- Simple

### Cons

- Fees
- Can not get in and out of contracts
- Contract amount is limited

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## LGM

### Pros

- Protects the milk:feed margin
- Flexible contract size
  - Great for smaller dairies
- Payment due at end
- Subsidized

### Cons

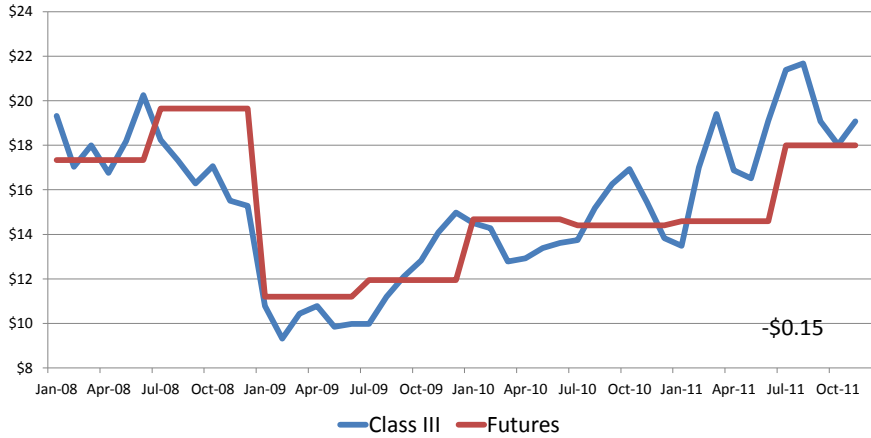
- Not available
- When available, only able to book once a month
- Not flexible
- Payment based on average
- Payment paid at end

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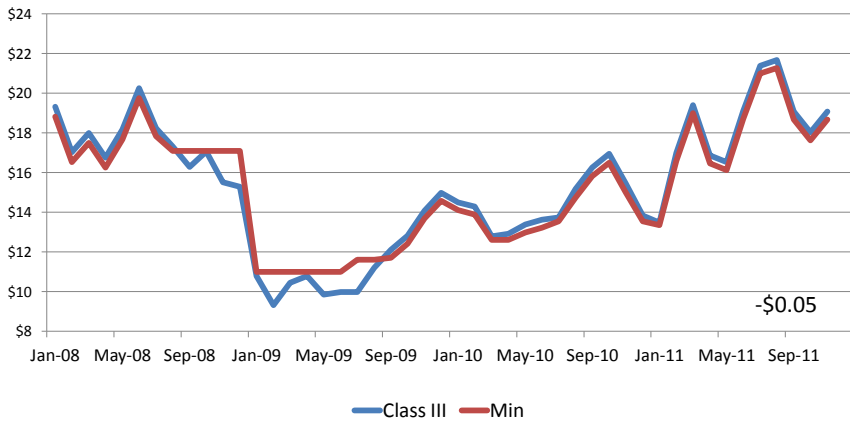
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## Class III vs. Futures



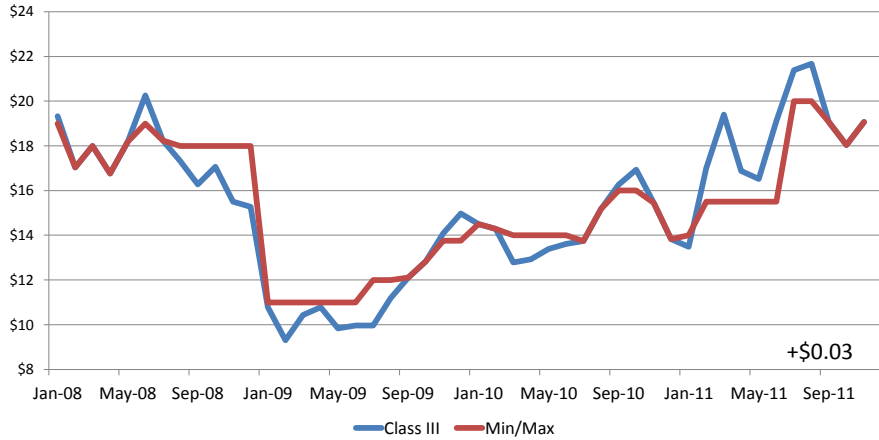
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## Class III vs. Buying Put Options



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## Class III vs. Min/Max



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Trade Date	4/2/07	10/1/07	4/1/08	10/1/08	4/1/09	10/1/09	4/1/10	10/1/10	4/1/11		
Contract Month	10/1/07	4/1/08	10/1/08	4/1/09	10/1/09	4/1/10	10/1/10	4/1/11	10/1/11	Avg. Cost	
Premium (\$/cwt)											
Class III Put Price	\$13.00	0.05	0.06	0.01	0.19	0.27	0.30	0.19	0.33	0.07	0.16
	\$14.00	0.19	0.21	0.05	0.42	0.54	0.66	0.46	0.77	0.18	0.39
	\$15.00	0.48	1.13	0.14	0.78	0.96	1.21	0.90	1.45	0.37	0.82
Class III Settlement											
	\$18.70	\$16.76	\$17.06	\$10.78	\$12.82	\$12.92	\$16.94	\$16.87	\$18.03		Avg. Gain
Put Option	\$13.00	0.00	0.00	0.00	2.22	0.18	0.08	0.00	0.00	0.00	0.28
Gain (premium not included)	\$14.00	0.00	0.00	0.00	3.22	1.18	1.08	0.00	0.00	0.00	0.61
	\$15.00	0.00	0.00	0.00	4.22	2.18	2.08	0.00	0.00	0.00	0.94

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