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MITIGATING RISK IN THE DAIRY SECTOR  
2011 USDA OUTLOOK FORUM  
CHERI DE JONG  
FEBRUARY 25, 2011

# MITIGATE RISKS – THE ISSUES.....

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- ✖ *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

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- + 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....





WELCOME



# DAIRY FARMS – OVERVIEW

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## ✕ 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

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## 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











# MITIGATE RISKS - DIVERSIFICATION

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## + 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

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- + 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 1<sup>st</sup> 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



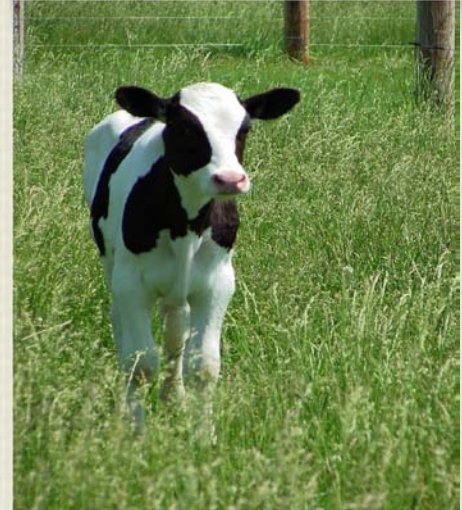




# MITIGATE RISKS – VERTICAL INTEGRATION

## + 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



# MITIGATE RISKS – EFFECTIVE MANAGEMENT

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+ 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!

# MITIGATE RISK – RISK MANAGEMENT

- ✖ 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



# MITIGATE RISKS – SUPPORTING ENTERPRISES

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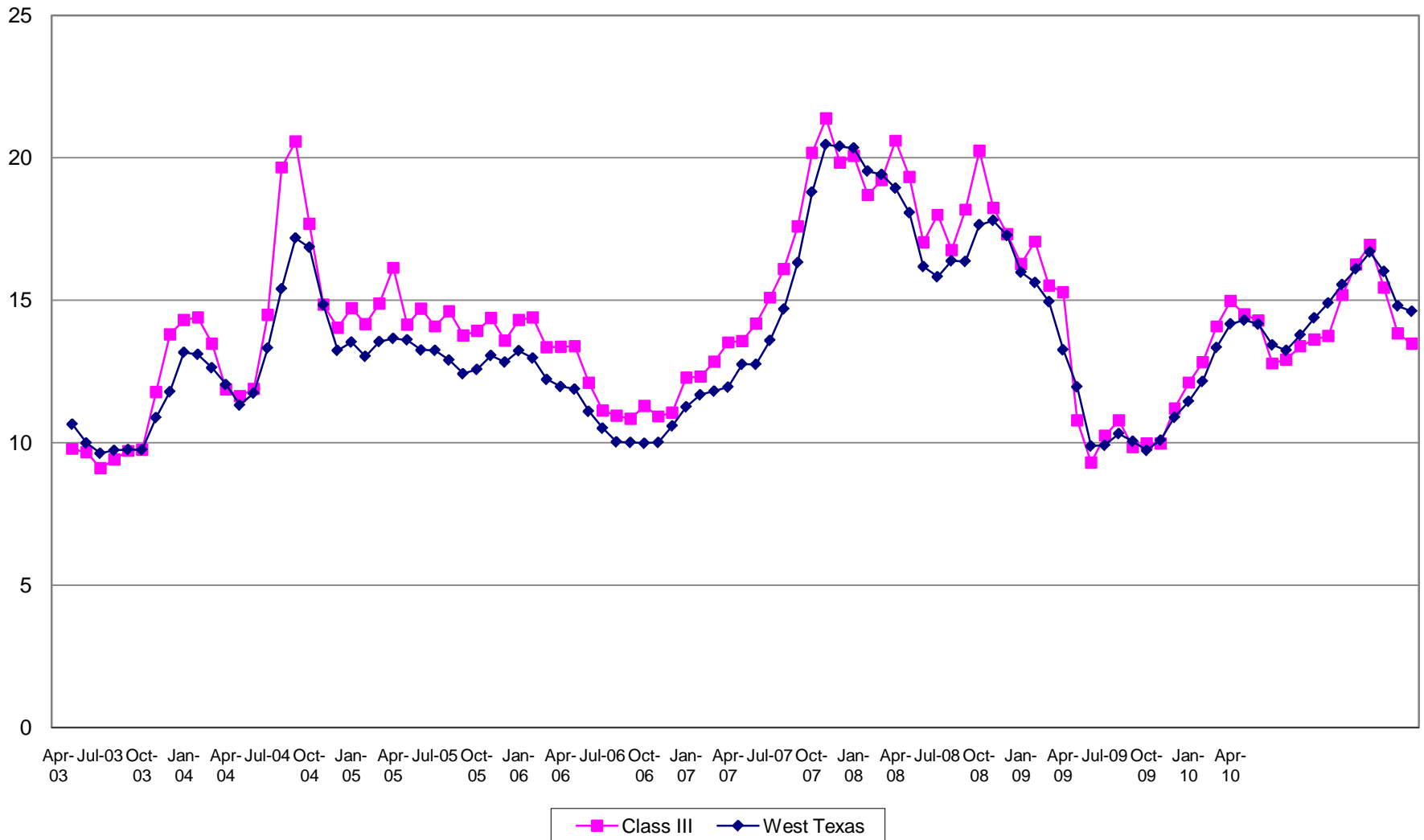
## + Business: Supplies and Parts.....

- ✗ 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 – MILK PRICES

WTX vs. Class III





# MITIGATE RISKS – VOLATILITY

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Average annual mailbox price:

2007	\$17.81/cwt
2008	\$16.63/cwt
2009	\$11.36/cwt
2010	\$15.10/cwt

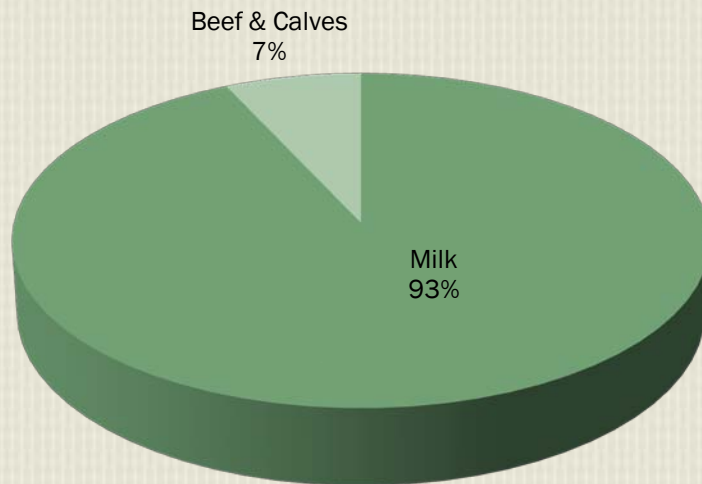


# MILK REVENUE MINUS FEED COST (\$/CWT)

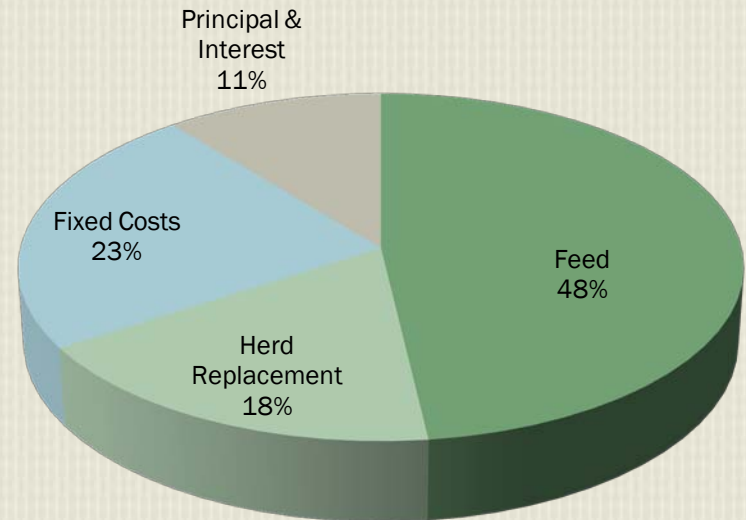


# DAIRY ECONOMICS

## Dairy Income

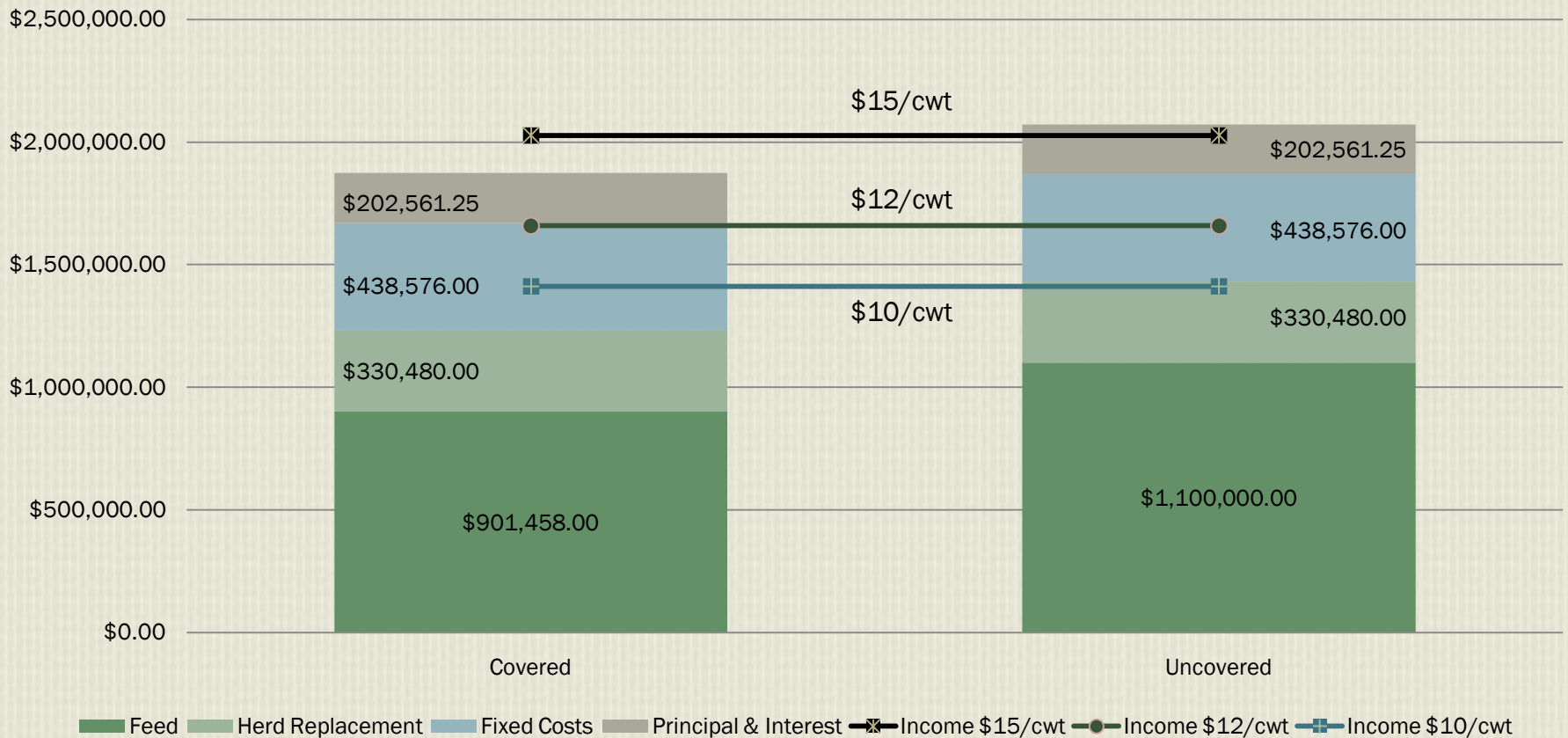


## Dairy Expenses



# DAIRY ECONOMICS

## Advantage of Feed Coverage in Volatile Markets



# MITIGATE RISKS – OUR PHILOSOPHY

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- ✖ 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

# MITIGATE RISKS – MOVING FORWARD

- ✖ 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

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+ 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!**

