

Dairy Options Program In Your Mailbox

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seven states have been selected to participate during the first six-month period. Other states that have counties participating include: California, Minnesota, New York, Texas, Vermont, and Wisconsin. Selection was based on those counties and states that have a high dairy concentration. Funding has been approved for a three-year program so hopefully other counties in Pennsylvania can be included after this initial round.

If you receive a letter from Risk Management/USDA, please take a few minutes and read it carefully! It will provide details about this program along with instructions on how you sign up to participate. From the time you receive the letter, you will have approximately two weeks to return the registration form. If you have questions about the information in the letter, do not hesitate to contact your local Penn State Extension office.

If a producer chooses to participate, they will need to attend a four-hour training program in late August or early September where the final details of the program will be explained. This program will be limited to 100 producers per county.

Just what is the DOPP? The Dairy Options Pilot Program allows USDA to help share the cost of brokerage fees and option premiums that you would purchase to set a floor price for your milk. This allows producers to gain

some education and experience in using options without spending much money. During the six-month period, if your county is selected to participate, you may purchase option contracts on up to 600,000 pounds of production. USDA will then pay 80 percent of the premium cost for the option and \$30 of brokerage fees for each transaction. The minimum amount that needs to be contracted during the six months of the program is only 100,000 pounds. This allows both large and small producers to participate in the program.

What is an option, you ask? A BFP milk option allows the holder (producer) the right to sell a BFP contract at a guaranteed minimum floor price while still providing for upside potential, should the market move upward unexpectedly. This type of option is referred to as a "Put" and is used to protect you from falling prices. An easy way to think of options is that they are similar to insurance. The better the policy, the more it costs. An option for \$13 BFP milk will cost more per cwt. than an option for \$11.75. What if the BFP is above my option price when the contract ends? If this happens, then your contract expires and you are fortunate to receive the higher cash market price. Similarly, if you have car insurance and do not have an accident, your policy expires without you collecting any money.

What price options can I pur-

chase with this program? Options are available in 25-cent increments above and below the current BFP or strike price for a given month. You will be allowed to purchase options that are at least 10 cents below the current BFP strike price. For example, if the August BFP is \$13.54, then you may purchase options from \$11.50 to \$13.35. This would then provide a floor price on the amount of milk in the option contract.

How do I initiate an option contract? Once producers have completed their training session in August or September, they will be given a list of brokers who are approved to help you work with BFP options. You can then decide what portion of production for which you'd like to purchase an option. No more than 200,000 pounds may be hedged in any one month. Each option contract must be held for a minimum of two months. For example, if it is September and you want to take a Put option under this program, you will need to work with December '98 or early '99 contracts.

Option contracts come in different sizes depending on which trading exchange you work with. BFP contracts are traded daily on the Coffee, Sugar & Cocoa Exchange in New York and at the Chicago Mercantile Exchange in Chicago. Contracts on the Coffee Exchange are in 100,000-pound increments while contract sizes at the Mer-

cantile Exchange are 50,000 pounds and 200,000 pounds.

If I participate in this program, does it change the way I get paid from my milk company or cooperative? Absolutely not. Your milk is still marketed as always and your milk check from your milk buyer will not change. Should the futures BFP price drop below your option floor price, you would receive money from your option account. That money combined with your cash price would equal your floor price.

Both trading exchanges have excellent educational material, available at no cost, that help to explain BFP futures and options trading. Information can be obtained from the Chicago Mercantile Exchange by calling (312)

930-1000, or from the Coffee, Sugar & Cocoa Exchange at (212) 742-6100. The Coffee exchange also has a free book available entitled: From Price Taker to Price Maker. This easy to read book discusses BFP hedging and provides numerous examples for you to follow.

If you are one of the six selected counties, be watching your mail for DOPP details. Any producers in PA who have questions on this program are encouraged to contact their county Extension office for additional information. Additional contact persons would be Glenn Shirk, Lancaster County Extension Office (717) 394-6851, and Larry Swartz or Larry Yager, Adams County Extension Office (717) 334-6271.



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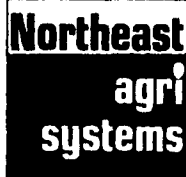


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