

CWT PRODUCTION REDUCTION PROGRAM BIDS

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Producers only have until August 22, 2003 to submit a bid under this program. Payments will be based on the amount bid per 100 lb and the reduction in sales relative to a base period. The rules and application forms are available at <http://www.cwt.coop>.

Many factors affect the size of the bid (program payments) that would make this program financially attractive, including: (1) The expected reduction in milk sales needed to qualify for payments, (2) The methods used to reduce milk sales and the associated out-of-pocket cost savings, (3) The effects on net income after the program payments end, for example the costs of rebuilding the herd and reduced income because of lower milk sales during the rebuilding program. I recommend the following partial budgeting approach to estimating the cost to the producer of participating in the program and to help determine the size of the bid.

1. Establish the farms quarterly milk sales during the October 1, 2002 through September 30, 2003 period, i.e., Oct-Dec, Jan-Mar, Apr-Jun, Jul-Sep. Each quarter is the production base for the contracted reduction and both the quarterly and annual targets must be met.
2. The program period for reduced sales is October 1, 2003 through September 30, 2004. However, most farms increase production year-by-year. Estimate future milk sales if the farm does NOT participate in the CWT production reduction program, based on existing cow and heifer numbers, reproduction status, expected culling rates and death loss, and projected milk production per cow.
3. Select a contract percent reduction (10% to 50% in 10% increments) relative to 10/1/02--9/30/03 sales and calculate the maximum quarterly sales that would be permitted.
4. Calculate the quarterly reduction in sales needed to meet the contract. This is the difference between projected sales and the permitted sales under the contract (item 2 minus item 3).
5. Calculate the value of this reduction in milk sales based on the expected mailbox prices of milk for each quarter. This is the estimated milk income that will be given up.
6. Consider the alternative methods available to reduce production to meet the contract. These methods include culling, early drying off and an extended dry period, changing from 3X to 2X milking, adjusting the feeding program for cows and heifers, adjusting the breeding dates, deferring planned purchases of cows or heifers, using milk for calves. These methods may be used singly or in combination. Cows may not be sold for dairy purposes.
7. Estimate the out-of-pocket cost savings based on the selected method(s) of reducing milk sales. For example, early culling of low producers will cut feed costs but low producers eat

less than high producers and dry cows must be fed. There should be a reduction in milking times but this will only cut actual hired labor costs if workers are paid for fewer hours. There will be some savings in utility costs. Do not include cull cow sales income because this is income would be received anyway; allow for differences in cull value based on time of sale.

8. Additional costs might be incurred at the end of the program if a producer intends to regain the milk production given up, e.g., by adding cows to the herd. These “costs” might include 1) The appropriate costs related to buying or rearing additional animals and 2) Net income lost during the rebuilding period, based on the estimated difference between the net income during rebuilding period relative to net income if the producer had stayed out of the program.
9. Calculate the total estimated impact on net income that will be lost by participating, net of cost savings, using items 5, 7 and 8. Calculate the bid necessary to breakeven by dividing the total cost by the contracted reduction in the farm sales (item 3). Use this breakeven figure as the basis for determining the actual bid per 100 lb. to be submitted. Other factors will influence the actual size of the bid, including a margin for error, an inducement to participate, and the desire to have the bid accepted.

We cannot generalize about who would benefit from the program because there is too much variation from farm-to-farm. Each producer should figure the impact on his or her herd. However, we can see how certain factors might affect the likelihood of participation.

Likelihood of Participation

Higher likelihood	Lower likelihood
If expected production is <u>lower</u> than program history or has increased little.	If expected production is significantly <u>higher</u> than program history.
If the projected mailbox price per 100 lb. is <u>low</u>	If the projected mailbox price per 100 lb. is <u>high</u>
If out-of-pocket expenses are <u>high</u> relative to price received for milk.	If out-of-pocket expenses are <u>low</u> relative to price received for milk.
If home produced feed is <u>short</u>	If home produced feed is <u>plentiful</u>
If the herd is largely a <u>grade</u> herd selling few cattle for dairy purposes.	If the herd is largely <u>registered</u> cattle <u>and</u> female cattle sales are substantial.
If dairyman is currently milking 3X	If dairyman is currently 2X
If dairyman has <u>plenty</u> of heifers of the right ages for rebuilding or if projected heifer prices are low.	If dairyman has <u>few</u> heifers available for rebuilding or if projected heifer prices are high.
If dairyman is planning to sell out soon or will be forced to sell out.	If dairyman is not planning to sell out and is financially sound.