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What is Dairy Margin Protection Program and How Has it Worked?

BACKGROUND

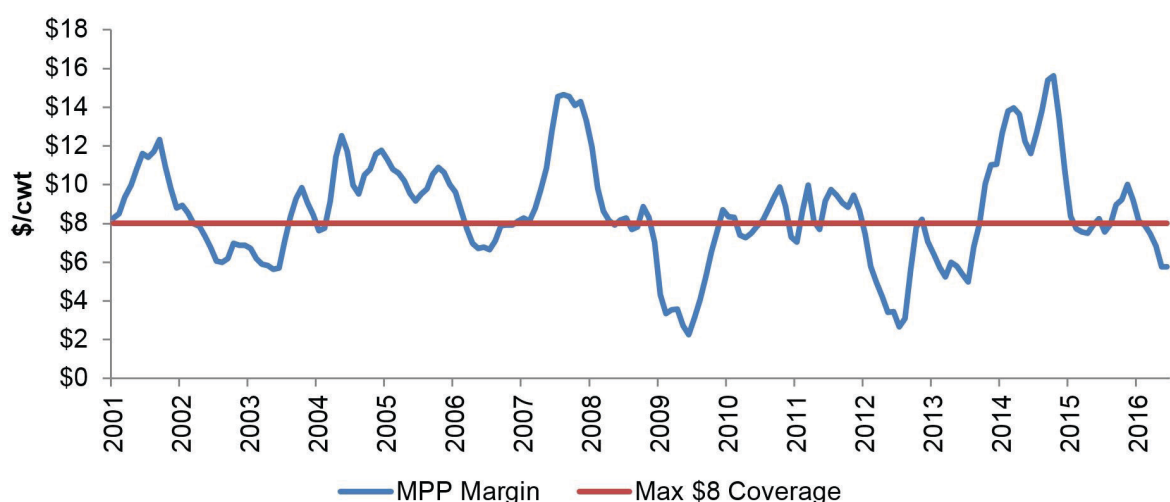
The Dairy Margin Protection Program (MPP) is a voluntary program that makes payments when the national average income-over-feed-cost (IOFC) margin index falls below a farmer-selected coverage level. Different coverage options reflect a dairy farmer's ability to protect different margin levels. Dairy producers pay premiums for coverage and must take an active role in selecting their coverage options each year.

MPP is based on an IOFC margin defined as the difference between the national average all-milk price and the formula-derived estimate of total herd feed costs. The MPP margin is calculated as:

$$\text{Milk Price} - [1.0728 \times (\text{corn price/bu}) + 0.00735 \times (\text{soybean meal price/ton}) + 0.0137 \times (\text{alfalfa hay price/ton})]$$

(The milk price is the National Agricultural Statistics Service (NASS) announced U.S. all-milk price per hundredweight (cwt), the corn price is the NASS announced corn price per bushel, the soybean meal price is the USDA Agricultural Marketing Service announced Central Illinois high protein soybean meal price per ton, and the alfalfa hay price is the NASS announced alfalfa hay price per ton.)

MPP Margin (Milk Price Minus Feed Costs), 2001 to May 2016



Payments are made when the MPP margin falls below a farmer-selected coverage level that ranges from \$4.00 to \$8.00 per hundredweight (cwt) in 50 cent increments. To determine the payment, MPP margins are averaged for consecutive two-month intervals such that up to six payments are possible each calendar year. Consecutive two-month periods are defined as January-February, March-April ..., November-December. In order to participate, farm operations must pay a \$100 annual administrative fee. This fee provides dairy producers with catastrophic coverage of \$4.00 per cwt. Additional margin protection on levels above \$4.00 per cwt can be selected by participating dairy

farmers at supplementary costs. Premium rates are fixed for the life of the 2014 Farm Bill, but are structured at a lower tier (Tier 1) for the first four million pounds of covered production. A 25 percent premium discount was mandated for 2014 and 2015 for Tier 1 rates for all coverage levels except the \$8.00 level.

MPP-Dairy Premiums and Administrative Fees		
MPP-Dairy Coverage Level	Actual Tier 1 Premium (2016-18)	Actual Tier 2 Premium
Administrative Fee in Dollars	\$100	
\$/hundredweight		
\$4.00	\$0.000	\$0.000
\$4.50	\$0.010	\$0.020
\$5.00	\$0.025	\$0.040
\$5.50	\$0.040	\$0.100
\$6.00	\$0.055	\$0.155
\$6.50	\$0.090	\$0.290
\$7.00	\$0.217	\$0.830
\$7.50	\$0.300	\$1.060
\$8.00	\$0.475	\$1.360

Once enrolled in MPP, participating dairy operations may not opt-out of the program. However, during the open enrollment period each year, dairy operations may change their level of MPP protection and how much milk is covered for the following calendar year. The open enrollment period occurs each year from July 1 to September 30. Dairy farmers may purchase coverage on 25 to 90 percent of their milk production history in five percent increments. The dairy farm's production history is defined as the highest level of annual milk production during the 2011, 2012, or 2013 calendar years. In subsequent years, USDA will update a farm's production history to reflect the increase in national average milk production.

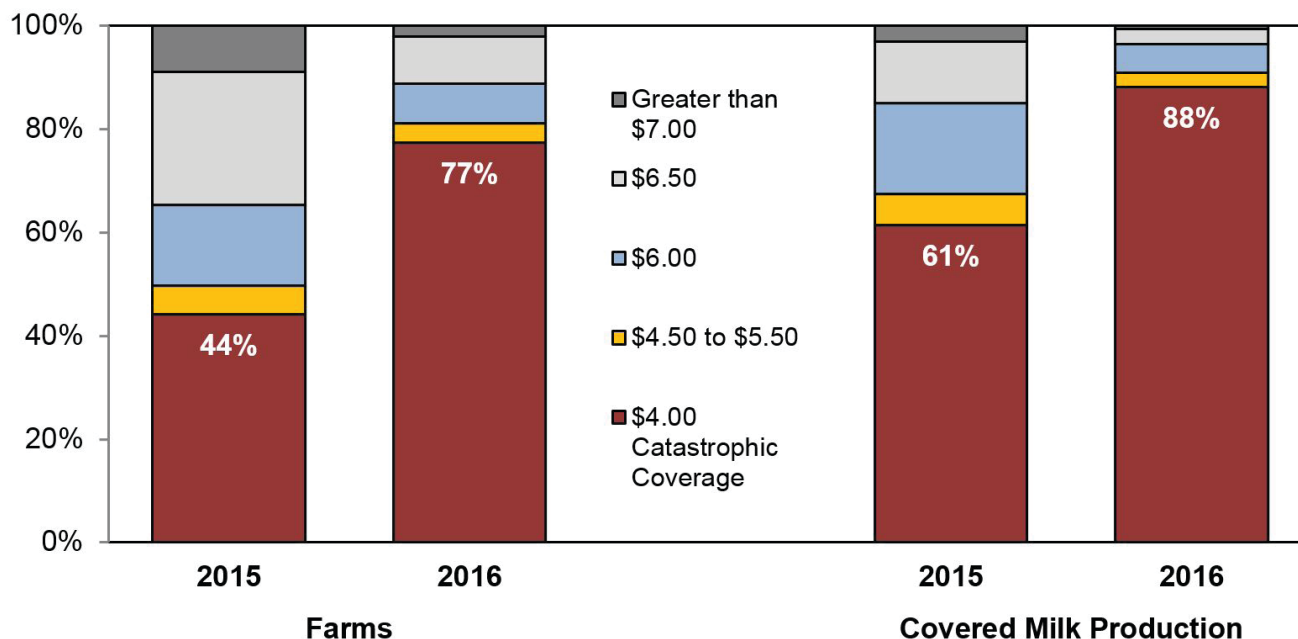
Program Participation:

In 2015 (the first full year of enrollment), about 24,000 dairy operations participated in the program. These farms represented about 50 percent of the licensed dairy operations and 80 percent of the U.S. total milk supply. Of the operations participating in MPP, 55 percent of farmers opted to purchase supplemental coverage above \$4.00 per hundredweight. About \$73 million was collected in MPP premiums and administrative fees. During 2015, the annual average MPP margin was \$8.35 per hundredweight and ranged from a low of \$7.50 in March and April 2015 to a high of \$9.55 per hundredweight in November and December 2015. As a result, only those dairy operations enrolled at the \$8.00 supplemental coverage option received a program payment. A \$700,000 indemnity was paid to the 264 dairy farmers who insured at the \$8.00 coverage level.

The 2016 participation in MPP was similar to 2015 in terms of the volume of milk enrolled in the program and the number of participating farms. However, fewer dairy farmers elected to purchase buy-up MPP coverage and instead opted to participate at the minimum catastrophic \$4.00 level. About \$23 million in premium and administrative fees was collected from dairy farmers. As of July 2016, the MPP margin fell to a low of \$5.75 per hundredweight. In August 2016, USDA announced an MPP payment of \$11.2 million to farmers participating at the \$6.00 level and above.

MPP Participation by Coverage Level for 2015 and the First Half of 2016

Percent of Farms or Production



Actual and estimates of premiums paid into MPP and program payments by coverage level (based on July 20, 2016 USDA projected MPP margins)						
Coverage Level	Number of Farms in 2015	Total MPP Premiums and Admin Fees in 2015	MPP Payments Made to Farmers in 2015	Number of Farms in 2016	Total MPP Premiums and Admin Fees in 2016	Estimate of MPP Payments Made to Farmers in 2016
\$8.00	264	\$3,369,992	\$727,831	138	\$1,007,442	\$1,033,267
\$7.50	1,430	\$7,744,556	\$0	225	\$1,175,433	\$1,280,959
\$7.00	501	\$1,468,205	\$0	158	\$546,430	\$474,799
\$6.50	6,397	\$24,008,345	\$0	2,184	\$6,200,826	\$5,475,358
\$6.00	3,850	\$31,284,784	\$0	1,877	\$10,194,428	\$3,210,940
\$5.50	506	\$1,726,101	\$0	342	\$543,918	0
\$5.00	743	\$2,101,739	\$0	463	\$1,194,619	0
\$4.50	136	\$71,693	\$0	405	\$43,135	0
\$4.00	10,939	\$1,093,900	\$0	18,801	\$1,880,100	0
TOTAL	25,162	\$72,869,315	\$727,831	24,292	\$22,786,331	\$11,475,323

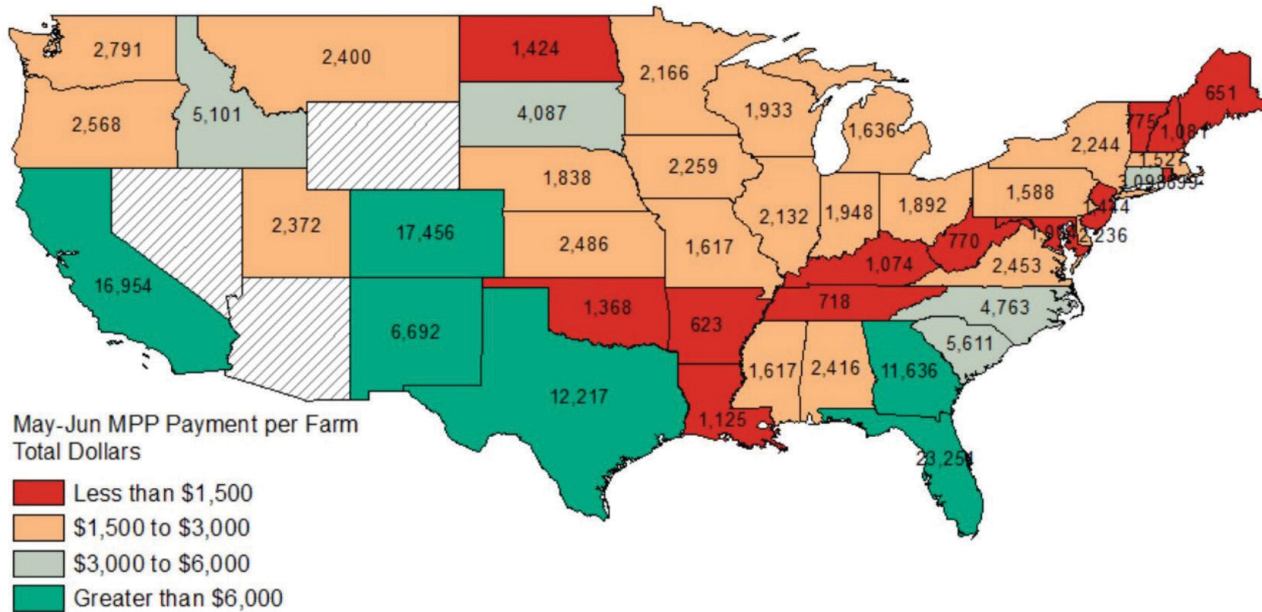
USDA Modifications to MPP:

- USDA extended the sign-up deadline for participation in both 2015 and 2016. The sign-up extension allowed farmers to better observe the risk environment in milk and feed prices to make more informed risk management decisions.
- USDA also altered the program to allow MPP premiums to be an authorized deduction from farmers' monthly milk checks. This reduced the financial burden and cash flow constraints that had been associated with paying MPP premiums in lump sum payments by specific deadlines.
- USDA provided participating dairy operations an opportunity to update their milk production history to accommodate intergenerational transfers. This allows new family members to join the farm and allows farms to purchase additional MPP coverage to accommodate the growth in the dairy operation.

- USDA modified the coverage levels under MPP to decouple \$4.00 and supplemental coverage options. The decoupling provides all participating operations with the \$4.00 catastrophic coverage on 90 percent of the milk production history and allows farms to cover a different volume of milk at supplemental coverage levels.

MPP has collected nearly \$100 million in farmer premiums and administrative fees during the first one and one-half years of the program. Indemnities and payments have been approximately \$12 million for the same time period.

Average MPP May-June 2016 Payments Per Farm Receiving Benefits (Does Not Include Premiums & Administrative Fees)



Options Papers on MPP include:

- How does MPP Catastrophic Coverage Compare to and Crop Catastrophic Coverage?
- Should the MPP Feed Ration be Increased by 10 Percent?
- Should MPP Premium Rates be Adjusted?
- Using State Data to Calculate Feed Costs for MPP
- What are the Differences Between MPP and LGM-Dairy?