Improving Your Dairy Farm Bottom Line by Using Price Risk Management

- The Livestock Gross Margin Insurance for Dairy Cattle (LGM-Dairy) is a federally reinsured insurance program that enables US dairy producers to establish minimum levels of milk income net of feed cost.
- Since December 2010 the LGM-Dairy has large premium subsidies that incentive its use as a price risk management tool.
- Given the structure of the program there are an infinite number of possible contract designs based on the choice of deductibles and proportion of production insured.
- Producers may adopt the use of this program depending on their risk preferences and the interplay of these preferences with the level of subsidization.

- LGM-Dairy contracts under different levels of subsidy and farmers' risk preferences were studied to find out contract designs farmers would most likely choose.
- This paper then studied the interplay between farmers' risk preferences, LGM-Dairy contracts, and premium subsidization in determining contracts.

The study found that:

1) Premium subsidy will largely increase the demand for it.
2) Total coverage would significantly increase with farmers' risk aversion.
3) The impact of farmers' risk aversion would diminish with higher deductible and higher subsidization

Excerpt from: Valvekar, M., J. P. Chavas, B. W. Gould,and V. E. Cabrera. 2011. Revenue risk management, risk aversion and the use of Livestock Gross Margin for Dairy Cattle insurance. Agricultural Systems 104:671-678.

RESOURCES

Victor E. Cabrera,
Assistant Professor
Extension Specialist in
Dairy Management
Dairy Science
608-265-8506
1675 Observatory Drive
Room 279
Madison, WI 53706

Brian W. Gould
Associate Professor
Agricultural and Applied
Economics
608-263-3212
427 Lorch St.
Madison, WI 53706

WEB

DairyMGT.info

Futures.aae.wisc.edu

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