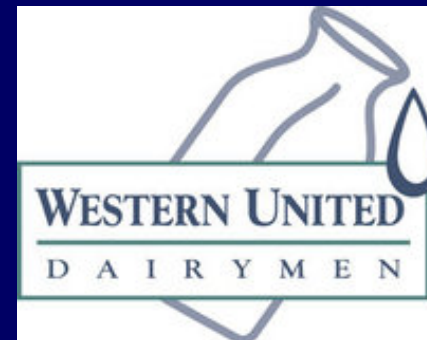




Dairy Financing Conference

February 22, 2011

Sponsors

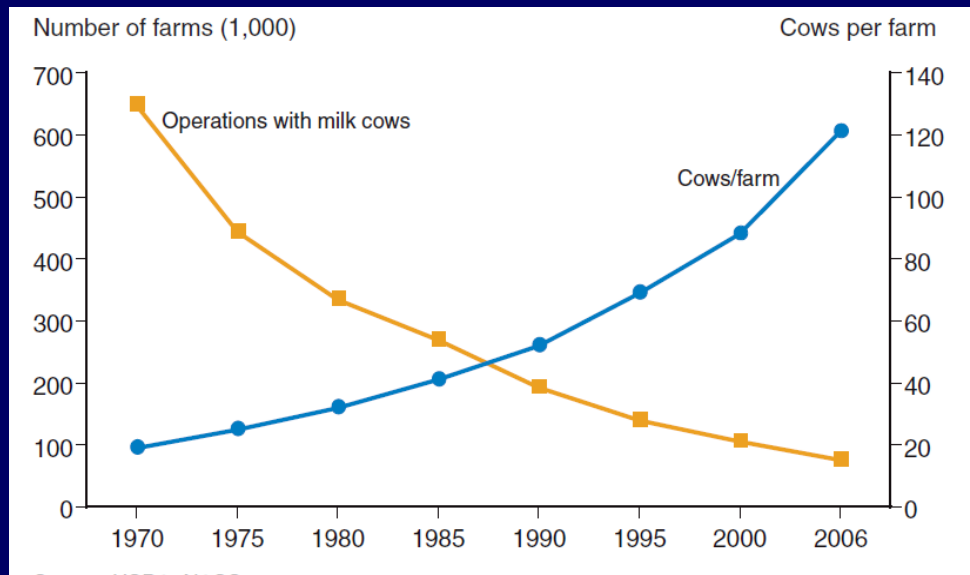


California- The Nations' Dairy Leader

- Dairy farming is the leading agricultural commodity in California producing \$4.5 billion in sales in 2009 with an economic impact of \$63 billion in economic activity and generating 443, 574 full time jobs (2008)
- 1,750 dairy farms house 1,879 million milk cows
- Largest producer of milk (20% of US), butter, ice cream, yogurt, Mozzarella cheese, nonfat dry milk and whey protein concentrate
- Second largest producer of cheese (25% of US) – the fastest growing dairy product accounting for 40% of the state's milk supply

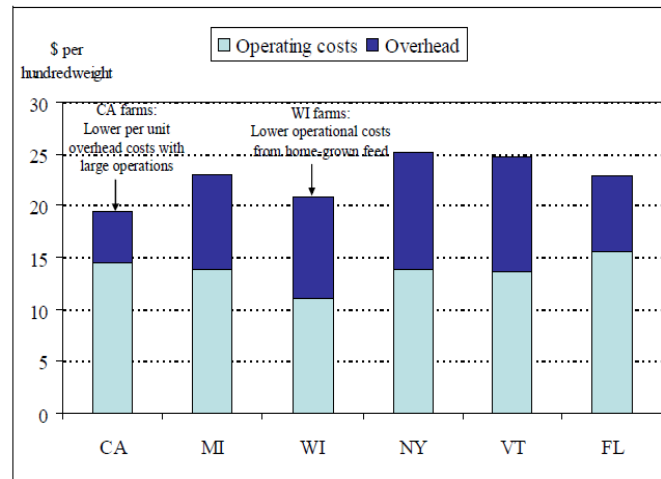
All data provided by the California Milk Advisory Board

Dairy is a Tough Business



Operating Costs High and Increasing

Figure 5. Average Cost of Milk Production

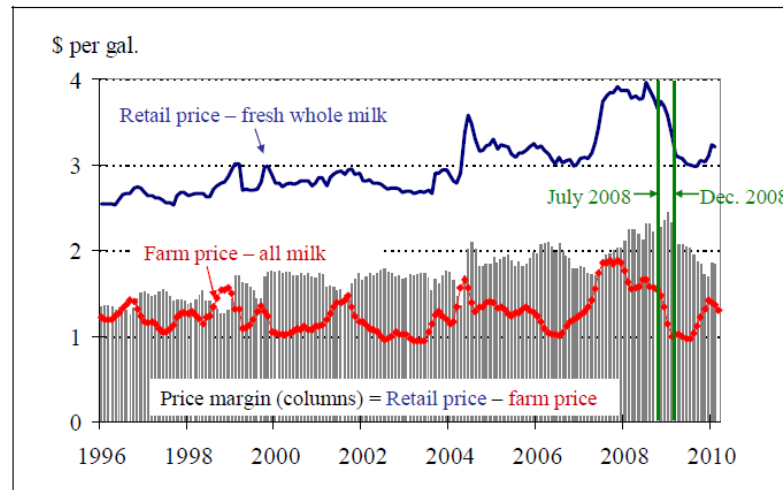


Source: U.S. Department of Agriculture, Economic Research Service.

Notes: Estimates for the month of January 2010.

Milk Prices Haven't Fully Recovered

Figure 1. Monthly Farm and Retail Milk Prices



Sources: U.S. Department of Agriculture (all milk farm prices) and Bureau of Labor Statistics (retail prices).

Notes: Farm price is converted from hundredweight to gallons using a factor of 8.6 lbs. per gallon.

Lots of Moving Pieces and Volatility

- “Dairy farmers in every state saw their collective milk income drop more than ten billion dollars in 2009, which doesn't even include billions more in lost equity.” NMPF President & CEO Jerry Kozak
- In calendar year 2009, the federal government spent more than \$1 billion to support the industry through various dairy programs. Following appeals from dairy farmers for more financial assistance, Congress granted \$350 million in October 2009 in the form of supplemental payments as well as government purchases of dairy products for domestic feeding programs.
- The financial stress of 2009 and similar episodes over the years have led the industry and members of Congress to reconsider the options available to handle fluctuations in milk prices and income for dairy farmers.
- The Federal Reserve is requiring 19 banks that underwent U.S.-mandated “stress tests” to now test their capital against a recession scenario in which the unemployment rate rises to 11%, according to a report Thursday, February 17, 2011.

AGENDA

- 8:30 am Chairman's Introduction,
- 8:45 am Dairy Industry Situation in California
- 9:30 am Credit Markets
- 10:15 am Coffee Break
- 10:45 am Financing and Working With Lenders
- 12:00 pm Lunch
- 1:00 pm Dairy Outlook and Planning Considerations
- 1:30 pm Improving Your Viability; What Should You be Doing?
- 2:30 pm Break
- 3:00 pm So Your Loan is in Special Assets (Workout) ... Now what?
- 4:00 pm Adjourn

Dairy Financing Conference

Working With Banks and Lenders



Visalia Marriott & Convention Center
February 22, 2011

www.thefoodpartners.com

Introduction

Lending is like any other business and it is a function of:

- Capital - the global money supply
- Demand - economic growth
- Price - perceived risk vs. reward

Introduction

Plentiful credit and low interest rates fueled an extraordinary economic expansion from 2000 to 2008, but some areas over expanded.

As a consequence, we are going through the most dramatic economic adjustment in decades.

What does this mean to you?

We'll look at:

Impact of the recession on -

- FDIC Insured Banks
- Farm Credit System

Reactions to the economic downturn

Regulatory environment

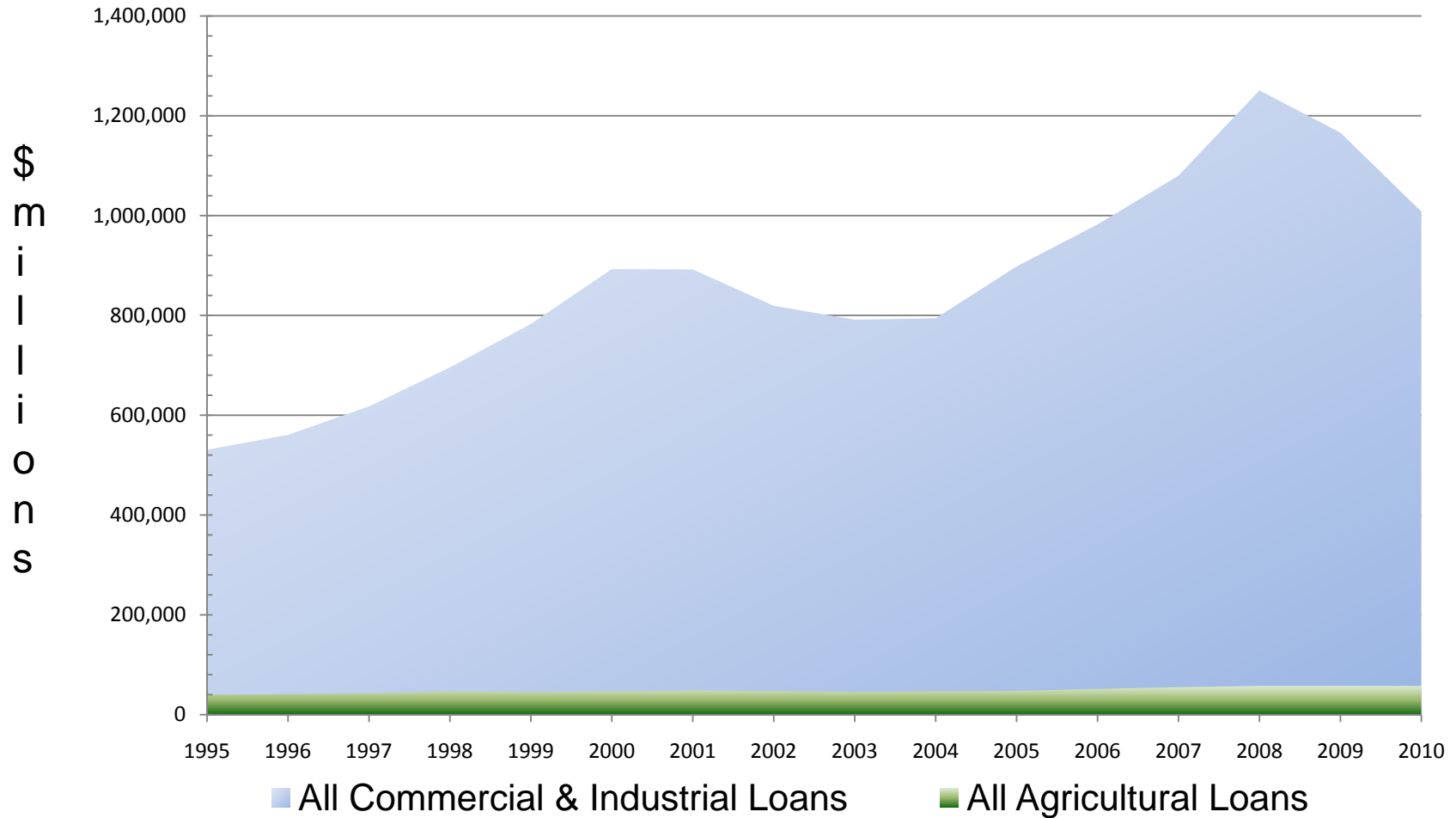
Outlook

Impact of the Recession



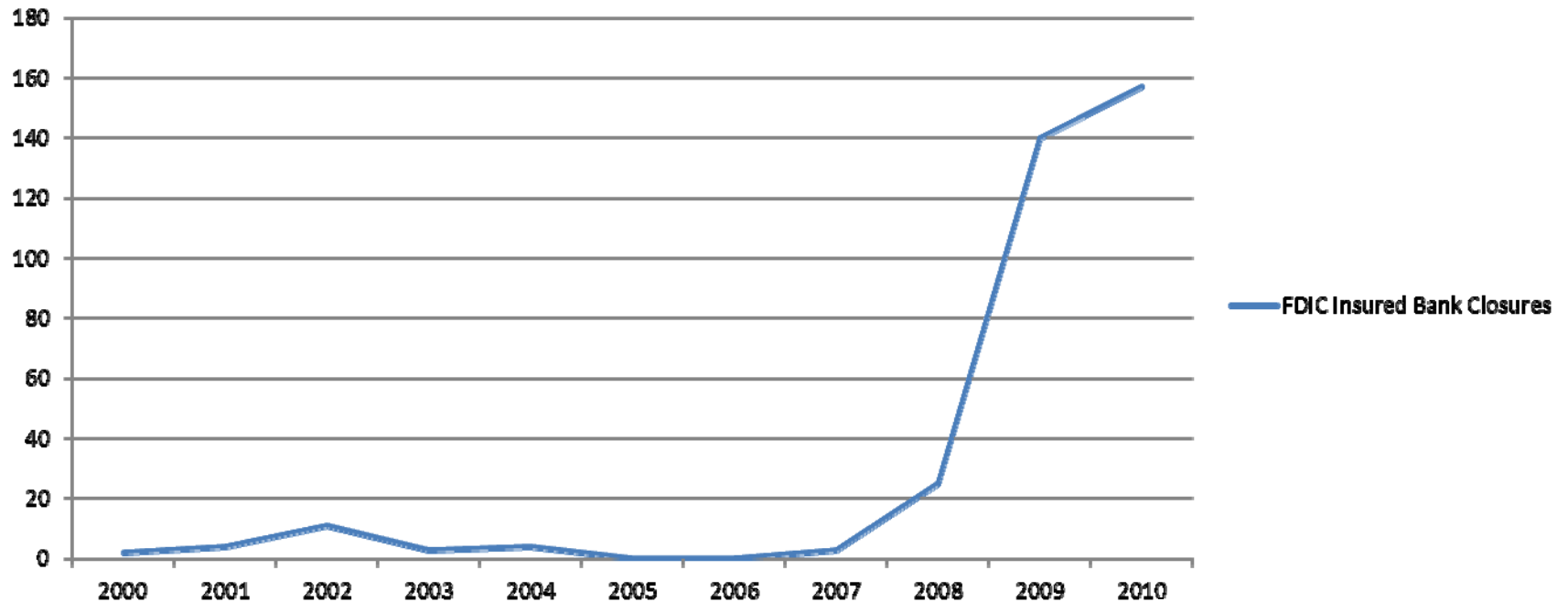
FDIC Insured Banks

C&I Loan Volume – FDIC Institutions



Source: Loans to Small Businesses and Farms, FDIC Insured Institution 1995–2010 at www.fdic.gov

Bank Closures – Up Dramatically



As of February 11, 2011 there were 18 bank closures YTD compared with 16 bank closures YTD in the same period in 2010

Source: www.fdic.gov

Performance Statistics – All FDIC Institutions

	Q3'10	Q4'09	Q4'08	Q4'07	Q4'06
Average Return on Assets (QTR)	0.44%	0.03%	-1.10%	0.18%	1.20%
Net Interest Margin (QTR)	3.75%	3.49%	3.33%	3.30%	3.20%
Noncurrent Rate (QTR)	5.12%	5.37%	2.97%	1.39%	0.79%
Net Charge-Off Rate (QTR)	2.32%	2.89%	1.95%	0.83%	0.47%

Source: www.fdic.gov Latest Industry Trends

FDIC Institutions – System Statistics

At September 30, 2010 the FDIC reported:

It insured 7,760 institutions

VS

8,099 institutions at September 30, 2009

8 new charters and 124 mergers YTD

VS

31 new charters and 179 mergers during all of 2009

1,583 of these institutions are defined as Agricultural Banks

VS

1,578 Agricultural Banks at September 30, 2009

860 Problem Institutions with assets of \$379 billion

VS

702 Problem Institutions with \$403 billion in assets at September 30, 2009

Source: www.fdic.gov

Impact of the Recession



Farm Credit System

Farm Credit System - Quarterly Comparison (in blns)

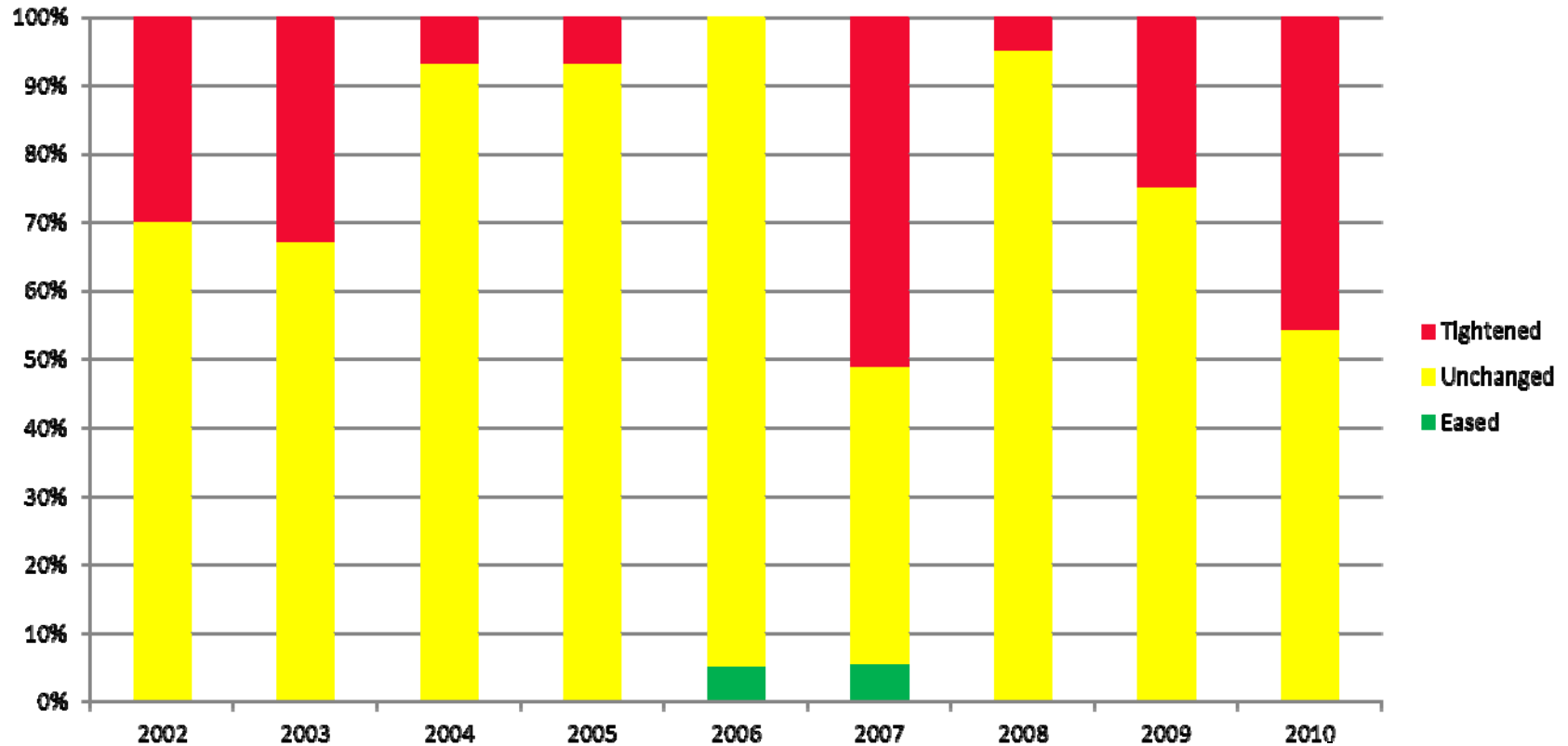
	Q3'10	Q2'10	Q1'10	Q4'09	Q3'09
Gross Loan Volume	\$168.48	\$162.19	\$162.50	\$164.83	\$162.19
Non-Performing Loans	3.74	3.75	3.72	3.53	4.29

During 2010, mergers within the Farm Credit System reduced the number of FCS members from 93 to 89

Source: Farm Credit Administration (www.fca.gov)

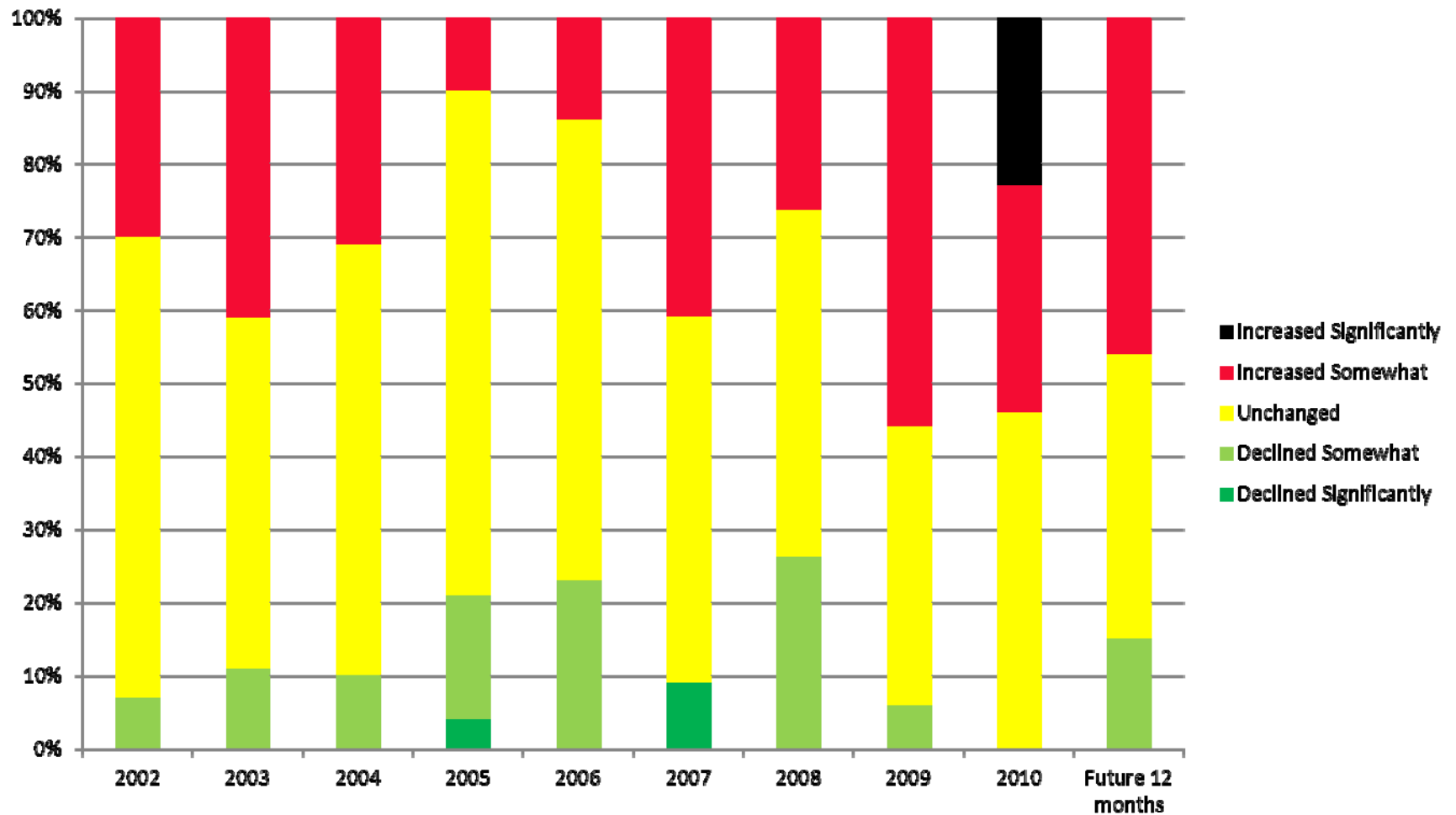
Reactions to the Economic Downturn

Changes in Agricultural Loan Underwriting Standards



Source: www.occ.gov 51 bank survey at August 2010

Changes in Credit Risk in Agricultural Loan Portfolios



Source: www.occ.gov 51 bank survey at August 2010

Regulatory Environment

Regulators – Plenty to go Around

- The **Board of Governors of the Federal Reserve** oversees state-chartered banks and trust companies that belong to the Federal Reserve System.
- The **Office of the Comptroller of the Currency** regulates banks that have the word "National" in or the letters "N.A." after their names.
- The **Federal Deposit Insurance Corporation** regulates state-chartered banks that do not belong to the Federal Reserve System.
- Individual **State Banking Departments** also oversee state chartered banks
- The **National Credit Union Administration** regulates federally chartered credit unions.
- The **Office of Thrift Supervision** oversees federal savings and loans and federal savings banks.
- The **Farm Credit Administration** regulates the Farm Credit System

Lending Standards – OCC Ag Lending Guidelines

- In-depth financial analysis
- Structuring loans in accordance with the type of borrowing and the expected income stream
- Reliable collateral evaluations and margins, and/or other steps to minimize credit risk
- Effective ongoing monitoring practices, including segregation of any prior period crop carryover debt
- Thorough evaluation of the borrower's character and history of managing debt repayment

Source: OCC Handbook Safety and Soundness - Agricultural Lending 12/1/98

Some Additional Regulatory Areas

Truth in Lending

Equal Credit Opportunity Act (ECOA)

Community Reinvestment Act (CRA)

Flood Insurance - FEMA Flood Hazard Determination

Home Mortgage Disclosure Act (HMDA)

Gramm-Leach-Bliley Act

Bank Secrecy Act (BSA) - Financial Crimes Enforcement Network of the Department of the Treasury (FinCEN)

Anti-Money Laundering statutes - FinCEN

Suspicious Activity Report (SARS) - FinCEN

Regulatory Changes

Dodd-Frank Wall Street Reform and Consumer Protection Act

Consumer Protections with Authority and Independence –
Creates a new independent watchdog

Ends Too Big to Fail Bailouts –
Ends the Federal Reserve's authority to prop up individual firms and establishes rigorous standards and supervision

Advance Warning System –
Creates a council to identify and address systemic risks

Transparency & Accountability for Exotic Instruments –
Eliminates loopholes that allow risky and abusive practices to go on unnoticed and unregulated

Source: http://banking.senate.gov/public/_files/070110_Dodd_Frank_Wall_Street_Reform_comprehensive_summary_Final.pdf

Regulatory Changes - continued

Executive Compensation and Corporate Governance –

Provides shareholders with a say on pay and corporate affairs with a non-binding vote on executive compensation and golden parachutes

Protects Investors –

Provides tough new rules for transparency and accountability for credit rating agencies to protect investors and businesses

Enforces Regulations on the Books –

Strengthens oversight and empowers regulators to aggressively pursue financial fraud, conflicts of interest and manipulation of the system

Key structural change –

The OCC assumes oversight of federal savings and loans and federal savings banks by July 21, 2011 eliminating the Office of Thrift Supervision

Source: http://banking.senate.gov/public/_files/070110_Dodd_Frank_Wall_Street_Reform_comprehensive_summary_Final.pdf

Regulatory Changes - continued

Bank for International Settlements – Basel II

Pillar 1 Minimum Capital Requirements –

Increases capital requirements for banks engaged in loan securitizations and requires more internal credit analysis versus third party credit ratings

Pillar 2 Supervisory Review Process –

Addresses several notable weaknesses revealed in the financial turmoil that began in 2007:

- Firm-wide governance and risk management
- Capturing off-balance sheet risk and securitization activities;
- Better manage risk concentrations;
- Provides incentives for banks to better manage risk and returns over the long term
- Sound compensation practices.

Source: www.bis.org

Regulatory Changes - continued

Bank for International Settlements – Basel II

Pillar 3 Market Discipline –

Requirements are strengthened in several key areas, including:

- Securitization exposures in the trading book
- Sponsorship of off-balance sheet entities
- Resecuritization exposures
- Holding risks with regard to the inventory securitization exposures held for sale

Source: www.bis.org

Outlook

Outlook for Lenders and You

The continuing consolidation of banks

Increased focus on Agribusiness as a source of growth and more stable business

Increased capital requirements, new restrictions on products and pricing, more regulatory oversight and broader risk management

More focus on client risk management

- Market Prices – Inputs and Outputs

- Interest Rates

- Operational – including management succession, ownership succession, environmental regulations

More focus on client financial management and condition

- Working capital

- Leverage

- Cost analysis

- Accurate and timely financial reports

Outlook for Lenders and You

Borrowers will need to have a prudent business strategy and a clear objective

Production growth or diversification should be based on a thorough economic analysis and sound financial base

Meaningful and timely loan performance monitoring

- Loan Covenants
- Position Reports/Borrowing Base



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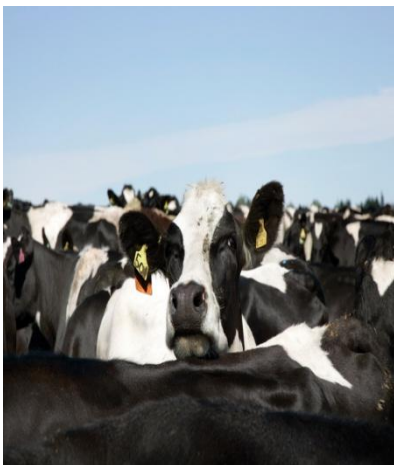
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WDBA Expansion Symposium

Entering a Global Market Era - Implications for US Dairy

Vernon M. Crowder
Vice President, Agricultural Economist
Food & Agri Research
Rabobank, N.A.

Food & Agribusiness Research and Advisory

A global network of research professionals – supporting knowledge based banking

- Over 70 analysts in 13 different countries
- Focus areas:
 - Dairy
 - Grains & Oilseeds
 - Animal Protein
 - Beverages
 - Farm Inputs
 - Food Retail
 - Sugar & Sweeteners
 - Fruits & Vegetables



Section 1

US dairy – entering a global market era

Section 2

What does the global market look like?

Section 3

Market status and outlook

Section 4

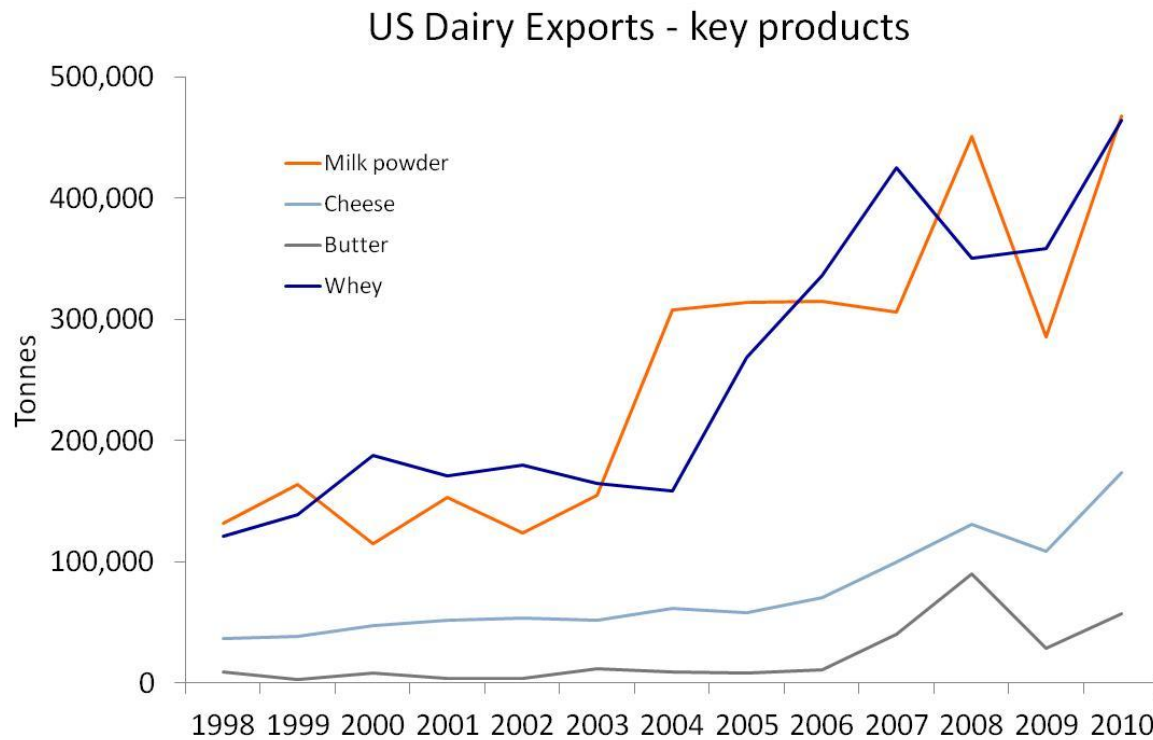
California milk shed

Section 5

Planning for a new era

US dairy exports have soared in recent years

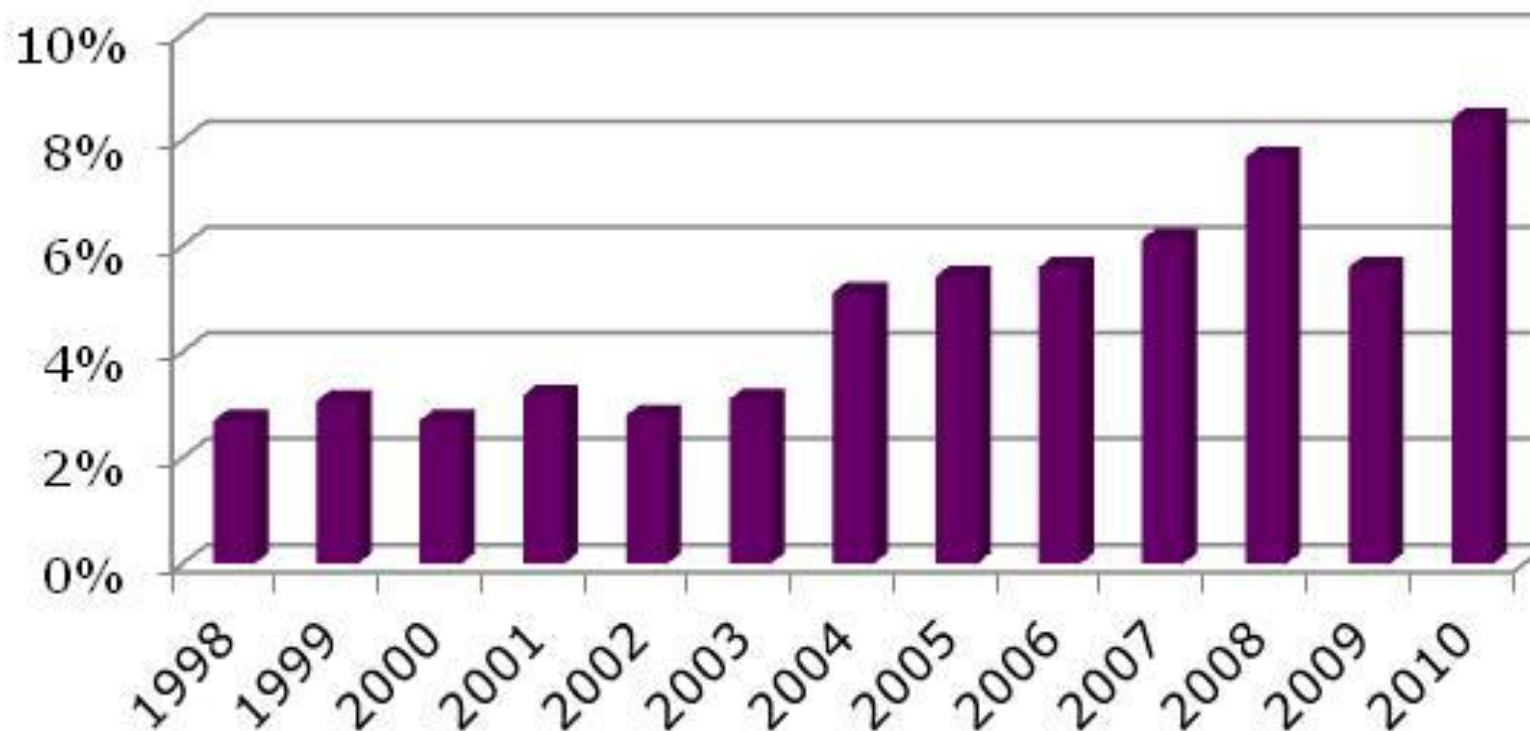
- A sustained growth phase coincided with increased US competitiveness
- An unprecedented boom in global commodity prices
- Phasing out of Mexican tariffs under NAFTA



Source: Rabobank, USDA.

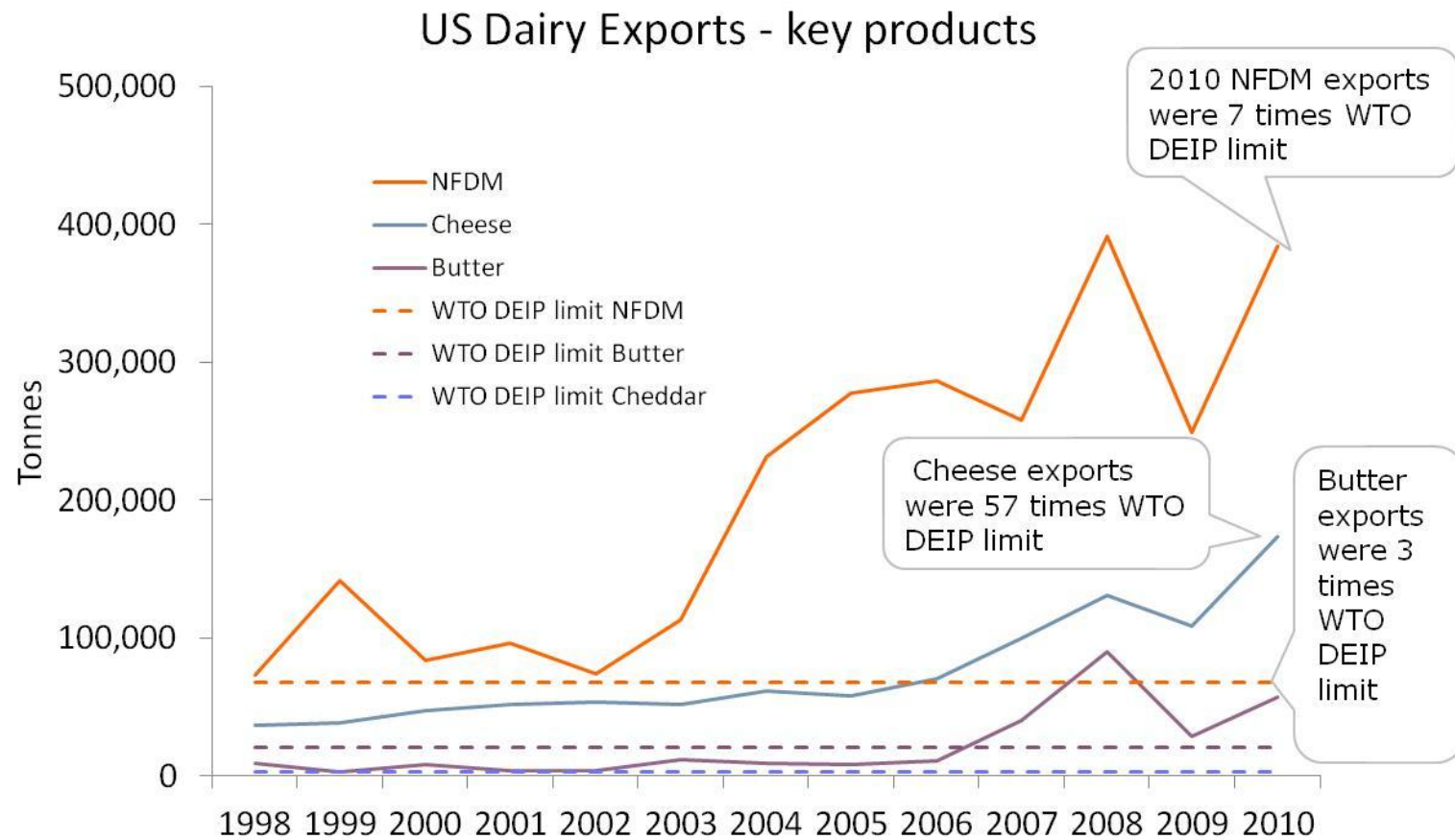
US dairy exports have soared in recent years

Share of US milk production exported



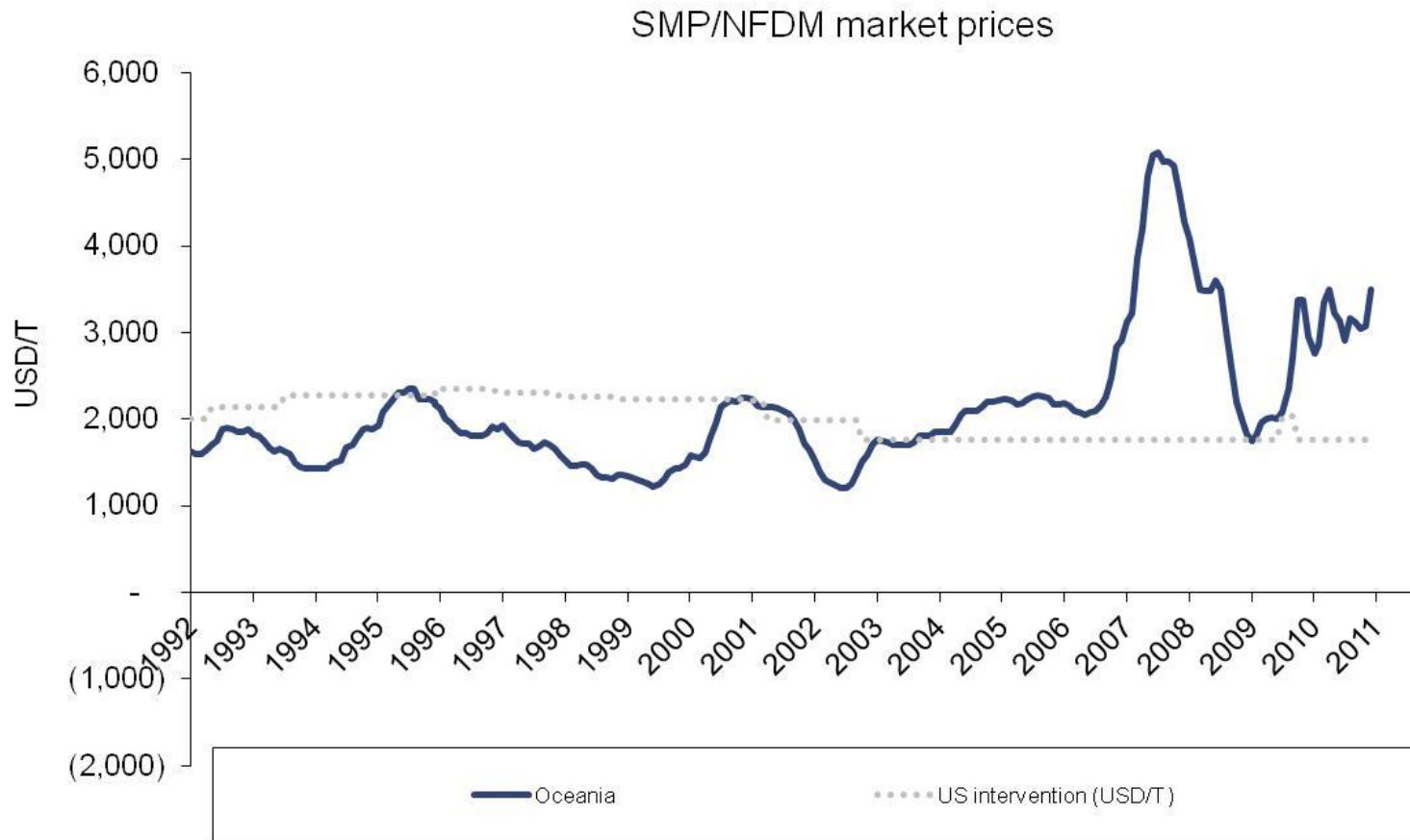
Source Rabobank. Note: Calculate in LME terms.

DEIP affords little protection at these export levels



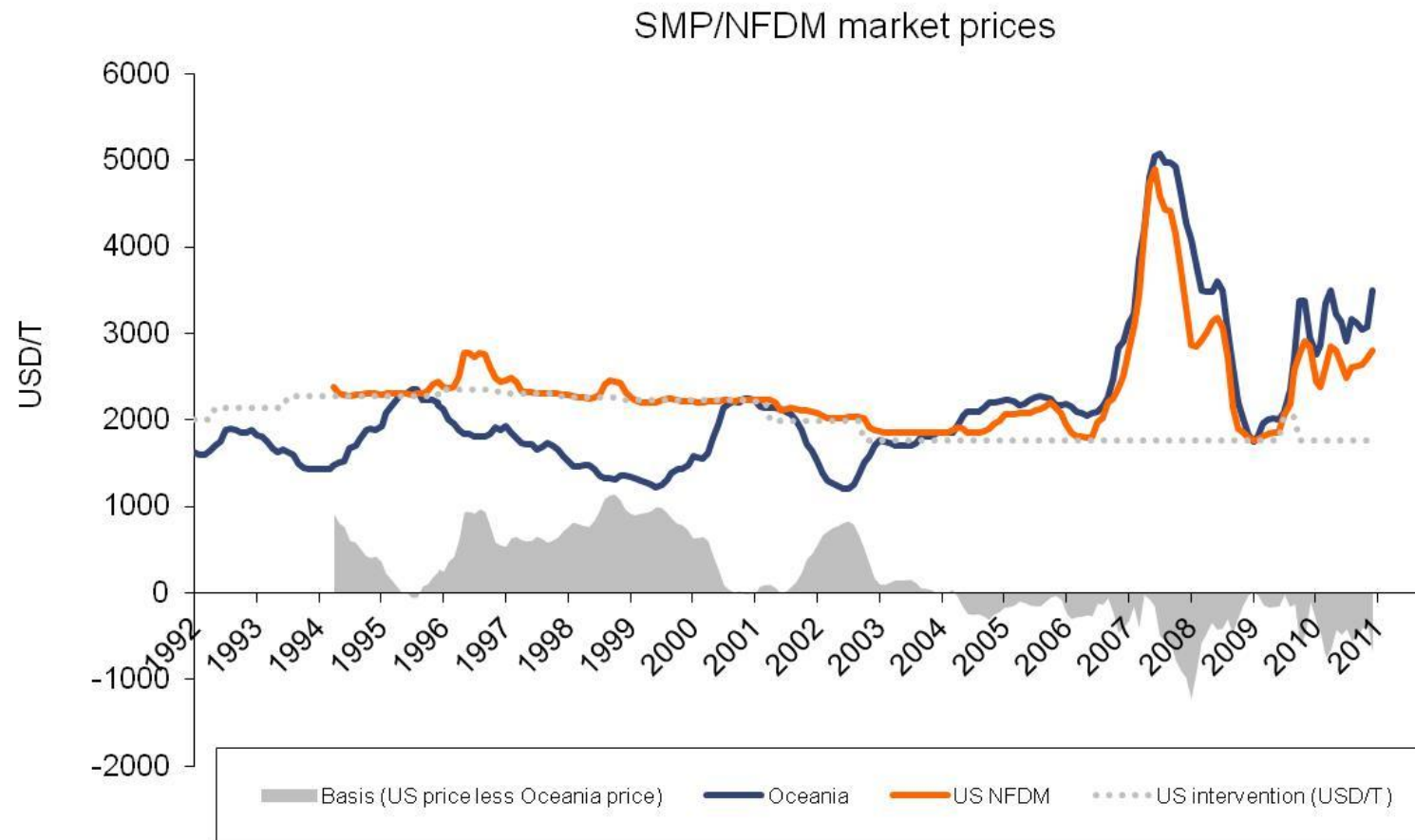
Source: Rabobank, USDA. Note 2010 is 11 months extrapolated.

Export commodity prices have been pushed well above domestic intervention levels



Source: USDA, MDC, Rabobank analysis

Export exposure, high world prices and absence of subsidies have brought convergence of domestic and offshore commodity prices



Source: USDA, MDC, Rabobank analysis

Commodity price convergence ensures that international markets now heavily impacting US milk prices

Class III milk price v International cheddar price



Source: CME, USDA, Rabobank analysis

A global market era for US dairy

- The US is now strongly linked to the international market
- It is almost certain to remain so for at least the medium term



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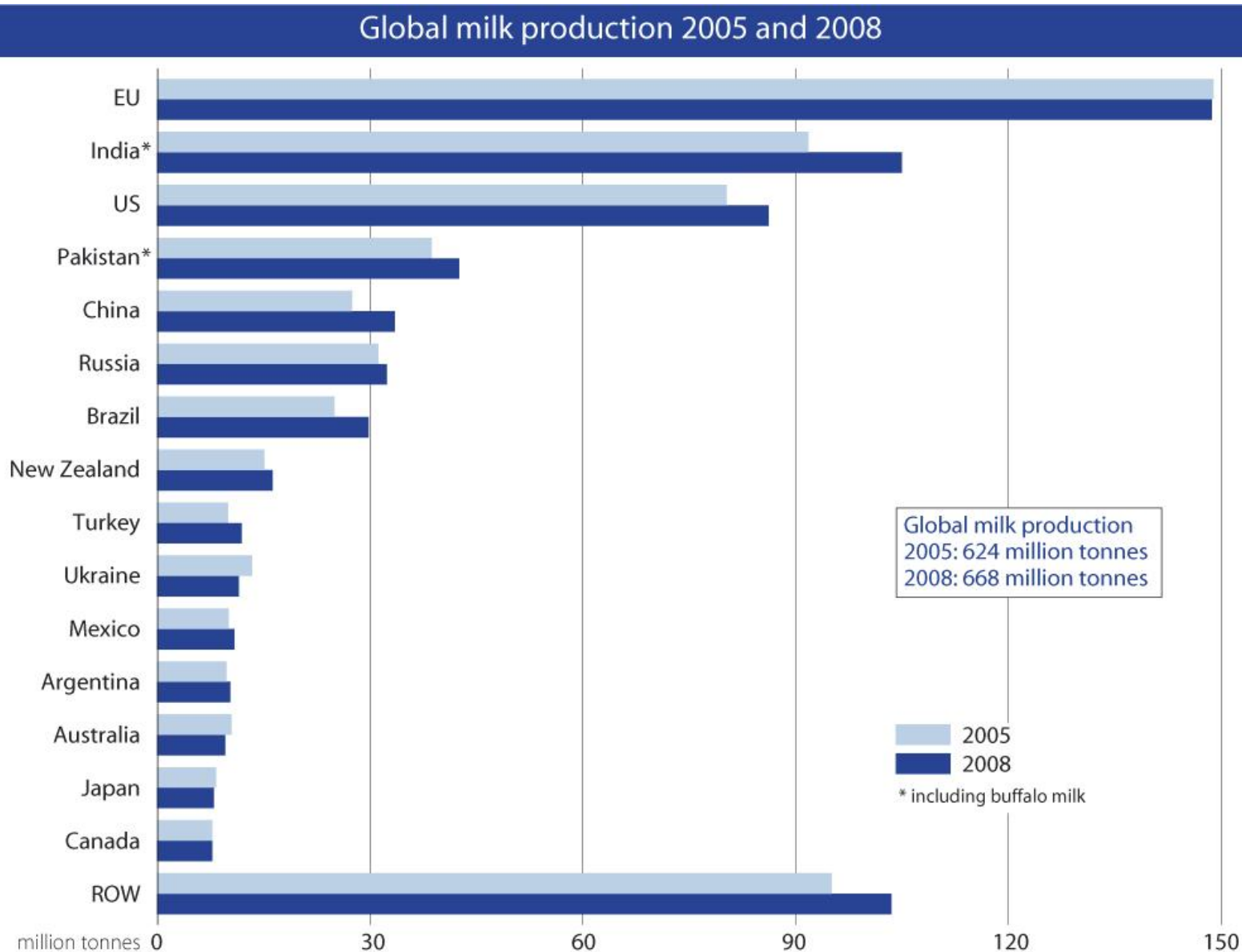
Planning for a new era

The world's dairy industry has traditionally been highly fragmented

- International trade has been very thin
- Market highly distorted by regulation
- Has ensured limited connectivity (at best) between pricing in different markets
- With markets and industries essentially national or regional

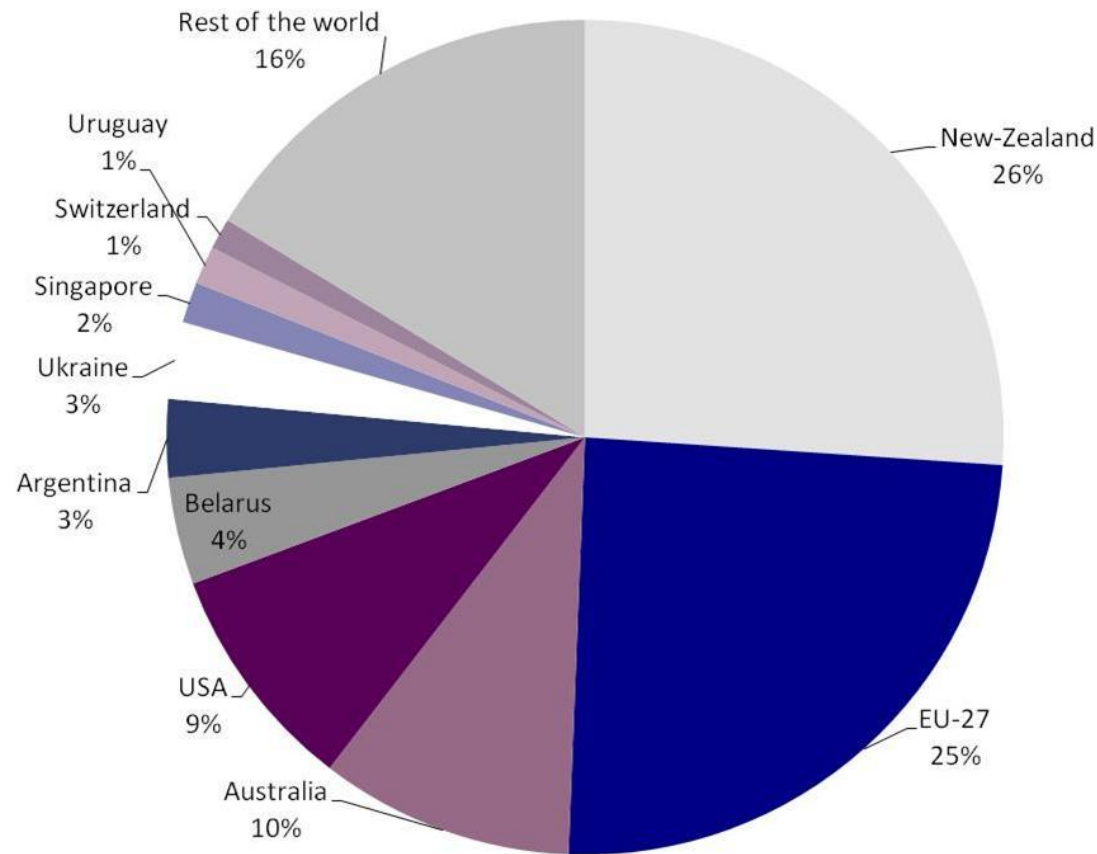
These things are changing !

List of biggest producers contains some surprises

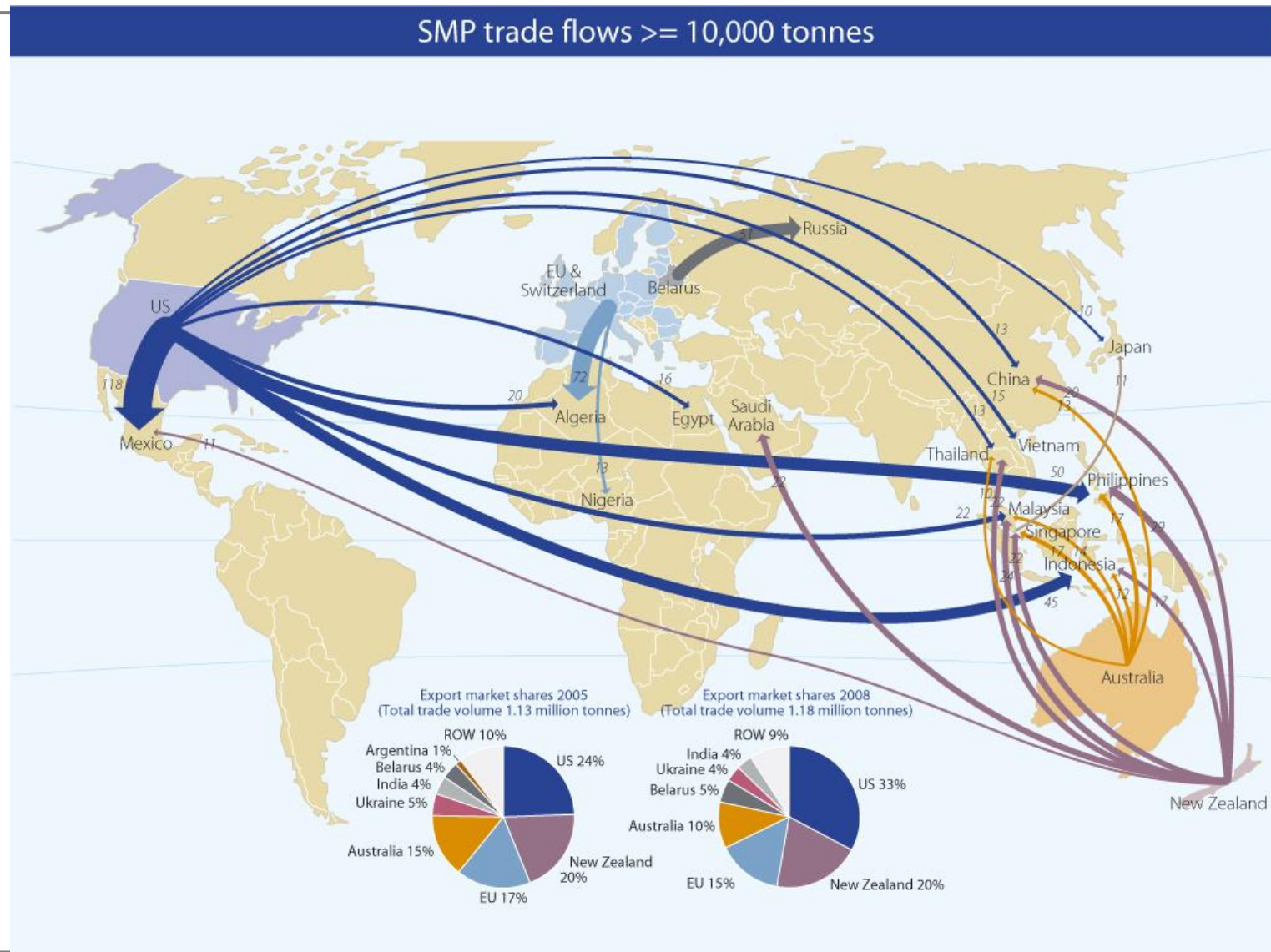


Exports are highly concentrated (imports are not)

Global export market shares (2008)



Trade flows from advanced to developing countries



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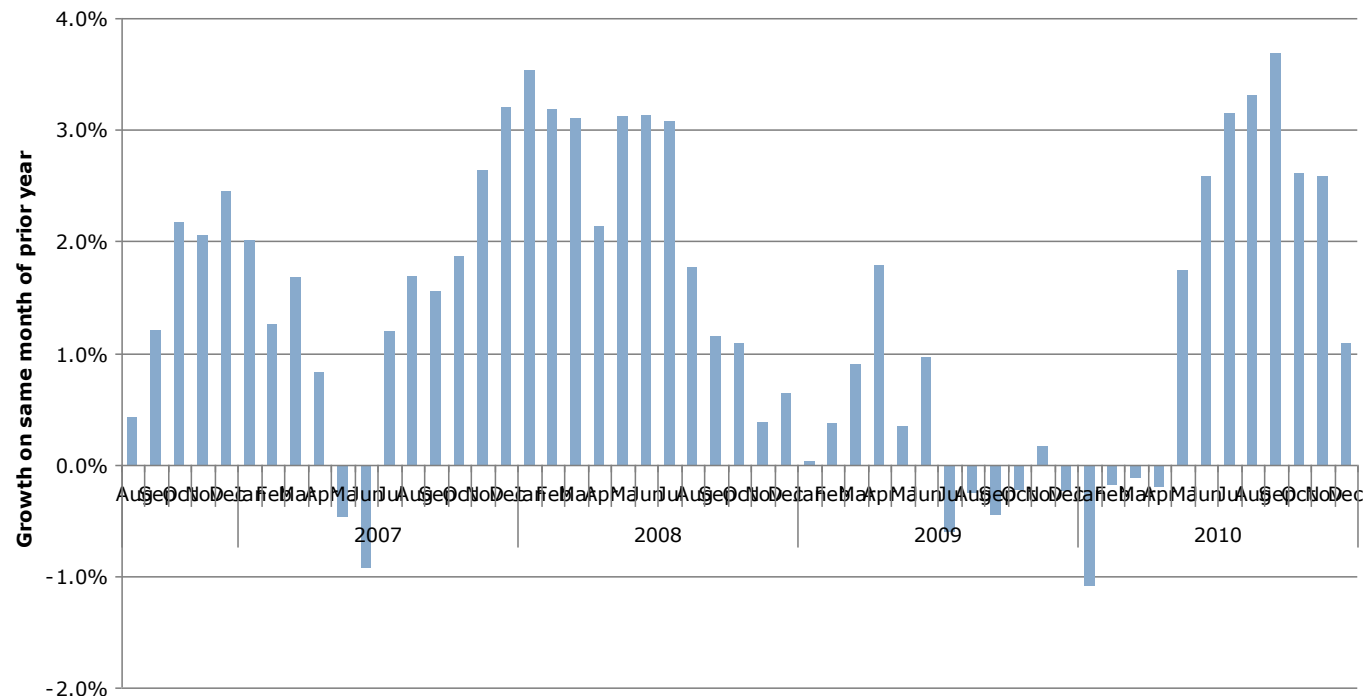
Planning for a new era

Current status – supply has been expanding, though weather impacted



- Farmers responding to improved milk prices
- Particularly strong milk supply growth in USA and EU
- But adverse weather in NZ and Australia has slowed momentum

Milk production growth of Big 6 exporters combined



Source: Rabobank

Note: includes EU 27, USA, NZ, Australia, Brazil and Argentina

Current status – vigorous demand on world markets



Global consumption is improving

- World economy continues to recover
- Robust dairy sales growth in SEA, Latin America and China

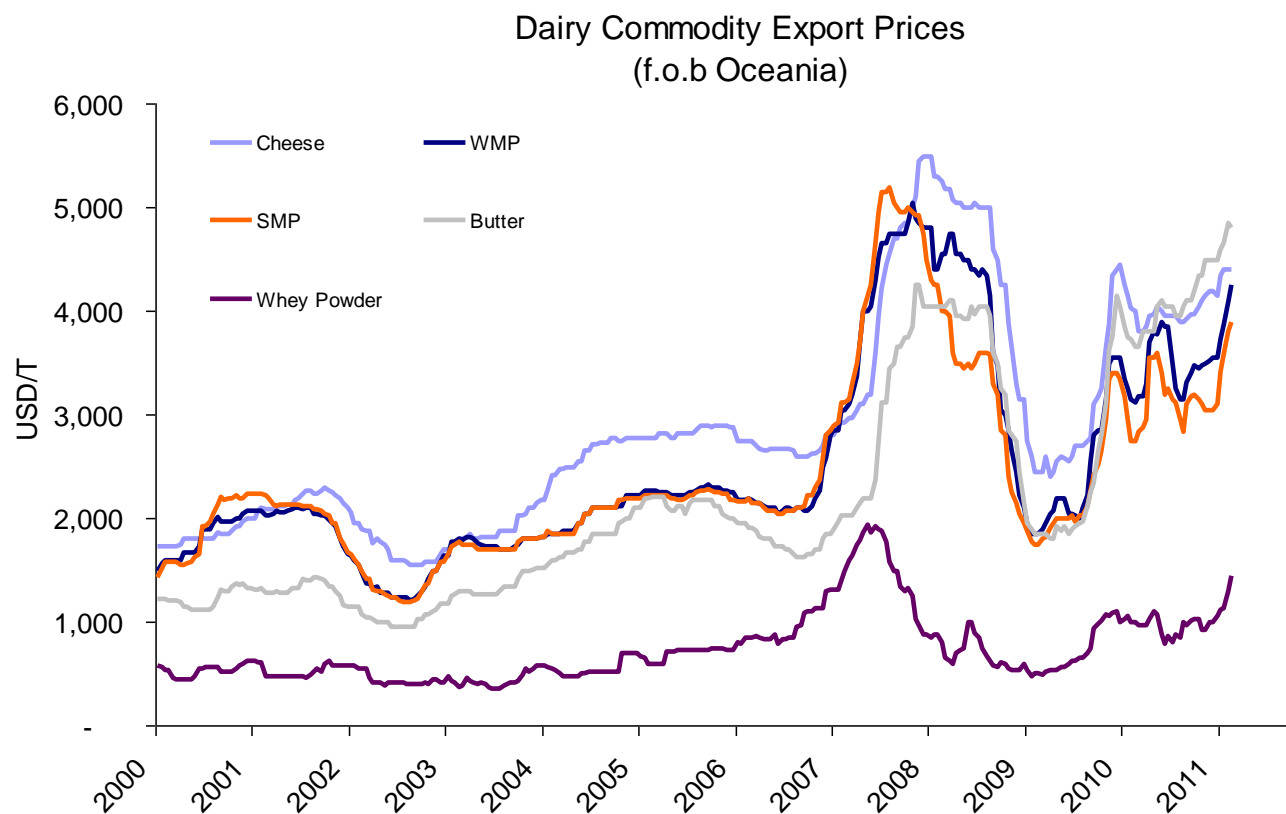
With imports further boosted by localised events

- China is buying huge quantities post melamine
- Russia forced to cover its needs post drought

Current status – a second price boom



- Vigorous importing has proved more than adequate to soak up rising export supply
- Market is extremely tight (and buyers nervous)
- International prices pushed back to extreme highs



Source: USDA, Rabobank

Demand growth should broaden and accelerate in 2011

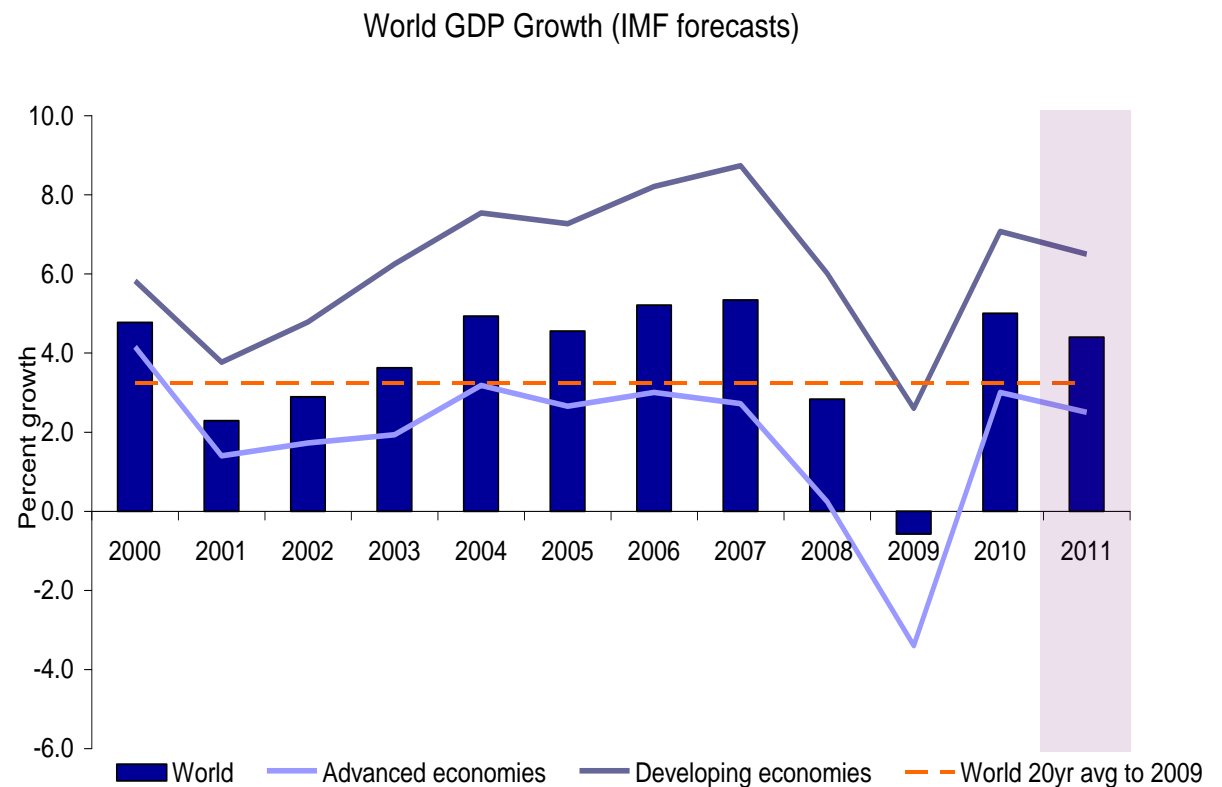


Conditions are improving

- Further economic growth
- Improved employment in OECD
- Importing countries to outperform
- China and Russia to stay strong

Though still not ideal

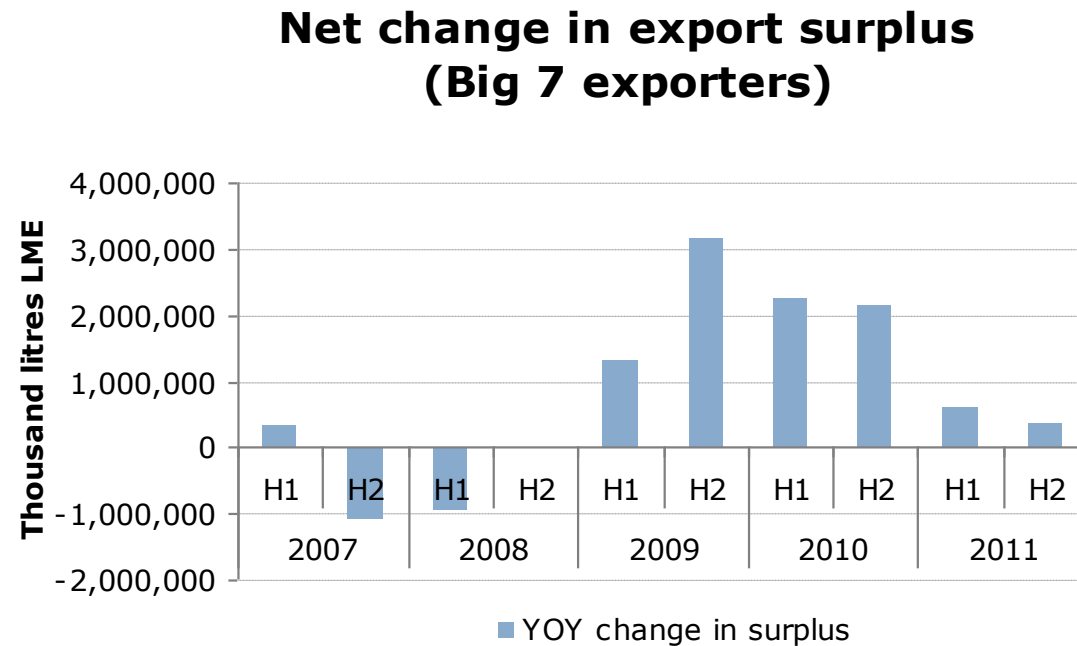
- Only slow employment growth
- Retail prices are high
- Pressure to substitute



Source: IMF Jan 2011

Exportable supply will expand, but less quickly

- Grain prices to temper supplementary feeding
- Deleveraging to constrain investment
- Rising local consumption to constrain export growth
- Stocks less alarming than 12 months ago



Source: Rabobank

Market to remain price supportive in 2011



Primary expectation

- Global dairy commodity prices to remain extremely high through 2011

Notable downside risks

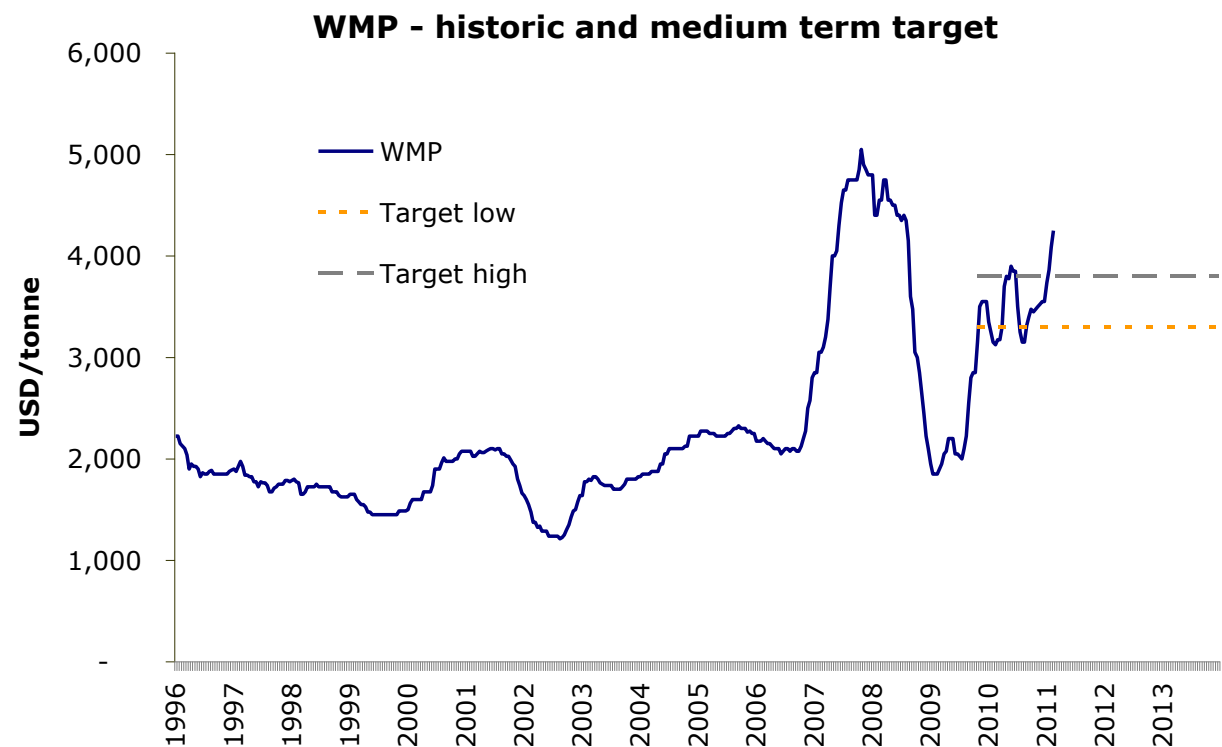
- Over production in US or EU through Q2
- China and/or Russia don't come to the party

Notable upside risks

- India may run short of milk (again)
- Any weather disruptions to next NZ season (from Q3)

Medium term prognosis – a new trading range

- Solid global demand growth, led by developing countries
- Most additional milk requirements will be met locally, but not all
- Low cost exporters are unlikely to meet import demand on their own
- Higher cost milk will be required to fill the gap
- Export subsidisation will be limited
- Production costs will remain high for all farmers



Source Rabobank

But volatility will remain

- Market is thin
- Milk supply and demand are inelastic
- Market shocks have become more common (input costs, climate)
- Increased role for non transparent players (esp China and Russia)



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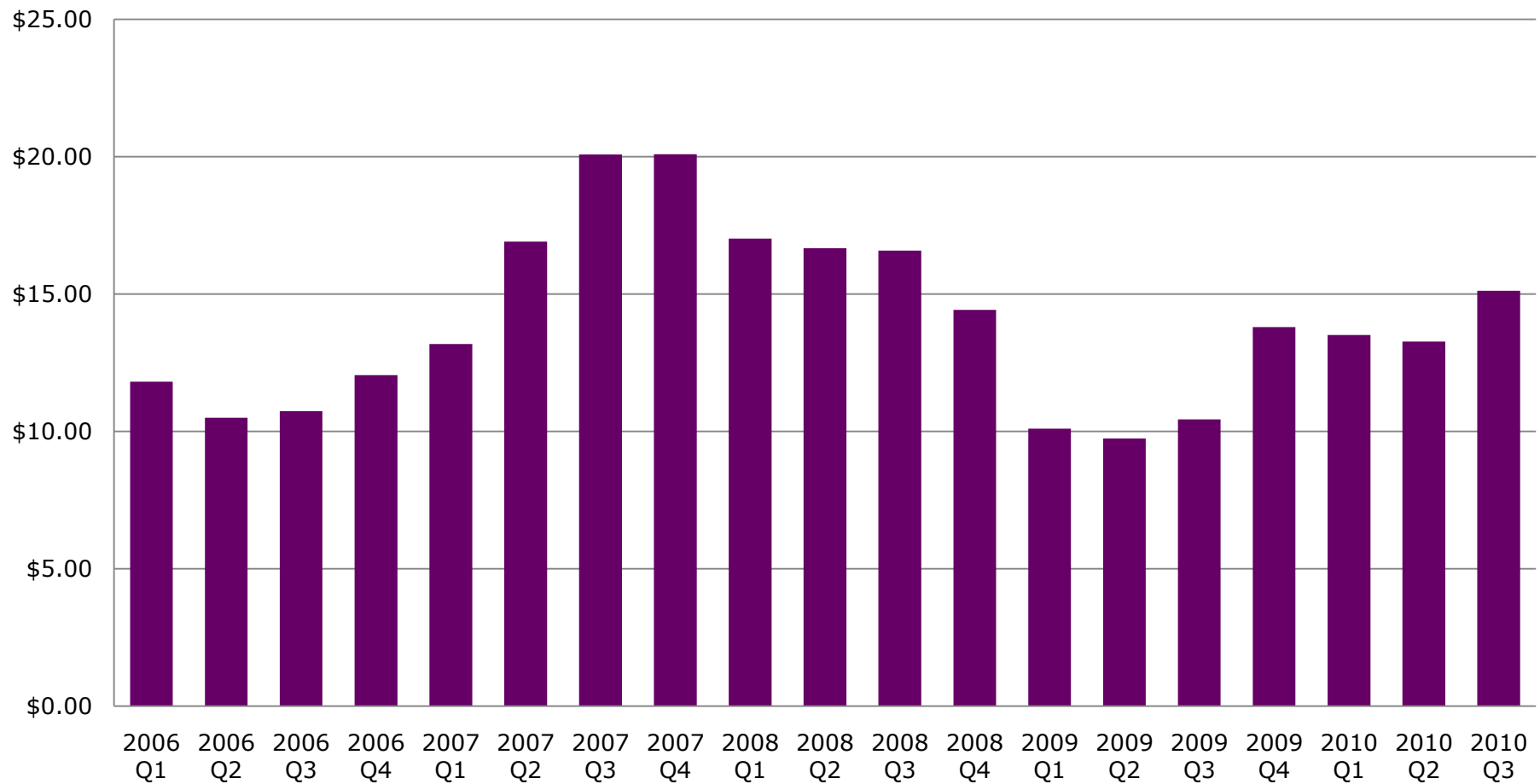
Section 5

Planning for a new era

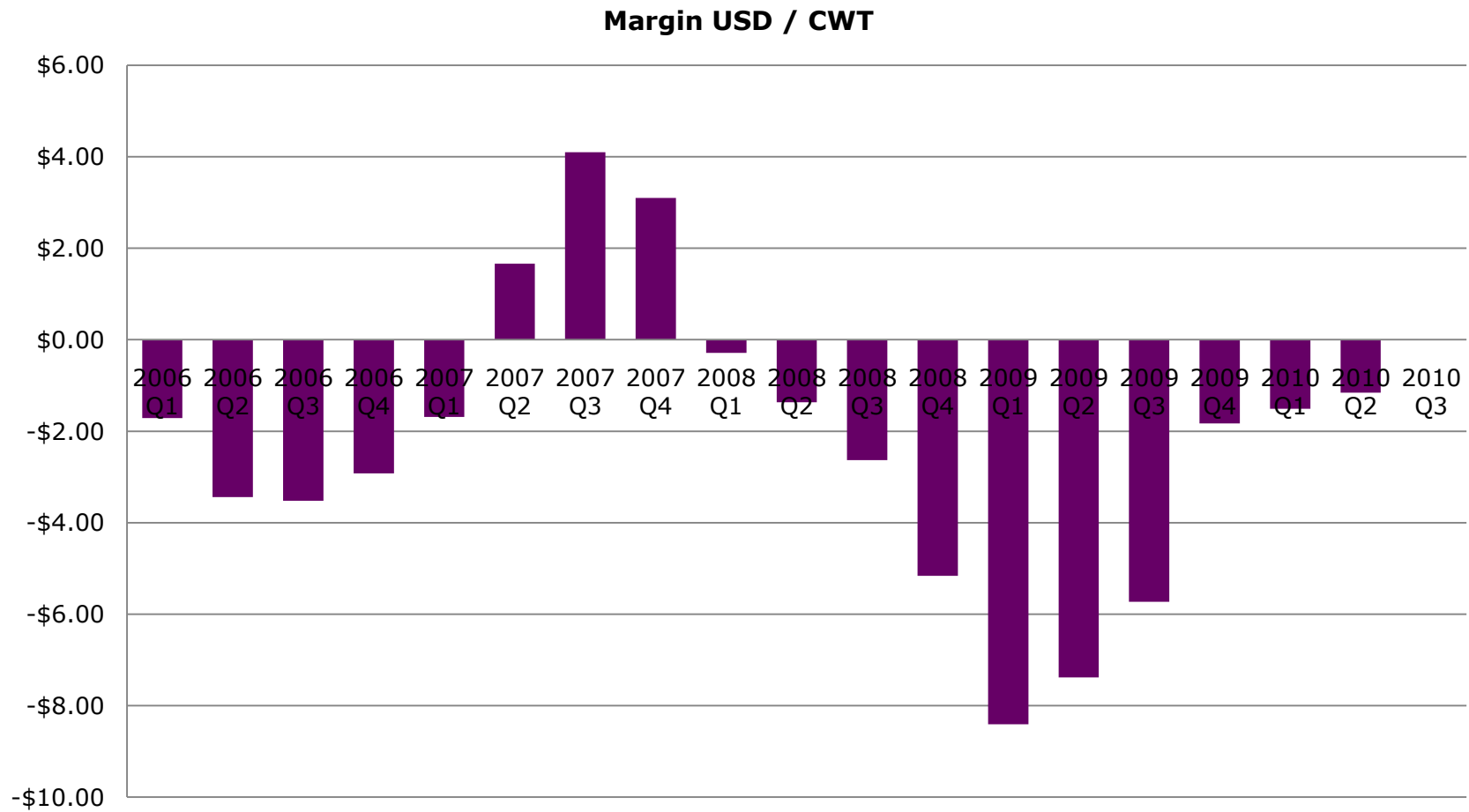
Mailbox Prices



Mailbox Price USD / CWT



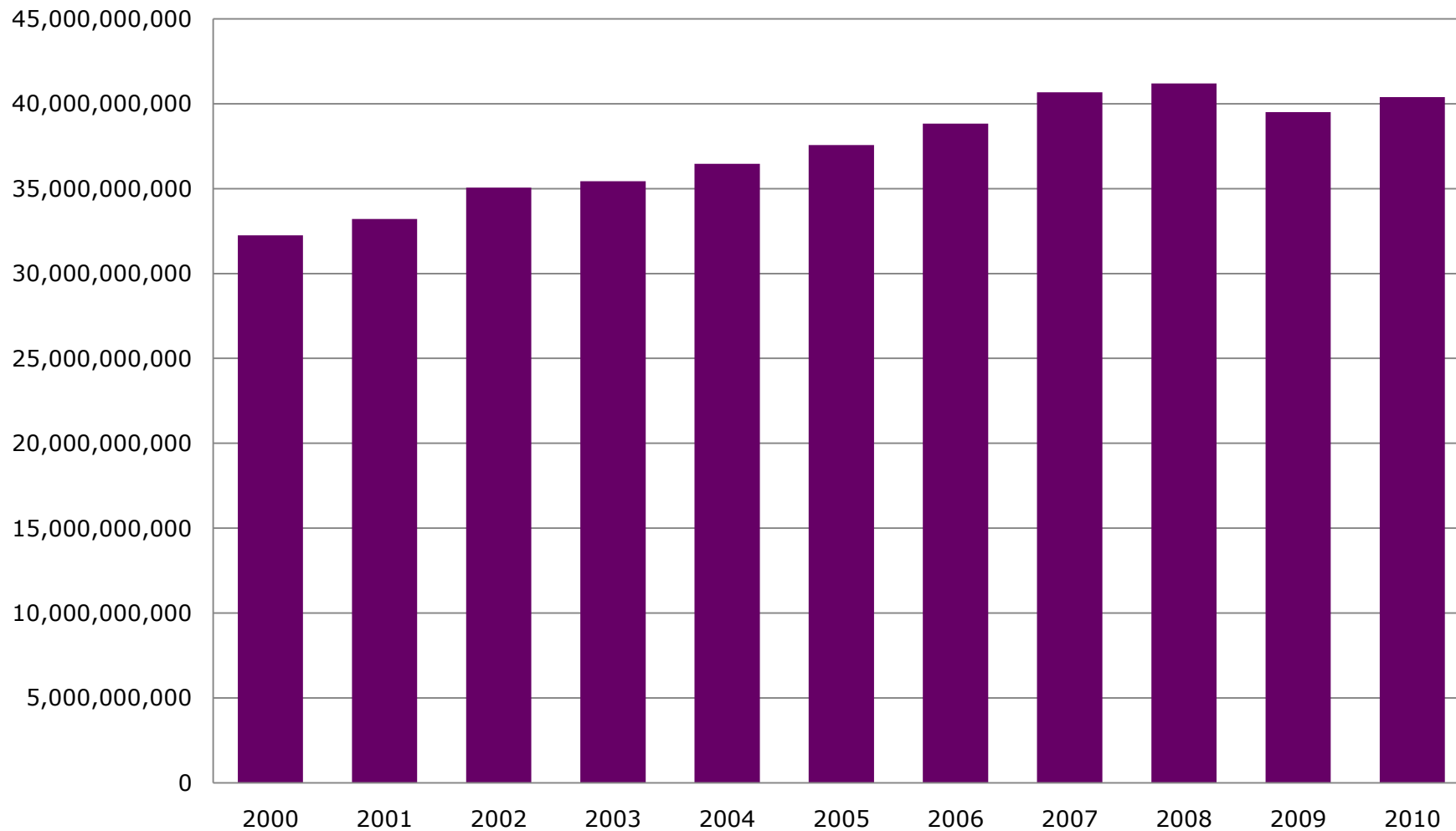
Margin



Dairy Production



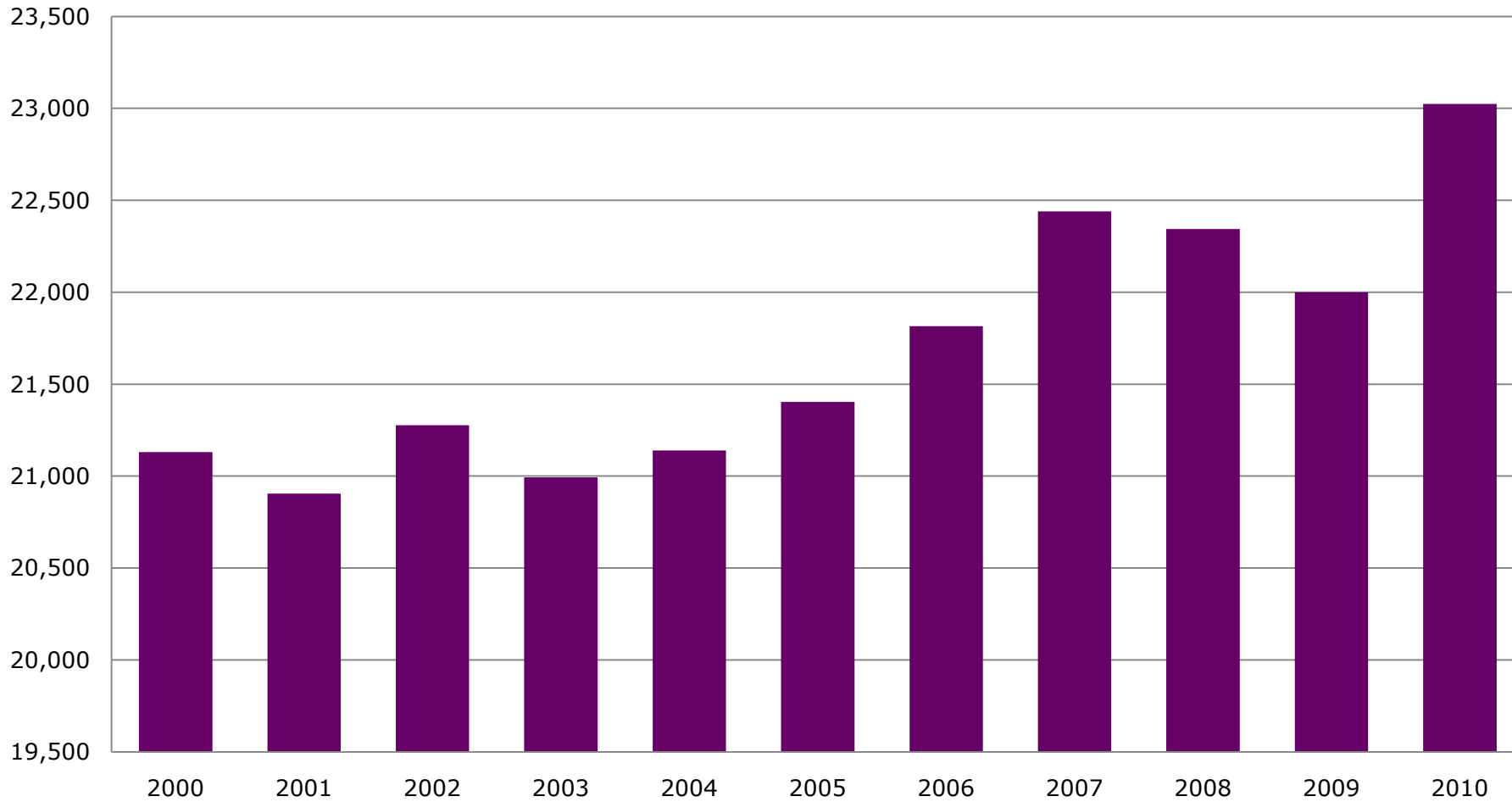
Milk production (pounds)



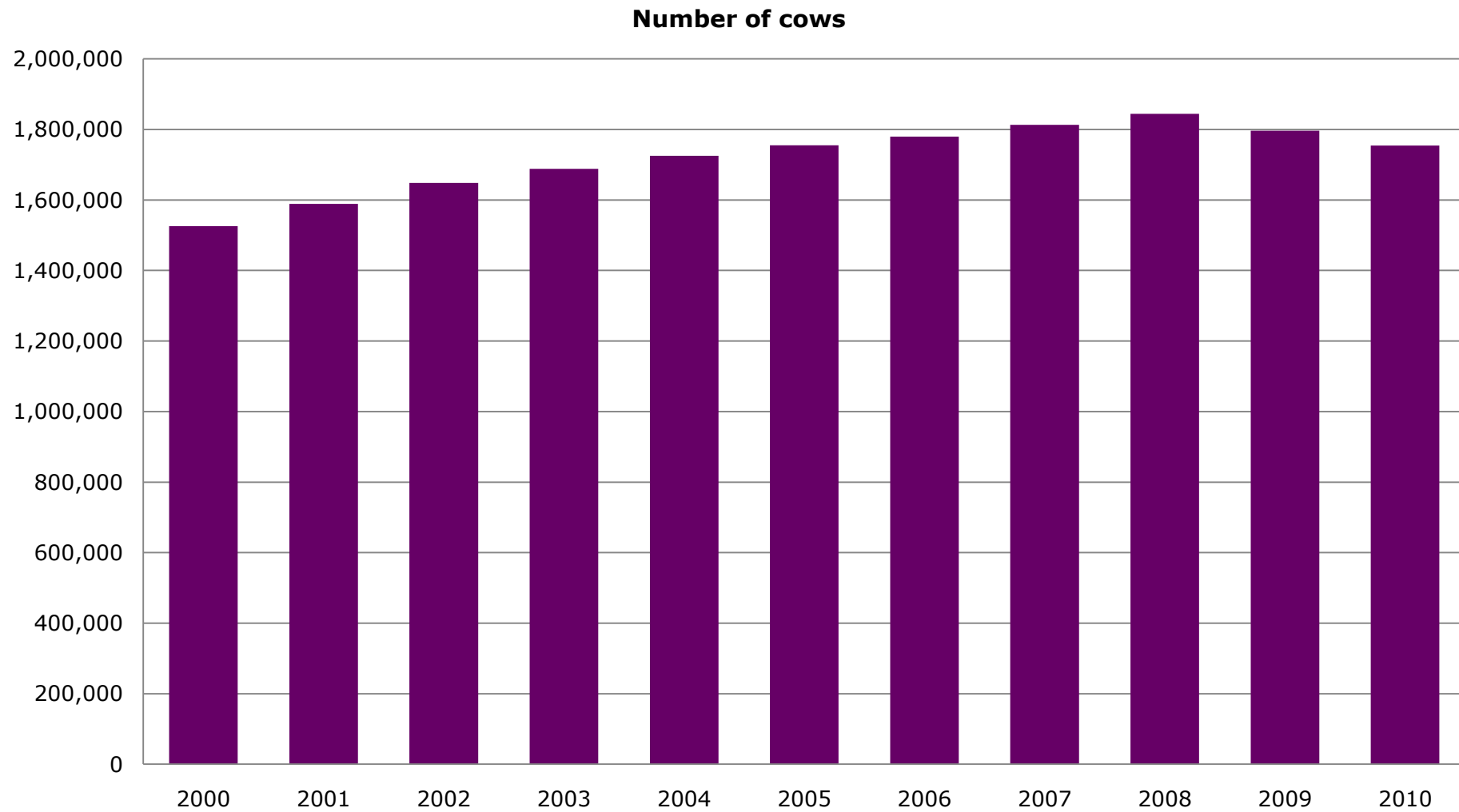
Dairy Production



Milk production cow/year (pounds)

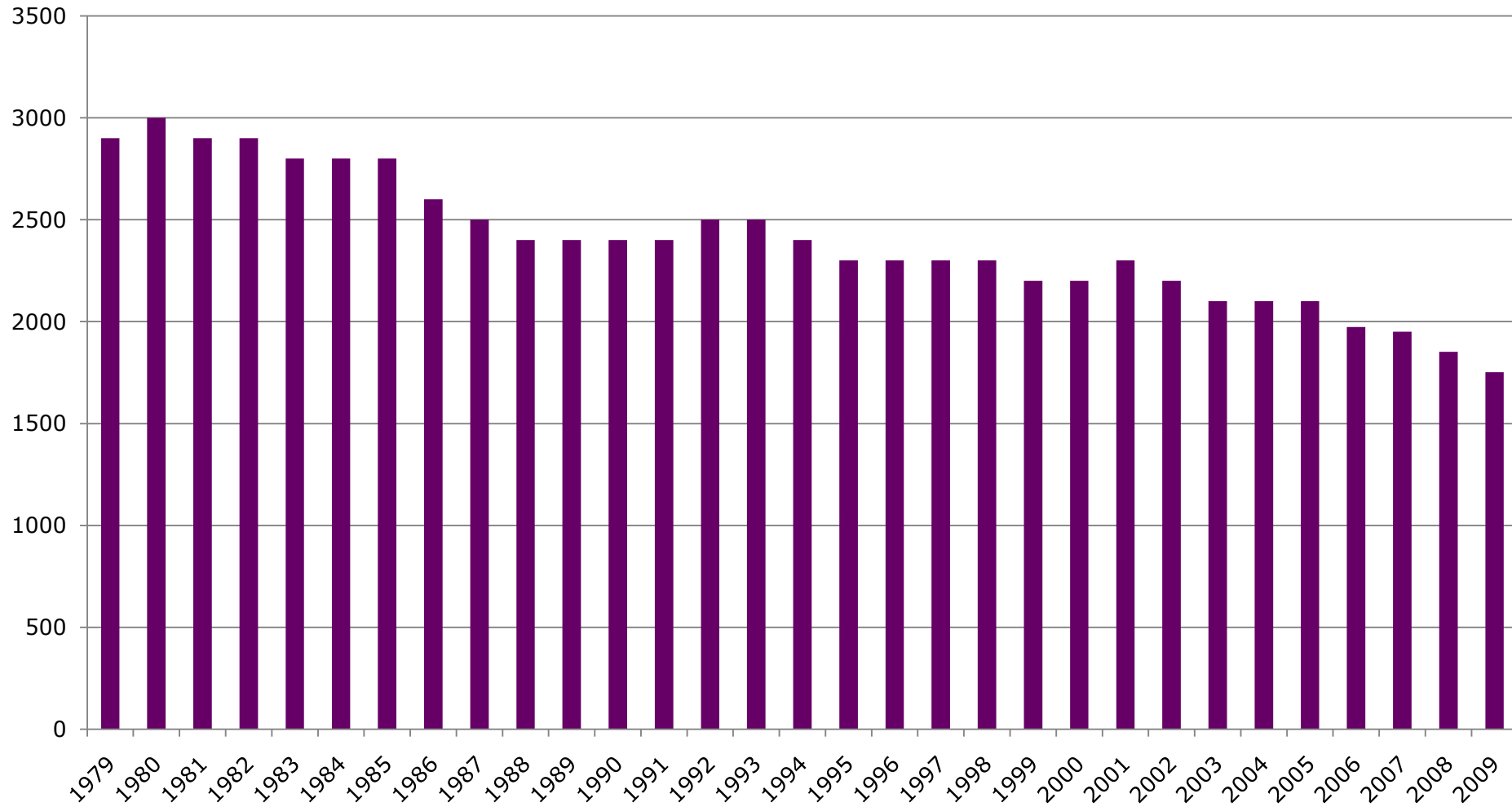


Number of cows



Dairies

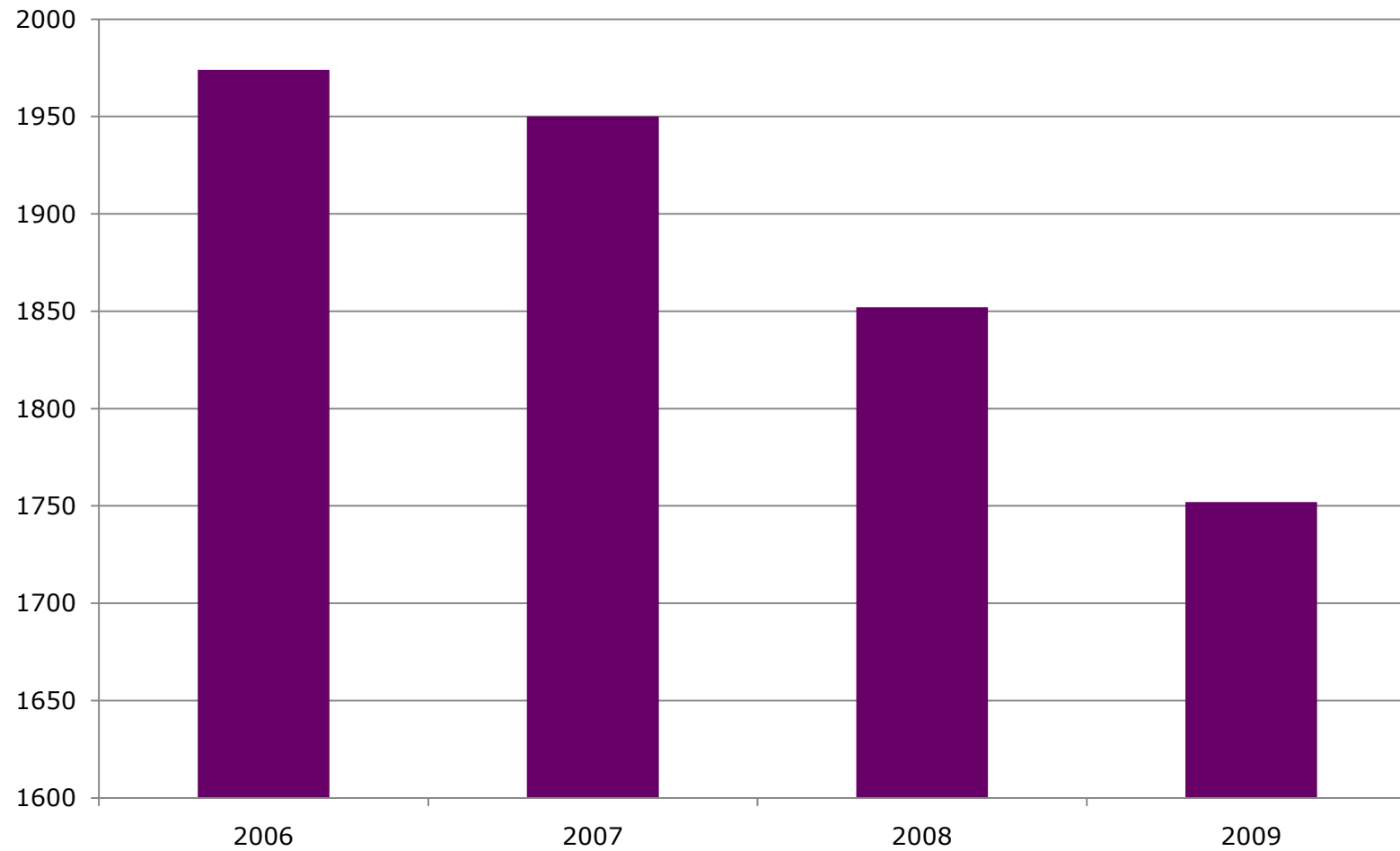
Dairies 1979 - 2009



Dairies



Dairies 2006 - 2009



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Planning for a new era

US industry has not been export ready

US industry has not been export ready

- Wrong products made
- Wrong specifications
- Weak or no customer relationships
- Inconsistent supply

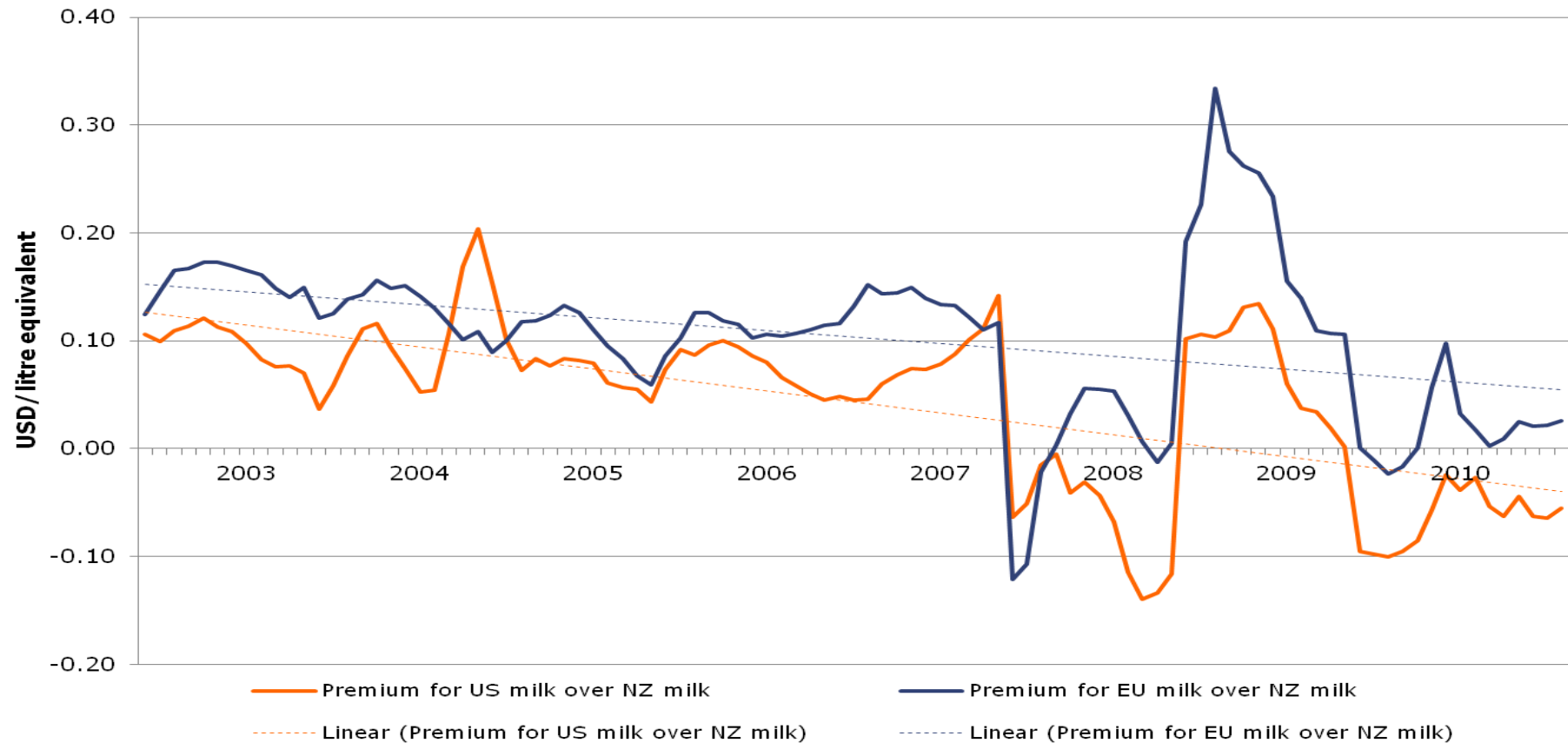
There is a real cost to this

- US commodities sold at a discount
- Industry funded subsidies used in a boom environment
- Milk prices lower than they could be....

US farmers now receiving less for their milk than NZ farmers

The rising value of export milk

EU and US milk prices less NZ milk price (2002-2010)



Source: USDA, Friesland Campina, Rabobank analysis

Note: US milk price is All Milk price, EU price is Friesland Campina milk price, NZ price is Fonterra commodity

Planning for a new era

Processor considerations

- Solutions are straight forward, but require application
- Signs that progress is being made
- But US market discount suggests the industry isn't there yet

Old regulatory system no longer appropriate

- Designed for a domestic market era
- DEIP system has little firepower
- CCC provides little protection

Producer considerations

- Global market era opens up opportunities for greater expansion
- But likely to be characterised by volatility
- Businesses need to be well managed to minimise that
- And robust to withstand what cant be mitigated

Conclusions

- US dairy industry has entered a global market era: it can't easily go back
- Has important implications all along the US supply chain
- Global market represents an opportunity, but also a threat (especially if interface not managed properly)
- US industry needs to act to thrive in this new era
- Progress is being made, but more needed.

Contact details

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***“The financial link in the
global food chain”™***



Rabobank

DAIRY MARKET OUTLOOK

February 2011



WHO WE ARE



- Research, consulting and risk management strategy firm
- Subscription service includes numerous, popular reports covering all aspects of the dairy markets – globally
- Price forecasts and market analysis for multiple markets
- Staff with relevant, applicable experience
- Strategic, long-term engagements with clients
- Highly-detailed, highly-specialized projects



- Licensed commodity broker introducing business to ADM Investor Services
- Trading desk staffed with experienced professionals
- Expert order handling in thinly traded markets
- Premier order execution on Globex via industry-leading OAK Desktop trading platform or using dedicated resources on the CME Group trading floor



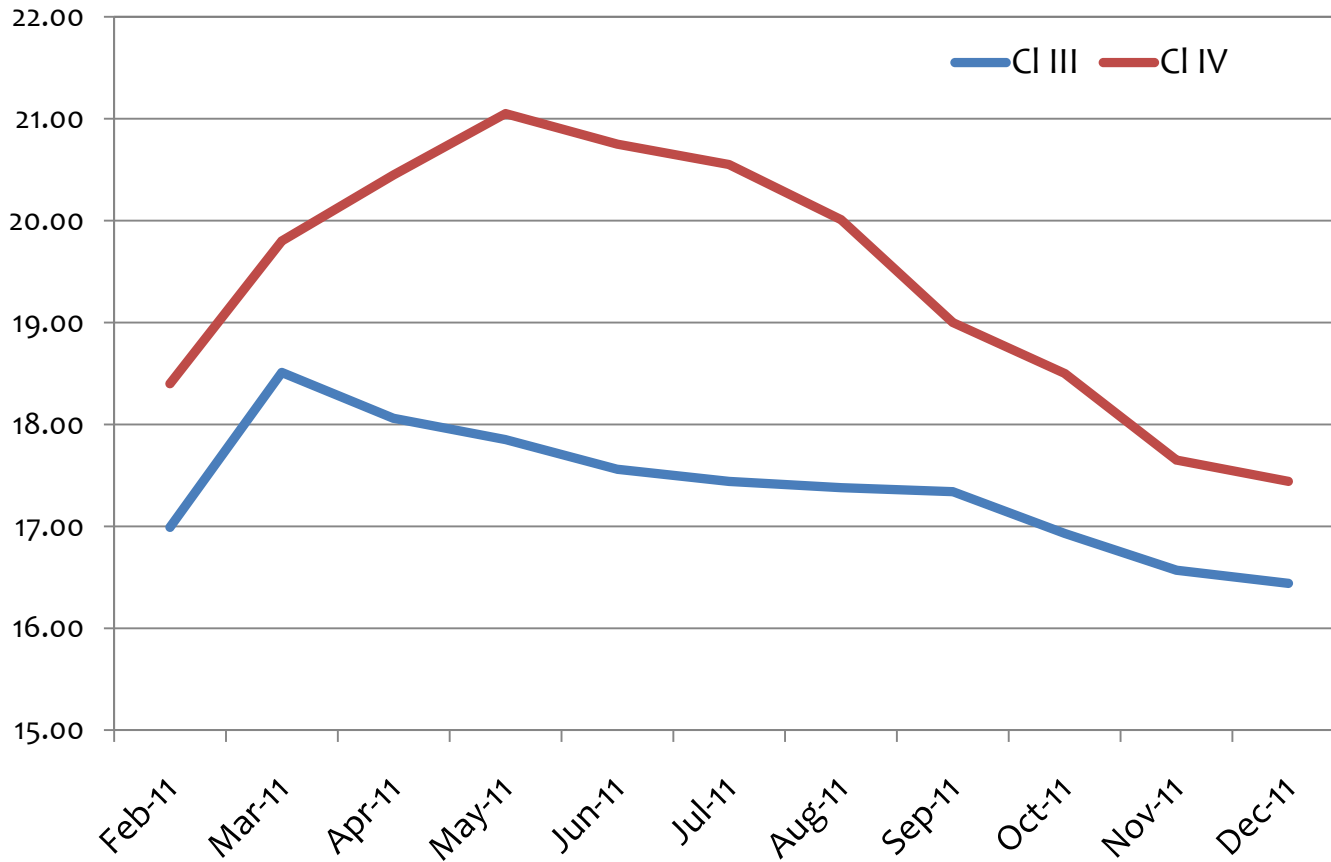
- Firm established to help clients find over-the-counter risk management solutions
- Operates in partnership with Wells Fargo Bank
- Works with clients at each stage in the marketing chain, offering access to liquidity in several product lines and combinations
- Detailed understanding of client needs and dedication to finding structures satisfying those imperatives

WELCOME RELIEF



SOME REAL OPPORTUNITIES

MARKET CLOSE FEB 18, 2011



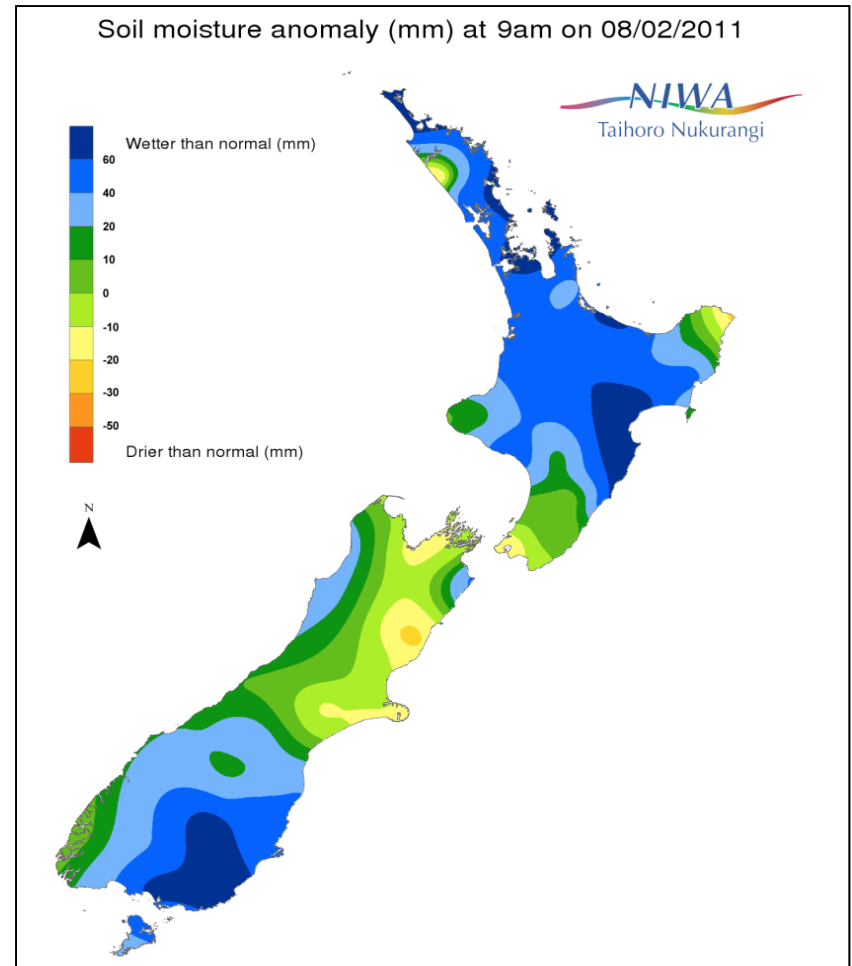
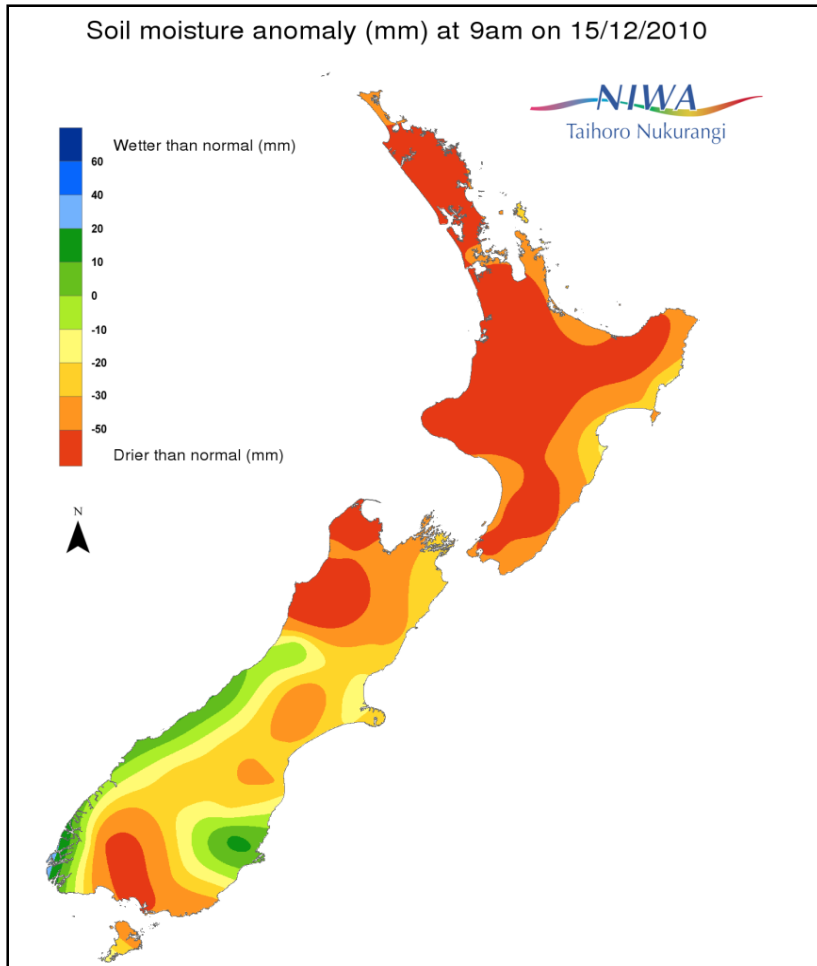
HOW WE GOT HERE

- The drivers of the recent rally are mostly international
- Predictions for 6 - 12% milk production gains in New Zealand for the 2011 season were thwarted by a late 2010 dry spell
- Strong milk powder demand by China after a sharp fall off in Aug – Oct
- Drought induced demand from Russia
- Insufficient inventory of butter and powder
- Buyers cupboards were bare coming into January as they were expecting a price break before restocking
- Expectations of a price break were predicated on strong NZ milk production

HOW WE GOT HERE

- **Structural tightness in butter and NFDM**
- **General bullishness in commodities**
 - **Psychological component**
 - **Real connection to milk price through production costs**
- **Emotion trumps fundamentals in cheese**
 - **“If everything else is high, why not cheese?”**
 - **Speculative interest in cheese/Class III is at a peak**

NZ RAINFALL IMPROVING

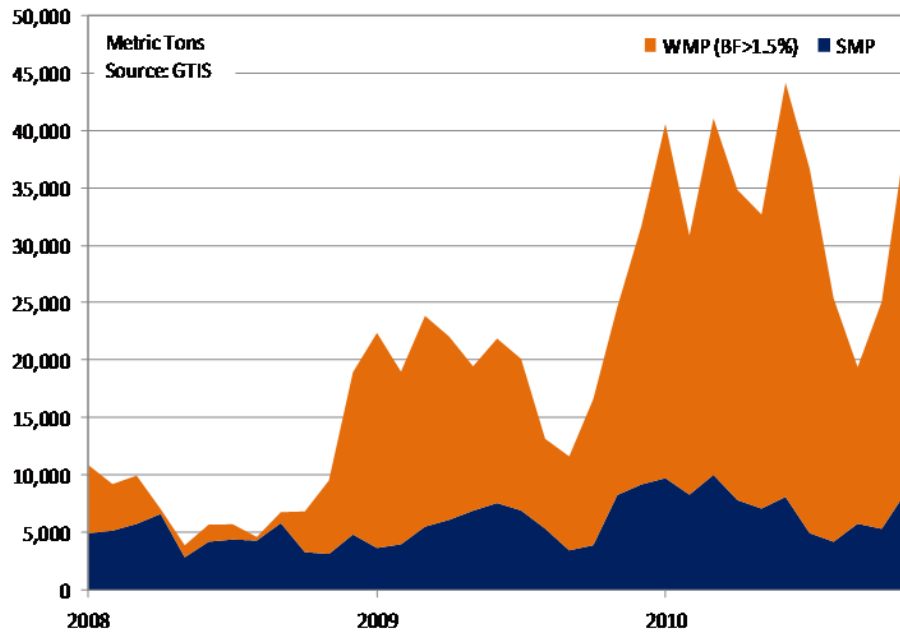


PUBLISHED REPORTS

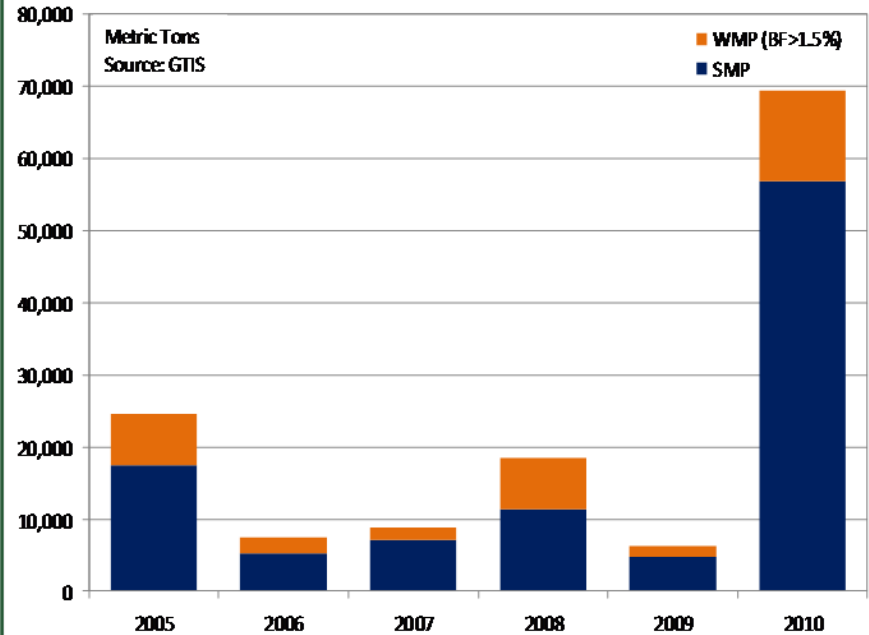
- **June: Dairy production is forecast to expand by 14 percent in the year to 31 May 2011, so long as climatic conditions allow milk yields to recover. (MAF Situation and Outlook)**
- **Sept 28: Looking further ahead Agrifax continues to predict 3 – 5% growth in New Zealand's milk supply for the current production season.**
- **Fonterra collected a daily record volume of milk on 27th October which was 4% higher than the volume collected at “peak” in the previous season.**
- **Dec 21: While on a season basis we estimate New Zealand is currently 1.4% ahead of last year**
- **Jan 20: Milk production running only around 0.5% ahead of last season but we see potential to achieve 2 - 3% growth for the current season.**

GLOBAL DEMAND

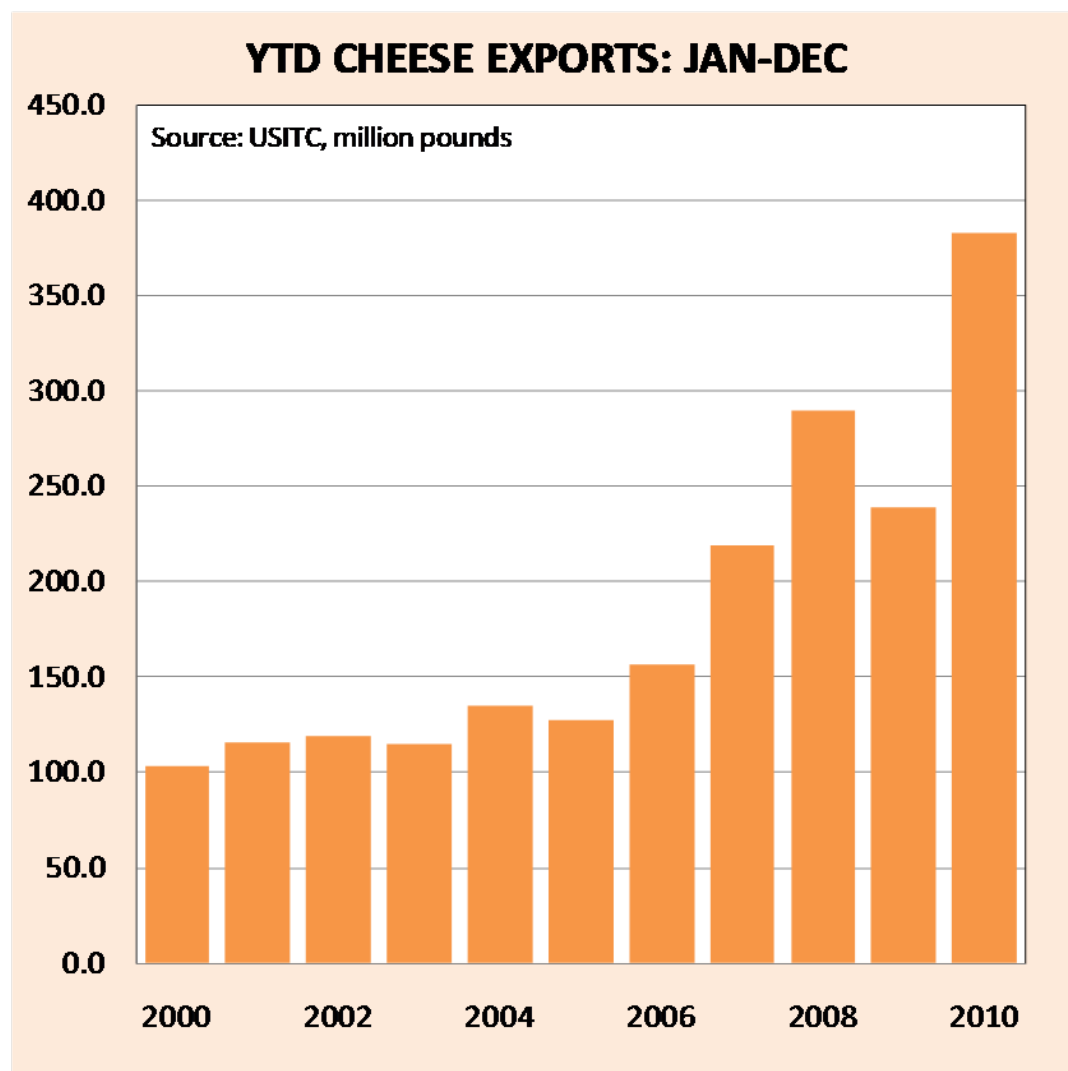
CHINA MILK POWDER IMPORTS



JAN - NOV RUSSIA MILK POWDER IMPORTS

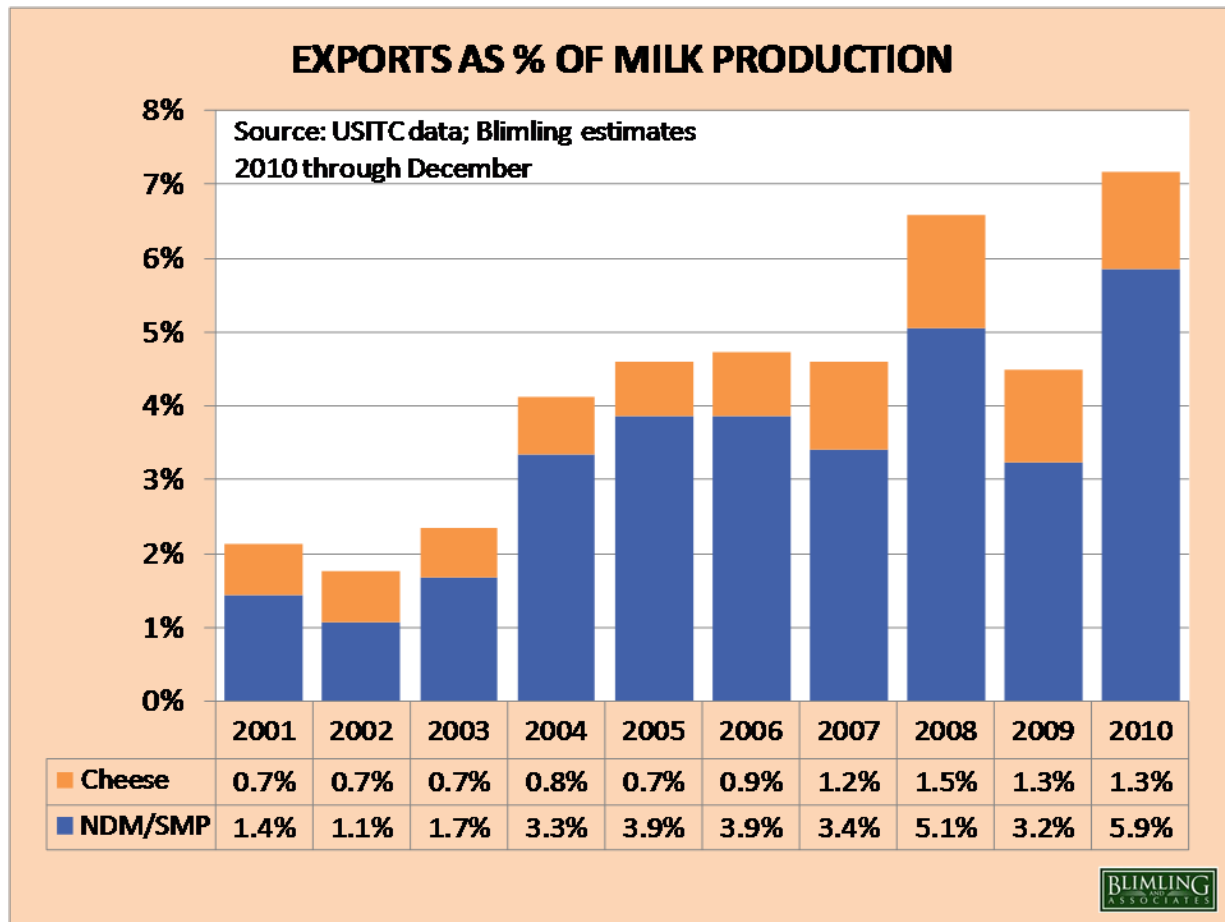


RECORD CHEESE EXPORTS



The trend has been toward greater export volumes and lesser import volumes. Is there any reason to expect a change in trend --- even if 2011 volume is down?

7% OF US MILK SUPPLY EXPORTED



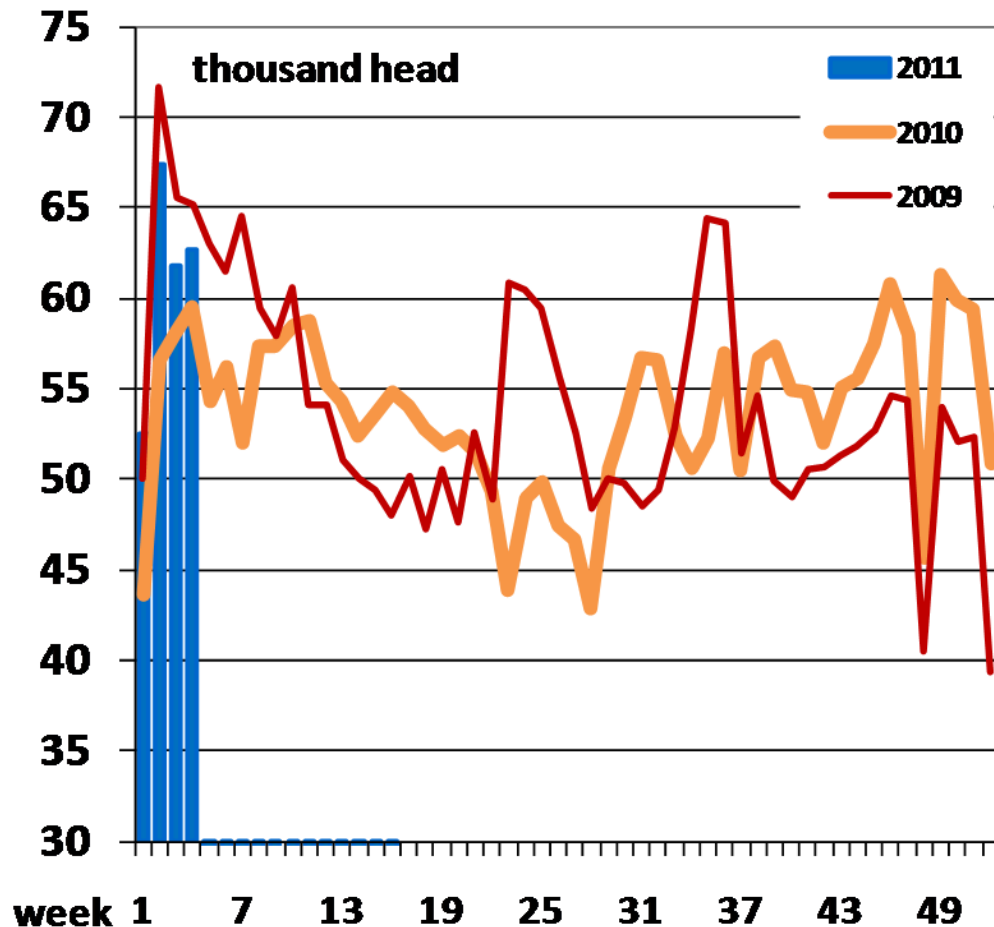
The swing in export opportunities between 2008 and 2009 was in large part a function of New Zealand having more product available. 2010 is a function of strong Russian and Chinese demand making room in the global market for US product.

COST SIDE PRESSURE



CULLING HAS BEEN BRISK

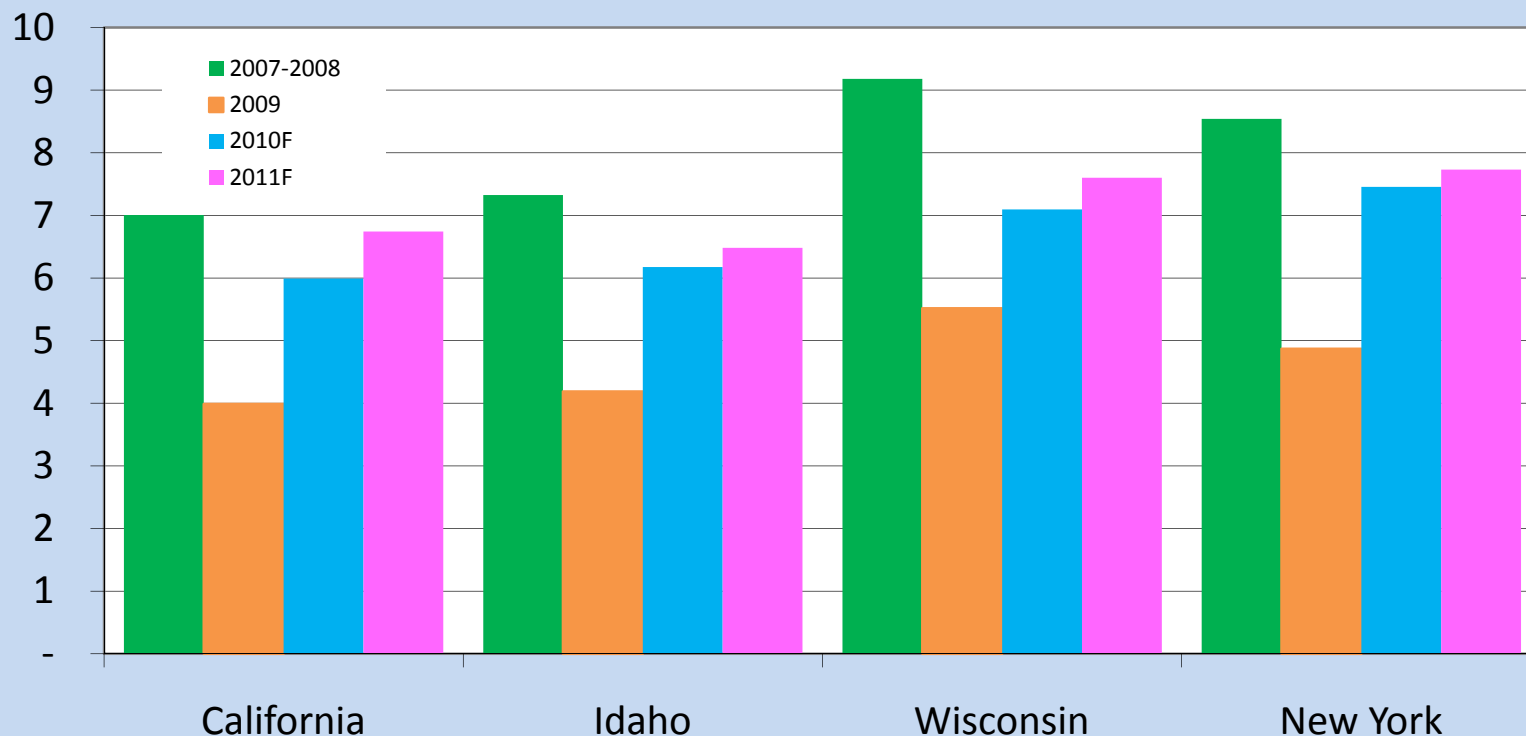
DAIRY COW SLAUGHTER



- Culling activity has been strong in response to high cull cow prices and abundant heifer supply
- High milk and springer prices should slow culling

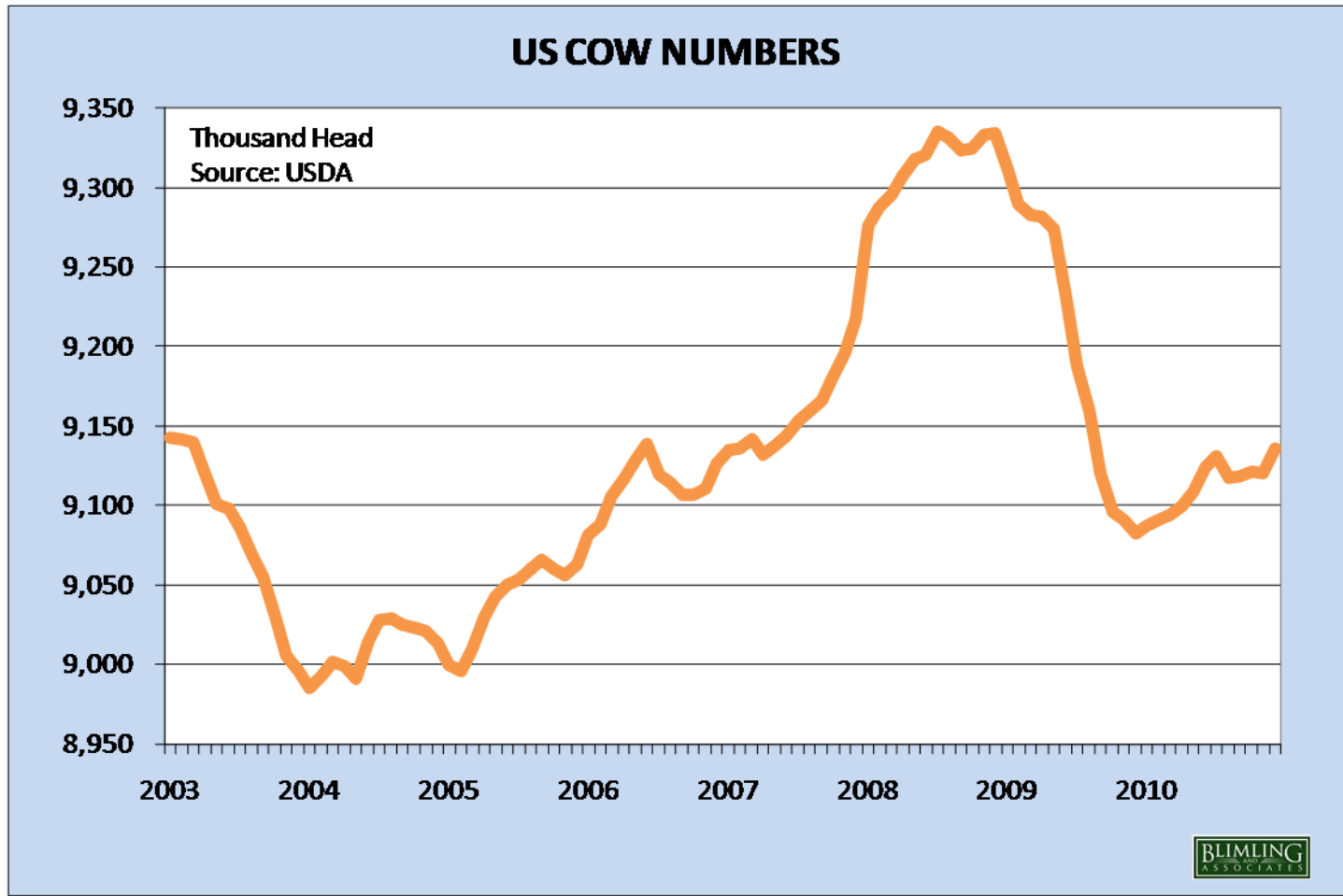
FARM MARGINS IMPROVING

ESTIMATED MILK INCOME OVER FEED

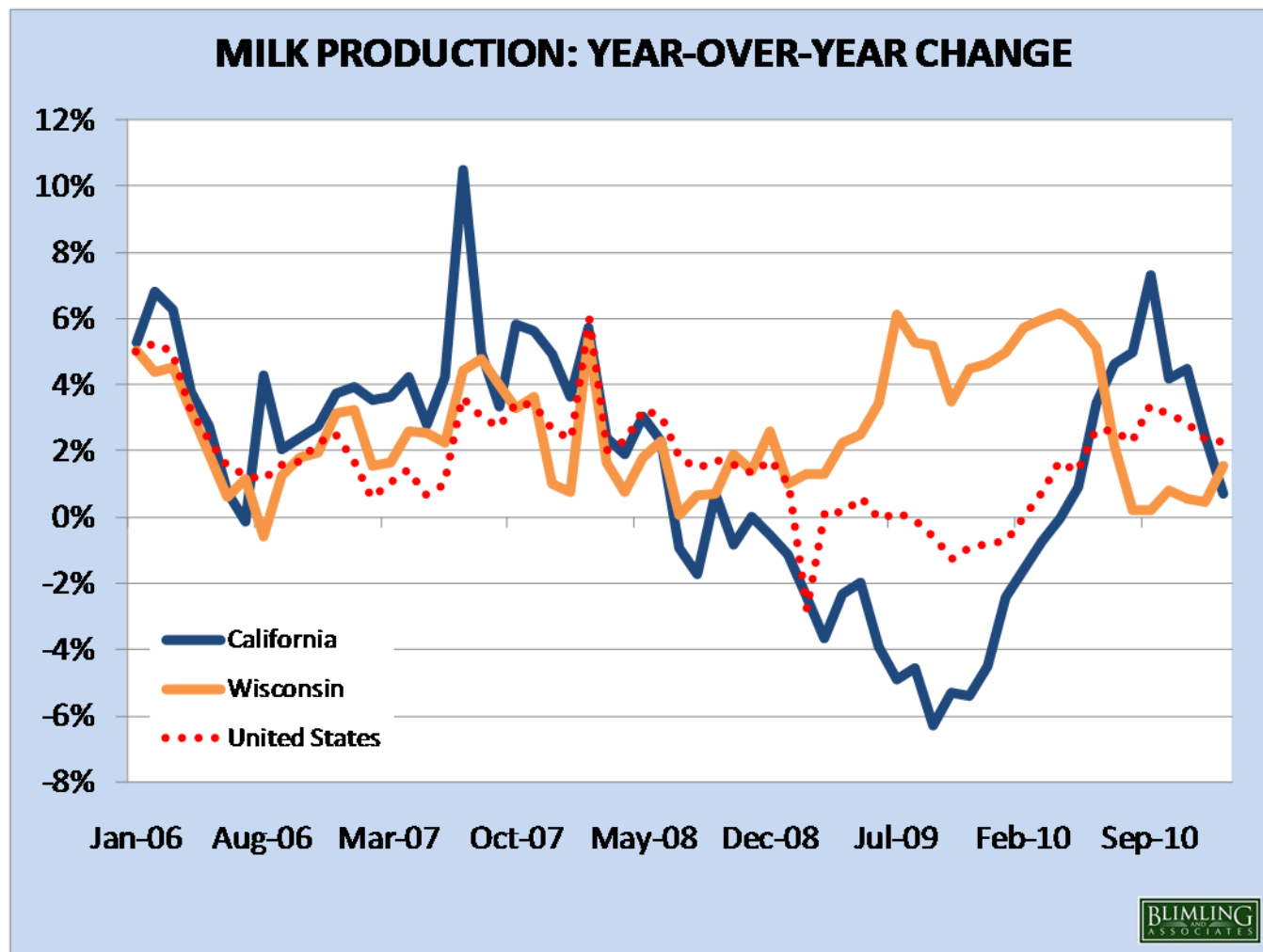


BLIMLING
AND
ASSOCIATES

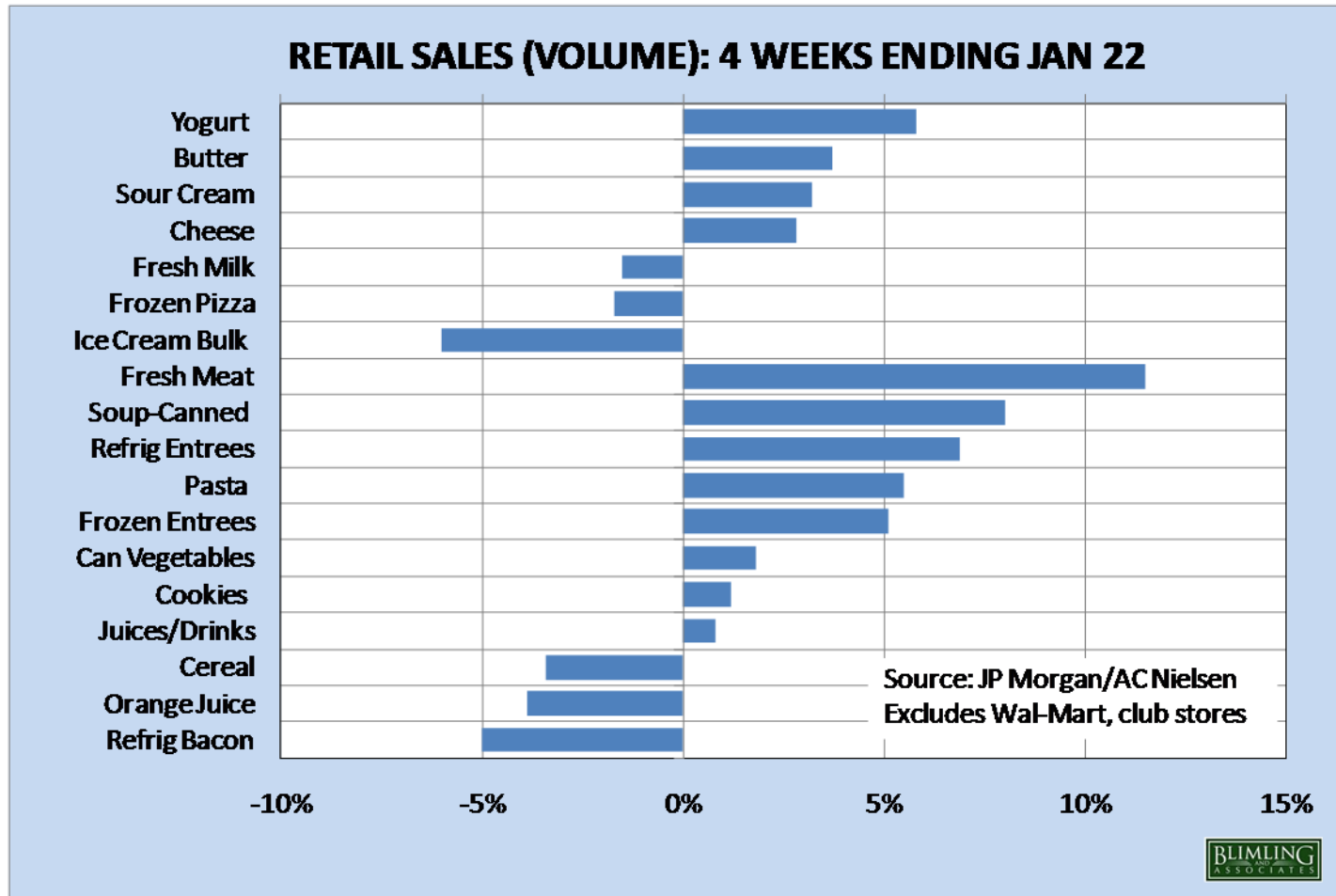
COW NUMBERS GROWING



WESTERN MILK SURGE?

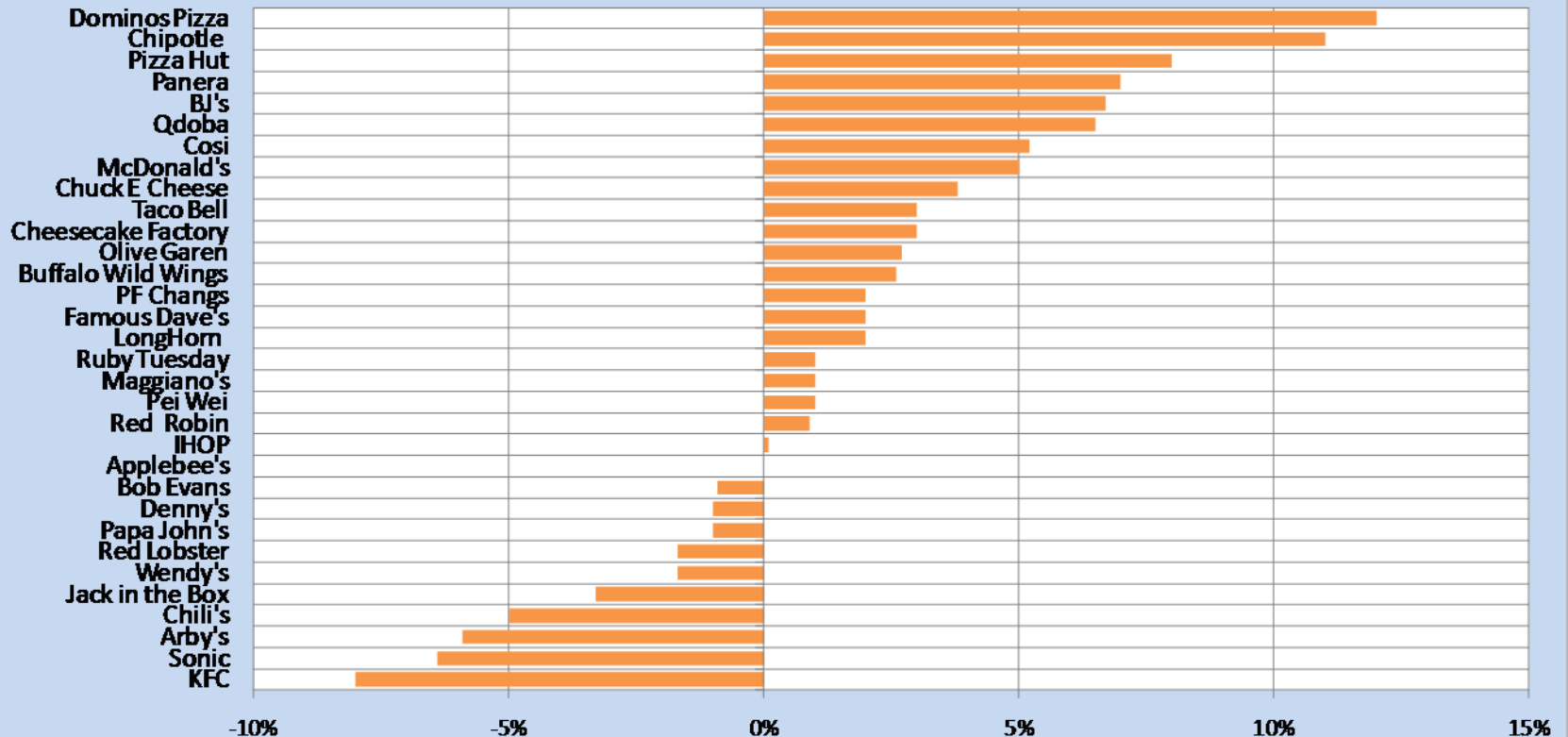


RETAIL SALES MIXED



RESTAURANTS IMPROVING

RESTAURANTS: SAME STORE SALES Q3'10VS Q3'09



SUMMARY

- Things will be good for the near term
- Butter/powder (Class IV) is on firm fundamental footing . . . cheese/Class III is a bit less so
- Strong exports are key to maintaining price
- Rally has been fueled by “one time shocks” such as Russian drought and NZ drought that will/have improve(d)
- Chinese demand and general commodity bullishness are more likely to endure

PRESSURE ON DAIRY COMMODITIES?

- One scenario leads to lots of milk without domestic or international demand
- On the flip side, if New Zealand doesn't make as much and Asian demand remains strong, California dairymen are well positioned to serve the world market.
- If this is the starting point, a defensive risk management strategy is required.

AND THEN THERE IS GRAIN...

- Feed costs are spiraling upward
- Hay prices are now joining grains – especially in CA
- Producers are more exposed to “spot” feed pricing than in the past due to lack of access to operating capital
- Milk prices are poised to fall as feed costs are rising
- Consumers simply can’t pay the price that dairymen require to cover their feed costs, especially during the winter/spring season
- Margin pressure on dairy producers could mean more liquidation at \$15/milk than was previously likely

THANKS FOR YOUR PARTICIPATION

This information is carefully compiled but not guaranteed to be complete or free from error, nor does it constitute a solicitation to buy or sell futures/options contracts.

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