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ACRE: Price Support or Crop Insurance?

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Although farm programs and crop insurance programs are increasingly similar, one feature continues to differentiate them: crop insurance programs use prices that reflect market conditions at sign-up time, whereas farm programs do not. Crop insurance programs must use current price information to set guarantees to keep farmers from moving into or out of the program based on whether revenue guarantees are more or less likely to generate a payout. Because the government does not ask farmers to contribute toward meeting the costs of farm programs, there is less financial need for the programs to reflect current market conditions. But the lack of influence of current market conditions on the prices used to set farm program guarantees often means that these programs will offer too little or too much support to farmers.

Today’s Safety Net
Currently, the only traditional farm program that offers any support to corn, soybean, and wheat farmers is the direct payment program, because it does not depend on the level of market prices. The countercyclical and marketing loan programs offer little or no support because market prices are expected to stay well above the levels that would trigger payments. The situation in the late 1990s and early 2000s was exactly the reverse in that the fixed support prices generated large payments to farmers and likely caused farmers to plant for the government rather than the market.

The new ACRE (Average Crop Revenue Election) program uses a hybrid approach to setting price guarantees by using a two-year moving average of past prices. This means that ACRE guarantees will reflect market conditions of the two previous years, but not necessarily of the current year.

As farmers finalize their 2009 spring planting decisions, estimated ACRE prices for the 2009 crop are $4.20/bu for corn, $9.88/bu for soybeans, and $6.67/bu for wheat. If 2009 state yields are close to their past five-year average, then ACRE payments will commence if prices fall 10 percent below these levels. Thus, ACRE provides good price protection (at a cost equal to 20 percent of a farmer’s direct payment) at $3.78/bu, $8.89/bu, and $6.00/bu for the three crops. For corn and soybeans, these protection points are somewhat below the expected market price. For wheat, the expected market price is about $5.50 per bushel, which is below the level of the ACRE protection point.

ACRE Probable Payouts
The graph below shows the range and associated probabilities of national average per acre payouts by crop if all 2009 corn, soybean, and wheat acreage is enrolled in ACRE. Large payouts will occur if 2009 prices drop dramatically or if large-production states have low yields. The vertical axis shows the probability that average U.S. ACRE payments per acre will be greater than or equal to the indicated level on the horizontal axis. As shown, there is a 50 percent chance that corn payments will exceed $7 per acre, a 50 percent chance that soybean payments will exceed $9 per acre, and a 50 percent chance that wheat payments will exceed $12 per acre. Given that 20 percent of per acre direct payments comes to an amount much lower than these payments, the chance is much better than 50-50 that average ACRE payments will exceed the average loss in direct payments. This suggests that many corn, soybean, and wheat farmers will find it advantageous to enroll in ACRE.

Because ACRE looks to the past for prices, and because ACRE guarantees can only change by a maximum of 10 percent in any year, there is a chance that 2010 ACRE guarantees will be much greater than what producers can expect to get from the market for their 2010 crop. This will occur if there is a large drop in crop prices during the next 10 months. Under these circumstances, farmers could once again use government prices instead of market prices for guidance about what to plant. This potential weakness of ACRE could have been avoided had Congress followed the precedent of crop insurance, which bases its guarantees on futures prices rather than historic prices.◆