Making the right crop insurance choices for 2014

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Buying crop insurance and making coverage decisions will be one of the most important risk management decisions farmers will make this winter.

The 2012 drought and 2013 drop in corn prices emphasize the need to manage revenue risk. Crop revenue coverage to insure against both yield losses and price declines the past two years has kept most farm operations financially viable. With lower corn and soybean projected prices forecast for 2014, crop insurance's ability to protect against loss of revenue will be critical.

With lower crop insurance revenue guarantees, many farmers may need more revenue coverage. For example, at the 75 percent coverage level, 2014 ratings for premiums are projected to be between 2 and 5 percent lower than those in 2013.

However, revenue guarantees are tied to new crop futures prices, which will likely drop 10 to 20 percent from those in 2013. A farm level revenue protection or revenue protection (RP) coverage this year with the same actual production history (APH) as last year may fall below the cost of production for many farm operations. Meanwhile, most crop production costs will remain high in 2014, lagging the decline in commodity prices, putting a squeeze on margins.

Having a crop revenue insurance protection policy, along with using a well-prepared and properly executed grain marketing plan, will allow farmers to protect the majority of their revenue.

Revenue guarantees lower

Farmers should consider moving to higher coverage levels to offset a portion of the risk with lower crop revenue guarantees. Revenue guarantees this year are calculated using the average futures price in the month of February for the December 2014 corn contract and the November 2014 soybean contract. These prices are called “crop insurance projected prices.”

The first step to using a crop insurance RP policy as part of your risk management strategy is to choose the right level of coverage. Farmers who insured at 75 percent with RP last year might consider increasing to 80 or 85 percent levels of coverage for 2014.

For example, say a farmer's corn APH is 180 bushel per acre and he is insured at the 75 percent level. With 2013's $5.65 per bushel projected price level, the per-acre guarantee was $763. This year’s guarantee may only be $4.50 per bushel, however, which means revenues of $608 per acre are protected. That's a revenue guarantee decline of $155 per acre compared to last year.

**Trend-adjusted (TA) option**

Farmers should nearly always take the TA option. That's the cheapest way to increase revenue guarantee without paying additional premium. By choosing the TA yield option, farmers can protect a higher level of yield than their 10-year APH yield average for a very small increase in premium. In fact, they might get an extra 8 to 10 bushel per acre for corn above their 10-year APH for the least amount of additional premium cost.

**Enterprise vs. optional units**

For most farmers, enterprise units make the most economic sense. At the 75 percent level of coverage, enterprise unit premiums are subsidized at 77 percent; for optional units, the subsidy is only 55 percent.

USDA’s Risk Management Agency increased subsidies for enterprise units beginning in 2009 because when farmers use enterprise units, similar crops are combined across the county to determine indemnity loss. In contrast, using optional units provides coverage for similar crops within the section of land. Farmers take more risk when using enterprise units but receive a larger percent subsidy.

If farmers have insured acres in more than one section of land, they should look at using enterprise units; they'll get the largest premium discount. Optional units insure crops at the section line. With enterprise units, they're combining all of their cornfields together in the county and all their soybean fields together in the county. This is where adding supplemental coverage fits in.

**Adding supplemental coverage**

Farmers need to look at having some supplemental crop insurance products, in addition to revenue protection. Various supplemental policies can be added to multi-peril RP policies. The supplemental policy choices include crop hail, wind and greensnap coverage, weather products and projected price discovery products.

If a farmer decides to use enterprise units and the TA option, he can add supplemental insurance products such as hail, wind and greensnap policies.

By using enterprise units, farmers will save more on the premium, but they’re exposed to risk when hail hits one of their farms, but doesn’t hit the other corn fields in the county.