

May 18, 2011

Friends:

Since the widespread adoption of the massively subsidized crop insurance program, its effects on farmer behavior have been widely debated.

This year, with simply pathetic weather in the eastern cornbelt, many are claiming that they will simply take the Prevented Planting option and not plant a crop. Since we don't buy that type of insurance (only use GRP) I did a little research in to the way the game works.

The effects of this may indeed have far-reaching impacts on our farm's risk management plan.

EXAMPLE (please correct if there is a mistake!)

An Indiana example.

55 bu APH Soybeans, 13.49 Price, 85% coverage, 60% PP. = $55 \times 13.49 \times .85 \times .6 = \$378/\text{ac}$

180 bu APH Corn, 6.01 Price, 85% coverage, 60% PP = $180 \times 6.01 \times .85 \times .6 = \$552/\text{ac}$

The premium paid for the insurance is irrelevant at this point.

OPTION A

Take PP on the corn equals \$552 Gross - \$100 embedded input costs (fert lost, spray/mow 3 times) = \$452 gain

OR

OPTION B

Take PP on corn and plant to beans, get partial PP pay. Corn PP Gain = $\$552 \text{ gain} \times 35\% = \$193/\text{ac}$ in your pocket. Plus you have the insurance on SB which assures a gain of $\$378/\text{ac} - \$85 \text{ input cost} = \$293/\text{ac}$ gain. So, insured MINIMUM gain combined would be = $\$486 (193+293)$

If you grow 50 bu beans @ \$13.00 = \$650 - \$100 inputs = \$550 gain

SO, you likely make \$550 planting the beans plus the \$193 PP corn payment for \$743 Total, vs, \$452 to not plant.

Unless I am wrong, there is a HUGE incentive to take PP on corn and then PLANT BEANS. \$291/acre. As well, you are insured to at least make the same amount that you would by not planting beans.

OR, there is a nice incentive to just plant late corn and take the ins. minimum gain of $\$552/\text{ac} - \text{inputs} - 1\%/\text{day}$ after June 5th. So, again, big incentive to take PP corn and plant beans.

PLAN IMP:

As the above highlights, soybeans have the potential to gain a few million acres resulting in a major price decline. Plus, the western corn belt is planted into very good condition during the ideal window. Crop condition scores in June should be very high.

IT IS NOT A TIME TO BE TAKING PRICE RISK. For soybeans especially, but nor for corn or wheat. The wheat seasonal is horrendous for the next 6 weeks.

Yes, there is some timing harmony that projects a potential final top around June 3rd, but this is very late in the game. New highs are only possible with ongoing weather failure. That is not a wise bet to make as a producer.

Take care,
Ken