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Use Crop Insurance as a Risk-Management Tool

Due to continued tight margins in crop production for the 2017 crop year, some farmers are contemplating reducing their crop insurance coverage in order to save on premium costs.

While there may be a small savings in the premium costs per acre, that decision could add considerable risk to the farm operation for the coming year. Many farm operators remember a few years ago when crop insurance coverage virtually guaranteed a profit from crop production in a given year. Crop price guarantees have changed and that may no longer be possible. However, the risk protection provided by crop insurance coverage may be more important now than ever.

The price guarantee for revenue protection (RP) crop insurance coverage for corn in 2013 was $5.65 per bushel. At that base price, a farm operator with a 180 bushel-per-acre actual production history (APH) yield could guarantee over $860 per acre with an 85 percent RP insurance policy, and over $810 per acre with an 80 percent RP policy. The average corn costs per acre on rented land in southern Minnesota for direct expenses, overhead costs, and land rent (based on the University of Minnesota's FINBIN website), was approximately $870 per acre in 2013.

The situation with soybeans and RP insurance coverage in 2013 was similar to corn. The 2013 price guarantee for RP soybean crop insurance was $12.87 per bushel. At that price guarantee, a farm operator with a 50 bushel-per-acre APH yield could guarantee nearly $550 per acre in 2013 with an 85 percent RP insurance policy, and approximately $515 per acre at 80 percent RP insurance coverage. The average FINBIN soybean costs per acre in southern Minnesota for direct expenses, overhead costs, and land rent was approximately $540 per acre in 2013.

The revenue guarantees per acre provided by RP crop insurance policies in 2013 virtually covered all direct and overhead expenses, as well as land rental costs, and in some cases, provided a small profit margin. By 2015, the corn price guarantee dropped to $4.15 per bushel, which lowered the dollar guarantee with a 180 bushel-

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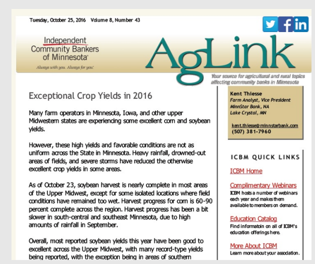

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per-acre APH yield to near $635 per acre with 85 percent RP insurance coverage, and to just below $600 per acre with 80 percent RP coverage. The 2015 corn average expense for land rents, direct and overhead expenses, still exceeded $800 per acre in many instances. Similarly, for soybeans, the RP price guarantee for 2015 was $9.73 per bushel, lowering the guarantee to just below $415 per acre with a 50 bushel-per-acre APH yield and 85 percent RP insurance coverage. The 2015 average expense for land rent, direct and overhead costs for soybeans was still near $525 per acre.

For the 2016 crop year, the RP crop insurance price guarantees dropped even further to $3.86 per bushel for corn and $8.85 per bushel for soybeans. However, the average total costs of production for corn and soybeans also declined significantly from 2015 levels. It appears that the 2017 crop insurance price guarantee for corn should be similar to 2016 levels, possibly slightly higher, and should be considerably higher for soybeans, compared to 2016 price guarantees. As of February 10, the RP price estimates were $3.96 per bushel for corn and $10.20 per bushel for soybeans.

Using those price guarantees, and a 190 bushel-per-acre APH corn yield, the resulting revenue guarantee would be near $640 per acre with an 85 percent RP policy and just over $600 per acre with an 80 percent RP policy. If we assume a 52 bushel-per-acre APH soybean yield, the resulting revenue guarantee would be just over $450 per acre with an 85 percent RP policy and near $425 per acre with an 80 percent RP policy. Estimated, average 2017 production costs in southern Minnesota for land rent, direct and overhead expenses, are expected to be near $700 per acre for corn, and $460 per acre for soybeans.

Some producers tend to overlook crop insurance as an important risk-management tool, since the available revenue guarantees are lower than the cost of production in many situations. However, the overall financial risk in 2017 may be far greater than it was in back or 2013, when overall crop revenues were much higher. Crop insurance premiums for 85 percent RP coverage for corn and soybeans in many areas are much more favorable now than they were in previous years. Some producers have been able to increase their APH corn and soybean yields in recent years by using the trend-adjusted-yield endorsement for their crop insurance coverage. This has helped expand the insurance guarantee with only a minimal premium cost increase.

In the 2016 crop year, many farm operators in south-central and southwest Minnesota saw the benefits of having 80 percent or 85 percent RP crop insurance coverage for corn and soybeans. Some portions of this region received record rainfall during the 2016 growing season and were impacted by severe storms with excessive rainfall events and hail, causing significant crop loss. In addition, the 2016 corn price dropped from a RP price guarantee of $3.86 per bushel in February to a harvest price $3.49 per bushel in October. This resulted in some substantial crop insurance indemnity payments for producers who incurred significant yield losses on corn in 2016 and had 80 percent or 85 percent RP crop insurance coverage in 2016. Producers with lower levels of coverage received very minimal 2016 indemnity payments.

As we enter 2017, we continue to have very tight crop margins for the coming year, and in some cases, negative margins on cash rental acres to cover land rents, direct, and overhead costs. Before reducing crop insurance coverage for 2017, a producer needs to assess whether they want to take on the extra risk of the reduced revenue guarantee of the lower crop insurance coverage. Reducing from an 85 percent RP policy to a 75 percent RP policy will reduce the insurance guarantee by $70-$80 per acre for corn, and $50-$60 per acre for soybeans. Producers are also encouraged to discuss this with their ag lender, before finalizing their 2017 crop insurance decisions.

The deadline to purchase crop insurance for corn and soybeans for the 2017 crop year is March 15, 2017. For more information on various crop insurance policies and alternatives for 2017, producers should contact a reputable crop insurance agent.

Kent Thiesse has written an information sheet titled: "2017 Crop Insurance Decisions". To receive a free copy of this information sheet, please forward an e-mail to: kent.thiesse@minnstarbank.com.

The following websites are also good sources for crop insurance information:

- University of Illinois FarmDoc
- USDA Risk Management Agency

For more information, contact Kent Thiesse, Farm Management Analyst and Vice President, MinnStar Bank, Lake Crystal at: 507-381-7960 or kent.thiesse@minnstarbank.com.

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