Gibson Insurance Group

"The Risk Management Specialists"

Crop Insurance 2014

Volume 14 Issue 3 September 2014

2015 Wheat Initial Price Guarantee

$6.01 *

estimated

Inside this issue:

GIBSON INSURANCE GROUP

337 Highway 50 East
P.O. Box 795
Tipton, MO 65081

Phone: 660-433-6300
Fax: 660-433-6315
gibsoninsurancegroup.com

2014 Farm Bill Sign-Up

This fall and winter all producers will be faced with the decisions on how to sign up their farms to take advantage of the 2014 farm bill. This sign up is very important because the decisions that we make at this time will remain in effect for the life of the bill. We will also have the opportunity to reallocate base acres that closer reflect the rotations that we plan on practicing in the next few years. This reallocation of base acres is something that very seldom happens so any decisions made may remain with us for the rest of our farming careers.

The two programs that we have to choose between are ARC and PLC. These programs are different but each could have advantages depending on your particular operation. There are times where ARC may be chosen on one crop or on one farm number and PLC will be chosen on another.

How do we decide what to do and why?

Before we even get into explaining these programs we need to arm ourselves with knowledge about our individual operations. Following are 10 questions that I would challenge you to research and answer on paper for each different farm number in your operation. This will be the first step in making the correct decision.

ARC or PLC ?

10 Important Questions

1. How many base acres do you have for each crop on each farm number? List the base acres separately between corn, soybeans, wheat, barley, and grain sorghum for <u>each</u> farm number. Now beside the base acres list the acres that you normally plant on this farm. This is important because planted acres will vary greatly from base acres. Producers may have converted crop ground to pasture or vice versa in the past. This will cause base acres and planted acres to vary greatly.
2. The grain markets have changed greatly over the last ten years. What do you expect the future to hold? Are we going to return to the prices of the last few years or are we in a downward spiral that will continue through the life of this farm bill? List on your paper what you expect over at least the next 3 years and why you think that this is the case. Remember there is no right or wrong answer, but this is an important step in deciding which program to choose.
3. How do your yields compare to the county average yields? Take time to look at your APH and compare it to the county yields over the last several years. Remember the weather in those years. Is your farm more prone to drought? The point is that some counties

2014 Farm Bill Sign Up (continued)

have a mix of quality hill land, good river bottom, and also considerable marginal crop ground; therefore some farms may be more prone to drought or flood than the county average. The results of this might be that your farm is consistently better or worse than the county average. In some of the new programs county yields will be used for triggers for program payments so it is important to do this step.

4. If you plant double crop soybeans, look at the county soybean yield carefully. Do your double crop soybeans correlate well with the county soybean yield? If you add your first crop soybean yield to the second crop soybean yields, does this come closer to the county average? This is more important as you go north in Missouri since many northern counties have less double crop soybeans planted due to the shorter growing season than southern Missouri. This step is very important if you plant wheat and double crop soybeans. Even if you don't plant wheat in your area, other producers in the county that do this practice can affect your trigger yields.
5. Look at your base acres. Do these bases reflect the rotation that you are currently using on your farm? Do you have a grain sorghum base or barley base that you are not using? These base acres can be moved to another crop that could be more advantageous to your operation. Remember a decision to change or reallocate bases should be considered a permanent decision. Seldom is there ever a chance to do this so consider this option carefully.
6. Now that you have collected this information on your farms, it is time to collect this same information on all rented ground. This will be a good time to talk to your landlords and help them make informed decisions on the farm bill as well. Operators will find that sometimes land lords may wish to choose a different program whether it be ARC or PLC. However, operators and landlords **must** choose the same program according to farm number. For operators who have a lot of rented farms it will be common for them to have ground in both programs at the same time.
7. Will your operation have any New Breaking ground in the next year? Over the past several years have you applied for a new breaking agreement that converted pasture land to row crop production? On these farms that have been broken, what are their bases for row crops? Many times land that has been converted from pasture will not have many if any base acres. This could greatly effect which program is most advantageous for enrollment.
8. At the risk of sounding like a broken record, do you know your cost of production for each crop that you are growing in your operation? I know that this is hard to do for some producers but it is imperative to know your current costs on the per acre basis. From the per acre basis it will be easy to convert these figures to a bushel basis by using your APH yields.
9. Do you have any irrigated ground? If so which crops could be irrigated in your operation? Does your irrigated practice cross section lines?
10. Finally the last question. Does all of your farm numbers have a conservation plan? Have you signed a 1026 on every piece of ground that you operate? The correct answer will be yes to this question. If you don't have this done it needs to be done now. I would suggest that every operator visit the NRCS office and get a copy of their 1026's for each farm that they operate. If a producer were to error and forget to do one farm, it will have a serious impact on the rest of the producer's operation. **This is very important , check now before harvest!!! Failure to have a signed 1026 for every farm on file may result in the loss of crop insurance subsidy!!!**

2014 Farm Bill Sign Up (continued)

Now that we have the information that we need lets look at the different programs and see where our operations fit. Remember we will be doing this by farm number and it is possible that we will choose different programs for different farms.

With the 2014 farm bill direct payments to producers have been eliminated. Farmers will no longer receive fixed payments per acre, whether crop prices are high or low or even if they plant a crop or not. With this new law producers must choose between two commodity programs. Price Loss Coverage (PLC) or Agricultural Risk Coverage (ARC). This is a one time decision will be effective and binding up through 2018 or up until the 2014 farm bill expires. These programs will provide income support to farmers under adverse price or yield conditions at levels above where their regular crop insurance coverage may apply.

We all remember the old ACRE program, ARC works very similar to this program that we remember from the last farm bill. These programs can get complicated so lets take a minute and walk through the program and the terminology and see how they work.

The ARC (county) is described as a program that establishes a county level revenue benchmark for crops that is equal to the five year Olympic average of county crop yields and national market prices.

This means that for my farm in Cooper county I will need to look at the yield history over the last 5 years for corn and throw out the high yield and the low yield and average the other 3 remaining years. Then I will do the same thing over the last 5 with the national market prices to establish a minimum revenue that this program will guarantee.

For Cooper county, Missouri the formula for corn will look like this:

Corn

Year	National Market Price	Yield
2009/10	$3.55	150
2010/11	$5.18	130.4
2011/12	$6.22	87
2012/13	$6.89	57.2
2013/14	$4.60	136

Now in order to get the Olympic average we need to throw out the high and low years for both the yield and price. For Cooper county we will discard 2009/10 as the low price and 2012/13 as the high price and average the remaining three years.

This will establish an Olympic average price that we will use of $5.33 per bushel for corn.

We must now do the same process for the yields. It just so happens that for Cooper county we will discard the same years since they had the high and low yields. This was by chance only.

When we average the remaining years we come up with a yield of 117.8 bushels per acre.

By multiplying the county yield and price we come up with the *county revenue benchmark* of $627.87 per acre. This is an important term to remember. The county revenue benchmark for corn in Cooper county is $627.87.

The ARC county program is designed to provide shallow loss coverage when actual county revenues fall below 86% of the revenue benchmark. For Cooper county this would mean that any time the county revenue on corn fell below $539.97 (86% of $627.87) a payment would start to generate.

The maximum payment that could be generated is 10% of the benchmark ($627.87 x 10%)or $62.78 per acre. This would only occur if the county revenue for corn fell to a level of $477.09 per acre. These payments are intended to come into play before your crop insurance policies kick in. <u>The down side to the program is that it only provides protection on 85% of the base acres that you have on corn.</u> This is important because many producers have more planted acres of a crop than they have base acres.

2014 Farm Bill Sign Up (continued)

Using Cooper county as an example:

In this county we have some very productive bottom ground and some highly productive hill ground. We also have some very marginal crop ground. In stressful years where there are small losses this program will possibly offer better protection to the more productive farms and to those farms that have a higher percentage of base acres.

If you do not choose to be in the ARC program you will be automatically enrolled in the PLC program by default.

PLC stands for Price Loss Coverage. This program is very similar to the old Counter Cyclical program (CCP) that we are familiar with from the past. The PLC program looks at commodity prices only and has no consideration to yield when calculating payments. This program is the easiest of the two to understand as we are always comparing the national marketing average price with a reference price to see if we are due a payment.

Reference prices of $3.70 corn, $5.50 wheat, and $8.40 soybeans have been established by law to be the reference prices for the length of this Farm Bill. Producers will be paid on 85% of their base acres when the prices fall below these levels. This makes this program very simple and predictable for the life of the bill.

Let me explain how this program would work for a Cooper county corn producer. There are a few pieces of information that need to be gathered to see how this product would work on your farm. First we need to come up with the number of corn base acres that is assigned to your farm. Secondly, we must come up with the program yield for these base acres. Lastly, we need to calculate your average yield from 2008-2012 and multiply this yield by 90% to arrive at this updated yield.

This producer has checked with the FSA office and has 100 corn base acres on his farm. FSA also informed him that he had a base yield of 86 bu/acre that was assigned to these base acres. When this producer averaged his yields from 2008-2012 the average for his corn was 118.2 bushels per acre. When we took this yield times 90% we came up with a new program yield of 106.38 bushels per acre. In this example it was well worth the effort to prove his yields to the FSA using crop insurance documentation to raise his program yield by 20 bushels per acre.

Now let's work an example based on the following two scenarios.

First, let's assume we have another banner year like we had this year and we have high yields nationwide driving the price of corn down to $3.25 per bushel for the national average market price.

The calculation would work as follows:

A Cooper county farmer **plants** 150 acres of corn.

He has 100 corn base acres.

This producer has updated his program yield to 106.3 bu/per acre (118.2 bu x 90%).

The national average market falls to $3.25 per bushel.

Remember the reference price is set @$3.70 per bushel

As you noticed the reference price is above the national market price so there will be a payment.

$3.70 (reference price) - $3.25 (national market price) = $0.45 per bushel difference.

Remember though this producer planted 150 acres of corn he only had 100 base acres. These payments are calculated on 85% of base acres. Therefore we have 85 acres x 106.3 program yield x $0.45 per bushel = total PLC corn payment of $4,065.97.

In the second example let's say that everything remains the same with the exception of the national market price. The national market price comes in at $4.02 per bushel.

In this example there will be no PLC payment as the national market price is higher than the reference price of $3.70 per bushel.

This same scenario will have to be run with both ARC and

2014 Farm Bill Sign Up (continued)

PLC on each crop that you have base acres for in order to see what is best for your operation .

Supplement Coverage Option (SCO)

***For PLC participants only*:**

Starting with the 2015 crop year, producers who choose PLC will be able to purchase a new Supplemental Coverage Option (SCO) as an inexpensive add on to their current crop insurance coverage. SCO essentially will allow producers to insure their remaining insurance deductible (up to a maximum of 86% coverage level) using a county-level yield coverage that mimics the type of insurance policy and levels that you currently have on your operation. The premium for SCO will be subsidized by 65%. These payments will not be subject to payment limitations.

This coverage follows the county yield and not the yield that you have on your farm. Therefore, it is very possible to have a good yield on your farm and still receive an SCO payment. The other important part to the SCO option is that it pays on all planted acres which differs from ARC and PLC which only pay on 85% of producers' base acres.

Producers will have the ability, in some counties of Missouri, to sign up for SCO on 2015 wheat. Remember, you will have to sign up for the PLC program in order to have SCO.

On my farm I will sign up for PLC and SCO. I think that I have a good understanding of the Farm Bill and how it will effect my operation. SCO will increase the coverage level on my wheat to 86% for only $2.77. On my operation this choice will work. However I would not suggest any producer to sign up for SCO until they take time to understand the Farm Bill and how these decisions could effect their operation. There are serious consequences for doing this wrong. As of this letter the FSA offices are still waiting to be trained on the two different programs. Therefore, it will be difficult for most producers to make informed decisions prior to late winter. This time frame will be well after the deadline of to sign for SCO wheat.

The Farm Bill tasked the Extension Service with educating producers about the different programs created in the bill. Once all the rules for the different programs have been published and agencies trained, it is our hope to partner with MU Extension, and possibly local FSA offices in setting up producer meetings in your area. We are hoping to set these up sometime later this fall .

Summer Weather: Good and Bad

The weather this summer has certainly been a very good one for the row-crop farmer. Rains, for the most part, have come just when crops have needed it and with amounts that will probably give producers historically high yields. Moderate temperatures during the growing season also helped to preserve soil moisture and reduce stress on growing plants.

While it appears that grain producers will not suffer a yield loss this year, forage production for area livestock producers was probably average to slightly above average in the late spring and early summer time period with these conditions. The rains this year have been extremely timely but the accumulated rainfall

ATTENTION LIVESTOCK PRODUCERS

Have you signed up for the 2012 Livestock Disaster yet?

Deadline is fast approaching: October 1

Livestock Risk Protection

LRP is a very simple and cost effective way of locking in a minimum price floor for your livestock.
Call us today so we can explain this program and its benefits to you and your operation.
660-433-6300

FYI

Harvest prices for corn, soybeans, and milo are set from October 1-31.

Corn—Daily close of the Dec14 Futures contract

Soybeans– Daily close of the Nov14 futures contract

Summer Weather: Good and Bad (continued)

amounts have not matched our normal amounts for the year so far. Producers with PRF coverage for the May and June period more than likely will suffer a loss. How can that be?

PRF coverage is based on a calculated historical index of the average amount of rainfall for specific periods of time over specific land areas. In the area of Central Missouri from Marshall to Fulton to Iberia to Warsaw there are 30 of these specific land areas (grids). During the May/June period the amount of rainfall that was recorded was lower than 90% (anything 89% or below will generate a loss), for all but 3 grids. These were located around the Fulton area. The majority of the grids in this area only had about 70% of normal rainfall index amount. At this level, producers including myself, will be receiving loss payments of $10-12 per covered acre. These amounts will pay the premium and leave some left over to help pay for fertilizer and forage harvesting. In addition, these producers still have at least another 60 days of coverage for the year. There was enough rainfall for initial forage growth but with grazing pressure or the harvest of forage the regrowth needed was impacted by the less than normal amount of precipitation. Grass is the cheapest source of feed for a livestock producer. Whenever we have periods of less than normal precipitation it can create a situation where the cost of forage goes up and the price of cattle goes down. This is why we think this product is so important for the livestock producer.

Wondering how much rain? There is now a place a producer can go to find out how much daily rainfall your farm or grid is getting. The Risk Management Agency has tasked the University of Missouri Extension with designing a program that will track daily rainfall amounts for specific grids in the state of Missouri. After signing up a producer will be emailed reports that track the rainfall amounts for his particular grid(s). Here is the link to their website to get your account signed up:

http://agebb.missouri.edu/horizonpoint/begin.htm.

You will need an email address, street address, and the latitude and longitude of your farm (MU Extension is working on an update that will allow you to enter your grid ID(s) instead). You can also go to the University of Missouri's Extension website:

http://crops.missouri.edu/insurance/prfinsurance.htm

Contact Ray Massey or John Travlos of Extension, two of the leaders of the project, to get more information on how it works and what your reports will look like.

Cattle Markets: Where to now?

In the cattle market this last week we found ourselves again near and in some cases setting all time price records. The fed cattle market was in the $162.00/cwt range while the feeder cattle market was reaching the contract high of 224.75. This market has created a lot of discussion around the office here and we are perplexed with the strength of these markets and where it is coming from. From supply side economics we understand that we do have the smallest cattle herd in the last 50 years. We do know that Asia is importing our most prime cuts of meat and the margin achieved by these cuts our supporting the less expensive cuts. But we have to ask ourselves is this the only thing that is going on?

This weekend I had the opportunity to visit with some cattle feeders and was concern with the market outlook that they projected. This outlook suggested that the only reason that the market was where it was is because of the short supply of cattle. It was their thought that this market

Cattle Markets: Where to now? (continued)

could not change direction until the herd size can be rebuilt to a point where we would have to discount the price in order for consumers to add more beef to their diets. Their point was that for the current time high prices in the beef industry were here to stay at least for the next several years. I cannot agree with this school of thought so we decided to look at historical prices and try to figure out what other factors were helping support this market.

In 1995, the cattle market was starting a gradual up trend with feeder cattle prices in the $60/cwt range. This was a time when the grain prices were at depressed levels and the costs of producing cattle was significantly less than they are currently. By the year 2000, these feeder cattle prices had increased by a third to the $90/cwt range following at a similar pace to the grain markets. This trend of upward prices continued to break $100/cwt for the first time in September of 2003. By 2005, this market had rallied to $116/cwt. In 2006, we saw the first correction in the cattle cycle and saw prices correct themselves to under $100/cwt. This correction was in relation with the 10 year cattle cycle that we watch. By the year 2010, we had recovered the lost ground due to the correction and had once again hit new highs of $118/cwt. During this time crop prices rose significantly and the margins to raising cattle even at these prices were thin. Cattle continued to rally in 2011 to $143/cwt, 2012 to $156/cwt, and 2013 to $164/cwt.

These increases during the past few years were significant but the fact is that even though we had some liquidation during the drought of 2012 it was not significant enough to cause this dramatic increase in price. What we did have during this time period was some significant participation in the cattle market by index funds. This managed money was on the short side from April until the first of July of 2013.

On July 2 2013 managed money changed positions held 6470 long positions and 5423 short positions with a net difference of 1047 contracts. Since this date this disparity has increased significantly which has helped to drive this market higher.

Of course this lopsided position is not the only thing that has driven the market but it is an important tool to watch. We have been watching the commitment of traders for years in the grain markets. One thing we have noticed is that when this difference starts to narrow the market starts losing its strength. At the current time, this market is still very long but when this starts to change price movement will follow rapidly. This movement will not come from supply side economics but rather the long only index funds reversing positions. This process can happen very quickly and the price fall will likely be significant.

In the risk management business it is not our goal to try to pick the top of the market. We have to evaluate the market conditions the best that we can and see if we believe the strength will last.

Currently, we are really in the eleventh year of what is normally a ten year cattle cycle. The managed money is still exceptionally long but we do have indications of herd building. Our export markets are strong and we have no indication of that changing. All this news though is built into the markets that we are seeing today. I don't know when this market will break, but it will. When this does happen we are poised for considerable down side pressure from managed money alone.

On my operation I will background cattle again this year. For 2014 the feeder cattle market is considerably higher than it was in 2013. My feed costs on the other hand are significantly lower. Budgeted margins are a bit tighter than they have been in the past. Like most producers I will be faced with an abundance of cheap feed this year and are considering trying to market this feed through cattle that I will feed on my operation.

I am concerned about how long the cattle market can sustain these high prices. I am convinced that this market has considerable more down side risk than it does upside potential. Therefore, when I place feeder cattle on my operation I am going to at least cover my variable cost with price insurance.

This product is called Livestock Risk Protection (LRP) it guarantees that if feeder cattle prices fall at a given time in the future

Managed Money Commitment of Traders

Date	Long	Short	Difference	Price
7/2/2013	6470	5423	1047	$151.80
9/24/2013	8746	2639	6107	$159.36
12/24/2013	13681	4929	8752	$167.00
5/20/2014	16105	907	15198	$192.85
8/26/2014	10848	1518	9330	$218.65

Cattle Markets: Where to now? (continued)

that this policy will make up the difference between the offered price and the feeder cattle index on a specific date in the future. The LRP contract acts like a put option and gives the producer the right to sell cattle at this price at a given date in the future. Unlike a put option LRP is sold on a per head basis that allows the producer to only cover the number of head he has on the farm rather than having to price coverage in 50,000 lb. increments.

This product has become a tool that I use every year in my operation. Last year I purchased this coverage on 81 head of feeder steers that I back grounded. When I purchased this group I paid $185/cwt for 4 weight feeders and at the same time locked in a minimum price of $166 /cwt for 8 weight cattle 21 weeks later. As it turned out the price continued to rise and I sold my 8 weight feeders for $173.97/cwt. This contract expired without me collecting on it however I had the peace of mind knowing that I had nearly $120/head profit locked in the worst price scenario. This year feeders will be more expensive and I will have a higher cash outlay to fill my lots. On Friday we looked at the LRP market and saw that we could lock in a minimum price for the first of January of $216/cwt and $214/cwt for the end of January. When I purchase cattle this fall I will exercise one of these offerings to protect against declining prices. It will be my intention to lock in as much profit as I can however the most important issue to me is to cover my variable costs and not lose money by feeding cattle.

GIBSON INSURANCE GROUP

Agents

Main Office
Dean Gibson
Brian Huhmann
Matt Rowell
660-433-6300

Boonville
Steve Timm
660-621-1212

St. Elizabeth
Bob Oligschlaeger
573-680-7794

Conway
Davey Perryman
417-719-8659

Montrose
Brandon Jurgensmeyer
660-351-2475

West Plains
Shane Rhoads
417-293-0661

GIBSON INSURANCE GROUP, INC.
P.O. BOX 795
TIPTON, MO 65081