Risk Management for Livestock Producers

Dr. Curt Lacy
University of Georgia

Let’s talk about risk

- It is NOT uncertainty!
- It is the negative outcome associated with an unforeseen event.
- Good risk managers
  - Know the odds
  - Don’t risk a lot to make a little.
  - Don’t risk more than they can afford lose.

Managing Risk in Agriculture

- What Is Your Goal?
  - Protect Profits
  - Protect Equity
  - Protect the Farm
- Available Risk Management Alternatives
  - LRP
  - Rainfall Index Insurance

Using Livestock Risk Protection (LRP) insurance to set a floor price

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LRP Is Price Risk Protection

- Establishes A Floor Selling Price For Livestock
- Pays Producers If A Regional/National Cash Price Index Falls Below A Set Price
  - Does Not Guarantee A Cash Price Received
  - Basis Risk Must Still Be Considered
- Covers Feeder Cattle, Fed Cattle, & Swine
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GA LRP BASIS, 2010-2012

Comparison of 500-600 pound Steers and CME FC Index

Key Points

• All Owners Of Eligible Livestock In LRP States
• Once Enrolled, Producers Have The Right But Not The Obligation To Purchase Coverage
• Coverage Obtained With A Specific Coverage Endorsement (SCE)
• Livestock Has To Be In Eligible State
  — Owners Can Be In Other States

What is LRP

• LRP can be viewed as “Price Insurance”
• LRP Is A Risk Management Tool
  — Protects Against Catastrophic Price Declines
  — NOT Designed To Enhance Profit
• Calculate Premium Cost As Part Of Breakeven For Livestock
  — Cheaper When Prices Are High
  — Premiums Increase As Prices Decline

Insurance Agents

• Available Through Crop Insurance Agent System
• Agent Locator Tool On USDA Website
  http://www3.rma.usda.gov/apps/agents/

Eligible Cattle

• Feeder Cattle
  — Feeder Steers, Bulls, & Heifers < 600 lbs
  — Feeder Steers & Heifers From 600-800 lbs
  — Includes Dairy & Brahman Breeds
• Fed Cattle
  — Steers & Heifers
  — Select Or Higher, Yield Grade 1-3
  — Weight: 1,000-1,400 lbs.

Coverage Availability

• Coverage Available About 5pm To 9am CST
  — Available Sat Mornings Until 9am, But Not Sun, Mon, & Holidays
• Coverage Initiated With Specific Coverage Endorsement (SCE)
  — No Limit On Number Of SCEs
• Producers Have Flexibility On The:
  — Timing Of Purchase
  — Time Length Of The SCE
  — Number Of Head Covered

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Limitations On Number Of Head Insured

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<tr>
<th></th>
<th>Fed Cattle</th>
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<td>Per Crop Year July 1-June 30</td>
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LRP Compared to Hedging or Options

- **Advantages**
  - No need to establish brokerage accounts
  - Can insure animals on individual basis
  - “Guaranteed” availability for price protection for far-off futures contracts

- **Disadvantages**
  - Paperwork can take a while
  - Available only for animals in certain states
  - Can’t “lock-in” a price
  - Can’t exercise or “sell back” contract if market goes up

Summary

- LRP is a relatively new price risk management tool available to cattle producers
- It is price insurance not enhancement
- To be eligible cattle must located in one of the program states
- More information is available at: http://www.fmra.usda.gov/apps/livestock_reports/

Rainfall Index Insurance

- New for 2012 in select states and counties.
- Based on a rainfall index as calculated by NOAA.
- Producers insure a grid-area = .25 degrees latitude x .25 degrees longitude = approximately 12 mi. x 12 mi.
- Producers insure for specific 2-month time periods

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Rainfall Index Insurance

- Participants choose PRODUCTION levels from 70-90% and PAYMENT levels from 100-150%.
- Indemnity triggers when your GRID rainfall index falls below your coverage level.

Pasture Insurance on 100 Acres in 2012

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<th>Harvestable Acre</th>
<th>Pasture Acre</th>
<th>Indemnity</th>
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History of Rainfall Index

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<th>Year</th>
<th>Jan-Feb</th>
<th>Mar-Apr</th>
<th>May-Jun</th>
<th>Jul-Aug</th>
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History of Indemnities for Grazing

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Hay Insurance on 100 Acres in 2012

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Risk Management Strategies

- No One Alternative Protects Against Everything
  - Understand Your Risks!
  - Know Your Operation
- Combining Risk Management Alternatives
  - Comprehensive
  - Requires Knowledge of Different Alternatives
- Keep it Simple

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