
Margin Protection 2023 Crop Year

Margin Protection Overview

Summer, 2022

Topics

- Margin Protection
 - Overview
 - Margin Protection Fundamentals
 - The Margin Concept
 - A simple example: MP
 - A simple example: MP - HPO

Background

- The Original Concept paper for Margin Protection was provided to RMA staff in 2007.
- The 2008 Farm bill included the “Concept” 508(h) process.
- Farm Risk and Watts & Associates submitted concepts under these provisions in 2009.
- The Agricultural Act of 2014 amended the Federal Crop Insurance Act to authorize MP.
- MP was offered for the first time in 2016 in select areas, only Iowa for Corn and Soybeans.
- For the 2018 Crop Year, FCIC approved a major expansion of MP throughout the Midwest.

What is Margin Protection?

- MP provides growers with an insurance product that protects their expected operating margin, i.e., the difference between expected revenue and specific expected costs.
- MP takes into consideration changes in crop prices, reductions of yields, **and changes in the prices of inputs used to grow the crop.**

Why Margin Protection?

- 1st Generation of Crop Insurance – Yield
 - GYC, APH, and YP
 - Insures against: reduction in yield
- 2nd Generation of Crop Insurance – Revenue
 - RA, CRC, IP, GRIP, RP, and ARP
 - Insures against: reduction in yield or price
 - Revenue = Price x Yield
- 3rd Generation of Crop Insurance – Margin
 - Margin Protection
 - Insures against: reduction in margin
 - Margin = (Price x Yield) - Cost

Margin Protection Basics

- Margin Protection has a September 30 SCD
 - Price discovery for Projected Prices is August 16 to September 15.
 - MP and RP use the same harvest prices.
- Margin Protection is Area-Based
 - The same expected county yields used for ARP are used for MP
 - MP offers coverage levels from 95% to 70% and protection factors from 0.8 to 1.2
- Margin Protection is Unique
 - Growers can choose to also buy (RP) in the spring. Growers who do so get a premium credit on the MP premium and receive the greater of the MP or RP indemnity in the fall.

The Margin Concept

- Crop insurance is designed to transfer risk from farmers to insurance companies. Crop insurance is designed to assure that at the end of the year farmers' potential losses are limited.
 - Yield Risk (bu/ac)
 - Price Risk (\$/bu)
 - Revenue Risk (bu/ac x \$/bu = \$/ac)
 - Cost risk (Cost expended \$/ac)
- The money that a farmer has left after harvesting bushels, selling them, and paying operating costs is the margin. This is the money the farmer has to cover land costs, pay for management labor, and support their family.
- Margin, not bushels, prices, or costs, is the number a farmer has been looking to insure.

Understanding Expected Costs

- Margin Protection makes no effort to measure any individual grower's actual costs incurred.
- Instead, assumptions are made based on the local agronomic conditions to establish the quantity of key inputs. These are based on the relationship between expected county yield and the volume of an input needed to grow a bushel
- Costs included:
 - Diesel
 - Nitrogen (Urea)
 - Phosphorus (DAP)
 - Interest
 - Potassium (Potash)
 - Seed and other costs

Margin Protection Concepts

- Prior to SCD, RMA releases

- County Expected Yield (ECY)
- Projected Price
- Expected Cost

- Expected Margin is calculated

Expected Margin = (ECY x Projected Price) – Expected Cost

- After Harvest, RMA releases

- Final County Yield (FY)
- Harvest Price
- Harvest Cost

- Harvest Margin is calculated

Harvest Margin = (final Yld x Harvest Price) – Harvest Cost

Simple Example: MP

Calculating an MP Trigger

- Expected Margin
(Expected Yield x Projected Price) – Expected Cost
 $(180 \text{ bu/ac} \times \$4.00) - \$260/\text{ac} = \$460/\text{ac}$
- Margin Deductible
Expected Revenue x (1-Coverage Level)
 $(180 \text{ bu/ac} \times \$4.00 \times (1-95\%)) = \$36/\text{ac}$
- Trigger Margin
Expected Margin – Margin Deductible
 $\$460/\text{ac} - \$36/\text{ac} = \$424/\text{ac}$

Simple Example: MP

Calculating an MP Indemnity

- Harvest Margin
(Harvest Yield x Harvest Price) – Harvest Cost
 $(160 \text{ bu/ac} \times \$3.80) - \$260/\text{ac} = \$348/\text{ac}$
- Margin Loss
Trigger Margin – Harvest Margin
 $\$424 - \$348 = \$76/\text{ac}$
- Margin Indemnity
Margin Loss x Protection Factor
 $\$76/\text{ac} \times 1.20 = \$91.20/\text{ac}$

Simple Example: MP-HPO

Calculating an MP Trigger

- Expected Margin
(Expected Yield x max{Proj, Harv}) – Expected Cost
(180 bu/ac x max{\$4.00, \$4.10}) - \$260/ac = \$478/ac
- Margin Deductible
Expected Revenue x (1-Coverage Level)
(180 bu/ac x \$4.10 x (1-95%) = \$36.90/ac
- Trigger Margin
Expected Margin – Margin Deductible
\$478/ac - \$36.9/ac = \$441.10/ac

Simple Example: MP-HPO

Calculating an MP Indemnity

- Harvest Margin
(Harvest Yield x Harvest Price) – Harvest Cost
 $(160 \text{ bu/ac} \times \$4.10) - \$260/\text{ac} = \$396/\text{ac}$
- Margin Loss
Trigger Margin – Harvest Margin
 $\$441.10 - \$396 = \$45.10/\text{ac}$
- Margin Indemnity
Margin Loss x Protection Factor
 $\$45.1/\text{ac} \times 1.20 = \$54.12/\text{ac}$

MP Liability

Calculating an MP Indemnity

- Liability
- Expected County Yield x Projected price x Coverage level x share x protection factor

- MP-HPO Liability
- Expected County Yield x max(Projected price, Harvest Price) x Coverage level x share x protection factor

Questions?

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