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Should the Livestock Insurance Programs be Altered?

BACKGROUND

The Livestock Gross Margin (LGM) insurance program and Livestock Risk Protection (LRP) programs provide protection against loss of gross margin or price declines for:

- LGM-Cattle: market value of livestock minus feeder cattle and feed costs on cattle (available in 20 states);
- LGM-Swine: market value of livestock minus feed costs on swine (available in the 48 contiguous states);
- LGM-Dairy: market value of milk minus feed cost on dairy (available in the 48 contiguous states); and
- LRP for Cattle, Swine, and Lamb (available in select states).

The LGM products provide protection when feed costs rise or output prices for cattle, swine, or milk fall below a guaranteed level. These products use futures prices for the livestock and feed ingredients to determine the margin guarantee, the actual margin, and any potential indemnities due to the agricultural producer.

The LRP products provide price protection only on a percentage of the end commodity value.

ISSUE

Despite being available since 2002, LGM and LRP have not been widely adopted across the livestock sector. Many cattle and swine operators use private risk management solutions and far more dairy producers are enrolled in the Dairy Margin Protection Program (MPP) rather than in LGM-Dairy. There are a number of likely causes for slow adoption, including:

- Unlike crop producers, dairy operations may not simultaneously participate in LGM-Dairy and USDA's Margin Protection Program. This limits the ability for dairy farmers to diversify risk management options.
- LGM and LRP premium subsidies and administrative and operating subsidies are capped at $20 million per fiscal year. Once the funding limit has been reached, products can no longer be sold. The uncertain availability likely limits its use as a risk management tool.
- Premium discounts are not available across all LGM and LRP products. LGM-Dairy carries a variable rate discount, while the LRP cattle and swine policies have a 13 percent discount and LRP lamb has a 20 percent premium discount.
- LGM products are only sold on the last business Friday of the month. Farmers and ranchers are unable to make marketing and risk management decisions using LGM products in response to market price swings. Agents have only a short window to get on the RMA website (a matter of hours per month) to get the policy approved. LRP (cattle and swine) is sold daily, and as a result is more widely used among cattle and swine producers.
- While LGM cattle and swine have fixed feed price parameters, LGM-Dairy feed ration coefficients can be adjusted up or down to accommodate dairies that buy feed, grow feed, or those who face little feed market risk. This makes LGM-Dairy a more complex risk management tool due to the large number of decision parameters farmers must choose.

- Premiums are due when the policy is purchased for cattle, but not until the end of the insurance period for swine and dairy. The front loaded premium on cattle reduces farm cash flow.
- RMA can decide to stop selling policies in instances of a news report, announcement, or other event that occurs during or after trading hours that is believed to result in market conditions significantly different than those used to rate the Livestock Gross Margin.
- LGM and LRP products have eligibility constraints on how many livestock or how much milk can be covered under an insurance policy period and on an annual basis.
- LGM products for Swine and Cattle assume a static market weight and are inflexible to market conditions that incentivize additional weight or lighter weight conditions.

In FY 2014 the FCIC paid approximately $6.3 billion in crop insurance discounts and $1.4 billion in adjusting & other expenses on behalf of policy holders. Livestock's contribution to the farm economy is equally as large as any crop or fiber with farm receipts in the tens of billions of dollars per year. However, USDA provides limited funding for livestock insurance products and these products do not align with marketing practices employed by livestock producers.

OPTION #1

Allow livestock producers to participate in additional crop insurance programs.

OPTION #2

Increase the current annual funding cap of $20 million for livestock insurance products.

OPTION #3

Request USDA make LGM product sales periods more often than monthly to allow producers to make more timely risk management and marketing decisions.

OPTION #4

Allow variable rate premium subsidies for LGM cattle and LGM swine to make these products more competitive with private market solutions.

OPTION #5

Explore new risk management tools that could be developed for livestock producers that might be less complex or require fewer decisions by agricultural producers.

Livestock Gross Margin Programs

	Cattle	Swine	Dairy	Lamb
Risk Protection	Doesn't insure against production loss: disease, natural disaster, etc.			N/A
Basis Risk	Is not addressed: Local prices vs national prices			
Insurance Period	Offered every month, for an 11-month period	Offered every month for a 6 rolling month period	Offered every month, for up to an 11-month period	
Insurable Limits	Cattle Owned: 5,000 head per 11-month insurance period & a limit of 10,000 head per crop year	Swine Owned: 15,000 for any 6-month contract, and 30,000 head per crop year	• No participation for producers participating in MPP-Dairy • Up to 24 million lbs.	
Availability	Select States	48 Contiguous states	48 Contiguous states	
Deductibles	$0-$150 per head, $10 increments	$0-$20 per head, $2 increments	$0-$2 per hundredweight, $0.10 increments	
Subsidy offered	No	No	Yes, Up to 50%	
Loss Ratio (Avg. 2003-2015)	0.55	1.80	0.59	
Total Policies Sold Since 2003	897	2,232	12,211	

Livestock Risk Protection Programs				
	Fed Cattle	**Feeder Cattle**	**Swine**	**Lamb**
Risk Protection	Price Risk only: 70-100% of expected ending value			Price Risk only: 80-95% of expected ending value
Basis Risk	Is not addressed: Local prices vs weighted average prices (series dependent)			
Insurance Period	Sold Daily Endorsements: 13, 17, 21, 26, 30, 34, 39, 43, 47, 52 weeks Offered every month for a 6 rolling month period		Sold Daily Endorsements: 13, 17, 21, 26 weeks	Sold weekly, Mondays only (unless a holiday) Endorsements: 13, 26, 39 weeks
Insurable Limits	2,000 head per endorsement, annual limit of 4,000 head	1,000 head per endorsement, 2,000 head per year	10,000 hogs per coverage endorsement, 32,000 head per year	2,000 head per endorsement, 28,000 head per producer per year
Availability	Select States (37)	Select States (38)	Select States (38)	Select States (28)
Subsidy offered	Yes-13%	Yes-13%	Yes-13%	Yes-20%
Coverage Categories	Heifers and Steers 1000-1400lbs	Calves, Heifers, Steers, Predominately Brahman, Predominately dairy Two Weight Categories: <600lb, and 600-900lbs		
Loss Ratio (Avg. 2003-2015)	0.49	0.75	0.72	2.70
Policies Sold Since 2003	6,435	57,942	2,191	2,240