Ag Decision Maker

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Five options offered for 2002 Farm Bill

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The Farm Security and Rural Investment Act of 2002, better known as the 2002 Farm Bill, offers farmers and landowners a chance to update the base acres and yields that are used to calculate their commodity program payments. The Farm Service Agency has defined five separate options from which to choose.

Handbook Updates

For those of you subscribing to the *Ag Decision Maker Handbook*, the following updates are included.

Crop Planning Prices—
File A1-10 (2 pages)

Livestock Planning Prices—
File B1-10 (1 page)

Please add these files to your handbook and remove the out-of-date material.

Option 1

The first option is to retain only the acreage bases that the producer had under the past program. These are shown as 2002 Product Flexibility Contracts (PFC) acres on the Farm Summary Report sent out by FSA around August 1. The example in this article shows current bases of 300 acres for corn and 25 acres for oats. Prior programs did not include bases for oilseeds, such as soybeans. If the producer has grown any soybeans in the past four years, option 1 will probably not be favorable. Farmers who have grown only corn and have not increased yields since the early 1980s are the only ones who would find option 1 attractive.

Option 2

Under option 2, producers can retain existing PFC acreage bases and add an oilseed base. The number of acres eligible for a soybean base is based on actual crop acres from 1998 through 2001. Eligible acres are the smaller of the average:

- actual planted and prevented planted soybean acres, or
- total acres of program crops minus the acres in existing bases.

For example, if the producer planted 500 total acres of corn and soybeans (50/50 rotation) each of the past four years, and

continued on page 2

Inside . . .

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Five options offered for 2002 Farm Bill, continued from page 1

his/her current bases are 300 acres of corn and 25 acres of oats, he/she could claim up to 175 acres toward his/her soybean base. However, if the producer averaged only 150 acres of soybeans in 1998–2001, then the soybean base will be only 150 acres.

Producers who grow both corn and soybeans, and who have a current PFC corn base somewhat larger than their average corn acres during 1998–2001, are most likely to maximize payments under option 2.

Option 3

Under option 3, the soybean base is the producer's average actual acres of soybeans for 1998 through 2001. However, if this is greater than what the producer's soybean base would be under option 2, he/she must reduce his/her base acres of other crops by the difference in soybean acres. In the example farm, the soybean base would increase from 175 acres in option 2 to 250 acres in option 3. Therefore, the oats base would have to decrease by 25 acres and the corn base by 50 acres.

If the producer has an existing base for oats, it will probably pay to shift it to his/her soybean base, as program payments for oats are quite small. Payments for other crops, such as corn, sorghum or wheat, are generally higher than for soybeans, however, so shifting acres from those crops to soybeans would reduce total payments. Only farmers who can maximize their soybean base by shifting oats base acres only will be likely to choose option 3. This is an unlikely situation in Iowa.

Option 4

The only option that allows for updating base acres is the one designated as option 4 by FSA. New bases are assigned for all program crops, equal to the average number of planted and prevented planted acres from 1998 through 2001. In the example both corn and soybeans would have a 250-acre base. Farmers whose new corn base would be not substantially smaller than their existing PFC corn base will probably prefer option 4.

This is also the only option that allows for updating program yields. FSA offers two different methods for computing new program yields, both based on average yields from 1998 through 2001. The average yields are calculated as the total bushels of each crop produced during 1998–2001 period, divided by the total acres of each crop harvested during the period.

The producer can also elect to keep his/her old program yields. It is unlikely that these will be higher than recent yields, however. An exception might be when no production data is available and the new yield is based on 75 percent of the county average during the past four years

Option 5

Option 5 is exactly like option 3 except that the producer can shift less than the maximum acres allowed from other crop bases into the soybean base. In the example, only the 25 acres of oats base is shifted to the soybean base. It will usually not pay to shift corn or other crop base acres to soybeans.

Most farmers in Iowa will choose either option 2 (retain existing corn base and yield and add a soybean base) or option 4 (update both base acres and yields). If an oats base exists, option 5 can be used to convert it to soybean base and still retain the corn base.

continued on page 3

Example Farm

2002 PFC acres are 300 for corn and 25 for oats.
Actual plantings for 1998 through 2001 have been
250 acres of corn and 250 acres of soybeans each year.
Acreage bases under each option are:

	Corn	Oats	Soybeans
Option 1	300	25	0
Option 2	300	25	175
Option 3	250	0	250
Option 4	250	0	250
Option 5	300	0	200

Five options offered for 2002 Farm Bill, continued from page 2

The tradeoff is between maximizing the corn base acres and increasing program yields. Updated program yields apply only to counter-cyclical payments, however, and current price forecasts for the 2002 crop are near or above the levels at which these payments would be made. For direct payments, maximizing corn base acres is all that really matters. In future years, counter cyclical payments may come back into play.

Two electronic spreadsheets are available for analyzing options for commodity acreage bases and yields. More details plus a hand worksheet are available under Crop Cost and Returns at the Ag Decision Maker Web site or from ISU Extension publication FM-1872a, "Commodity Programs for Crops." The Farm Bill Payment Analyzer can be downloaded from the *Ag Decision Maker* Web site at: www.extension.iastate.edu/agdm. The Farm Service Agency (FSA) will be using a program developed at Texas A and M University, which can be accessed at: http://www.afpc.tamu.edu/models/base/.

Pre-harvest new-crop corn and soybean pricing strategies show incentives for using options markets

by Robert Wisner, extension grain marketing specialist, rwwisner@iastate.edu, 515-294-6310; Dean Baldwin and Neal Blue, Ohio State University

Recent research on pre-harvest pricing strategies for the 1985–86 through 2001–02 marketing years confirms our earlier work showing significant incentives for pre-harvest pricing with the use of options markets. Previous research through the 1997 marketing year identified potential $18,000 to $19,000 average yearly gains in net income for a 1,000 acre cash grain farm (half corn and half soybeans) versus harvest cash sales.

These results came from pricing 80 percent of a 10-year moving average of the farm's production with corn put option purchases in mid-May, and 20 percent with hedge sales in July for harvest delivery.

Soybeans were priced with synthetic puts (hedge sale of November futures, plus purchase of call options two strike prices out of the money). Calls were purchased to take advantage of possible weather rallies in late spring or early summer, and were sold the first week of July to avoid a strong seasonal tendency toward declining call premiums into late summer and fall. From July onward, price protection was retained through the hedge sales.

Years after short crops

If the previous year's U.S. production was a weather-reduced short crop (production fell below the previous year's use due to adverse weather over a sizeable part of the Corn Belt, but not necessarily in your area), grain is priced in late February before harvest with hedge sales of December futures. Pre-harvest pricing in the winter in those years typically offered higher income than pricing at planting time or waiting until harvest time. Hedge sales were closed out in mid October for soybeans and in early November for corn.

Additional marketing gains were available in many years, especially in the post-1995 Freedom-to-Farm years, by taking advantage of post-harvest basis improvement and market carry (premium of July futures prices over harvest-delivery futures). Although these gains were not considered in the pre-harvest study, the pre-harvest strategies analyzed in this study would give farmers the flexibility to store grain and gain from basis improvement after harvest.*

continued on page 4

*(For information on how to implement these post harvest strategies, see "MRP Modules" on http://www.econ.iastate.edu/faculty/)