2012 Illinois Farm Economics Summit

The Profitability of Illinois Agriculture:

Managing in a Turbulent World

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Agricultural and Consumer Economics

FBFM

UNIVERSITY OF ILLINOIS EXTENSION
College of Agricultural, Consumer and Environmental Sciences

Dates/Locations

- *Monday, December 10, 2012 - Champaign, IL*
  - *I Hotel and Conference Center*
- *Tuesday, December 11, 2012 - Sycamore, IL*
  - *Center for Agriculture*
- *Wednesday, December 12, 2012 - Galesburg, IL*
  - *Best Western Prairie Inn*
- *Thursday, December 13, 2012 - Mt. Vernon, IL*
  - *Holiday Inn*
- *Friday, December 14, 2012 - Bloomington, IL*
  - *Doubletree Hotel*

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2012 Illinois Farm Economics Summit

The Profitability of Illinois Agriculture: Managing in a Turbulent World

7:45 – 8:15 am........................ Registration and Coffee

8:15 – 8:20 am........................ Introduction and Overview
- *Todd Gleason*

8:20 – 8:50 am........................ Crop and Livestock Price Prospects for 2013
- *Darrel Good*

8:50 – 9:20 am........................ 2013 Projected Grain Incomes: A Drought Reprieve
- *Gary Schnitkey*

9:20 – 9:50 am........................ The Impact of Biofuels Mandates on Grain and Oilseed Markets
- *Scott Irwin*

9:50 – 10:10 am...................... Break

10:10 – 10:40 am.................... Tax Reporting Options on Crop Insurance
- *Gary Hoff*

10:40 – 11:10 am.................... Crop Insurance – 2012 Performance and Updates for 2013
- *Bruce Sherrick*

11:10 – 11:40 pm.................... Overview and Impacts of Proposed Changes in the 2012 Farm Bill
- *Nick Paulson*

11:40 – 12:10 pm.................... Question and Answer/Wrap-Up

12:10 – 1:10 pm...................... Lunch (Included)

Crop and Livestock Price Prospects for 2013

Darrel Good, Professor Emeritus
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Email: d-good@illinois.edu

CROPS

The crop price environment will likely remain very volatile in 2013, reflecting production uncertainty and unsettled economic issues. However, a transition to lower prices is anticipated as production rebounds. The extent of the price decline will depend heavily on the outcome of the 2013 crops.

The small **corn** crop and high prices in 2012 will result in a substantial decline in consumption and small inventories by the end of the current marketing year. Smaller crops in other parts of the world and continued strong demand will also reduce foreign inventories. Argentine corn production is expected to rebound in 2013. Stable U.S. acreage and a return to a trend yield would result in a U.S. crop in 2013 in excess of 14 billion bushels, allowing a substantial re-building of inventories. Prices are expected to decline from the record high levels of 2012 as production rebounds. An average farm price above $7 is expected for the 2012-13 marketing year, but the average for the 2013-14 marketing year could be in the $4.75 to $5.50 range.

Both South America and the U.S. had small **soybean** crops in 2012, resulting in sharply higher prices in the last half of the year. Like corn, U.S. and world production is expected to rebound in 2013. The USDA has projected a record South American harvest. Stable acreage and a trend yield in the U.S. would result in a crop near the record of 2009. If production unfolds as expected, world inventories will expand during the 2013-14 marketing year and prices will continue to retreat. An average farm price near $14.50 is expected for the 2012-13 marketing year, while the average for the 2013-14 marketing year is expected to be in the $11 to $12 range.

U.S. **wheat** production rebounded in 2012, but production in the rest of the world declined sharply, leading to some improvement in U.S. export demand. High corn prices also increased the level of domestic wheat feeding, but year-ending stocks will be adequate. U.S. acreage is expected to increase in 2013 and foreign production is expected to rebound. The near term focus will be on the status of drought conditions in the HRW areas. Most of the 2012 wheat crop in Illinois has been sold, at an average price near $8. Prices during the first half of 2013 are expected to remain high. A subsequent decline to the $6 to $7 range would be expected with good U.S. and world crop prospects.

LIVESTOCK

U.S. **pork** production is expected to decline from 23.26 billion pounds in 2012 to 22.94 billion pounds in 2013. Exports are expected to remain near the 2012 level of 5.4 billion pounds. Domestic pork supplies are projected at 44.9 pounds per capita in 2013, down from 45.7 pounds in 2011 and 2012. The average price of hogs was near $66 in 2011 and $61 in 2012. An average near $64 is expected for 2013.

U.S. **beef** production is expected to decline from 25.7 billion pounds in 2012 to 24.6 billion pounds in 2013. From a 19 year low of 460 million pounds in 2004, U.S. beef exports grew to 2.79 billion pounds in 2011, but declined to 2.47 billion pounds in 2012. Declining production is expected to limit exports to 2.45 billion pounds in 2013. Domestic per capita beef supplies in 2013 are projected at 54.8 pounds, down from 56.8 pounds in 2012. Fed cattle prices averaged near $122 in 2012 and are projected to average near $125 in 2013.

Notes

Additional Resources

The slides for this presentation can be found at:
http://www.farmdoc.illinois.edu/presentations/IFES_2012

For current outlook information, see:
http://www.farmdoc.illinois.edu/marketing/newsletters.html

http://www.agmanager.info/

http://www.agecon.purdue.edu/extension/prices/index.asp

http://cattlemarketanalysis.org/

http://www.extension.iastate.edu/agdm/

2013 Projected Crop Farm Incomes: A Drought Reprieve

Gary Schnitkey, Professor
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Email: schnitke@illinois.edu

2012 Crop Farm Incomes

Net farm incomes in 2012 on many grain farms will be above expectations, even given relatively low corn and soybean yields caused by the drought. This will occur because of two factors countering yield losses: 1) higher corn and soybean prices and 2) crop insurance payments.

Corn and soybean prices increased beginning in the summer and fall of 2012. Cash prices for corn were in the mid-$6.00 range per bushel in the spring, reaching the high-$7.00 per bushel range in the fall. Soybeans were in the $14 per bushel range in April and reached the $15 range in the fall of 2012. Price increases partially countered yield declines on farms that did not have a great deal of per-harvest hedging in the spring.

About 60% of corn and soybean acres in Illinois were insured with crop insurance products that cover much of the yield losses. These products, which include Revenue Protection (RP) and the Group Risk Income Plan with the harvest revenue option (GRIP-HR), have guarantees that increase when harvest prices are above the projected prices, the situation that occurred this year for both corn and soybeans.

There will be some farms that have low or negative grain farm incomes. Those farms likely did not purchased RP or GRIP-HR at high coverage levels. Moreover those farms that hedged production a great deal of production in the spring could face losses, as they did not partake in the price increases on those bushels that were hedged. A combination of no crop insurance and a large amount of hedging could lead to sizable losses.

2013 Crop Farm Incomes

Prices on futures contracts in mid-November 2012 suggest harvest time prices for 2013 around $5.50 per bushel for corn and $12.50 for soybeans. These prices – in combination with trend yields, non-land costs that did not increase between 2012 and 2013, and cash rents increasing about $15 per acre --would result in relatively high 2013 grain farm incomes that would exceed average income levels between 2009 through 2012. Overall, projections are for an above average income year in 2013.

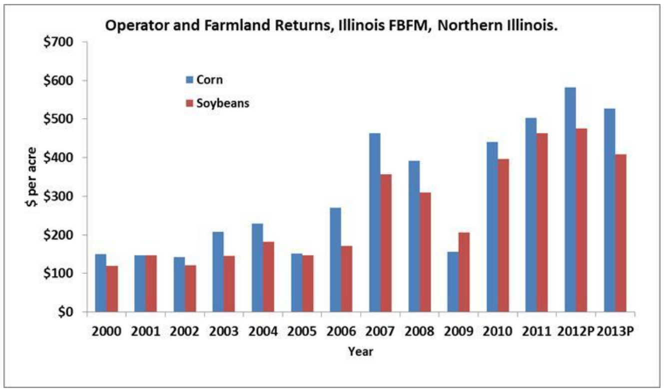
Of course, 2013 incomes could be much lower. For those farms taking RP and GRIP-HR crop insurance, much of the downside risk will be determined when projected prices are set at the end of February. Projected prices near $6.00 per bushel for corn and $12.50 per bushel for soybeans would result in guarantees at or above 2012 levels, again providing many farms with the opportunities to insure positive incomes by taking high levels of crop insurance.

Farms most at risk for low and negative incomes are grain farms that cash rent a large portion of their farmland at high rent levels. These farms cannot assure themselves positive incomes in 2013 even if they take high levels of crop insurance.

A Reprieve

The drought resulted in higher corn and soybean prices. These prices delay the return to more normal price levels, likely in the mid-$4.00 range for corn and mid-$12 per bushel range for soybeans. The higher projected prices then result in higher projected 2013 incomes then had the drought not occurred.

One unfortunate aspect of this drought increase may be that cash rent levels likely will continue to increase in 2013. These increases likely are larger than would have occurred without the drought. When corn and soybean prices return to more normal levels, the necessary downward adjustments in cash rents may be more painful and protracted than had the drought not occurred, particular for cash rents in the higher range.



Notes

Additional Resources

The slides for this presentation can be found at:
http://www.farmdoc.illinois.edu/presentations/IFES_2012

For current farm management information
http://www.farmdoc.illinois.edu/manage/index.asp

For an evaluation of projected prices on 2012 revenue risk
http://farmdocdaily.illinois.edu/2012/11/2013-crop-revenue-risk-waiting.html

Farmer and landowner returns under alternative corn and soybean prices
http://farmdocdaily.illinois.edu/2012/10/landowner-and-farmer-returns-u.html

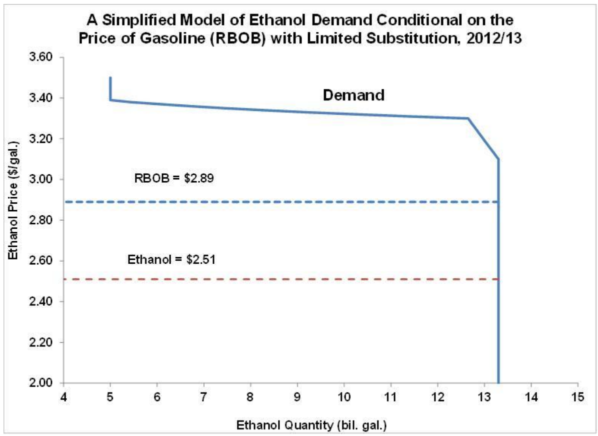
The Impact of Biofuels Mandates on Grain and Oilseed Markets

Scott Irwin, Professor
Department of Agricultural and Consumer Economics
Email: sirwin@illinois.edu

Minimum volumes of biofuel usage were first mandated for the U.S. in the 2005 Energy Policy Act and then revised in the Energy Independence and Security Act of 2007. The current legislation sets annual minimum volumes through 2022 in four categories of biofuels: cellulosic, biomass-based diesel, undifferentiated advanced, and renewable. There is a hierarchy among these different categories based on their life-cycle contribution to reducing "green house" gas (GHG) emissions. Most people are surprised to learn that there is not an explicit mandate for corn-based ethanol. Instead, corn-based ethanol has been the cheapest alternative to date for fulfilling the renewable component of the mandates.

As events this summer have highlighted, there is a raging debate about the impact of the RFS mandates on grain and oilseed markets. Many have argued that ethanol production and blending is motivated only by the RFS and that a lower mandate would result in less ethanol production and blending and less corn consumption in that sector. In an effort to provide some relief to other consumption sectors due to the drought-related drop in corn production in 2012, several state governors filed a request for the U.S. Environmental Protection Agency (EPA) to impose a partial or full waiver of the RFS for 2013. While the logic of this request seems straightforward, the structure of the demand and supply functions in the ethanol sector indicates that waiving the mandate would have at most limited impact on the amount of corn used in ethanol production in 2013. The main reason is that the increasing amounts of ethanol supplies since 2006 have resulted in a fundamental shift in gasoline formulation. A simplified description of the change is that the refining industry has moved to using predominantly 84 octane "conventional" gasoline that is then blended with the higher octane ethanol (around 113) to produce the 87 octane gasoline that is most popular at the retail level in the U.S. With this change, so long as the price of ethanol is below the price of wholesale gasoline there is no market incentive for gasoline blenders to reduce their use of ethanol. The EPA agreed with this logic in their recent denial of the requests to waive the mandate.

The future outlook for continued growth in corn-based ethanol use is clouded by several factors, including the 10% blend wall, slow implementation of higher blends, declining total gasoline demand, and ethanol imports from Brazil. One might be tempted to conclude that the biofuels-fueled boom in crop prices is coming to an end as corn consumption for ethanol levels out and corn production begins to catch up. Instead, it is possible that the new era of higher crop prices could be extended well into the future as a result of the RFS for advanced biofuels that in all likelihood can only be met with a rapid expansion in biodiesel production. The new price era, then, would not be extended by rising corn demand, but by rising vegetable oil demand. Whether this scenario actually is realized depends crucially on the evolution of biofuels policy here in the U.S. and energy policies in Brazil.



Notes

Additional Resources

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http://www.farmdoc.illinois.edu/presentations/IFES_2012

http://farmdocdaily.illinois.edu/2012/05/is-the-long-ethanol-boom-comin-1.html

http://farmdocdaily.illinois.edu/2012/08/ethanoldoes-the-rfs-matter.html

http://farmdocdaily.illinois.edu/2012/09/the-impending-collision-of-bio.html

Crop Insurance - Tax Reporting Options

Gary J. Hoff, Associate Director, University of Illinois Tax School
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Email: ghoff@illinois.edu

Approximately 80% of Illinois farmers purchased various types of crop insurance on their 2012 crops. The total premiums for these policies were over $770 million. It is projected that the total claims will exceed twice the amount of the premiums.

If farmers do not defer their crop insurance proceeds until 2013, they will have an additional $1.5 billion of taxable income this year.

In the past, it was not difficult to decide to defer reporting the crop insurance income until the next year. However, with today's tax climate, one has to wonder if it will save tax or increase the tax bill by deferring.

Marginal income tax rates are in a state of flux. Will they remain the same or will they increase, at least for higher income taxpayers? The 33% rate will increase to 36% and the 35% rate will increase to 39.6%

The new Medicare tax increase will begin in 2013. The new tax is based on the lesser of net unearned income or modified adjusted gross income in excess of $250,000 for joint return filers and $200,000 for single filers. The tax will be 3.8% on net unearned income including interest, dividends, annuities, rents and royalties (crop share), passive trades or businesses, and gains from other than business property. The tax is .9% on earned income.

If the "Bush tax cuts" are allowed to expire, the IRC §179 expensing deduction will go from $139,000 in 2012 to $25,000 in 2013. There will no longer be any 100% or 50% bonus depreciation. And, unless an AMT patch is made, millions more taxpayers will be subject to the alternative minimum tax this year.

If you want to defer 2012 crop insurance proceeds until 2013, you must follow certain rules:

1. There must be a history of deferring at least 50% of the crop until the following year. If multiple crops are involved, the 50% test must be satisfied for each crop.
2. If you have multiple farms and keep separate records for each farm, the election need not be made on all farms. However, you will need separate tax forms for each farm.
3. An election must be attached to the income tax return and must contain certain items.
4. If you receive the crop insurance check for the 2012 crop in 2013, you cannot defer the income until 2014.
5. You must use the cash method of accounting.
6. There are many types of crop insurance. Only those payments for loss of crop qualify for deferment. Policies that insure revenue do not qualify. A policy that has both a yield and a revenue component can be separated and the yield component deferred, but it may be difficult to determine the payment due to yield loss.

	2012	2013	Increase
FICA	**$19,753**	**$21,955**	**42,202**
New Medicare Tax	**0**	**1,900**	**1,900**
High Income Health Insurance	**0**	**327**	**327**
Tax rate change	**85,649**	**97,623**	**11,974**
AMT	**8,578**	**0**	**(8,578)**
Total Federal Tax	**$113,980**	**$121,805**	**$7,825**

Notes

Additional Resources

The slides for this presentation can be found at:
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For current tax information, see:
http://www.taxschool.illinois.edu/taxbookarchive
http://ruraltax.org
http://www.irs.gov

For expiring tax provisions, see:
https://www.jct.gov/publications.html?func=startdown&id=4383

Crop Insurance – 2012 Performance and Updates for 2013

Bruce Sherrick, Professor
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Though final numbers will not be known until early 2013, crop insurance policies resulted in very large indemnity payments over a large region of the Corn Belt for both corn and soybeans for the 2012 crop. Policies that included the harvest price option benefitted significantly from the increased harvest prices (corn = $7.50 and soybeans = $15.39) relative to March projected prices (corn of $5.68 and soybeans of $12.55), and the resulting increased guarantees. Producers without claims benefitted from the higher market prices that accompanied the lower production due to drought. The Risk Management Agency has announced several important changes to available crop insurance programs for the 2013 crop year as well and these will be identified and discussed including substantial changes to group policies, extensions and expansions of the Trend Adjusted APH endorsement, impacts of rerating, and the likely impact of the payouts from this year's policies.

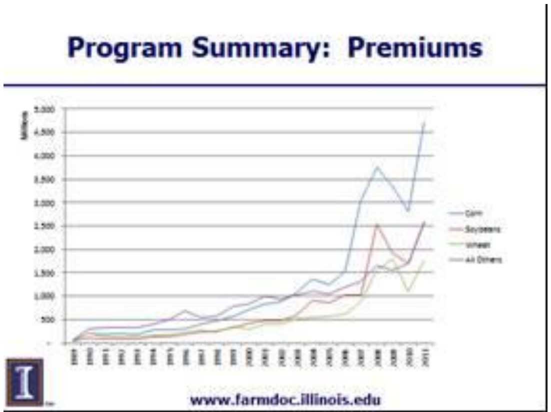
This session will begin with an assessment of the extent and types of coverage utilized by farmers in 2012, and will examine the relative performance of alternative crop insurance products available from RMA. Overall program composition and premium shares continue to move toward corn and soybeans driven largely by higher commodity values.

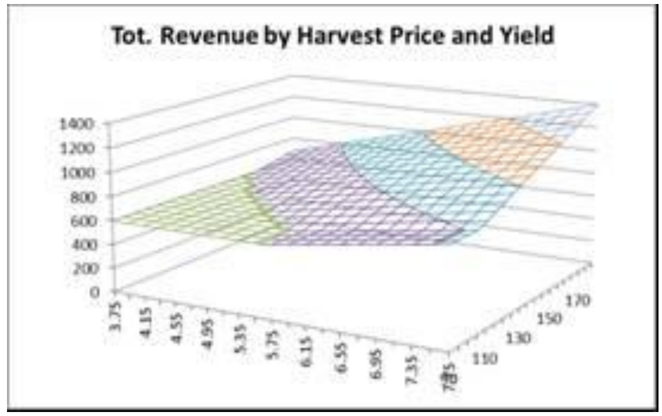
Expected costs of insurance by product given current market conditions will be examined and compared using the crop insurance decision tool available at the *farmdoc* website. Additionally, the *iFARM* crop insurance evaluator will be used to show how the alternative products would be expected to perform in terms of net cost of insurance, frequency of payment, degree of relatedness to revenue, and effectiveness at preventing low revenues for specific farm conditions under possible yield and price outcomes.

Importantly, numerous additional "shallow loss" and supplemental yield, price, and revenue programs are being discussed as part of the farm bill negotiations. The relationship to traditional crop insurance will be discussed along with guidance for evaluating the alternatives that are currently being debated.

Overall, the session should improve your understanding of new programs and features, and help develop an accurate understanding of your own crop insurance alternatives to best manage relevant risks.

The *farmdoc* crop insurance section contains premium calculators, payment evaluators, and other tools to help farmers evaluate their crop insurance alternatives. Final premium impacts depend on the projected price and volatility factors that will not be final until March 2013.





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Additional Resources

The slides for this presentation can be found at:
http://www.farmdoc.illinois.edu/presentations/IFES_2012

Risk Management Agency website:
http://www.rma.usda.gov/

farmdoc Crop Insurance Section :
http://www.farmdoc.illinois.edu/cropins/index.asp

Overview and Impacts of Proposed Changes in the 2012 Farm Bill

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The main issue shaping the political debate around the 2012 Farm Bill is the desire to cut spending for deficit reduction. While farm programs do not represent the biggest piece of the Farm Bill pie, they are the main targets for program modifications and reductions in overall support as they become more difficult to justify with farm incomes reaching record levels.

The United States Senate has passed its version of the 2012 Farm Bill. The House Ag Committee has also passed a version of the 2012 Farm Bill, but it has not yet reached a vote on the House floor. While the two versions of the Farm Bill are different and will require some reconciliation before a final Farm Bill is sent to the President's desk, they have both been scored to achieve savings relative to current programs.

Both versions achieve these savings via cuts to Commodity, Nutrition, and Conservation programs while projected support for Crop Insurance programs would increase. These proposed changes suggest a shift in farm program focus from income supports to risk management where the federal crop insurance program serves as the main safety net for crop producers.

Existing commodity programs – direct and counter-cyclical, ACRE, and SURE – are eliminated in both Farm Bill proposals. The Senate version replaces these programs with a "shallow-loss" revenue program where farmers would have the choice between county- and farm-level coverage. The House version would offer producer's the choice between a county-level revenue program or price supports with updated target prices for eligible commodities. In addition, supplemental crop insurance coverage is created in both versions.

The shallow loss revenue programs base their guarantees on Olympic averages of recent yields and national cash prices, and have payment limits and eligibility rules based on adjusted gross income. In contrast, supplemental insurance coverage bases its guarantee on insurance (futures) prices and trend yields and will not be subject to payment limitations, but will require the producer to pay a subsidized portion of the premium.

Thus, these new and modified programs will require producers to make choices among programs which offer varying forms of price and yield risk protection. Furthermore, their individual crop insurance purchases may also influence the risk protection offered by the supplemental insurance coverage option and their choice among the modified commodity programs.

Despite more than a year of debate, the likelihood of a Farm Bill being passed in 2012 is still very uncertain. The threat of "permanent" law being put in place if current programs expire should encourage some form of action by Congress prior to the end of 2012. Possible scenarios for the Farm Bill in the lame duck session include House and Senate passage via standard or expedited processes, or a short- or long-term extension of current programs. Given the short timeframe, the general view is that some form of extension will be passed and the Farm Bill will be revisited in 2013.

Figure 1: Projected Changes in Program Spending by Title for the 2012 Farm Bill FY 2013-2022

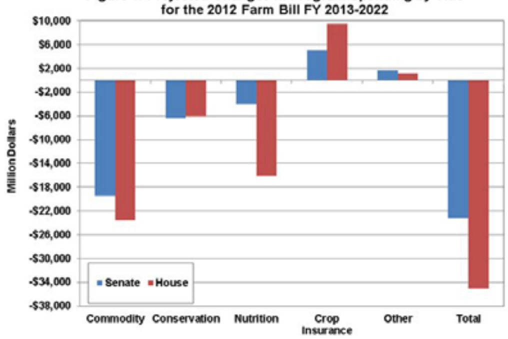

Figure 2: Illustration of SCO with 75% Individual Insurance Coverage

Notes

Additional Resources

The slides for this presentation can be found at:
http://www.farmdoc.illinois.edu/presentations/IFES_2012

Monke, J., M. Stubbs, and R. A. Aussenberg. "Expiration and Possible Extension of the 2008 Farm Bill." R42442, Congressional Research Service, July 25, 2012.
http://nationalaglawcenter.org/assets/crs/R42442.pdf

Paulson, N., G. Schnitkey, and C. Zulauf. 2012. "Comparison of Changes in Program Spending in the Senate and House Farm Bills."
http://farmdocdaily.illinois.edu/2012/07/comparison-of-changes-in-progr.html

Zulauf, C., G. Schnitkey, and N. Paulson. 2012. "First Draft of New House Farm Bill."
http://farmdocdaily.illinois.edu/2012/07/first-draft-of-new-house-farm.html

Zulauf, C. "Update on U.S. Senate Version of Crop Safety Net."
http://farmdocdaily.illinois.edu/2012/07/update-on-us-senate-version-of.html