Managing Risk

WHY BUY CROP INSURANCE?

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Have you been missing out on crop insurance because you've heard it's a lousy way to make money? If so, read this article. You probably don't understand the rationale behind crop insurance and other risk management strategies.

Crop insurance is not an investment tool! It's a risk management tool that is used to put a safety net under cash income. In times of low production and damaging weather such as hailstorms, wind storms, and drought, crop insurance enables farm families to meet their financial obligations, both business and personal, and helps ensure the survival of the farm business.

To understand the role that insurance plays in financial security, consider what happens at the end of a difficult season. If the grower has an operating loan, low receipts may make it impossible to repay all or a portion of that loan, and the unpaid debt gets rolled over into intermediate debt. Liabilities on the balance sheet are now higher than they were at the end of the season the year before, and debt payments are increased. If the farm was already operating at a high debt to asset ratio (e. g. 70 percent), the lender will look hard at the business' financial situation before advancing operating capital for the next season. This happened to many apple growers over the period 1998-2000, when low market prices and a string of weather events threatened the financial security of many of the state's fruit farms. Some went out of business and many teetered on the brink of insolvency.

Crop insurance provides a safety net that prevents receipts from going below a certain level. Multiple Peril Crop Insurance (MPCI)**,** offers basic protection against the risk of production losses due to weather, wildlife damage, fire, or other catastrophe. Another crop insurance product, Adjusted Gross Revenue (AGR) Insurance**,** helps in the event of low prices as well as low production. Both MPCI and AGR are available for many of the major fruit and vegetable crops grown in the Northeast, and they can be combined to provide coordinated premium payments as well as coordinated benefits. For crops that are not yet insurable under the Federal Crop Insurance Program, the Non-insured Crop Assistance Program (NAP) may be helpful.

Now, back to the idea that crop insurance is not a good *investment*. It is correct that, over time, you will not make money by consistently buying crop insurance. In the long run, you can expect to pay out more in premiums than you receive in payments. So why buy crop insurance?

Insurance is about protecting investments, not making money. Consider fire insurance. Would you like to collect on fire insurance? Most of us wouldn't! We expect to pay premiums every year, and hope that we don't ever collect from fire damage. What about collision insurance on your vehicles? Most people would prefer not to collect on their collision insurance. You probably pay a hefty amount each year for fire and vehicle insurance, and you probably don't expect to make money doing so.

Fire and vehicle insurance both illustrate the general principle behind crop insurance. That is, over time we expect to pay more in premiums than we collect. But by insuring we are avoiding the small probability of a large loss that would make us unable to meet personal or business financial obligations*. Crop insurance helps the business to survive in the hopefully occasional year in which receipts are low.

The incidence of crop disasters is probably slightly higher than the incidence of vehicle damages from which the average person would collect on their vehicle insurance. And crop disasters are far more frequent than fires that destroy property. Yet most Northeast growers are not taking advantage of this important risk management tool.

In 2000, the Hudson Valley experienced severe hail damage that left fruit growers with an estimated two million bushels of unmarketable apples. We conducted a retrospective survey and analysis of how growers had managed their hail damaged crops. We asked what growers wished they had done differently in 2000. Six of the 30 who responded said they wished they had bought crop insurance prior to the season. As one grower put it, "Over 20 years you lose money buying insurance. The idea is to be there after 20 years."

Keeping your business going through tough times is the idea behind crop insurance. To find out whether it makes sense to insure your fruit, vegetable or other horticultural crop, contact your insurance agent.

*Actually, with government subsidized crop insurance, payout may be more than premiums paid. However, that has not generally been the case with specialty crops in the Northeast; growers should expect to pay out more in premiums than they receive in payment over time.

NOTE: The **deadline is MARCH 15** for insuring eligible spring-planted crops. (The deadline for perennial crops was last November.)
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For more information on horticultural crop insurance, or on risk management in general, follow the links below:

- **Risk Management**
- **Multiple Peril Crop Insurance**
- **Adjusted Gross Revenue Insurance**
- **Noninsured Crop Disaster Assistance Program**

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