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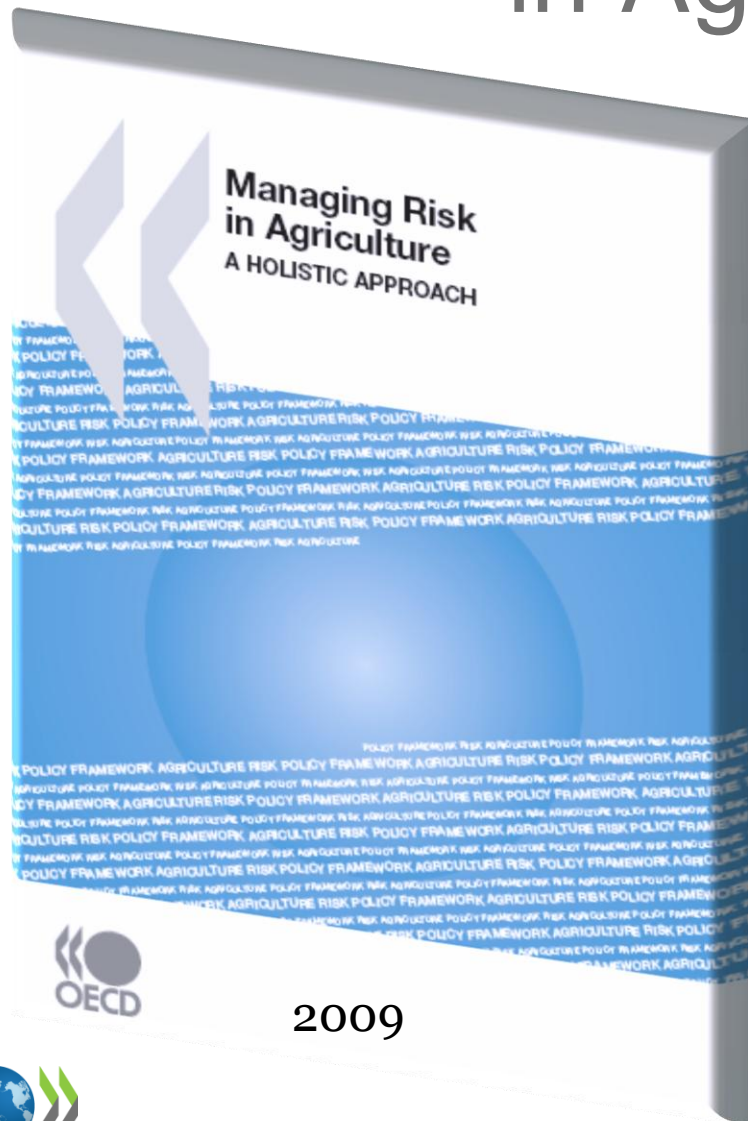
# Risk management in Agriculture: What Role for Governments?

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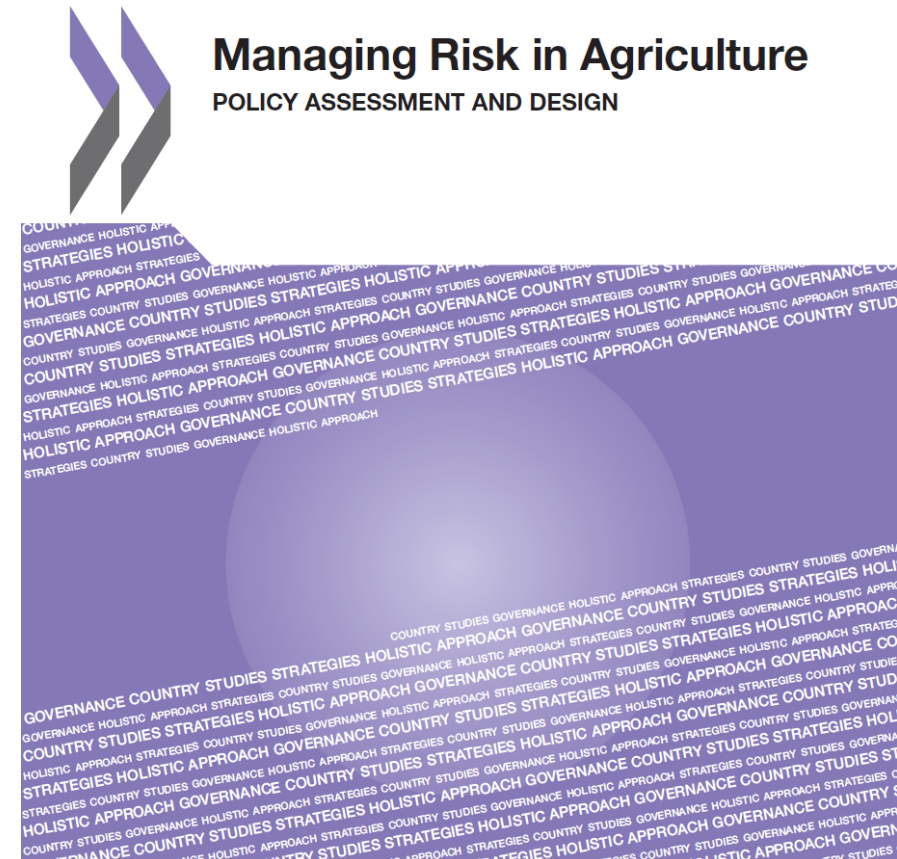
123 EAAE seminar « Price volatility  
and Farm Income Stabilization »

Dublin, 23-24 February 2012

# OECD Work on Risk Management in Agriculture



2009



2011

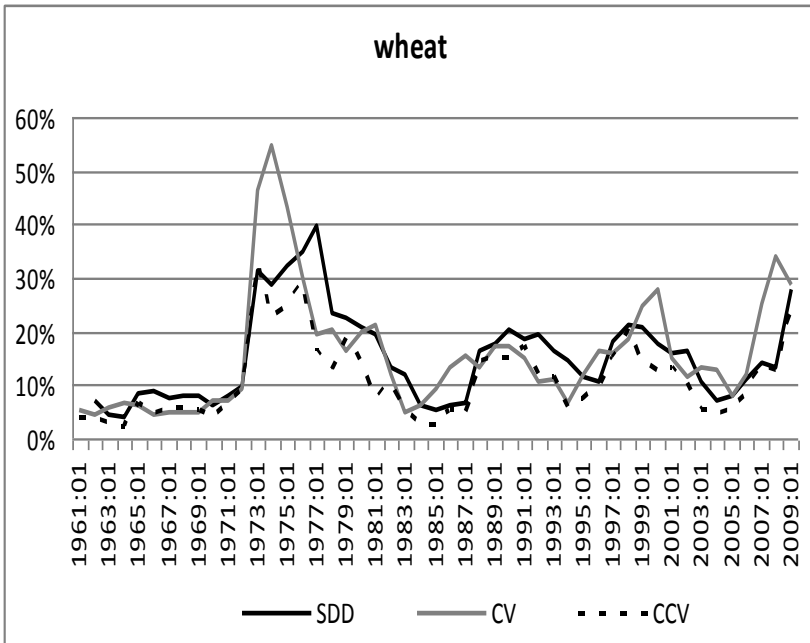
# Outline

- Volatility and stabilization
- A framework to think of policies
- Policy experiences
  1. Direct Payments
  2. Price Interventions
  3. Insurance support
  4. Mutual Funds
  5. Income stabilization
  6. Food aid
  7. Funds for “crisis”

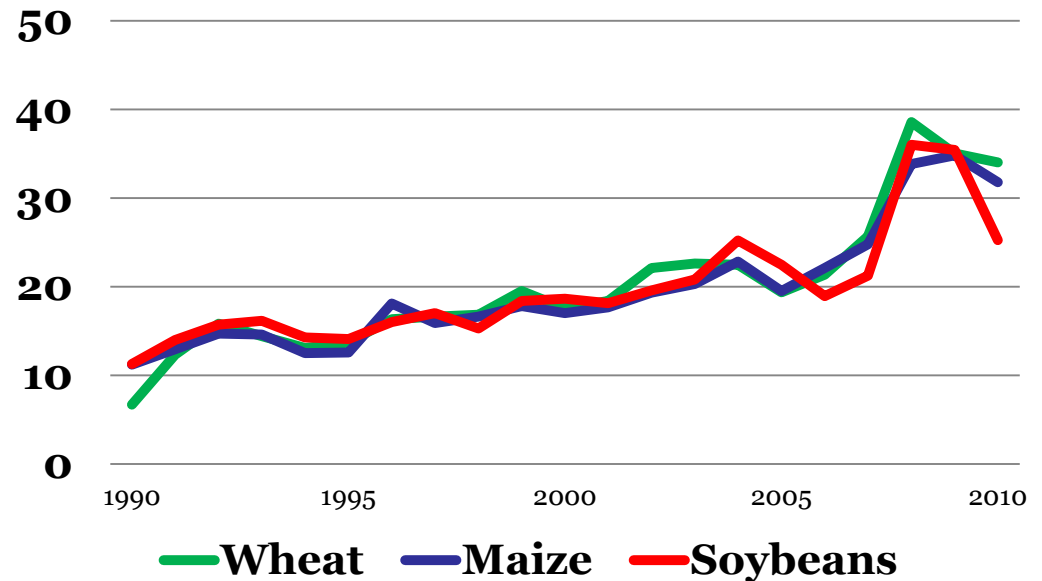
# Has Price Volatility Increased?

## Annual Price volatility

wheat



## Implied Price volatility (CBT)

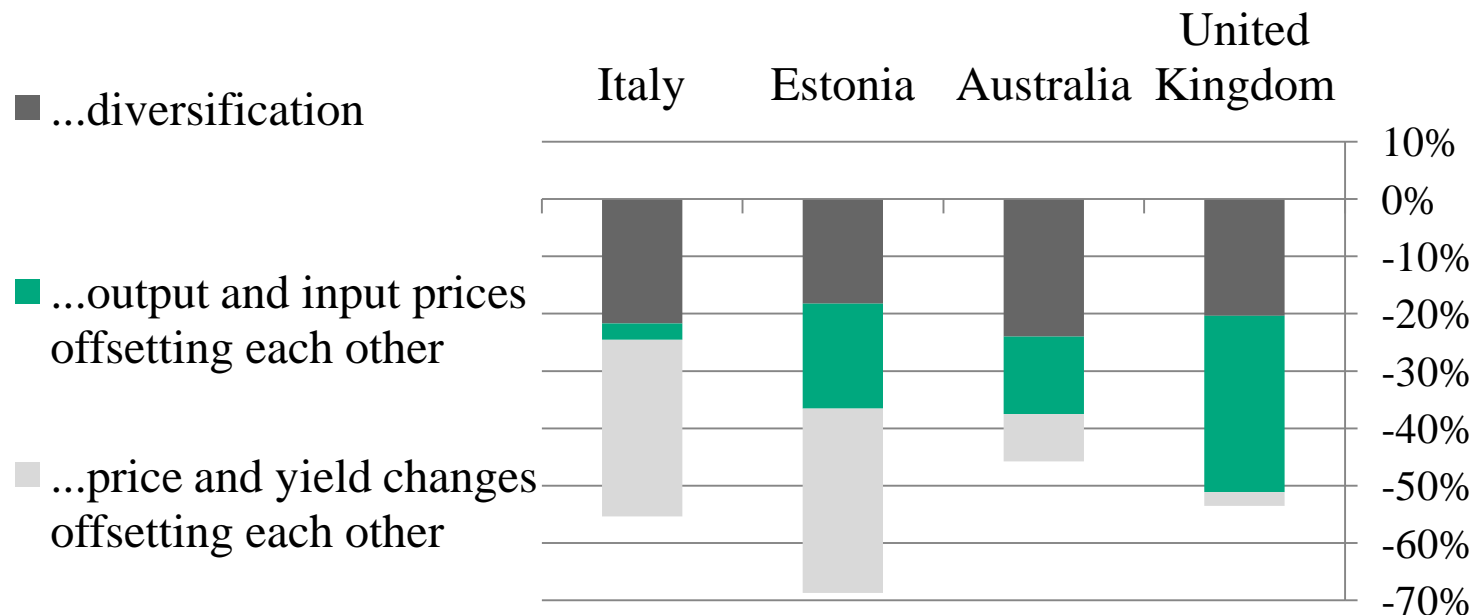


# What does it mean for farm income?

## Not much: interactions between risks, strategies and policies

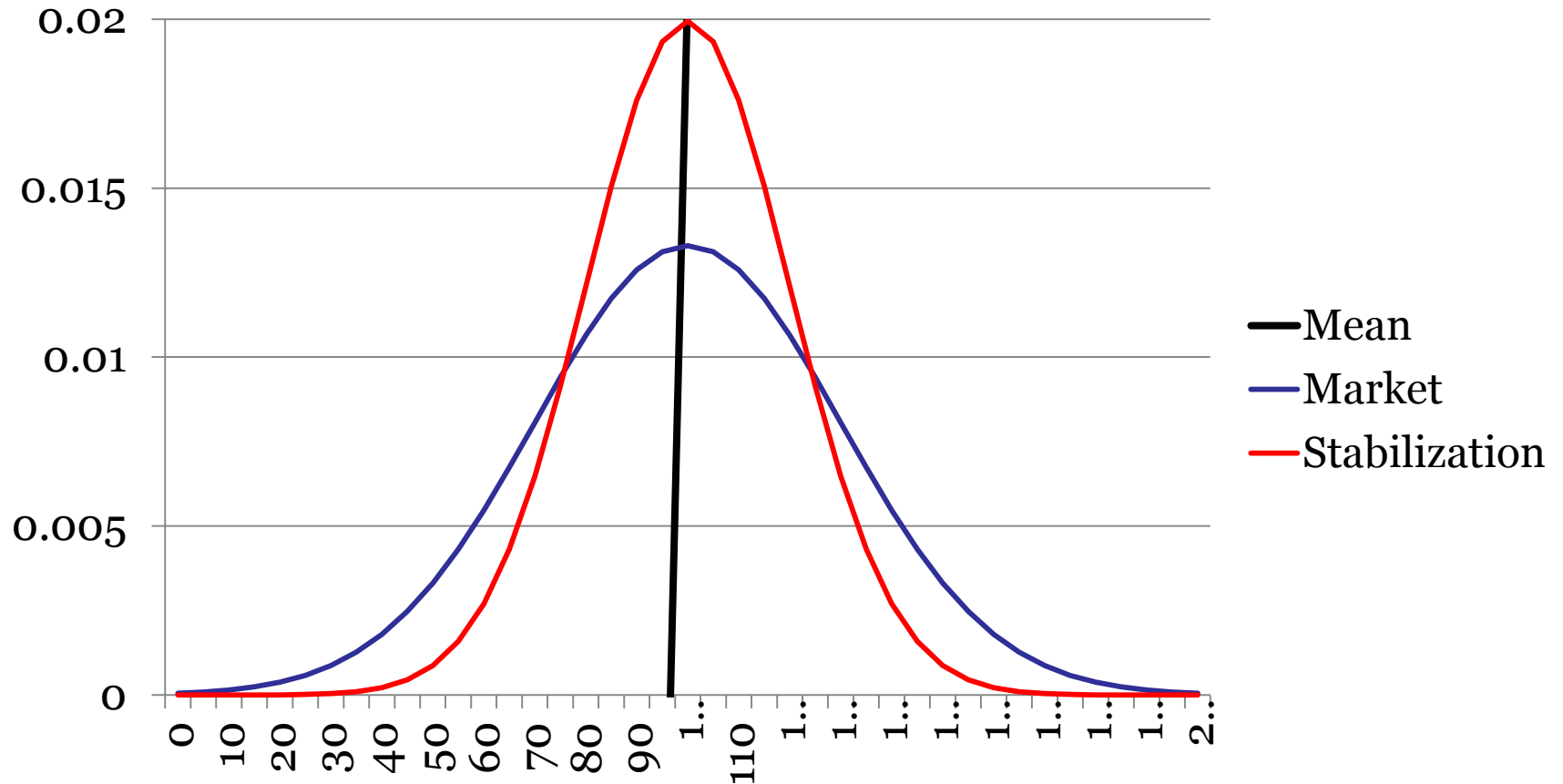
- *Correlations, diversification, government's programmes*

**Farm income variance is reduced by ...**

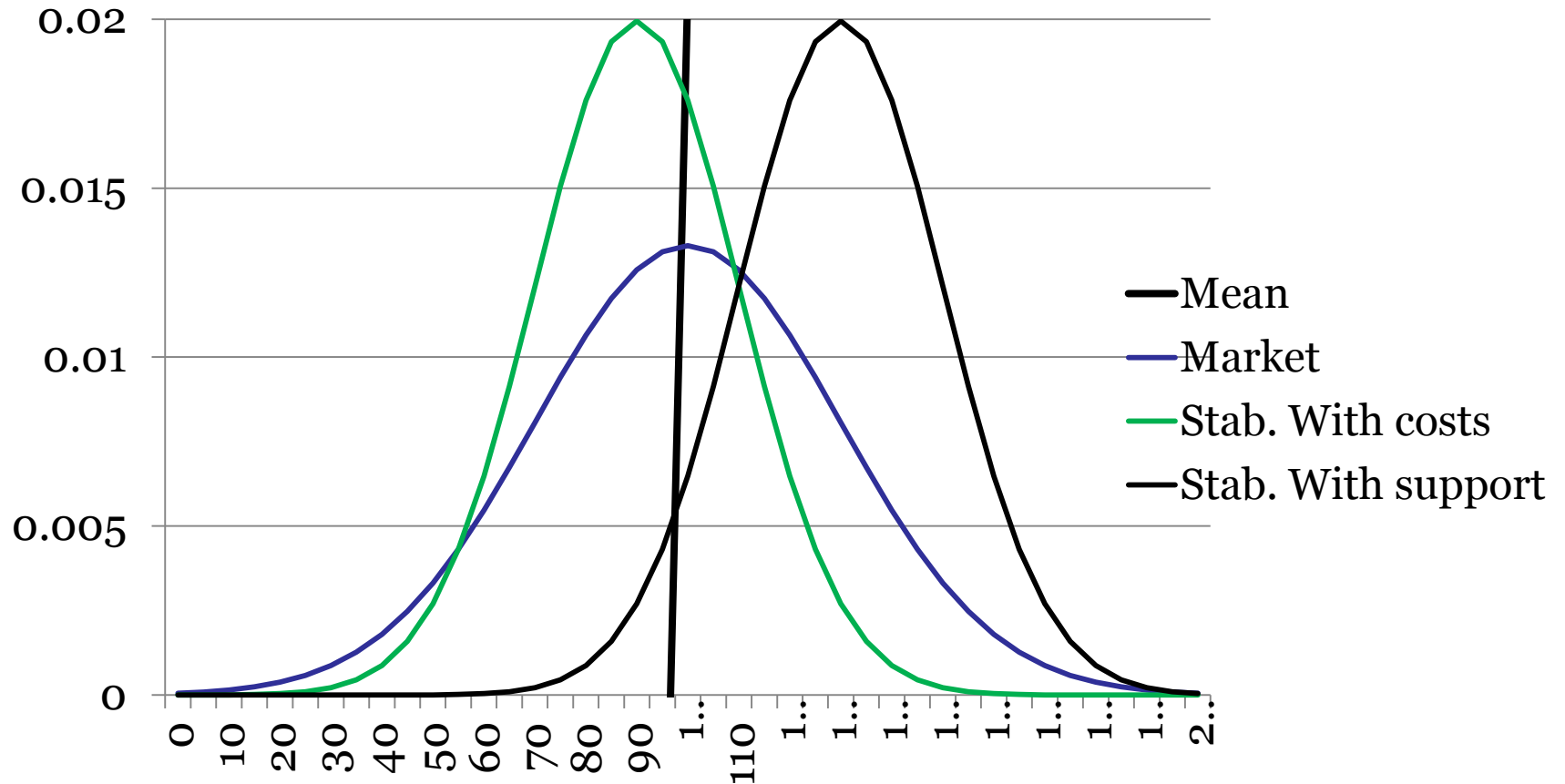


Decomposition of the variance of income of arable crop farms. The reference level of risk is the calculated variance in the counterfactual case of zero correlations, co-variances and diversification. Based on time series of individual farmers.

# What does stabilization mean?

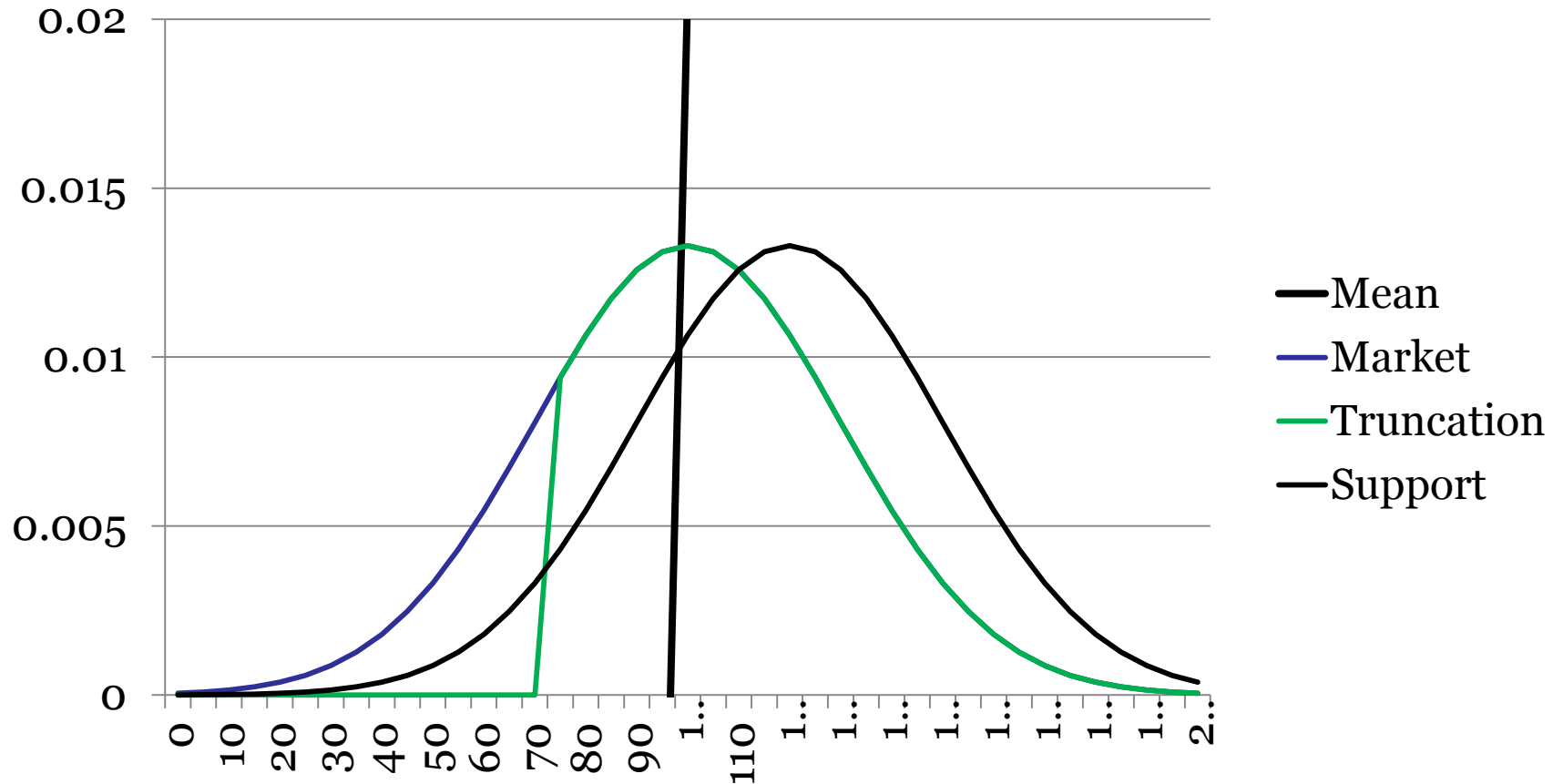


# What does stabilization mean?

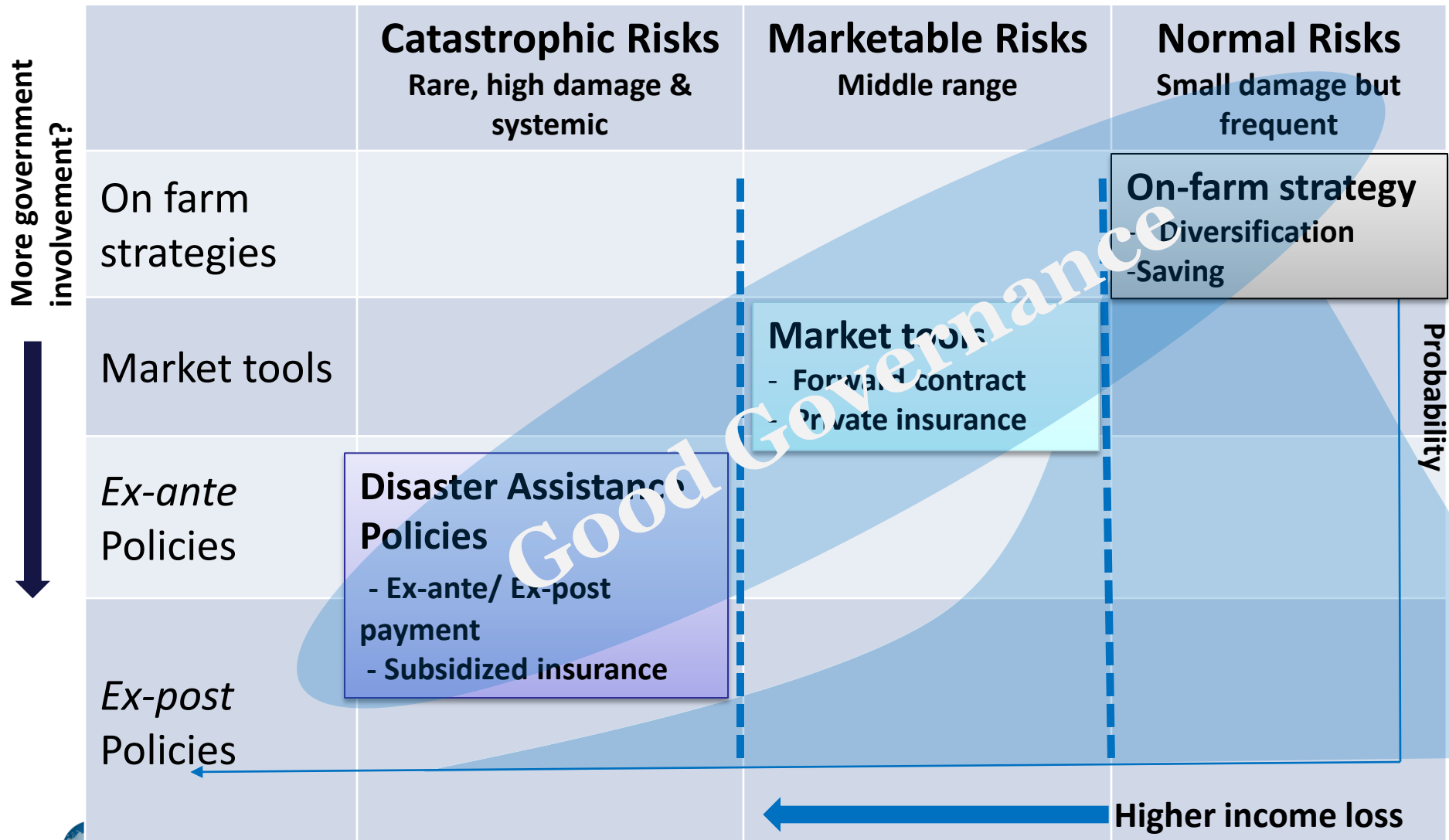




# What does stabilization mean?



# Good policy response: Risk layering



# Crowding-out effects

- Government compensation for non-catastrophic risks off-sets pro-active risk management strategies:
  - Diversification: the main strategy
  - Market instruments
    - Contracts / integration
    - Futures: farmers benefit
    - Private insurance: asymmetric information
- Strongest crowding out from policies that address normal business risk:
  - Price support, income stabilization, CCP
- Weakest crowding out: Fixed highly decoupled

# Policy approaches in different OECD countries

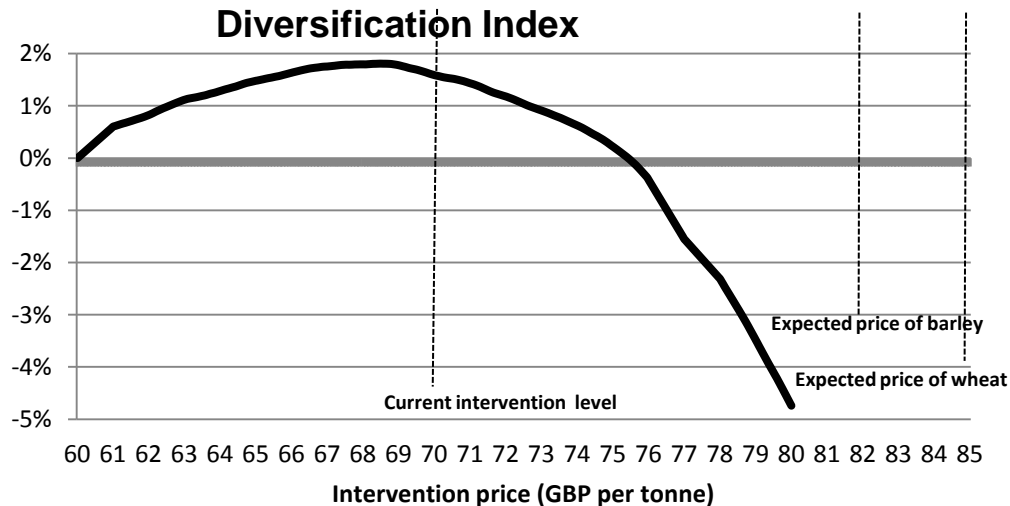
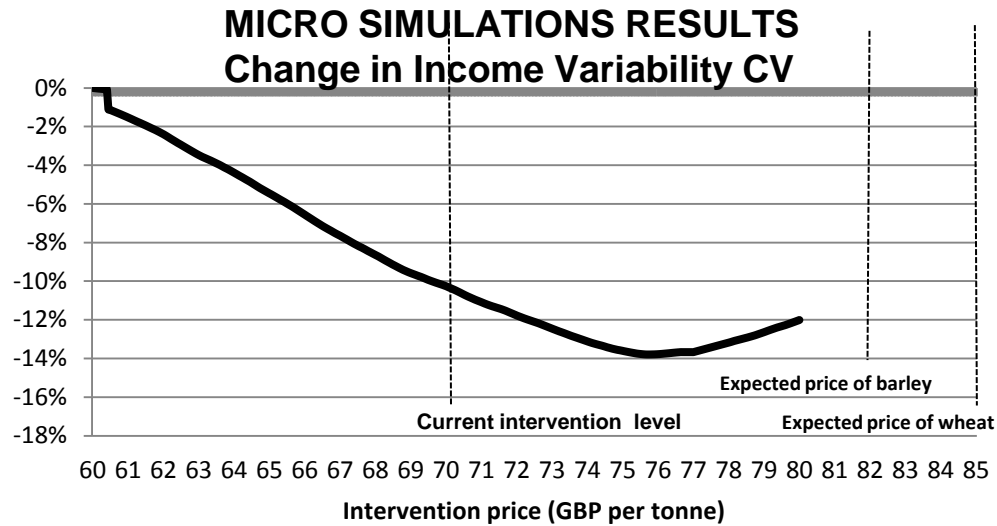
- Canada: margin stabilization
  - Agri-Invest, AgriStability, Agri-Insurance, Agri-Recovery
- US: Price / revenue stabilization
  - DP, CCP, ACRE, Insurance
- Australia y NZ: Disaster assistance
  - Bio-security; Drought and adverse events
- Japan: Price support and stabilization
- UE: Before MPS, today DP, Recently: risk management



# 1. Direct Payments

- Useful for risk management
- Other countries make them countercyclical
  - US' MLA, CCP, ACRE...
  - Canada income stabilization (AgriStability)
- Advantages and disadvantages of countercyclical payments:
  - Socially acceptable
  - No payments when prices / revenue / income are high
  - Complexity of targeting

# 2. Price Interventions

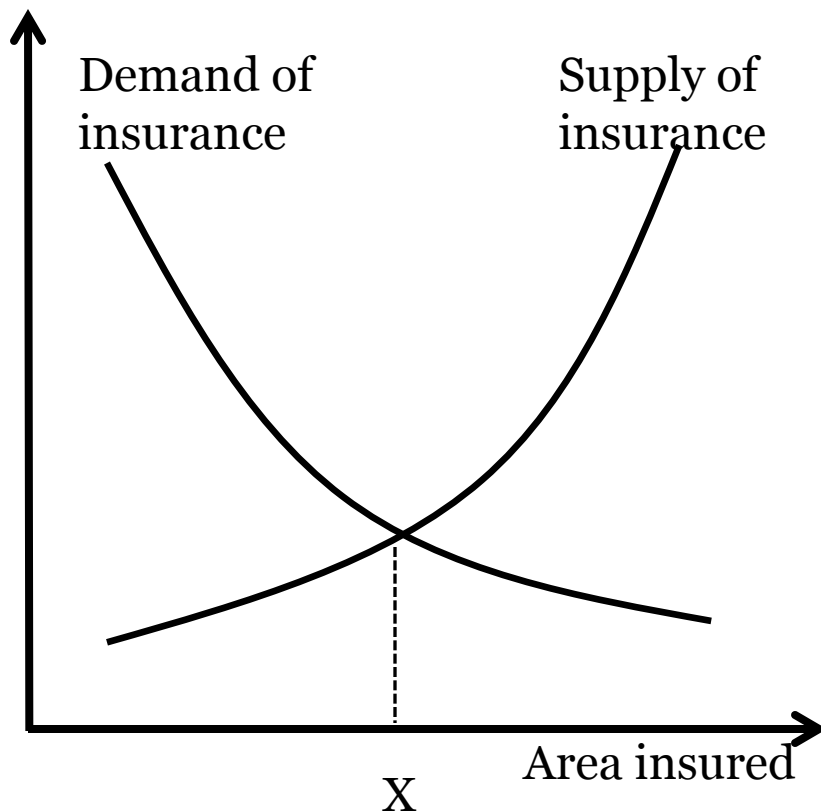


# Price Interventions: EU “Safety nets”?

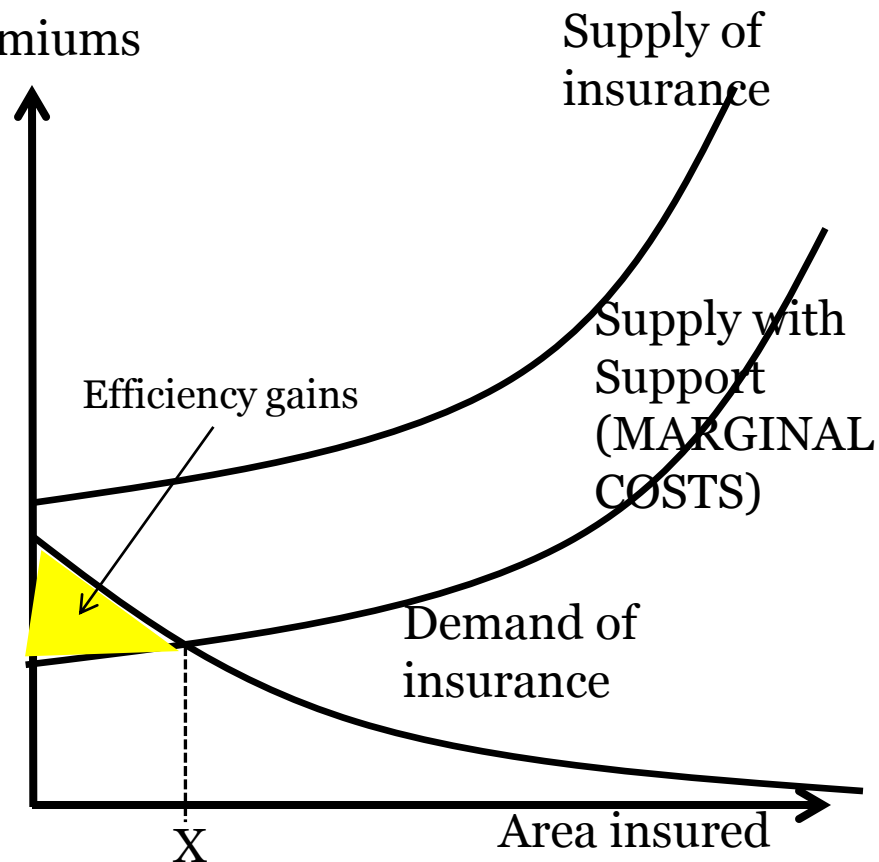
- It has nothing to do with a “safety net”
- They **Reduce** risk rather than **Manage** risk
- Only effective for very low Intervention prices
- Beyond certain level, it increases variability:
- Today “irrelevant” due to high world prices
- Other countries:
  - MPS in most countries
  - US’ MLA

# 3. Insurance market: will risk be transferred?

Premiums



Premiums

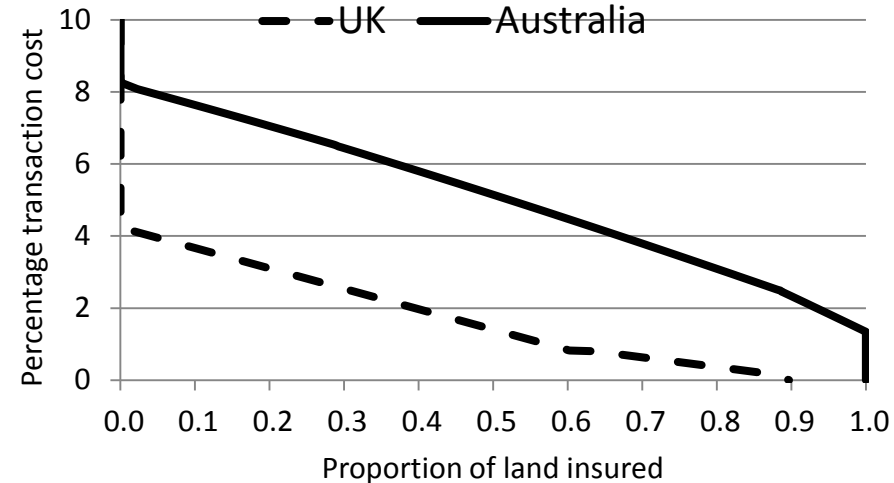




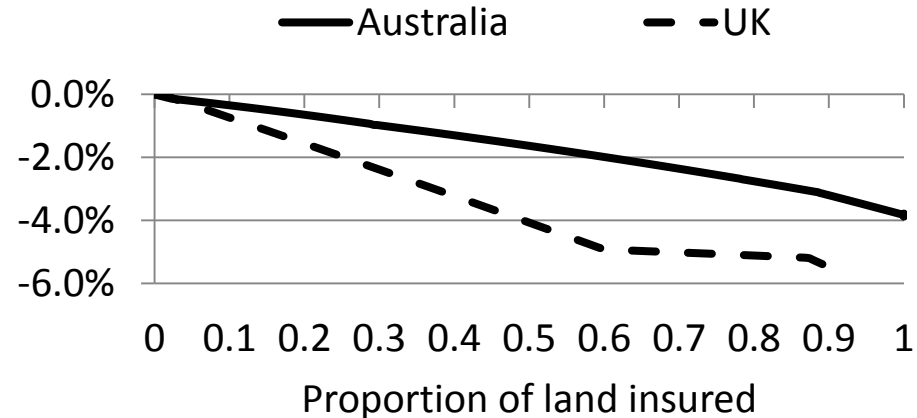
# Support to Insurance

- Demand for insurance is hard to increase
- Start-up support
- Many countries have subsidized insurance (us, Canada, Spain...)
  - Differentiate catastrophic and marketable policies
  - Phase-out subsidies for non-catastrophic
  - Avoid rent seeking

## Demand for crop yield insurance



## Crowding out: Diversification index



# 4. Mutual funds for Animal diseases

- There are examples in different countries that these can work
- Main difficulty is a clear-cut definition of government actions:
  - the rules that trigger control measures
  - the rates of co-financing with producers, and
  - the boundaries of public compensation
- Need of an overall agreement on how to govern animal diseases

# 5. Mutual funds for income stabilization

Not many examples in the world.

- Agri-Stability in Canada is not a Mutual Fund but a CCP

- Trade-offs exist between targeting income and timely delivery

- Delays to collect information and Black box adjustments

- With delays payments are not counter-cyclical, become mere income support, and create demand for additional measures

- Tax files are best sources of income information

- In theory, smaller mutuals can better monitor income.

# 6. Food aid

- Many other countries have domestic food aid programs:
  - In the US, 33 \$ billion annually in 2008-10 > PSE
- The main issue is good targeting of the population in need.

# 7. Funds for crisis

## Governance of Catastrophic risk

- OECD Governments will always be called on to provide disaster assistance
  - Political pressure
  - Be prepared with some *ex ante* framework
    - Procedures, Delineation of responsibilities, Triggering criteria, Types or levels of assistance
    - Examples: N. Zealand, Australia, Canada, The Netherlands, Spain

# ... Catastrophic assistance

- Crop insurance as a disaster assistance device
  - + Farmers pay, transparent trigger, stable budget
  - Refrain from non-catastrophes, deter *ex post* assistance and efficient administration
  - *Only for production risk*
- How to enhance the role of the EU Commission in the Governance of catastrophic risk?

# Conclusions

- Government policies should take a holistic approach
- Agricultural risk management policies should focus on catastrophic risks
- Subsidized insurance as disaster assistance has flaws...
- Support to market based instruments should focus on “start-up” conditions
- Government policies should not provide support to deal with normal risk

# Conclusions EC Proposals on RM

- Risk management focus is welcome
- Progressive approach to develop risk management instruments, and farmers' engagement
- Developing governance frameworks for catastrophic risk across the EU
- The governance of the funds for crisis is crucial



# For more information



## Trade and Agriculture Directorate

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**[www.oecd.org/agriculture/policies/risk](http://www.oecd.org/agriculture/policies/risk)**
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