

New water stress insurance

By John van der Vegt, AgriRisk Services

All manufacturers face production risks. But Australian farmers are out on their own in terms of having their income producing assets so heavily exposed to natural perils. And of all the crop producers, Australian dryland wheat farmers arguably have to deal with the highest level of production risk.

Depending on their location crops are routinely exposed to insufficient and excessive rainfall, drought, frost, hail, flood, fire, disease and so on. Managing the majority of these risks is difficult and in some circumstances impossible.

Multi-Peril Crop Insurance (MPCI)

When a large number of growers are impacted by the same peril, these growers can often seek government assistance through the exceptional circumstances provisions – but this process is often complicated and inequitable. These situations also reignite the groundswell for more comprehensive insurance programs such as MPCI.

MPCI programs operate in a number of developed and developing countries around the world. As their name implies, they offer significantly broader coverage than the single or named peril (such as fire and hail) policies on offer to Australian farmers.

In some instances the MPCI programs provide an income guarantee for farmers virtually transferring all production (and often marketing) risks to the insurer.

So why aren't MPCI programs available in Australia?

Following significant frost losses in Western Australia in the late 1990s a government taskforce was established to look at the feasibility of establishing an MPCI program for Australian wheat growers. In 2003 the task force concluded that the cost of the cover would be relatively high – in many areas above 10 per cent of crop revenues – and as a consequence the participation of growers would be low.

This would increase 'adverse' selection by growers – whereby higher risk growers would tend to take up the insurance due to their higher likelihood to make a claim. It was therefore concluded that most insurers would not be interested in providing the coverage simply because they did not see how they would make a return on their investment in the product.

After reviewing many successful MPCI



A pilot scheme in 2008 has led to the limited release this season of an innovative water stress insurance product.

programs, the taskforce noted that they seem to have two key features:

- Strong government support – generally the level of support via premium subsidy is higher than 50 per cent. This of course makes the premiums far more affordable for growers. In the US the government's contribution to MPCI exceeds US\$8 billion.
- The insurances are compulsory – this removes the moral hazard aspects, guarantees a premium pool and allows the government to remove any other exceptional circumstances type funding.

Also in many of the countries where MPCI is successful, there is a strong rural economy and a significant voting base. By significantly funding an MPCI the government can ensure the viability of these rural economies and hopefully secure their voting base.

In contrast, Australia of course has a very small rural voting base and it is fair to say that the government is less likely to provide significant assistance to a single interest group on the basis of inequity, notwithstanding the importance of the wheat crop to Australia's 30–40,000 growers, their rural communities and export earnings.

Managing the rainfall risk

Whilst there doesn't seem to be a solution to the MPCI issues in the short term, the specialist crop insurer, Primacy Underwriting Agency, have been looking at MPCI to ascertain whether an alternative program might assist growers in managing their production risks.

Primacy have analysed dryland wheat growers' production risks and found that some 70 to 90 per cent of yield variability is attributable to rainfall, either insufficient or excessive. This is followed by hail, frost, fire and disease.

Rather than trying to manage all of these perils like an MPCI program, Primacy have concentrated on managing the most critical risk – rainfall.

Last season Primacy introduced YieldShield, an innovative insurance product designed to assist dryland wheat growers in managing water stress (insufficient or excessive rainfall) once their crops have reached first jointing.

The product was released on a limited pilot program basis available across 100 growing shires.

Based on solid grower feedback during this 2008 pilot phase, the product has been simplified and released for the 2009 winter cropping season. It is ideally suited to larger crop growers looking to manage their exposure to water stress.

They will generally be growers who try to forward sell their production and are then concerned about their exposure to contract washout. They are also likely to be growers who have previously looked at marketing tools or rainfall derivatives to manage the risk.

YieldShield is only available through a limited number of accredited insurance brokers including AgriRisk Services. For more information contact AgriRisk on FREECALL 1800 659 034 or yieldshield@agririsk.com.au ■