

DEPARTMENT OF AGRICULTURAL ECONOMICS

Risk Management Education: Perspectives of Producers and Agribusinesses

Texas and Kansas Risk Management Education Teams

Sensing that the significant policy changes in the 1996 Farm Bill could greatly increase economic risk at the farm and ranch level, the U.S. Congress directed the USDA to develop and deliver expanded risk management education to producers and agribusinesses. The challenge is to implement innovative educational programs that will help producers manage risk through improved assessment of the sources of risk and the effective application of the management tools available. The Texas and Kansas Agricultural Extension Services have formed a joint education initiative to meet this challenge.

To determine what the educational program's content and structure should be, Extension economists met with focus groups consisting of farmers, ranchers, lenders and other agribusiness representatives to find out their needs. These are the groups most directly affected by changes in the economic environment. Focus groups met in areas of Texas and Kansas where the new risk management education programs will be tested (Figure 1). The 23 focus groups (17 in Texas and six in Kansas) included 101 farmers and ranchers, 22 lenders and 14 representing other agribusiness firms.

Farmers and ranchers met in separate groups from the groups of lenders and other agribusiness representatives.

Discussions were designed to capture input to the following educational emphases:

- Developing educational materials to be used by farmers and by groups of farmers involved in risk management learning activities; and
- Developing a computer-assisted decision aid (FARM Assist) to help individual producers evaluate the degree of risk associated with alternative risk management strategies that could be used in their operations.

Focus group participants were asked about the sources of risk they, or their clientele, face in farming operations; the importance of alternative risk management strategies; the way in which they prefer to receive risk management information; and, the most appropriate educational format for learning about risk management strategies. This publication summarizes the feedback received from focus group participants.

Sources of Risk and Uncertainty

Focus group participants rated 21 sources of risk on a 5-point scale, with 5 meaning the source is very important and 1 meaning it is not important. The ten most important sources of risk as indicated by their average ratings are:

	Texas	Kansas	Combined
Commodity price variability	4.4	4.7	4.5
Commodity yield variability	4.3	4.3	4.3
Changes in input costs	4.1	4.1	4.1
Changes in environmental regulations	4.0	4.1	4.0
Unforeseen litigation	4.0	3.6	3.9
Changes in machinery costs	3.9	3.7	3.9
Injury, illness or death of operator	3.7	3.9	3.8
Changes in interest rates	3.7	3.9	3.8
Availability of skilled labor	3.7	3.8	3.7
Family health problems	3.7	3.8	3.7

The top three sources of risk and uncertainty were related to revenue (price and yield) and input costs. The top four sources of risk were the same for Texas and Kansas respondents. Uncertainty from changing environmental regulations was fourth. Items identified but which did not rank in the top ten sources of risk

and uncertainty included changes in farm programs, credit availability, technology, family relationships, land costs, contractual arrangements, and leasing arrangements. However, all of these had a rating higher than 3.0, meaning they are considered at least moderately important by the producers and agribusinesses.

The focus group discussions covered a broad range of farm and ranch business management concerns, which emphasized the need for help with decisions relating to the scale and structure of operations. Some areas of concern (other than those mentioned above) were purchasing versus leasing additional land, buying versus leasing equipment, evaluating new technologies such as precision farming, and retaining ownership of calves through the feedlot.

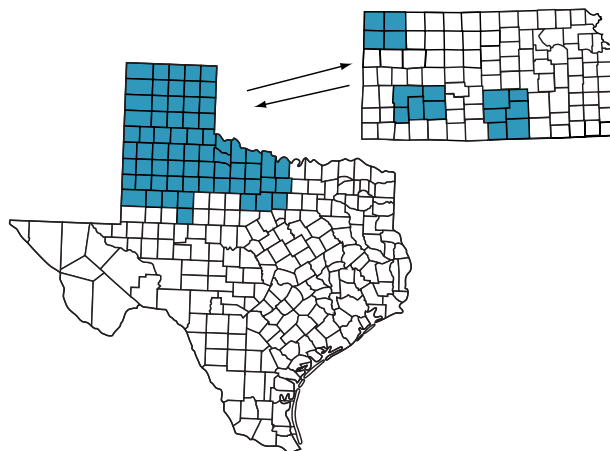
Important Risk Management Strategies

Participants rated the relative importance of 35 risk management strategies to the overall farm/ranch operations. The 15 most important strategies, as viewed by the participants, and based on the same 5 to 1 scale, were:

	Texas	Kansas	Combined
Debt management	4.2	3.7	4.0
Enterprise diversification	4.0	4.0	4.0
Forward contract selling	3.9	3.9	3.9
Liability insurance	3.8	4.0	3.9
Hedging the selling price	3.9	3.7	3.9
Government program participation	3.8	3.7	3.7
Commodity options	3.7	3.8	3.7
Cash contingency reserves	3.6	3.9	3.7
Multi-peril crop insurance	3.7	3.7	3.7
Operator life insurance	3.7	3.6	3.7
Using futures to hedge	3.6	3.9	3.7
Being low cost producer	3.6	3.6	3.6
Off-farm investments	3.6	3.6	3.6
Using variety of production techniques	3.5	3.6	3.5
Purchasing health insurance	3.4	3.5	3.4

The important risk management strategies were the same in both states. Of the top 15 combined risk management strategies, 13 were in the top 15 in Kansas and 14 were in the top 15 in Texas. Diversification ranked first in Kansas and second in Texas, reflecting the potential use of the flexibility provisions of the 1996 Farm Bill. Alternative methods for managing price risk tended to dominate the list, although financial management (debt and cash reserves) strategies also were very important. Multi-peril crop insurance

Figure 1. Texas and Kansas Pilot Areas



ranked 10th overall. It is interesting to note that while changing farm programs were of less concern as a source of risk, both Texas and Kansas respondents still rated government program participation high as a strategy for reducing risk. Strategies that ranked in the top 15 in Kansas, but not overall, were hail and fire insurance for crops (11th) and using a written marketing plan (12th). One strategy that ranked in the top 15 in Texas, but not overall, was the production of specialty crops under contract. Items not ranking in the top 15 in either state included minimum price contracts, production and marketing consultants, income insurance, hedging inputs, maximum input price contracts, cooperative pooling, buy-sell agreements among producers, backup management/labor, off-farm employment, disability insurance, machinery insurance, geographic distribution of production, and marital agreements regarding assets. Once again, however, most of these strategies received an average rating of 3.0 or higher—indicating that they still were considered important.

The unstructured part of the focus group discussions emphasized the broad scope in which farmers view the risk management issue. Strategies that seemed to receive greater attention in this forum included technology evaluation, estate planning, cooperative and group marketing, niche markets, and enterprise analysis. There also was considerably greater emphasis on risk management related to commodity pricing and yields compared to input costs.

Discussions also helped identify the specific economic performance measures used in making risk management decisions. Aside from using the traditional financial statements and ratios, the ability to analyze trends in these variables was viewed as par-

ticularly important. Evaluating farm/ranch operations by enterprise and by operating units also was emphasized. Respondents said a computer-assisted risk management decision support system should be capable of evaluating up to 50 operating units and 20 enterprises per unit, although a couple of respondents thought it important to be able to consider more than 100 operating units. Participants said they would also like to be able to evaluate alternative business organization structures, including sole proprietorship, partnership, limited partnership, subchapter S and C corporations, trusts, and closed cooperatives.

Media for Receiving Risk Management Education

Focus group participants rated the relative importance of seven media, or methods, in which risk management education can be delivered. The following preference order was revealed, again on a 5 to 1 scale of most important to least important:

	Texas	Kansas	Combined
Risk management meetings\clubs	3.9	4.1	4.0
Printed publications	3.7	3.6	3.6
Video tapes	3.2	3.4	3.3
Farm magazines/press	3.2	2.9	3.1
Home study courses	2.9	2.9	2.9
Internet publications	2.9	3.0	2.9
Audio tapes	2.5	2.7	2.6

While farmers may complain about too many meetings, meetings still are considered the best way to receive risk management education. Printed materials rank second, but participants emphasized they had to be short and to-the-point, with real-life examples/illustrations. In other words, producers do not want to be inundated with lengthy, complex material that is hard to read and understand.

Format for Learning Risk Management

Finally, focus groups rated the importance of six formats for educational programs. The six, in order of preference, are:

	Texas	Kansas	Combined
Short seminars (1 day)	3.9	4.0	3.9
Short presentations (1 hour or less)	3.6	3.2	3.5
In-depth multi-day workshops	2.8	2.9	2.9
Home self-study	2.7	2.7	2.7
Satellite/closed circuit TV seminars	2.6	2.7	2.6
Internet classes	2.3	2.6	2.4

The ranking of these six educational formats was identical for both states. One-day seminars appeared to be preferred because of the complexity of the material. In spite of that, however, participants preferred to receive education in 1-day segments or less, rather than in adjacent multi-day workshops. Home study, satellite and Internet methods received relatively lower ratings. The Internet alternative ranked marginally higher in Kansas than in Texas.

Implications of What We Learned

Farmers see risk management as a very broad concept that extends beyond crop insurance, futures, options, and contractual arrangements that affect revenue. They want to be able to better evaluate new farm program provisions that increase flexibility and open the door for greater diversification. They also want to know how to evaluate the economics of new technologies that might increase and stabilize yields, and control production costs. They are also interested in the potential of niche markets.

In other words, producers are looking for help in evaluating a broad range of issues beyond just the traditional risk management tools which have tended to focus mainly on prices and yields. Producers recognize the need for tools that help them measure and evaluate alternative risk management strategies, but they also want help with decisions relative to scale of operation, leasing arrangements and technological change.

A computer-assisted decision tool must be able to evaluate expected performance over time so that trends are discernible. It must be organized both on an enterprise and on a whole farm basis, both with and without the inclusion of the family budget. It must consider all major alternatives for business organization, because many operations include a number of organizational forms.

Producers prefer that risk management education take place in meeting segments of 1 day or less duration. They recognize that short, multiple-subject Extension programs can increase awareness, but meaningful education is difficult in this format. In-depth programs should be supported with publications that are short, focused, and contain real-life examples. In the future, the Internet might be an alternative means of distributing these articles, but people still want to be able to get in touch with an expert who can offer assistance.

The information on risk management education provided by these focus groups is challenging, but very useful. The initial products and programs developed by

the Texas/Kansas risk management teams may not satisfy all the needs and preferences that were identified, but a target is there to work towards.

Needless to say, the authors greatly appreciate all those who took the time and effort to participate in one of the focus group sessions to provide valuable feedback.

Along the way, we will go back to the focus groups and ask them to evaluate our performance and provide further advice.

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