
KENTUCKY FARM BUSINESS MANAGEMENT PROGRAM STATE NEWSLETTER

Vol. 7, No. 1
June 4, 2003

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KFBM UPDATE

⇒ Don't forget the meetings to be held in regards to the **KFBM Futuring Committee**. One was June 5 at Madisonville and another will be held June 23 at Elizabethtown. If you cannot attend either meeting but have some input you would like to contribute, please contact a committee member or a specialist.

⇒ Mark your calendars now for the **summer board meeting** to be held in Owensboro on July 24.

USDA UPDATE

Brian Lacefield

DCP—The deadline for the Direct and Counter-Cyclical Payment (DCP) Program is June 2, 2003. Presently, over 98% of the eligible farms in KY are enrolled. However, the remaining farms may still be enrolled in the program through September 2003 for a \$100 dollar fee per farm. No base or yield changes may be made.

For each farm that has been signed-up for the DCP Program you should have a USDA form 509-b. These have the base acres and yields for both the Direct and

Counter-Cyclical payments. Please have a copy of these for your fieldman on your next visit. The information on this report will be necessary for getting accurate calculations on your accrual FSA payments at the end of the year.

CRP—Sign-up dates for the Conservation Reserve Program (CRP) have been extended though June 13, 2003. To submit CRP offers, producers must visit their local Farm Service Agency. FSA offices will accept offers only during the sign-up period.

CDP—Sign-up for Crop Disaster Program (CDP) will begin June 6, 2003. Payments will be made shortly after sign-up. This program will reimburse producers for qualifying losses for 2001 or 2002 due to damaging weather or related conditions. Producers must choose between receiving payments for 2001 or 2002 crops. (Not Both)

LCPII—Sign-up continues for the Livestock Compensation Program II (LCPII) into June. This payment is for producers who did not receive Livestock Compensation Payments (LCP) last fall. If you received a payment last fall you are not eligible for this payment. Producers must provide

documentation to verify the eligibility of livestock claimed for payments that have been sold or died after June 1, 2002.

Additional information and specific details on these programs are available from your local Farm Service Agency office. Also visit the USDA on the Internet at www.usda.gov.



WEST KENTUCKY GRAIN MARKET PROJECT

Steve Riggins

Monthly Update, May 30, 2003

May has been a challenging month for grain farmers trying to make and/or implement marketing plans. As the month began, farmers were generally ahead of schedule for spring fieldwork and planting progress and there was concern about the quality of the winter wheat crop due to lack of moisture. The July Chicago Board of Trade (CBOT) soft red wheat futures contract retested the low it had made in late March at just under \$2.80 and promptly rallied to \$3.45 as weather concerns and a few new export sales occurred. As May ends the contract has given back about 20 cents of more than a 65-cent rally.

The November soybean contract started the month already in a rally mode at just over \$5.40 per bushel

and rallied all the way to \$5.85 before retreating over the last 8-9 days of the month to around \$5.62. Initially, continuing concerns about the robust U.S. soybean export pace fueled the rally as traders became concerned about a very tight projected ending stocks number for this summer. The final surge in prices occurred because of a well-publicized case of BSE in Canada and traders speculation of what impact this might have on the demand for U.S. corn and soybean meal.

Corn price action for the December CBOT contract during the month of May was very similar to the action of the wheat contract. The contract started the month at about \$2.32, which was very near the low set in late March, and quickly rose to a high of \$2.53 by mid-month. As the end of the month arrives the contract has given back about half of the initial rally of 21 cents. Much of the price action in all three commodities during May was weather induced with the exception of the soybean export pace and the BSE case.

The current weather situation, especially for corn and soybeans, is a gamblers dream come true. Just when it looked like farmers would not get to plant all the corn and soybeans they wanted due to excess rain the weather changed and farmers made significant progress on both crops. However, it is too soon in the year for anyone to feel they have a very good idea about final actual crop size. Some of the crop is off to a great start, some is in need of sunshine, some still needs to be planted and some needs to be replanted. Currently all three crops look to be in much better condition than last season's crops. This is the factor providing the brakes to rally

attempts. However, U.S. and global supplies of corn and wheat are not large relative to recent use levels and U.S. soybean supplies are very tight compared to historic stocks/use ratios. If U.S. production of corn and soybeans are sub-par, prices should yet set new highs. The wheat situation is probably most dependent on global demand for U.S. produced wheat as the U.S. crop is about made. How does one market in this environment?

There is no perfect plan! It will only look obvious after it is too late. A prudent plan might include some percentage of grain contracted with some or all of the contracted quantity "covered" by the purchase of calls (a minimum price strategy for the quantity that is covered). It might also make some sense to purchase vertical call spreads to help reduce the up-front cost of the options. Of course, this would limit any gains to the net of the vertical spread minus the net cost of the options, i.e. the spread between the two calls minus the purchase price of the lower strike call plus the price received from the higher strike call which is sold. Perhaps it would make sense to use the straight call purchase plus contracts on a portion and the vertical call spreads plus contracts on another portion of sales.

If the market rallied to new highs the producer could consider additional coverage, beyond the comfort level of contracts, via the purchase of put options. The goal would be to insure a minimum price well above the loan rate level.

If the weather ultimately proves to be favorable for crop production it is highly probable that LDP payments will be available this

fall. If LDP payments occur farmers should consider how to protect their Counter Cyclical (CC) payments.

A somewhat more esoteric strategy for farmers to consider for soybeans would be to sell put options at strike prices that equal their respective county marketing assistance loan rates. At current "new-crop" bids and option premiums this strategy coupled with a contract sale provides a soybean price for Kentucky producers well above \$5.50. If the market continued to rally the farmer would not benefit unless additional actions were taken. If prices fell between now and delivery the farmer could lose money on the option they sold but they would also start to see LDP's if prices went below loan rates. The gains from the LDP's would not necessarily offset the loss from the option but the difference should not be large.

These are only a few of the possible marketing strategies farmers might consider. Weather will remain the key focus of the market for several more weeks. A reasonable marketing plan should outperform all but the luckiest individuals who insist on playing no limit poker.

Tobacco Grower Settlement/Buyout Update

Will Snell

An agreement has been reached to partially settle the class action anti-trust lawsuit brought about by U.S. tobacco growers against the major U.S. tobacco manufacturers and dealers. The lawsuit alleged that U.S. tobacco buyers colluded to fix auction prices and whose actions were intended to dismantle the

federal tobacco program. Lawyers from both sides met for months to discuss the issues and the potential for an out-of-court settlement. While not admitting any guilt to the alleged charges, all the major tobacco companies and dealers, with the exception of R.J. Reynolds Tobacco Company signed on to the agreement. On May 15, 2003 U.S. District Judge, William L. Osteen granted "preliminary approval" of the agreement with final approval expected in October. The total settlement is for \$211.8 million with \$200 million designated for U.S. tobacco growers and quota owners, \$5 million to lobby Congress for a buyout, \$3 million allocated to tobacco research and extension programs at land-grant universities, \$2 million to monitor purchase guarantees outlined in the agreement, and \$1.8 million for administrative costs associated with distribution of settlement funds. Attorney fees will be determined by Judge Osteen and will be in addition to the \$211.8 million settlement.

As part of the agreement, all U.S. burley and flue cured tobacco growers and quota owners during crop years 1996-2000 will be eligible for cash payments. According to the Washington D.C. law firm (HOWERY SIMON ARNOLD & WHITE) handling the agreement, a formal class notice, along with a claim form will be mailed to all tobacco growers and quota owners by June 20th. Notices will also be placed in various newspapers and a toll-free hot-line will be available to assist applicants. The deadline to make a claim is expected to be around mid October 2003, with payments delivered by a projected date of May 2004. Per pound payment levels and specific payment procedures are unknown at the

present time. Given that the average burley and flue quota during 1996-2000 was around 1.3 billion lbs, the average payment could be approximately 15 cents/lb based on one's average quota during this period (assuming 100% application rate). The payment rate will be adjusted if less than 100% of the pounds are applied for and these payments will be made irrespective to Phase II and potential buyout payments.

Within the agreement, Philip Morris, Brown and Williamson, and Lorillard agreed to a minimal purchase agreement of 405 million pounds annually for the next 10 years (or 12 years if a buyout occurs), subject to changes in overall cigarette production. Philip Morris' annual minimum commitment is 330 million pounds, with Brown and Williamson minimum level at 55 million pounds and Lorillard at 20 million pounds. As Table 1 on the following page indicates total U.S. burley and flue-cured purchases by the domestic manufacturers, including RJR have generally been in the 500 million to 1 billion pound range over the past decade. But actual purchases and intention levels have certainly exhibited a significant downward trend during the post Master Settlement Agreement (MSA) era. For 2003, burley and flue intentions totaled 468 million pounds, of which the manufacturers are required to buy 90% (assuming 100% of the quota is produced).

Keep in mind a couple of items in reviewing these data. First, this is a minimum purchase level for the major U.S. cigarette manufacturers, excluding RJR (which based on recent purchase behavior would not significantly change the total volume). Second, this minimum purchase level will

likely be adjusted downward as imported and deep discount cigarettes sold by the non-settling companies continue to erode the settling manufacturers' market share, along with expected further reductions in U.S. cigarette consumption and exports. In addition to the volume commitment, there is also a percentage domestic content commitment. Philip Morris agreed to a minimum domestic content level of 70% for flue-cured and 65% for burley, while Brown and Williamson and Lorillard agreed to a 35% level for U.S. tobacco. This domestic content level is applicable only to cigarettes produced AND consumed in the U.S. The anti-trust case against RJR continues with an April 2004 court date.

What about the buyout? Tobacco farm leadership continues to meet weekly in the "war room" to discuss legislative strategy and action. Right now the farm groups are targeting various members of the House Ag Committee to see if there is enough support to move the Fletcher bill. The Senate working group has been modifying their original proposal. This revised proposal will likely contain some means to maintain production rights in traditional areas, limit production, and may contain some mechanisms to protect growers from price risks. However, the Senate version will likely be less than the \$15 to \$19 billion bills that have been floated in the House. Presently, it appears that the Senate package could be around \$13 billion with 2002 being adopted as the base year.

An important question that is being discussed much within farm and health group circles is how the \$5 million designated in the grower settlement agreement will be utilized in lobbying Congress for a buyout. The agreement specifically states that

"Buyout legislation shall mean any act of Congress, signed into law, that compensates current or former domestic flue-cured and burley tobacco quota holders and/or domestic tobacco growers and eliminates the tobacco quota and price support provisions of the Federal Tobacco Program" (p. 5). According to the law firm handling the agreement, this does not preclude lobbying for buyout legislation that controls production and some sort of safety net on price.

Farm and health group interests are meeting regularly in Washington D.C. as a group in an organization called AHEAD (Alliance for Health and Agriculture Development) to discuss legislative strategy related to the buyout. Our next two meetings are scheduled for June 4th and June 24th in Washington D.C. Also, a farmer fly-in is tentatively being planned for July 14-16th in our nation's capital as grass root efforts to push for a buyout intensify.

Table 1. Tobacco Purchase Intentions vs. Actual Purchases

	Total Purchase Intentions: U.S. Flue and Burley (mil lbs)	Total Actual Purchases: US Flue and Burley (mil lbs)
1992	943	873
1993	834	717
1994	612	903
1995	955	1052
1996	900	1005
1997	1010	829
1998	876	843
1999	618	600
2000	529	607
2001	522	532
2002	537	*
2003	468	*

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