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Wageningen UR contributes fundamentally to the quality of life by a combination of research and education in the field of life sciences.

Design and economic impact of risk management tools for European agriculture

EU sixth framework project coordinated by Wageningen University

Income Stabilisation

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Outline

Income stabilisation

This project analyses the opportunities that risk management tools offer for stabilising farm incomes in the European Union in the contemporary context of new agricultural risks, an enlarged European Union, changing views about eligible forms of income support and disaster relief, and on-going developments at international risk management markets.

Three pillars

The project has three main components: a detailed analysis of farmers' risk exposure in the past and projected risks in the future; a review of risk management experience and farmers' perceptions of risk; and the design of viable risk management instruments, taking into account their economic impact and the policy options.

Scope of Income Stabilisation project

Risk	*Normal business risk & crisis risk*[1]
Farm types	*Specialised & mixed & large-scale & small-scale farms*
Commodities	*Crop & livestock*
EU regions	*Established & new member states*[2]
Risk management	*Private & public & public-private partnerships*

1. Subdivided into single farm and multiple farm crisis risk, and into "foreseeable" and unpredictable crisis risk
2. In-depth analyses focus on participating member states: the Netherlands, Germany, Spain, Poland, Hungary

Project outcomes

After drawing together and fine-tuning the project's results in a closing workshop with various stakeholders, the project will advise the Commission on potential risk management instruments for various farm types and regions throughout the European Union, making recommendations for the design and implementation of such instruments.

Coordination and information

The Income Stabilisation project is an EU sixth framework project that runs from April 2005 to April 2008. The project is coordinated by Prof. Dr Ruud Huirne, Wageningen University, Hollandseweg 1, 6706 KN Wageningen, the Netherlands.
See also www.incomestabilisation.org.

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Risk exposure

Past risk exposure: let farm data tell the story

This component of the project thoroughly analyses farm-level data from the Farm Accountancy Data Network (FADN) in order to provide insight into the volatility of farmers' risk exposure and into the chances of facing catastrophically low price, production or income levels.

Research objectives

- To provide insight into farm-level price, production and income distributions, including downside risk.
- To make a clear distinction between normal income fluctuations and income crises.
- To discuss the usefulness of FADN data for measuring farmers' income (crisis) risk.

Future risk exposure: what can we expect in the next ten years?

Since risks are constantly changing, data from the past generally tell only part of the story. This component of the project provides insight into the impact of future World Trade Organisation (WTO) and Common Agricultural Policy (CAP) policy scenarios on farmers' risk exposure and risk management opportunities.

Research objectives

- To define likely future CAP and WTO scenarios with their implications for price, production, farm income, and risk management strategies and permitted income stabilising tools.
- To analyse the impact of these scenarios on price, production and income probability distributions of farmers in the European Union.
- To analyse the impact of these scenarios on the chances of catastrophically low incomes.

Risk management experience and perception

Successes and failures in the international risk management arena

This component of the project reviews historical, current and developing risk management instruments, both within the European Union and in non-EU countries.

Research objectives

- To report on successful and unsuccessful risk management instruments.
- To analyse the major characteristics of these schemes (e.g. the risks covered and the underwriting criteria applied), and their performance and economic impact. Important performance issues are loss ratios and participation rates, while the relevant economic criteria are the degree of risk reduction achieved, the reported incentive issues for all parties involved, and the budgetary implications.
- Given the lessons learned, to identify the opportunities for viable (crisis) risk management in the European Union.

Risk and risk management perception: an investigation of farmers' beliefs

Risk analyses by scientists do not necessarily correspond to the perception of risks by farmers. Also, what may be perceived as theoretically promising risk management instruments may not work well for farmers. What is needed, then, is an in-depth analysis of farmers' perceptions of risk exposure, and (new) risk management instruments.

Research objectives

- To analyse farmers' perceptions of (crisis) risk and (crisis) risk management.
- To analyse farmers' perceptions of the (financial) role of various possible risk financing partners, ranging from their own role to that of national and European governments.

Viable risk management instruments

The economics of risk management instruments: farm-level and budgetary impact
Theoretically ideal concepts may not work well at the farm level, or may just be too costly. This component of the project models the economic impact of potential risk management instruments for the European Union, both at farm level and at the level of EU and national governments.

Research objectives

- To select promising risk management instruments, including purely private instruments, public-private partnership instruments and entirely public risk management instruments. For each instrument, it needs to be decided which part of the losses is borne by private partners and which, if any, by the public sector.
- To develop a whole-farm optimisation model and to analyse the economic impact of potential risk management instruments at farm level, including their impact on production decisions and on the level of (crisis) risk.
- To develop a risk financing simulation model and to analyse the budgetary impact of potential risk management instruments for governments, both at the national and the EU level.

The end product: viable risk management instruments for the European Union
The various themes of the project, i.e. risk exposure, risk management experience, risk perception and the economic impact of various schemes, are brought together in this final component of the project. Before drawing conclusions, a workshop is held to fine-tune the project findings in collaboration with various stakeholders (Warsaw, Spring 2008).

Research objectives

- To synthesise all previous project components in order to come up with policy options for (crisis) risk management that are feasible from a design and budgetary point of view, legitimate in CAP and WTO frameworks, and interesting for farmers. Design issues reflect aspects of rent-seeking behaviour, asymmetric information, data problems and transaction costs.
- To develop blueprints for the implementation of viable risk management instruments for EU agriculture, including recommendations for pilot tests.
- To discuss the possible impact of the instruments on the competitiveness of EU agriculture, production levels and market prices.