The Risk Transfer

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To fix or not to fix—that is the question

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Several seasons ago Agricola were the first underwriting agency to introduce a "Fixed" cotton hail insurance policy. Under this policy type, growers are required to lock-in their sum insured based on a fixed yield when they take out the policy. These policies have come to dominate the cotton crop hail insurance market place.

Until last season, the only alternative was the old Primacy "Revenue" policy. *Revenue* policies are great for the grower — I should know because I introduced them in the mid 1990's at GIO. However, it has now became clear they have a flaw — they are difficult to price properly. Hence, the *Fixed* policy has become more popular as it can be priced more competitively.

Better pricing comes at a cost to cotton growers — the cost is inflexibility. For dryland or semi-irrigated growers setting their sum insured based on a fixed yield at the beginning of the season is not a good idea.

Last season Rural Affinity introduced a *Hybrid* policy that maintains much of the pricing advantage of the Fixed policy but lets growers set an adjustable yield that operates in a similar way to the *Revenue* policy. If structured correctly, this offers the best of both worlds — pricing can still be determined accurately while growers are not locked into a sum insured based on a fixed yield set at the beginning of the season.

For this season, with many growers planning to plant dryland or semi-irrigated cotton crops, having an adjustable yield based sum insured will be more important than in previous seasons. So, to fix your yield or not becomes a very important question.

David Blackett

Structuring a Fixed or a Hybrid policy correctly—as anyone who has had a total loss claim will tell you—is not as easy as some insurance brokers make out. That's why Innovative Risk Trannsfer has enlisted agronomic expertise in the form of Cotton Growers Services Branch Managers. Together we can make sure the right growing costs are deducted from your claim if you have a total loss.

Special points of interest

Allianz Australia Insurance Limited has acquired 70% of the shares in Primacy Underwriting Agency Pty Ltd and 60% of the shares in Agricola Holdings Pty Ltd, the two largest cotton crop underwriting agencies —*this move could see competition reduce.*

Our strategic alliance with Cotton Growers Services and Rural Affinity from 2006 together with Allianz's move makes us the largest alternative cotton hail insurance supplier —*someone has to keep them honest.*

IRT with CGS give clients a full broking and consulting service including insurance placement, claims and risk management —*and isn't that the service you ought to be getting?*

End Point Royalty—How will your policy measure up?

...underwriting agencies are going to have to come to terms with adjustable growing costs

At the time of going to print we have not seen the various underwriting agency policy offerings for this season. How they deal with the End Point Royalty program will determine who has the better policy. As with fixing yields under the *Fixed* policy discussed in our first article, *Fixed* policies also force you to lock in your growing costs at the beginning of the season.

The adjustable nature of the End Point Royalty program means that the underwriting agencies are going to have to come to terms with adjustable growing costs. This is potentially difficult for them but beneficial for cotton growers if the agencies are able to amend their policies to cater for it.

Again, the *Revenue* policy deals with this adjustability but the price penalty still applies which is likely to see this product remain uncompetitive.

The End Point Royalty program gives underwriting agencies the opportunity to improve their policies by allowing their *Fixed* policies to be adjustable for a major growing cost and yield.

Cotton growers who choose the End Point Royalty program will benefit from their major input cost being proportionally linked to yield. For the smart underwriter, there is an opportunity to capitalise on the pricing opportunity this provides. If a major growing cost and yield are directly linked then some of the difficulties in pricing are avoided. This would mean they could provide the flexibility of the *Revenue* policy at the pricing of the *Fixed* policy — now that would be innovative risk transfer.

It remains to be seen how smart these guys are.

To see how your policy measures up, talk to your CGS Branch Manager or us when you are reviewing your quotes this season.

Water, water everywhere

With the water position for many growers changing by the week, the outlook for the 2010 cotton planting is constantly changing. Fortunately for us all, for the better — provided the fields dry out enough to plant.

How you price water under your cotton hail insurance policy and how your underwriting agency will deal with water if you have a claim is also an issue worth considering when arranging your cotton hail insurance policy.

Last season, one of our growers had to use extra water to re-plant cotton written off by loss adjusters. He was required to re-planted under the terms of the policy. This is the case with all policies for the time of loss but the policy did not operate as you would expect.

We negotiated a satisfactory outcome for our grower and have worked with insurers to fix the problem for this season.

You should check your policy to make sure you understand how you will be forced to use and who pays for extra water used — and how much insurers will pay you for the extra water.

And finally

For those of you with good memories, you will know that our last newsletter was in July 2003. We always intended this newsletter to be an occasional production but 7 years is a bit ridiculous. Now “I” have become “we”, we hope to be able to send you more regular issues — the team assure me I will.

Innovative Risk Transfer Pty Limited

ABN 33 093 837 631

Australian Financial Services Licence 252978

Suite 1.02, 460 Pacific Hwy,
CROWS NEST NSW

PO Box 310
BROADWAY NSW 2007

Enquiries
P: 02 9460 8791
F: 02 9009 0655
E: info@risktransfer.com.au

David Blackett
0417 235 634
david@risktransfer.com.au

Ingrid Argo
0438 615 740
ingrid@risktransfer.com.au

Andrew Ahern
0414 969 722
andrew@risktransfer.com.au
(Authorised Rep. No. 277680)

Sarah Padgett
02 9460 8791
sarah@risktransfer.com.au

COTTON GROWERS SERVICES PTY. LTD.

Authorised Representatives

CGS	292677
John Ash	294357
Alex Brooker	328677
Anne Coote	340339
Kerri Jocumsen	294356
Susie McCutcheon	328678
Pat McGuinness	332663
Carol Sanson	306257
Andrew Stewart	294358

Contact your nearest CGS Authorised Representative with your crop insurance enquiries or contact us direct.