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Executive Summary

September 25, 2017

INSTITUTION: University of Georgia

PROJECT TITLE: US Peanut Producers: A Multi-Economic Analysis of Their Competitive
Position in the Domestic and Global Markets

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EXECUTIVE SUMMARY: When the U.S. peanut program was significantly changed in the 2002 Farm Bill, there were components of the old quota program that were carried over into the new peanut program while other parts were not. The definitions for Segregation 1, Segregation 2 and Segregation 3 for farmer stock peanuts were not changed. However, what farmer stock peanuts could be used in the domestic edible channel was changed. Under the old quota peanut program, any farmer stock peanut that was graded a segregation 2 or 3 had to be crushed. This was based on value and not actually tonnage. Under the new peanut program, this criterion was eliminated and only the outgoing criterion is utilized. For example, if a farmer delivers a ton of peanuts that were graded Segregation 2, the sheller has the opportunity to potentially clean them up to meet the outgoing specifications for edible sale. For farmer stock peanuts, the main criterion for Segregation 2 was that the percent damage had to exceed 2.49%. Until recently, the outgoing specification was also the 2.49% damage threshold. Shellers requested through the Peanut Standards Board that the outgoing specification for maximum allowable damage in a lot to be increased to 3.49%. The Peanut Standards Board approved the request and was accepted by the Secretary of Agriculture.

Another feature of the peanut program that was not changed was the loan value for Segregation 2 peanuts. Under the old quota peanut program, Segregation 2 and 3 peanuts in the CCC loan had to be crushed and be no-net cost to the U.S. government. Since crushed peanut value was low due to volume and based on historical prices, the loan value for Segregation 2 peanuts was set very low. It had ranged in the \$120-\$130 per ton range under the previous quota program. Under the current peanut program, the loan value for a Segregation 2 peanut is \$124.08 per ton. Basically, there has been no change in the loan value of Segregation 2 peanuts.

The National Center for Peanut Competitiveness (NCPC) analyzed the situation for Segregation 2 peanuts. NCPC met with the State Peanut Supervisors in charge of grading farmer stock peanuts at their post-harvest grading meeting in Albany, Georgia. They were willing to assist the NCPC in assembling the data required for analysis. Due to detailed data requirements and manpower, only Alabama and Georgia were able to provide the required data. From 2002-2015, Alabama and Georgia graded between 58% to 70% of all peanuts graded in the U.S. Concerns were expressed by individuals that any changes in defining the threshold for a Segregation 2 peanut (i.e., increased damage level from 2.49% to 3.49%) would alter the current

loan differentials. NCPA spent time with Mr. Ben Smith who was de facto the sheller's point person in regards to loan differentials and the peanut industry's loan differential guru. After a thorough discussion with Mr. Smith, it was determined that any modifications to the criterion for Segregation 2 peanuts would not impact the existing loan differential calculations. From the U.S. perspective for the crop years 2002 to 2015, Segregation 2 peanuts constitute normally less than 1% of the entire crop. However, in the last couple of years, the share has increased. Of course the peanut growers have experienced some very challenging weather conditions in recent years.

Individual grade records for the crop years 2013-2015 for Alabama and Georgia (FV-95s without any identity factors for confidentiality) were provided which resulted in several hundred thousand sets of records. The records were sorted into several classifications. First, the records were sorted as to Segregation 1 or 2 or 3. Within Segregation 1, the records were subdivided into 2 damage levels: 0.00% to 1.49% and 1.5% to 2.49%. The reason is that there is a damage deduct for Segregation 1 peanuts with a damage level of 1.5% to 2.49%. Segregation 2 peanuts were subdivided into 5 subcategories (2.50-2.99%, 3.00-3.49%, 3.50-3.99%, 4.00-4.49%, and >4.49%). There were no subdivisions for Segregation 3 peanuts. Tonnage by classification is reported as well as to share within the Segregation and share for total production graded. All weighted grade factors were calculated by taking the individual grade factor for that record and weighted by the net tonnage for that record. The methodology used to calculate value per ton for that load of peanuts was utilized (i.e., as used to create the FSA-1007 form). Just as it is done in creating the current FSA-1007 form for Segregation 2 peanuts, the peanut damage deduct of \$3.40 is used in the calculation of the weighted per ton value for the sub classifications of Segregation 2 peanuts. While the weighted per ton value for the Segregation 2 peanuts can be significantly above the loan rate of \$124.08, the peanut farmer will only receive the loan rate which is significantly below their variable cost of production.

A farmer having their entire crop graded to be Segregation 2 is an economic devastation which could lead to bankruptcy while the true value seems to be significantly higher. Based on the tonnage of the peanut crop, potential value and current use of Segregation 2 peanuts in the edible market (after being cleaned up), a re-examination of what constitutes a Segregation 2 peanut and the associated loan value would be prudent. Based on this research, the peanut grower leadership requested to the Peanut Standards Board that the threshold for Segregation 2 peanuts be increased to 3.49% which the Peanut Standards Board approved and is awaiting the Secretary of Agriculture's approval.

Another key area of research dealt with the peanut warehousing capacity. Given that cotton does not have a commodity program and only relied on crop insurance for its safety net, the extremely low cotton prices coupled with the other commodities' low prices has forced Southern farmers to look towards peanuts as the safety net for their farming operations. These factors lead to an increased 2015 peanut production which created an expected excess supply of peanut for 2016. According to USDA-ERS, national peanuts stocks were expected to be close to 1.44 million tons by August 1, 2016. This would be a historically high compared to 2015 (1.05) and 2014 (0.93). Similarly, the 2015 U.S. peanut acreage estimate (1.625 million acres) was approximately 20 percent higher than the 2014 U.S. peanut acreage. This percentage increase translated into nearly 250,000 additional acres. The supply situation coupled with expected low prices for alternative competitive crops has been a concern for the peanut industry as it relates to needed storage capacity. Without adequate storage

capacity, many peanut producers may not be able to store their peanuts in a federal license warehouse and participate in the marketing loan program. Based on USDA forecasted beginning inventory for the 2016 peanut crop coupled with the expected production, research was directed to determine if adequate storage facilities would be available. The research indicated that there was the potential of a severe shortage of federal license warehouses. The research findings were disseminated out to the Southeast peanut producers. In response to the research findings, the Southeast cut their peanut acreage by approximately 11% from their 2014 peanut acreage level.