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Marketing Alternatives for Producers of Wheat and Other Grains: A Workbook

Cooperative Extension, South Dakota State University

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Marketing Alternatives for Producers of Wheat and Other Grains

A Workbook

Cooperative Extension Service    South Dakota State University
U. S. Department of Agriculture
This Workbook is designed as a follow up to the lecture program on Marketing Alternatives for Producers of Wheat and Other Grains.* With a lecture of two to four hours as a prerequisite, completion of the Workbook can be accomplished in two hours.

The Workbook is not designed necessarily to test what one has learned from the lecture, but rather it is suggested as a continuation of the learning process with the participants having access to the answers as they please. The challenge should be offered to have the participants attempt to work out the answers, then check for correctness and discuss the reasons for the recommended answers.

All of the problems are either actual trading results of producers, or they are illustrations designed with actual prices used to describe a situation. It is important to indicate that all of the trading examples either did or could have happened as described. Current prices and local situations should be used whenever possible.

MARKETING ALTERNATIVES FOR PRODUCERS OF WHEAT AND OTHER GRAINS

Prepared by

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Published by

South Dakota Extension Service
Understanding Grain Futures
Workbook

1. What is meant by localizing a grain futures price?

2. Why is localizing futures prices important?

3. a. If the Chicago July futures price for a grain is $4.50, and the freight and other costs to this local elevator on a given day for that particular grain are 25¢ a bushel - what is the local elevator's July basis for that grain __________.
   b. If the local elevator in the above example usually charges the producer 10¢ a bushel margin, what is the producer's basis? __________

4. Define basis in your own words.

5. The basis is usually (greater) or (smaller) at harvest time? (Underline correct answer)

6. Hedging in futures is to take an __________ and __________ position from your cash price position.

7. When forward pricing a grain for a pre-harvest sale you would first (sell) or (buy) the futures.

8. When making a basis storage hedge, you would first (buy) or (sell) the futures.
9. What is your market position if you sell a unit of July wheat, and buy a unit of September wheat in the same market?

10. Which of the following grains can be traded in futures markets of the United States?

- Wheat
- Corn
- Soy Beans
- Flaxseed
- Barley
- Oats
- Sorghum
- Rye
- Rapeseed
- Rice

11. The primary new crop futures trading month for

- Corn = ________________
- Soybeans = ________________
- Oats = ________________
- Spring Wheat Minneapolis = ________________
- Winter Wheat Kansas City = ________________
- Soft Red Wheat Chicago = ________________

12. What does it mean when a futures price is quoted over the radio as up 6 to down 2?

13. a. From the actual 1973-74 Corn Crop year the local elevator price for corn on November 1, 1973 was $2.04 and the Chicago July Future was $2.47. What was the local July basis on November 1? ________________

b. A record of Sioux City cash prices and Chicago Futures prices for corn for the 1972-73 crop is as follows: What is the Sioux City basis for each day listed?
<table>
<thead>
<tr>
<th>Month</th>
<th>Nov 1</th>
<th>Nov 15</th>
<th>Dec 1</th>
<th>Dec 15</th>
<th>Jan 1</th>
<th>Jan 15</th>
<th>Feb 1</th>
<th>Feb 15</th>
<th>March 1</th>
<th>March 15</th>
</tr>
</thead>
<tbody>
<tr>
<td>Price</td>
<td>1.20</td>
<td>1.23</td>
<td>1.33</td>
<td>1.44</td>
<td>1.38</td>
<td>1.41</td>
<td>1.39</td>
<td>1.38</td>
<td>1.44</td>
<td>1.41</td>
</tr>
<tr>
<td>Future</td>
<td>1.47</td>
<td>1.47</td>
<td>1.52</td>
<td>1.55</td>
<td>1.51</td>
<td>1.41</td>
<td>1.44</td>
<td>1.41</td>
<td>1.44</td>
<td>1.41</td>
</tr>
</tbody>
</table>

c. From the above figures fill in the following T account, for a basis hedge.

<table>
<thead>
<tr>
<th>Cash</th>
<th>Futures</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nov 1 Value of cash corn</td>
<td>Nov 1 Sold 1 unit Chicago July futures @</td>
</tr>
<tr>
<td>Jan 15 Sold cash corn @</td>
<td>Jan 15 Bought 1 unit of Chicago July Corn @</td>
</tr>
<tr>
<td>Gain-loss</td>
<td>Gain-loss</td>
</tr>
</tbody>
</table>

Total Value of Corn Jan 15

d. What would be the result if the corn were stored with no hedge from November 1 to January 15 - gain ________ or loss ________

e. Total gross return with the hedge was ________ more, less, than with no hedge.

f. What action did the cash and future price take in the above example to narrow the basis?

14. a. The actual cash and futures price relationships for Minneapolis cash wheat and Minneapolis September wheat futures are listed below. What is the Minneapolis basis for each date?

Note: To arrive at the producer's basis in the following problem, the elevator's margin must be added to the hometown basis.
<table>
<thead>
<tr>
<th></th>
<th>Mpls. Cash 13 Pro HRS Wheat</th>
<th>Mpls. Sept Futures</th>
<th>Mpls. Basis</th>
<th>Hometown Rail Basis</th>
<th>Hometown Truck Basis</th>
</tr>
</thead>
<tbody>
<tr>
<td>Aug 15</td>
<td>1.87</td>
<td>1.85</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sept 1</td>
<td>1.88</td>
<td>1.83</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1971</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Aug 15</td>
<td>1.52</td>
<td>1.55</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sept 1</td>
<td>1.54</td>
<td>1.54</td>
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<tr>
<td>1972</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Aug 15</td>
<td>1.74</td>
<td>1.79</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sept 1</td>
<td>1.92</td>
<td>1.95</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1973</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Aug 15</td>
<td>4.57</td>
<td>4.73</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sept 1</td>
<td>4.43</td>
<td>4.43</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1974</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Aug 19</td>
<td>4.67</td>
<td>4.71</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sept 1</td>
<td>4.65</td>
<td>4.70</td>
<td></td>
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</tr>
</tbody>
</table>

b. If the rail freight from hometown to Minneapolis was 13¢ a bushel in 1970 and 71, 15¢ a bushel in 1972, 18¢ a bushel in 1973, and 20¢ in 1974, what is the hometown elevator rail basis for each date given in the above table? (This method of determining hometown basis is acceptable for developing history when local prices are not available. However, whenever possible, actual hometown prices should be used to determine local basis.)

c. If in 1972 and 1973 there were no rail cars available and truck wheat was discounted 20¢ a bushel. The trucks were charging the same as rail freight. What was the hometown truck basis in those years?

d. On March 1, 1974 Minneapolis September Wheat traded at about $5.45 and December wheat traded at about $5.46. The prospects looked good for the end of the box car shortage, and it was assumed the local elevator would have a margin of 10¢ a bushel for handling wheat. What could the producer at hometown reasonably expect for his wheat at harvest, if he sold Mpls Dec (December wheat used to offer longer time to complete delivery of grain) wheat futures on March 1?

15. A farmer, who needed to purchase some additional oats for feed for use later in the year, had no storage available on his farm. Because of a firm conviction that oats would go up, on July 13, 1973 he bought a unit of Chicago March oats at $1.08. On July 13 he could have purchased cash oats from his local elevator for 82¢ a bushel. The elevator would store oats for 2¢ a bushel per month. On January 15 the farmer had emptied his bin and was ready to take delivery of additional oats. He then bought cash oats from his local elevator for $1.41 per bushel. On that same day he sold his March oats futures for $1.56. What did his cash oats actually cost him? (See next page for worksheet.)
<table>
<thead>
<tr>
<th>Date</th>
<th>Event Description</th>
<th>Date</th>
<th>Event Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>7/15/73</td>
<td>Present value of cash oats for purchase</td>
<td>7/15/73</td>
<td>Bought 5000 bu. Chicago March oats @ 100</td>
</tr>
<tr>
<td>1/15/74</td>
<td>Bought feed oats @ 150</td>
<td>1/15/74</td>
<td>Sold 5000 bu. Chicago March oats @ 150</td>
</tr>
</tbody>
</table>

Oats cost increase-decrease from 7/15

Gross Price for Oats

Cost for placing and closing the hedge @ 9%

Interest cost @ 9% (assuming $900 Margin and $30 Commission)

What would have been the cost per bushel if the farmer had bought 5000 bu. of cash oats July 15 and stored them in the elevator until Jan 15-74

Cost of oats
Storage per bu - 6 mo.
Total
Plus Interest cost @ 9%
(Storage rate 2 cents per bu per mo)

16. a. Where there are alternative crops that can be grown, compare the futures prices anytime ahead of seed buying or soil preparation time and see how they compare. Consider corn and soybeans as alternative crops on a randomly picked date of March 4, 1974. New crop (Dec) corn futures traded at about $2.98 and new crop (Nov) soybeans traded at about $6.26. If the recent harvest time basis for corn in your area has been 38 under, and your recent harvest time soybean basis has been 50 under at harvest; what could you expect for a harvest time cash price for corn ___________, for soybeans ___________ on the basis of the current futures price?

b. If your normal yield of corn is 80 bushels per acre and the normal yield of soybeans is 30 bushel per acre, how many gross dollars per acre would this mean for corn ___________, soybeans ___________?

c. If it cost $60 per acre to grow and harvest corn, and $45 per acre to grow soybeans, which crop would be the most profitable to plant ___________, and by how many dollars per acre ___________?
Your crop yield and production costs

<table>
<thead>
<tr>
<th>CROP YIELD &amp;</th>
<th>Production Costs</th>
<th>Crop 1</th>
<th>Crop 2</th>
<th>Crop 3</th>
<th>Crop 4</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Projected yield per a.</td>
<td></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>DIRECT COSTS Per acre</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2. Seed</td>
<td></td>
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<tr>
<td>3. Fertilizer</td>
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<tr>
<td>4. Pesticides - Ag Chemicals</td>
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<tr>
<td>5. Machinery repairs</td>
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<tr>
<td>6. Fuel &amp; lubricants</td>
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<tr>
<td>7. Interest</td>
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<td>8. Crop insurance</td>
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<tr>
<td>9. Overhead</td>
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<tr>
<td>10. TOTAL DIRECT COST</td>
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<tr>
<td>FIXED COSTS: Per acre</td>
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</tr>
<tr>
<td>11. Machinery deprec.</td>
<td></td>
<td></td>
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</tr>
<tr>
<td>12. Machinery interest</td>
<td></td>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>13. Labor</td>
<td></td>
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<tr>
<td>14. Land charge</td>
<td></td>
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<tr>
<td>15. TOTAL FIXED COSTS</td>
<td></td>
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<td></td>
<td></td>
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<tr>
<td>16. TOTAL COSTS/ACRE</td>
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<td></td>
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<td></td>
</tr>
<tr>
<td>17. COSTS PER BUSHEL</td>
<td></td>
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</tr>
</tbody>
</table>

17. Why is the cost of storing grain an important consideration when hedging grain?

18. a. It is not uncommon when a producer wants to sell grain far in advance of delivery. The buyer will say that he will protect him on the basis. What kind of price protection does the producer have if he is protected on the basis? (answer b and c before a)
b. If you make an agreement to be protected on the basis for your corn as of Oct 1 when your local cash price is $3.00 and the Chicago July future is $3.48 ( Basis?) and you want to sell your corn May 1 the following year when your local cash price is still $3.00 and the Chicago July future was $3.27 ( Basis) What would you get for your corn if you were protected on the July basis as of Oct 1?

c. If you make an agreement to protect the basis on your wheat as of May 1, when your local cash price for new wheat is $4.37 and the September future for your market is $4.57 ( Basis?) and you deliver the wheat September 4 future when the cash price is $4.35 and the September future is $4.64 ( Basis). What would you actually get for wheat if you were protected on the September basis as of May 1?

19. How many ways can you think of for the "basis" to narrow?

EXAMPLE

1. The cash price goes up 4. while the futures price does down

      3

2. 5.

3. 6.
20. Can you deduct a futures trade loss from your income tax?  
   yes ___, no ____  
   Explain; 

21. Futures trade gains are taxed as net income. yes ___, no ____  
   Explain; 

22. What does a commission fee of $35 round term mean?
23. A stop loss order will always protect a futures trader from excessive losses. yes ___, no ___
   Explain;

24. a. Why will a processor buy a grain future while a producer is selling the same future?

   b. Why will one trader buy while another one is selling the same future?
Answers:

Understanding Grain Futures

1. Localizing futures is to estimate from the past market actions and to assess any expected changes as a result of current conditions into what a grain futures price means to you in cash price at a given time. For example, if your local cash wheat price was 30¢ under the Minneapolis September future on August 15 in 1970, 32¢ under in 1972, and 34¢ under in 1973, you would probably expect the cash to be 36¢ under the September future in 1974. Some of the additional basis is caused by freight increases and some is caused by an increase in handling margins.

Aug. 15 - Mpls Sept. Wheat $4.29
expected basis .36 under
Expected cash price if $3.93
futures are used to forward price grain.

2. Localizing futures prices is important, because if prices are not localized, you would not know what kind of cash price you were "locking in" if you trade in futures.

3. a. This question was not meant to be tricky, however many people give the local cash price instead of the basis. The basis is very simply 25 under
b. Producer basis 25 + 10 = 35 under

4. Basis is the spread between the futures price considered, and the cash price at a location. Thus, there may be a basis for every grain traded in the futures, for every trading month, and for every grain buying location in the country.

5. Greater - the basis usually widens at harvest time, and then narrows after harvest.

6. Hedging in futures is to take an equal and opposite position from your cash grain position.

7. Sell. If you bought first you would be long cash and futures both.

8. Sell. In order to take an equal and opposite position.

9. You would be short a unit of July wheat, and long a unit of September wheat. You would have a position in both contracts which would both have to be offset.

10. Wheat, corn, soybeans, oats, and sorghum. Barley, rye, flax, and rapeseed are traded on the Winnipeg futures market.

11. The primary new crop futures trading months for various grains are:
Corn - December
Soybeans - November
Oats - July, perhaps Sept. in the north
Spring wheat - September (Minneapolis)
Winter Wheat - July (Kansas City)
Soft Red Wheat - July (Chicago)
12. The current future is quoted first, thus the current futures were called up 6 and the deferred futures called down 2.

13. a. **July Basis Nov. 1 = 43 under**
   
   **Date:**
   
   **July Basis**
   
   - Nov. 1 27 $3/4$ under
   - Dec. 1 19 7/8 under
   - Jan. 1 13 7/8 under
   - Feb. 1 5 3/8 under
   - Mar. 1 16 under
   
   b. **Nov. 1**
   
   - 15 24 1/8 under
   - 15 11 under
   - 15 00 1/2 under
   - 15 7 1/2 under
   
   c. **Cash Futures**
   
<table>
<thead>
<tr>
<th>Nov. 1 Value of cash corn</th>
<th>Nov. 1 Sold Chicago July Future @ $1.47 3/4</th>
</tr>
</thead>
<tbody>
<tr>
<td>Jan. 1 sold cash corn @ $1.41</td>
<td>Jan. 15 Bought Chicago July Future @ $1.41 1/2</td>
</tr>
<tr>
<td>cents per bu. Gain .21</td>
<td>cents per bu. Gain .06 1/4</td>
</tr>
</tbody>
</table>
   
   **Total value of corn Jan. 15 $1.41 + .06 1/4 = $1.47 1/4**

   d. Cash price gain of 21¢ per bushel.

   e. 6 1/4 more gain by using a basis hedge, plus protection against a price decline.

   f. The cash went up while the futures declined.

14.

<table>
<thead>
<tr>
<th>Date</th>
<th>a. Minneapolis basis</th>
<th>b. Hometown basis</th>
</tr>
</thead>
<tbody>
<tr>
<td>1970</td>
<td>Aug. 15 2 over</td>
<td>11 under</td>
</tr>
<tr>
<td></td>
<td>Sept. 1 5 over</td>
<td>8 under</td>
</tr>
<tr>
<td>1971</td>
<td>Aug. 15 3 under</td>
<td>16 under</td>
</tr>
<tr>
<td></td>
<td>Sept. 1 0</td>
<td>13 under</td>
</tr>
<tr>
<td>1972</td>
<td>Aug. 15 5 under</td>
<td>20 under</td>
</tr>
<tr>
<td></td>
<td>Sept. 1 3 under</td>
<td>18 under</td>
</tr>
<tr>
<td>1973</td>
<td>Aug. 15 16 under</td>
<td>34 under</td>
</tr>
<tr>
<td></td>
<td>Sept. 1 0</td>
<td>18 under</td>
</tr>
<tr>
<td>1974</td>
<td>Aug. 15 4 under</td>
<td>24 under</td>
</tr>
<tr>
<td></td>
<td>Sept. 1 5 under</td>
<td>25 under</td>
</tr>
</tbody>
</table>

   c. **Rail Basis Truck Basis**

   | 1972 | Aug. 1 20 under      | 40 under          |
   |      | Sept. 1 18 under     | 38 under          |
   | 1973 | Aug. 1 34 under      | 54 under          |
   |      | Sept. 1 18 under     | 38 under          |

   each basis increases by 20¢ when a 20 cent truck discount is effected and no rail alternative is available.
The expected basis is derived from answer 14. b the hometown basis. The basis has been increasing and another raise in transportation costs is expected, therefore if the basis was about 25 under last year, it seems reasonable that the basis would be about 27 under the coming harvest time. If the basis was less than estimated the cash price for wheat would be greater where the future was sold to establish a price.

15. a.

<table>
<thead>
<tr>
<th>Cash</th>
<th>Futures</th>
</tr>
</thead>
<tbody>
<tr>
<td>July 15-73 Value of Cash oats for purchase $ .82</td>
<td>July 15 Bought 5000 bu. Chicago oats for purchase $1.08</td>
</tr>
<tr>
<td>Jan. 15-74 Bought cash feed oats $1.41</td>
<td>July 15 Sold 5000 bu. Chicago oats for purchase $1.56</td>
</tr>
</tbody>
</table>

Oats cost: increase $ .59 Gain $ .48

Gross Price paid for oats is $1.41 elevator price - .48 cents a bushel futures gain = $ .93 per bushel.

Cost for placing and closing futures trade $30 for 5000 bu. .60 of a cent or slightly more than ½ cent a bushel for cost of commission.

Interest cost 7/15/73 to 1/15/74 for $900 margin @ 9% interest = $40.50 or .81 of a cent per bushel.

The Total cost of commission and interest would be less than 1½ cents per bushel (.60 of a cent + .81 of a cent = 1.41 cents per bushel)

b. Cost of oats = $ .82 x 5000 bu. = $4100.00
   Storage 6 mo = 12¢ per bu. x 5000 bu. = $600.00
   Int - 6 mo @ 9% x $4100 = 184.50
   Total cost of oats = $4884.50

$4884.50 ÷ 5000 bu. = 97.69 cents per bushel

16. a. Corn
   $2.98 future price
   .38 under (expected basis)
   $2.60 Expected price for corn

   b. Corn
   $2.60
   x .80 - bu. per acre - .30
   $208.00 - Gross per acre -172.80
   c. -60.00 - cost per acre - 45.00
   corn
   $ 148.00 - Net return/acre 127.80
   corn most profitable by $20.20 per acre
17. Because the cost of storing grain including shrink, insurance, interest and risk must be deducted from any expected gains in price. Another way of saying it is that the expected price rise from storing grain must exceed the total cost of storage to be profitable.

18. a. The producer has no real price protection at all, he is only assured of selling his cash grain at a pre-determined difference (basis) between a grain futures and his local price. Judgment must be made as to when to use this strategy and when not to. A guide for using this technique is to not protect the basis when it is historically wide, but to accept use of the technique if the basis is historically narrow. One should remember the basis on most grains usually narrows after harvest time. This method of pricing can save a producer storage, shrink, interest and other costs associated with storing grain if it is used properly.

b. This is an example of a situation where protecting the basis will probably not be successful because it is done at harvest time, a time of historically wide basis.

\[
\begin{align*}
\text{July Basis Oct. 1} & : 48 \text{ under} \\
\text{July Basis May 1} & : 27 \text{ under}
\end{align*}
\]

Actual price for corn May 1, priced on Oct. 1

\[
\begin{align*}
\text{July Basis} & : \text{Actual Price for Grain} \\
\text{July Basis Oct. 1} & : \text{July corn future May 1 3.27} \\
\text{July Basis May 1} & : 0.48
\end{align*}
\]

May 1 price for corn based on historical relationship =

\[
\begin{align*}
\text{July corn future May 1} & : 3.27 \\
\text{July Basis - May 1} & : 0.27 \text{ under}
\end{align*}
\]

Approximate May 1 price $3.00

c. September Wheat basis May 1 - 20 under

\[
\begin{align*}
\text{September Wheat basis Sept 4} & : 29 \text{ under}
\end{align*}
\]

Actual price for Wheat Sept 4 priced on May 1

\[
\begin{align*}
\text{September wheat future Sept 4} & : 4.64 \\
\text{September basis - May 1} & : 20 \text{ under}
\end{align*}
\]

Price of Grain September 4 priced on days basis

\[
\begin{align*}
\text{September wheat future} & : 4.64 \\
\text{Basis September 4} & : 29 \text{ under}
\end{align*}
\]

September cash price $4.35 for wheat

19. 1. Cash price may go up while futures go down
2. Cash price may remain constant while futures go down
3. Cash prices may go down slowly while futures go down rapidly
4. Cash price may go up rapidly while futures go up slowly
5. Cash price may go up while futures remain constant
20. Answer: Yes and No
   a. Yes. A futures trade loss can be deducted from income tax
      if it is a proven legitimate hedge.
   b. No. Gambling losses in futures are not deductible except
      as deducted from futures gains in the same year. If you
      have only futures losses in a year, they are not deductible
      except as $1000 per year, any balance can however be carried
      into the next year if the total loss is entered.

21. Commodity futures -- like securities -- are capital assets.
    So the capital gain and loss rules apply. Holding a contract
    longer than six months means getting favorable long-term tax
    treatment.

    Wash sales: When a securities investor sells stock at a loss
    and replaces it within 30 days with more of the same, that's
    a wash sale. And the tax law won't let him deduct the capital
    loss. But for commodity trading, it's a different story.
    There's --

    NO WASH-SALE RULE. An investor can take his loss in a
    particular commodity, buy more of the same commodity moments
    later and still get a capital loss deduction on the sale.

22. Commission fee of $35 for round term means the total commission
    for the in and out, or for the original futures contract and
    the offsetting contract.

23. Stop loss orders are not a cure-all for limiting losses in
    futures trading. They can be a help in many cases if one
    realizes the shortcomings of a stop loss and does not depend
    on it to unfailingly protect a price. For example:
    1. A stop loss placed incorrectly could put one out of
       the market even while the market trend was in the
       expected direction.
    2. If the market goes by your stop loss order, the order
       then becomes a market order and as a result one may get sold
       out at a figure quite far removed from the stop loss
       figure.
    3. Stop loss orders can be used to protect profits or
       to limit losses.

24. a. A processor may be buying futures so as to establish a
    price now for his finished product several months later.
    The processor probably didn't have the room to store the
    cash grain, or buying the futures may be cheaper than
    buying and storing cash grain. The processor may not be
    greatly concerned about whether the price was going up
    or down. The producer may be selling either to lock in
    a price, or a basis for storage return, or disposing of
    a risk he doesn't choose to carry. This is usually done
    on his part with the assumption price will go down.
b. Two traders who are speculating in futures may take opposite positions in the market based on how they interpret the news that is before them. This may be because of the different interpretation of the same news, or because one has some different news than the others.
MARKETING ALTERNATIVES

True or False Learning Quiz

T  F
1. (   ) (   ) Every producer or elevator manager should understand grain futures.

2. (   ) (   ) Every producer or elevator manager should trade in futures.

3. (   ) (   ) Nearly every local cash grain price has a relationship to a grain futures.

"Basis" in grain terminology can be described as:

4. (   ) (   ) The inflexible difference between cash and futures prices.

5. (   ) (   ) The futures price localized to a specific locality.

6. (   ) (   ) The varying spread between cash and futures prices.

7. (   ) (   ) Basis is a market price with marketing costs subtracted.

8. (   ) (   ) There are three major wheat futures markets in the United States.

9. (   ) (   ) There is little reason to learn about futures if you do not plan to trade in them.

10. (   ) (   ) Most people deliver the cash grain to offset a futures trade.

11. (   ) (   ) You must always buy some futures before you can sell them.

12. (   ) (   ) Hedging will protect a price - nothing more.

13. (   ) (   ) If you are properly hedged you don't care if the cash price goes up or down.

14. (   ) (   ) Transportation is usually the largest part of "Basis".

15. (   ) (   ) Margin and commission for futures trading are the same thing.

16. (   ) (   ) When selling wheat futures to forward price your wheat crop, you should sell in the highest market - Chicago, Kansas City or Minneapolis.

17. (   ) (   ) To offset the purchase of 5000 bu. of Kansas City July Wheat, you need only to sell 5000 bushel of Kansas City September Wheat.
18. ( ) ( ) Futures prices are practically the only way you can price your grain for future delivery.

19. ( ) ( ) You can at anytime shift the price risk from cash grain to futures without incurring additional risk.

20. ( ) ( ) You can usually even up your position in the futures within a fraction of a cent of the current price any day trading is open.

21. ( ) ( ) Hedging will limit windfall profits.

22. ( ) ( ) You should never hedge if you expect the cash price to go up.

23. ( ) ( ) If your assessment of the market direction is correct you will get all the margin money back.

24. ( ) ( ) An inverse carrying charge in the futures is when deferred crop futures are lower than current futures of the same crop.

25. ( ) ( ) An inverse carrying charge usually suggests cash grain should be sold, not stored.

Multiple Choice

Which of the following functions could a hedge perform?

( ) (a) Protect against a price drop
( ) (b) Earn a payment for storage
( ) (c) Establish a selling price into another year
( ) (d) Help take advantage of higher spot market
( ) (e) Be an important price tool during transportation shortages

Understanding grain futures could benefit one in which of the following situations?

( ) (a) Assessing new crop prices
( ) (b) Assessing one grain price in relationship to another
( ) (c) Determining what crop to plant
( ) (d) Determining whether to sell or store grain
( ) (e) Determining when to sell cash grain
MARKETING ALTERNATIVES
True - False - Answers

1. True Everyone interested in grain marketing should be interested in understanding futures because of the relationship to cash grain prices.

2. False Many people do not have the mental attitude nor the understanding of futures to be a trader.

3. True Even a "feeder market price" has some relationship to grain futures because of the substitution possibilities as to what grain you feed or where you buy your grain.

4. False Basis is a changing difference between cash and future prices.

5. True Local basis is a futures price localized, or it is placing a local cash price to a futures price.


7. False A little confusing - but basis is the difference between cash and futures prices and is not a price in itself.

8. True Chicago, Kansas City and Minneapolis.

9. False The more one can learn about grain futures the more one can apply that knowledge to his cash price judgments and decisions.

10. False Less than 2% of futures contracts have the actual cash grain delivered on them - offsetting contracts settle most futures contracts.

11. False You may of course sell first and buy later.

12. False A hedge may also prove profitable because of basis change.

13. True When you are properly hedged in a basis hedge, your profits will come from the action of the basis, not whether the price goes up or down.

14. True Other elements determining basis are - demand for storage, cost of interest, risk, etc.

15. False Margin is the earnest money used to insure performance - commission is the charge for doing the mechanics and bookwork of trading.

16. False You should trade in the market most representative of your market and your kind of grain. For the very experienced trader, "spreads" between markets could be used.
17. False  You must sell 5000 bu. of Kansas City July wheat to offset the purchase of 5000 bu. of Kansas City July wheat. In the case stated in question 17, you would have a position in two contracts.

18. False  You can contract cash grain without the use of futures. Cash contracts are used much more often than pricing through futures at the country level.

19. False  The question is a little tricky because you can shift the risk from cash to futures sometimes at no additional risk, but not anytime. Exchanging a long cash position for a long futures position during a wide basis incurs more risk.

20. True  You can usually, but not always make a trade within a narrow range of current price. When the market is making limit moves one may not be able to trade at all.

21. True  A hedged position will definitely limit windfall profits; the purpose of a hedge is to minimize risk or to profit from a basis change.

22. True and False  This statement is basically true; one should not expect to profit from a hedge, if he assumes the cash price will go up more than the basis will narrow. One may, however, hedge even if he expects the price to go up, if he cannot afford the risk of a possible price decrease.

23. True  Margin money is all returned on a proper assessment of the market.

24. True  Such as a situation where December wheat is $5.00, March $4.90, and May $4.85.

25. True  An inverse carrying charge indicates there is a greater demand for that grain currently than is expected in the future. Conditions can change again making storage of grain appear profitable.

Multiple Choice

All Are Correct.