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Marketing Alternatives for Producers of Wheat and Other Grains: Teaching Guide

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Richard K. Rudel

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Marketing Alternatives for Producers of Wheat and Other Grains

Teaching Guide

Cooperative Extension Service
South Dakota State University
U. S. Department of Agriculture
Marketing Alternatives for Producers of Wheat and Other Grains

Cooperative Extension Service, State University of New York

Teaching Guide
MARKETING ALTERNATIVES FOR PRODUCERS OF WHEAT AND OTHER GRAINS

A TEACHING GUIDE

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South Dakota State University
Brookings, South Dakota 57006

Published by
South Dakota Extension Service
GRAIN MARKETING ALTERNATIVES
WORKSHOP GUIDELINES

Lecture Time: Minimum time - 2 hours
Suggested time - 4 hours

Workbook Time: About 2 to 3 hours, depending on experience of participants and the amount of individual help given.

Size of Group: Lecture series can be presented to nearly any size group that can easily see the overhead transparencies used.

The work session group should not exceed 30 persons for each leader.

Suggested Supplementary Materials for Participants:

1. Workbook, Marketing Alternatives for Producers of Wheat and Other Grains. South Dakota State University Brookings, South Dakota 57006. (A copy for each work session participant is necessary.)

2. Marketing Alternatives for Producers of Wheat (alternatives about the same for all grains) available from South Dakota State University Bulletin Room, Brookings, South Dakota 57006.

3. The Benefits of Grain Futures - Even if you don't trade in them - FS 622, Bulletin Room, South Dakota State University, Brookings, South Dakota 57006.


TEACHING GUIDE

Marketing Alternatives for Producers of Wheat and Other Grains

The grain producer doesn't always have to "take" the price offered to him. He can choose the time and way he will sell his grain.

This guide examines marketing alternatives that could be as profitable to the producer as raising more bushels of grain per acre.

He needs to keep up with the news from the world markets and domestic agricultural policies; and he needs to know his options. They have been identified and described in the publication, Marketing Alternatives for Producers of Wheat.

This teaching guide provides Extension personnel and other educators the basic techniques and methods to use in informing producers about selected marketing alternatives. Producers need to understand how and why these different strategies work and to know the advantages, disadvantages, and risks associated with each alternative.
ALTERNATIVES FOR MARKETING GRAIN

Alternative I. SELL CASH GRAIN AT HARVEST

Advantages

A. Extensive storage facilities on the farm are not needed. These storage facilities are costly and, with the current prices for materials, costs may average 1-3 cents a bushel per year for the life of the facility. For example, if additional basic storage had been built during the summer of 1974: (Excluding unloading equipment)

A 2,400 bushel wooden granary cost 90 cents per bushel to construct; depreciating this over 20 years gives a cost of 4.5 cents per bushel per year.

A 5,000 bushel steel bin cost 39 cents per bushel to construct; depreciating this over 20 years gives a cost of 1.95 cents per bushel per year.

A 10,000 bushel steel bin cost 28 cents per bushel to construct; depreciating this over 20 years gives a cost of 1.4 cents per bushel per year.

A 69,000 bushel steel quonset cost 24 cents per bushel to construct; depreciating this over 20 years gives a cost of 1.2 cents per bushel per year.

In addition to the actual construction costs of the storage facilities, producers would have an interest cost. Table 1 illustrates the interest costs associated with the facilities listed above.

B. Maintenance of quality is not the producer's responsibility.

1. Loss of one grade from #2 to #3 wheat can cost up to 16¢ per bushel (discounts are similar for other grains).
Table 1. Interest Costs for Selected Grain Storage Facilities.

<table>
<thead>
<tr>
<th>Facility</th>
<th>Interest Rate*</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>7 percent/yr.</td>
</tr>
<tr>
<td>2,400 Bu. Wooden Granary</td>
<td>3.15</td>
</tr>
<tr>
<td>5,000 Bu. Steel Bin</td>
<td>1.36</td>
</tr>
<tr>
<td>10,000 Bu. Steel Bin</td>
<td>0.98</td>
</tr>
<tr>
<td>69,000 Bu. Steel Quonset</td>
<td>0.84</td>
</tr>
</tbody>
</table>

*Computations based on 100 percent financing and equal annual principal payments over the pay out period. In this case specific annual interest rates were 7 percent and 10 percent which were divided by 2 to obtain the average interest rates of 3.5 and 5.0 percent. If producers use their own money then a charge approximated to these rates would still be made, because the producer could have realized this amount from investing his funds elsewhere (in bonds, savings accounts, etc.).

Table 2. Representative Discounts for Loss of One Grade for Wheat

<table>
<thead>
<tr>
<th>Representative Discounts</th>
<th>Grade Limits</th>
<th>Discount</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>#2</td>
<td>#3</td>
</tr>
<tr>
<td>Damage</td>
<td>4%</td>
<td>7%</td>
</tr>
<tr>
<td>Heat Damage</td>
<td>.2%</td>
<td>.5%</td>
</tr>
<tr>
<td>Test Weight</td>
<td>57#</td>
<td>55#</td>
</tr>
<tr>
<td>Shrunken and Broken Kernels</td>
<td>5%</td>
<td>8%</td>
</tr>
<tr>
<td>Foreign Material</td>
<td>1%</td>
<td>2%</td>
</tr>
</tbody>
</table>

Loss in test weight can occur from insects, heat damage or moisture, all of which can be storage related.
2. Spoilage is not the only cause for a loss of 5¢ a bushel or more in grade. Other factors that may cause a loss of grade are:

a. A common discount for foreign material for wheat is 1/2 cent a bushel discount for each 1/2% FM over 1/2 or fraction thereof. "Foreign material shall be all matter other than wheat which is not separated from the wheat in the proper determination of dockage". Thus the accidental or intentional addition of any other substance to the wheat stored could lower the grade.¹ A common discount for broken kernels of wheat is 3 cents per bushel discount to 5% and 1 cent for each 1% over 5%. "Shrunken and broken kernels shall be all kernels and pieces of kernels of wheat and other matter that will pass readily through a 0.064 x 3/8 oblong hole sieve".²

b. Other special grade changes which can develop while storing grain and which can cause a decrease in price are: (1) tough wheat, (2) musty wheat, or (3) weevily wheat.

C. The producer has the use of cash at harvest time.

1. Selling cash grain at harvest usually provides cash to producers quicker than other marketing alternatives.

2. By selling grain at harvest producers don’t have to absorb the costs of interest associated with storing the grain. This advantage is readily visible if producers have to borrow money and pay interest or if they take the cash and invest it in interest bearing liquidities. See Table 3 for interest costs per bushel per month at various prices.

<table>
<thead>
<tr>
<th>Grain Value per bushel</th>
<th>Monthly Interest Cost</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>7%</td>
</tr>
<tr>
<td>$1.00</td>
<td>0.58</td>
</tr>
<tr>
<td>2.00</td>
<td>1.17</td>
</tr>
<tr>
<td>3.00</td>
<td>1.75</td>
</tr>
<tr>
<td>4.00</td>
<td>2.33</td>
</tr>
<tr>
<td>5.00</td>
<td>2.92</td>
</tr>
</tbody>
</table>

From the above table, interest gained or lost over a 6 month period covered a range from about 4 cents to slightly over 25 cents per bushel, depending on the value of grain and the interest rate.
3. By selling at harvest, producers do not bear the insurance costs of farm stored grain.

Table 4. Estimated Insurance Costs for Selected Grain Values at Insurance Rates of $5.85 per $1,000 of Valuation

<table>
<thead>
<tr>
<th>Grain Value</th>
<th>Annual Cost Per Bushel</th>
<th>Six Month Cost Per Bushel</th>
</tr>
</thead>
<tbody>
<tr>
<td>$1.00</td>
<td>0.585</td>
<td>0.297</td>
</tr>
<tr>
<td>2.00</td>
<td>1.170</td>
<td>0.585</td>
</tr>
<tr>
<td>3.00</td>
<td>1.751</td>
<td>0.876</td>
</tr>
<tr>
<td>4.00</td>
<td>2.340</td>
<td>1.170</td>
</tr>
<tr>
<td>5.00</td>
<td>2.925</td>
<td>1.463</td>
</tr>
</tbody>
</table>

From the above prices, insurance costs over a 6 month period could range from about .3 cents a bushel to 1.4 cents a bushel.

D. Selling directly from the field eliminates storage shrink for producers.

1. Informal tests have indicated storage shrink averages about 1-2 percent for wheat. This does not include moisture loss. Any moisture loss under the grade limits is an additional storage cost.
Formula to Check Storage Loss in Weight

Weigh-in Weight _______ Moisture at binning _______
Weigh-out Weight _______ Moisture at removal _______
Add in Moisture loss to Grade Limit _______
 Subtract Moisture less than Grade Limit _______
Total Shrink _______

Example A

| Weigh in WT | 100,000 lbs. | MT 14.5 MT |
| Weigh out WT | 97,000 lbs. | MT 13.5 MT |
| Add in 1% WT loss | 1,000 lbs. |
| 14.5 to 13.5 |
| Storage Shrink | 2,000 lbs. |

Example B

| Weigh in WT | 100,000 lbs. | MT 14.5 MT |
| Weigh out WT | 95,000 lbs. | MT 11.5 MT |
| Add in 1% WT loss | 1,000 lbs. |
| 14.5 to 13.5 |
| Subtract 2% WT loss | 2,000 lbs. |
| 13.5 to 11.5% |
| Storage Shrink | 4,000 lbs. |

In example A the moisture reduction from 14.5 percent to 13.5 percent, although it is a part of the loss in bushels, usually commands about a 4 cent a bushel increase in price and thus is not charged against the shrink. This accounts for the 1,000 pounds of wheat added back to the weigh-out weight.
In Example B with moisture decrease from 14.5 percent to 11.5 percent, only the moisture decrease of 2 percent is counted as shrink because as in Example A the decrease in moisture from 14.5 percent to 13.5 percent commands a price increase. There is generally no premium for a moisture decrease below 13.5 percent. Therefore, 1,000 lbs. is added to the weigh-out-weight, and the additional 2 percent moisture loss is deducted along with the 2 percent intangible shrink.

E. The producer can usually start harvest earlier as elevators can handle wheat that is higher in moisture than is considered safe for on farm storage. This is especially important for producers in high risk hail areas.

Disadvantages

A. Grain prices are historically low at harvest time. (Develop a history for your area of cash prices for each month.)

B. There is usually a congestion of transportation and handling facilities at harvest time. Many who would like to deliver the grain right from the field are unable to do so.

C. Selling at harvest time sometimes offers less flexibility in adjusting income for taxes. Many times a producer's annual income and tax liability are not known at harvest time. If
grain is sold at harvest time and the money used, income from that sale of grain cannot be adjusted later for income tax purposes.

D. The producer loses control of the grain and any potential for using it as collateral.

Alternative II. STORE GRAIN AT HARVEST FOR LATER SALE

Advantages

A. Storing grain at harvest often yields a higher farm price later on in the crop year.

Table 5. High and Low Price Ranges for Wheat at Kansas City

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Harvest Low</td>
<td>$1.32</td>
<td>1.30</td>
<td>1.34</td>
<td>1.48</td>
<td>1.45</td>
<td>2.60</td>
</tr>
<tr>
<td>Harvest High Until Next Harvest Change*</td>
<td>$1.61</td>
<td>1.38</td>
<td>1.69</td>
<td>1.67</td>
<td>2.80</td>
<td>6.23</td>
</tr>
<tr>
<td>Average Accumulative Price Change</td>
<td>+ .29</td>
<td>+ .08</td>
<td>+ .35</td>
<td>+ .19</td>
<td>+ 1.35</td>
<td>+ 3.63</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>.45</td>
<td>.98</td>
</tr>
</tbody>
</table>

*The yearly price trend can be downward, but the benefits of harvest time storage are positive.

B. Additional advantages of storing grain for later sale are tempered depending on whether the farmer chooses commercial or on-farm-storage. If commercial storage is readily available the producer may
need fewer on-farm-storage facilities and handling equipment. Furthermore, the risk of quality maintenance and the cost of shrink are shifted from the producer to the elevator. For example, a 2 percent loss from an extra handling and storing in one's own bin on $4.00 per bushel wheat would amount to 8 cents per bushel, which could pay for several weeks storage at a commercial elevator. Commercial storage also permits the farmer to execute his sell decision immediately since the grain has already been delivered.

C. Sometimes it is more convenient to use on-farm-storage. For some producers there are real savings of time in unloading grain at home during harvest, and then deliver it to the market at a later date. In some cases there are substantial savings in transportation costs where grain is custom combined. In addition, on-farm-storage helps to ensure a competitive storage cost. It also increases flexibility - the producer can deal with other buyers instead of just the elevator where he might have his grain stored.

Disadvantages
A. If on-farm-storage is used, the producer assumes the risks of shrink and maintenance of quality.
B. There is an additional expense because of the extra handling necessitated by on-farm-storage.
In addition to the cost of shrink, there is also an additional cost for the extra elevation into and out of a bin. There may be an additional hauling cost for delivering grain to a farm bin and then later to market.

C. Additional interest charge should be assessed against stored grain:
   1. If money is borrowed, the interest rate of borrowing should be assessed to the stored grain.
   2. If the producer has his own money, the amount of interest that invested money could return should be assessed to the stored grain.

D. Conditions can make farm stored grains inaccessible during a price bulge.
   1. Bad weather conditions, difficulties in transportation, and other factors may prevent delivery of grain for a high price based on immediate shipment.

Alternative III. CONTRACT CASH GRAIN BEFORE HARVEST

Advantages

A. Price is established ahead of harvest.
   1. In most years harvest time is a time of lower prices; therefore, it should be an advantage to establish a price prior to harvest time. (See Table 5.)
2. Harvest time confusion may lead a producer to unknowingly take a price that is lower than necessary. If possible, the cost of production for a grain should always be assessed before accepting a price to prevent locking in a loss.

B. The producer is usually assured of an outlet for his grain.
   1. During a time of shortage of grain transportation equipment, contracted grain which is a responsibility of the local elevator will generally be given priority for delivery.

C. A cash grain contract is usually made with a local person.
   1. Cash grain contracts are normally made with local elevator managers. This may be an advantage to the producer in comparison to futures contracts which are more likely to be made with someone not so well known.

D. Cash grain contracts can be made in any multiple.
   1. Cash grain contracts can be made to fit the producer's expected production, even to a specified number of bushels such as 3,250 bushels, as compared to most futures contracts which must be made in multiples of 5,000 bushels.
2. Cash grain contracts can be made in small amounts so as to be adaptable to the smaller farmer, or to one who produces a variety of crops instead of one major crop.

E. A cash contract is normally free from any assessments after the contract is made.

1. There is at times a demand for earnest money for a cash contract, but then there would be no other demands regardless of the price trend. By comparison if a future price contract goes against expectations, the producers may have to meet several additional margin calls.

2. There is normally no broker's fee for a cash contract, in contrast to a futures contract.

F. Cash contracts are usually for a specific price.

1. Cash contracts are typically made for a specific grade such as $3.79 for #2 wheat, 13 percent protein. Thus, if a producer delivered #2 wheat, 13 percent protein, he would get $3.79 per bushel. If there were grade and protein differences the market premiums or discounts would apply from the $3.79 figure. By contrast, in localizing futures prices, the estimated price is based on historical evidence which may not always fall within the expected narrow
range. Even though the "basis" (the relationship between futures and local cash price) has been within a five cent a bushel range in the last five years, there is no guarantee it will fall within that range the sixth year. Cash-futures relationships will be discussed in more detail later.

G. Cash grain contracting prior to harvest allows advance preparation in delivery and handling for both buyers and sellers.

Disadvantages

A. Cash contracts reduce a producer's flexibility:

1. A cash contract with delivery and payment at harvest does not allow a producer to adjust his income for tax purposes, assuming he has contracted most or all of his production.

2. Sometimes weather will not permit harvest at the expected time. Cash contracts often carry penalties for late delivery, and there are few satisfactory alternatives to delivery.

B. A cash contract must usually be delivered.

1. Usually a cash contract has contingencies from the local elevator to a commission company to a processor, all of whom want delivery of the commodity contracted for.
Cash contracts do not generally have provisions for loss of crop or changing one's mind. Delivery is expected and is enforceable. By comparison futures have alternatives that will be discussed later.

2. A cash contract for grain is no better than the integrity of the people making the contract or the legal instrument which is drawn. If one does not wish to engage in a binding contract, then there is no need to contract at all.

Recommended Elements of a Cash Grain Contract.

A. The date the agreement is made and the date signed are important elements of a grain contract.

1. It is possible that a person may arrange on the telephone to sell grain at an agreed upon price. The actual agreement may be signed a few days later when the price stated in the agreement is not the current price. For buyer and seller protection it is advisable to have both dates attested to by the parties involved.

B. The selling price must be stated in a manner that cannot be misunderstood. Most contracts will call for a local price; others may call for a terminal price less freight, where delivery cost may still be in question.
C. The amount of bushels involved in the agreement must be stated, as well as any deviation allowable from the stated figure, and the disposition of any over-delivery.

D. The kind of grain sold should be stated. While this sounds simple, in the case of wheat, the kind of wheat should be stated because of the difference in value of soft red, hard winter, hard spring, durum, amber durum or white wheat.

E. The quality of grain the contract price is based on must be defined.

   1. For wheat, a contract should say, for example, the price is for #2 - hard red spring wheat, 58# test weight, and 13 percent protein.

   2. If possible a contract should indicate any premiums or discounts from the contract price. However, sometimes the premiums and/or discounts cannot be contracted for in advance. In this case the contract may specify market discounts and premiums on day of delivery to apply.

   3. There is considerable room for disagreement regarding protein for wheat and test weight for oats in contractual agreements. For wheat it is a matter of specifying the protein called for. For oats the problem is more complex. Where the legal weight is 32# per bushel, #2 oats need weigh only 32# per bushel (33# June 1, 1975), but the contract price may call for 38# or better. Because of the abundance of
heavy oats, the contract may call for 38# oats with discounts for lighter oats, rather than a price based on 32# test weight with premiums for heavier oats to apply.

4. It is well to determine if there is any grade of grain too low to apply on the contract even at a discount.

F. The place and time of delivery and payment should be stated in the contract.

1. In most contracts made with local elevators the place of delivery is implied if not written. While there has perhaps been little trouble about place of delivery it should be specifically designated in a contract. The time limits for delivery should also be specified.

G. Any penalties for early or late delivery must be stated.

1. In most formal cash grain contracts there is a time limit for delivery beyond which the contract is not binding or is binding with a penalty subtracted from the contract price. Penalties of 5 cents a bushel per week have been known in recent months for late delivery. Penalties cannot always be avoided but they should be known at the time the contract is made.

2. Late deliveries may not always be the fault of the producer. Perhaps the elevator cannot get transportation. All contingencies can't be
mentioned in every contract, but the element of responsibility when the elevator cannot accept contracted grain should be established.

H. Adjustments for over or under-delivery should be specified in a cash grain contract.

1. Limits on the amount of bushels of grain to be delivered will usually be insisted upon by the contractor. The producer should know what his responsibilities are for any deviations from the contracted bushels. Many contracts will allow for a slight deviation in bushels. However, it is the larger deviations that are of most concern.

a. If the producer falls far short of bushels delivered for his contract, how is he expected to settle for this difference? Must he buy bushels to apply on the contract, or must the market difference in price be settled by a cash payment?

b. In the event the price of grain goes above the contract price at the time of delivery, the producer will want to know the disposition of any grain over the contract amount. It is usually assumed the first grain delivered applies on a contract. The bushels and price after the contract is filled then apply to over-deliveries.
c. Another area of possible disagreement on cash contracts can come about when wet grain is delivered on the contract. Do the wet bushels apply on the contract or do the dry bushels apply? While it is not unusual for wet wheat or small grains to be delivered to an elevator, the difference between wet and dry bushels is not usually as great as in the case of corn. For example, where 30 1/2 percent moisture corn is delivered to the elevator, and the limit of moisture for #2 corn is 15 1/2 there is a 15 percent moisture difference. This 15 percent difference plus a 3 percent probable drying shrink could make 18 percent difference as to whether wet or dry grain applied on the contract.

I. Premiums, such as protein premiums, and discounts for grade are often not quoted far in advance of harvest. Protein premiums are hardly ever quoted in a contract other than to specify a minimum the contract calls for. Grade discounts for some grains are sometimes available in advance and should be a part of the contract when possible. If nothing more definite is available then the contract should state "premiums and grade discounts at time of arrive to apply."
The "Uniform Commercial Code" is a comprehensive statute governing commercial transactions involving personal property. Many topics are covered by the code, including sales contracts and storage documents. Producers of wheat who intend to contract their grain can utilize the information provided in this statute to ensure that their sales contract contains and makes explicit the required elements. A copy of the uniform commercial code is provided for reference in Appendix Table I.

**Alternative IV. CONTRACT GRAIN FOR DEFERRED PAYMENT**

**A.** Contracting cash grain for deferred payment is usually done for the producer's benefit in adjusting receipts for tax purposes. This strategy is legal and should be used by producers to spread cash receipts. Cash accounting is an advantage farmers have over most other industries. Formerly it was thought a farmer could first let his check lay at the elevator; and then cash it after January 1 in an effort to adjust income. Recent interpretation by the Internal Revenue Service specifies "That anytime a cash basis tax paying farmer can make a demand for payment he is in essence in receipt of income and is taxable even though he did not actually receive cash."
The producer must give up title to the grain, and waive any rights to demand payment until
maturity of the contract. This is usually accomplished by signing a special form at the local elevator.

B. Anytime a producer has grain priced and does not use the money he has an interest loss each day for the value of the grain. There may be times the producer really doesn't need the money for his grain for several months. In this situation, several elevator companies have agreed they would pay an amount for the use of the money where grain is delivered and shipped out. This can be advantageous for both the producer and the elevator. If the producer has the grain stored on the farm, has it sold but is awaiting delivery until after January 1 this option would not be available to him. Sometimes this return on value may be included in the contract price of the grain. At other times it may be handled as interest. If a producer makes a deferred payment agreement it is well for him to know his state law governing this type of transaction. Some states have a limited time period of protection under their grain dealers act (check the law of your state). If the elevator is to have use of the money for a considerable length of time it is advisable to shift the deferment agreement to a note after the income shifting requirements have been met. In a case where the solvency
of an elevator might be questioned, there has been a demand by some producers that the elevators place their deferred payment money in an escrow account. This type of demand on the elevator would probably eliminate or substantially decrease any payment for use of the money.

To this point in the discussion of marketing alternatives we have mentioned grain futures but they have not been discussed as a marketing strategy. Now as we begin to consider futures trading as a marketing strategy it would be well to define a few terms peculiar to grain futures.

Basis, in grain terminology, is the difference between a grain futures price and a specified cash grain price. Each locality has a different "basis", mostly because of the costs of getting grain to a market. Where a comparatively free market exists the "basis" for a locality becomes predictable within certain limitations. Normally the basis is wider at harvest time, then narrows later. This usually consists of deducting the cost of transportation from a terminal market to the local area.

Localized future is the basis analyzed so as to estimate what a futures price reflects in a local cash price for that grain.
Offsetting contract is a cancelling process. When a futures contract is bought, a later "offsetting" contract must be sold to equalize your position in the market. Delivery of grain may be taken, but only 1 to 2 percent of futures contracts are settled this way. If a futures is sold first, then an offsetting contract must be bought. The offsetting contract must be made in the same market, for the same commodity, and for the same futures month. If a person makes what he thinks to be an offsetting contract in a different futures trading month, he will then have a position in two contracts.

To arrive price is a cash grain price bid to country elevators, giving a price as of that day for grain to be delivered at some specified later date at a specific market.

Hedging is to take an equal and opposite position from your intended or present inventory of grain.

Cash price is usually assumed to be the current bid price for the actual grain.

Short sale is to have sold into a futures market with the intent to buy back later.

Long sale is to have bought into the futures market with the intent to sell later.

Since these terms are used frequently in the following sections, an understanding of them is important to achieving a working knowledge of market strategies involving grain futures.
Alternative V. FORWARD PRICE GRAIN BY USING FUTURES

Advantages

A. Grain futures generally offer a longer time to choose a price. There has been a demand by producers for cash grain contracts to be offered much earlier. To date, cash contracts are generally offered only a few weeks in advance of harvest. However, where elevator managers understand and use grain futures on a regular basis, the cash contract has been offered far in advance of harvest. This is because futures often offer a period of a year or more in which to lock in a price. The local elevator manager may offer the producer a cash grain contract and he in turn will hedge the grain in the futures. Where the local producer has a good understanding of grain futures he can, through his broker, hedge his crop in the futures market.

B. Localized futures prices may represent a higher price than cash "to arrive" prices at a specific market. This relationship, while not normal, could occur when a local elevator manager is concerned about the ability to get rail cars and is faced with a severe truck discount. Futures may also represent a higher price than cash price when the world demand for a commodity is greater than a local demand. Several instances where the localized futures price was higher than the
to arrive local cash price were observed in 1973 during the severe box car shortage. Soybean prices for a locality on August 14, 1973, were $8.61 per bushel for a localized futures price and $8.40 for a "to arrive" cash price. The conservative cash bid was because of the uncertainty of transportation. In the above example if rail transportation is available at harvest time, a forward price by using futures would yield about 20 cents a bushel more than the to arrive bid. If rail transportation is not available, and a 20 cent per bushel truck discount persists, then the two prices would be essentially the same.

C. Grain futures are usually simpler to offset in case of a crop failure. As was discussed under the disadvantages of forward pricing cash grain, cash contracts must be fulfilled somehow, and delivery is usually enforceable. The fear of crop failure often keeps producers in some areas from forward pricing even though they have been offered an acceptable price. For grain forward priced through futures, there are simple options open to the producer. He may in the event of a crop failure, immediately buy an offsetting futures contract and fulfill his obligation to the market. Just because it is comparatively simple to equalize a futures position does not mean that it is necessarily inexpensive. The expected drop in
futures at the time a future sale was made may not have occurred yet, or futures may even have gone up at the time you would like to equalize your position. Another option available from forward pricing by use of grain futures is that if you lose a crop and you are in a short position in the futures, you may continue to hold that short position if the market tends to move downward according to your expectations.

D. Forward pricing grain by using futures is easier to adjust to changing conditions than is a cash grain contract. For example: you may forward price your grain based on the best information available at the time; however, soon after pricing the grain, some new developments become known that reverse your expectation of the market, and cause you to want to alter your position in the market. If the grain was forward priced with a cash grain contract, either the actual grain would need to be purchased from someone to satisfy the contract or the grain merchant may allow the producer to pay any loss incurred by default. If the grain was forward priced in the futures, you would only need to buy an offsetting contract.

E. Using futures increases the number of buyers in both the export and domestic market. Futures also increase the probability of receiving the
highest possible price, as the futures contracts are traded to the best bid at auction.

Disadvantages

A. One of the most easily recognized disadvantages of forward pricing grain by use of futures is the demand for a margin deposit of about 10-15 percent of the value of the grain before a trade can be made. This margin money is not an expense of trading as it will all be returned at the completion of the trade if the market moved as you expected. If the market moves contrary to your expectations, your loss will be charged against the margin deposited, and the balance will be returned to you. Whether you gain or lose you will be charged a brokerage fee of $30 - $35 for each 5,000 bushel contract. This fee is for the "round term" contract, or in other words it includes the "in" contract and the offsetting "out" contract. While it is not a disadvantage of the market system, there is the temptation for a producer to forget the original intent to lock in a price and begin speculating. However, the lifting of a short hedge when there is a fundamental change in supply and demand is only prudent.
Short Trade - Price Decline

March 1  Sell 5000 bu. of September Wheat @ $4.00 Margin Deposit $2,500.00

July 10  Buy 5000 bu. of September Wheat @ $3.80 gain in futures 20¢ x 5000 bu. = $1,000.00

Brokers Commission - $30.00

Account Balance July 10 $3,470.00

Short Trade - Price Rise

March 1  Sell 5000 bu. of September Wheat @ $4.00 Margin Deposit $2,500.00

July 10  Buy 5000 bu. of September Wheat @ $4.20 loss in futures 20¢ x 5000 bu. - $1,000.00

Brokers Commission - $30.00

Account Balance July 10 $1,470.00

Long Trade - Price Rise

Aug. 10  Buy 5000 bu. March Wheat @ $4.15 Margin Deposit $2,500.00

Dec. 20  Sell 5000 bu. March Wheat @ $4.30 gain in futures 15¢ x 5000 bu. = $750.00

Brokers Margin - $30.00

Dec. 20 Account Balance $3,220.00
B. Another disadvantage to forward-pricing grain by using futures is that additional margin deposit may be called for if the market moves more than a few cents contrary to your expectations. This is true even if the market eventually moves in the direction anticipated but has a move in the opposite direction before turning in the expected manner. For example, let us say you believed from everything you read, heard and saw that wheat would go down before new crop harvest. To protect against that expected drop you sold 5,000 bushels of wheat futures. Presently the margin deposit required for one 5,000 bushel contract is $2,500 with a maintenance margin of $1,500. If the market went up nine cents a bushel before it began a decline you would most likely not have a margin call. If the market went up eleven cents you would most likely be asked to post $550 (11 cents x 5,000 bushels) more margin to bring the balance...
back to $2,500. As the market declined you could withdraw any excess over $2,500. With a cash contract, price variations do not necessitate any action on the part of the seller.

C. A possible disadvantage to forward-pricing grain by using futures is that nearly all futures are sold in multiples of 5,000 bushels. For the person who wanted to hedge 3,000 bushels or 8,000, or 12,000 bushels this is a disadvantage. Cash contracts, as previously stated, can usually be made in any multiple.

D. The expected price from forward-pricing by use of futures is based on historical relationships and as such is not a definite figure. You must learn from history about what futures prices represent in cash prices in your own locality. Because of variations due to such things as transportation, local elevator margins and availability of storage space, the local price represented by futures may easily vary by approximately five cents a bushel from one year to another. This variance is not considered to affect the use of futures as a forward pricing tool. Some years forward pricing through futures may be a few cents more than expected, and other years a few cents less than expected. For someone who wants to forward contract at an exact price, any variation is a disadvantage (See Table 6).
<table>
<thead>
<tr>
<th>Date</th>
<th>Mpls. Cash 13 Pro HRS-W</th>
<th>Mpls. Sept. Wheat Futures</th>
<th>Mpls. Basis</th>
<th>Freight-Hometown To Minneapolis</th>
<th>Hometown* Basis</th>
</tr>
</thead>
<tbody>
<tr>
<td>1969</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Aug. 15</td>
<td>1.57</td>
<td>1.55</td>
<td>2 over</td>
<td>14¢ Per Bu.</td>
<td>12 under</td>
</tr>
<tr>
<td>Sept. 1</td>
<td>1.63</td>
<td>1.60</td>
<td>3 over</td>
<td></td>
<td>11 under</td>
</tr>
<tr>
<td>1970</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Aug. 15</td>
<td>1.87</td>
<td>1.85</td>
<td>2 over</td>
<td>16¢ Per Bu.</td>
<td>14 under</td>
</tr>
<tr>
<td>Sept. 1</td>
<td>1.88</td>
<td>1.83</td>
<td>5 over</td>
<td></td>
<td>11 under</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>3 under</td>
<td>16¢ Per Bu.</td>
<td>19 under</td>
</tr>
<tr>
<td>Sept. 1</td>
<td>1.54</td>
<td>1.54</td>
<td>even</td>
<td></td>
<td>16 under</td>
</tr>
<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>5 under</td>
<td>17¢ Per Bu.</td>
<td>22 under</td>
</tr>
<tr>
<td>Sept. 1</td>
<td>1.92</td>
<td>1.95</td>
<td>3 under</td>
<td></td>
<td>20 under</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>16 under</td>
<td>18¢ Per Bu.</td>
<td>34 under</td>
</tr>
<tr>
<td>Sept. 1</td>
<td>4.43</td>
<td>4.43</td>
<td>even</td>
<td></td>
<td>18 under</td>
</tr>
<tr>
<td>1974</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Aug. 15</td>
<td>4.78</td>
<td>4.77</td>
<td>1 over</td>
<td>19¢ Per Bu.</td>
<td>18 under</td>
</tr>
<tr>
<td>Sept. 1</td>
<td>4.80</td>
<td>4.70</td>
<td>10 over</td>
<td></td>
<td>9 under</td>
</tr>
</tbody>
</table>

*The elevator’s handling margin must be added to the hometown basis to determine the producer’s basis.*
When futures prices are localized by historical records, one can theorize that because this (x) has been the price range for several years, then the localized futures price should be approximately this (x) next year. Conditions, of course, can change causing historical records to not be as relative as in other years. A critical shortage of transportation in 1973 greatly affected historical cash-futures relationships. Cash prices were discounted because nobody knew when grain could be shipped. Uncertainty usually affects local cash prices whether or not you use futures to establish a price.

E. It is not possible to forward price all grains and oilseeds by using futures because not all are traded in futures. For example, there is no futures market for rye and flax in the United States. Both are traded on the Winnipeg grain exchange but these futures prices are seldom relative to U.S. cash prices. Barley, triticale, rapeseed, millet, and sunflowers are other examples of grains and oilseeds not presently traded in the futures market of the U.S.
F. A sixth disadvantage to forward pricing grain through futures is that preliminary study must be done to localize futures prices. Someone, and preferably the trader himself, must develop through historical or other means, an analysis of what futures prices represent in local cash prices. Without this knowledge of forward pricing grain with futures, he may lock in a price far different than intended.

G. Usually futures contracts introduce at least a third or new party into the marketing transaction—the speculator. Speculators may affect the futures market in either a positive or negative manner. Extreme speculation whether on the up side or down side may disturb the normal basis temporarily and thus cause a variance from original net price goals.

H. Using futures requires training and expertise. Many times the producer either can not or will not be able to keep in close enough communication with brokers. Thus, decisions on futures are often delayed and made after the fact rather than on an immediate basis. Some producers may be better off to hire an expert in futures trading to act on their behalf.

I. Although it is unusual, a producer may want to deliver his cash grain against his futures contract. Currently, less than two percent
of the grain is delivered in this manner; however, proposals have been made to increase the number of delivery points. This may result in eliminating the problem of few and far distant points of delivery presently in use and thereby increase the opportunity for delivery of cash grain against futures.

Alternative VI. **STEPS IN FORWARD PRICING GRAIN BY USE OF FUTURES**

A. Futures prices must be localized to the area so you know at what price the grain is being quoted.

1. Localizing futures prices has been explained previously.

B. Select the appropriate new crop future.

1. For example: If you live in the Northern Plains spring area, although the Minneapolis September future is considered a new crop future, your crop may not be ready for market at the time you should offset your futures contract. If this situation is expected, then perhaps the following December future would be a better forward pricing month under these conditions. The same conditions may apply to the July future in Chicago and Kansas City for areas related to those markets.
C. Sell the futures in the appropriate amount.
   1. It is recommended that you not oversell your expected production. As long as most futures contracts are in multiples of 5,000 bushels you should make futures contracts based on a conservative estimate of yield. A plan used by some producers is to sell 1/3 of the crop before it is planted, sell 1/3 when the crop is growing, and leave 1/3 unsold to hedge against a price rise or a reduced yield.

D. Sell cash grain and on same day "buy back" or buy offsetting futures contract.
   1. To be a true forward price sale, the futures position should be offset as close to the time of pricing the cash grain as possible. If there is a delay in this procedure, you may find yourself in a speculative position again instead of a hedged position. Many beginning traders assume that if they make a futures sale they just deliver the grain against the futures and their responsibility is completed. Delivery can be made on futures in some instances but less than two percent of all futures trades are settled in this manner. In most cases delivery points for grains are too far distant, and it is therefore too costly to make delivery on futures.
contracts. The most-used system is to deliver the grain to your elevator, sell it, and then buy an offsetting futures contract. This does not in any way keep you from keeping the cash grain after you have offset the futures contract if you choose to do so. Various options you have for your cash grain will be discussed in following sections.
Alternative VII.  **FORWARD PRICE GRAIN BY USING FUTURES AND SELL CASH GRAIN AT HARVEST**

Example 1

* July 5  * Sell 5000 bu. of Minneapolis Dec. wheat @ $2.62  
  $2.62
  History indicates this represents about $2.32 in local cash price.
  
  To arrive bid for cash wheat is $2.37 but delivery must be guaranteed for Sept. 1 arrival.
  
  Sept 6  * Harvested, delivered and sold 5000 bu. of cash wheat @ $4.09  
  $4.09
  Sept 6  * Bought 5000 bu. of Minneapolis Dec. wheat (offsetting contract) @ $4.39
  
  Sold Dec. Wheat for $2.62 - bought
  Dec. wheat for $4.39, loss per bu. = $1.77
  Gross price for wheat  $2.32

*Actual 1973 price conditions.

It is possible that some people will say the futures failed the producer in the above example because they only brought a combined price of $2.32 while the cash price was $4.09. The futures did not fail the producer. They brought exactly what the producer expected in cash price at the time the sale
was made (July 5). In most years prior to 1973, sales made ahead of harvest resulted in a higher total price than the harvest time cash price.

The reason the producer in the above example sold futures instead of taking the $2.37 cash contract was that he could not guarantee delivery in Minneapolis by September 1.

The $1.77 loss in futures was paid by meeting margin calls. Every time the futures price went up ten cents, the producer was asked to add more margin to his account.

In looking back the judgment of the producer looks bad in continuing the futures sale so long. It must be remembered the protected price is about twice as high as the previous year's prices, and thus looked good to the producer. A producer usually has no reason to forward price unless he believes the price will go down, or unless it is important to "lock in" a price to insure a profit.

Alternative VIII. FORWARD PRICE GRAIN AND STORE GRAIN AT HARVEST

A. In the previous example, the producer may if he chooses store the cash wheat instead of selling it. He could sell and buy the future in the same manner. A producer or grain merchandiser may choose to store the cash wheat even after it had been forward priced through the futures, in anticipation of a higher price, or in
anticipation of a higher protein premium, or perhaps because he had all sales he wanted for the year for income tax purposes.

B. If in Example 1 after the producer had sold Minneapolis December futures @ $2.62 July 5, he became convinced that he made a mistake and should be in a long position instead of a short position, he could have chosen several different options.

1. On July 10, for example, he could have "bought back" his 5000 bushels of December wheat at a 10 cent a bushel profit and then speculated on the price of the cash wheat he was raising. This strategy might also include storing the wheat for a year.

2. He could have left his forward price futures sale intact until the time of harvest, but instead of selling the cash wheat he could have stored it in the hopes of recovering some of the futures loss. In 1973 he could have recovered 60 cents of the $1.77 futures loss by September 17.

3. He could have not only "evened" his short future position on July 10, but could have established a long position in the futures as well as remaining long in the cash grain. This would double the producer's
risk, but would also double the profit potential if his judgment of the market was correct.

Example 2

<table>
<thead>
<tr>
<th>Cash</th>
<th>Futures</th>
</tr>
</thead>
<tbody>
<tr>
<td>July 5</td>
<td>Cash wheat value $2.32</td>
</tr>
<tr>
<td>July 17</td>
<td>Cash wheat value $2.21</td>
</tr>
<tr>
<td>July 17</td>
<td></td>
</tr>
<tr>
<td>Sept 6</td>
<td>Sold cash wheat @ $4.09</td>
</tr>
</tbody>
</table>

Total price for wheat $4.09

.10 1st futures gain
1.87 2nd futures gain
$6.06

This is a highly speculative system and should not be tried without a strong conviction and some trading skills.

Forward pricing of wheat has been quite responsive to historic cash-futures relationships, but because of the great influence of CCC stocks and policy, wheat has not had a predictable storage hedge basis. It is expected that the diminished role of CCC and the greater free market influence will result in wheat prices being more responsive to similar price making factors as for corn and soybeans. Because the storage hedge basis in wheat has not been predictable, an
example of soybean prices and situation will be used to describe the storing and hedging options after grain has been forward priced by use of futures.

Example 3

*Aug. 14 Sell 5000 bu. of Chicago November soybeans @ $9.01

History indicates this normally represents about $8.61 in local cash price.

Present cash bean to arrive price $8.40.

Oct. 12 Harvested and stored 5000 bu. of cash beans.

Present market price $5.50.

Oct. 12 Bought 5000 bu. of Chicago November soybeans (offsetting contract) @ $6.29

Futures gain per bu. $2.72

*Actual 1973 prices conditions

The price for the producer's beans on October 12 is $5.50 market price plus $2.72 futures gain or $8.22, however, the final price is not established.

The stored grain does not have a price established and is once again in a speculative position. The value could go up or down.

The $2.72 futures gain is determined and can be applied to the total price of the beans when a price is established on the cash grain.
A critical shortage of transportation caused the cash price to fall far below the historical cash-futures relationships. This caused the producer to miss his target price by ($8.61 - $8.22) 39 cents. The $8.22 was, however, $2.72 better than the current cash price of $5.50.

Alternative IX. **FORWARD PRICE GRAIN BY USING FUTURES AND HEDGE GRAIN AT HARVEST**

A. A third option available to one who forward prices his grain in the futures is that of placing a hedge after the forward pricing future is lifted. This strategy could be used to:

1. Protect against a price drop while waiting to sell the grain.
2. Receive additional payment for storage by having an improvement in the basis.
3. Insure a minimum price while deferring income into another year.
4. Protect a price while determining whether the grain is needed for feed or seed.

B. Under this option there are two different reasons for placing a hedge on grain after harvest. Both purposes may be used simultaneously or they may be used individually. The purposes are to protect a price and to increase income from a basis improvement. The need or desire
to protect a price is quite universally understood. A producer may be satisfied with the price but because of a shortage of transportation or space cannot sell the grain immediately. In addition a producer may be satisfied with the price but doesn't want the income until later, or he may be satisfied with the price but would like to keep the grain around to determine if it's needed for feed or seed, or until quality or protein premiums go up.

C. Not so well understood perhaps, especially by those who raise mostly wheat, is the profit opportunity from an improvement in the basis, regardless of which way the cash price goes. For corn and soybeans, historically the basis (the spread between futures and the cash price considered) widens at harvest time and then narrows later. Anytime a person concludes from the history of the price relationship that the basis will narrow more than the cash price will go up for a commodity, then he can profitably store the grain and sell the future. By this strategy a person would have protection against a large cash price drop and should make some additional income from the basis improvement such as in the following example.
**Example 4**

**1972-73 Corn Crop Year**
*(Actual prices for a Location)*

<table>
<thead>
<tr>
<th>Date</th>
<th>Action Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dec. 1</td>
<td>Stored cash corn</td>
</tr>
<tr>
<td></td>
<td>Price $1.33 per bu.</td>
</tr>
<tr>
<td></td>
<td>Sold Chicago July futures @ $1.53</td>
</tr>
<tr>
<td>Jan. 15</td>
<td>Sold cash corn</td>
</tr>
<tr>
<td></td>
<td>@ $1.41</td>
</tr>
<tr>
<td>Gain in cash</td>
<td>8¢ per bu.</td>
</tr>
<tr>
<td></td>
<td>Bought Chicago July futures @ $1.41</td>
</tr>
<tr>
<td>Gain in futures</td>
<td>12¢ per bu.</td>
</tr>
</tbody>
</table>

Had the corn been stored without a hedge the gain realized would have been 8 cents per bushel in cash price. With the basis hedge, the grain was 8 cents in cash price plus 12 cents in futures for a total gross gain of 20 cents per bushel.

An additional benefit is the quite reliable protection against a price drop while the basis hedge is in force.

There are several ways the basis may narrow and thus prove profitable to the basis hedger (Figure 1).

1. The cash price may remain constant while the futures go down
2. The cash price may go up - while the futures hold constant
3. The cash price may go up - while the futures go down
4. The cash price may go down slowly - while the futures go down rapidly
5. The cash price may go up rapidly - while the futures go up slowly.
FIGURE 1. WAYS THE "BASIS" MAY NARROW AND CREATE PROFIT AND PROTECTION FROM HEDGE.
As has been stated before, it is expected that as wheat is sold primarily on the open market it too may develop some predictable basis patterns. The relationship between the cash prices and futures prices (without protein premiums) has substantially narrowed at times, but because of the great CCC influence on wheat the basis action has been difficult to predict.

Alternative X. TRANSFERRING SPECULATION FROM CASH GRAIN TO FUTURES

A. It is well to note at the very beginning that this marketing alternative is not a hedge. It is a method of transferring the price risk one already has in the cash grain to futures. There are several reasons why a producer would want to use these alternatives if he felt strongly that prices would go up.

One reason why a producer may want to shift the risk from cash grain to futures is when no storage is available either on the farm or at local or terminal elevators. If the producer thought the cost of buying or renting storage was too high, this might also cause him to consider buying futures and selling the cash grain.
Another reason why a producer would sell his cash grain at harvest and buy futures is if he has an urgent need for cash. He may have a note due at the bank or a machinery or land payment due; and either cannot or does not want to refinance. In the transfer of speculation in this case, the producer can sell his cash grain, then take about 10-15 percent of the money received and buy an equal amount of bushels in the futures. The remaining 85-90 percent of the proceeds could be used to pay bills.

A third reason for a producer to sell cash grain and buy futures would be the desire to escape the shrink or losses of holding grain on the farm. Perhaps the storage facility is such that there is a possibility of excessive shrink and/or losses through holes, or from birds, rodents and insects. Perhaps there is also a fear that the grain will not pass the food and drug standards because of access by the birds, rodents and insects. A 3 percent shrink or loss on $4.00 per bushel wheat amounts to 12 cents a bushel. Condemnation by the food and drug administration could easily amount to $1.00 a bushel loss.
A fourth reason a producer would sell his grain and buy futures is if his grain was not of storable quality. It is not unusual in some years to produce low quality grain that does not store well. The grain may be high in moisture or be badly weathered, affected by blight or it may have sprout damage or any of several other characteristics which add greatly to the risk of storing. The same quality factors discussed may actually depress prices at harvest and make the producer more inclined to hold an inventory of grain for an anticipated price rise later.

B. The procedure for transferring the speculation from cash grain to futures is:

Sell cash grain and buy a near equal amount of futures representing that year's crop; then sell the futures anytime before the contract termination date.

C. An assessment of carrying charges* represented by the futures trading months is important before buying futures. If carrying charges are considered normal, buying the latest old crop futures month would give more time for the

*Carrying charges in grain futures is the difference in price from the nearest future to a deferred future. The deferred future for the same crop year is usually the higher, reflecting some of the cost of storing the grain from one trading month until another.
expected price rise, without transferring the trade ahead each time a futures trading month expires. Every time a futures contract is "rolled ahead" there is another brokerage charge to be paid by the producer. If the carrying charge is considerably higher than usual, then perhaps the nearby futures month should be bought. This decision is seldom critical to the success or failure of the strategy.

D. A producer may sell his grain at harvest and then sell futures also in expectation of a price decline. This is again speculation and is not the shifting of a long position in cash grain to a long position in grain futures.

Guides for Successful Transfer of Risk from Cash Grain to Futures

1. The normal cash-futures relationships for your area should be known, but it is not as critical as in forward pricing of grain. For this purpose the trader is interested in whether the future will go up from the present level, without great concern over its relationship to the cash price.

2. There should be conviction and evidence that both cash and futures prices will go up. It could be possible for example that the deferred futures have already accounted for the situation that causes the producer to think that grain will go up.
3. Replacement of cash grain with futures can be done successfully when the basis is normal or narrower than usual or when further gains in basis will not cover storage costs, and when there is evidence the futures will go higher. The replacement should be done with caution at a time of historically wide basis because of the high risk of having the futures come down even though the cash price might go up. During the unusual years of 1972 and 1973 the futures went up after harvest even though the basis for most grains was exceptionally wide at harvest time.

4. The trader should expect as he replaces cash grain with futures that in most years the futures will not go up as much as the cash grain goes up (See Table 7).

Alternative XI. THE SHORT TERM FUTURES HEDGE

A. The short term hedge is not a strategy that is likely to be used often by producers or grain elevator operators, but it is a technique that is worth knowing about for the few times it would be profitable to use it. If there is no special advantage to using the futures, it is usually less costly to hedge in the cash market.

Two of the more common reasons to use a short term futures hedge are if:

1. There was a considerably higher base price being offered for wheat, on spot at a certain location or,
<table>
<thead>
<tr>
<th>Year</th>
<th>Kansas City May Future</th>
<th>#2 Hard &amp; Dark Kansas City Cash Wheat</th>
<th>Change from July 1 Futures Change</th>
<th>Cash Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>1970-71</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>July 1</td>
<td>1.40</td>
<td>1.34</td>
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</tr>
<tr>
<td>Oct. 1</td>
<td>1.60</td>
<td>1.58</td>
<td>+20</td>
<td>+24</td>
</tr>
<tr>
<td>Jan. 1</td>
<td>1.55</td>
<td>1.64</td>
<td>+15</td>
<td>+30</td>
</tr>
<tr>
<td>Mar. 1</td>
<td>1.48</td>
<td>1.60</td>
<td>+8</td>
<td>+26</td>
</tr>
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<td>71-72</td>
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<tr>
<td>July 1</td>
<td>1.52</td>
<td>1.59</td>
<td></td>
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<tr>
<td>Oct. 1</td>
<td>1.40</td>
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<td>-1</td>
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<td>2.44</td>
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<td>Mar. 1</td>
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<td>July 1</td>
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<td>4.60</td>
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<td>5.08</td>
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<td>Mar. 1</td>
<td>5.48</td>
<td>5.72</td>
<td>+2.94</td>
<td>+3.07</td>
</tr>
</tbody>
</table>
2. There was a considerably higher price offered for certain protein levels on spot over what is offered in the to arrive cash bids.

The short term futures hedge in the two above situations will allow the producer or elevator company to protect against a price loss and at the same time give him the opportunity to take advantage of a higher price "on spot" or at a specific location.

Example 5 will demonstrate how the short term futures hedge can be used to advantage by sellers of wheat (hypothetical situation).

Example 5

<table>
<thead>
<tr>
<th>Date</th>
<th>Event Description</th>
<th>Price Details</th>
</tr>
</thead>
<tbody>
<tr>
<td>Feb. 1</td>
<td>Sold March futures @ $3.18</td>
<td></td>
</tr>
<tr>
<td>Feb. 6</td>
<td>Bought March futures @ $3.02</td>
<td></td>
</tr>
<tr>
<td>Feb. 1</td>
<td>Spot market for 13 protein wheat (localized price) $3.07</td>
<td></td>
</tr>
<tr>
<td>Feb. 6</td>
<td>Wheat arrived at destination and was sold for a localized price of $2.90</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To arrive price $2.83</td>
<td></td>
</tr>
</tbody>
</table>

Cash price loss 17¢ per bu. Futures price gain 16¢ per bu.

Total price for 13 protein wheat sold on the spot market Feb. 6 was $2.90 + 16 cents gain on futures hedge or a price of $3.06 less futures commission.
In Example 5, if the seller of wheat had sold on the to arrive price Feb. 1, he would have received $3.00 for his wheat. Had he shipped the grain into the market unhedged he would have received $2.90 on the spot market of Feb. 6, and he would have had the risk of a greater drop in price from Feb. 1 to Feb. 6.

With the use of a short term hedge the seller was able to realize $3.06 per bushel for his wheat (less futures commission about 1/2 cent per bu.) on Feb. 6, and have protection against a large price drop.

Some producers sell their grain to other than a local elevator. In this type of marketing it is often difficult to get a to arrive price. The producer in this situation could protect or establish a price while his grain is being delivered, with a short term futures hedge.

Alternative XII. OTHER MARKETING ALTERNATIVES

A. There are many marketing alternatives other than those discussed so far. A brief mention of a few of these will serve to remind a producer that he may want to investigate other alternatives before finally selecting a marketing method.

1. Consideration should be given to the use of grain as a feed. This would be particularly true if the grain was of
poor quality and subject to severe
price discounts. Grains should be
compared by price per cwt. and not
by value per bushel to get comparative
value as feed. Nutritional value should
also be considered and allowed for in
the comparison.

2. A producer may choose to sell his grain
through a local and a regional cooperative
with the thought in mind that, if he didn't
get all his grain was worth at the original
price, he could get the remainder in
patronage refunds.

3. A producer may choose to pool his grain
with others of his area and sell as a
large unit, such as is done by members
of the National Farmers Organization.

4. In some grains there is the opportunity
to grow a particular crop where the price
is established ahead of time. This may be
for a flat price, a minimum price, plus
any raise, or as a set premium over
market. This is prevalent now with
specialty crops such as sunflowers, edible
beans, special varieties of corn and soybeans,
peas, mustard, and could develop for
some wheats.
5. A producer may choose to grow a specialized crop for a special market such as amber durum wheat or malting barley.

6. A producer may want to raise grain to be used as seed. A premium price would then reward him for the extra care needed in growing and handling.

7. Some producers have the opportunity to consign their crop to the elevator manager who as a grain specialist markets the grain to the best advantage. Usually a base amount is paid for the grain, and then a final accounting is made after the grain is sold.

8. A producer may sell direct to a processor, trucker, terminal, or feeder. Since the 1968 revision of the grain standards act, grain need not be sold through or graded at terminal market. Parties may legally agree to buy and sell on sample.

9. It is very possible for the producer to make an agreement whereby he could have a profit sharing agreement with a processor. There are undoubtedly other marketing considerations not mentioned here that are important to some producers.
Producers should be aware of the many grain marketing alternatives available to them. Then they have a greater choice in selecting and determining a price and how and when they can market their grain. Properly understood and used, these alternatives could be as profitable as raising more bushels of grain per acre.
APPENDIX A

THE UNIFORM COMMERCIAL CODE

Introduction

I. The uniform code was first adopted by Pennsylvania in 1953. Since that time 48 additional states have adopted the code.

II. The Code is a comprehensive statute governing commercial transactions which involve personal property.

A. Included are such topics as sales contracts, notes, checks, shipping and storage documents, stocks and bonds, and financing transactions.

B. Real estate transactions are excluded, but may be indirectly affected where negotiable instruments are involved.

Article 2--Sales

I. Contracts for sale of goods. Goods are all things which are movable, including:

(a) The unborn young of animals
(b) Growing crops
(c) Temporary buildings or other items attached to realty which can be easily removed without materially harming the land, and
(d) Timber, minerals or permanent buildings if they are to be severed from the land by the seller and not the buyer.

II. The obligations and responsibilities of a merchant are greater under the Code than those of a non-merchant.

A. A merchant is either:

1. Someone who deals in goods of the kind being sold; or
2. Someone who by his occupation holds himself out as having knowledge or skill peculiar to either the goods involved or the practice of buying and selling such goods.

B. The courts have not yet decided whether a farmer may be a merchant.

III. A contract for sale of goods is formed by an offer from one party which is accepted by the other party.

A. A written offer signed by a merchant may be made irrevocable, or firm, for a period of up to three months.

B. Unless an offer specifies otherwise, it may be accepted in any reasonable manner or medium.
C. A contract may be formed even though the acceptance contains terms in addition to those in the offer.

1. Between merchants, the additional terms become part of the contract unless the other party objects.

IV. Generally, a contract for the sale of goods for $500.00 or more must be in writing and signed by the party against whom enforcement is sought.

A. But, a merchant who receives a written confirmation of a contract will be bound, even though he has not signed it, unless he objects within ten days.

V. Missing or ambiguous terms in the contract.

A. Quantity must be agreed upon by the parties and a contract is generally unenforceable if this term is missing.

B. All other terms may, if necessary, be supplied by the Code. Unless the parties agree otherwise:

1. Price--The buyer is obligated to pay a reasonable price for the goods.

2. Place of delivery--The seller has no obligation to deliver goods to the buyer's place of business.
   (a) The place of delivery is the seller's place of business, or if he has none, his residence.
   (b) If both parties are aware that the goods are located some place else, that becomes the place of delivery.

3. Time of delivery--The seller must deliver the goods, or stand ready to do so, within a reasonable time after the contract is made.
   (a) Timely delivery may be excused where unforeseen circumstances make the delivery commercially impracticable.

4. Partial delivery--Unless delivery in a single lot would be impractical or impossible, partial delivery is generally not allowed.

5. Payment--The buyer must tender payment at the time the goods are delivered.
VI. Express warranties are created in three different ways under the Code:

1. Any affirmation of fact or promise made by the seller to the buyer which relates to the goods and becomes part of the basis of the bargain, creates an express warranty that the goods shall conform to the affirmation or promise.

2. Any description of the goods which is made part of the basis of the bargain creates an express warranty that the goods shall conform to the description.

3. Any sample or model which is made part of the basis of the bargain creates an express warranty that the goods shall conform to the sample or model.

VII. A warranty that the goods shall be "merchantable" is implied if the seller is a merchant with respect to goods of that kind.

A. To be "merchantable" the goods must meet the following requirements:

1. The goods must pass without objection in the trade under the contract description.

2. Fungible goods must be of fair average quality within the description.

3. The goods must be fit for the ordinary purposes for which they are used.

4. The goods must run of even kind, quality and quantity within each unit involved.

5. The goods must be adequately packaged and labeled in accordance with the agreement.

6. The goods must conform to any promises or affirmations of fact made on the container or label.

VIII. If the seller has reason to know any particular purpose for which the goods are required, and that the buyer is relying on the seller's skill or judgment in selecting or furnishing such goods, there is an implied warranty that the goods shall be fit for that purpose.

IX. All implied warranties are excluded if the goods are sold "as is" or "with all faults."

A. The implied warranty of merchantability may also be excluded by language in the contract which mentions merchantability.

B. The implied warranty of fitness may be excluded by conspicuous, written provisions in the contract.
C. Where the buyer has examined or refused to examine the goods there are no implied warranties with respect to defects which such an examination should have disclosed.

X. Unless otherwise agreed, the seller warrants that his title to the goods is good, that its transfer is rightful, and that the goods are free of any rightful claims by third persons which are unknown to the buyer.

A. Special circumstances may exclude or modify the warranty of title if the buyer has reason to know that the seller does not claim title in himself or that he is purporting to sell only such right or title as he or a third person might have.

XI. Generally, risk of loss passes to the buyer upon tender or delivery by the seller.

A. But, if the seller is a merchant, risk of loss does not pass to the buyer until he has actually received the goods.

B. If the seller is required by the contract to deliver the goods at a particular destination, risk of loss does not pass to the buyer until the goods are tendered to the buyer at that destination.

C. But if the seller is merely required to ship the goods at the buyer's expense, risk of loss passes to the buyer when the goods are put in possession of the carrier.

D. Where the goods tendered do not conform to the contract, risk of loss remains with the seller until the defect is cured or the goods are actually accepted by the buyer.

E. If goods are identified when the contract is made, and an accidental loss is suffered before the risk passes to the buyer, the contract is avoided if the loss is total.

1. If such a loss is not total, the buyer may accept the damaged goods with an adjustment in price if he so desires.

XII. As a general rule, the buyer has a right to inspect the goods before acceptance or payment.

A. But the buyer is not entitled to inspection before payment if:

1. Delivery is C.O.D., or

2. The contract requires payment before inspection.

XIII. If the goods or tender of delivery fail to conform to the terms of the contract, the buyer may reject any or all of the goods.
A. The seller must be promptly notified if the goods are rejected.

B. The seller may cure a defective delivery if he notifies the buyer of his intention to do so and then makes a conforming delivery before the time for performance of the contract has expired.

C. A merchant buyer must follow any reasonable instructions from the seller for disposal of the goods, and must take reasonable steps to sell the goods on the seller's behalf if they are perishable.

1. If the seller gives no instructions, the buyer may

(a) store the rejected goods on behalf of the seller,

(b) sell them on his behalf or

(c) return them.

XIV. Once the goods are accepted they may not be rejected and the buyer is obligated to pay for them.

A. But if the buyer was reasonably induced to accept the goods without discovering that they were defective, he may revoke his acceptance.

1. The buyer must notify the seller of such revocation within a reasonable time after the defects are discovered or should have been discovered.

XV. Where the seller fails to deliver the goods, or to cure a defective delivery which has been rejected, the buyer may "cover" by purchasing substitute goods elsewhere.

A. The extra cost of the cover purchase may be recovered as damages from the seller.

XVI. If the seller has the goods but simply refuses to deliver them, and the buyer is unable to purchase substitute goods elsewhere, the buyer is entitled to obtain possession of the goods through a court order.

XVII. The measure of damages for non-delivery of suitable goods is the difference between the contract price and the market price for similar goods at the time when the buyer learned of the seller's breach.

A. The buyer is also entitled to incidental damages such as:

1. Reasonable expenses for the inspection, transportation and care of goods rightfully rejected.

2. Reasonable expenses incurred in making a cover purchase.

3. Injury to person or property caused by breach of warranty.
XVIII. If defective goods are accepted by the buyer he may still re­cover damages for breach of contract provided he promptly notifies the seller of the nonconformity.

A. The damages for goods accepted by the buyer which are not as warranted are the difference between the value of the goods as accepted and the value they would have had if they had been as warranted.

B. A buyer who has accepted defective goods may deduct the damages due him from the price provided he notifies the seller of his intention to do so.

XIX. If the buyer is insolvent, the seller may refuse to deliver the goods except for cash.

A. Goods already shipped to an insolvent buyer may be stopped in transit.

B. If an insolvent buyer has received goods on credit, the seller may reclaim them by making a demand within 10 days for their return.

XX. Once the buyer has accepted goods conforming to the contract they cannot be returned and he is obligated to pay the price when it becomes due.

A. The seller is also entitled to receive the price of identified goods which the buyer wrongfully refuses to accept.

1. But if the seller must first make a reasonable effort to resell the goods to someone else.

XXI. If the goods are resold because the buyer refuses to accept them, the seller may recover as damages the difference between the resale price and the contract price.

A. Resale of the goods may be at either public or private sale.

1. The goods being resold must be identified as referring to the breached contract.

2. A public resale must be made at a usual place or market for public sales.

3. The seller may enter the bidding at a public sale and himself become the buyer.

B. The seller must notify the buyer of the proposed resale.
XXII. The measure of damages for wrongful refusal by the buyer to accept the goods is the difference between the contract price and the market price at the time and place for delivery.

A. But if the contract involved standard priced goods, the seller may recover the profit which he would have made on the sale.

XXIII. Within reason, the parties may agree to additional or substitute remedies for breach of the contract.

XXIV. An action for breach of any contract for the sale of goods must be brought within four years after the breach occurs.
## INSURANCE COST OF STORED GRAIN

<table>
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<tr>
<th>Grain Value</th>
<th>Annual Cost Per Bushel</th>
<th>Six Month Cost Per Bushel</th>
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<td>$1.00</td>
<td>0.585</td>
<td>0.297</td>
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<td>2.00</td>
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<td>3.00</td>
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<td>4.00</td>
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<tr>
<td>5.00</td>
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Based on Rate of $5.85 Per $1,000
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<th>GRAIN VALUE PER BUSHEL</th>
<th>7% CENTS</th>
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<td>2.92</td>
<td>3.33</td>
<td>3.75</td>
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</table>
SELL CASH GRAIN AT HARVEST

ADVANTAGES

1. NO NEED FOR EXTENSIVE STORAGE ON FARM
2. MAINTENANCE OF QUALITY NOT PRODUCER RESPONSIBILITY
3. PROVIDES CASH AT HARVEST
4. ELIMINATION OF STORAGE SHRINK FOR PRODUCER

DISADVANTAGES

1. PRODUCER RARELY GETS SEASON HIGH PRICE AT HARVEST
2. CONGESTION OF TRANSPORTATION AND HANDLING FACILITIES
3. SOMETIMES LESS FLEXIBILITY IN ADJUSTING INCOME FOR TAX
4. PRODUCER LOSES CONTROL OF GRAIN FOR USE AS COLLATERAL
STORE GRAIN AT HARVEST FOR LATER SALE

ADVANTAGES

1. GENERALLY A GOOD RETURN FOR STORAGE

2. STORE AT ELEVATOR
   A. FEWER FACILITIES NEEDED
   B. RISK OF SHRINK AND QUALITY SHIFTED
   C. ESCAPE FROM EXTRA HANDLING

3. STORE AT FARM
   A. OFTEN SAVES TIME AND COST
   B. INSURES COMPETITIVE STORAGE COST

DISADVANTAGES

1. FARM STORAGE COSTS
   A. SHRINK
   B. MAINTENANCE OF QUALITY
   C. EXTRA HANDLING
   D. INTEREST ON CAPITAL INVESTED IN GRAIN
   E. FARM STORED GRAIN NOT ALWAYS ACCESSIBLE
CONTRACT CASH GRAIN
BEFORE HARVEST

ADVANTAGES

1. PRICE IS ESTABLISHED AHEAD OF HARVEST

2. PRODUCER USUALLY ASSURED OF OUTLET FOR GRAIN

3. CASH CONTRACT USUALLY MADE WITH LOCAL PERSON

4. CONTRACT CAN BE MADE IN ANY MULTIPLE

5. FREEDOM FROM MARGIN CALLS AND RE-OCCURRING CHARGES

6. CASH CONTRACT FOR SPECIFIC PRICE

DISADVANTAGES

1. REDUCES PRODUCER FLEXIBILITY

2. CASH CONTRACT MUST BE DELIVERED
RECOMMENDED ELEMENTS OF
CASH GRAIN CONTRACT

1. THE DATE AGREEMENT IS MADE - ALSO DATE SIGNED IF DIFFERENT
2. THE SELLING PRICE
3. THE AMOUNT OF BUSHELS SOLD
4. THE KIND OF GRAIN
5. QUALITY CONTRACT PRICE CALLS FOR
6. PLACE AND TIME OF DELIVERY
7. PENALTIES FOR EARLY OR LATE DELIVERY
8. ADJUSTMENTS FOR OVER OR UNDER DELIVERY
9. PREMIUMS AND GRADE DISCOUNTS
10. THE UNIFORM COMMERCIAL CODE
CONTRACTING GRAIN FOR DEFERRED PAYMENT

1. USUALLY FOR TAX ADVANTAGE

2. SEVERAL ADVANTAGEOUS SALES MAY OCCUR SAME YEAR

3. SOMETIMES SOLD GRAIN CAN EARN STORAGE FOR PRODUCER
DEFINITION OF TERMS PECULIAR TO
GRAIN FUTURES TRADING

1. BASIS

2. LOCALIZED FUTURES PRICE

3. OFFSETTING CONTRACT

4. TO ARRIVE PRICE

5. HEDGE

6. CASH PRICE

7. SHORT SALE

8. LONG SALE
FORWARD PRICE GRAIN BY USING FUTURES

ADVANTAGES

1. FUTURES GENERALLY OFFER LONGER TIME TO CHOOSE PRICE
2. FUTURES MAY REPRESENT HIGHER PRICE THAN CASH PRICES
3. USUALLY SIMPLER TO OFFSET IN CASE OF CROP FAILURE
4. USUALLY SIMPLER TO ADJUST TO CHANGING CONDITIONS
5. INCREASES BUYERS IN DOMESTIC AND EXPORT MARKET

DISADVANTAGES

1. MARGIN DEPOSIT OF ABOUT 15% OF VALUE REQUIRED
2. ADDITIONAL MARGINS MAY BE REQUIRED IF MARKET MOVES CONTRARY TO EXPECTATIONS
3. FUTURES CONTRACTS USUALLY ONLY IN MULTIPLES OF 5,000 BU.
4. EXPECTED PRICE BASED ON HISTORICAL RELATIONSHIPS
5. NOT ALL GRAINS TRADED IN FUTURES CONTRACTS

6. LOCAL CASH-FUTURES PRICE RELATIONSHIP MUST BE KNOWN

7. GREATER SPECULATOR INFLUENCE

8. FUTURES TRADING REQUIRES TRAINING

9. CASH GRAIN SELDOM DELIVERED TO SATISFY FUTURES CONTRACT
**SHORT TRADE - PRICE RISE**

<table>
<thead>
<tr>
<th>Date</th>
<th>Action</th>
<th>Quantity</th>
<th>Price</th>
<th>Margin Deposit</th>
<th>Balance</th>
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<tbody>
<tr>
<td>March 1</td>
<td>Sell 5000 Bu. of ___ Sept. Wheat @ $4.00</td>
<td></td>
<td></td>
<td>$2,500.00</td>
<td></td>
</tr>
<tr>
<td>July 10</td>
<td>Buy 5000 Bu. of ___ Sept. Wheat @ $4.20</td>
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<td></td>
<td></td>
<td>$1,000.00</td>
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<tr>
<td></td>
<td>Loss in Futures 20¢ x 5000 Bu.</td>
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<td>$1,000.00</td>
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<tr>
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<td>Broker's Commission</td>
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<td>Account Balance July 10</td>
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<td>$1,470.00</td>
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</tbody>
</table>
SHORT TRADE - PRICE DECLINE

MARCH 1  SELL 5000 BU. OF _____ SEPT. WHEAT @ $4.00  MARGIN DEPOSIT $2,500.00

JULY 1  BUY 5000 BU. OF _____ SEPT. WHEAT @ $3.80  GAIN IN FUTURES 20¢ x 5000 BU. = + $1,000.00

BROKER'S COMMISSION - $ 30.00

ACCOUNT BALANCE JULY 10 $3,470.00
LONG TRADE - PRICE RISE

AUG. 10  BUY 5,000 BU. _____ MARCH WHEAT a $4.15

MARGIN DEPOSIT $2,500.00

DEC. 20  SELL 5,000 BU. _____ MARCH WHEAT a $4.30

GRAIN IN FUTURES 15¢ x 5000 BU. = +$ 750.00

BROKER’S COMMISSION -$ 30.00

DEC. 20 ACCOUNT BALANCE $3,220.00
LONG TRADE - PRICE DECLINE

AUG. 10  BUY 5,000 BU. MARCH WHEAT @ $4.15
MARGIN DEPOSIT $2,500.00

DEC. 20  SELL 5,000 BU. MARCH WHEAT @ $4.00
LOSS IN FUTURES 15¢ x 5000 BU. -$ 750.00

BROKER'S COMMISSION -$ 30.00

DEC. 20 ACCOUNT BALANCE $1,720.00
<table>
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<tr>
<th>Date</th>
<th>Mpls. Cash 13 Pro HRS-W</th>
<th>Mpls. Sept. Wheat Futures</th>
<th>Mpls. Basis</th>
<th>Freight-Hometown To Minneapolis</th>
<th>Hometown Basis</th>
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<td>1969</td>
<td></td>
<td></td>
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<tr>
<td>Aug. 15</td>
<td>1.57</td>
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<td>2 OVER</td>
<td>14¢ Per Bu.</td>
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<td>1.63</td>
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<td>1970</td>
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<td>11 UNDER</td>
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<td>1971</td>
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</tr>
<tr>
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<td>1.55</td>
<td>3 UNDER</td>
<td>16¢ Per Bu.</td>
<td>19 UNDER</td>
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<tr>
<td>Sept. 1</td>
<td>1.54</td>
<td>1.54</td>
<td>EVEN</td>
<td></td>
<td>16 UNDER</td>
</tr>
<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>5 UNDER</td>
<td>17¢ Per Bu.</td>
<td>22 UNDER</td>
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<tr>
<td>Sept. 1</td>
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<td>1.95</td>
<td>3 UNDER</td>
<td></td>
<td>20 UNDER</td>
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<tr>
<td>1973</td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Aug. 15</td>
<td>4.57</td>
<td>4.73</td>
<td>16 UNDER</td>
<td>18¢ Per Bu.</td>
<td>34 UNDER</td>
</tr>
<tr>
<td>Sept. 1</td>
<td>4.43</td>
<td>4.43</td>
<td>EVEN</td>
<td></td>
<td>18 UNDER</td>
</tr>
<tr>
<td>1974</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Aug. 15</td>
<td>4.78</td>
<td>4.77</td>
<td>1 OVER</td>
<td>19¢ Per Bu.</td>
<td>18 UNDER</td>
</tr>
<tr>
<td>Sept. 1</td>
<td>4.80</td>
<td>4.70</td>
<td>10 OVER</td>
<td></td>
<td>9 UNDER</td>
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</table>
FORWARD PRICE GRAIN BY USING FUTURES—SELL CASH GRAIN AT HARVEST

STEPS

1. DETERMINE APPROXIMATE CASH PRICE REPRESENTED BY FUTURE (LOCALIZE FUTURES)

2. SELECT THE APPROPRIATE CROP FUTURE

3. SELL THE FUTURE IN THE APPROPRIATE AMOUNT

4. SELL CASH GRAIN — SAME DAY

5. "BUY BACK" FUTURES
FORWARD PRICE WHEAT BY USING FUTURES AND SELL CASH WHEAT AT HARVEST

Example 1

*JULY 5. SELL 5000 BU. OF MINNEAPOLIS DEC. WHEAT @ $2.62

HISTORY INDICATES THIS REPRESENTS ABOUT $2.32 IN LOCAL CASH PRICE.
TO ARRIVE BID FOR CASH WHEAT IS $2.37 BUT DELIVERY MUST BE GUARANTEED FOR SEPT. 1 ARRIVAL.

SEPT 6. HARVESTED, DELIVERED AND SOLD 5000 BU. OF CASH WHEAT @ $4.09

SEPT 6. BOUGHT 5000 BU. OF MINNEAPOLIS DEC. WHEAT (OFFSETTING CONTRACT) @ $4.39

SOLD DEC. WHEAT FOR $2.62 - BOUGHT DEC. WHEAT FOR $4.39,
LOSS PER BU. = $1.77

GROSS PRICE FOR WHEAT $2.32

*ACTUAL 1973 PRICE CONDITIONS.
### Example 2

#### CASH

<table>
<thead>
<tr>
<th>Date</th>
<th>Description</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>JULY 5</td>
<td>Cash Wheat Value</td>
<td>$2.32</td>
</tr>
<tr>
<td>JULY 17</td>
<td>Cash Wheat Value</td>
<td>$2.21</td>
</tr>
<tr>
<td>JULY 17</td>
<td></td>
<td></td>
</tr>
<tr>
<td>SEPT 6</td>
<td>Sold Cash Wheat</td>
<td>$4.09</td>
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</tbody>
</table>

#### FUTURES

<table>
<thead>
<tr>
<th>Date</th>
<th>Description</th>
<th>Price</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Sell 5,000 Bu. Minneapolis December Wheat @ $2.62</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Buy 5,000 Bu. Minneapolis December Wheat @ $2.52 (Offset Contract) Gain 10¢</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Buy Additional 5,000 Bu. Minneapolis December Wheat @ $2.52 (Long Contract)</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Sell 5,000 Bu. Minneapolis December Wheat @ $4.39 Futures Gain $1.87</td>
<td></td>
</tr>
</tbody>
</table>

**Total Price for Wheat**:

- $4.09
- $1.87
- $1.87
- $6.06
Example 3

*AUG. 14 SELL 5,000 BU. OF CHICAGO NOVEMBER SOYBEANS @ $9.01

HISTORY INDICATES THIS NORMALLY REPRESENTS ABOUT $8.61 IN LOCAL CASH PRICE

PRESENT CASH BEAN TO ARRIVE PRICE $8.40

OCT. 12 HARVESTED AND STORED 5,000 BU. OF CASH BEANS

PRESENT MARKET PRICE $5.50

OCT. 12 BOUGHT 5,000 BU. OF CHICAGO NOVEMBER SOYBEANS @ $6.29 (OFFSETTING CONTRACT) FUTURES GAIN PER BU. $2.72

*ACTUAL 1973 PRICES CONDITIONS
### Example 4

**1972-73 Corn Crop Year**  
*(Actual Prices for a Location)*

<table>
<thead>
<tr>
<th>Date</th>
<th>Action</th>
<th>Price</th>
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<tr>
<td>Dec. 1</td>
<td>Stored Cash Corn</td>
<td>$1.33</td>
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<tr>
<td></td>
<td>sold Chicago July Futures</td>
<td>$1.53</td>
</tr>
<tr>
<td>Jan. 15</td>
<td>Sold Cash Corn</td>
<td>$1.41</td>
</tr>
<tr>
<td></td>
<td>Bought Chicago July Futures</td>
<td>$1.41</td>
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</table>

Gain in Cash: 8¢ per bu.  
Gain in Futures: 12¢ per bu.
FIGURE 1. WAYS THE "BASIS" MAY NARROW AND CREATE PROFIT AND PROTECTION FROM HEDGE.
TRANSFERRED SPECULATION FROM CASH GRAIN TO FUTURES

REASON FOR USING ALTERNATIVE

1. MAY BE NO STORAGE AVAILABLE

2. URGENT NEED FOR CASH FROM GRAIN SALE

3. DESIRE TO ESCAPE SHRINK AND TAXES

4. GRAIN NOT OF STOREABLE QUALITY

PROCEDURE

SELL GRAIN - BUY EQUAL AMOUNT OF GRAIN FUTURES

SELL GRAIN FUTURES ANYTIME BEFORE TERMINATION DATE
GUIDES FOR SUCCESSFUL USE IN TRANSFERRING CASH INVENTORY RISK TO FUTURES

1. NORMAL CASH - FUTURES RELATIONSHIPS MUST BE KNOWN

2. MUST BE EVIDENCE BOTH CASH AND FUTURES WILL RISE

3. REPLACE CASH GRAIN WITH FUTURES AT TIME OF NORMAL OR NARROW BASIS

4. MOST YEARS FUTURES GO UP HALF AS MUCH AS CASH PRICES
<table>
<thead>
<tr>
<th>Year</th>
<th>Kansas City May Future</th>
<th>Kansas City Cash Wheat</th>
<th>Futures Change</th>
<th>Cash Change</th>
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<tbody>
<tr>
<td>1970-71</td>
<td></td>
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<td></td>
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<tr>
<td>July 1</td>
<td>1.40</td>
<td>1.34</td>
<td>+20</td>
<td>+24</td>
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<tr>
<td>Oct. 1</td>
<td>1.60</td>
<td>1.58</td>
<td>+15</td>
<td>+30</td>
</tr>
<tr>
<td>Jan. 1</td>
<td>1.55</td>
<td>1.64</td>
<td>+8</td>
<td>+26</td>
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<tr>
<td>Mar. 1</td>
<td>1.48</td>
<td>1.60</td>
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<tr>
<td>71-72</td>
<td></td>
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<td></td>
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<tr>
<td>July 1</td>
<td>1.52</td>
<td>1.59</td>
<td>-12</td>
<td>-2</td>
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<tr>
<td>Oct. 1</td>
<td>1.40</td>
<td>1.57</td>
<td>-5</td>
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<tr>
<td>Jan. 1</td>
<td>1.47</td>
<td>1.57</td>
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<td>-1</td>
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<tr>
<td>Mar. 1</td>
<td>1.47</td>
<td>1.58</td>
<td></td>
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</tr>
<tr>
<td>72-73</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>July 1</td>
<td>1.51</td>
<td>1.56</td>
<td>+54</td>
<td>+62</td>
</tr>
<tr>
<td>Oct. 1</td>
<td>2.06</td>
<td>2.18</td>
<td>+93</td>
<td>+1.17</td>
</tr>
<tr>
<td>Jan. 1</td>
<td>2.44</td>
<td>2.73</td>
<td>+75</td>
<td>+1.05</td>
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<tr>
<td>Mar. 1</td>
<td>2.26</td>
<td>2.61</td>
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<tr>
<td>73-74</td>
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<td></td>
<td></td>
</tr>
<tr>
<td>July 1</td>
<td>2.54</td>
<td>2.65</td>
<td>+2.06</td>
<td>+2.13</td>
</tr>
<tr>
<td>Oct. 1</td>
<td>4.60</td>
<td>4.78</td>
<td>+2.54</td>
<td>+2.81</td>
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<tr>
<td>Jan. 1</td>
<td>5.08</td>
<td>5.46</td>
<td>+2.94</td>
<td>+3.07</td>
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<tr>
<td>Mar. 1</td>
<td>5.48</td>
<td>5.72</td>
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</tr>
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</table>
SHORT TERM FUTURES HEDGE

Example 5

FEB. 1  SPOT MARKET FOR 13 PROTEIN WHEAT LOCALIZED $3.07 TO ARRIVE
FEB. 1  SOLD MARCH FUTURES at $3.18
13 PROTEIN WHEAT $3.00 TO ARRIVE MARKET FOR

FEB. 6  WHEAT ARRIVED AND
       WAS SOLD FOR A LOCALIZED PRICE
       OF $2.90

       TO ARRIVE PRICE $2.83

TOTAL PRICE FOR 13 PROTEIN WHEAT SOLD ON THE SPOT MARKET FEB. 6 WAS $2.90 + 16 CENT GAIN ON FUTURES HEDGE OR A PRICE OF $3.06 LESS FUTURES COMMISSION
OTHER MARKETING ALTERNATIVES

1. ANIMAL FEED

2. SELL THROUGH COOPERATIVE

3. POOL GRAIN

4. CONTRACT GROWING LARGER UNIT

5. SPECIALITY CROPS

6. SEED

7. CONSIGN TO GRAIN MERCHANT

8. SELL DIRECT

9. PRODUCER - PROCESSOR PROFIT SHARING
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<td>VIII. Forward Price Grain and Store at Harvest</td>
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