

# CROP MARKETING STRATEGIES

IOWA STATE UNIVERSITY  
University Extension



JUNE 2006

VOLUME 6

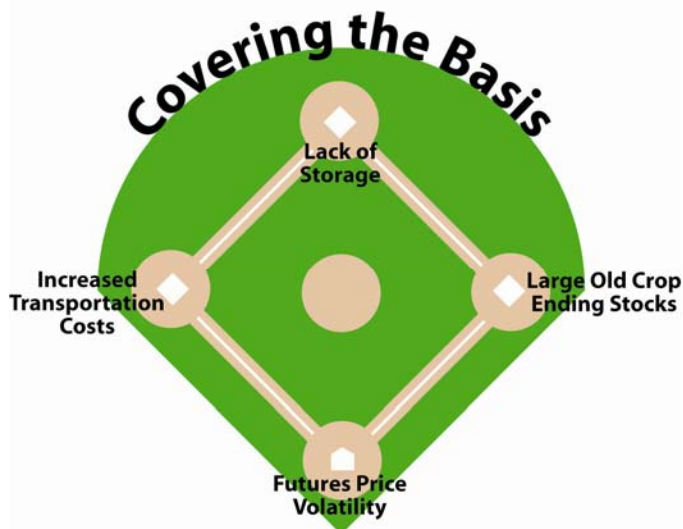
## Understanding Crop Basis

One of the most predictable price movements for both the corn and soybean markets is that of basis (difference between the local cash price and the nearby futures price). Basis should reflect a more localized supply and demand for both corn and soybeans. It does vary by geography and related costs of storage, transportation, and processor demand. Also, producer's price and basis outlook, as well as their own cash flow needs, influences basis.

When basis is deemed to be "wide" the difference between cash and futures price is larger. Unless cash prices are extremely high, most producers don't like to sell their cash grain when basis is wide. A narrow basis means this difference is smaller, a benefit to the producer unless cash prices are low.

So, for most of 2006, why has the basis been so wide? Several reasons come to mind:

- 1) the U.S. corn and soybean ending stocks for the 2005-06 crop marketing year is large
- 2) most commercial storage facilities across Iowa and the Corn Belt remain at or near capacity
- 3) higher energy prices for transporting grain to a processor is being passed on to the producer through a wider basis



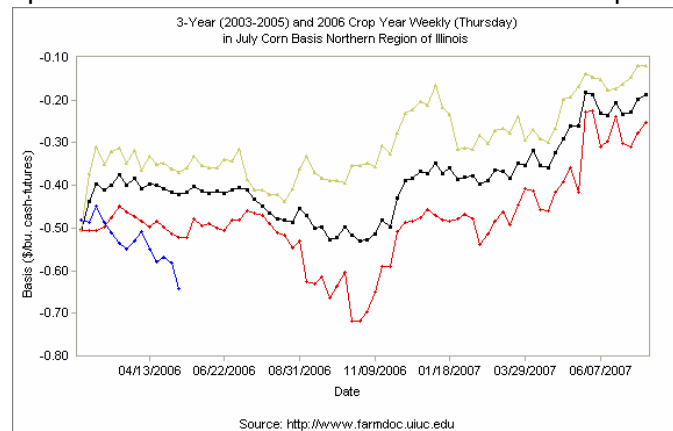
- 4) and extreme futures price volatility, especially in the corn market, as high futures prices and large carries for the deferred months reward delivery of corn at some point and time in future.

## Cost of Ownership

Unfortunately, producers face cost of ownership for storing grain, cash flow needs and availability for additional storage capacity as harvest approaches. A typical cost for storing corn and soybeans commercially is about 4 cents per bushel per month. On-farm storage is typically half of this amount, but slightly higher when storage structures are financed. The total U.S. storage capacity for grain has not seen significant expansion since the mid 1980s. Large Iowa crops the past 2 years resulted in higher volumes of Iowa's corn crop being stored out-of-doors at local elevators. Thus, large ending stocks have resulted in wider basis. However, growing U.S. demand for bio-fuels means processing corn and soybeans locally will likely result in the need for more storage facilities for both corn and soybeans.

## Seasonal Basis Patterns

In order to better understand basis, consider collecting at least weekly basis information from your local market place. This data should be collected for at least the 3 most recent years with a specific futures contract month and local cash price



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recorded for the same day of the week. Consider creating a line graph to express basis with price on the y axis and the time of year on the x axis. The result can be a useful seasonal basis pattern to help time cash sales.

Using at least 3 years of recent data allows for a maximum, minimum, average and current basis to be viewed. Note above in the example “old crop corn basis” using July corn futures that the 2006 basis is “wider” as compared to recent years. More importantly, the seasonal basis pattern is for basis to remain flat during the early part of summer, but then to “widen” by late June and into the harvest low that typically occurs in October or early November.

## Old Crop Basis

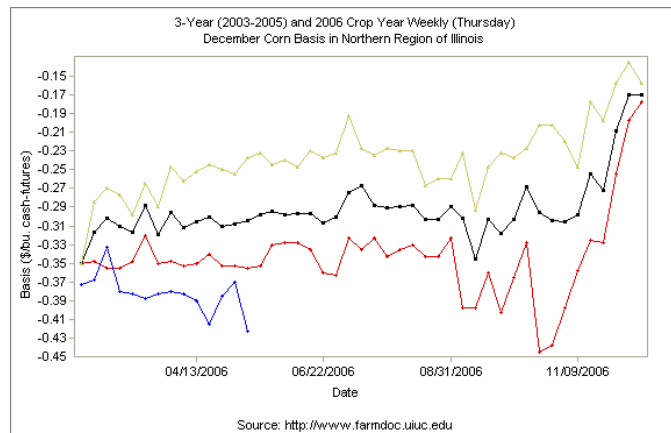
Should most of the Corn Belt see normal growing conditions this late spring and summer, expect the old crop basis to continue to be “wide.” Thus, the reflection of basis would mean committing bushels to delivery prior to the likely “widen basis” in July through October. Producers that think basis will remain wide, but futures price will increase, might want to consider committing those bushels to delivery, but retaining ownership via a long futures or call option strategy.

With U.S. ending corn stocks projected at 2.246 billion bushel as of September 1<sup>st</sup>, 2006, the supply of corn is large enough to keep basis wide throughout most of the Corn Belt. A threat to the 2006 growing crop might provide a “narrowing of basis” opportunities, but for new crop delivery of corn after harvest.

## New Crop Basis

The new crop corn basis using the December corn futures contracts over the past few years has similar characteristics to that of old crop corn basis. The 2006 basis featured on the graph is much wider than recent years and the trend is for basis to remain flat until late June to early July. A narrowing of basis is likely reflecting a threat to the growing crop. Once the threat passes, then basis tends to widen from mid-summer into harvest. The graphic reflects the widest basis at harvest in October with rapid basis improvement in late November. However, the availability of storage will likely be

needed to take advantage of this “narrowing” of basis.



## Conclusion

Basis is an important consideration for cash marketing of both corn and soybeans. Its movement in the local cash market is much more predictable than that of the nearby futures price. A local basis should reflect supply and demand for corn and soybeans in that particular market. It does vary geographically as well as the time of the year.

To best utilize local basis information, consider collecting this data weekly from your local market for at least the 3 most recent years is important. Continue to update this data as the reflection of large ending stocks for both corn and soybeans provide a challenge this year of “wide” basis. The growing demand base emerging with the bio-fuels industry will likely mean changes in local basis in then next few years. Understanding crop basis will allow for producers to improve their ability to better time both future price decisions in conjunction with basis considerations.

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