Using Crop Contracts

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Using Various Crop Contracts

• Important to understand contracts
  – What they are designed to do
  – What they are not designed to do
• Separate the basis and price decision
• Using various crop contracts over a period of time offers risk management diversity.
Crop Marketing Matrix

1. Store & wait
2. Delayed price contract
3. Minimum price contract

Futures Price

Up

1. Basis contract
2. Sell Cash Bushels and Buy Futures or Call Option
3. Minimum price contract

Basis

Expected Change

Strengthen

1. Hedge
2. Non-roll hedge to arrive
3. Buy put option

Weak

Down

1. Cash sale now
2. Forward Contract

Let’s talk about a Basis Contract

Advantages:
1. Open to higher prices
2. Basis set and won’t deteriorate
3. May reduce storage costs
4. Convenient contract quantities
5. Perhaps partial payment in advance

Disadvantages:
1. Price risk until the crop price is set
2. No basis improvement
3. May need to pay back advance
4. Unsecured creditor to buyer
5. Market knowledge needed (price and basis)
Crop Marketing Matrix

1. Store & wait
2. Delayed price contract
3. Minimum price contract

Basis

1. Hedge
2. Non-roll hedge to arrive
3. Buy put option

Futures Price

1. Basis contract
2. Sell Cash Bushels and Buy Futures or Call Option
3. Minimum price contract

Expected Change

1. Cash sale now
2. Forward Contract

Basis

1. Basis risk is still present
2. Delivery is required
3. Must be done in specific contract size (5,000 bu.)
4. Seller may not have margin calls, but check the contract
5. Will not get a higher futures price
6. Market knowledge needed (price and basis)

Advantages:
1. Futures price is set
2. Basis can improve
3. Probably higher fees than selling futures
4. Seller may not have margin calls, but check the contract
5. May move protection forward within same marketing year

Disadvantages:
Key points:

- Read and Understand all the contracts you use.
- Use the right contract for the right, current conditions
- Separate the basis and price decision
- Vary the crop contracts over a period of time – not all your “eggs in one basket”.

Thanks for joining the