



# Basic Grain Marketing Workshop & Market Outlook

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Alliant Energy Center-Madison, WI.

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# Agenda

- Price and its components
- How do we sell Price?
- What is a hedger?
- What is hedging?
- The Hedger's toolbox
- Who do I "hedge" with?
- Examples
- Market Outlook for Corn, Beans & Wheat



# What is PRICE ?

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# For a horror movie



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# For a game show



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# For starting pitching

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# The Components of Price

**Futures** – the price of a commodity determined via a futures exchange through world wide price discovery

**Basis** – the difference between the futures price and the local cash price for a commodity



# How do we sell “Price”?

- We sell the “price” at the co-op
  - Made up of “futures + basis”
- We sell the “futures” portion only
  - Like a HTA
- We sell the “basis” portion only
  - Like a “basis fix” contract



# Your Role as a Hedger

- Manage risk responsibly and profitably
- Become a student of the markets
- Understand the marketing tools and concepts needed to succeed
- Use discipline in your hedging approach
- Be willing to evolve your marketing practices





# What is Hedging?

In its simplest form: “ Hedging” is making a transaction which offsets the risk of another, such as **growing a crop and selling futures.**

**Hedging is temporary,  
held until we actually SELL the crop**

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# Time to learn



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# What is Hedging ?

## T Exercise

| Expected production/ownership | Cash sales/futures sales |
|-------------------------------|--------------------------|
|                               |                          |

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# Understanding Futures

- Functions
- Price Discovery – Futures reflect the world situation for a specific commodity at a delivery point
  - S&D: current crop production, world ag policies, world S&D, carryouts, weather, etc.
  - Investor desires



# Futures are a .....

- Price Prediction
  - Futures are the expectations of both buyers and sellers, reflecting price ideas for today, tomorrow, next month, next year (or beyond)
  - Futures are a worldwide event now
  - Futures move faster than ever before



# Futures are a ...

- Risk Management Tool
  - Futures can be used to reduce market risk
  - Conversely, risk can be increased also
  - We have plenty of other things to worry about
    - let's not spend a lot of time worrying over futures



# The CBOT

- Founded in 1848
- Merchants looking to centralize grain trade
- Early on meant only “to-arrive” contracts
- By 1865, “standardized agreements” developed called futures contracts
- Serves as a clearinghouse for buyer and seller, allowing easy entry and exit
- Imagine a marketplace without futures



# Futures Market Participants

**Hedger** - Buys or sells futures to eliminate price risk

**Speculator** - Buys or sells futures, taking on risk, in hopes of gaining profit

- Speculative traders add liquidity to the markets so the markets can function better. Allows easy entry and exit.



# Seasonality

December Corn Futures 15 Year Seasonal



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# Tools of Hedging

There are two general categories of tools to manage risk.

## 1) Exchange-offered Contracts

- Futures Contract
- Mini Futures Contracts
- Options Contracts (no mini's here, sorry)

## 2) Contracts offered OTC (Over The Counter)

- Averaging Contract
- Builder Contracts
- Premium Contracts



# Basis

Basis is affected by many things, but the two biggest factors are:

- What does it cost for a recipient to get the grain to the market (Transportation)?
  - Price can fluctuate, sometimes wildly
- How badly does the market want the grain (Demand)?
  - This concept is straightforward; buyers will bid a higher basis if they need grain and lower if they don't.
  - Has seasonality and historical ranges



# What is an Option ?

- **Buying an option** gives you the right, but not the obligation, to buy or sell the underlying futures contract at a certain price for a limited amount of time.
- It is best to compare it to an ***insurance policy***. You pay a premium for “a right” and protection while the seller collects the premium and assumes “the risk.”
- Value is determined via bid/ask system.



# Types of Options

- **Call:** Gives the buyer the right, but not the obligation, to go long the underlying futures contract at a specific price.
  - “upside” futures insurance
- **Put:** Gives the buyer the right, but not the obligation, to go short the underlying futures contract at a specific price.
  - “downside” futures insurance



# Option Facts

- Can be offset, exercised or left to expire
- No margins required when initially bought (versus initially sold)
- Option buyer has rights and pays premium
- Seller gets paid (premium) but has risk
- Each option has value, expiration and strike
- Options are tied to an underlying future



# Options = an Insurance Policy

- Option BUYER (Policy Holder)
  - Pays premium
  - Receives right to reimbursement if risk occurs
- Option SELLER (Policy Writer)
  - Receives premium
  - Takes on obligation to reimburse policy holder if risk occurs and policy holder files claim



# Who do I work with?

- Find someone you are comfortable with
  - Local co-op
  - A commodity broker
- Realize your choices are many and can vary
  - And so will what they can do for you and what they will charge





# Minimum Price Strategies

- **Minimum Price Contract**
  - Call option purchase tied to a spot or forward sale. Widely offered.
    - Minimum price = Sale price less Call option purchase price.
  - Put option purchase places a floor with no cash obligation.



# Call Option - example

- CH16 trading at \$3.75. Cash corn is -35H, or \$3.40.
- Producer sells cash corn for spot delivery.
- Buys a CH16 \$3.80 call option for \$.10.
- The “min” cash floor is  $\$3.40 \text{ minus } \$.10 = \$3.30$ .
- Call expires 2/19/2016
- Advantage: A minimum cash price for corn has been established; futures upside is left open.
- Disadvantage: The cost of option, basis is set.



# Put Option - example

- CH16 futures trading at \$3.75
- Buy a CH16 \$3.70 put option for \$.10
- The put acts as a “substitute” hedge
- Futures “floor” is \$3.70 futures minus \$.10 = \$3.60
- Advantages: futures upside left open and no cash obligation. Basis not “set” yet.
- Disadvantage: “true” floor is under current futures price. Basis not “set” yet.
- When we “sell” the grain, we would “sell” the put.



# Remember

- “Price” is more than a price
- Hedging works
- Futures/options perform many functions
- Our markets offer many risk management tools for your use
- There are good, knowledgeable people around to help you - find them, use them
- Re-invent yourself, as needed



# Corn Outlook

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# U.S. Corn Supply/Demand

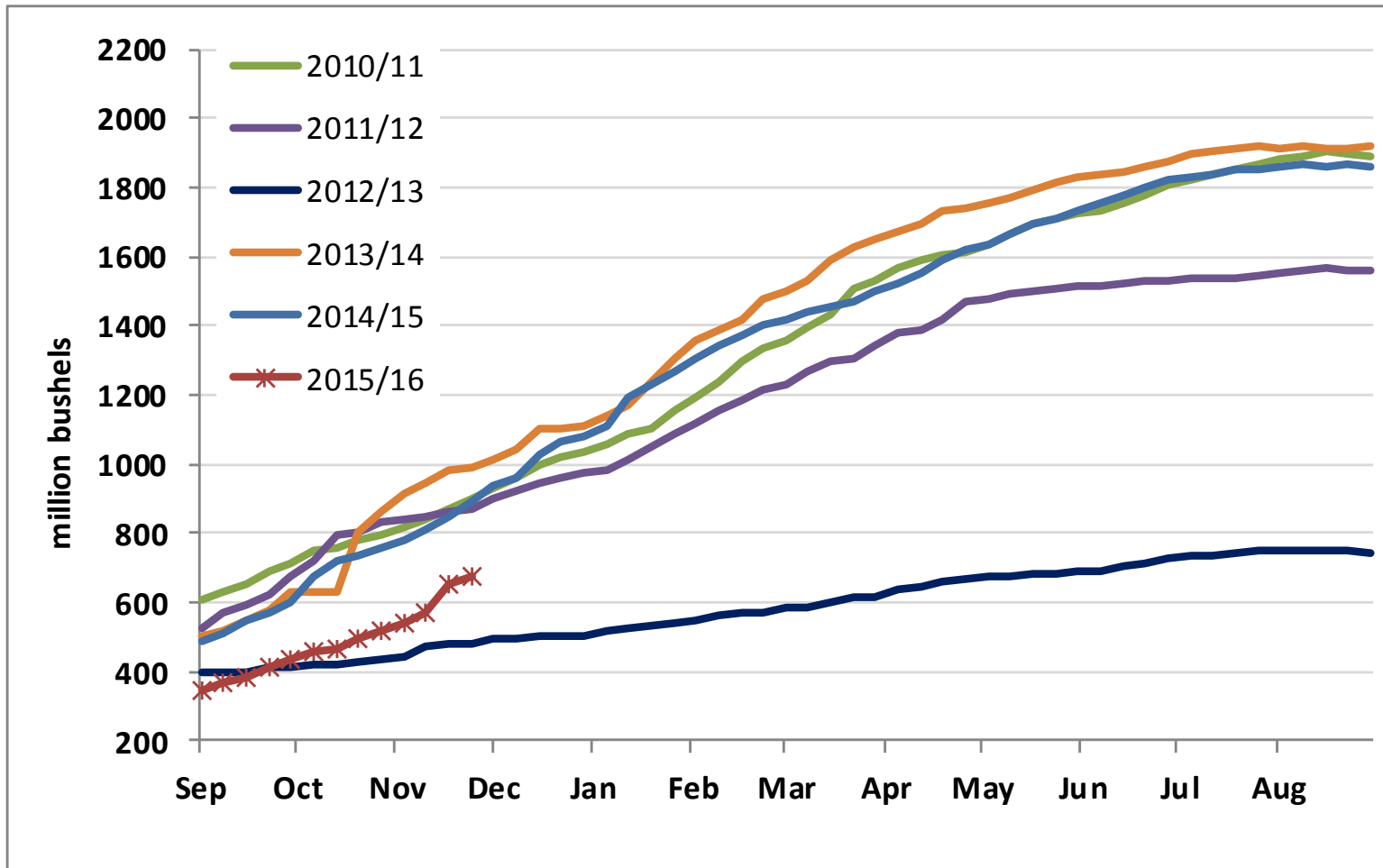


|                      | <u>2009/2010</u> | <u>2010/2011</u> | <u>2011/2012</u> | <u>2012/2013</u> | <u>2013/2014</u> | <u>2014/2015</u> | <u>2015/2016</u> |
|----------------------|------------------|------------------|------------------|------------------|------------------|------------------|------------------|
| Planted Acres        | 86.4             | 88.2             | 91.9             | 97.3             | 95.4             | 90.6             | 88.4             |
| Harvested Acres      | 79.5             | 81.4             | 83.9             | 87.4             | 87.5             | 83.1             | 80.7             |
| Yield                | 164.7            | 152.6            | 146.8            | 123.1            | 158.1            | 171.0            | 169.3            |
| Beginning Stocks     | 1673             | 1708             | 1128             | 989              | 821              | 1232             | 1731             |
| Production           | 13092            | 12425            | 12314            | 10755            | 13829            | 14215            | 13653            |
| Imports              | 8                | 28               | 29               | 160              | 36               | 32               | 30               |
| Total Supply         | 14773            | 14161            | 13471            | 11904            | 14686            | 15479            | 15415            |
| Feed/Residual        | 5126             | 4777             | 4518             | 4315             | 5040             | 5315             | 5300             |
| Food/Seed/Industrial | 5961             | 6425             | 6424             | 6038             | 6493             | 6568             | 6580             |
| Ethanol              | 4591             | 5019             | 5000             | 4641             | 5124             | 5209             | 5200             |
| Domestic Use         | 11087            | 11202            | 10943            | 10353            | 11533            | 11883            | 11880            |
| Exports              | 1979             | 1831             | 1539             | 730              | 1920             | 1864             | 1750             |
| Total Use            | 13066            | 13033            | 12482            | 11083            | 13454            | 13748            | 13630            |
| Ending Stocks        | 1708             | 1128             | 989              | 821              | 1232             | 1731             | 1785             |
| Stocks/Use           | 13%              | 9%               | 8%               | 7%               | 9%               | 13%              | 13%              |

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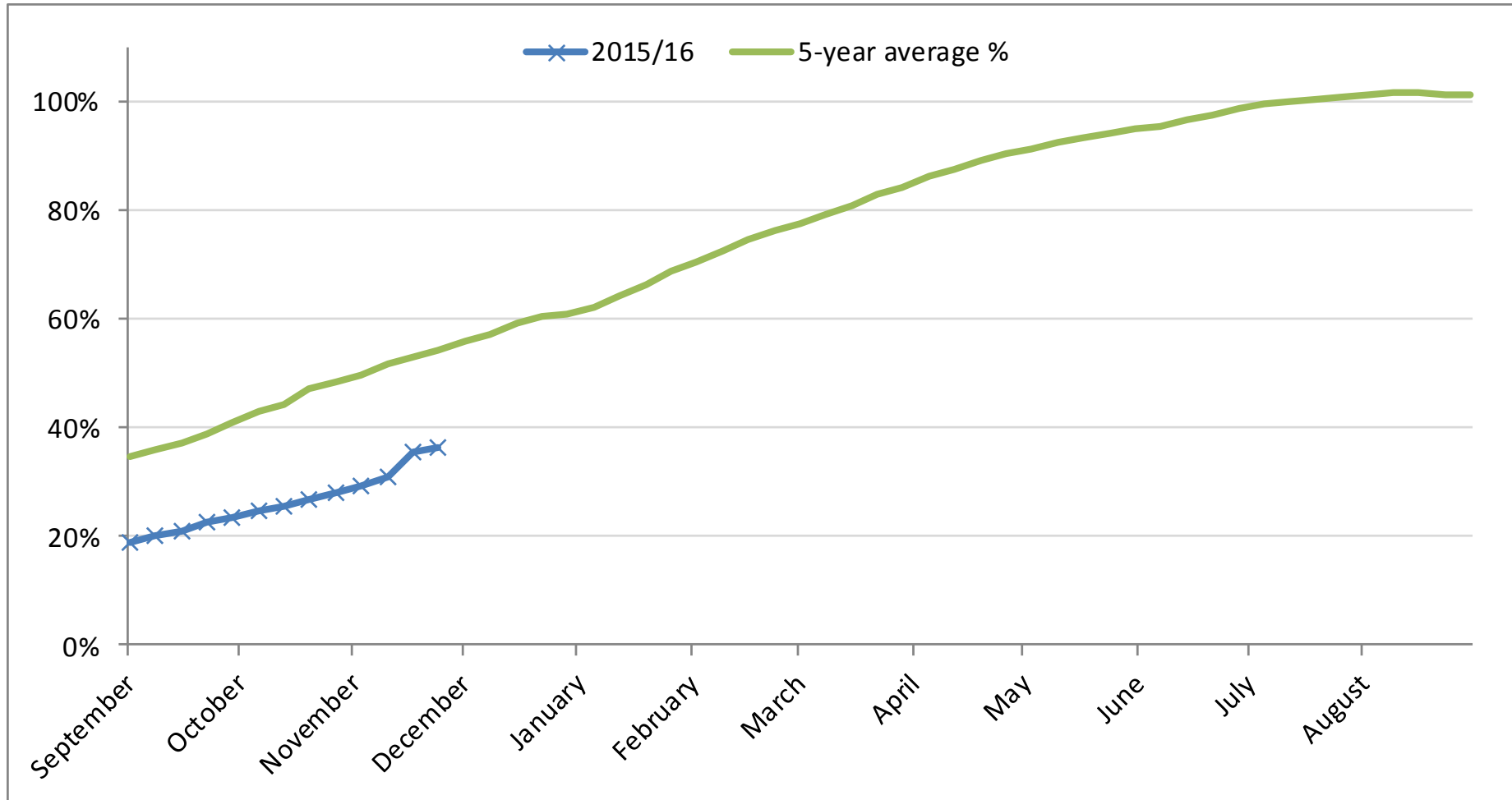
# U.S. Corn Export Commitments



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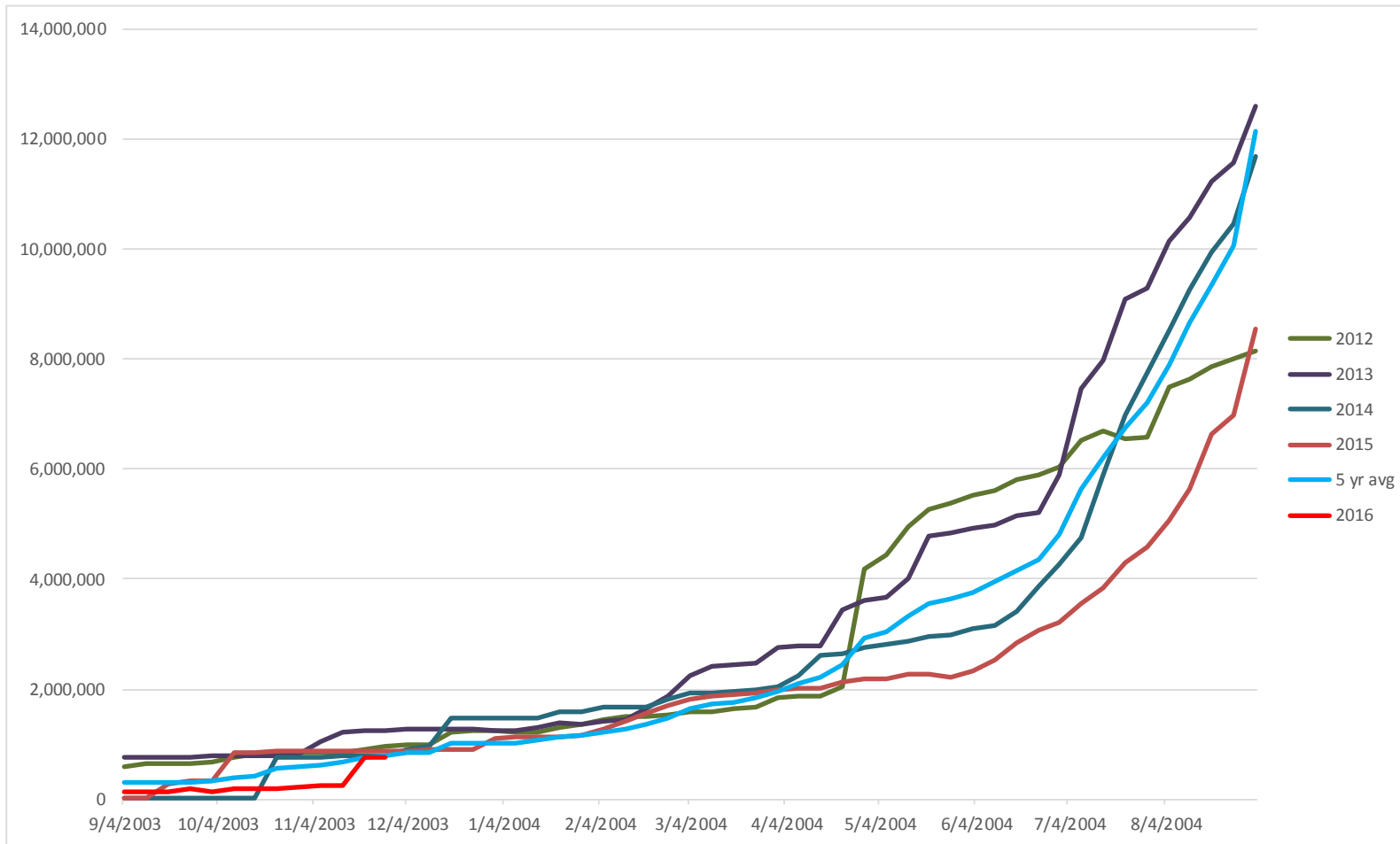


# Export Commitments: % of Final



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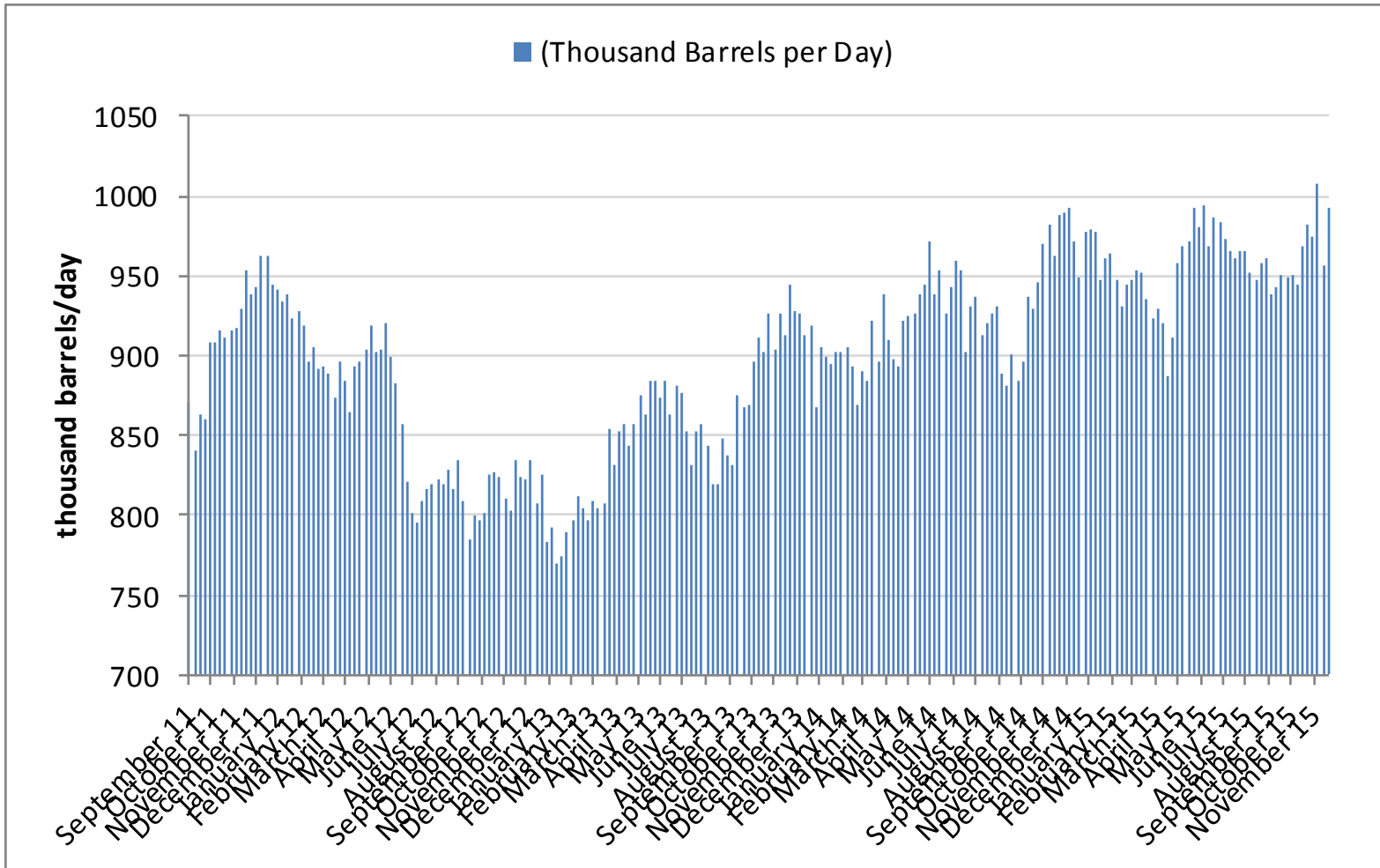
# Next Marketing Year Export Sales



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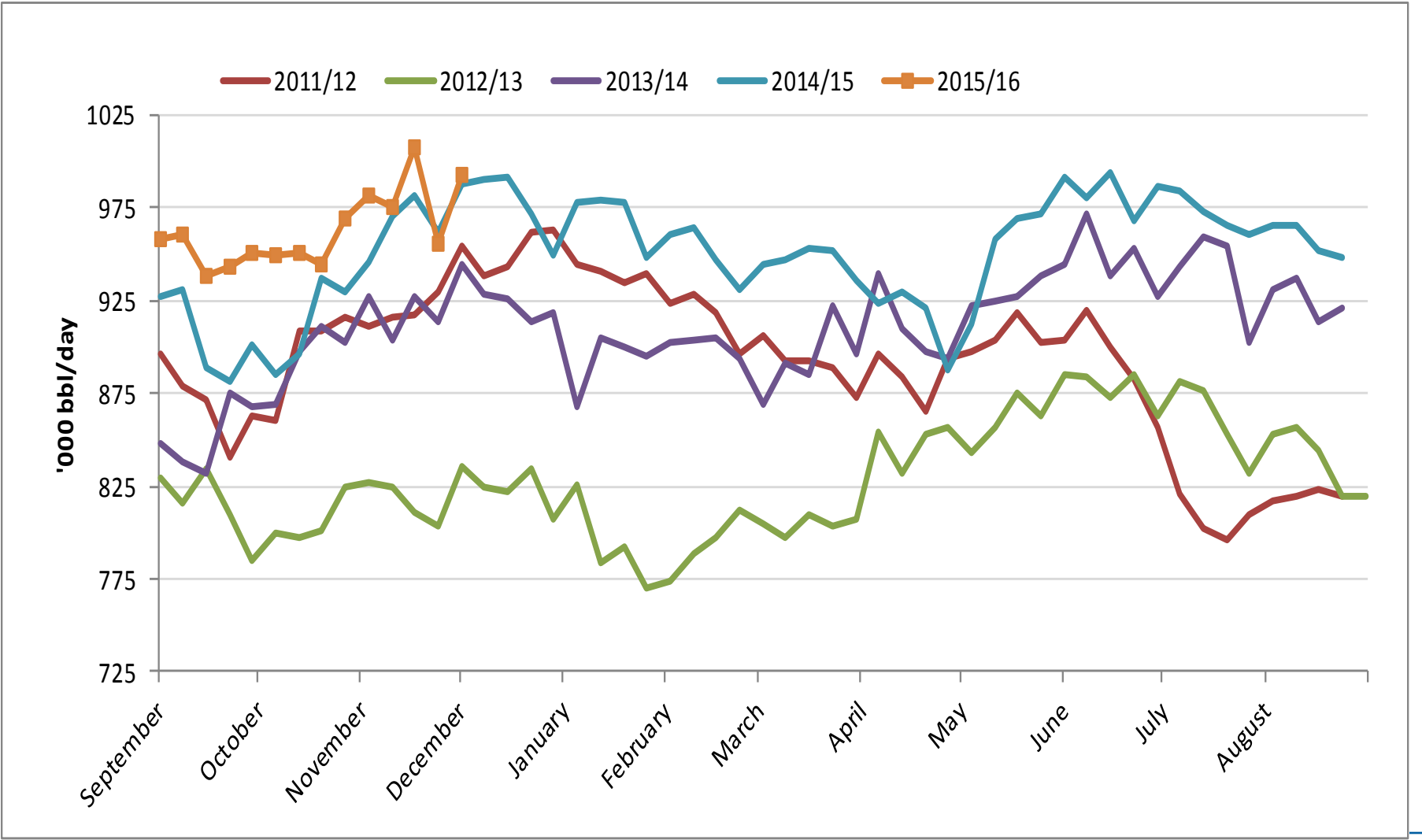


# Weekly Ethanol Production



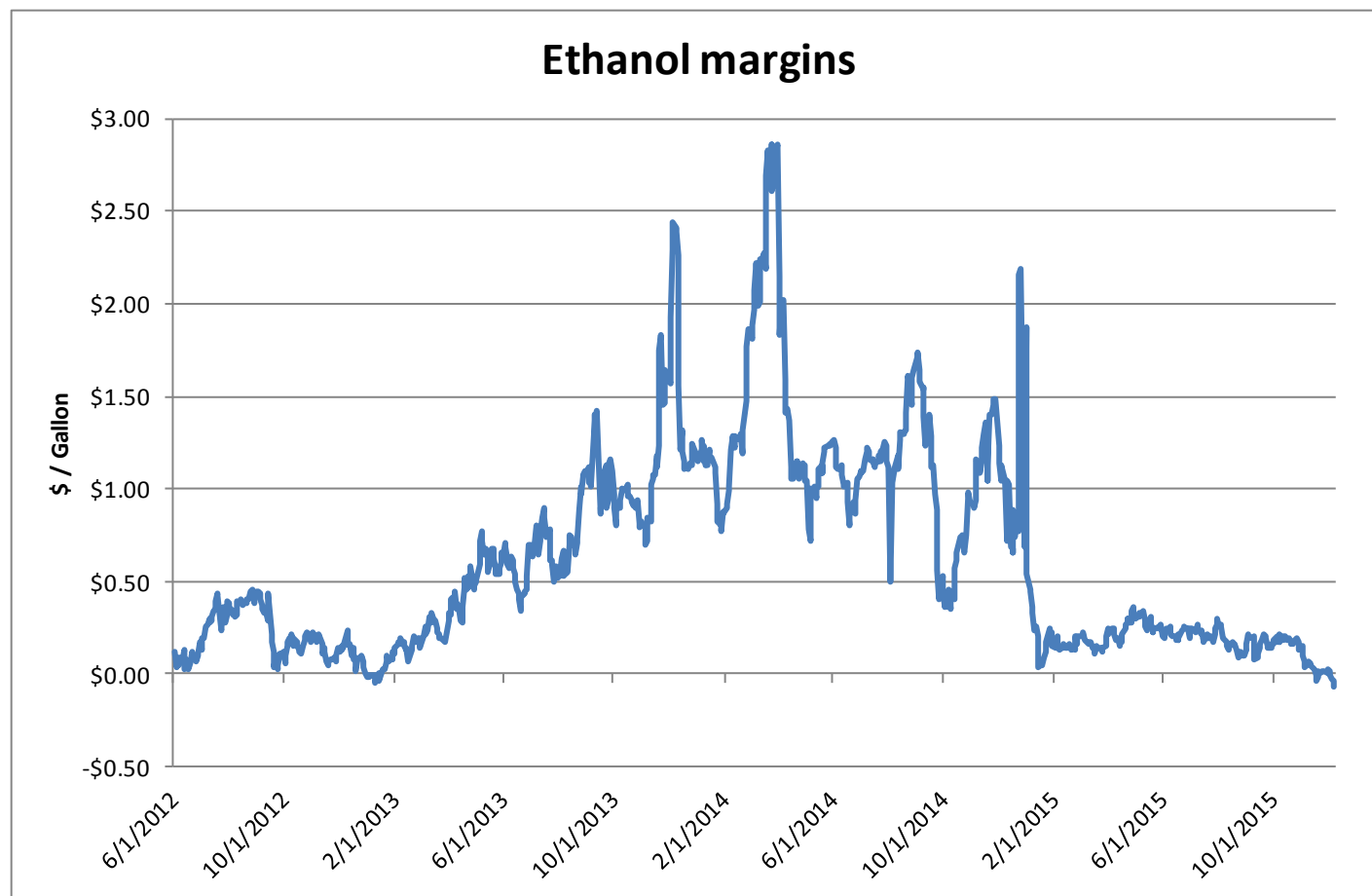
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# Ethanol Production



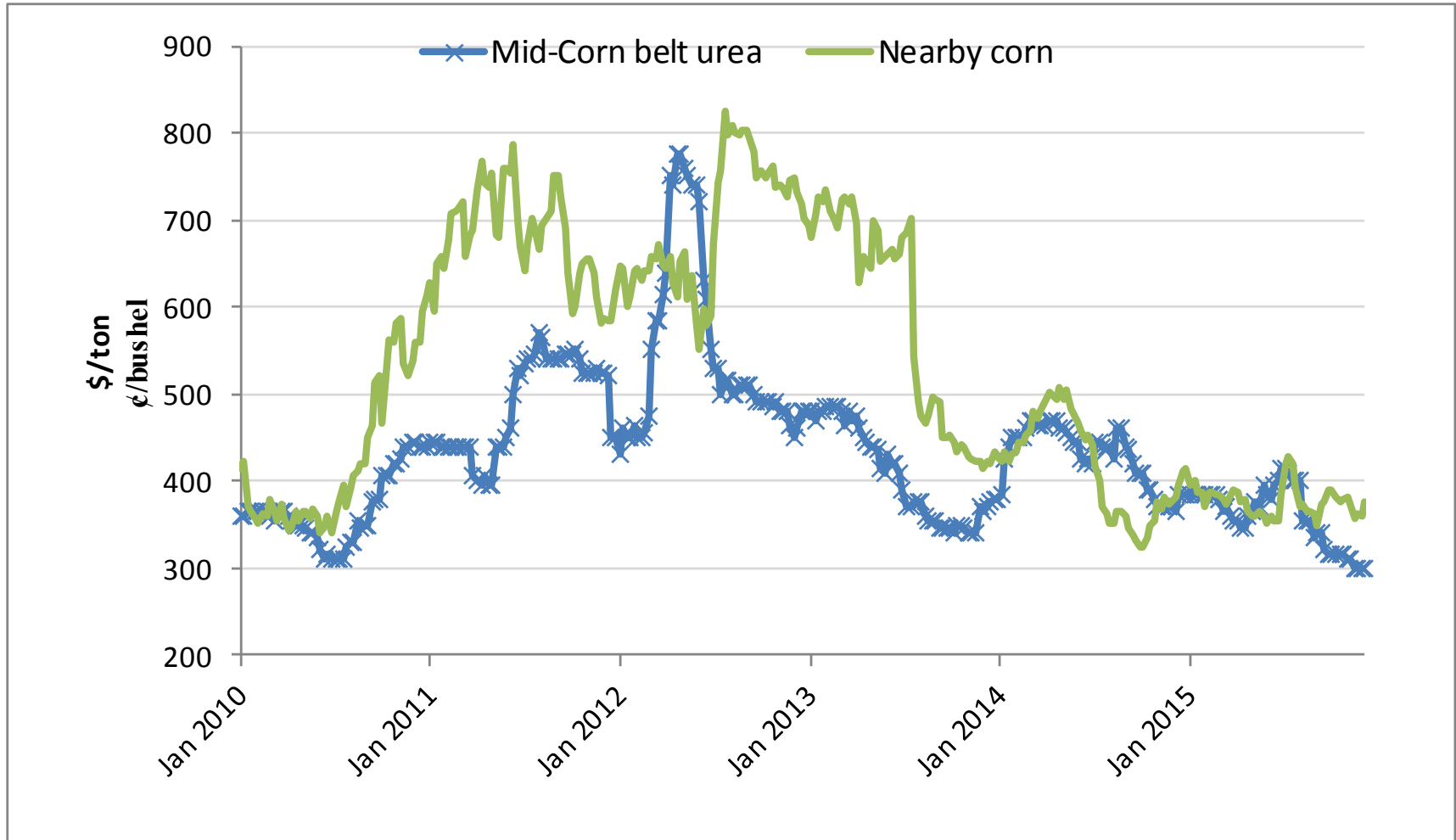
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# Gross Ethanol Margins per Gallon



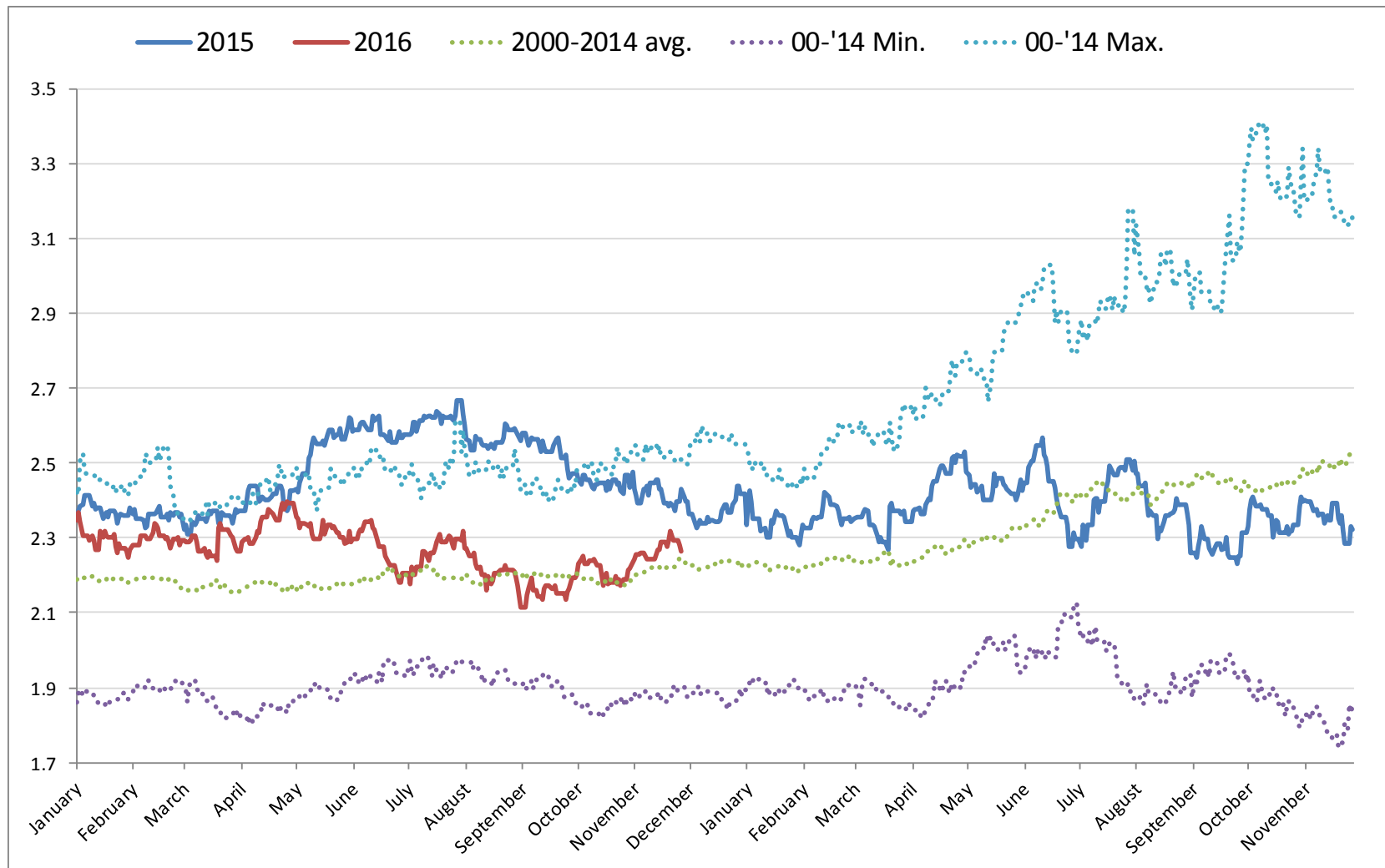
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# Urea and Corn



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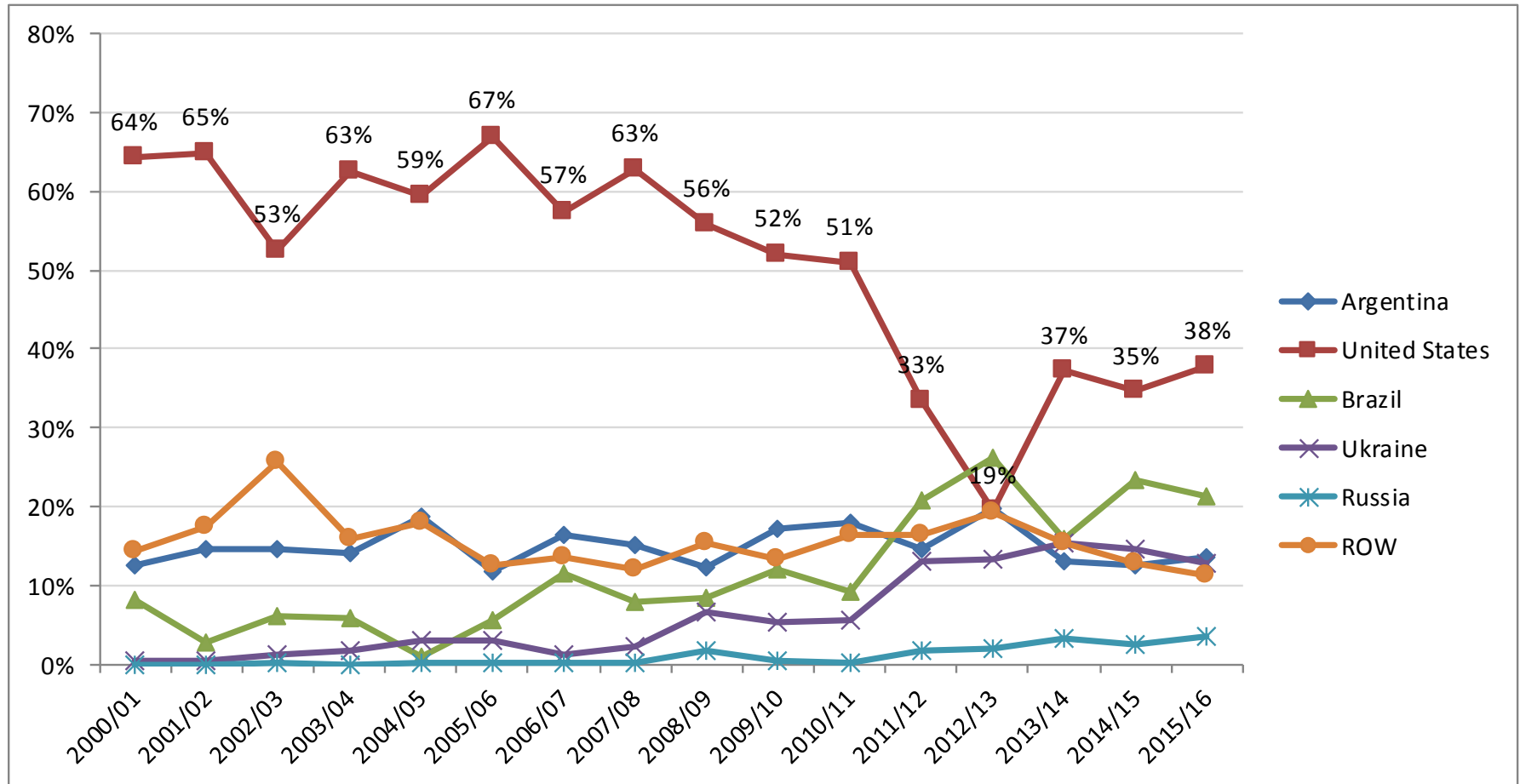
# New-crop Soybean/Corn Ratio



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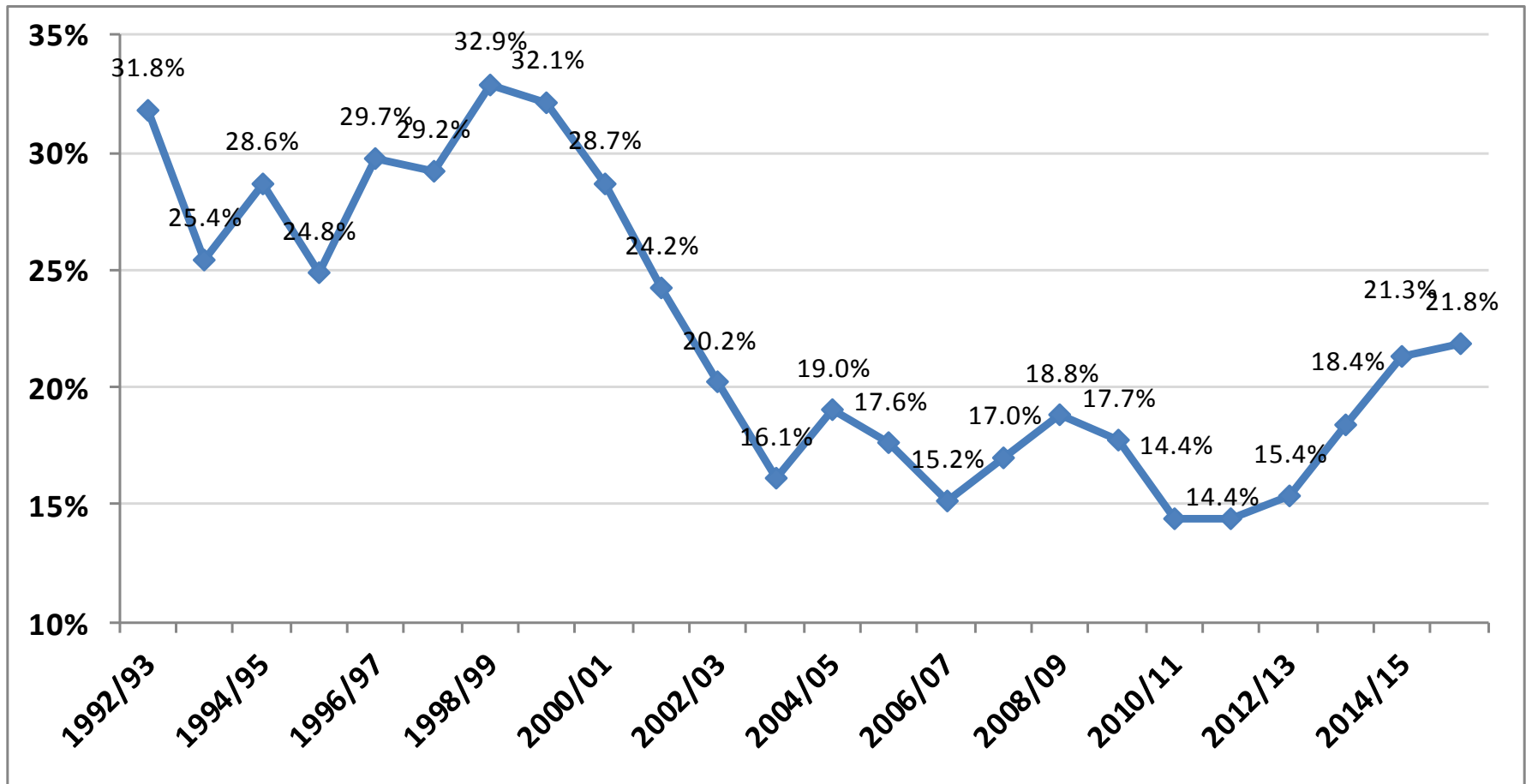
# World Corn Export Share



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# World Corn Stocks-to-Use Ratio

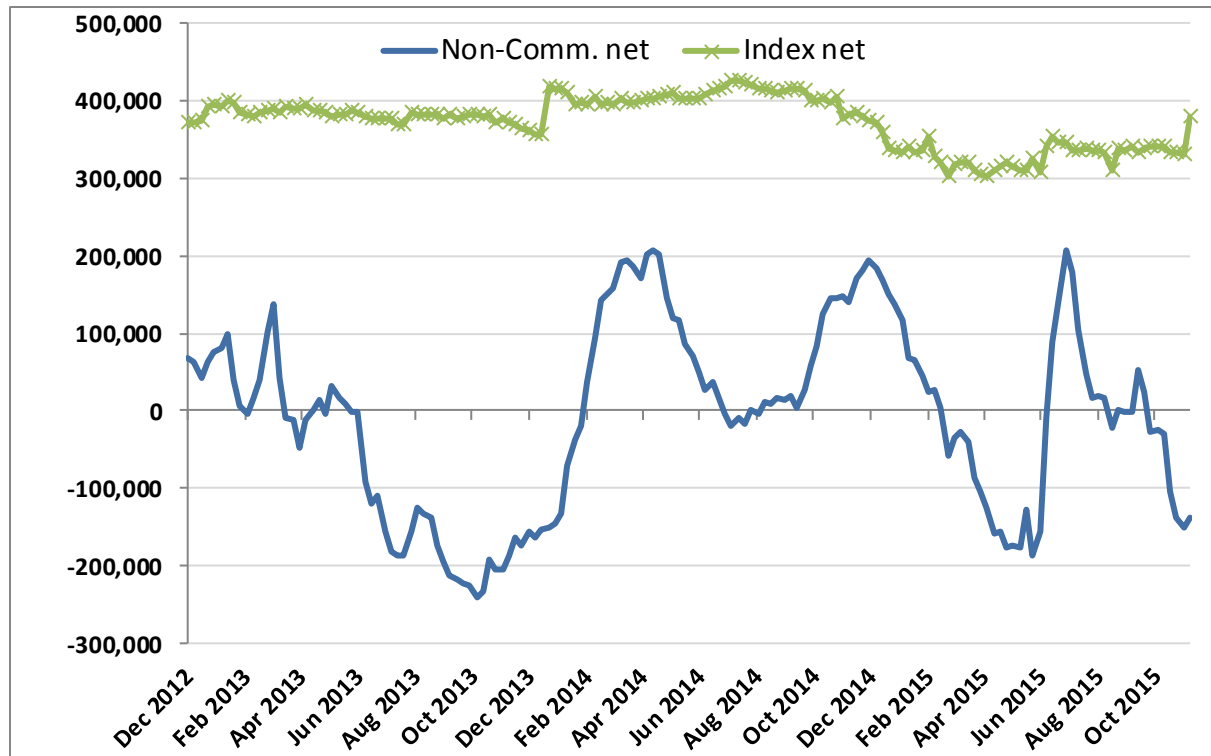


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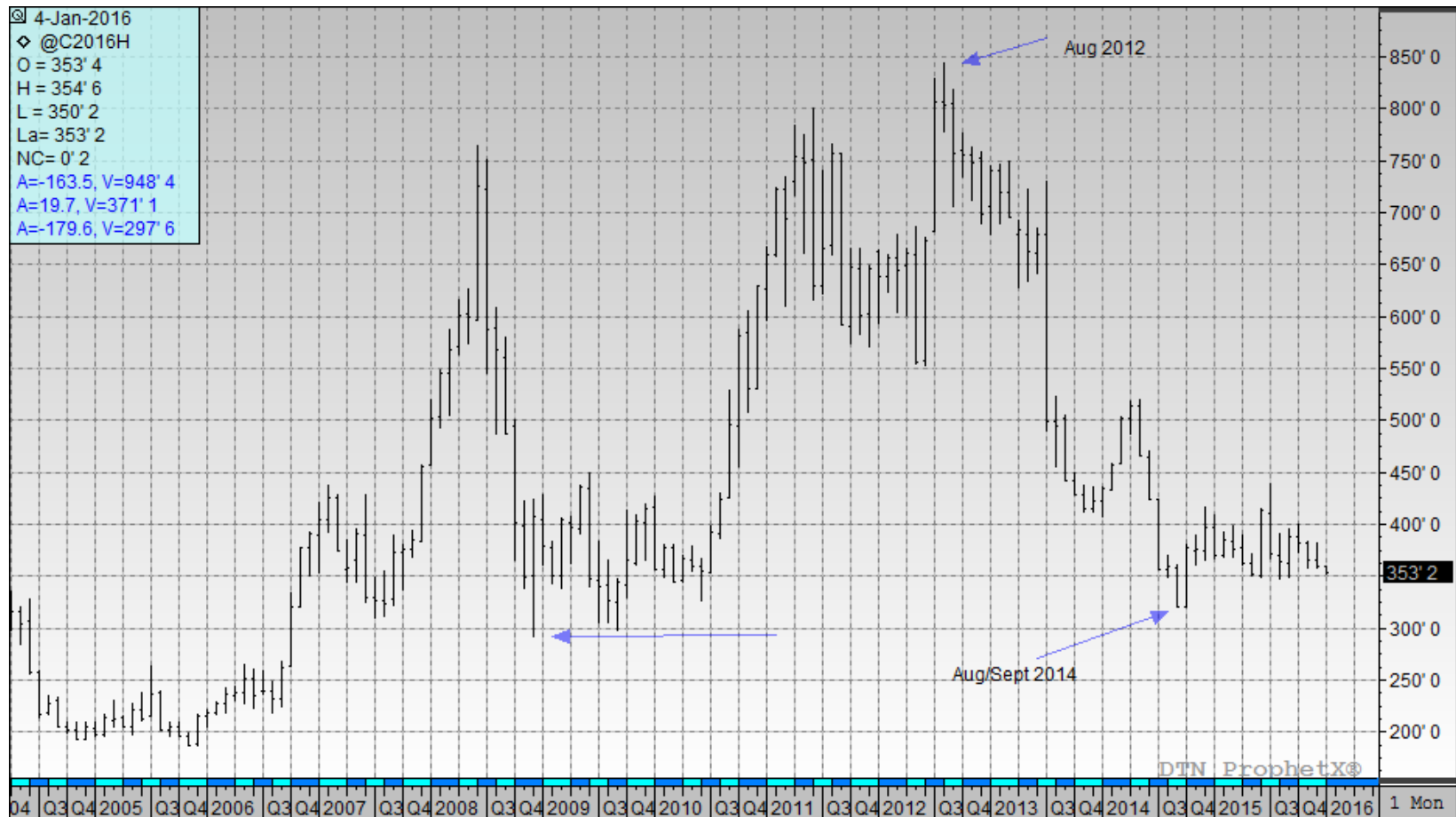
# Net Fund Positions-CME Corn

## CIT Report - Futures and Options Combined



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# Corn – continuous



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# Soybean Outlook

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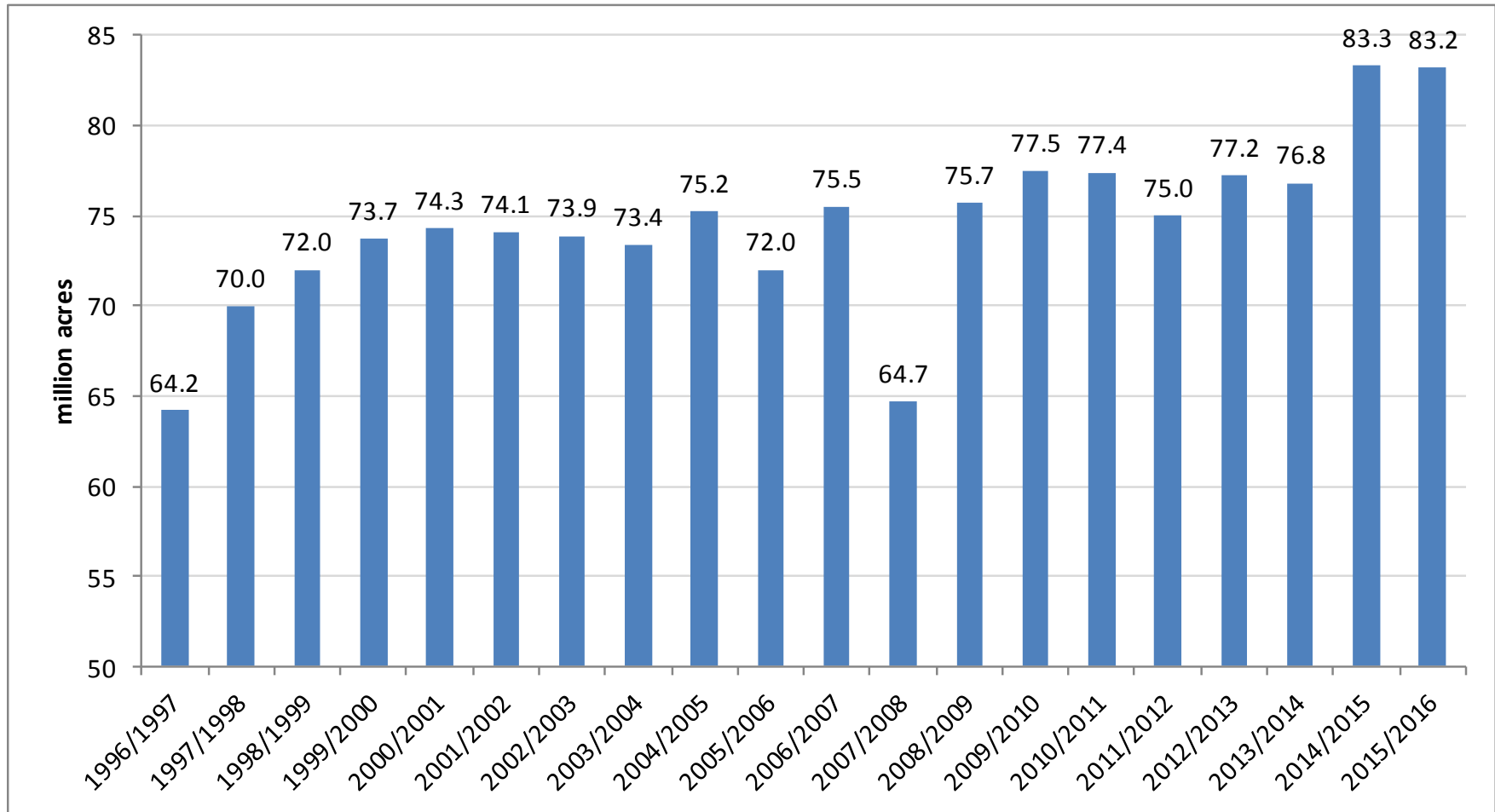
# U.S. Soybean Supply/Demand

|                  | <u>2010/2011</u> | <u>2011/2012</u> | <u>2012/2013</u> | <u>2013/2014</u> | <u>2014/2015</u> | <u>2015/2016</u> |
|------------------|------------------|------------------|------------------|------------------|------------------|------------------|
| Planted Acres    | 77.4             | 75.0             | 77.2             | 76.8             | 83.3             | 83.2             |
| Harvested Acres  | 76.6             | 73.8             | 76.1             | 76.3             | 82.6             | 82.4             |
| Yield            | 43.5             | 42.0             | 40.0             | 44.0             | 47.5             | 48.3             |
| Beginning Stocks | 151              | 215              | 169              | 141              | 92               | 191              |
| Production       | 3331             | 3097             | 3042             | 3358             | 3927             | 3981             |
| Imports          | 14               | 16               | 41               | 72               | 33               | 30               |
| Total Supply     | 3497             | 3328             | 3252             | 3570             | 4052             | 4203             |
| Crush            | 1648             | 1703             | 1689             | 1734             | 1873             | 1890             |
| Exports          | 1505             | 1366             | 1328             | 1638             | 1843             | 1715             |
| Seed             | 87               | 90               | 89               | 97               | 97               | 92               |
| Residual         | 43               | -2               | 16               | 10               | 48               | 41               |
| Total Use        | 3283             | 3157             | 3122             | 3479             | 3861             | 3738             |
| Ending Stocks    | 214              | 171              | 130              | 92               | 191              | 465              |
| Stocks/Use       | 6.5%             | 5.4%             | 4.2%             | 2.7%             | 4.9%             | 12.4%            |

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# U.S. Soybeans Planted Acres

16/17 82.0

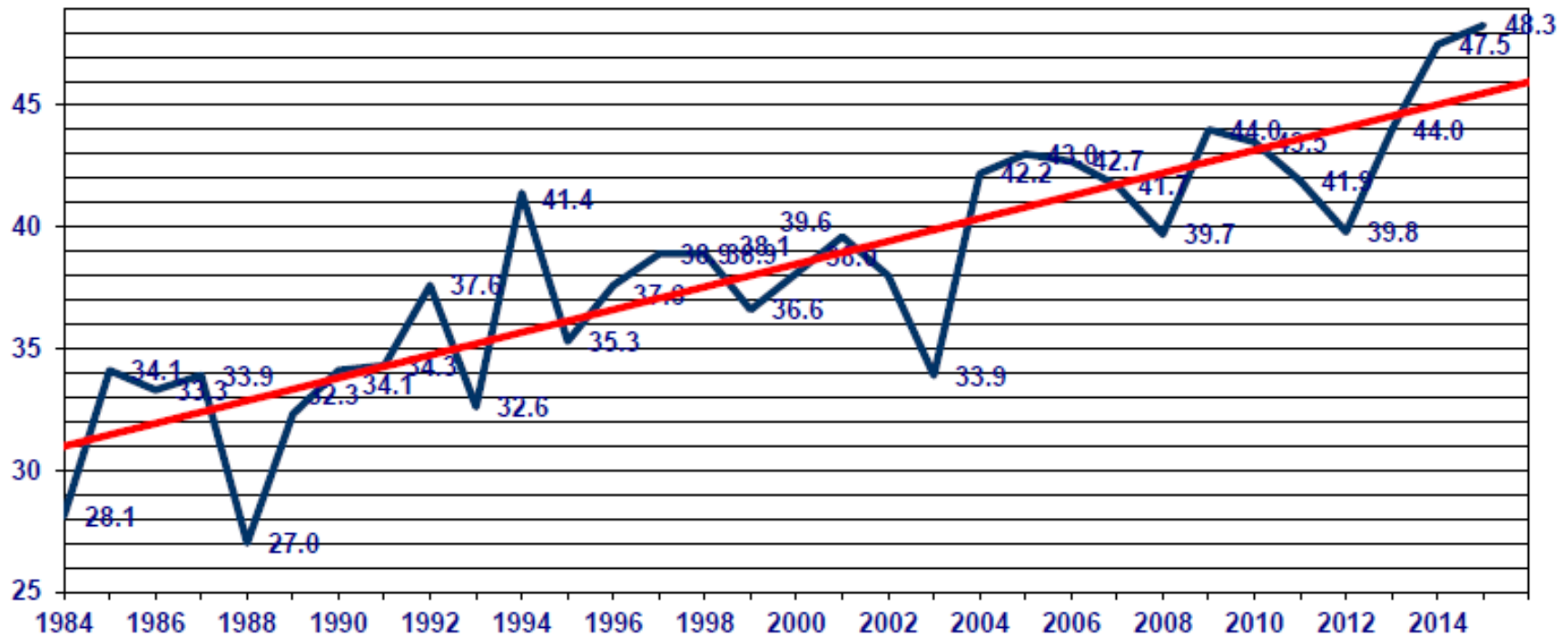


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# U.S. Soybean Yield

16/17 46.7 BPA

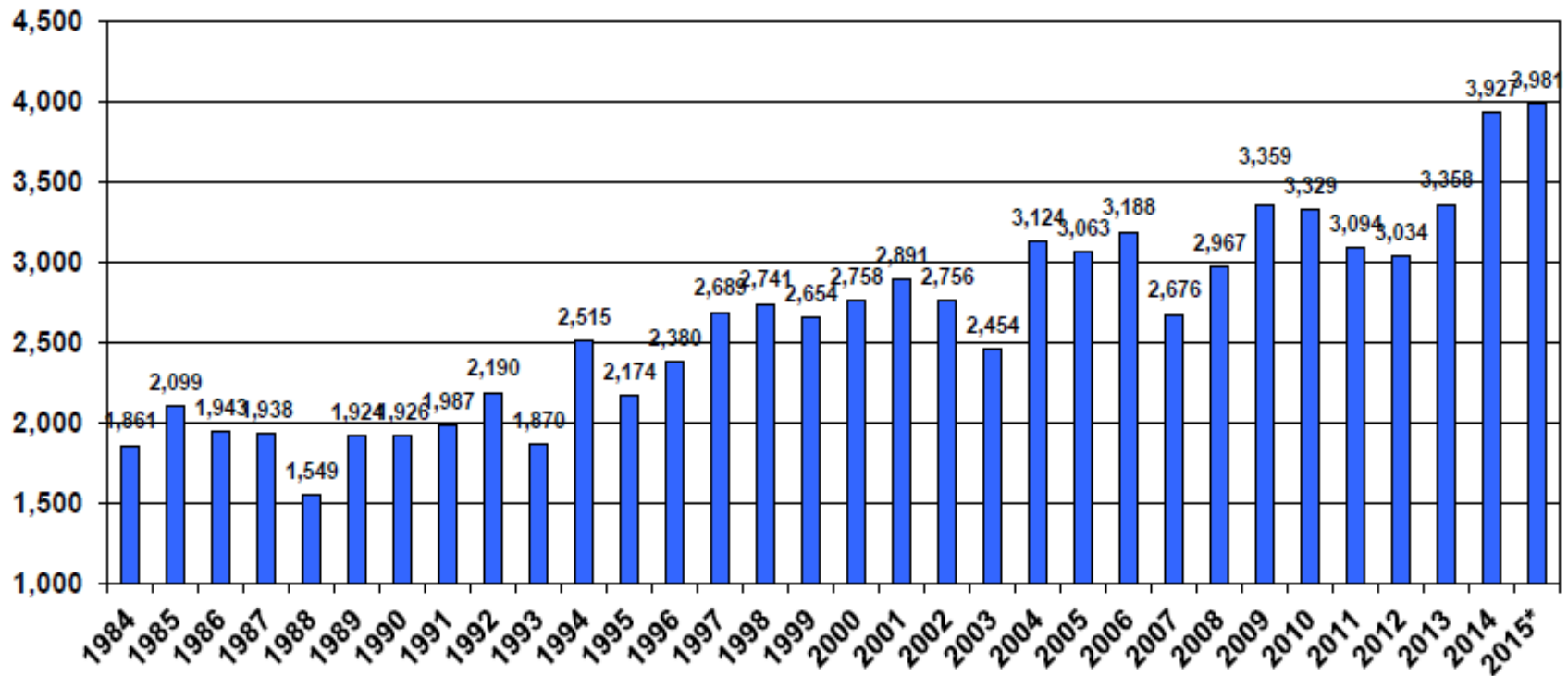


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# U.S. Soybean Production

16/17 3.785

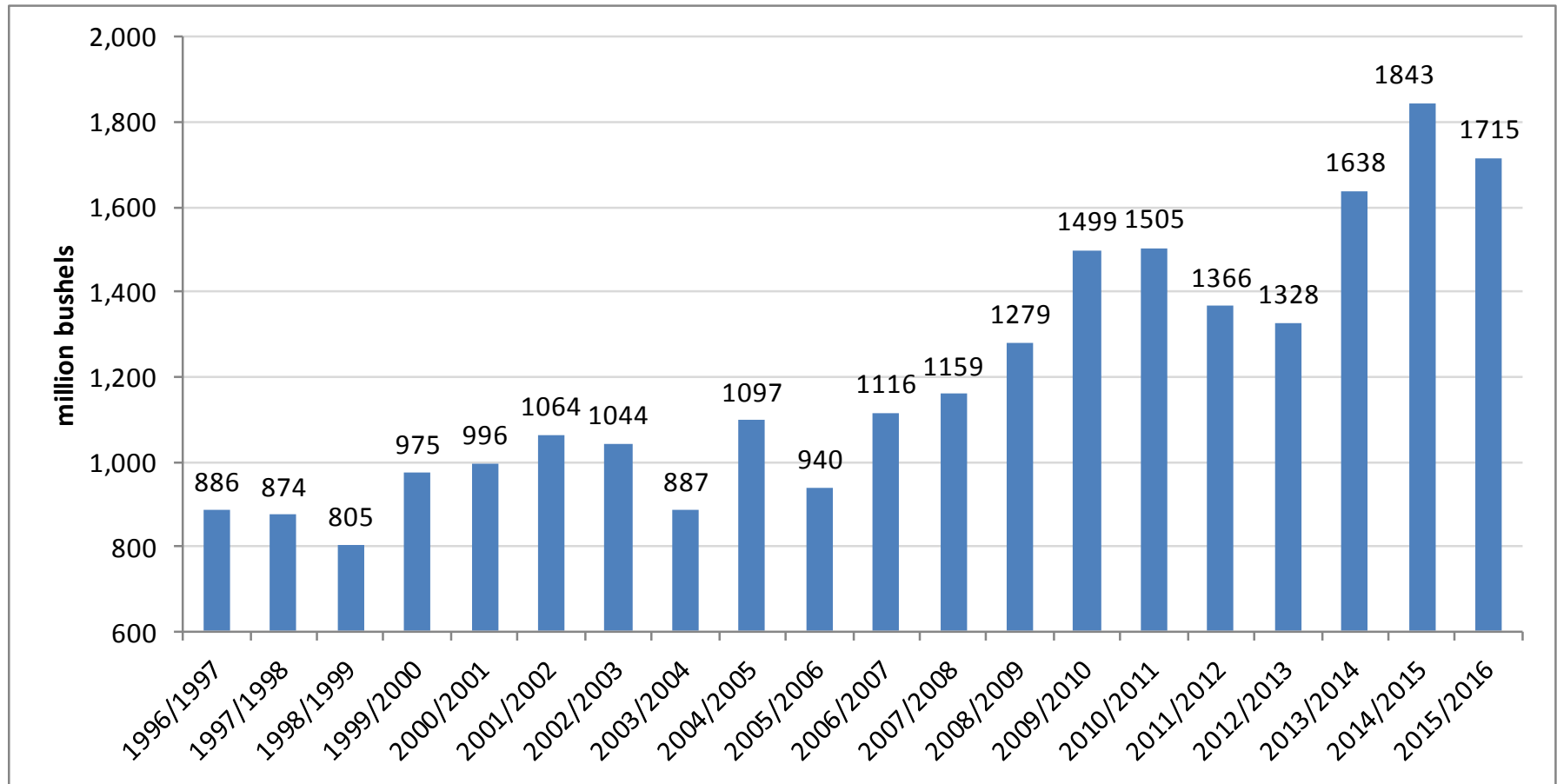


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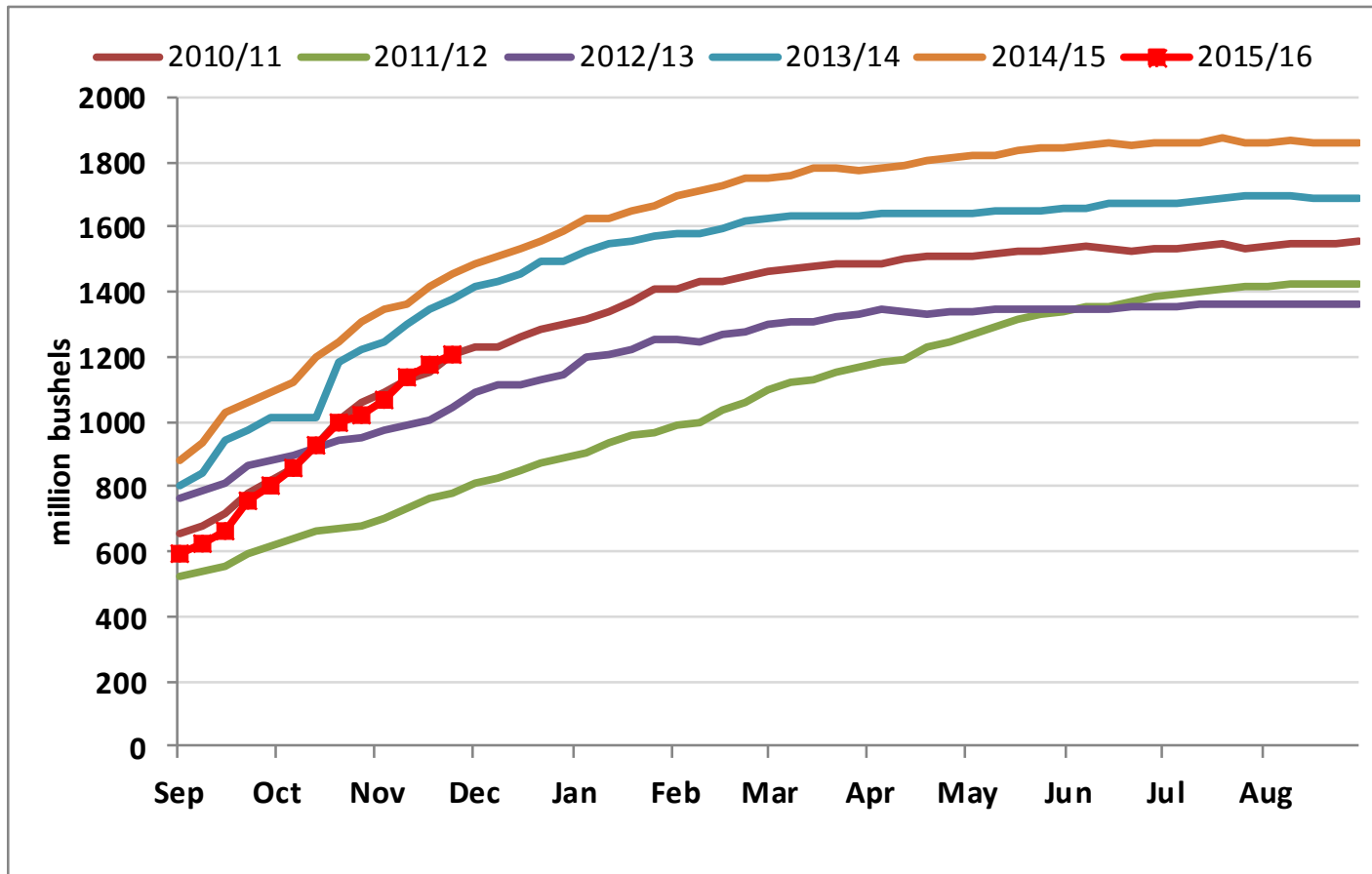
# U.S. Soybean Exports



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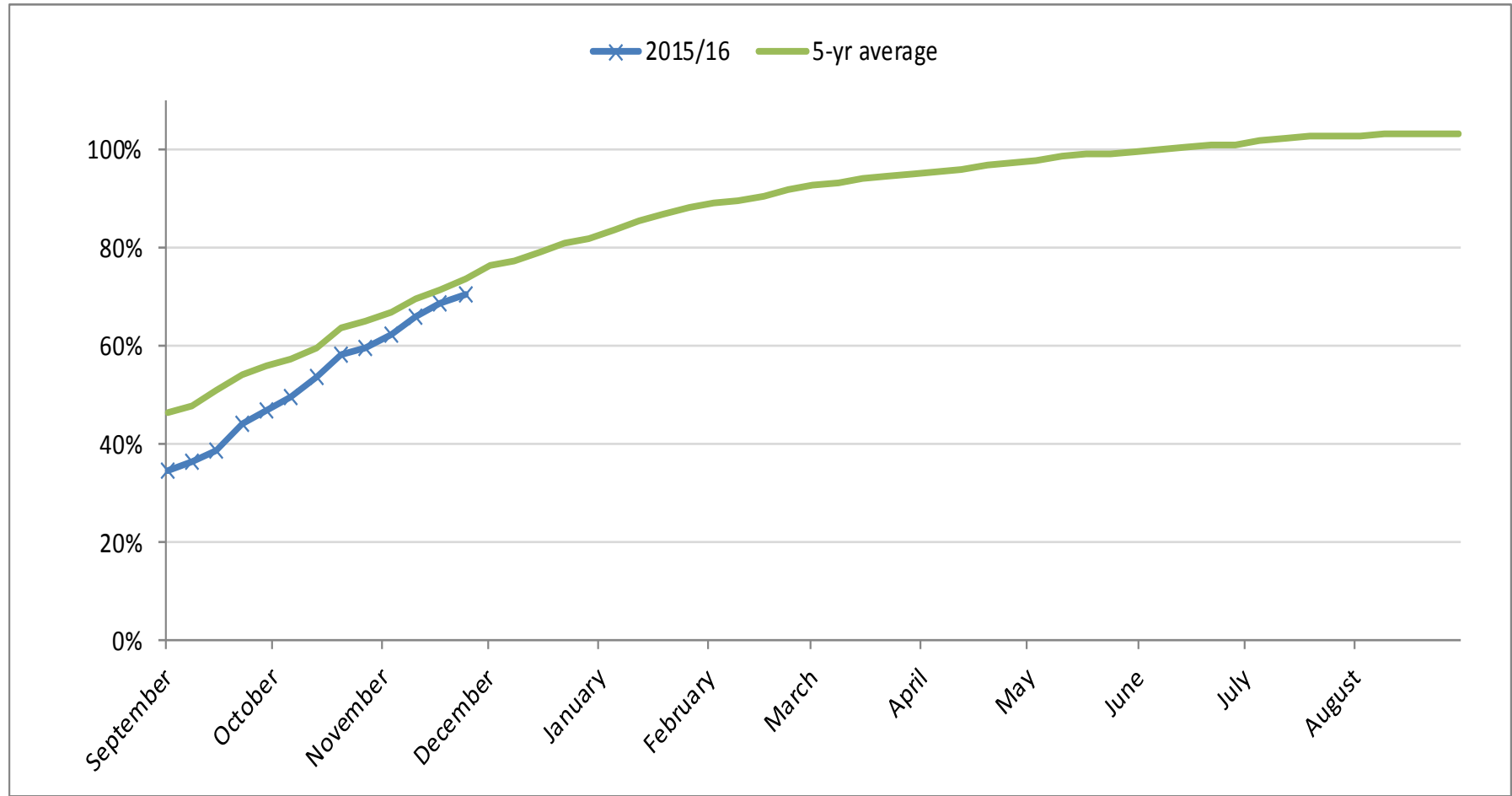
# U.S. Bean Export Commitments



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# Export Commitments: % of Final Soybeans



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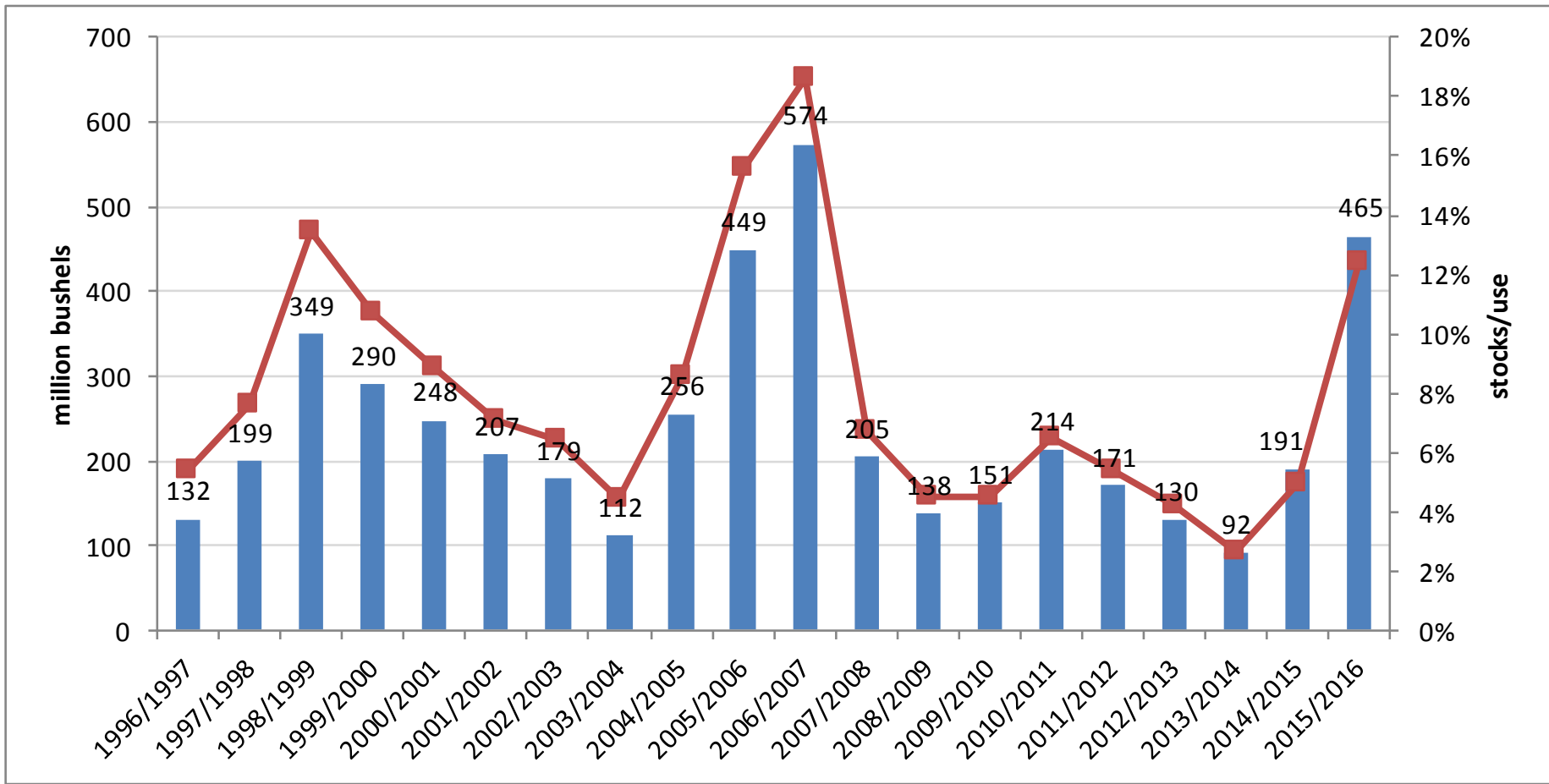
# CME Nearby Soybean Crush



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# U.S. Soybean Ending Stocks and Stocks/Use Ratio

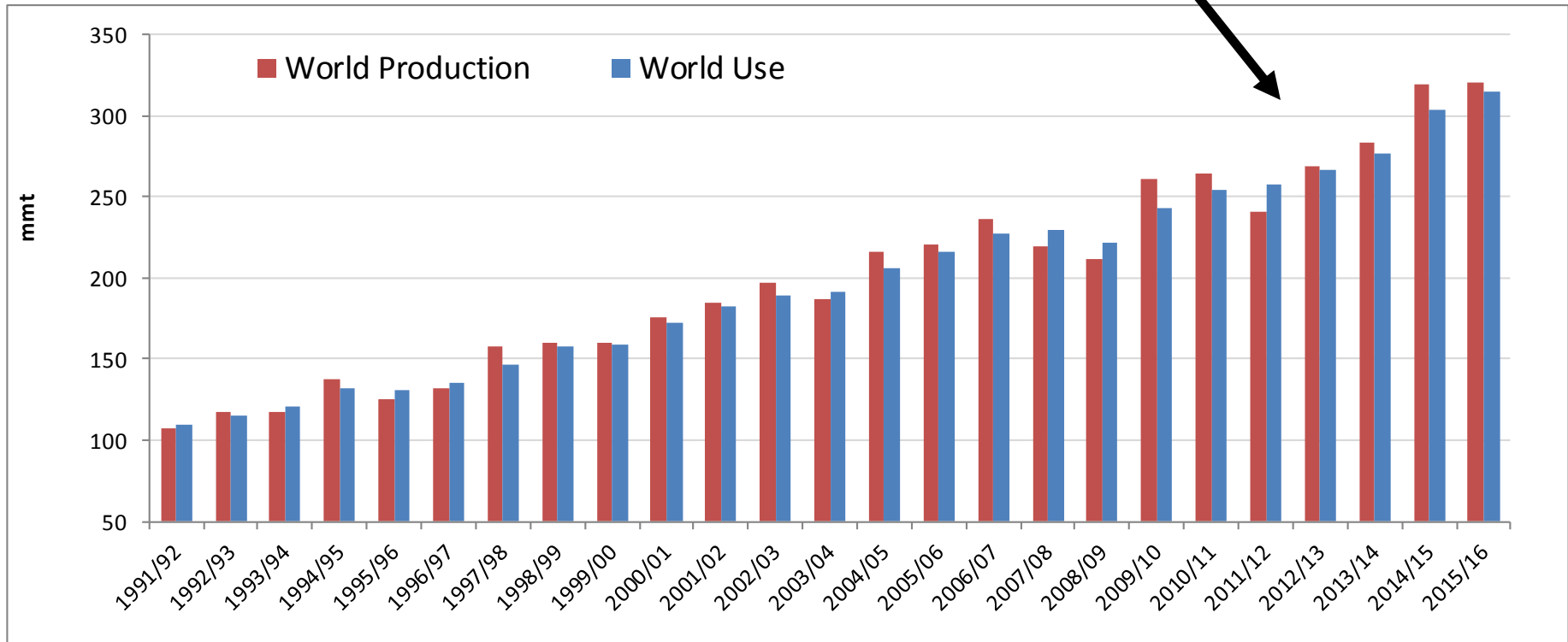


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# World Soybeans

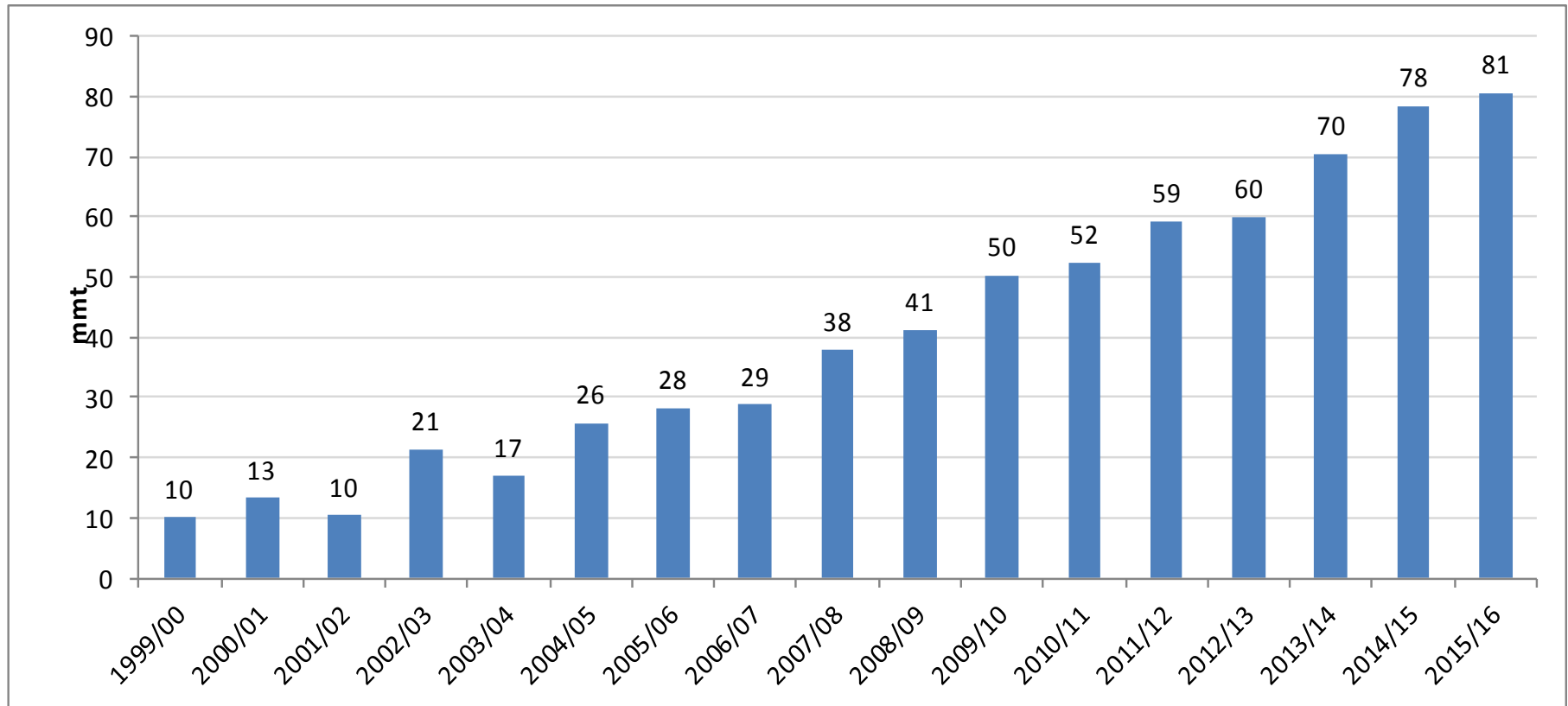
The last 4 years, and 6 out of the last 7 years we've seen more production than use



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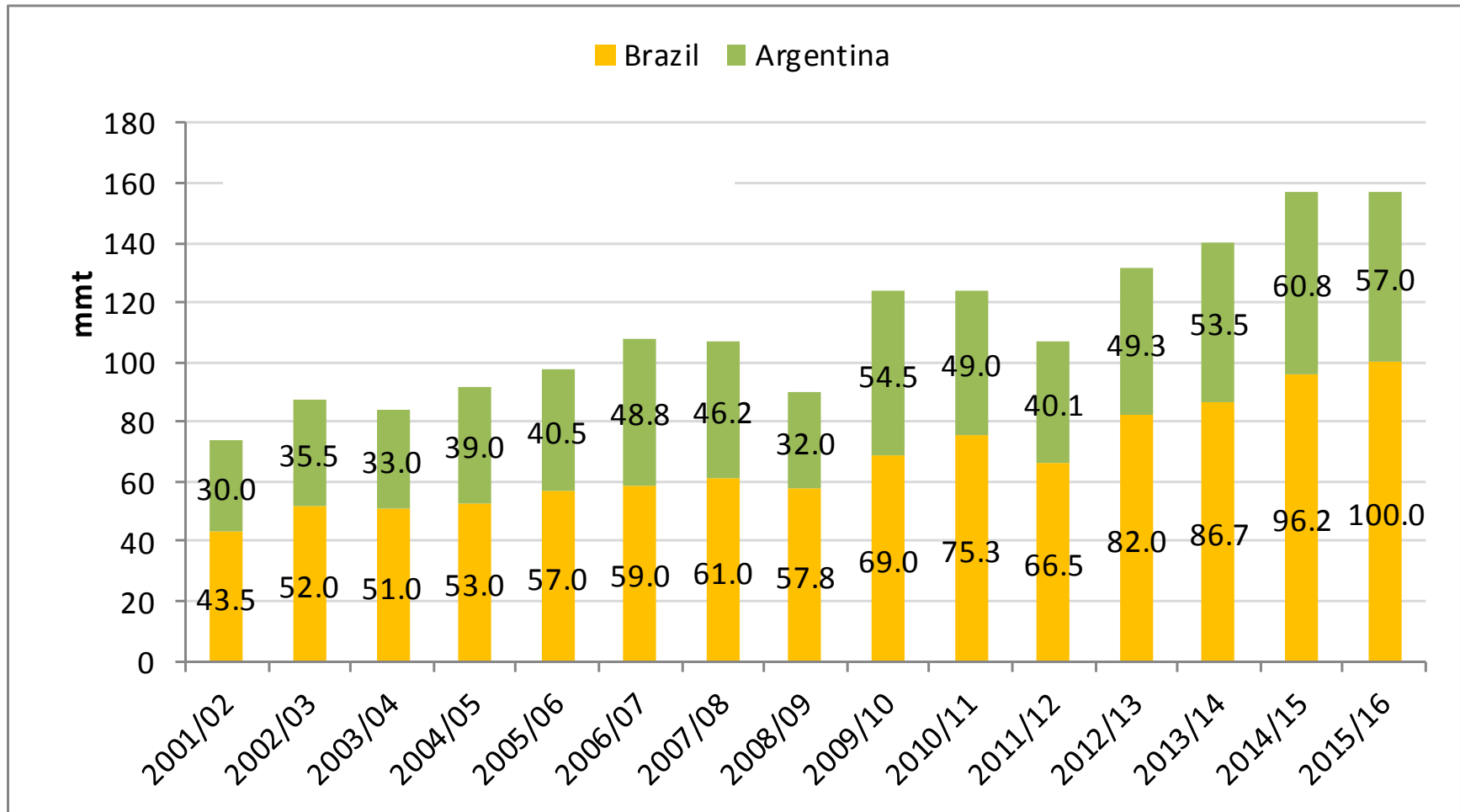


# Chinese Soybean Imports



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# Production: Brazil & Argentina

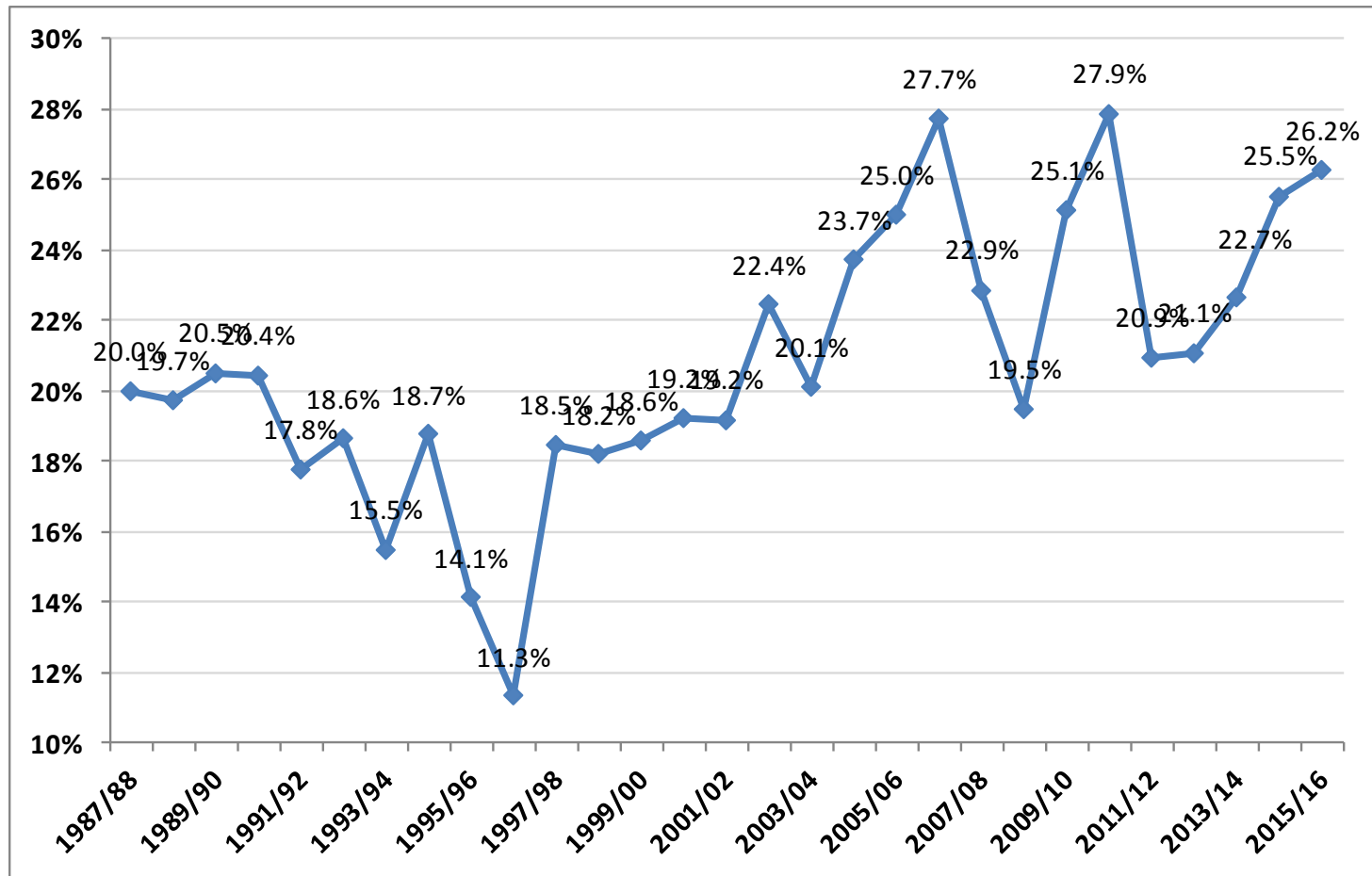


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# World Soybean Stocks/Use Ratio

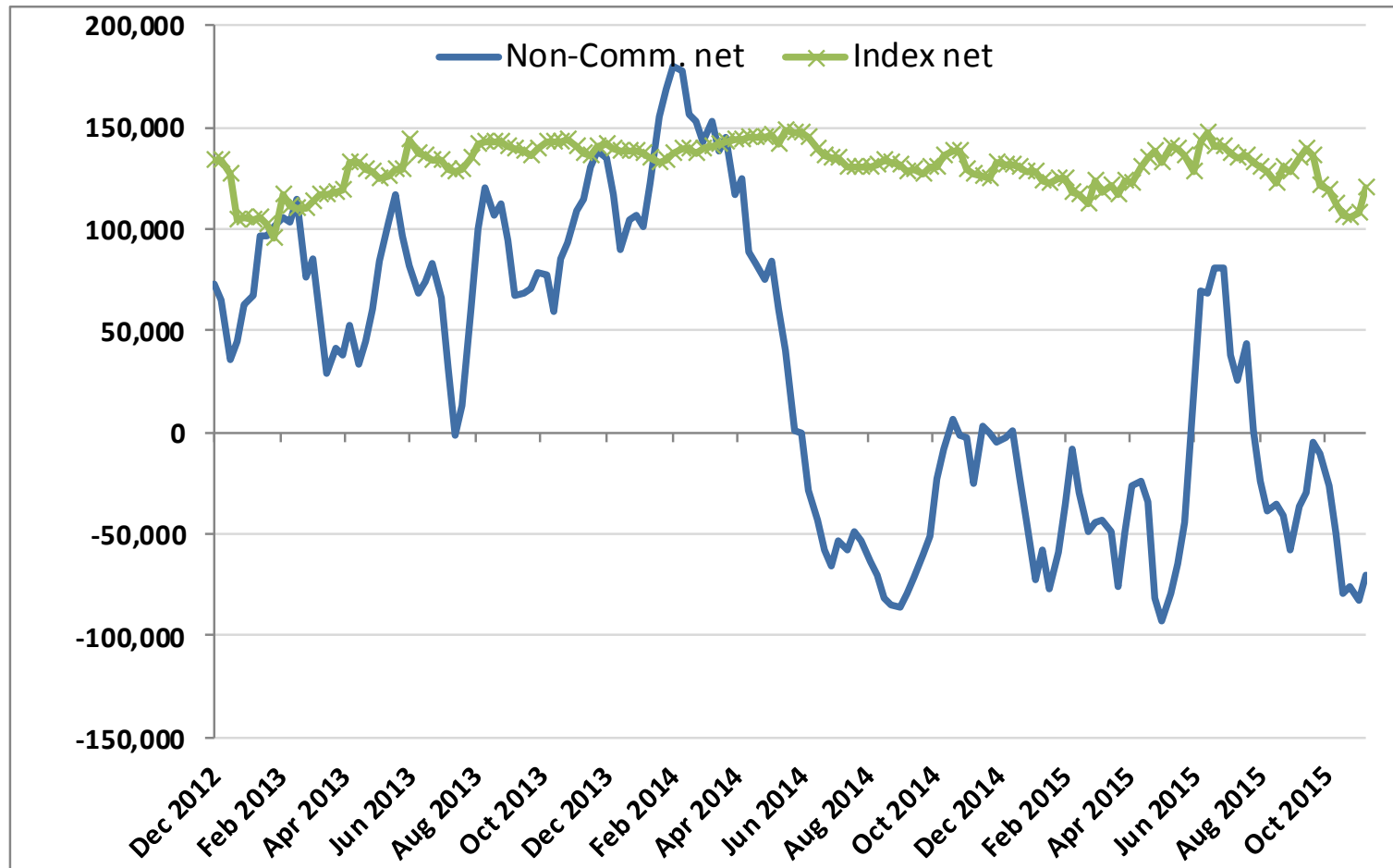


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# Net Fund Positions-CME Soybeans

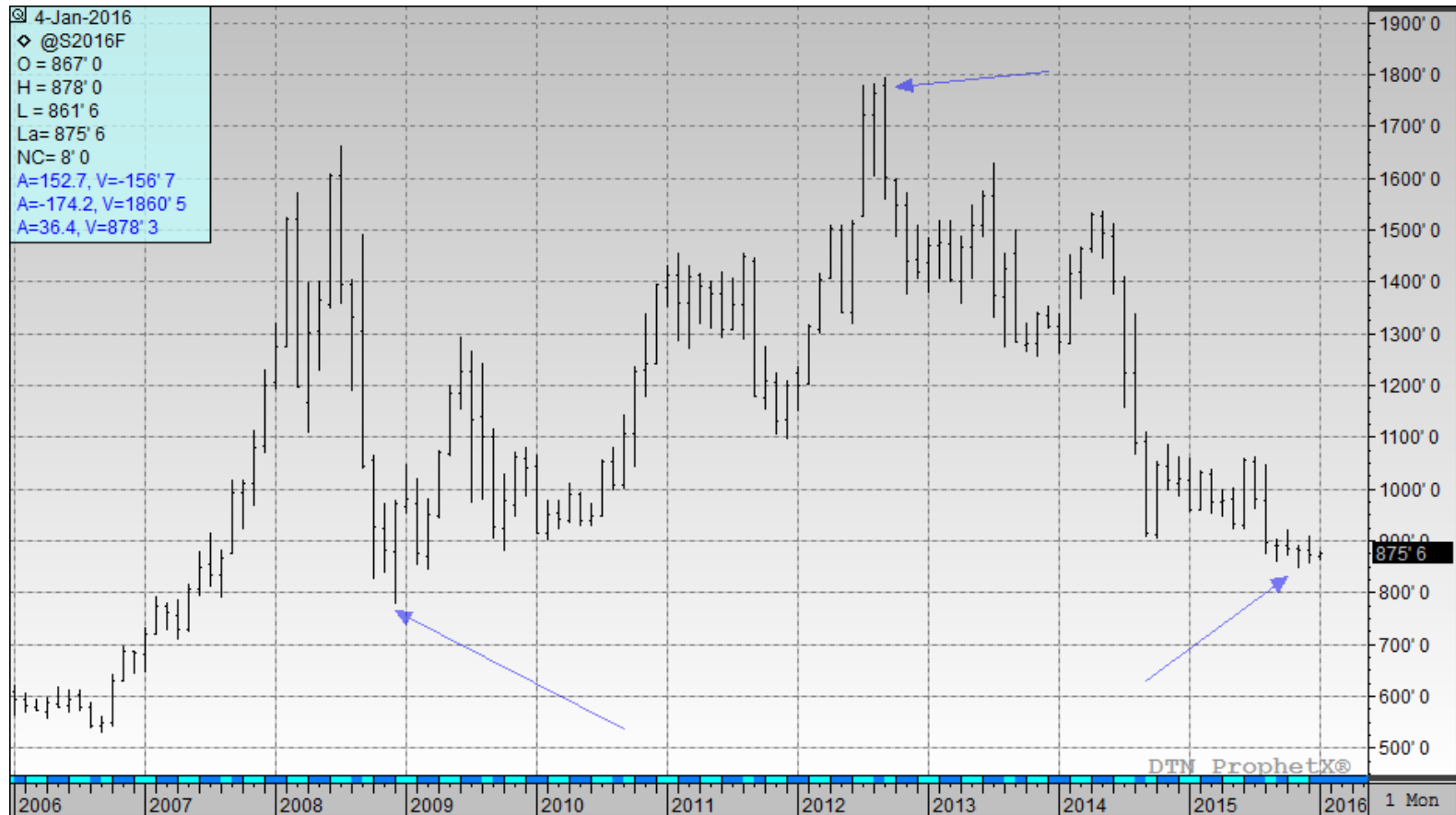
## CIT Report - Futures and Options Combined



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# Soybean – continuous



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# Wheat Outlook

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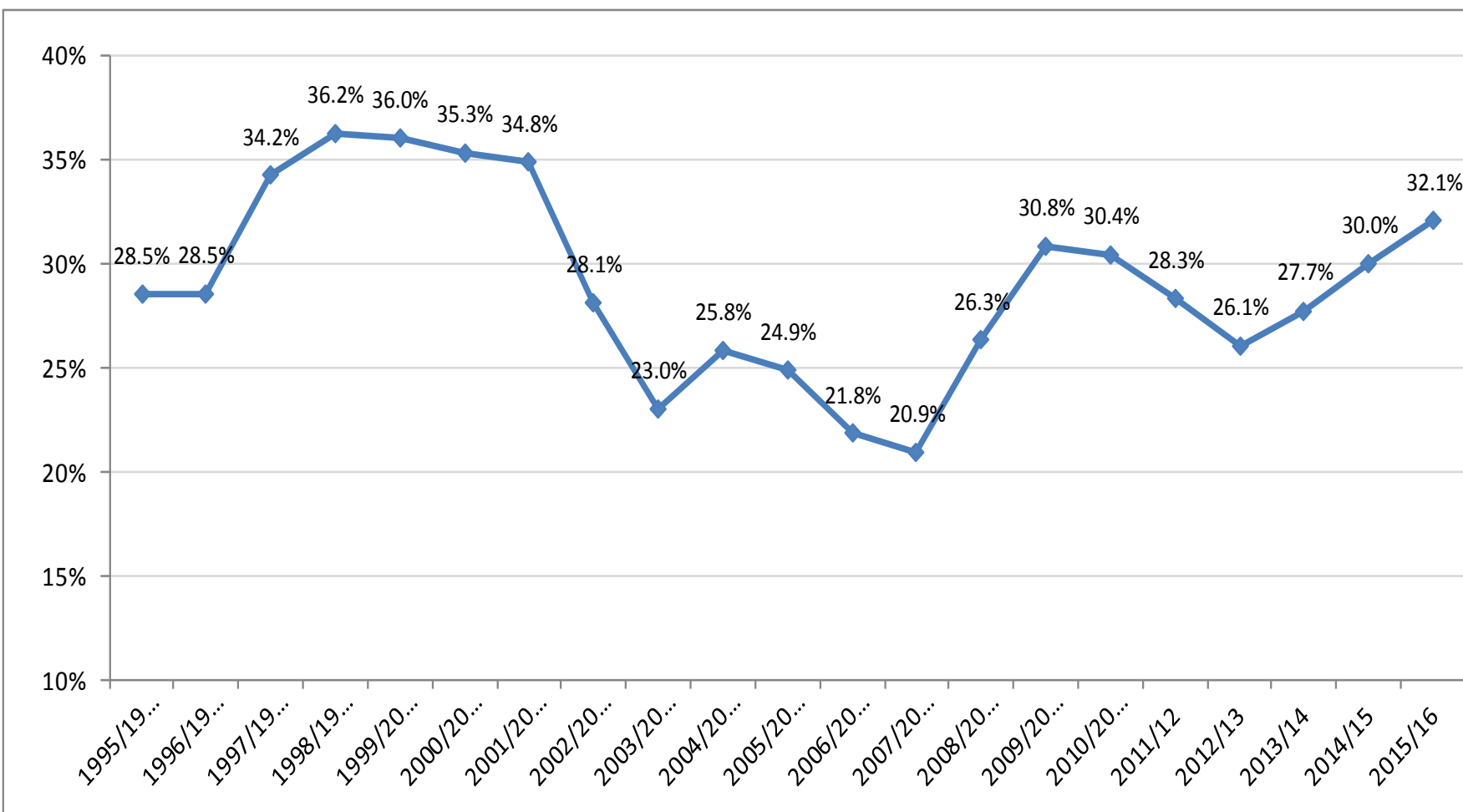
# U.S. Wheat Supply/Demand

|                  | <u>2009/2010</u> | <u>2010/2011</u> | <u>2011/2012</u> | <u>2012/2013</u> | <u>2013/14</u> | <u>2014/15</u> | <u>2015/2016</u> |
|------------------|------------------|------------------|------------------|------------------|----------------|----------------|------------------|
| Planted Acres    | 59.2             | 53.6             | 54.4             | 55.3             | 56.2           | 56.8           | 54.6             |
| Harvested Acres  | 49.9             | 46.9             | 45.7             | 48.8             | 45.3           | 46.4           | 47.1             |
| Yield            | 44.5             | 46.1             | 43.6             | 46.2             | 47.1           | 43.7           | 43.6             |
| Beginning Stocks | 656              | 976              | 863              | 743              | 718            | 590            | 753              |
| Production       | 2218             | 2163             | 1993             | 2252             | 2135           | 2026           | 2052             |
| Imports          | 119              | 97               | 112              | 123              | 173            | 149            | 125              |
| Total Supply     | 2993             | 3236             | 2968             | 3118             | 3026           | 2766           | 2930             |
| Feed/Residual    | 150              | 85               | 157              | 364              | 228            | 120            | 180              |
| Food             | 919              | 926              | 941              | 945              | 955            | 958            | 967              |
| Seed             | 69               | 71               | 76               | 73               | 77             | 81             | 72               |
| Domestic Use     | 1138             | 1081             | 1175             | 1381             | 1260           | 1159           | 1219             |
| Exports          | 879              | 1291             | 1051             | 1012             | 1176           | 854            | 800              |
| Total Use        | 2018             | 2373             | 2226             | 2394             | 2436           | 2013           | 2019             |
| Ending Stocks    | 976              | 863              | 742              | 724              | 590            | 753            | 911              |
| Stocks/Use       | 48%              | 36%              | 33%              | 30%              | 24%            | 37%            | 45%              |

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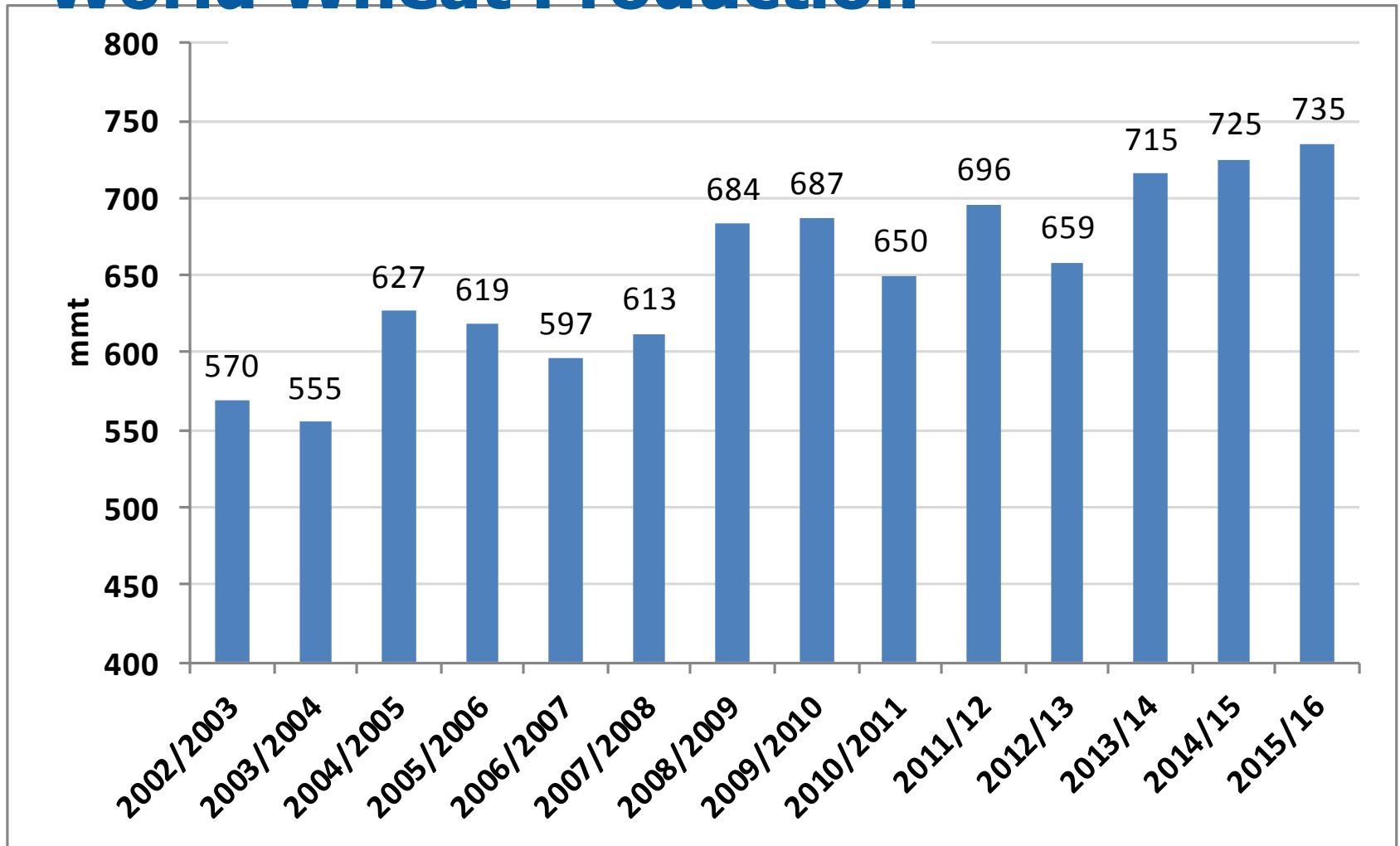
# World Stocks-to-Use Ratio



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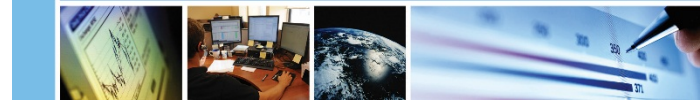


# World Wheat Production

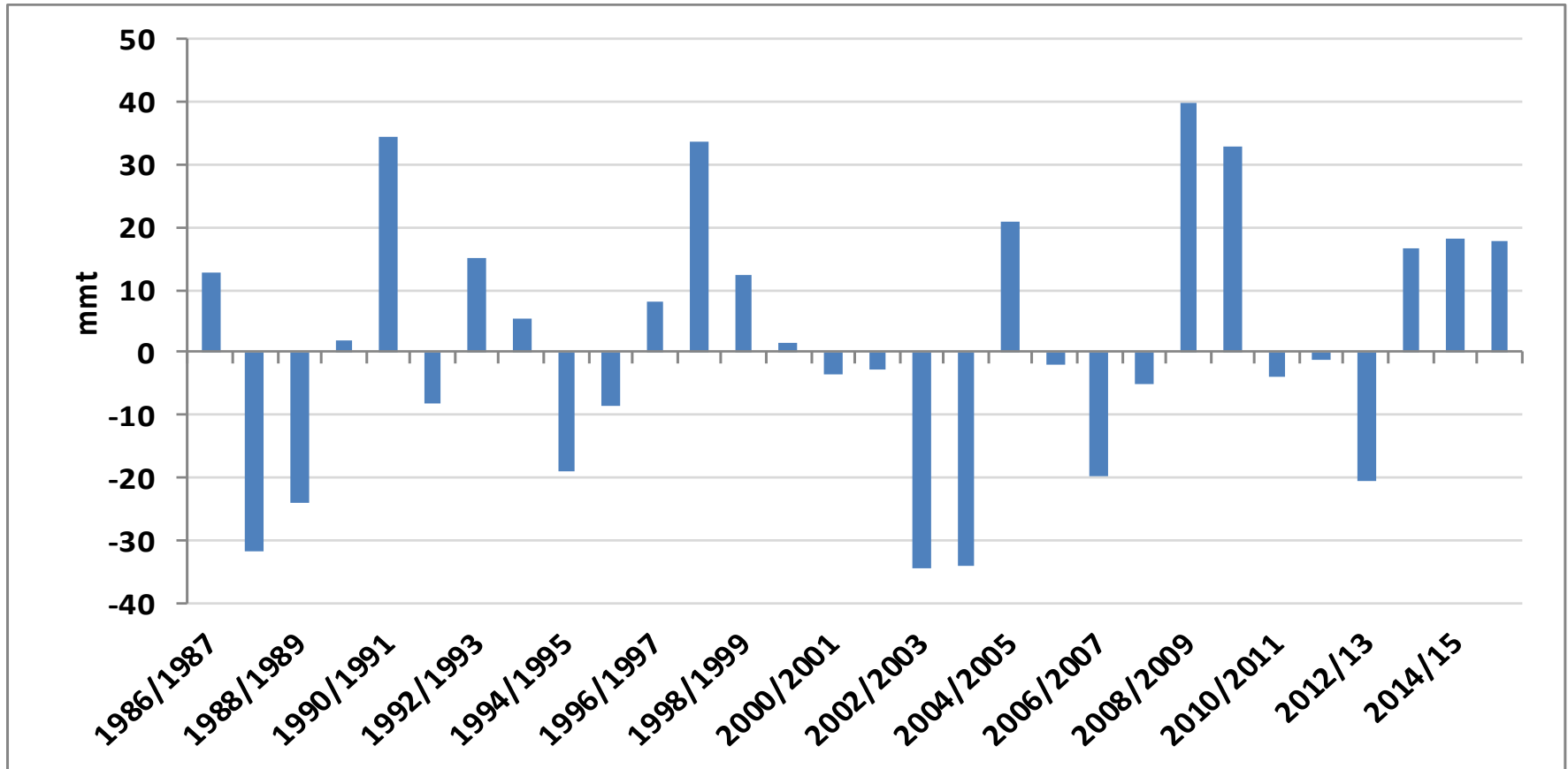


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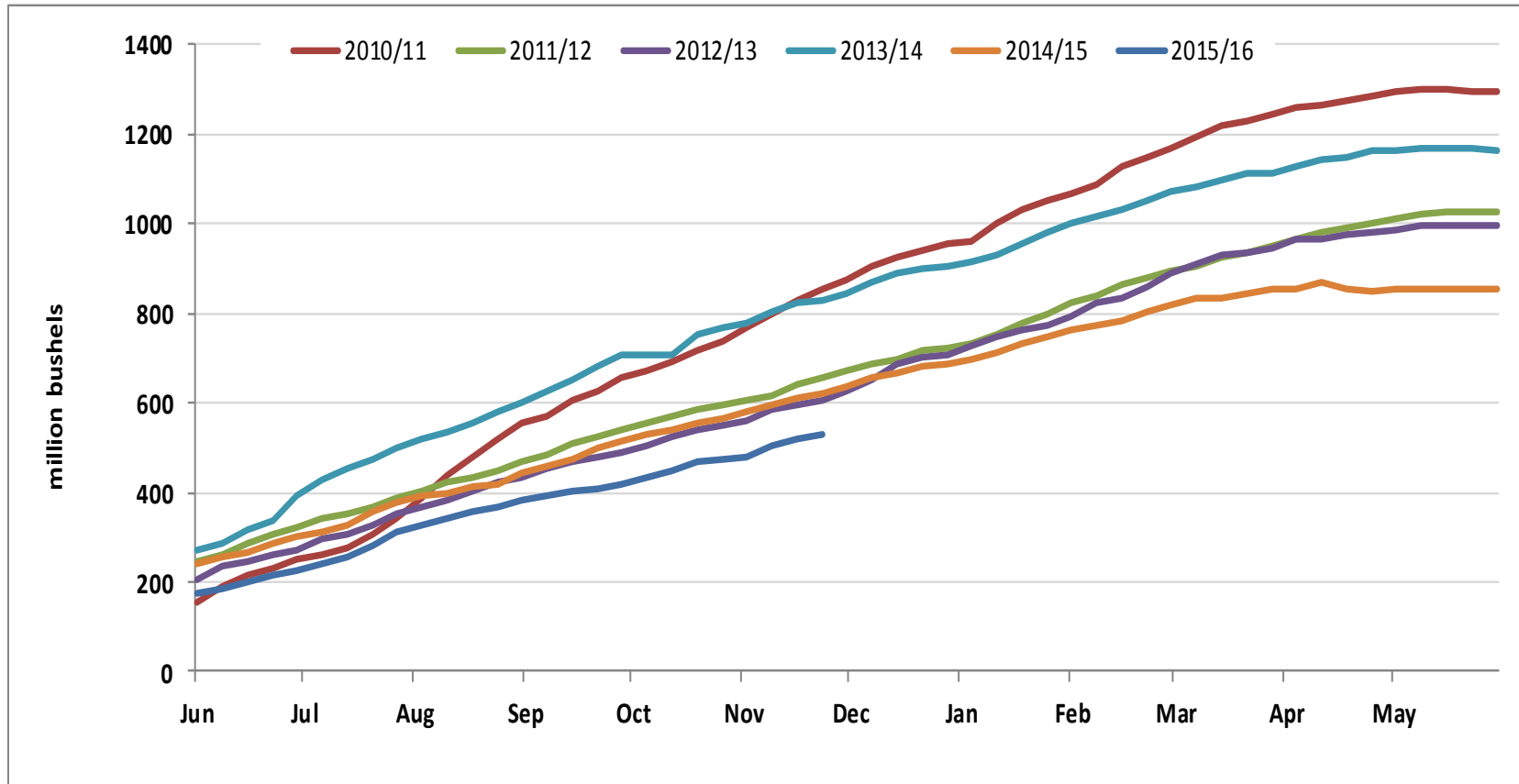
# Annual Change in World Stocks



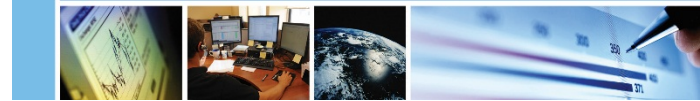
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# U.S. Wheat Export Commitments

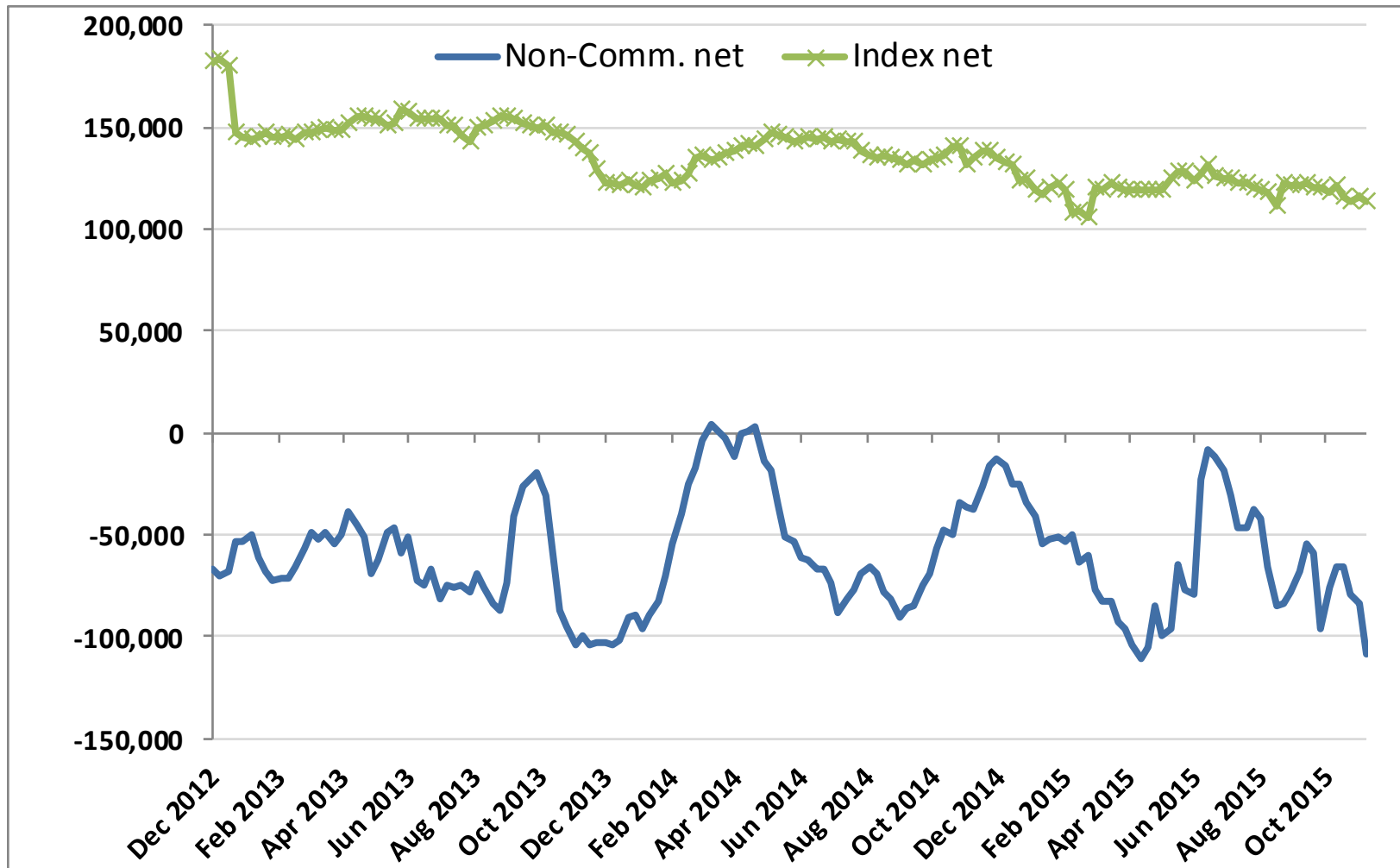


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# Net Fund Positions-CME Wheat

## CIT Report - Futures and Options Combined

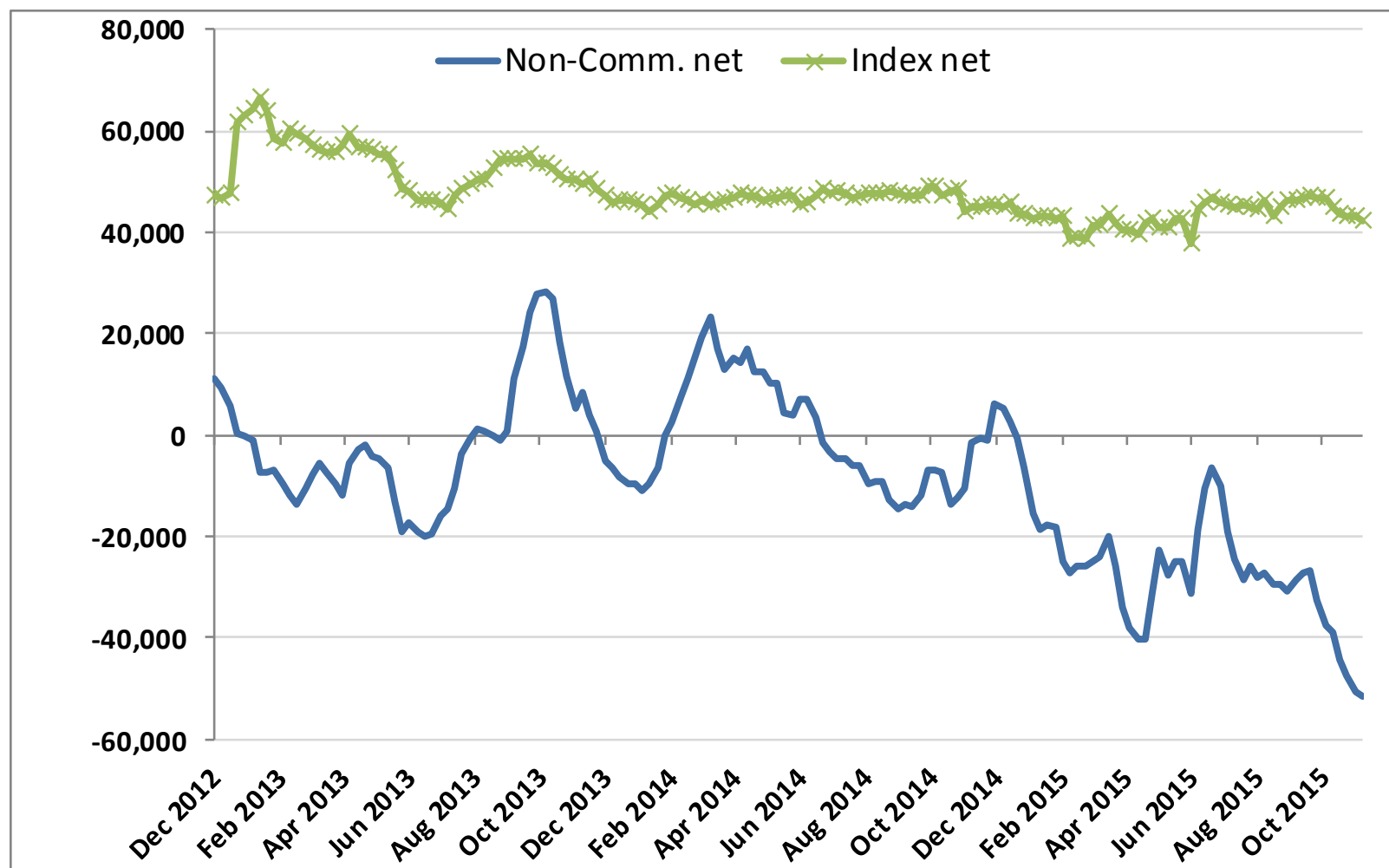


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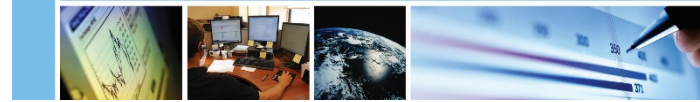


# Net Fund Positions-KCBOT Wheat

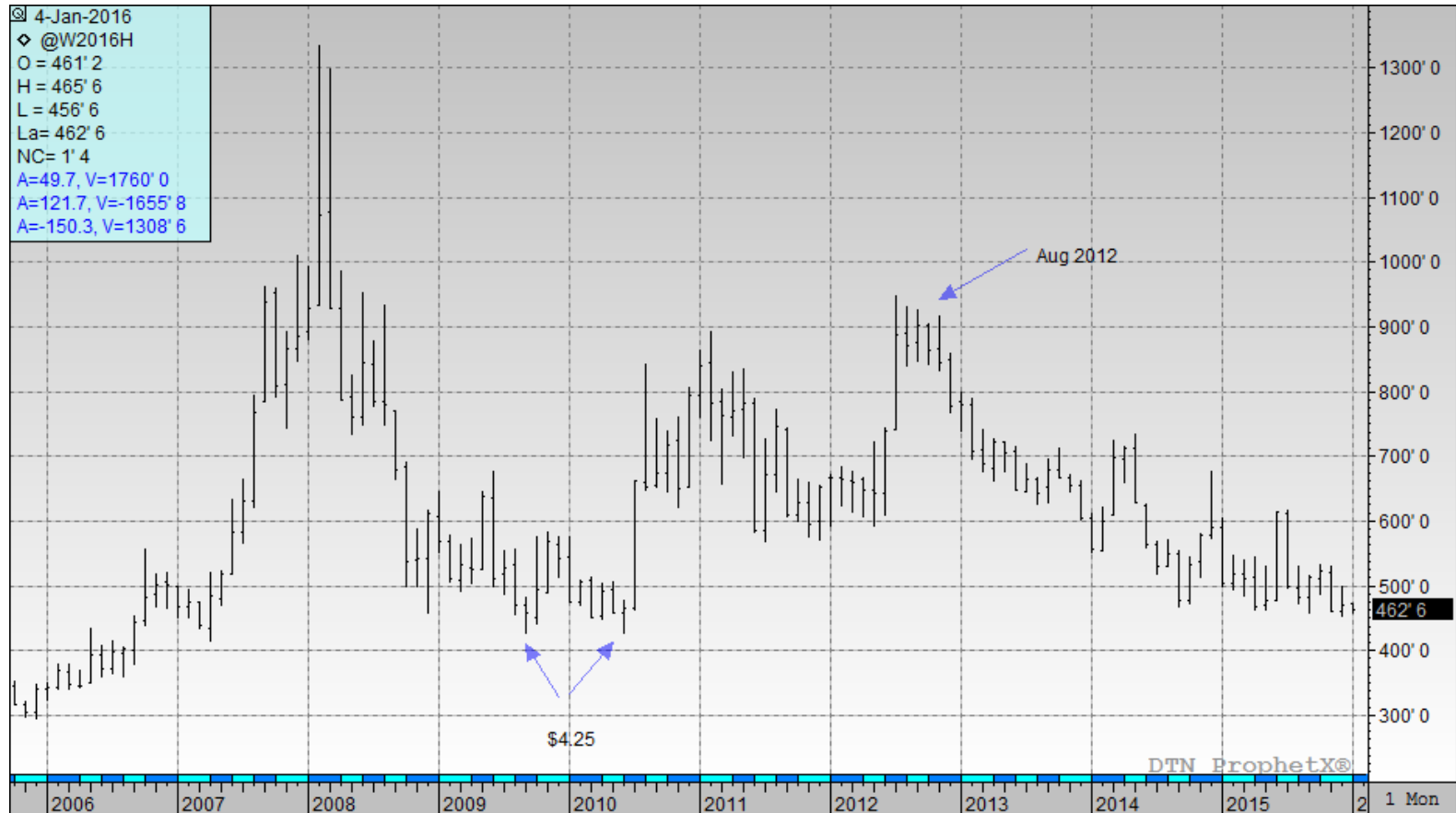
## CIT Report - Futures and Options Combined



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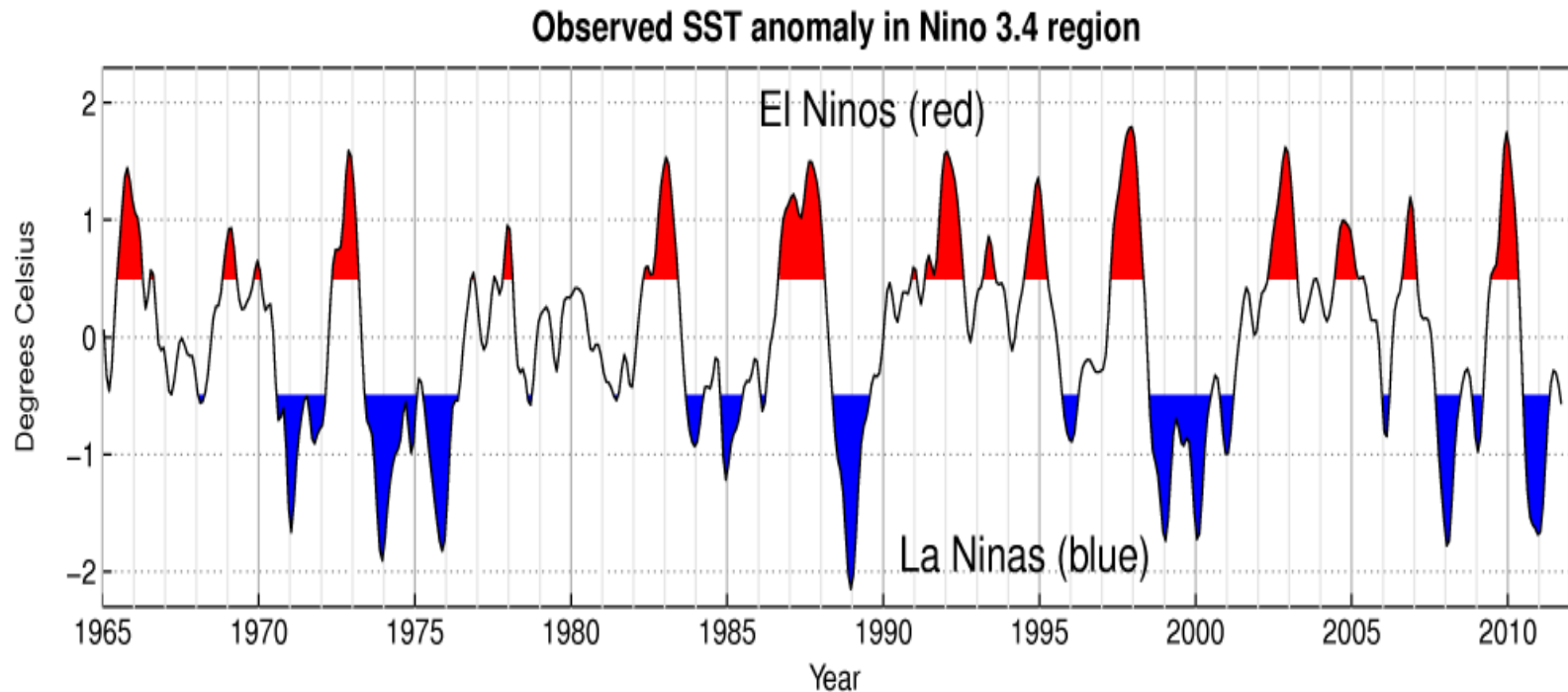
# Chicago wheat – continuous



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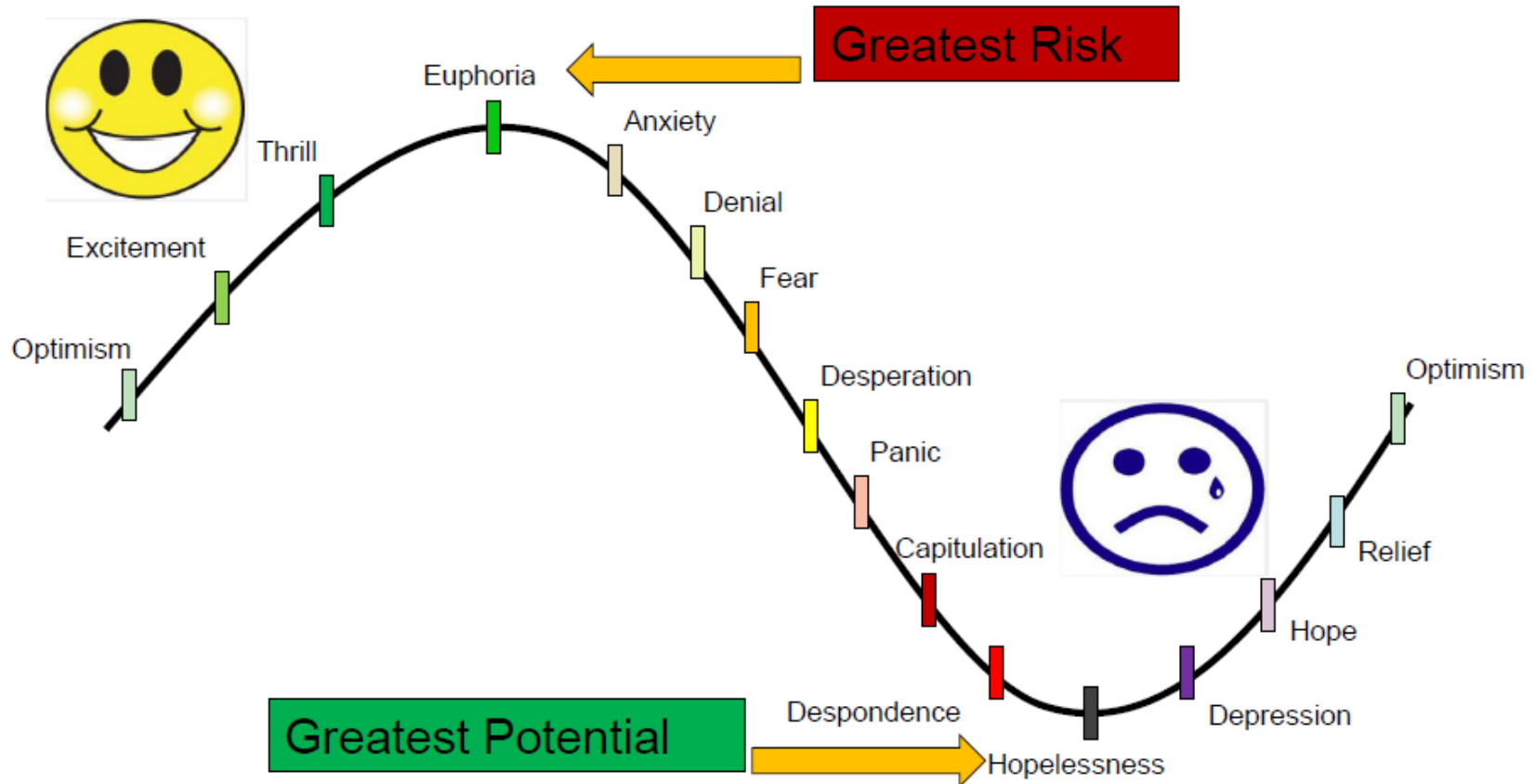
# Weather



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# Marketing: Emotion is the Problem



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# Thank you !

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