Grain Marketing Basics Workshop

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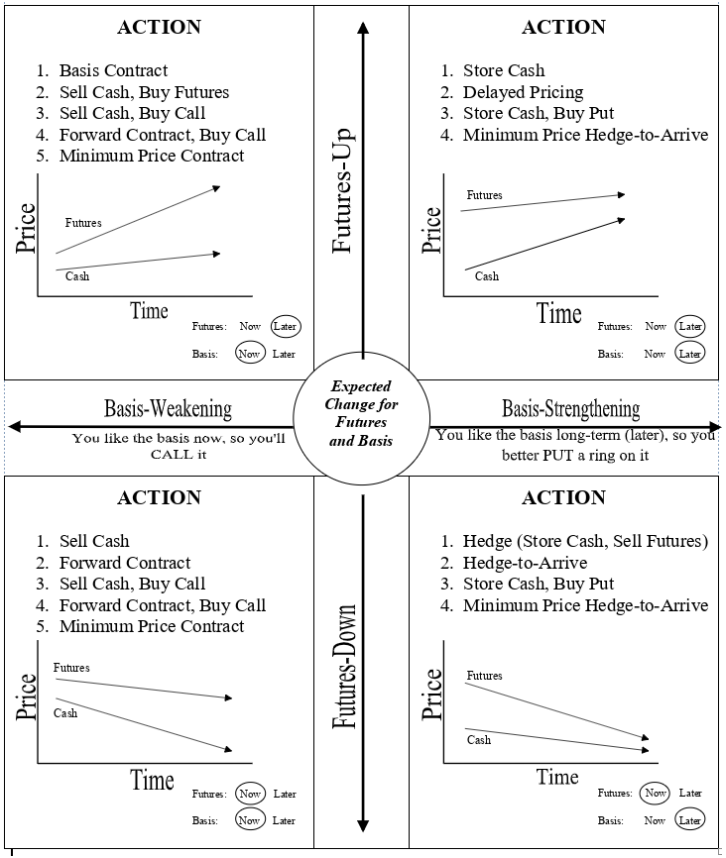
Tonight's plan

- Pricing decision tool
- When to store cash, buy put
- When to sell cash, buy call
- Guest speakers: Q&A with MAC
- Brief review

Quadrant pricing tool



- Shows which tools should be considered based on market expectations
- Need to form expectations about both futures and basis

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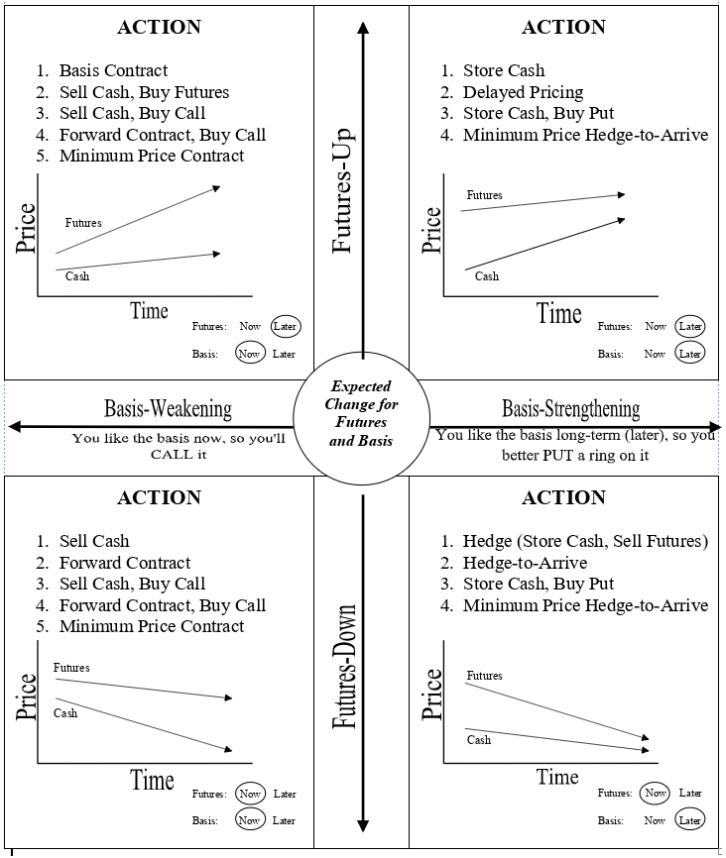

- Shows which tools should be considered based on market expectations
- Need to form expectations about both futures and basis
- **What if you aren't sure about futures?**

Options intro

- Options provide a "right to buy" or a "right to sell" a futures contract at a specified price.
- **Call option**: gives the holder the right to buy
- **Put option**: gives the holder the right to sell
- **Strike price:** the price at which the option provides the right to buy/sell
- **Option premium**: the market value of the option
  - The price of the "insurance"

What factors affect premiums?

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  - **Intrinsic value= 0**

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  - Strike price on **call**=5.50
  - Underlying futures=5.00
  - **Intrinsic value= 0**

- **Time value:** portion of the option premium resulting from the length of time to expiration

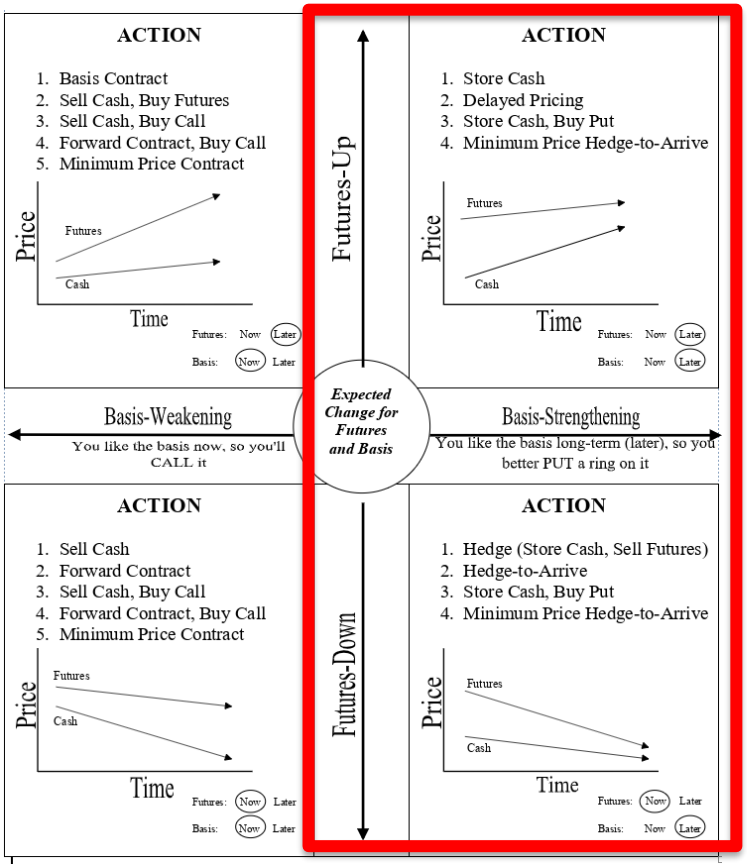
"In the money" vs "out of the money"

- **In-the-money** options have intrinsic value
- **Out-of-the-money** options do not have intrinsic value

Example: Suppose a May futures contract is trading at 5.00

- A $4 call is in-the-money, a $4 put is out-of-the-money
- A $5.05 put is in-the-money, a $5.05 call is out-of-the-money

Option tools for basis strengthening

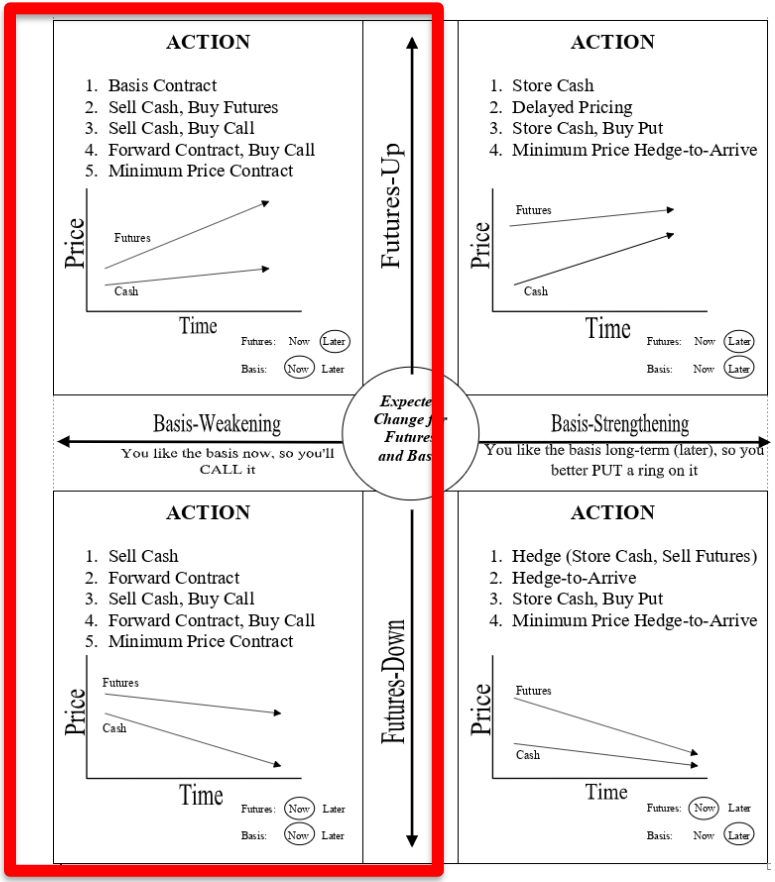


Store cash, buy put:

- Provided you have on-farm storage, you hold grain and wait for improved basis.
- Buying a put protects you against falling futures prices
- Still can benefit from price increases

Chalkboard videos 1 & 2 & 3

Option tools for basis weakening



Sell cash, buy call:

- Sell cash to lock in basis now
- Buy a call to take advantage of potential increases in the futures price
- Protected against price decreases

Chalkboard video 4

Q & A with MAC

Review

Cash Price = Futures Price + Basis

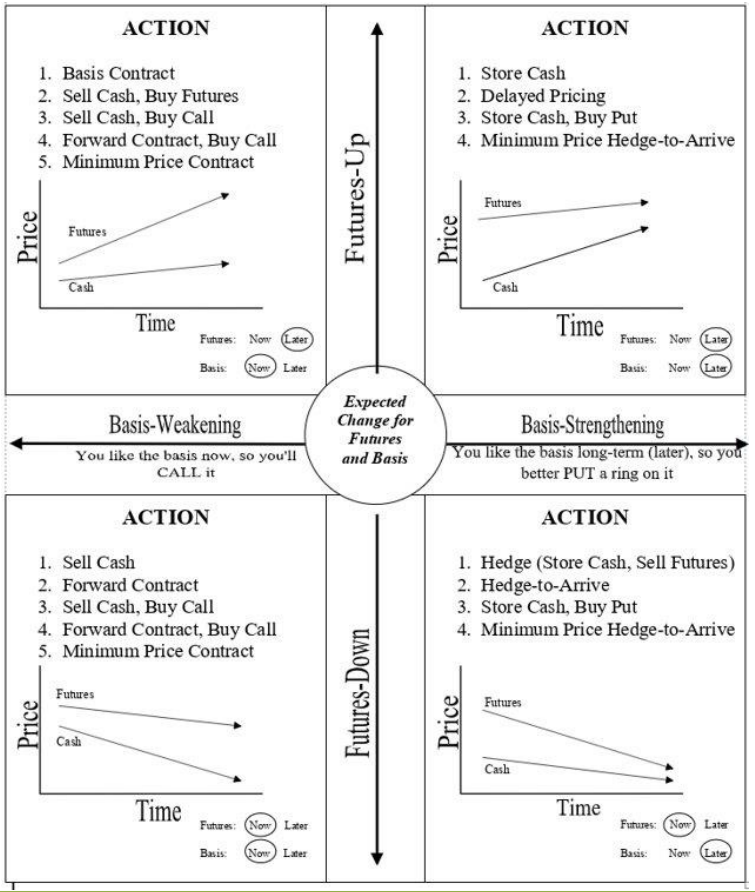
"Your price"
(if you're in the spot market)

World price

Local supply and demand factors

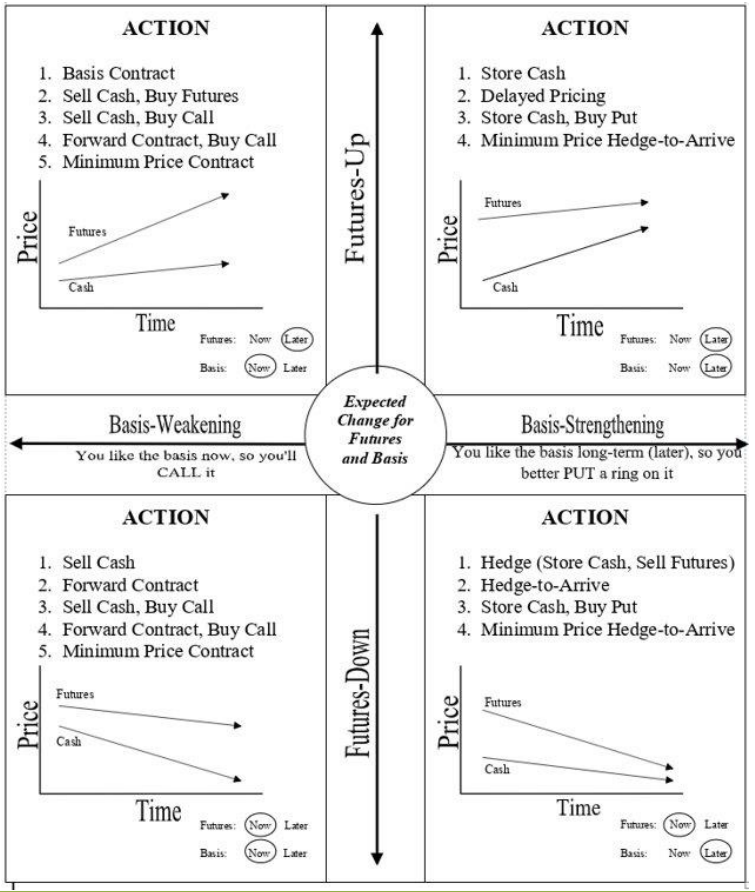
Review

- **Futures prices** are hard to predict
- **Basis** is easier to predict



Review

- **Futures prices** are hard to predict
- **Basis** is easier to predict
- Know when to get out of a hedge with breakeven basis



Other things to think about

- Knowing your cost of production (https://www.canr.msu.edu/resources/crop-budget-estimator-tool-detailed)
- Knowing your time value of money
  - What interest are you paying on your operating loan?
  - What's your storage cost?
- Creating a marketing plan
  - Starts before you plant with forward contracting
  - Have price triggers: "How would my plan change if prices went to $X?"
- How much risk can you afford? (https://www.canr.msu.edu/resources/farm-balance-sheet-template)

Thank you!

- All videos and slides for this workshop will be available to you
- More questions? E-mail me: gammansm@msu.edu
- Be on the lookout for an intro grain marketing online course through MSU. Will be based on the content in this workshop