Modifying Marketing Plans for Low Yields

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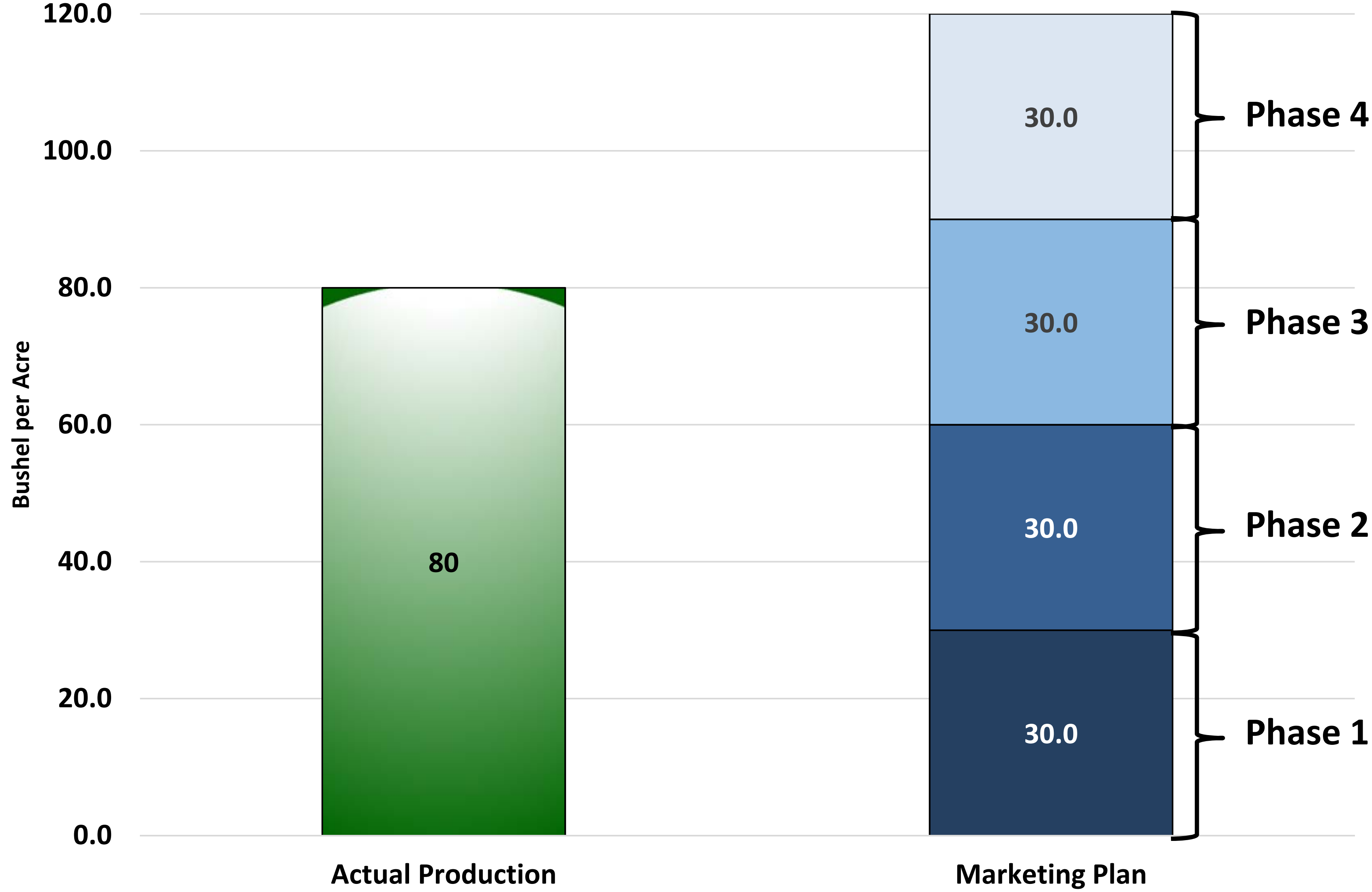
What happens when your marketing plan out performs your crop yields?

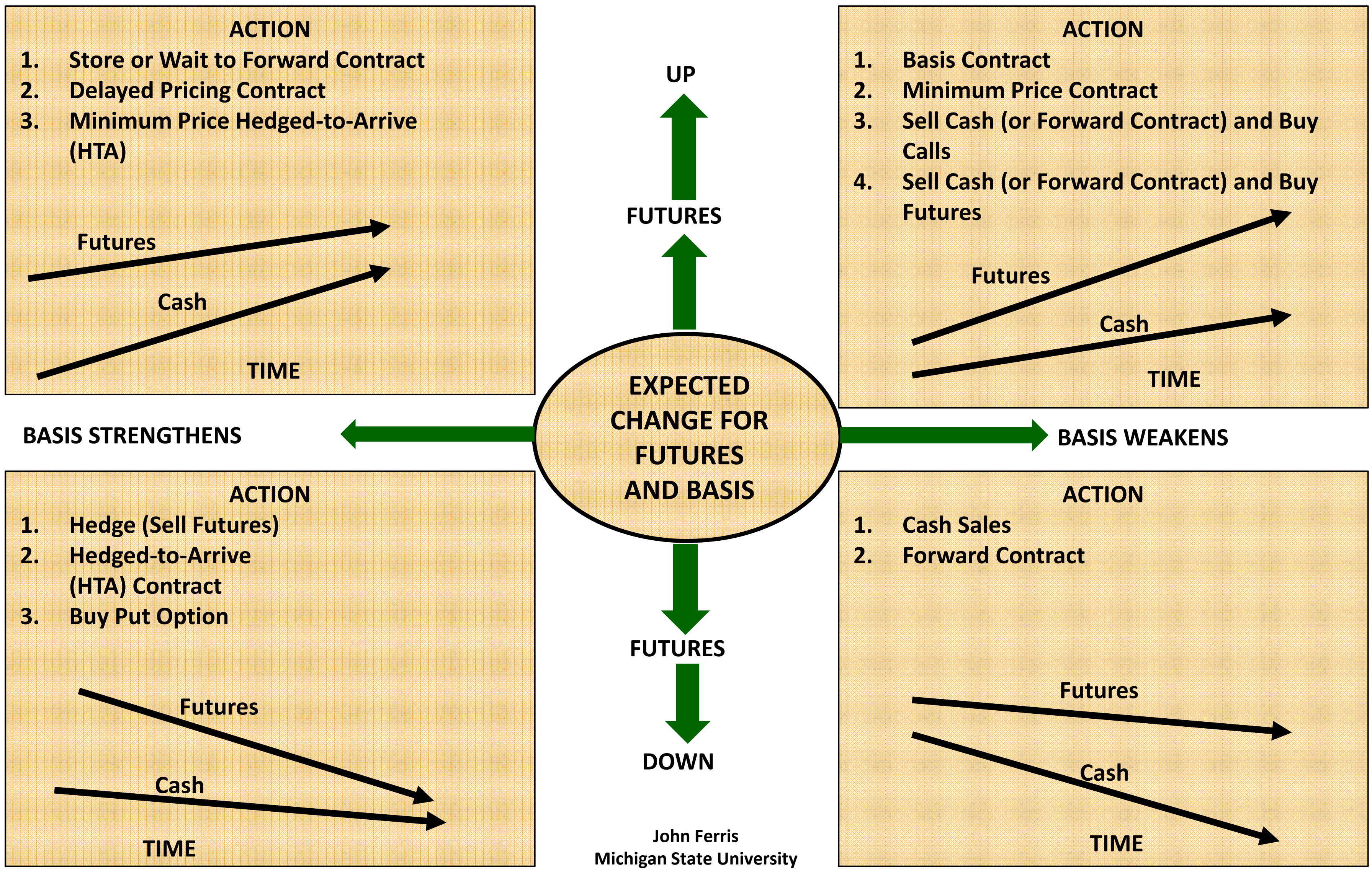
Marketing Plan vs Actual Production



It depends upon the marketing tool used, the timing of the shortfall, the degree of shortfall and local market conditions.

What Marketing Tool Was Used?

Strategies for Product Sellers



Why do I like this Matrix?

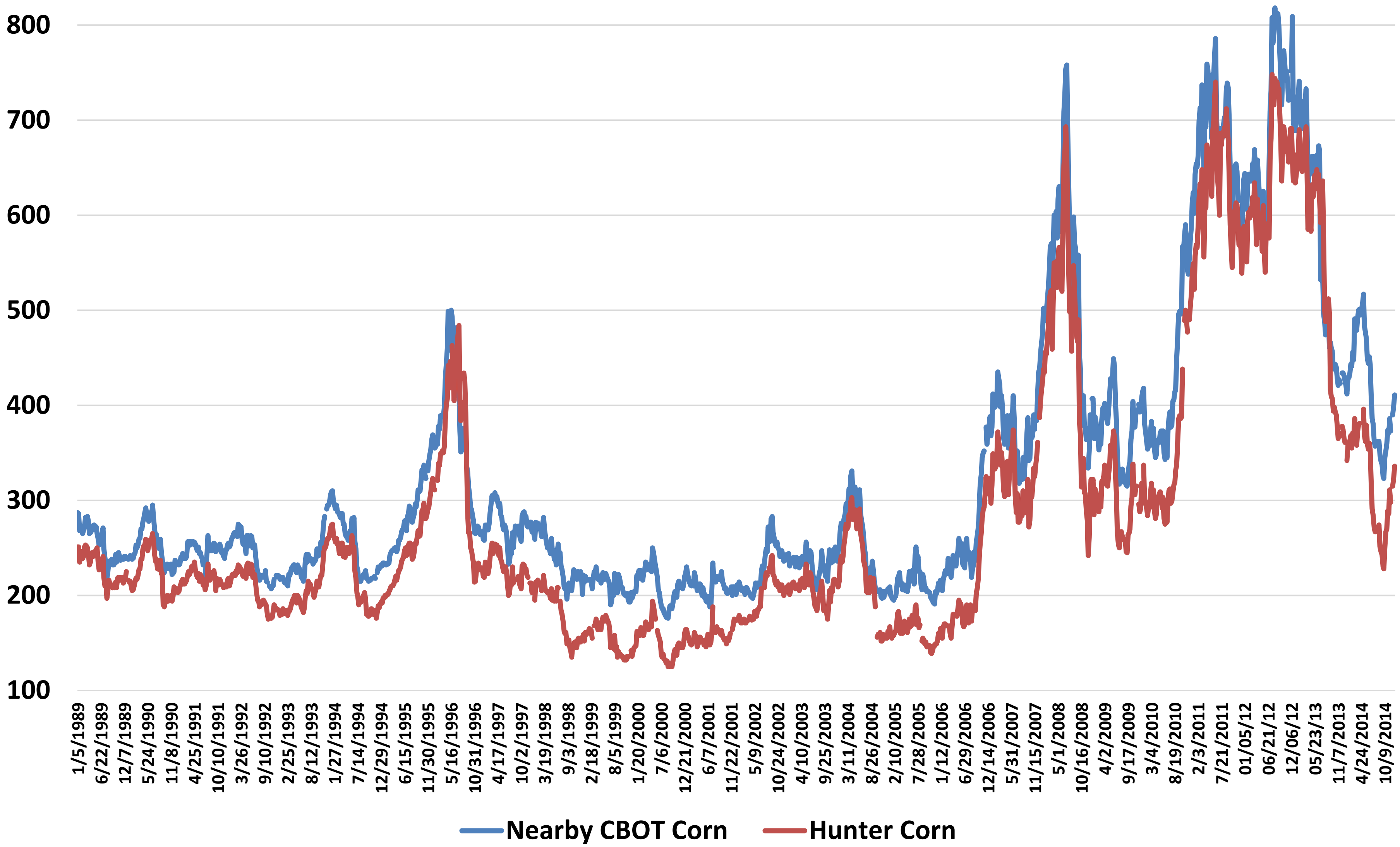
- Includes “cash only”, futures/options, and alternative contracting strategies.
- Helps explain why some marketing tools work well one year, and poorly the next year.
- Helps explain why basis changes can help enhance effective sales price.
- Helps highlight the differences in risk exposure.

Choosing a Marketing Tool

- Focus on marketing tools which incorporate futures strategies and futures based contracts.
- Not all marketing tools work equally well in different market conditions.
- Using the “correct” tool at the “correct” time can add to your bottom line.

Are Market Prices Becoming More Volatile?

Historic Corn Prices



Need for a Flexible Marketing Plan

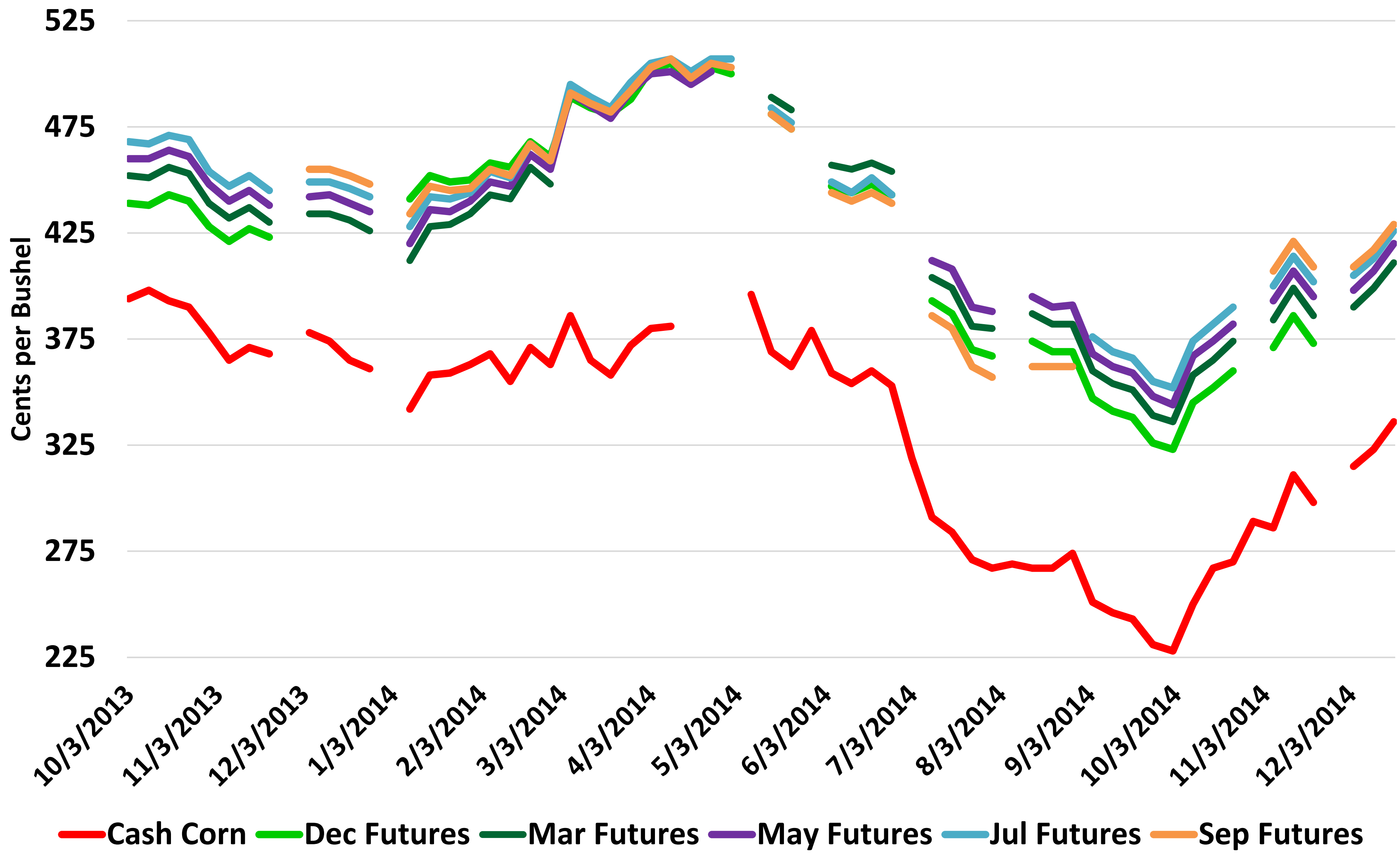
- Price volatility, ***across marketing years as well as within marketing years***, makes setting price and timing objectives more difficult.
  - Following a trend is easy, picking the turns is hard!
- More aggressive basis swings provide stronger incentive to manage on-farm inventories (storage).
- Choosing the correct marketing tool is becoming more important.

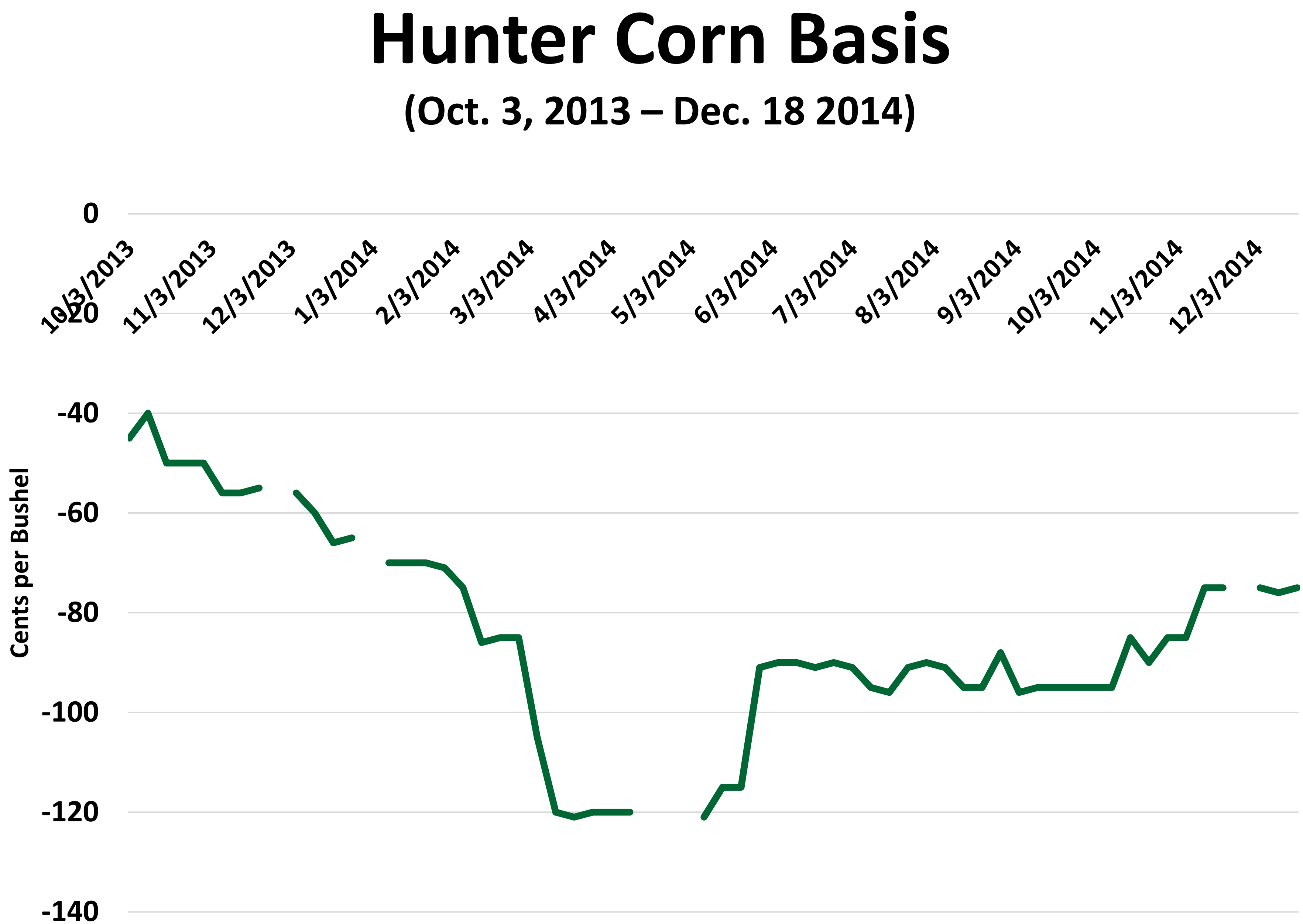
Watch the Basis!

- Cash and Futures Markets tend to move together, but not exactly at the same rate.
- **Basis = Local Cash Price – Nearby Futures Price**
- Cash and Futures Markets do not have the exact same participants with the same objectives.
- Cash and Future Markets do not respond at the same rate to new information.

CBOT Corn Futures vs. Cash Prices

(Oct. 3, 2013 – Dec. 18 2014)




Hunter Corn Basis
(Oct. 3, 2013 – Dec. 18 2014)
Cents per Bushel
0
-20
-40
-60
-80
-100
-120
-140
10/3/2013
11/3/2013
12/3/2013
1/3/2014
2/3/2014
3/3/2014
4/3/2014
5/3/2014
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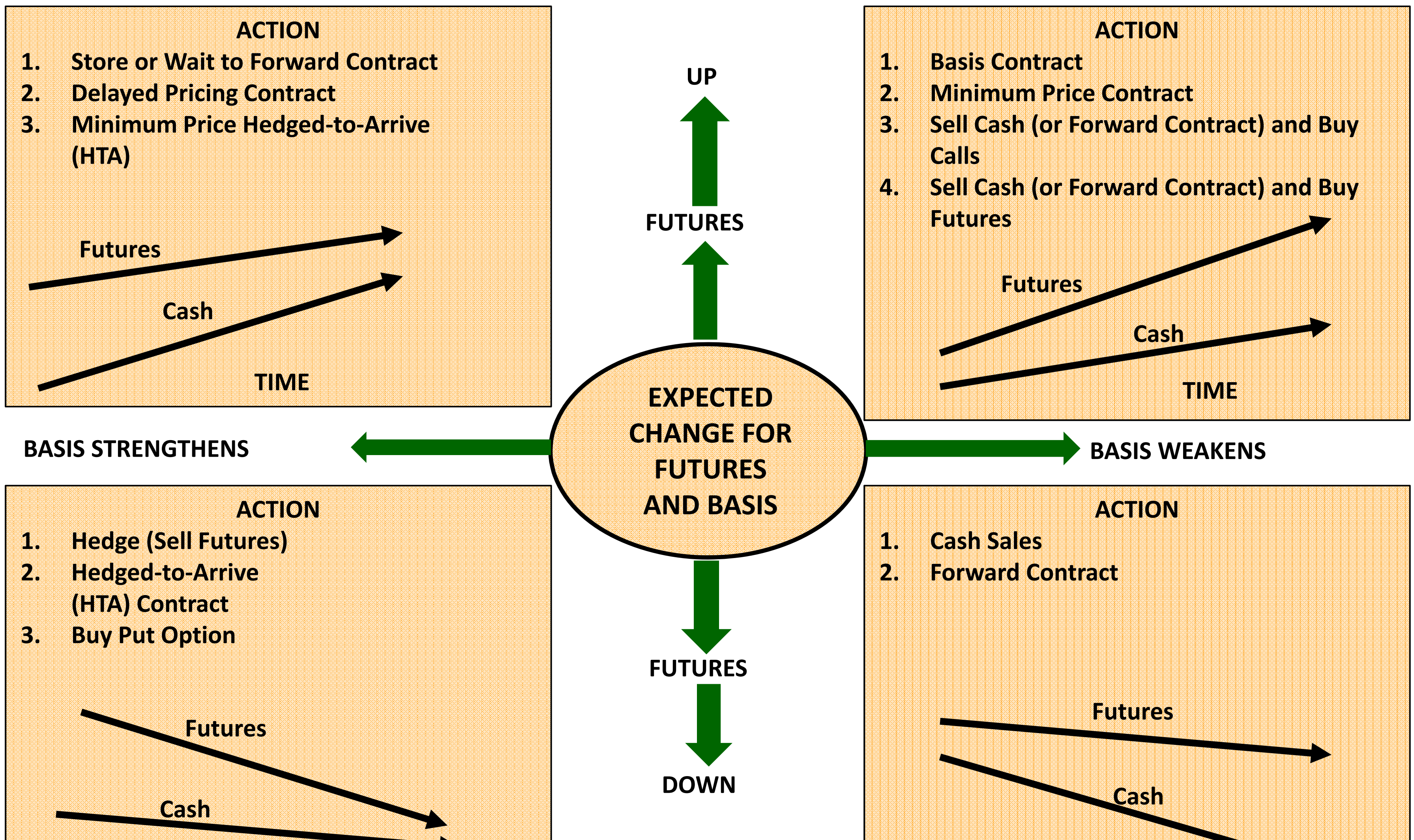
12/3/2014

Strategies for Product Sellers



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Are you trying to “lock in” a targeted price OR are you trying to enhance price?

What is the objective of the marketing strategy?

- Lock in a price = Hedging
  - Have opposite positions in two highly correlated markets at the same time
    - Buy (produce) cash corn and Sell corn futures
    - Sell cash corn and Buy corn futures
- Enhance price = Speculate
  - Own/Hold cash corn
  - Buy or sell corn futures or options contract

What happens when there is a shortfall?

Futures or Options Based Contracts

- Working directly with a broker.
- No requirement to deliver grain.
- Hold existing position(s) and recognize a hedge strategy has become a speculative strategy.
- Offset existing position(s) and recognize gain or loss.

Delivery Based Contracts

- Working with elevator or processor.
- Grain delivery is expected.
- Elevator/Processor does not want to be your broker!
- Timing: Notify buyer as soon potential shortfall is recognized.
- Size and timing of shortfall may impact the alternatives available to deal with situation.
- Expected to deliver production that is available.

Cash Forward Contract

- Deliver stored grain to fulfill shortfall.
- Buyer uses spot market <u>cash</u> price to cancel contract. Seller pays/receives difference between contracted price and spot price.
- Buyer uses change in <u>futures</u> market price to cancel contract. Seller pays/receives difference (basis in contract is used to determine price).
- Cancellation fees are normally charged.

Cash Forward Contract

- Contract is “rolled forward” into next cropping season. Price difference between current and forward price is incorporated into new contract.
- Next years contract price is forward futures price less contract basis.
  - Basis may also be adjusted if significant difference between original contract basis and forward basis exist.
- Service fees may be deducted from new contract price. (cover margin calls)

Futures Fixed/Hedge-to-Arrive

- Deliver stored grain to fulfill contract.
- Cancellation: Buyer offsets futures market position. Seller is charged/paid for any price difference, plus fees.
- Roll Forward: Contract is rolled into next cropping season. Price difference between current and forward futures price is applied to new contract, plus fees. Basis is open.

Minimum Price Contract

- Deliver stored grain to fulfill contract.
- Buyer offsets options market position. Seller is charged/paid for any premium price difference, plus fees.
- Rolling forward is possible, but may not make economic sense due to large option premiums.

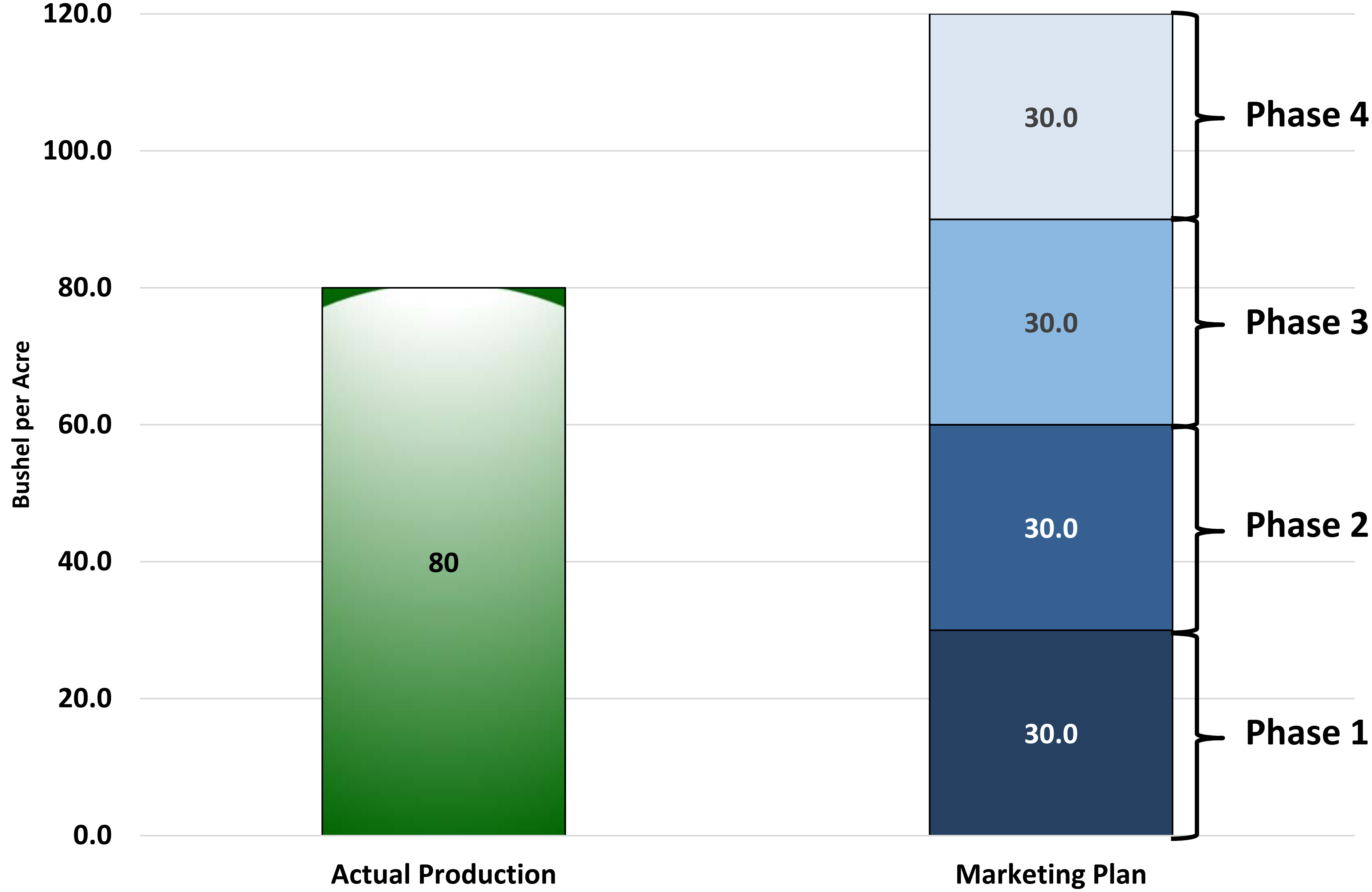
Basis Fixed Contract

- Deliver stored grain to fulfill contract.
- Buyer purchases spot market grain to fill shortfall. Seller is charged/paid for any basis difference, plus fees.
  – May be change in local basis or change in destination basis.
- Basis fixed contracts can be rolled forward, but usually at basis levels for forward delivery.

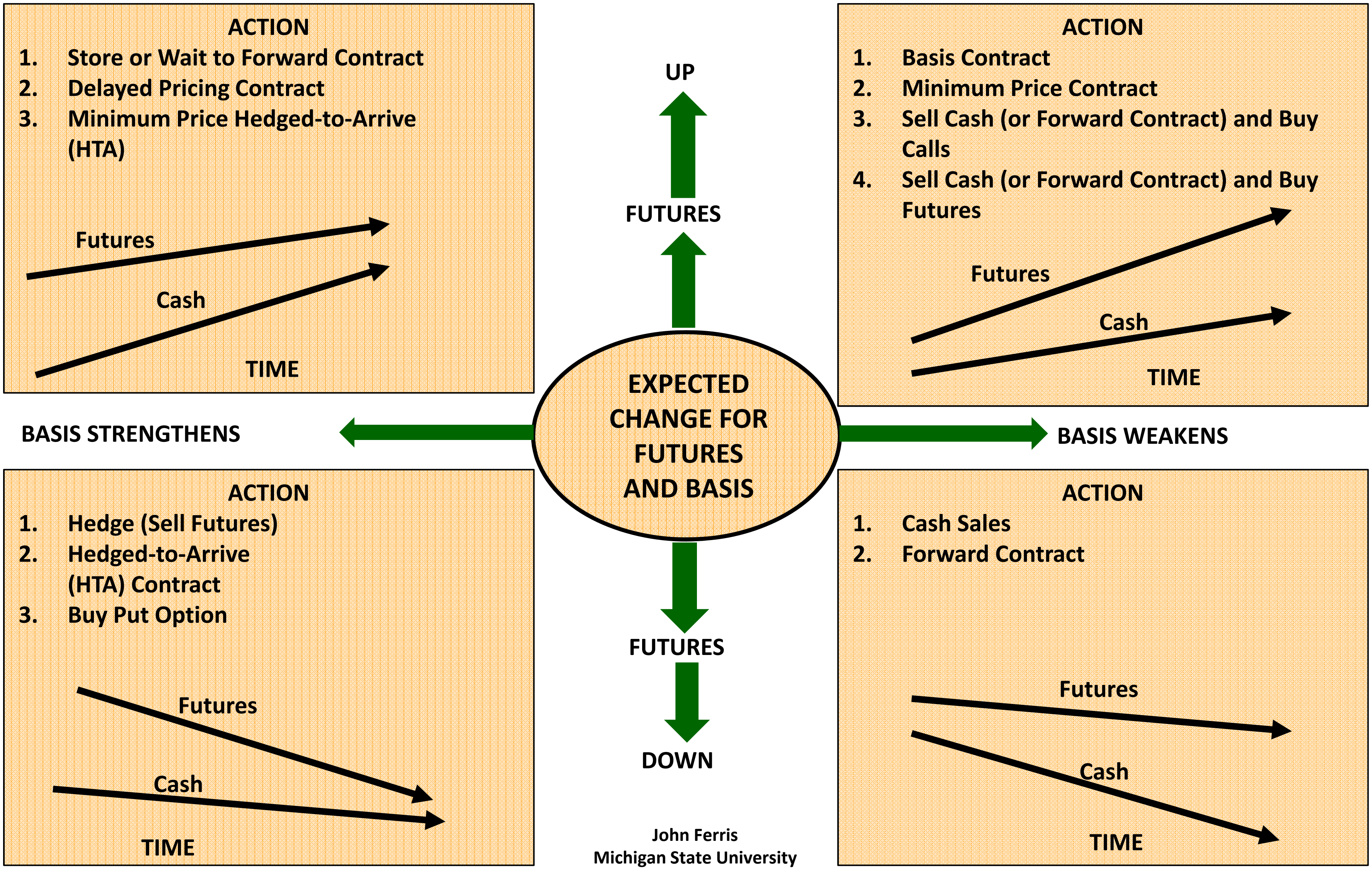
Factors Impacting Alternatives

- Is shortfall widespread in local market or unique to you?
  - May impact whether there is a basis adjustment (size of adjustment) and fees charged.
- Is shortfall realized early in the growing season or near harvest?
  - May impact whether there is a basis adjustment and fees charged.
- Have crop prices changed significantly?
  - Increase
  - Decrease

Marketing Plan vs Actual Production



Strategies for Product Sellers



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Questions?