Agricultural
Marketing Guide >>

A Grain Marketing Decision Tool

Introduction

Strong marketing skills are important for a successful farm. This article will describe a decision process that can be used to help make grain-marketing decisions.

> For an introduction to the topic see **“Developing a Marketing Plan for Your Crops”** on our YouTube channel: http://www.youtube.com/watch?v=drwUuM4vh20

Why Use a Decision Grid?

Farmers are faced with more pricing and marketing alternatives than ever before. Should they spot price? Hedge? Forward contract? Lock in basis? There are many alternatives available, and properly used they can help manage price risk. However, farmers must know when and how to use each one.

There are a considerable number of pricing and delivery alternatives for marketing crops on the open market. Farmers must assess all of these marketing alternatives to make sound crop marketing decisions. Marketing alternatives and signals may be different when making marketing decisions about binned crop (where you have full information) and crop that’s still growing in the field (where there is still uncertainty about yield, quality, and grade).

The market decision processes presented in this article can be applied to all crops that use futures markets for price discovery.

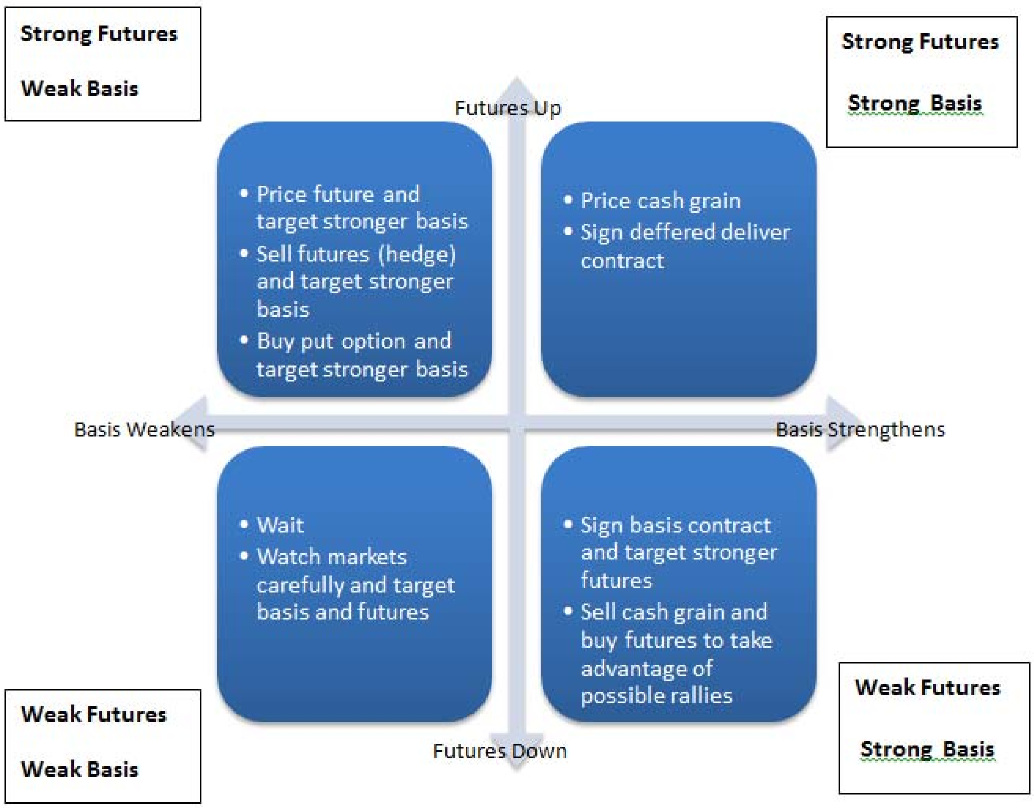
The Decision Grid

The decision grid helps to analyze prices and breaks these prices down to their component parts – futures and basis.

The **futures price** is the price that is traded on futures markets. A strong futures price is one that is high or higher than expected under current circumstances. This doesn’t mean the futures price is at, near, or above historical highs.

The **basis** is the difference between the near futures price and the local cash price. A strong (narrow) basis means the cash price is high relative to the futures market. This usually means local supplies are limited or that local demand is strong. A weak (widening) basis means the cash price is low relative to the futures market. This signals weakening local demand or over supply in the local market.

As a marketer develops experience over time, they are able to determine what are historically strong or weak futures prices and basis. This decision grid can be used to choose your marketing tools based on what you expect to happen with the futures price and basis.



First let's look at the decision grid, starting with '**strong futures, weak basis**.' This is a signal to take action on the strong futures price and to wait for better basis. One way to do this is to sell deferred futures and store your grain. A second way to do this is to buy a put option, which sets a minimum price at which you may sell your grain. Brokers charge a premium on the purchase options, so you only make a net gain if prices go down more than you paid for the option.

Now, let's look at '**strong futures, strong basis**.' This is a signal to price cash grain or sign a deferred delivery contract to lock in the good basis and futures price.

Next, let's look at '**weak futures, weak basis**.' This scenario often occurs right after harvest, when many farmers are looking to sell and storage may be filling up. This is a signal to store your grain and keep a close eye on the markets for opportunities. Wait for basis and futures
price to improve.

Finally, let's look at '**weak futures, strong basis**.' If futures prices are lower than expected, but local buyers are still bidding on deliveries, basis may be strong. A good approach here is to sell your grain for cash prices to take advantage of the strong basis. While selling grain you can also purchase futures or a call option to take advantage of any rally in the futures price. Alternatively, you could sign a basis contract to lock in the favourable basis price. Finally, waiting it out is always an alternative.

Summary

They key to making solid grain marketing decisions is keeping informed. Having a marketing plan with reasonable profit targets means you can capitalize on marketing opportunities when they arise.

Other Resources

Introduction to Crop Marketing
http://www1.agric.gov.ab.ca/$department/deptdocs.nsf/all/sis11390

Open Market Crop Contracts
http://www1.agric.gov.ab.ca/$department/deptdocs.nsf/all/sis10994

Basis – How Cash Grain Prices are Established
http://www1.agric.gov.ab.ca/$department/deptdocs.nsf/all/sis10871

Using Hedging to Protect Farm Product Prices
http://www1.agric.gov.ab.ca/$department/deptdocs.nsf/all/sis10282

Grain Storage as a Marketing Strategy
http://www1.agric.gov.ab.ca/$department/deptdocs.nsf/all/sis10941

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