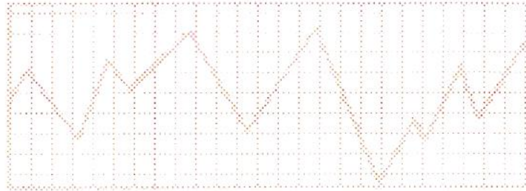

WEEKLY OUTLOOK

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PRICING NEW CROP CORN AND SOYBEANS

Historically, some of the best pricing opportunities for corn and soybeans occur during the growing season. The reason is fairly obvious. Weather and crop concerns or actual crop problems result in premiums in the market. Those premiums then disappear as weather and crop conditions improve. Over the past 20 years, December corn futures have established a contract high in the June through September period 9 times. On 7 other occasions the contract high was established in the July through October period of the previous year.

The pattern has been almost identical for November soybean futures. Highs occurred in the May through September period 9 times and in the June through October period of the previous year 7 times.

The current contract highs for December 1993 corn futures and November 1993 soybean futures were established in May 1992, at $2.685 and $6.20, respectively. Based on historical patterns, it is unlikely that those highs will stand as the contract highs. Periods of weather concerns during the upcoming growing season are expected to result in new highs. At the close of trading on January 22, December futures were $.23 below the contract high and November futures were $.25 below the high.

Even when good pricing opportunities are expected and then present themselves, making pricing decisions in a weather-related price rally is difficult. Two sources of significant uncertainty might exist for individual producers — extent of yield reduction, if any, resulting from weather problems and the likely duration and magnitude of the price rally. That is, a producer may be concerned about forward pricing too much and/or too early. Producers may want to consider marketing strategies that include the use of the options market to help manage the risk associated with price rallies during the growing season. Consider the following examples in the corn market.

Strategy I is for a producer who is confident that a price rally will occur during the 1993 growing season, wants to price a significant portion of the crop on that rally, but wants some protection in the case of a significant price increase after the crop has been priced. That producer might consider buying out-of-the-money call options in a deferred contract yet this winter, while price volatility is low and options relatively low priced. When prices rally this spring or summer, the producer would have the confidence to price new crop

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corn. The call options would allow the producer to gain most of the benefit of further rallies if they occurred. With this strategy, the producer might consider buying call options with a strike price near the likely level of a spring/summer price rally. In the past 2 years, for example, December futures have rallied to the $2.70 to $2.75 area during the growing season. A larger supply this year might result in a smaller rally. On January 22, a September 1993 call option with a strike price of $2.60 was priced at $.0875 per bushel. A $2.70 call was priced at $.0625 per bushel. The major risk of this strategy is that prices do not rally and actually move below current levels. In that case, the producer approaches harvest with none of the crop sold.

Strategy II is for the producer who prefers to make pricing and options decisions simultaneously, rather than one leg at a time. For example, a producer might choose to price new crop corn now to take advantage of the higher prices being offered for new crop corn. At the same time, the producer could purchase a call option with a lower strike price, say $2.40 or $2.50. On January 22, September call options with those strike prices were priced at $.145 and $.1175 per bushel, respectively. To lower the cost of the options, call options with a higher strike price could be sold. This strategy allows the producer to benefit from higher prices if they occur, but also establishes a ceiling on price.

The strategies outlined here are just two of a large number of strategies that could be considered for 1993. The important point is that now is the time to form price expectations for 1993 and to put a marketing plan in place.

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