True or False (Each question counts as 2 points)

1. The change in the basis under July futures from harvest time to late spring is the gross hedging return for storage for that time period  

2. Historical records show that there is a 50% chance that December corn futures contract prices will rise from winter and spring to harvest time.

3. The Loan Deficiency Payment (LDP) is always the amount that the cash price is below the CCC loan rate.

4. Hedge-to-Arrive (Futures only) contracts lock in the basis but not the futures.

5. A different grain marketing strategy may be needed for farms with a high yield risk than for those in areas with lower yield risk.

6. Counter-party risk in grain contracts is the risk that the company you are doing business with will not fulfill their contractual obligations.

7. The cash-flow breakeven price is calculated by dividing the total cash-flow costs per acre for producing the crop (after deducting government payments) by the expected yield per acre.

8. Crop-share renting of land offers producers less flexibility in marketing grain than cash-renting of land.

9. When determining the effective hedge price, the two main items to subtract from the initial futures price are (1) the expected basis under the relevant futures contract when the hedge is lifted and (2) brokerage fees.

10. It is almost always better to use the Marketing Loan to take advantage of the low CCC interest rate rather than to take the LDP at harvest.

11. When a grain producer buys call options, he/she has a profit if futures prices decline.
12. When a person sells a corn, wheat, or soybean call option, he/she has a profit if prices rise above the strike price. _______

13. When a person buys a corn call option, his/her maximum potential gain is known. _______

14. If a grain producer buys a put option to market the crop, the transaction establishes a price floor. _______

15. If a grain producer buys a put option to market grain, it allows him/her to benefit if prices increase later in the year. _______

16. China is a major market for U.S. corn. _______

17. The basis under July futures has a definite seasonal pattern. _______

18. Automated grain contracts concentrate a producer’s sales in the time period when prices historically have had a strong tendency to be at their highest levels. _______

19. Automated grain contracts provide a specific known sale price at the time the farmer enters into the contract. _______

20. With accumulator contracts, a farmer knows at the time the contract is signed how many bushels have been sold and the exact price of those bushels. _______

21. New generation grain contracts typically are offered to farmers at no additional cost. _______

22. Cash-flow requirements for producing corn can vary from one farm to another by as much as $1.00 per bushel. _______

23. With new-generation grain contracts, farmers need to watch the local basis and make decisions about when to lock it in after the contract has been signed. _______

Fill in the blanks
(Each question counts as 2 points)

1. Purchasing a put option gives the buyer the ________ but not the __________ to _______ _______ _______ _______.
2. Purchasing a call option gives the buyer the _______ but not the _______ to _____ _______ ________ ________.

3. A synthetic put involves selling grain on futures or forward contracts and _______ (what kind?) options.

4. The purposes of a synthetic put are to _______ _______ _______ and _______ _______ _______.

5. Elevators are offering “New Generation” grain contracts because of pressure to _______ _______ _______.

6. Premium-offer contracts involve sale of _______ options.

7. The incentive for farmers to use Premium Offer contracts is to gain a _______ over _______ prices.

8. Marketing needs and appropriate marketing strategies are strongly influenced by what two individual farm risk-related factors? ________________ and ________________.

9. Selling corn or soybeans before harvest at prices below the loan rate is high risk because the _____ and ________________ cannot be locked in at the same time the grain is sold.

10. Crop Revenue Coverage Insurance insures _______ per acre.

Multiple Choice -- one correct answer for each  (Each question counts as 2 points)

1. When a grain producer buys call options, he/she (a) establishes a floor on the selling price of the grain, (b) establishes a market position similar to a forward contract, (c) retains the right to benefit from higher prices if the futures market rises substantially.

2. The net worth risk ratio measures (a) the break-even price that must be received from the crop to cover costs, (b) the price per bushel at which 10% of the equity in the grain enterprise is lost, (c) the maximum dollars per acre which can be lost in any one year before a predetermined percentage of the equity is lost.

3. CRC insurance is a tool that (a) insures net revenue per acre, (b) always protects against lower prices, (c) is an important potential companion tool for pre-harvest grain sales.

4. A synthetic put is (a) a simultaneous sale of futures contracts and purchase of a call option in the same contract month, (b) a simultaneous sale of futures contracts and sale of a call option in the same contract month, (c) a simultaneous sale of futures contracts and purchase of a put option in the same month.
5. A synthetic put is designed to (a) establish a price floor while retaining the opportunity to gain if prices rise sharply, (b) generate additional income to help pay the brokerage cost from selling futures contracts.

6. A University of Illinois evaluation of grain market advisory services shows that (a) all advisory services have consistently provided their customers with a higher price than the average price received by farmers for the marketing year, (b) only 3 out of 16 advisory services were able to beat the farmer benchmark corn price and 1 out of 15 were able to beat the farmer soybean benchmark price every year, (c) 8 out of 16 advisory services were able to beat the farmer benchmark price every year, (d) there is little variation in performance from one advisory service to another.

7. A University of Illinois evaluation of grain market advisory services shows that (a) most individual market advisory services are able to beat the farmer benchmark price by about the same amount each year or (b) advisory service performance varies substantially from year to year.

8. New-crop corn and soybean futures prices in the winter and spring before harvest since the mid-1970s have been (a) above harvest-time prices much more often than below harvest-time prices, (b) below harvest-time prices much more often than above harvest-time prices, (c) above and below harvest-time prices with about equal frequency.

9. If the corn basis under July futures is –78 at harvest and normally has been –34 in early June, (a) the market is discouraging farmers from storing, (b) signaling that cash prices will be higher in the spring, (c) offering a significant return for hedging & storing corn to early summer.

10. An important starting point in developing an individual farmer’s marketing plans for the coming marketing year is (a) watching commodity price charts, (b) estimating the break-even cash-flow cost per bushel.

11. Consider this market situation: Corn market conditions at harvest reflect a very depressed basis and a large carry in the futures market (premium of the next July futures contract price above the near-by December contract. Which of the following marketing strategies would be most appropriate for these conditions: (a) store and buy July futures, (b) sell for later delivery using a basis contract, (c) sell on a HTA (futures only) contract based on July futures, (d) sell at harvest.

12. The soybean market at harvest reflects the following conditions: a very strong basis, a market inverse with May and July futures for the next calendar year being well below those of the current November futures. Which of the following marketing strategies would be most appropriate for these conditions: (a) store and hedge by selling July futures, (b) sell on a HTA (futures only) contract based on July futures, (d) sell at harvest.
Complete the calculations (Each question counts as 2 points)

1. Calculate the net returns for hedging and storing from harvest to late January and to late May with the following information:
   - Cash price: $1.84
   - Mid-Oct. Dec. futures price: $2.20
   - Mid-Oct. July futures price: $2.30
   - Expected basis under July futures in late January: -$0.38
   - Expected basis under July futures in late May: -$0.27
   - Storage costs to late January: $0.10
   - Storage costs to late May: $0.16

   Show your calculations.

2. Calculate the effective (or actual) December futures hedge price from the following information:
   - December corn futures sold in January before harvest at $2.48 per bushel.
   - December futures at harvest time: $2.15 per bushel.
   - Forward contract price in January before harvest: $2.10 per bushel
   - Cash price at harvest: $1.80 per bushel
   - Brokerage fee: $0.01 per bushel
   - Expected harvest basis under December when futures were sold: -$0.36 per bushel

   Effective hedge price: $________/bu.

3. Use the following information to determine the price needed to cover cash-flow costs of production for the following producer:
Total cash-flow costs per acre after deducting expected govt. payments, without family living expenses: $326
Total cash-flow costs per acre after deducting expected govt. payments and including family living: 351
Normal yield 180 bu./A.

$_____ /Bu.

Should family living be included as a cost of production for marketing purposes? _____ Yes _____ No.

4. What key financial item or items explain why a young farmer may not want to pattern her/his marketing strategies after those of an older, established farmer in the neighborhood.

______________________________.

5. Given the following information from the peak of the harvest season, calculate what the market is willing to pay farmers to store their corn crop until late spring:

<table>
<thead>
<tr>
<th>Situation</th>
<th>December futures price</th>
<th>July futures price</th>
<th>Local cash corn price in October</th>
<th>Expected basis under July in May</th>
</tr>
</thead>
<tbody>
<tr>
<td>I</td>
<td>$2.35</td>
<td>2.48</td>
<td>2.00</td>
<td>-0.31</td>
</tr>
<tr>
<td>II</td>
<td>1.98</td>
<td>2.20</td>
<td>1.55</td>
<td>-0.34</td>
</tr>
</tbody>
</table>

Potential gross storage hedging returns _____ _____

Show your calculations

Extra Credit (2 points each):
A.) List four “new generation” grain contracts:

1. __________________________________________________________

2. __________________________________________________________

3. __________________________________________________________

4. __________________________________________________________
B.) List three overall economic functions that need to be performed by the grain marketing system (2 points each)

1. __________________________________________________________________________

2. __________________________________________________________________________

3. __________________________________________________________________________

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