

Econ 337 Agricultural Marketing, Spring 2018
 In Class Activity 1, January 23, 2018

Basis and the ability to hedge wheat					
	Action	Date	Cash Price	Futures Price	Basis
Scenario 1 Price levels rise basis increases	Plant crop Sell futures	April 15	\$7.50	\$8.00	-\$0.50
	Sell crop and offset futures	October 15	\$8.00	\$8.25	-0.25
	Profit/bu				
		Effective Price Received			
Scenario 2 Price levels fall basis increases	Plant crop Sell futures	April 15	\$7.50	\$8.00	-\$0.50
	Sell crop and offset futures	October 15	\$7.00	\$7.25	-\$0.25
	Profit/bu				
		Effective Price Received			
Scenario 3 Price levels rise basis decreases	Plant crop Sell futures	April 15	\$7.50	\$8.00	-\$0.50
	Sell crop and offset futures	October 15	\$8.00	\$8.75	-\$0.75
	Profit/bu				
		Effective Price Received			
Scenario 4 Price levels fall basis decreases	Plant crop Sell futures	April 15	\$7.50	\$8.00	-\$0.50
	Sell crop and offset futures	October 15	\$7.00	\$7.75	-\$0.75
	Profit/bu				
		Effective Price Received			

In order to hedge using futures a farmer takes a short position in the futures market at the time he wants to lock in his price. Unfortunately, variation in the basis reduces the effectiveness of his hedge.

1. Fill in the shaded cells to indicate the profit (per bushel) he receives in the cash market, the profit he receives on his futures position, and his effective price received.

2. Farmers who have hedged are said to be long in the basis. Explain why this is true.