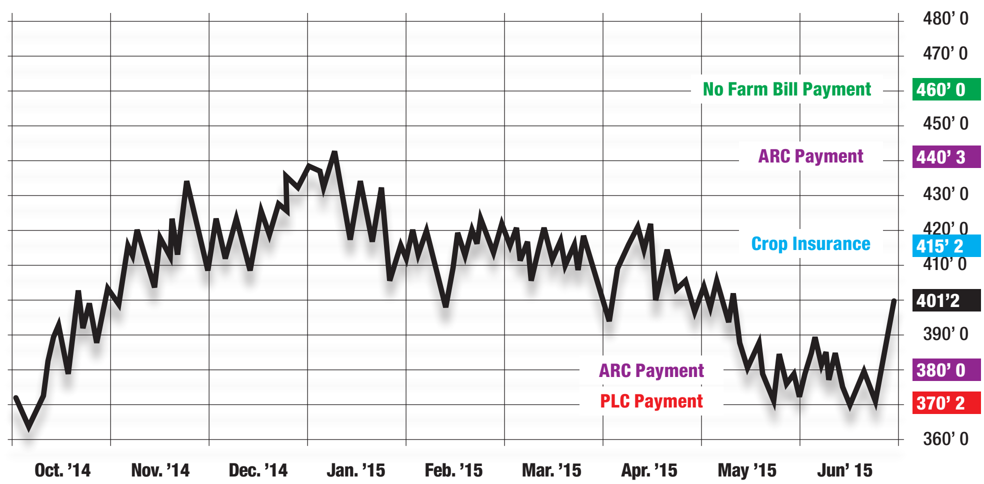
By Al Kluis

December 2015 CBOT Corn



This is the chart of December 2015 CBOT corn futures. You can see the $4.40 high made in late December 2014. From that high, prices dropped all the way back to the recent low at $3.65. Long-term chart support is at the low at $3.18 from September 2014. If corn prices stay at this level or move lower, most Corn Belt farmers will have a crop insurance claim and will likely receive large ARC-CO payments.

PROBLEMS AND OPPORTUNITIES FOR BIG CROPS

CONSIDER PREHARVEST ALTERNATIVES NOW.

At a marketing seminar this spring, a frustrated Iowa farmer raised his hand. “I didn’t think we could have two big corn crops in a row,” he said. “I already had cash corn to sell, and now I have new-crop corn I need to get sold. What should I do?”

I told him I was also surprised at the relentless bear market in corn again this spring and summer. On top of his concern about the price of the cash corn he was holding (some of which was in commercial storage), the big new crop meant he would need to sell ahead at least 50% of his new crop or put it in commercial storage at harvest, too.

I asked him a lot of questions and then explained several alternatives. One recommendation was easy. I told him to sell the cash corn he was holding in commercial storage and to replace with call options. He had a good basis. My concern was that if corn futures rallied, then the cash basis would deteriorate. Holding cash corn was a lose-lose proposition. If some weather-related problem developed and futures rallied, then it was cheaper – and less risky – to hold call options than to continue paying interest at the bank and paying storage charges to the elevator.

The second part of his question, about that new-crop corn, was a lot tougher. It was hard for me to recommend that he sell his crop ahead when the new-crop price was below his cost of production (and below the crop insurance guarantee) even if it looked like prices were still heading lower.

It is frustrating to watch December 2015 corn futures go under $3.70. However, if you are a Corn Belt farmer who has crop insurance and you are enrolled in the ARC-CO program, you do not have a lot of additional financial risk. The lower the new-crop corn prices go, the higher your likely crop insurance payment will be. Your potential farm program payment increases at the same time.

WHAT TO DO

Consider these three alternatives prior to corn harvest.

1. Puts. Buy some at-the-money put options. Corn prices are likely to keep moving lower into harvest; the puts will protect you against lower prices.

If you have crop insurance, then only do this on 10% to 30% of your 2015 crop. Consider taking the gain or just stepping aside on the positions in late September.

2. Synthetic Puts. Sell some of the corn ahead in the cash market and buy some March 2016 corn calls. In the industry, this is called a synthetic put.

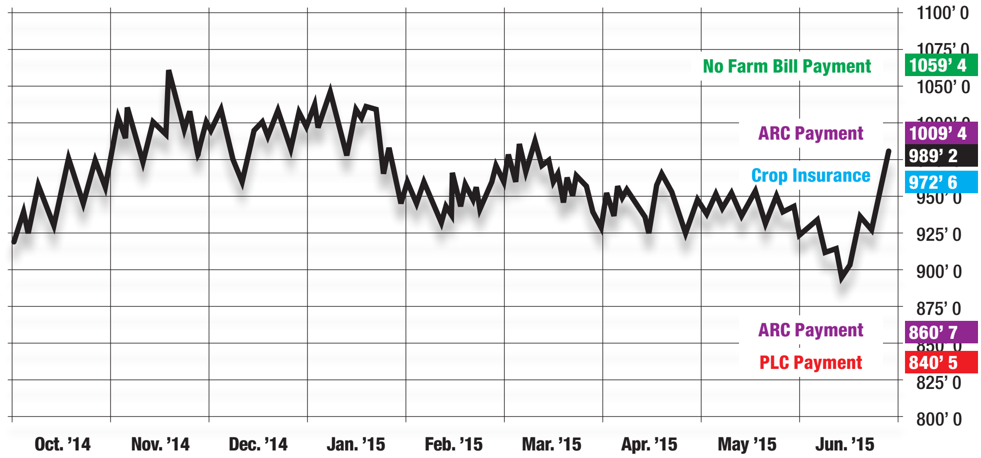
If the market moves lower into fall, then you can deliver the corn at the higher price. If the corn market eventually moves higher, you will be underwater on your contracts, but your calls will make money. Do this for 10% to 30% of your 2015 corn crop.

3. Spreads. At harvest, sell the cash corn and buy July 2016 corn calls or bull call spreads. This bull call strategy costs less than paying the shrink on corn and the other elevator costs you incur when you put your corn into commercial storage. Your total elevator costs (drying, shrink, plus storage) can easily add up to 25¢. Instead, use that 25¢ to buy calls or call spreads. It is a more complex strategy, but it is one that works.

WHAT ABOUT BEANS?

The frustrated Iowa farmer mentioned previously did not ask about soybeans.

November 2015 CBOT Soybeans



You can see the $10.56 high made in November 2014. From that high, prices fell to just below $9 per bushel by late May 2015. The chart shows support at $8.96 and then at $8.50. If soybean prices stay at this level or move lower, most soybean farmers will have a crop insurance claim and will likely receive large ARC-CO payments.

However, the same concepts should be applied to the soybean market If you have limited storage, then you want to haul all of your soybeans in and replace those sales with call options. Storing corn at home and hauling the soybeans to town at harvest are usually the right financial and marketing decisions.

KEY PRICE LEVELS TO WATCH

The December corn chart (shown on p. 24) shows the $4.15 crop insurance guarantee, the approximate levels where you will receive ARC-CO payments, and where PLC payments may begin. I am watching the double bottom in December corn at $3.64 and the harvest of 2014 low at $3.18 on my long-term monthly corn continuation chart as a possible low in the fall of 2015. If that low is taken out, then corn could drop down to long-term support at $2.90.

For November soybeans, the chart (above) shows the $9.73 crop insurance guarantee, the approximate levels where you will receive ARC-CO payments, and where PLC payments may begin. I am watching the life-of-contract low at $8.96 (at the time of this writing) and the April high at $9.78. If the November soybean contract closes below $8.96, then the next long-term support is at $8.50.

KEY TIME PERIODS TO MONITOR

Watch the last week of September for a possible major low. This is the anniversary of when prices bottomed in 2014. If that scenario does not work and if prices move lower through October, then the ideal time period for a major low moves to late December 2015.

Looking ahead to next year, begin putting your 2016 plan together now. In years with large crops, the new-crop pricing opportunity usually occurs early in the year. For your 2016 crop, you need to consider some hedges during the week of November 27, 2015, the week of January 22, 2016, and the week of March 18, 2016. The week of March 18, 2016, is also a key time to consider some new-crop puts.

If you learn to consistently get some of your crops priced ahead using this type of plan, the odds are very high that you will be better off than hoping for a summer rally or being forced to sell at harvest.

To avoid having the same marketing problems again next year, be more proactive by making your new-crop 2016 marketing plan early.

2 OPPORTUNITIES

Tere are two opportunities where lower prices could add to your bottom line.

Opportunity #1: The way the farm program and crop insurance works, the ideal situation would be to have prices crash during October and then rally back by the spring of 2016.

If nearby corn futures drop to $2.90 in October 2015 and rally back to $3.90 by July 2016, then you will make more money than if corn rallied to $4 this fall.

It pencils out because you could end up with a large crop insurance claim and you could also maximize your farm program payment. This is especially true if you have 20% to 40% of your crop forward-sold.

Opportunity #2: Take advantage of the large carrying charge that is developing in the corn market.

For those of you who have some hedges on and corn in storage, you should be able to roll your hedges ahead from December 2015 to July 2016 for 26¢ to 28¢. That carry plus basis improvement of 20¢ to 30¢ could make your farm an additional 48¢ to 60¢ per bushel.

That is a lot of additional income for your farm when prices are this low. SF

NOTE: Trading of futures and options has substantial financial risk of loss and is not for all investors.

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Al Kluis has been trading grain futures since 1974. Sign up for a free trial to his daily morning email and weekly "Al Kluis Report" by going to alkluis.com.

Join Kluis and his team for his free Second Tuesday webinar on Tuesday, August 11, at 8 p.m. CST. Register at alkluis.com.

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