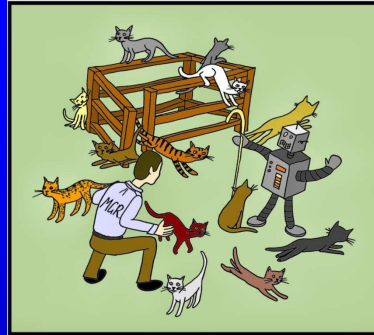




How to Capture a Market Carry



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What IS a Carry?

When something is worth
more later than it is worth
today



Why Are Carries Important?

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Elevators Make Money:

- Buy grain and hedge
- Sell at a higher basis
- Usually involves holding and shipping later.
 - But holding incurs costs
- Sell at a higher basis
- (Other: drying, storage, blending etc)

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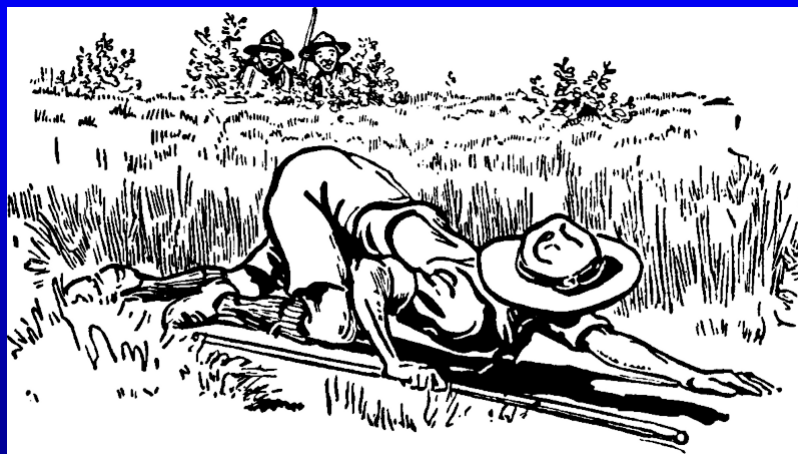
Carries and Returns

Can be elusive

5



You Need to be Alert



6



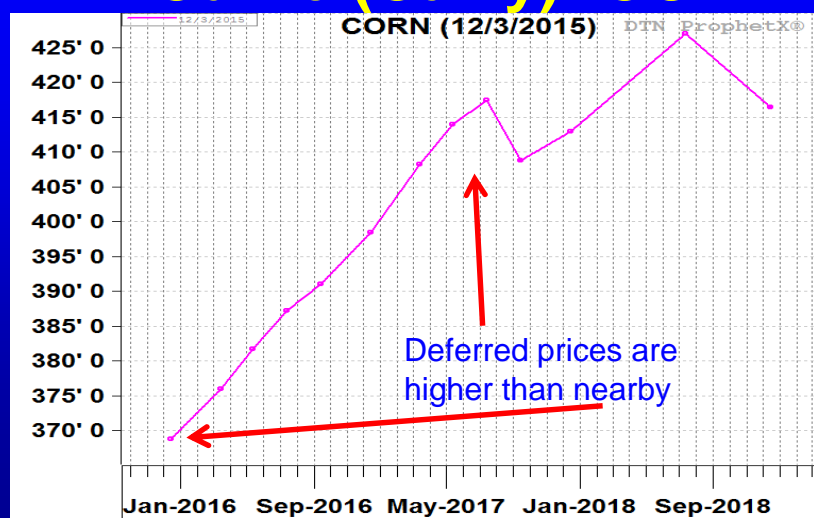
Capturing Carries:

- Means understanding where the carries are
 - Cash basis and/or
 - Futures spreads
- And knowing what to do

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Forward Futures Curve (Carry): CORN



8



Lots of Balls to Juggle



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Capturing a Carry

1. Buy nearby cash + Sell deferred cash (no hedging)
2. Buy nearby cash + Sell nearby futures;
3. Buy nearby cash + Sell deferred futures

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4. Move short hedges forward before you sell the cash basis
5. Sell the cash basis and move short hedges forward later
6. Pre-set a futures carry

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**The challenge is
identifying which
approach is best
– and when.**

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Buy cash / Sell Cash

W. Corn Belt ethanol					
	Dec		March		June
Basis	0		-0.11		-0.13
+ Futures	3.77	CH	3.83	CK	3.88 CN
= Cash	3.77		3.72		3.75
- Inter.	0.00		(0.06)		(0.12)
= Net Cash	3.77		3.66		3.63
= Net Carry	--		(0.11)		(0.14)

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Buy cash / Sell Cash

E Corn Belt River Mkt					
	Dec		March		June
Basis	0.09		0.15		0.08
+ Futures	3.77	CH	3.83	CK	3.88 CN
= Cash	3.86		3.98		3.96
- Inter.	0.00		(0.06)		(0.12)
= Net Cash	3.86		3.92		3.84
= Net Carry	--		0.06		(0.02)

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Strategy 4 ex.:
Buy cash
Hedge nearby futures
Set spread later
Sell basis later

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Ex. Basis ↑ + Wider Spread
= Bigger Net Carry

E Corn Belt River Mkt				
	Dec		March	June
Basis	0.09		0.18	0.08
+ Futures	3.77	CH	3.85	CK 3.88 CN
= Cash	3.86		4.03	3.96
- Inter.	0.00		(0.06)	(0.12)
= Net Cash	3.86		3.97	3.84
= Net Carry	--		0.11	(0.02)

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Maximize Both Parts

Futures Carry

+

Basis Carry

=

Cash Market Carry (-costs)

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- Stay alert for when buyers are ready to negotiate basis
- Understand what affects basis and futures spreads.

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Futures Spreads can be Volatile

and hard to manage for many merchandisers

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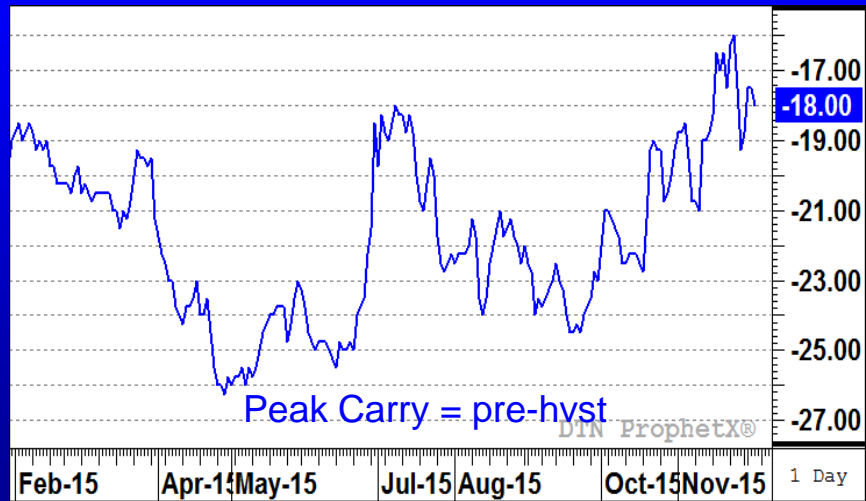
Best Spread Opportunities

Do NOT always come
at harvest
or when you buy the grain

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Dec15/July16 CORN



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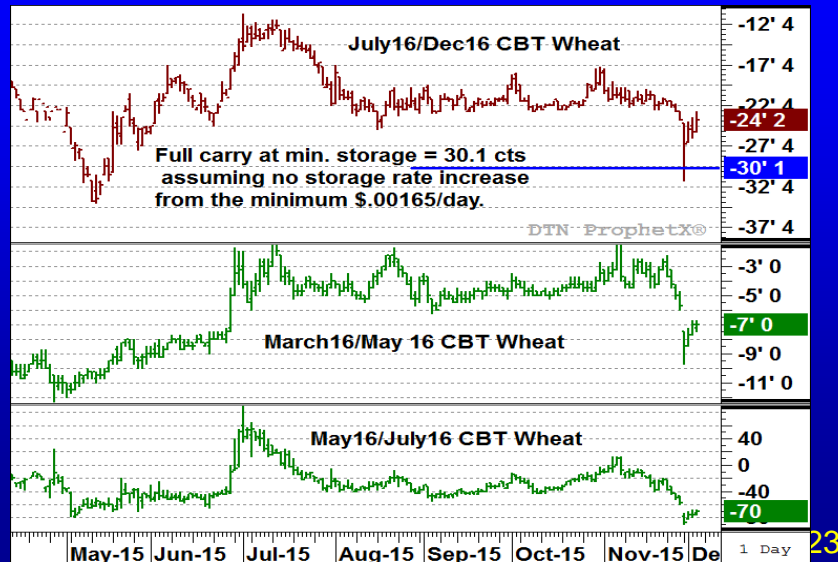
Jly 15/Dec15 SRW



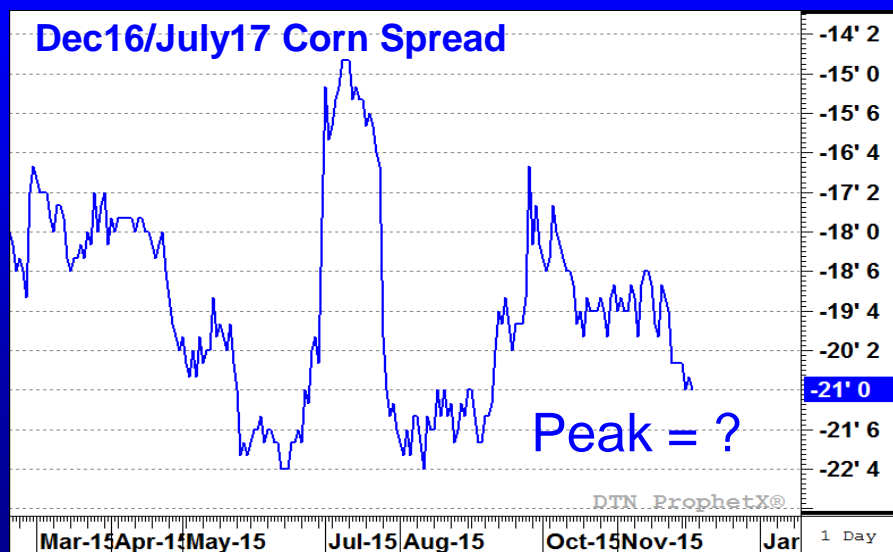
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Looking Ahead:



'16 Crop Corn:





How do you decide when to set a futures carry?

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Corralling the Cats

- Set futures carries when further potential gains are minimal (~80% of FFC ?)
 - First, learn how to calculate FFC
- Be willing to set spreads before you even buy or sell the basis
- Best opportunities may occur early

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Financial Full (Futures) Carry

- When the price difference between two futures months equals the full cost of carrying/holding
 - from Day 2 of the nearby month
 - to Day 1 of the deferred month.
- Costs include interest and storage.

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Financial Full Carry (FFC) in Futures

$$\begin{aligned} & \# \text{ days } \times \\ & ((\text{Interest rate} / 360) \times \text{Futures Price} \\ & + \text{Daily Storage Rate}) \end{aligned}$$

Int Rate: use 2% over 3-Mo. Libor
(not country elevator interest cost)

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Corn Full Carry

- Changes as price and inter. rates change.
- Currently about 5.9 ¢ / month
– March/May = 11.84 FFC
- Int. at 2.44% (2 > Libor)
- Storage at ~5¢/mo (\$0.00165/day)

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CBOT Dec15/March16 Wheat Full Carry

- 92 days (varies by cycle)
- X ((2.4162%/360
- X \$4.55 Dec Wht
- + \$.00165/day storage) = FC

$$92 * ((.00006717 * \$4.55) + \$0.00165) = 18¢$$

Calculated on 12/1)

30



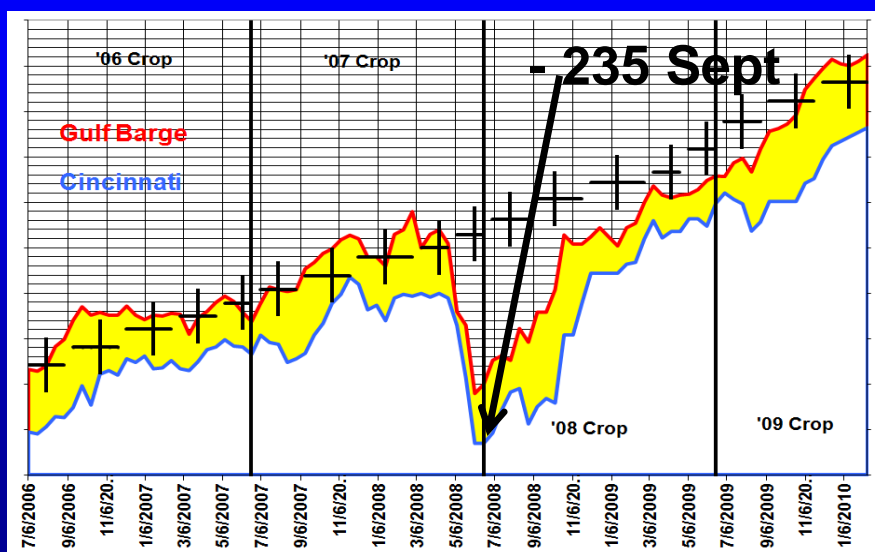
CBOT Wheat is Unique

“VSR”
Variable Storage Rate

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The Birth of VSR





2008 SRW

- Too much supply (record crop)
- Not enough demand
- Harvest basis fell to cheaper than -200 on the River
- Farmers called Congress!

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CBT's Solution? VSR

- Allows the max. storage charge a futures delivery elevator can charge on shipping certificates to fluctuate.
 - Min = \$.00165/bu/day (5 cts/mo)
 - Can rise by 3 cts/mo; No cap
- CBOT Implemented in July 2010

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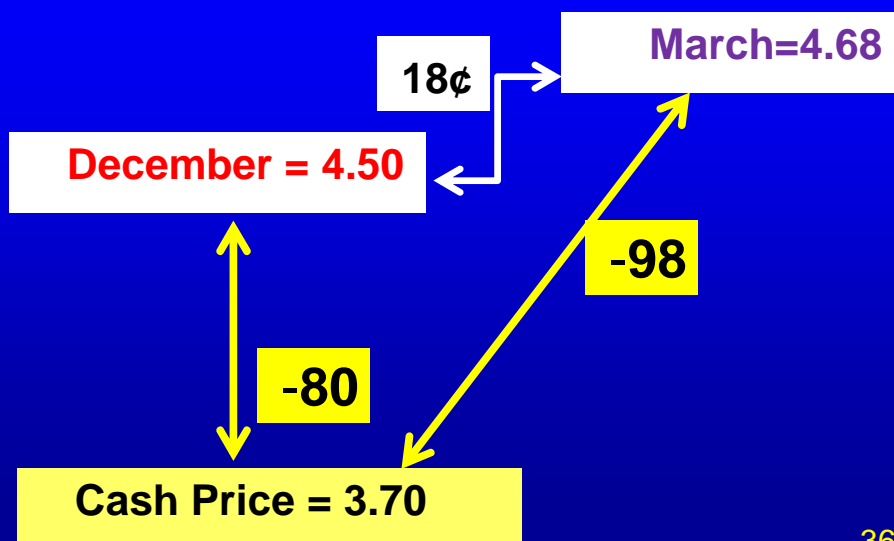
Principle Behind VSR

- Shifts part of the carry out of nearby discounted basis and into futures spreads.
- Higher storage rates means higher Futures Full Carry and potentially bigger futures carries.

35



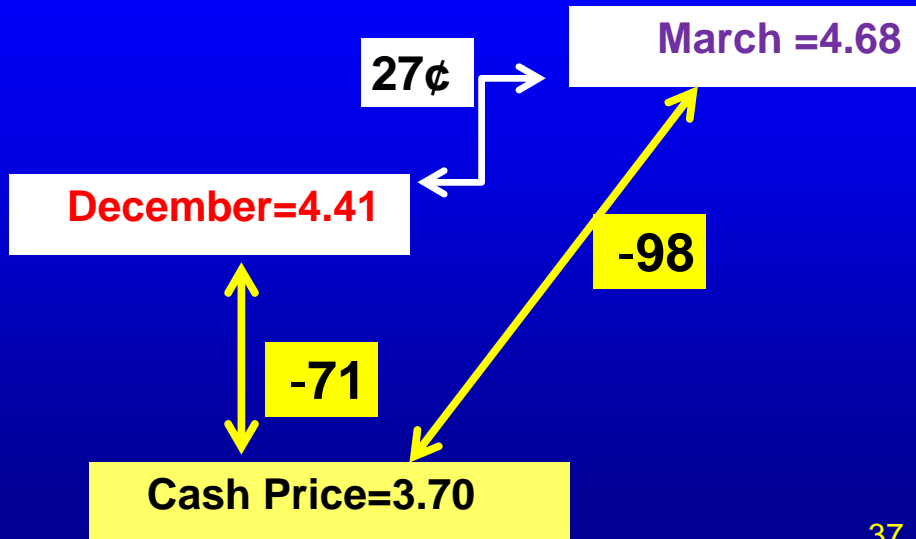
Ex.: Full Carry = 18¢



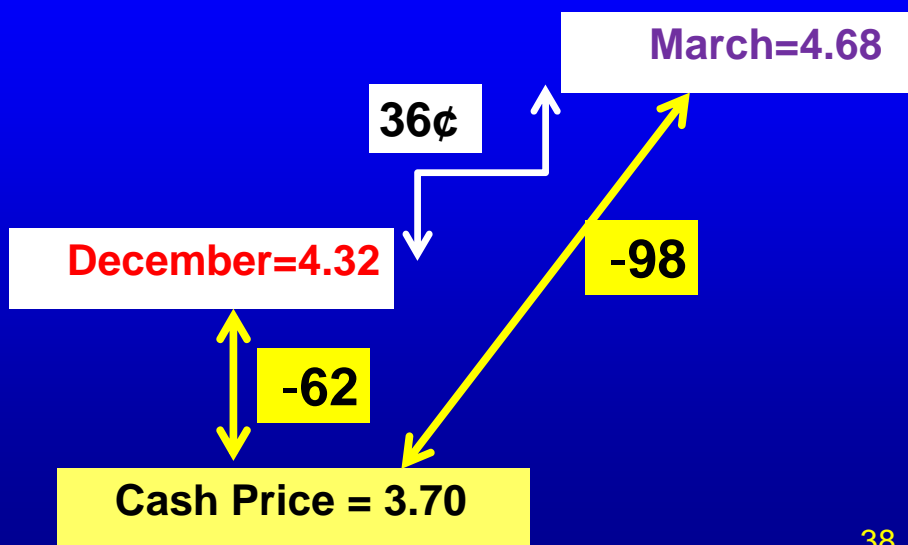
36



VSR Full Carry @27¢

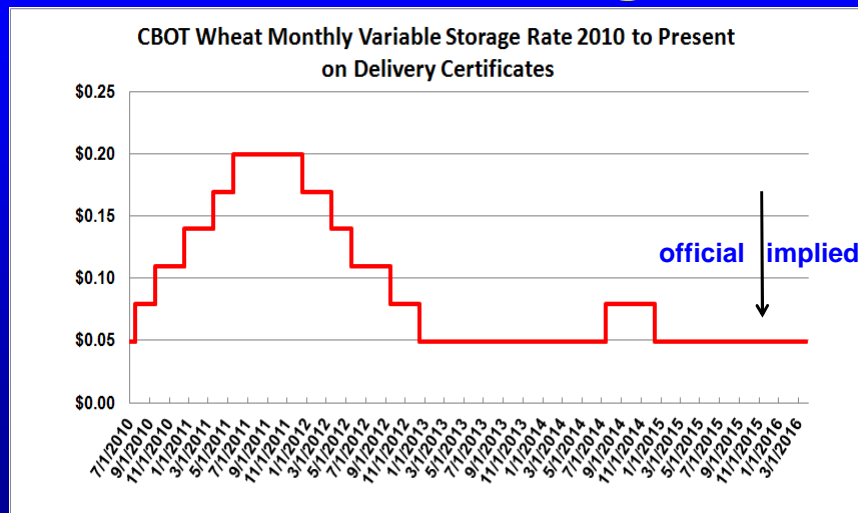


VSR Full Carry @ 36¢





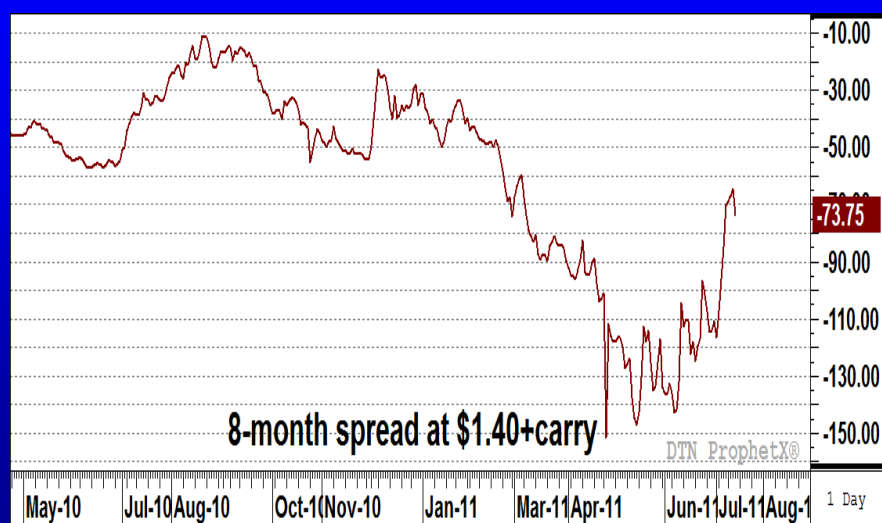
Variable Storage Rate



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SRW July 11 / March 12



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VSR Does Not Change the Cash Value of Wheat

It tends to bring nearby futures
closer to nearby cash
(Convergence)

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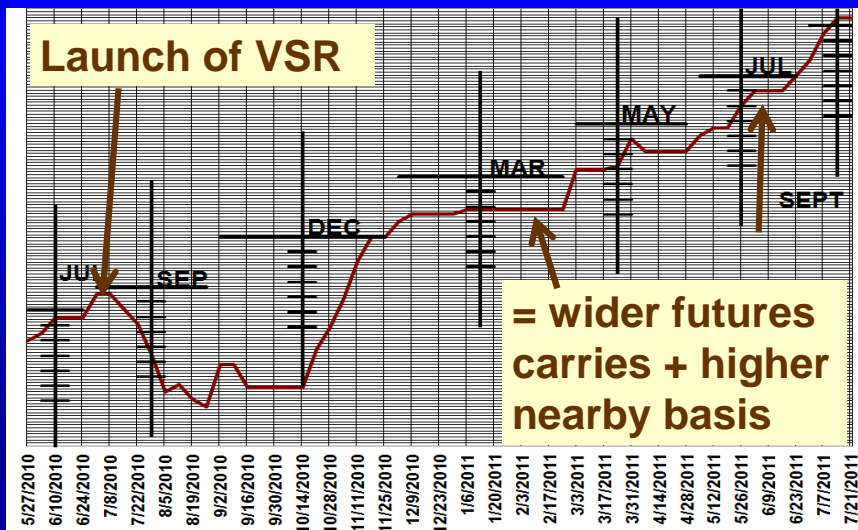


**And allows potentially
much wider futures
spreads**

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SRW: Cinncy '10 crop



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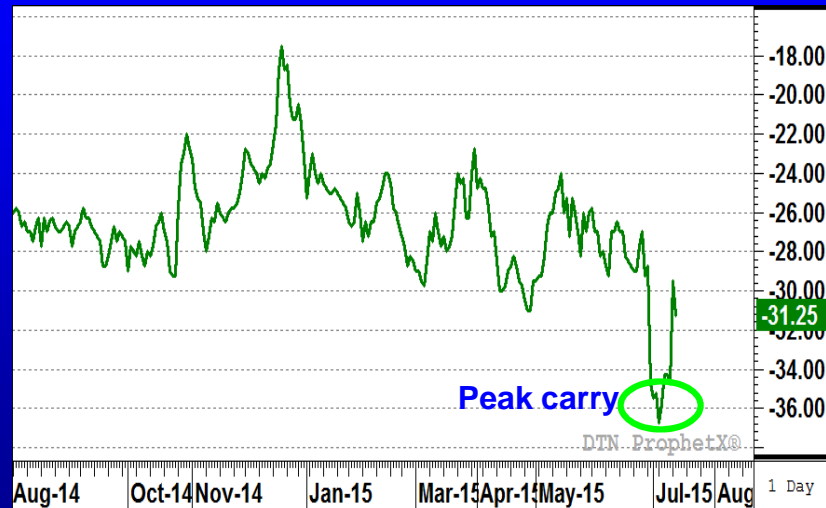
KCBT

- Their version of VSR:
- Seasonal storage rate:
 - July/Aug/Sept/Oct/Nov (JASON)
 - Rate set at \$.00296/day 9 cts/mo
- Other 7 months:
 - \$.00197/day (6 cts/month)

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KCBT July/Dec15



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Next step in learning how to maximize returns

- Learn economics of making/taking delivery of futures
 - Factors
 - Spread impact
 - Basis
- But not today...not enough time!

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Success!



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