Preston

BASIS ONLY

What is a Basis Only contract?

A basis only contract allows you to lock in a favorable basis level prior to, or upon, delivery. You then have the opportunity to take advantage of any gains provided by the futures market.

What is a "*basis*"?

Basis is the difference between the current cash price and the futures price. For example, if the March futures are trading at $3.60 and we are paying $3.40 cash, our basis is 20 *under* the March futures.

Advantages:

- **Ability to lock in a favorable basis level**
- **Avoid risk of the basis weakening**
- **Opportunity for unlimited gains within the futures market**
- **No Fees**

Disadvantages:

- **Unable to capture basis improvements**
- **Delivery—not flexible**
- **Subject to any decrease in the futures market**

How it works:

You are considering various contracting options; you know that you want to keep your options open in the futures market, but you are ready to haul corn now. You decide to enter into a basis only contract; which will allow you to set your basis now, deliver now *or* later, and take advantage of unlimited gains in the futures market.

It is currently January and the March futures price is $3.75. The basis is 20 under the March futures, making our cash price $3.55 January Delivery. With your contract, you will only be locking in the basis.

It is February 5th, and the March futures price for corn has increased to $3.85. Even though you have until the end of February to set the futures price, you decide to go ahead and apply the $3.85 to your contract.

Here's the math:

March Futures Price (in Feb.)	$3.85
March basis (in Jan.)	-$0.20
Price Received	$3.65

You will be paid $3.65 for your corn—a gain of $0.10/bu.

Scenario #1:

IN JANUARY		**IN FEBRUARY**	
March futures	$3.75	March futures	$3.65
March basis	-$0.20	March basis (previously set)	-$0.20
Cash Price	$3.55	Cash Price	$3.45
Set Basis ONLY		***Loss of $0.10/bu compared to January cash price.***	

Scenario #2, Carry Market: It is the end of February and you decide to roll the contract. The fee is $0.02 *plus* the spread (the difference between the March futures price and the May futures price).

Roll Fee	-$0.02
Spread ($3.65H-$3.75K) +	-$0.10
Total	-$0.12

Adjusted Basis = 20 - 12 = 32 under

Must price or roll by the end of April.

Can not roll into a new crop year

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