Buck a trend at your peril

With the monthly grain market moving by £10-14/t, it is utter madness not to have some insurance in place, says **Jeremy Cole.**

An unexpected sunburnt face from walking in Derbyshire during the first sunny weekend for ages made me reflect on what a difference a few days can make.

Let's take a few days earlier this summer. Grain prices rose considerably in June, with November 07 LIFFE futures soared from £103 to £116.50. The climb has continued due to fears about climate change, consumption and the food versus fuel debate.

Demand in the US for biofuels has seen quantities of corn used in ethanol production increase by 300% in five years. To reach its goal of 20% fuel from ethanol, corn usage will have to exceed production.

That in itself is obviously of great concern to US feed users. But it also means export homes will have no US corn to buy. They will be forced to make other arrangements. China will be using 5mt of corn for its plants, rather than the 2mt now.

More immediately, global futures prices are influenced by monthly supply, demand and stock reports around the world. The US recently reported that the soya acreage was down 3m acres, far below estimates. Unsurprisingly futures rose £10 in a day.

November 07 futures are £116.50, so ex farm is approx £113. This means that from today, no UK farmer should have grain going off the farm in November 07 at less than £108/t and Options are available to guarantee this.

Premiums to achieve this can cost as little as £5. With current market movements of £10-14/month, it is utter madness not to have some insurance in place, as markets can fall as well as rise.

If, as is believed, 30% of the 2007 harvest has already been sold, then 70% is at risk of a market fall. It is more important to protect that chunk than play catch-up on the grain that has been sold at £85-95. Put those sales behind you and move on.

For harvest 2007 crops there is a short term hedging/insurance need, from now until harvest, as at least 25% dare not be sold at any price, higher or lower. Once harvested quantities are known then a longer term strategy can be adopted. It may be different.

A non-selling farmer must hedge the downside risk, as it is the opposite of their physical position, whether they like it or not, unless they just don't care about consequences to their bottom line.

The only further thought needed is how much insurance to cover – in other words, what downside risk is acceptable? 100% unhedged grain loses £1 of every £1 the market falls. Covering 50% means the downside risk is halved.

This means the average premium, and so maximum cost of the insurance, is reduced to £2.50/t over the whole unsold tonnage. Over the total tonnage the cost is therefore even less.

Market signals look bullish for the future but volatility will remain and probably increase. Set a Standard of Living Line for your farm and sell before it is reached on a falling market. Ratchet it up as the market rises, bail out with an Option if it falls.

Getting the market wrong now could be very painful indeed, especially as we seem to be edging towards predictions of wheat worth £200/t by May 2009.

Jeremy Cole, Bsc Agri Econ (Reading), runs Agricole – an independent grain brokering and marketing service for farmers. For a weekly grain market report, call 01954 719452 or visit www.agricole.co.uk

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