

SOYBEAN PRODUCTION SYSTEMS

Forward Pricing Practices of Indiana Soybean Producers

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Many producers are concerned by the constant ups and downs in soybean prices. To reduce that anxiety, some have turned to securing a price for their crops prior to harvest. Previous research suggests that this practice, called forward pricing, can enhance producer returns (Wisner, Blue, and Baldwin; Hagedorn, Irwin, Good, and Colino).

But how common is forward pricing? Who is doing it? What benefits are they receiving?

To answer these questions, and to assess other forward marketing practices, Purdue Extension, in consultation with the Indiana Agricultural Statistics Service (IASS), sent surveys to a sample of Indiana soybean producers representing various farm sizes and regions around the state in 2005.

This publication focuses on the grain marketing differences found across farm sizes and regions based on survey results (other publications focus on other issues).

For this survey, farm sizes are grouped by total cropland:

- 0-99 acres
- 100-249 acres
- 250-499 acres
- 500-999 acres
- 1,000 acres or more

For this survey, there were three regions: north, central, and south.

Big Farms Favor Pricing Tools

Survey results showed that the larger the farm, the more likely producers were to forward price their crops (see Tables 1-3, page 2). And those who used more than one forward pricing tool were more likely to be large-scale producers.



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Table 1. Number of Forward Pricing Tools Used in 2004 by Farm Size

Farm Size (acres)	Number of Forward Pricing Tools Used			
	None	1	2	3
	Percent of Respondents			
1-99	89.9	10.1	0	0
100-249	82.7	16.9	0.4	0
250-499	71.5	26.1	1.9	0.5
500-999	60.4	34.2	3.6	1.8
1,000+	43.0	46.5	7.8	2.6
Overall	68.9	27.1	3.0	1.0

Table 2. Number of Forward Pricing Tools Used in 2005 by Farm Size

Farm Size (acres)	Number of Forward Pricing Tools Used			
	None	1	2	3 or more
	Percent of Respondents			
1-99	89.3	10.1	0	0.6
100-249	79.6	19.6	0.8	0
250-499	73.4	24.2	1.9	0.5
500-999	56.9	36.4	5.3	1.3
1,000+	41.3	47.8	8.7	2.2
Overall	67.3	28.1	3.6	0.9

Table 3. Percent of Producers Who Used Each Pricing Tool When Forward Pricing*

Pricing Tool	Year	
	2004	2005
	Percent Used	
Cash Forward Contract	89.2	88.1
Minimum Price Contract	3.5	5.3
Average Price Contract	7.8	8.9
Futures Hedge	8.1	8.0
Options Contract	4.7	5.0
Complex	2.6	1.9

* Columns do not add up to 100 percent because producers can report more than one pricing tool.

For example, the survey results show that in 2004, 10 percent of producers with less than 100 acres used forward pricing tools, while 57 percent of those with more than 1,000 acres used forward pricing tools.

There are several explanations for this difference.

First, most pricing tools require a minimum of 1,000 bushels and standard futures contracts require producers to price in units of 5,000 bushels. Obviously, such minimums are a steep requirement for smaller producers. For example, a 100-acre producer with a 50:50 corn-soybean rotation and an average soybean yield of 50 bushels per acre can only expect

to produce 2,500 bushels, well below the minimum for futures hedges.

Second, many pricing tools are very demanding of a producer's time and effort. The larger the operation, the more producers can spread this cost in time and effort over many units.

Third, and most importantly, larger producers tend to earn a larger share of their total household income from farming than smaller producers. With such stakes, managing price risk through forward pricing becomes more important to the larger producers.

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Cash Forward Contracts the Most Popular

The survey showed that producers are using a variety of pricing tools — and many are using more than one. The survey found that cash forward contracts are by far the most common pricing tool, with almost 90 percent of the producers who forward price using this tool. Cash forward contracts are offered by local elevators, which may indicate why producers favor these pricing tools.

Futures hedges and average price contracts were the next most popular with about 8 percent of producers using each one. Average price contracts, also called new generation contracts, were introduced about six years ago. That they are comparable with futures hedges shows they are growing in acceptance.

The other tools were options contracts (used by about 5 percent of producers who forward price), minimum price contracts (4-5 percent), and more complex pricing tools that involve more than one position on the same grain (2-3 percent).

Conclusions

The survey results show that producers' forward marketing practices vary depending on farm size. Overall, producers (and especially small-scale producers with farms of 500 acres or less) prefer not using forward pricing tools to market soybeans. Large-scale producers with more than 1,000 acres were the only group in which more than 50 percent reported using forward pricing tools. Furthermore, except for large-scale farmers, those who do forward price prefer using the pricing tools (such as forward contracts) that are offered by their local elevators rather than tools offered by the futures market.

The survey also showed that despite Purdue Extension's efforts to teach farmers about futures and options, only a tiny number of farmers use them. But this could be due to minimum contract sizes rather than a lack of producer understanding. In the future, Purdue Extension plans to hold meetings on grain marketing around Indiana. Contact your local Purdue Extension Educator for information on grain marketing education programs.

More information about forward pricing tools is available in Purdue Extension publication 6-59, the *Commodity Marketing Series CD*. The CD contains information on a range of pricing tools available both at local elevators and the futures market. To order, visit the Purdue Extension Education Store, <https://secure.agriculture.purdue.edu/store/item.asp?itemID=3864>

To read about other findings from this survey, and for more soybean information from Purdue Extension, visit www.coolbean.info.

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References

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