

Country Elevator Use of the Market

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It has been an interesting day and a half as we got a glimpse of the world's greatest grain market and heard some of the processes and techniques used.

The topic assigned to me is "Country Elevator Use of the Market."

What is a country elevator? The country elevator is the tallest building in town and the biggest business that handles more money and has more customers. This country elevator business is big business for there are some 16,000 to 18,000 of them in our nation and about 1,700 in Illinois alone.

This is where grain that is the farmers' raw material, most of the nation's new wealth, first enters the commercial channels to be processed and packaged and distributed to consumers both here and abroad. It is here that the raw material, of little value as harvested, is first weighed and graded and paid for. It is important business to everyone—our food supply.

All of the customers of a country elevator are farmers and the elevator does business with the same producers every year. The competition is terrific for if the grades are not accurate or the weights questionable or the price is not high the customer will drive across the street or to the next town. It is very important to a community that as much grain be delivered to its elevators as possible for this is where the money comes from, this new wealth that has been created.

The farmer himself has changed drastically these past 20 years—he has had to keep up with the financial requirements of efficient farming and with the scientific knowledge necessary to keep abreast of the changing opportunities. He must keep posted on the latest government programs and where to best market his products. The cost-price squeeze has eliminated the hicks and most of our farmers are college graduates, good businessmen and prosperous

leading citizens. No more peasants. Let us never forget how important the farmer is for he raises most of our food and he also pays many of our salaries.

Thirty years ago the average country elevator had a storage capacity of 26,000 bushels—now in our area the average capacity is 150,000 to 200,000 bushels. This 600% increase is the result of the government farm programs, the increased yields per acre and the new harvesting methods. The increase in storage capacity, along with different transportation facilities and rates, has changed the movement of grain from our area and also affects our use of the Chicago futures contracts.

Most of the grain the farmer delivers is sold by the country elevator in one of three methods: 1. to the merchandisers, 2. to the truckers, and 3. through the Chicago futures markets. The merchandisers collect the bids from processors, from the consuming areas of the south and southeast, from terminal and river loading points, and from exporters at the Atlantic and the Gulf. The truckers buy grain from the country elevator and haul it to processors or markets or to river points or to points on the Southern Railroad—often these are backhauls. Very little of the grain in our cash grain surplus producing area is marketed through livestock, and very little of our grain moves to Chicago and New England as it used to move. This new movement tends to be from points of origin at the country elevator to final destinations under the new incentive rates without stops at concentration points for storage and distribution. Now this third market is our topic today—what does the Chicago futures market mean to the country elevator operator?

The most important fact about this market for the country elevator is that it is the greatest auction in the world, where the raw materials that the country elevator handles are auctioned every day with buyers and sellers from all over the world. A place where the grain is priced exactly for a particular location for a specific delivery and for a designated quality. The country elevator knows when the market goes up and when it goes down for the prices are broadcast constantly. The country elevator knows the exact price of the grain and so does the processor and the exporter and the banker and the farmer—everyone knows exactly what grain is worth.

Now the next most important fact is that the country elevator can buy all the grain he wants at this auction and he can sell all the grain he wants, for any delivery, and so can the processor buy grain against the sale of his products and the exporter can buy at the market to fill an export sale. In other words, the country elevator can get someone else to take the risks of the market action without paying a premium—just the market price, because he can either buy or sell at the market price.

Few people have stopped to realize how valuable it is to know exactly what a product is worth at all times or are aware of how valuable it is to be able to transfer the risks involved to someone else. Few know or understand how these privileges reduce the margins necessary in the handling of a product. By being able to buy what you have sold or by being able to sell what you have bought at the market eliminates much of the risk involved—almost perfect insurance.

Think for a moment how valuable it would be if we had more of these free open auctions that we could all use.

Recently I wanted to build a house, but I owned one and the best real estate man in town took 14 months to sell my house and I still don't know if I sold the house too low or too high. The real estate man charged me the usual 5% commission which really was a service charge because he had no risk involved in the transaction. And then I had to buy an auto and I got \$300 discount because I didn't have a car to trade in and I paid cash. I had removed much of the risk from the dealer but he probably still had 15 or 20% margin in the transaction. And then I had to buy some furniture and drapes and rugs and I felt certain the dealers earned their 40% or 50% margins because they had on hand what my wife wanted. What a customer is going to want and how many—these are serious risk decisions. If you have too many bathing suits during a cool summer or too many sleds the year it doesn't snow you will have to sell at a loss. It seems apparent that the margins in most of the articles we buy are in direct proportion to the risks involved.

It cost \$1,750 commission to sell my house and it took 14 months and yet I can sell \$37,500 worth of soybeans instantly on the Chicago futures market for any delivery for only \$72 or 1/2 of 1% commission and I would know that I had sold at the going market price. For this \$72 someone else took the risk out of my purchase of soybeans from the farmers. Therefore I don't have to charge the farmer for the risk of market changes in handling his product for I can get someone else to take that risk for less than 1/2¢ per bushel—did you ever hear of such cheap insurance? In this, I'm talking of commissions I must pay and not of the "margin" or performance bond I must post to guarantee my contract. Think how many houses we would move into or autos we would try if we knew exactly what they were worth and could get another when we wanted at such minimum expense.

If the country elevator had to assume the risks of market fluctuations and did not know exactly what the grain was worth at all times the mark-up necessary to handle the farmers' raw materials would be more like the 20 to 30% required by other merchandisers of products. The mark-up would be prohibitive as it has proven to be in a number of countries where no futures market was available. Because of this knowledge of the exact value of the grain and the ability to transfer the risk to someone else for 1/4 of 1% there is a smaller margin charged against the marketing of the farmers' raw materials than any other commodity—in other words, a greater proportion of the selling price of the grain farmer's products is returned to him than to any other producer. The farmer can also use this market and reduce his risks by selling part of his crop before harvest or during harvest or after harvest—whenever he wishes because he knows the value of his grain for the various deliveries.

Now let's take a quick look at a typical Chicago futures contract to see why we use it at times as our third outlet in preference to selling to the merchandisers or the truckers. Why is this third outlet for the farmers' grain so valuable to the country elevator? I have used corn as an example but the same process applies to wheat or soybeans or oats or any commodity that has a futures market.

Last July 28th, nearly 2 months ago, we had one of our big farmers who wanted to sell 25,000 bushels of his new crop of corn for harvest delivery.

Harvest delivery means October, November, or December delivery and this farmer wanted to be sure he had some place to deliver corn at harvesttime for his crops looked big on that date. We got the bids from the merchandisers and found that all the high bids specified a particular delivery—like the first or last half of a chosen month. We didn't want to sell grain for the long haul to the ports unless we knew the grain would be dry and of good quality. Even the truckers wanted to know what the quality of the grain would be and when they could pick it up. We didn't know what the quality of the grain would be nor did we know when the grain would be delivered—no one knew. Here comes the risk factor again. And gentlemen, when I have to buy grain and don't know when it will be delivered or what the quality will be I think of a remark an old friend uses under these conditions. He would say "Eb, I am not after any cheese, I am just trying to get my head out of this trap." I just want to get rid of the risk of market fluctuations and the risk of when the grain would be delivered and what the quality would be. After looking over all the bids we decided the best way to protect against these risks was to sell 25,000 bushels of corn for delivery in Chicago during December here in this market. Here are some of the reasons the sale of December corn was the most attractive contract.

When harvest is going on, in another month or so, the grain will be delivered, either wet or dry, and I can grade it. Then I can offer that particular quality of grain for sale to the market that will pay the highest price and take the minimum discounts for the particular quality. If bids I get are higher than the corn would net me if I delivered it on the contract I already have in Chicago for December delivery—as it probably will be because of our location—I have a privilege that I have on no other contract. If the bid is higher I will sell the corn to the most advantageous market and immediately buy in the 25,000 bushels of December corn I sold last July. I have been protected all this time from the market fluctuation and have been able to grade the grain and ship to the market bidding the top price for that particular quality of corn, thereby permitting me to give my farmer the top price in July and to give him the minimum discounts at harvesttime. There is no other way this could be accomplished and this is not a theoretical situation.

Another invaluable possibility may develop at harvesttime if we use the Chicago futures contracts for our cash corn. Let's assume that in another month or so with harvest in full swing that the corn is of good quality and dry and that there is congestion in the markets. Congestion normally makes the bids for immediate shipment at a discount under the bids for deferred or later shipment. When this is true the nearby futures, like our December contracts, will be selling below the far off or deferred months like the March or the May contracts. When the premium gets high enough so we can afford to carry the grain in our elevator to the more deferred month, we can buy in the contract we sold for December delivery in Chicago and immediately sell the same 25,000 bushels of corn for March or May delivery—whichever we choose. And because this is a great auction we can change the shipment without paying any penalty for the privilege (by just paying a commission) and thereby earn a rent on our storage room, what we call carrying charges.

You can see that by keeping the grain in our elevator for future shipment we are keeping the grain off of the market during the congestion and supplying the grain at a later date when it is needed, distributing our food throughout the

year. This ability to earn rent on our storage room is the most valuable asset of the futures market for the country elevator, for the change in the government storage policies has taken away the earning capacity of most of these large elevators and if they don't learn to use the futures market they will suffer some serious losses.

Now the greatest value of these Chicago futures contracts to everyone is that by the ability to eliminate the risks of carrying grain, anyone can get proper financing so that the nation's yearly food supply at harvesttime is carried and distributed throughout the year as we need it. No country elevator or processor or exporter has enough money to carry their elevators full of grain without borrowing large amounts from the bankers. When you talk to a banker about a collateral commodity loan he asks just two questions: 1. What kind of a warehouse receipt you will give that will transfer the title of the grain to the bank? And 2. Is the grain sold? If the answer to these two questions is satisfactory the banker has the best possible loan and he will give you a large percentage of the value of the grain at the best possible interest rates. If you don't have a satisfactory warehouse receipt or if your grain is not sold, the loan will be drastically reduced and the interest rate will probably be higher—the old risk factor again. This is the way the processor and the exporter and the warehouseman finance their storage operations. This is the way industry gets away from the risks of market fluctuation and thereby reduces the margins in all branches of the industry and this risk saving margin is passed back to the country elevator and by them on to the farmer. And it makes it possible for me to have an adequate supply of cash so I can make immediate payments to the farmer.

So you can see that this Chicago futures cash contract sold by the country elevator offers many opportunities and many choices in the handling of the farmers' products to everyone's benefit. It is natural for the country elevator to chose a contract with such flexibility whenever possible, rather than a rigid contract. Many would prefer a choice. Any country elevator that does not use these Chicago contracts when they are the high bid is not doing the maximum job of merchandising the farmer's grain and doesn't give him the best choices.

And now for the tragic part of the story. A very small minority of the country elevators use this third method of marketing their grain through the Chicago futures cash contracts. The reason they don't use this market is that they are not allowed to use the market because it is written in their bylaws that they cannot use the futures market. The directors of the companies will not let them use this market nor will bankers in these towns finance them if they use the futures market. The reasons for these restrictions are primarily based upon the lack of understanding of what this market is and why it is a great asset to the marketing of the farmers' grain. Most of the people in our country, including bankers and landowners and manufacturers and lawyers and farmers themselves, think of this market, not as an actual cash grain contract, but rather as some artificial or fictitious contract that only people who know all the answers trade in among themselves. They think this is a controlled market and not a free open world auction.

Most of the feeling towards the Chicago Board of Trade is one of antagonism that has been built up since the old bucket shop days and by the speculator stories about gambling and swindles that happen occasionally everywhere.

No—this is not a fictitious market, it is an actual auction of cash grain and it is not a controlled market. You have seen how our own government has spent billions of dollars each year trying to control the prices of grain and trying to reduce our production without success, for the prices are not satisfactory and we keep producing more and more record crops each year. And you have read about Russia spending billions trying to increase their production with disastrous results and smaller and smaller crops each year. These markets are not controlled by men or governments but only the natural events like drought or flood or war or peace. In fact it is controlled by only one thing—the actual demand and supply of man's food, too little or too much is reflected in the values of cents per bushel on the Chicago Board of Trade auction and anyone can sell or buy. It is because of these misunderstandings and these antagonisms and because they are so prevalent in the country that the country elevators cannot make use of this most valuable marketing tool.

It would seem that only the Chicago Board of Trade and some of the universities are doing a constructive job of trying to inform the people about the facts of this market. I would sincerely hope this education work will continue, and will expand with help such as you can give.

I have read more newsprint about Billie Sol Estes and Tony DeAngelis than I ever read about the advantages of this type of marketing. You have a great opportunity to educate the people about the proper uses of this great market and also about how to keep from speculating on our food products.

I hope we can maintain a system that permits a minimum of risk so we can continue to handle the farmers products at the lowest margins possible. I hope that in spite of interferences we will continue to have the most efficient agricultural producers in the world. And may you never forget that a free open agriculture with free open marketing facilities is the key to our prosperous agriculture.