Section 3

Terminal Elevator Use of Futures

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Terminal Elevator Operations

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In the time allotted to me, I am going to try to tell you something about the operations of a terminal elevator business. I first want to give you a general idea of the location of the facilities of my firm, the Norris Grain Company, which extend throughout the entire middle western grain belt with a total capacity of approximately 29,000,000 bushels located as follows:

Location	Elevators	Bushels
Chicago	5	7,400,000
Duluth	4	3,700,000
Kansas City	3	6,800,000
St. Louis	2	2,400,000
Toledo	2	2,500,000
Peoria, IL	1	1,000,000
Burlington, IA	1	1,200,000
Sheldon, IL	1	940,000
Baltimore, MD	1	250,000
(Sub-total)		25,790,000
Inland Waterway Operated by Chicago	7	695,000
County Elevators Operated by Chicago	2	290,000
County Elevators Operated by Kansas City	58	2,500,000
Total		29,270,000

All of the above terminal elevators respresenting 25,000,000 bushels are operated as separate entities with the exception of Burlington which is under the Peoria management and Sheldon is handled through Chicago. There is, however, close cooperation between all of the units with respect to important information and the diversion of business from one office to another when that office cannot handle the business. The foregoing gives you an idea of a terminal elevator set-up with facilities for handling and processing grain.

Necessity for Terminal Elevators

Why is the terminal elevator necessary? Because all crops are harvested at maturity and a large percentage of each crop must be moved at harvest. If there were a demand at harvest for each crop so that the buyers' demands would equal in bushels the amount available for sale, we would have, as former President Hoover stated, "Perfection," but that does not exist. Consequently, someone must take the surplus at harvest, and carry it until such time as there is a consumer demand. This function falls on the terminal elevator who, under our present marketing machinery, buys the grain and hedges it. Since the imposition of support prices by the government resulting in large quantities of grain being taken over by the Commodity Credit Corporation, an agency of the government, the terminal elevators have contracted to carry large quantities of this grain at a rate of storage less than the published tariff available to the public. In addition to storing large quantities for the government, terminal elevators have carried on their merchandising operations and have had supplies available for corn processors, feed manufacturers, and millers with the exception of the declining days of the Office of Price Administration when the "Black Market" was a popular source of supply. I hope we never see a situation like that again.

Warehousing of Grain in Terminal Elevators

The terminal elevator in addition to its merchandising operations, the warehousing of grain for the government under contract, will contract to carry grain for a producer, country elevator, miller, or processor if room is available; also makes deliveries on future contracts if the elevator is located in a futures market. In Chicago all elevators approved for delivery on future contracts are federal licensed warehouses, while in Minneapolis and Kansas City they are licensed by the state in which they are located. A tariff must be filed with their respective exchanges and agency under whom they are licensed and a bond must be posted to guarantee performance according to the regulations under which they are licensed. A warehouseman licensed under the Federal Warehouse Act, or under the warehouse laws of a state having satisfactory regulations over the operations of their warehouses, can borrow eighty to ninety percent of the value of the grain on which the receipt is issued and so can the individual, corporation, or partnership. A prominent Chicago banker, not many years ago, said he would just as soon make a loan on a warehouse receipt issued by an operator of a licensed warehouse in Chicago as he would a government bond.

Merchandising Operations of Terminal Elevators

A great many people believe the merchandising of grain is entirely different than other types of merchandising. This is not the case. You must know how to originate it and where to sell it. The first place to look for grain is the country elevator who buys it from the producer; many merchandisers obtain their supplies from that source, and others get their grains from commission men, who have offices at strategic country points, and through those offices keep the country elevators posted with bids and other important market news. In recent years trucking operations have increased to the extent that elevators with truck unloading facilities buy a substantial quantity through that source. The construction of facilities on waterways has, during the last fifteen years, increased the movement by water to Chicago and south to St. Louis and New Orleans. The cheaper water transportation rates, as compared to rail costs, have brought millions of bushels of grain, particularly corn, to the river outlets and then to Chicago, St. Louis, or New Orleans, and, in lesser quantities to consuming points on the Ohio River.

All grain originating through the various sources previously referred to, is bought on the basis of the current or nearby future. As an example, #2 Yellow corn is deliverable on futures contracts at ½¢ premium. An elevator that can buy #2 Yellow corn at ½ over September, can put it in store for delivery, and when it is loaded out, receive 1½¢ per bushel. Of course, if there is a demand for corn from processors or feed manufacturers at a price relative to the future, that is, higher than can be realized by making delivery, the elevator operator is in close touch with the trade in an attempt to merchandise his corn or other grain at a reasonable profit over and above the cost. For instance, at the present time in view of the small amount of space in this market and the lack of demand for #2 Yellow corn, the value today is 1½¢ under September for #2 Yellow corn delivered Chicago by barges. This means an elevator qualified for delivery on futures contracts, may deliver the corn on September at ½¢ premium and when the corn is loaded out, receive an additional 1½¢. This operation results in a gross profit of 3½¢ a bushel.

In view of the lack of room and a new corn and soybean movement just around the corner, many elevators want to save this room for the new crops and, consequently, are selling corn at less than they can get for it on delivery. This is based on a belief that the new corn and soybeans are going to be bought at a much wider discount under the futures.

At the time grain is delivered on future contracts in Chicago, the elevator operator receives with it a warehouse receipt in an equal amount and that warehouse receipt as previously mentioned, may be used and is used, for collateral.

The keeping condition of grain being carried in store for the public is guaranteed by the elevator operator under the rules of the Chicago Board of Trade. If at any time, a public elevator operator finds that any part of the corn or the grain which he has in store, is not keeping properly and is beginning to deteriorate, the rules provide a necessary procedure whereby the owner of the elevator and the holder of the warehouse receipt get together and dispose of the grain.

Terminal Elevator Hedging

In time of short supply, the elevator man has a problem of deciding where to place his hedges. Sometimes when grain is selling at a premium over the nearby delivery, he may not feel justified in placing his hedge there. Consequently, he has to take into consideration the many factors affecting the market, such as the supply, the demand, the condition of the crops, and in recent years, since the inception of the government loan program resulting in the acquisition of large quantities of grain by the Commodity Credit Corporation, the futures markets have not reflected their normal relationship considering the tremendous crops we have raised. This has caused many headaches for the operator in deciding where to place his hedges. This year, however, as it became evident that there would be a substantial quantity of wheat for sale, largely due to lack of room at country points, terminal elevators, when the crop started to move, were able to buy #2 Red or #2 Hard wheat deliverable on contract at September price at from 4¢ to 6¢ under the September delivery. The lack of demand especially for #2 Red winter wheat resulted in deliveries on September contracts totaling almost two million bushels. That had the effect of widening the difference between September and December wheat from 3¢ to 6¢ a bushel. This gave millers and warehousemen an opportunity to change hedges from September to December at an attractive basis, especially those who waited and changed their hedges at from 5¢ to 6¢ per bushel. Incidentally, the reason for the lack of interest in #2 Red wheat is due to the large crop east of here that will not be wanted until early next spring.

The speculator, some of whom have taken delivery of this wheat by buying September and selling December at 5½¢ to 6¢ difference, sees an opportunity to make a small profit. He figures the wheat costs him September price and the storage and interest from the present time to the first of December when that wheat can be redelivered costs approximately 5¼¢ a bushel in the low rate insurance houses. In the meantime, before December 1st arrives, there may be an improvement in the demand for Red wheat, resulting in disposing of the cash wheat at a basis that will show him a larger profit. The present difference between the September and December wheat, affords an opportunity for milling interests also to take delivery of wheat that they do not want or have no room for at the present time, but will be available later if they need it. In the event they do not need it between now and December 1st, they can redeliver it without cost. The merchandising of grain into consuming areas in the East and for export, requires close contact with brokers who handle domestic and export grain, as well as direct contact with processors and manufacturers in areas where there are not any brokers.

Grain is offered for various shipments to the trade at a premium or discount relative to the future. Terminal operators in futures markets, if room is not available to make delivery, frequently sell grain for shipment at less than they can get by making delivery. There are also merchandisers at interior points not in position to make delivery who at times offer grain at a discount under the futures. As a matter of fact, at the present time #2 Yellow corn is being offered for shipment out of Ohio at a delivered price, which equals 1¢ per bushel under September, f.o.b. Chicago. A great deal of grain is sold basis the futures in exchange. However, recently, large users of grain in the East have bought their requirements basis the future and established the price the day the grain is loaded. This is an advantage which our futures market and buyers cannot enjoy, for no one would sell any quantity of grain at a flat price and handle it for the narrow margin as the grain trade. Incidentally, the margin of profit in those commodities without facilities for hedging is much wider than those commodities which have futures markets.

Former President Hoover testified before the Agriculture Committee in 1925, referring to hedging and stated as follows: "In my own belief, hedging would be worth discussion as applicable to that grain not now traded in, because the margin between the farmer and the consumer is certainly less in those grains that have a free hedging market, than it is in those commodities that do not have an opportunity for such action in distribution."

Need for Liquid Futures Market in Grain Merchandising

While the terminal elevator handles a very large part of our crops each year, there are also smaller merchandisers at interior points properly licensed under the Federal Warehouse Act and with satisfactory weights and grades, the latter having expanded materially in recent years under the supervision of the United States Department of Agriculture.

In closing, I should like to deviate from the operations of a terminal elevator and impress upon you how important I think the futues market is with respect to our cash grain business. To me, the cash and futures markets are almost Siamese twins—permanently damage the futures market, and the cash market will die. Should this occur, I see nothing else in distant view, but a government monopoly, possibly a distribution scheme under political auspices—a scheme of paternalism that I believe would eventually operate to the disadvantage of the farmers, producers, consumers, and the general public. The first punative impact would be financial—taxes or otherwise. The next stage would be regimentation and the destruction of the freedoms which are inherent in the American way of life.

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