

*The Use  
Made of  
Commodity Markets  
by Terminal  
Elevators*

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I would be unthoughtful and ungrateful if I did not first express my appreciation to the Chicago Board of Trade for its invitation to appear before this group of distinguished educators through the medium of the Seventh Annual Symposium. It is only through knowledge gained by meetings such as this, and distributed by our educational institutions that our industry will be better understood.

There is no question but that the Chicago Board of Trade as well as the general grain trade has been abused severely and unjustly many times in the past. This criticism came largely from those who were uninformed or ill-informed. In some instances it was actuated purely by selfish motives and in other cases by political expediency. I have not been 100 per-cent in agreement with the Chicago Board of Trade in all of its regulations. I know that all institutions as well as individuals have their faults. During the 1930s when the government was trying to enhance prices, if I recall correctly, the Chicago Board of Trade was condemned for allowing the Russians to sell rye futures—likewise and reversely during the last war the same institution was criticized for allowing the Chinese to buy bean futures. This was during a period when the government was attempting to curtail inflationary tendencies.

In 1948, the Chicago Board of Trade celebrated its 100th birthday. I feel that any economic institution that not only can survive but actually expand during one century in this country, must have given a definite and constructive service to society. There will always be a grain industry in the United States and to say that grain markets can be eliminated is taking a most myopic view of the general commodity marketing picture. The present method of grain marketing has been the outgrowth of an economic system which had its inception when the Pilgrims landed at Plymouth Rock in 1620. It has been able to adjust itself to an expanding and variable economy over the generations, which in itself, attests to the fact that it has met a definite need. As

far as I am concerned I am willing to use, as well as help improve, what we have until a better marketing system is found.

I am the General Manager of the Indiana Grain Cooperative, Grain Marketing Division of the Indiana Farm Bureau Cooperative Association. Our organization is owned by some 200 Country Cooperative Elevators in Indiana, along with membership of and in regional cooperatives in practically all of the surplus grain producing states. There is practically no difference in the mechanical operation of our marketing system than that of the private grain trade. We buy grain from our membership at the market price and sell it to the best advantage just like any private operator. Under the cooperative law, however, we must return to the patrons any net profit we may have made.

We offer various types of marketing to our membership. Among these are: purchases to arrive, consignments, storage for later sale, and also, to the extent that storage space is available, service shipments under the government loan program. We have had tremendous demands made upon us the last two years to provide storage under the latter category. This applies largely to wheat and is occasioned by the fact that the market at harvesttime has been very substantially below government loan values. The supply of commercial storage space in Chicago and the territory east of Chicago to the Atlantic seaboard has not been equal to the demand, and, as a result, soft red wheat producers have not been able generally to avail themselves of a greater income through the medium of the government support program.

Under all the government loan programs, it is the farmer's responsibility to place his collateral in a "loanable" position. This may be either on the farm or in some approved commercial warehouse. We are in a strictly soft red wheat area and regardless of what some people think, soft wheat is a perishable commodity, much more so than the hard wheat types. Deterioration in quality usually comes in the form of what is known in the parlance of the grain trade, as "sick wheat." It is a disease which attacks the germ of the wheat. Under the present grain standards, the kernels so affected are considered damaged ones and the numerical grade is lowered accordingly. Millers also tell us that "sick wheat" affects the quality of the flour, creating a rancidity which is objectionable to the housewife, the baker, and to your palates. Obviously, "sick wheat" has no demand from the millers and in order to find a market, it must compete with feed grains. Consequently, any soft red wheat that becomes out of condition sells at tremendously heavy discounts.

Our producers have had this experience many times and, as a result, are reluctant to store on the farm if commercial storage is available. This has created an unusually heavy demand for commercial storage the past two years because of the fact that, at the beginning of wheat harvest, the market price has been from fifty to sixty cents under the loan. In spite of the storability hazards of red wheat, there has been a tremendous increase in the amount of farm storage constructed the past year. There were about 8,000,000 bushels of wheat of the 1953 crop put under the loan program in Indiana. The latest figure indicated by State Agricultural Stabilization and Conservation Committee officials on the 1954 crop was 13,000,000 bushels. It is evident, therefore, that the Indiana farmer is assuming his own responsibility in placing his wheat in a loanable position. Regardless of this new trend, I still feel he would prefer to use commercial storage if it were available. Dry

harvesting conditions have been conducive to the greater use of farm storage the past two years. Wheat placed in storage with a moisture content of 12½ percent or less can be carried with reasonable safety if insecticides are used periodically and effectively; at least that was the experience of the farmers in Indiana on the 1953 crop. After many years in the grain business, I have arrived at the conclusion that there is only one way to carry soft red wheat, and that is to apply heat. We dry all of our wheat if it does not come in from the country at 12½ percent moisture or less. This is a particularly expensive operation since the maximum moisture of No. 2 wheat is 14 percent and all of our sales to millers are on this basis with no premium for less moisture. It is not as expensive, however, as waking up some morning and finding we have an elevator full of "sick wheat."

Indiana and states east of us have always prided themselves on the quality of their soft wheat, and have jealously guarded that position. Much time, money, and effort have been spent by the Millers National Federation, the Crop Improvement Association, and the grain trade generally to develop true soft wheat varieties. Soil and climatic conditions are ideal for its production. There have been several attempts in the past to introduce hard wheat in our area, all of which have met with but little success. It seems as if hard wheat does not so remain very long. After a generation or so, it becomes mixed or hard, depending upon the season, but usually mixed. Even if it tests hard according to grain grading standards, it does not command a premium over soft because it still does not meet the quality specifications of millers. We cannot compete with southwestern hard wheat any more than southwestern soft wheat can compete with our soft wheat. Under delivery rules of the Chicago Board of Trade, soft wheat and hard wheat have an equal value—this is how it should be.

We were much disappointed and disturbed when the government announced a 4¢ per bushel discount on soft wheat as compared to hard wheat, under its 1954 wheat loans for the territory east of the Rockies, and farmers were very articulate in their disapproval. On a national basis, perhaps there was some justification for it but it could not be justified on a soft wheat area basis. It had the effect of putting a premium on a product that could not be produced successfully in our area and it undid the good which had been accomplished only after long and laborious efforts. I am happy to report, however, that after calling it to the attention of the proper Washington officials, soft wheat has been restored to its rightful lofty position under the 1955 loan program.

Our cooperative membership in the country operates largely on the same principle as the private elevator. The local elevator not only handles the farmers' grain but also furnishes supplies to farmers in the way of fertilizer, petroleum products, farm machinery, feeds, fencing and many other commodities. We have some heavy volume stations in the surplus grain area and some of lower volume in the deficit areas. Usually, in the surplus areas the supply business is smaller, and the reverse is true in deficit areas. The volume of their supply business depends on the area in which they are located. Some are more successful than others and the degree of success can usually be measured by the quality of local management.

The country cooperatives are owned and controlled exclusively by local producers. The state organization has no investment in them. However, we do

lend advisory and sometimes financial assistance when called upon. We try to keep them informed at all times on markets, market trends, government programs, and all the other things they have a right to expect of us who have been entrusted with the marketing of their grain and furnishing of their farm supplies. We have no contractual or agency relationship with our membership and we depend entirely upon the quality of our service in maintaining an arrangement which works out to our mutual business advantage.

Methods of handling grain have changed greatly during the past decade. Farm mechanization has created new problems for the grain industry. It used to take from six to eight weeks, with good weather, to complete a harvest. I used to be in the private grain business as a country elevator operator. I recall distinctly that we had a big day if we received wheat from eight different threshing rigs; now, with the combine, it is not unusual to get grain from fifty different ones. Transportation also has changed. The truck has displaced the wagon and, in many instances, the railroads, too. There has also been a large increase in water-borne grain, particularly in the southeast, through the development of the Tennessee River. To meet this change from a terminal and regional standpoint we have tried to fortify ourselves against any contingency. Our terminal elevators can all handle grain by trucks as well as railroad cars. Our elevators at Evansville, Indiana, on the Ohio River and at Decatur, Alabama, on the Tennessee River are all equipped with marine legs to handle grain by barge transportation. We are presently locating at Toledo, Ohio, in preparation to take advantage of any opportunities that may be offered through the development of the St. Lawrence Seaway. To meet the demands of a heavy fall harvest of corn, the drying capacity of our various terminal units has been increased to 100,000 bushels daily. The things we have done, others have done too. It is mentioned simply to give you some idea of the changes that are taking place within our industry.

We do not encourage our country membership to use the grain futures markets either for speculation or hedging. In fact, we actually discourage it. Our country elevators have had some unfortunate experiences in the past in trying to carry an inventory under a hedge. They do not seem to understand the connection between the cash grain market and the futures. Either through carelessness, negligence, or for some other reason, they often failed to divest themselves of the cash grain and the futures simultaneously. This put them in a speculative position immediately and with disastrous results ultimately. We prefer to place and remove all of the hedges ourselves.

As a protective service to our membership in marketing grain we do offer to buy grain in any quantity. We do not require their sales to us to be in carlots or multiples of 1,000 bushels. We will purchase in 100, 200, or 300 bushels as the case may be. When such sales aggregate a carlot, we then give the country elevator shipping instructions. This works no undue hardship on us. While the amount may be small with each elevator, yet when there are a hundred elevators concerned, the aggregate puts us in a position to use 5,000-bushel multiples for hedges. It is a protection to the small volume house and a well-appreciated service particularly during periods of erratic and volatile markets.

The outlets for our grain are many and diverse. White corn millers often want a particular quality re-cleaned. Some feed manufacturers want No. 3 or 4 yellow corn; others want No. 2 yellow corn. Wheat millers also want a

particular type. Industrial alcohol manufacturers are not so much interested in quality as in price. We happen to be located at the front door of a large segment of the whiskey distilling industry. Our sales to them are substantial. Contrary to common conception, they use only the best No. 2 yellow corn; 14 percent moisture or less is a minimum requirement and often re-cleaned. They think, not in terms of the price of a bushel of corn, but what that corn will yield in gallons of alcohol. To meet these demands, all modern terminals are equipped with cleaners, scourers, clippers, dehydrators, and other machinery. It is obvious, therefore, that grain marketing in its true sense means much more than just receiving grain from the country, placing it in a terminal elevator, and then loading it out again.

The various consuming interests in the grain trade employ different patterns in their purchases. We have one account that buys about 5,000 bushels of corn at the close of the market each day. Another smaller one which buys one car each Monday, Tuesday, and Thursday. Still another buys a week's supply every Wednesday but does not price it until later in the week. One distiller account buys a six-month supply in each purchase semiannually. Distillers as a rule, however, buy in units of 100,000 to 250,000 bushels for scattered shipment over a specified period.

Most terminal elevator operators, including ourselves, carry an inventory of hedged grain. This places them in a position of meeting the buyers' demands at the market at any time and for any shipment, and, if the elevator is properly equipped, any specified quality.

Soybeans may still be thought of as something new in this country, when one realizes that as recently as thirty years ago, the harvest of soybeans in the United States was less than 2 percent of the 1954 crop. On the other hand, in the year 3000 B.C., they were an important component in the economy and lives of the Chinese people. In 1952, the states of Illinois, Indiana, Ohio, and Iowa produced over 62 percent of the entire soybean crop in the United States, and, indeed, they now play a major role in the economy of Midwestern farmers.

It is interesting to note that since we had a production of only 5,000,000 bushels of soybeans in 1924, there has been an astounding 6,000 percent increase in soybean production. But even more unique is the fact that commercial demand for the products of this raw commodity has kept pace with the phenomenal increase in production. This is attested to by the fact there has never been a heavy surplus of soybeans in this country. We have used all of our production except a carry-over of about 13,000,000 bushels of the 1942 crop, and a carry-over of about 10,000,000 bushels of the 1952 crop.

There are three methods of processing soybeans:

1. The hydraulic.
2. The expeller or screw press.
3. The extraction or solvent.

The solvent method is the most extensively used; in fact, there is a solvent capacity of 265,000,000 bushels in the heavy soybean processing area. When only this solvent capacity is related to the total production in the United States

in 1953 of 262,000,000 bushels, one begins to wonder if the only limitation to soybean processing might be our ability to produce the raw commodity.

Even though soybean production was still in the diaper stage, the Chicago Board of Trade was quick to recognize the need and to establish a futures market for this commodity and its products. It is evident that these futures markets have substantially contributed to the daily and orderly manner of marketing soybeans for the farmer and supplying him with "bean" meal, which is one of the largest proteins used in feeds. In fact, soybeans furnish 40 percent of the supply of the protein concentrates.

Their marketing poses a problem that is not encountered in the marketing of grains, such as corn, rye, oats, etc. While only a small percentage of corn (about 15 percent) moves into commercial outlets for processing, a much larger percentage of the soybean production finds its way into commercial channels, as there is only a small demand for soybeans on the farm for seed or feed utilization. Since soybean processors have located their plants at interior points in the heavy bean producing areas, Chicago is not a major receiving market for cash beans, but the Chicago futures market is of primary importance, providing hedging facilities for soybeans and its end products, meal and oil.

In marketing large quantities of soybeans in Indiana, our organization uses the futures markets almost daily. The latter affords two distinct advantages. First, it permits us to hedge our anticipated purchases of the next morning, and secondly, it allows us to accumulate a hedged inventory. Since the processors are located at interior points, the type of transportation billing they receive is very important, as there is a substantial billing loss in the processing of soybeans. Through the accumulation of an inventory, we are able, in a large degree, to give various processors the type of billing that best fits their needs, thereby minimizing the loss suffered on soybean oil on which "transit privileges" are not enjoyed.

I have mentioned the primary role that the futures market, which provides the necessary hedging machinery, has played in reducing the distribution cost of grains. With the violent changes that take place at times in soybean prices, I shudder to think what the impact would be, not only on cost of distribution, but also on the merchandiser of soybeans, without the hedging facilities of the futures market.

Our board of directors is composed 100 percent of farmers and they know the hazards of speculation. I am under a rather heavy bond to impress upon me that such activities are to be avoided. Frankly, I cannot define speculation or speculators. Is a man who invests in real estate with the expectation of an enhancement in value, a speculator or an investor? Are insurance companies who insure your life or your properties investors or speculators? We call them "underwriters," but are they speculators? Is the man who buys 5,000 bushels of July wheat in the pit a speculator or investor? The very men who have given me my directive are in the most hazardous of all business, that of farming. They must outguess weather, pests, insects, etc. in order to produce and after they have produced, must hope that sales will be at a price high enough to insure adequate income over expenses that preclude insolvency—are these men speculators?

However, I know what they want done. I am not supposed to buy and sell grain futures unless there is an offsetting and like amount of cash grain involved. In other words, I must keep hedged at all times. The roles played by the professional speculator or investor, as we know him, must be underemphasized. It is he who largely offers liquidity to the market. Grain merchandising is done on the narrowest of all margins. Most purchases and sales of cash grain are handled at less than one percent gross. This is occasioned by the fact that the industry knows that grain can be bought almost instantly, as well as sold instantly through functionaries associated with the commodity markets.

Our organization uses the futures markets extensively and their importance to the grain industry must not be overlooked. Our present marketing system cannot survive without the futures markets. They have a multiplicity of uses. By taking delivery, they may be a source of supply to a buyer. By making delivery, they may be an outlet for a seller of the cash article. They can also be used as a vehicle for speculation, investment, or hedging.

Our firm uses the grain futures market almost exclusively for hedging against cash grain inventories, although there have been a few times that we have used them as a source of supply. Webster says a hedge is an instrument used to minimize a loss. I do not quite agree with the definition. I like to think of a hedge in grain merchandising as an instrument to insure a merchandising profit.

I do not mean to imply that simply by hedging, you are assured of a profit, because you still must have an adequate margin between your buying and selling price at the outset. The purchase at the inception must be at the right relationship to the future.

During the heavy rush of harvest movement of grain, it would be impossible for us to operate successfully without using the futures markets as a hedge. When we are servicing so many country elevators during that period, it is physically impossible for us to merchandise grain as fast as we buy it. During the recent wheat harvest, we received more than 100 telephone calls from our country membership booking wheat. Many mornings our purchases will aggregate in excess of 300,000 bushels; 750,000 frequently and 1,500,000 occasionally. To eliminate an undue risk, we often anticipate our next morning's purchases by selling futures on the day previous. Then during the trading hours we sell the cash wheat and buy back our futures. If during the harvest movement, the basis for cash wheat is substantially below the futures, instead of selling the cash wheat at the time of purchases we often bring the wheat to our terminal elevators in Evansville, Indianapolis, Louisville, and Decatur, (Alabama) for later sale. This is particularly true if the distant futures are high enough to secure adequate carrying charges. It is historic and fundamental that the cash structure in Chicago will approximate the current future in value at maturity.

It is axiomatic that any merchandiser, to be successful, must have available to his buyer that which the latter needs at the market price and at the time he wants it. This is true whether it is sweet potatoes, Sunkist oranges, or B.V.D.s. Grain merchandisers are no exceptions, and it is only through the use of the commodity exchanges that this is possible.

Hedging also, with reputable firms, makes it less difficult to acquire operating capital. One of the first questions a prudent banker will ask is, "do you hedge?" If you do, he knows that the security you offer him in the way of warehouse receipts is always worth the current market. Good grain firms, with sound hedging policies, are always welcomed by lending agencies because their warehouse receipts are considered prime collateral. Many banks will lend 90 percent of the current market value on grain warehouse receipts if the grain represented by them is hedged.

The question has often been asked me—why is it necessary to use the commodity futures markets when the government is supporting prices on one hand and providing a ceiling on the other, within certain limitations, by making supplies available which it previously had acquired? It is a good question but difficult to answer. Ours is a generous and beneficent government. Its benefactions have reached the innermost recesses of our economic world. We are living in a "rigged" economy in which the law of supply and demand operates only with difficulty. I have always felt that it should be the function of the government to step in and assist when one segment of our economy gets out of line with other segments, particularly so, when maladjustments are actuated by laws or regulations fashioned by the government. Agriculture is no exception. As a result of this unfair economic relationship, we have the present farm support program as statutory. In its operation, the government now finds itself with huge supplies of grain on hand and is in the same position of the speculator who tries to corner the grain market. The law of supply and demand still functions and is no respecter of persons. The law may be temporarily suspended but never totally repealed. The government is now faced with the difficult task of "burying the corpse." Unfortunately, the present law prohibits the Commodity Credit Corporation from disposing of the corpse until it smells to high heaven. Someone must come up with an answer to eliminate this undesirable feature of the law. It is apparent now that the agency which was used to enhance grain prices is the same one which is accused of deflating those same prices.

There is no question but that in the operation of their support program, many erstwhile functions of the grain trade have been assumed by the government. This may be deliberate or inadvertent, probably the latter, but, nevertheless, it has happened. It is only fair to say that the present administration is cognizant of what is taking place; it has made several procedural changes whereby the grain trade may be used in the normal manner in disposing of some of these surpluses. For this, we are grateful and the government is to be congratulated.

The point I am making is simply this: If the government itself is not able to support prices indefinitely (with all its resources) then the maintenance of our commodity exchanges becomes all the more important. As long as I am charged with the responsibility of managing a regional farmers' marketing cooperative, we will always use a sound hedging program which is available only through those exchanges.

Regardless of how short the supply of any commodity becomes, there will always be plenty to go around in a free market. Our commodity exchanges must be perpetuated as an agency wherein the producer, the consumer, and the general public may express their views as to values. Free markets, if

unabused and uninhibited by unnecessary controls, will fill every need except in periods of severe economic readjustments.

The operations of the futures markets are intricate, difficult, and incomprehensible to many people. While I am necessarily not familiar with all of the intricate details and mechanisms of futures trading, we use them extensively in our daily operations and I do know as manager of a large producers' grain marketing organization—that the spread between what the producer gets and what the consumers pay, would be many, many times greater without the commodity exchanges than with them.

