

Futures Markets and Price Risk Management

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I. Introduction and Background

A. The Basics

1. What is the futures market?
2. What is a futures contract?
3. Contract specifications
4. Who uses futures markets – hedgers, speculators, etc?

B. The Operation of the Futures Market

1. How is a contract traded – brokers, runners, exchange members
2. How does a futures market account work – margins, margin calls, fees
3. Zero sum game, one trader's loss = another trader's gain
4. Role of clearing house

C. Reading Reports

1. Examining a futures market reports
2. Examining a price chart

II. The Concept of Basis

A. What is Basis?

1. Why are local prices and futures prices different?
2. KY basis chart

B. Using futures to predict prices and understand prices

1. What goes into futures prices?
2. Adjusting futures price to estimate local price
3. Opportunities for Risk Management

III. Using futures to manage price risk

- A. Opportunities to manage price risk
 - 1. Why risk management is possible
 - 2. Taking a futures position
 - a. long and short positions
 - b. choosing a contract month
 - c. anticipating basis

- B. The straight hedge
 - 1. Concept
 - 2. Feeder cattle example
 - 3. Straight hedge philosophy

- C. Setting a price floor
 - 1. What are options?
 - 2. Concept
 - 3. Feeder cattle example
 - 4. Option philosophy

IV. Advanced Price Risk Management Strategies

- 1. Setting a fence
 - a. Concept
 - b. Example
 - c. Philosophy
- 2. Vertical put spreads
 - a. Concept
 - b. Example
 - c. Philosophy
- 3. Others