



ADDING MGEX NSI FUTURES TO HEDGING STRATEGIES

Finding the right trading strategy is difficult, especially in volatile markets. Below is a strategy to consider that reduces basis risk through a combined use of physically delivered futures contracts and MGEX (Minneapolis Grain Exchange) financially settled National Soybean Index (NSI) futures contracts.

The below example shows how soybean hedgers can use a combination of traditional CME Group, Inc. (CME) hedges and the complimentary MGEX NSI futures to reduce basis risk. Since NSI futures contracts offer a stable country-level basis, hedgers can dedicate a portion of their hedging to the NSI futures contract and reduce overall basis risk. The following table shows the soybean basis characteristics for North Central Iowa for the 2000-2007 crop years at various levels of NSI hedging.

Table 1. North Central Iowa Soybean Basis Statistics, 2000-2007 Crop Years

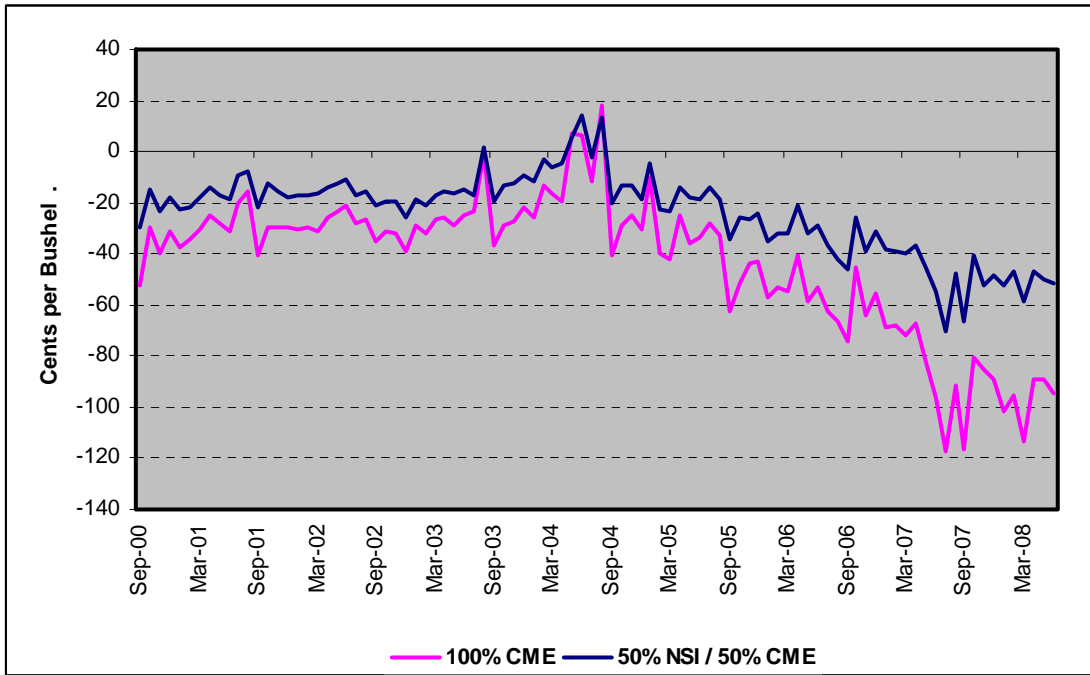
	100% CME	25% NSI	50% NSI	25% NSI	100% NSI
Average	-43.6	-33.8	-24.0	-14.2	-4.4
St. Deviation	27.9	22.0	16.2	10.8	6.6
Basis Range	135.3	109.6	84.1	64.4	44.7

As shown in the table, putting just 25% of the hedge in MGEX NSI futures can lower basis risk. As measured by the standard deviation, the 25% NSI (75% CME) hedge reduced basis volatility by almost 6 cents per bushel from 27.9 to 22.0 cents (21% decline). Likewise, the 100% CME hedge has a historical basis range of \$1.35. This wide-ranging basis can be reduced to 84.1 cents by simply placing one-half of the hedges in the NSI futures.

Additional basis stability can be achieved by using the MGEX NSI futures contract as a complimentary tool to traditional physically delivered futures contracts when hedging soybean positions. Therefore, it is very practical to view the NSI futures contract as a complimentary product to existing soybean futures hedging strategies.

Figure 1 shows the basis behavior for a hedging program that splits 50% of the hedging into MGEX NSI futures and 50% into CME futures. While a 100% NSI hedge provides the most stable basis, the combined program still results in a more stable basis than exclusively using traditional soybean futures hedging strategies.

Figure 1. North Central Iowa Soybean Basis, 2000-2007



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