

Trading Australian Wheat Basis

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Being aware of the relative value between Australian and international wheat prices is important for anyone that is exposed to the fluctuations in the price of wheat. Understanding basis, how it is calculated and what moves it, assists traders to discover local pricing dynamics while being able to measure the effectiveness of hedge transactions.

ASX Grains futures and options contracts provide a way to get exposure to and manage Australian wheat basis. Traders can also take advantage of opportunities in a market with anonymous trading, transparent pricing with no counterparty risk.

What is basis and why does it matter?

Basis is the difference between the physical grain price and the futures grain price. More commonly, basis is any traded relative value spread by location, quality, physical or derivative.

When using futures to hedge a physical position, traders are still exposed to basis risk where the physical is not perfectly correlated to the futures. Being aware of movements in basis is critical to determine the effectiveness of a hedge.

What influences basis?

Different factors influence each leg of a basis trade:

- The world price discovery for wheat typically occurs on the CME with trading in Chicago SRW Wheat Futures. This price is influenced by factors such as global macroeconomic drivers, global supply and demand, and fund activity.
- Australian wheat basis is influenced by local market supply and demand, logistics, local weather and crop conditions.

Factors which influence a stronger or weaker Australian wheat basis include:

Strong basis

- Drought / El Nino
- Wet Harvest / Quality Issues
- Strong Domestic Demand
- Strong Export Demand

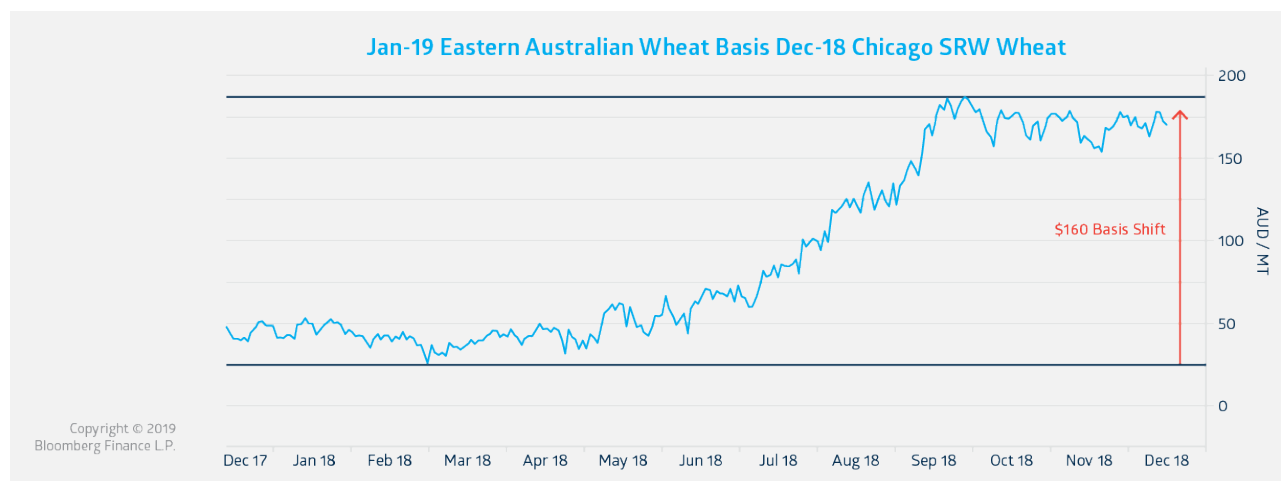
Weak basis

- Peak Supply at Harvest
- Good Rainfall
- Good Crop Forecast
- High Yields

Using ASX Grains futures to trade basis

Hedging Australian wheat using CME Chicago SRW Wheat Futures exposes your overall hedged position to movements in basis. Trading ASX NSW Wheat Futures versus CME Chicago SRW Wheat Futures also allows you to get direct exposure to Australian wheat basis.

The following chart illustrates basis risk by showing extreme movements in Australian wheat basis against CME Chicago SRW Wheat Futures.





Example: Basis trading

An Australian wheat exporter has bought 2,000MT of grain at harvest on ASX but is yet to sell this grain to Asian customers. The exporter hedges the grain by selling CME Wheat futures and hedging the AUD/USD FX rate.

Legs

Buy 100 lots January 2016 NSW Wheat @ \$298 AUD/MT

Sell 15 lots December 2015 CME SRW Wheat @515.25 USc/bu

Buy FX Forward*: 596,000 AUD @ 0.7660

*Notional contract value of FX hedge 596,000 AUD = 2000MT x298 AUD/MT

This locks in a long position in Australian wheat basis for the exporter who has now secured a supply of grain, whilst being able to price the Australian dollar wheat value when they choose at a point in the future.

How to calculate the basis value

Convert AUD/MT position to USc/bu
 $(298 \times 0.7660 \times 100) / 36.7437 = 621.25 \text{ USc/bu}$

Subtract CME trade price from ASX trade price
 $621.25 - 515.25 = 106 \text{ USc/bu}$

Basis value = 106 USc/bu over

Ready to trade basis? ASX Trade24

ASX Trade24 is ASX's electronic trading platform providing customers with access to all ASX Grains contracts. The platform is purpose-built for ease of access with a full suite of trading order management functionalities, to ensure you experience more flexibility in how you trade.

To access ASX Trade24, contact ASX Grains today.

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