FINC 623/ECON623
Homework Assignment—Risk Minimization Hedging
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Maximum team size: 3 persons

Note: This assignment uses data contained in the spreadsheet RISKMINHEDGE.XLS

The actual data for this assignment are from the corn and wheat futures contracts with an expiration of September 2002. Let us assume that the corn data are for spot corn instead of for a corn futures contract. Assume that today is May 31, 2002 and that you want to use the wheat futures contract to hedge your cash corn position of 200,000 bushels of corn.

Using the closing data for March-May 2002, determine the risk minimizing hedge in terms of contracts of wheat. (Be sure to determine and consider the contract size for the wheat futures.) Use the method discussed in *FOS 5e*, pp. 137-141. **Giant hint: Price levels or price changes?**

Evaluate the effectiveness of the hedge from June 1 to August 15, 2002.

Prepare a 1-page report that contains the following elements:

1. A one-sentence statement of the wheat futures position you would undertake.
2. Present the estimated regression equation that determined your hedge.
3. For the evaluation period, compute the gain or loss for the hedged and unhedged positions in dollar terms.
4. Prepare a graph like Figure 4.4 on p. 141 of *FOS*, except show the total value of the hedged and unhedged positions.