

CME Commodity Products

## Trading Options on CME Random Length Lumber Futures



## Global Leadership in the Financial Marketplace

CME is the largest and most diverse financial exchange in the world for trading futures and options - handling nearly 800 million contracts worth more than \$460 trillion in a single year. Founded in 1898, we serve the risk-management needs of customers around the globe by offering the widest range of benchmark financial products available on any exchange, traded via our CME Globex electronic trading platform and on our trading floors. Our innovative products cover major market segments including interest rates, equities, foreign exchange, commodities and alternative investment products. In addition, our clearing house matches and settles all trades and guarantees the creditworthiness of every transaction that takes place in our markets.

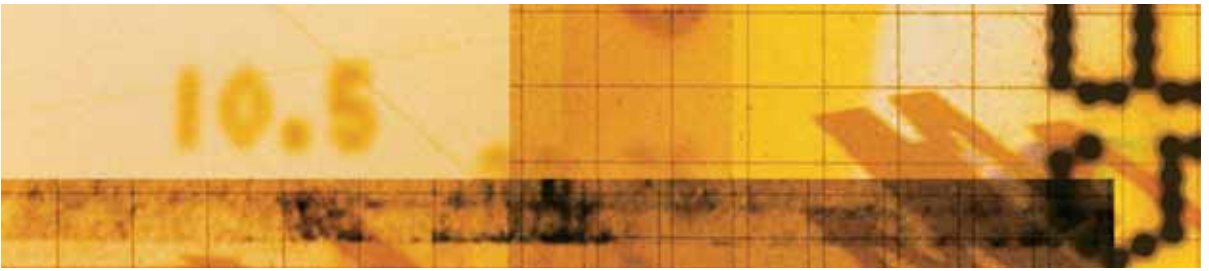
## CME Commodity Products

CME agricultural commodity products help farmers and agribusinesses manage the constant price risks they face, enabling them to lock in profits, enhance business planning and more effectively serve their markets. Commodity-related businesses that use CME commodity products to support and strengthen their operations are able to provide products to their customers at better prices.



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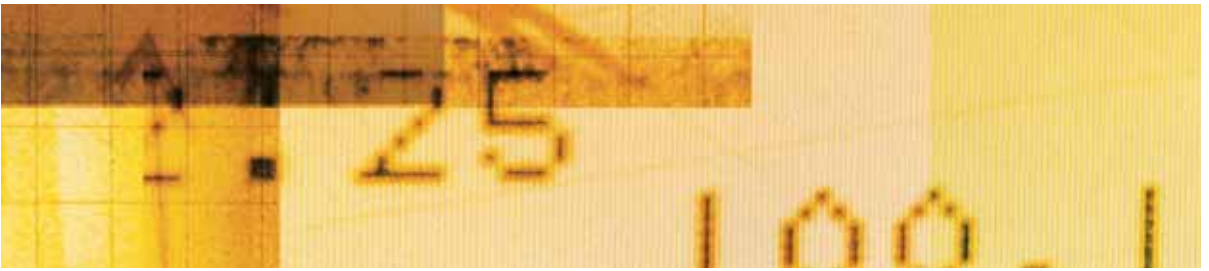
## About CME Random Length Lumber Futures and Options

### CME and the Random Length Lumber Marketplace

Cash lumber prices are unpredictable and volatile. Supplies can be constrained due to mill closings, environmental policies and other factors. Demand also tends to shift rapidly, based on interest rates and other economic conditions that affect housing starts. As a result, lumber prices react to supply and demand imbalances with frequent and often extreme changes.

Highly volatile prices can mean opportunity for large profits. But in an industry like lumber - valued at \$30 billion for the North American market - where costs are high and margins are tight, volatile prices can also mean risk of loss, sometimes devastating loss.

In 1969, CME became the first exchange to offer price protection to the forest products industry with the listing of CME Random Length Lumber futures contracts. Firms engaged in producing, processing, marketing or using lumber and lumber products have been able to hedge their risk exposure - reduce the risk of holding or acquiring inventory through taking an equal and opposite position in CME Random Length Lumber futures. Usually, but not always, hedgers transfer unwanted price risk to speculators. Speculators are investors who hope to achieve profits by buying futures when they think prices will rise, or by selling futures when they think prices will fall. Both hedgers and speculators are necessary for the efficient operation of a futures market.



## Advantages of CME Random Length Lumber Markets

CME Random Length Lumber markets offer the following key benefits:

- » **Risk Management** - CME Random Length Lumber futures serve as hedging instruments and as a means of capitalizing on commodity price fluctuations.
- » **Price discovery** - The futures markets assimilate current information about the underlying commodities, and in the process of trading, prices are negotiated that indicate levels above which buyers will not buy and below which sellers will not sell. CME Random Length Lumber futures do not create cash prices; they do, however, generate a current view of an equilibrium price or what the market will bear. If buyers are more eager than sellers, prices tend to go up. When the opposite is true, prices tend to go down.
- » **Spreading opportunities** - CME Random Length Lumber futures can also be used with a number of spreading strategies, to take advantage of the relative out-performance of one commodity sector versus another
- » **Market integrity** - By serving as the counterparty to every trade, the CME Clearing House virtually eliminates the risk of credit default (the risk that the other party to the contract will not perform) and protects the financial integrity of CME markets. Our centralized clearing function also enables any market participant to close or modify positions independent of the other party or parties in the original trade.
- » **Regulatory assurance** - The quality and strength of our regulatory capabilities ensure the financial security of our markets. Our integrated compliance and market surveillance functions assure market participants of the highest trading standards and supervision. CME markets are monitored by the Commodity Futures Trading Commission (CFTC), an independent federal regulatory agency.



## Trading Options on CME Random Length Lumber Futures

Basic economic uncertainty and price volatility represent both opportunities and risks for firms involved in the lumber industry. Since 1969, companies and individuals engaged in producing, processing and marketing lumber products have been able to reduce their price risk by hedging with the CME Random Length Lumber futures. In May 1987, CME provided the lumber industry with a new tool for managing its inherent price risk - options on lumber futures.

Options on CME Random Length Lumber futures offer many opportunities for both hedgers and speculators:

- » Limited risk
- » Unlimited profit/price protection
- » A variety of strategies to address all market conditions

Options on lumber futures are part of the successful family of options contracts currently trading at CME. CME also trades options on its foreign exchange, equity index, weather, livestock, dairy and interest rate futures contracts.

Options are a tool both hedgers and speculators can use to manage their price risk. This section of this brochure offers an introduction to the mechanics of options trading and basic lumber option hedging strategies. It explains what option contracts are and how they can become an effective part of traders' pricing plans.