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In The Cattle Markets

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Seasonality of Feeder Futures

Last spring I had the privilege to teach an SDSU course titled “Trading in Agricultural Futures and Options”. An assigned exercise was to propose and evaluate a strategy that could be routinely implemented. Seasonality was a common theme, asking things like “When do new-crop soybean futures peak in price?” After hearing some of the pitches by students, I wrote a note to myself to evaluate seasonality of feeder cattle futures prices.

Conventional wisdom says that markets are efficient and that any pattern that could be exploited should be arbitrated or bid away by speculators. At the same time, this is the feeder cattle market, which is a little thinner and more difficult to trade than many markets. As it is approaching the time of year for potentially backgrounding calves in the northern plains, the focus will be on the March feeder cattle futures. Thus, someone with calves may be following the March price and trying to decide if and when to hedge. It would be instructive to know when to place a hedge, when to wait, or if it does not matter.

In the past, I have used futures data from LMIC to track how futures prices in November compare to eventual prices in March. The process was to compare the average of March futures prices during November (four months from expiration) to the average of March futures prices during March (the expiration month). There was never much evidence to suggest any bias in the price; averages in November were often as wrong on the low side as on the high side and by similar amounts. Does that pattern still hold? A year ago the March 2018 contract traded at an average of \$153.56 during November and at an average of \$140.04 during March, suggesting hedging in November would have been a good choice. However, during the past decade there were five years of increases, five years of decreases and an average change of \$0.12. The averages were computed from the daily data to account for contract roll-over times. So yes, the pattern still holds. Note that the average change masks the decrease of \$19.02 in the 2015 contract and the increase of \$14.89 in the 2011 contract.

What about other months and any seasonality? During the past decade, the highest monthly average has occurred in November four times and in March four times, peaking in December and February the other times. Thus, looking back both hedgers and those that stayed in the cash market were equally likely to have topped the market in a given year. Considering hedging earlier reveals years with higher highs in October, August, July, May and April. Maybe January, which never had a high, could be looked at from the buyer’s side. As frustrating as this may sound, the lack of any seasonal pattern in the futures is reassuring. Selective hedging, hedging when there is profit to be locked in or extreme risk to avoid, continues to be a sound approach for those using feeder cattle futures.

The Markets

In the cash market, fed cattle traded higher for the week. Feeder cattle traded mostly higher, with some variation across weights and locations. Both live and feeder cattle futures price changes were mixed last week as trading continues in narrow ranges across expiration months. The volatility remains low in both markets, with some of the lowest implied volatility observed since September of 2014. The volatility is exceptionally low for the deferred live cattle contracts. Corn was up slightly for the week. Regionally, hay prices are relatively low and corn basis is relatively wide. Both trends are supportive of calf and feeder prices in the northern plains.

<i>Data Source: USDA-AMS Market News</i>		Week of 9/7/18	Week of 8/31/18	Week of 9/8/17
5-Area Fed Steer	all grades, live weight, \$/cwt	\$107.67	\$107.18	\$104.92
	all grades, dressed weight, \$/cwt	\$170.25	\$169.59	\$166.13
Boxed Beef	Choice Price, 600-900 lb., \$/cwt	\$209.13	\$212.03	\$192.35
	Choice-Select Spread, \$/cwt	\$9.62	\$8.79	\$2.03
700-800 lb. Feeder Steer	Montana 3-market, \$/cwt	\$151.72	\$150.50	\$158.00
	Nebraska 7-market, \$/cwt	\$165.69	\$157.01	\$161.24
	Oklahoma 8-market, \$/cwt	\$153.79	\$151.88	\$149.42
500-600 lb. Feeder Steer	Montana 3-market, \$/cwt	\$180.00	\$162.50	\$159.62
	Nebraska 7-market, \$/cwt	\$174.18	\$182.46	\$167.43
	Oklahoma 8-market, \$/cwt	\$159.44	\$161.82	\$157.69
Feed Grains	Corn, Omaha, NE, \$/bu (Thursday)	\$3.33	\$3.18	\$3.20
	DDGS, Nebraska, \$/ton	\$132.50	\$139.00	\$108.00