

In The Cattle Markets

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Higher Market Volatility

So much of the recent news in this publication series and elsewhere has revolved around the record level of prices and the implications for herd expansion. Typically record prices are joined at the hip with increased price risk (the high risk, high return phenomenon). How does the market picture look as we wave good-bye to 2014?

Not surprisingly, market risks have moved higher along with prices. Figure 1 provides a lengthy history of implied volatility for feeder and live cattle futures. The timeline begins just after the high prices experienced in 2003 and the ensuing price decline following the BSE case. Implied volatility values were in the 20 to 33 percent range in early 2004 for live cattle and 12 to 23 percent for feeder cattle. The increased volatility in 2008 and 2009 is also easily identifiable in figure 1 as implied volatility raced up to 25 percent for both live and feeder cattle. Recently, this measure began to decrease in mid-2012, falling to about 7 percent one year ago. However, as prices have increased, so has volatility with feeder cattle futures price implied volatility at about 12 percent and live cattle futures price volatility at about 14 percent.

Specifically, looking more closely at feeder cattle price volatility for contract months in 2015, this phenomenon is no different. As time passed and as contracts became available in 2014, implied volatility measures increased along with prices. These peaked in August 2014, ranging from 12 to 14 percent depending on the contract. Interestingly, the January 2015 contract carried more risk (i.e., a larger implied volatility value) than the more deferred contracts, but this has since been reversed. Keep in mind that these deferred contracts typically traded below nearby months. In other words, futures market participants hesitated to push prices in very distant months to the high levels of those in more current months.

As the market has steadied (and even declined at times) implied volatility values have begun to decline as well. This is expected since a steady market is also viewed as a less risky one and therefore volatility measures should fall.

In retrospect, market volatility is lower now that it has been in the past. Never the less, the extremely strong bull market that has been in place in 2014 has pushed market price uncertainty higher. When considering risk management strategies tied to options (puts, calls, and LRP insurance) this led to higher premiums relative to what would have been seen in less risky times. On the positive side, the current decline in implied volatility measures is noticeable in the premiums prices.

Figure 1. Market Implied Volatility of Feeder and Live Cattle Futures Prices

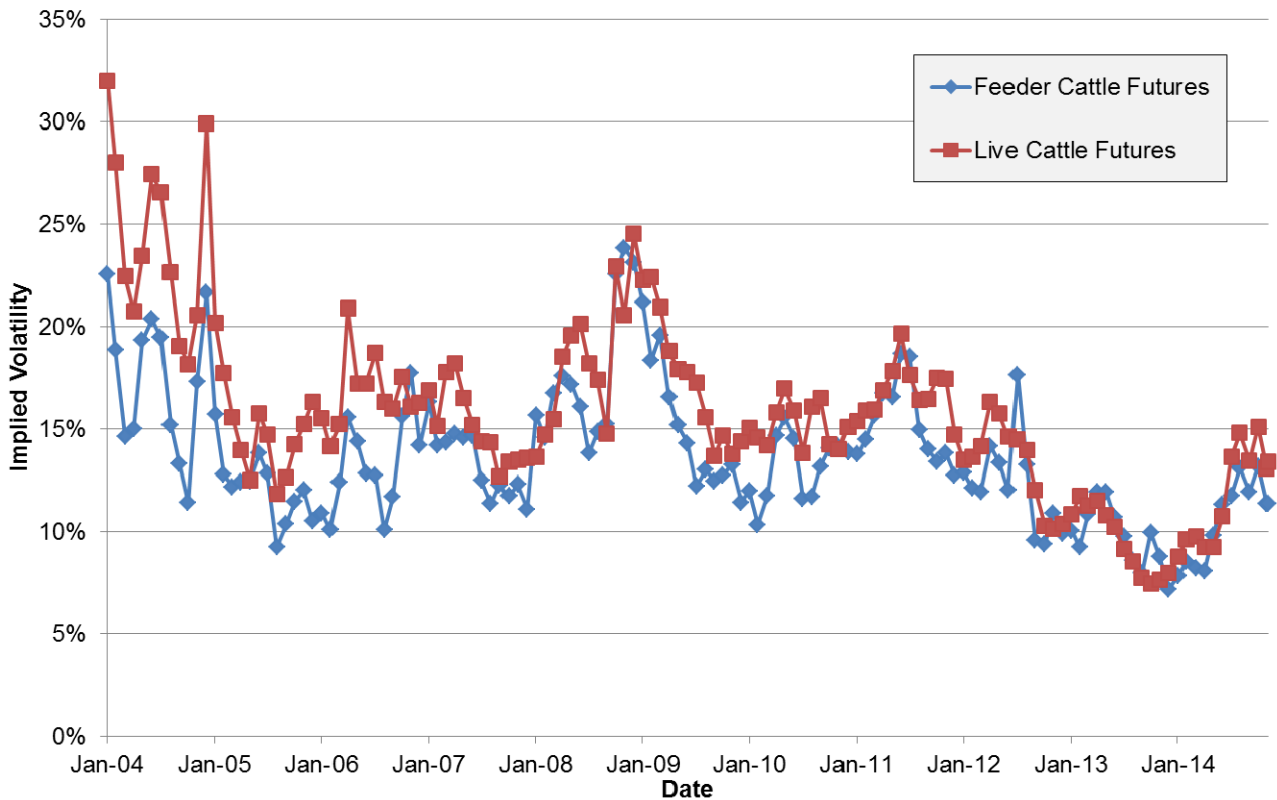
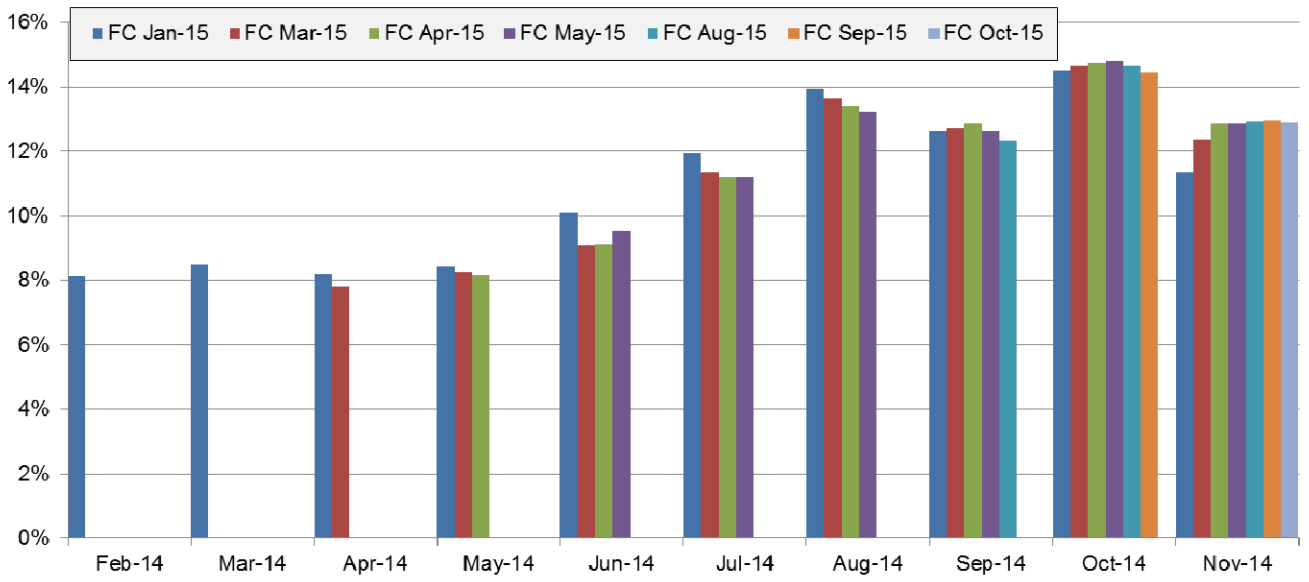


Figure 2. Feeder Cattle Futures Price Implied Volatility 2015 Contract Months



The Markets

Fed steer declined this week. The five area weighted average live and dressed prices were \$166.83 and \$263.95 per hundredweight, respectively, down \$4.55 and \$2.77. Wholesale Choice boxed beef ended the week with an average price of \$255.44 per hundredweight, down \$1.33. Heavy feeder steers in Oklahoma averaged \$238.49, while light steers were \$293.15. Cash corn in Omaha gained 14 cents per bushel, rising to \$3.78.

		Week of	Week of	Week of
<i>Data Source: USDA-AMS Market News</i>		12/5/14	11/28/14	12/6/13
5-Area Fed Steer	all grades, live weight, \$/cwt	\$166.83	\$171.38	\$131.87
	all grades, dressed weight, \$/cwt	\$263.95	\$266.72	\$208.78
Boxed Beef	Choice Price, 600-900 lb., \$/cwt	\$255.44	\$256.77	\$202.65
	Choice-Select Spread, \$/cwt	\$13.90	\$12.83	\$13.03
700-800 lb. Feeder Steer Price	Montana 3-market average, \$/cwt	\$236.80	--	--
	Nebraska 7-market average, \$/cwt	\$126.80	\$259.78	\$171.61
	Oklahoma 8-market average, \$/cwt	\$238.49	--	\$163.55
500-600 lb. Feeder Steer Price	Montana 3-market average, \$/cwt	\$297.33	--	\$184.49
	Nebraska 7-market average, \$/cwt	\$297.18	\$305.82	\$198.56
	Oklahoma 8-market average, \$/cwt	\$293.15	--	\$187.06
Feed Grains	Corn, Omaha, NE, \$/bu (Thursday)	\$3.78	\$3.64	\$4.25
	DDGS Price, Nebraska, \$/ton	\$125.95	\$129.75	\$217.80