

A Different Animal: Futures Contract Design, Hedging Effectiveness, and Transparency in Thinly Traded Cash Markets for Cattle and Hogs

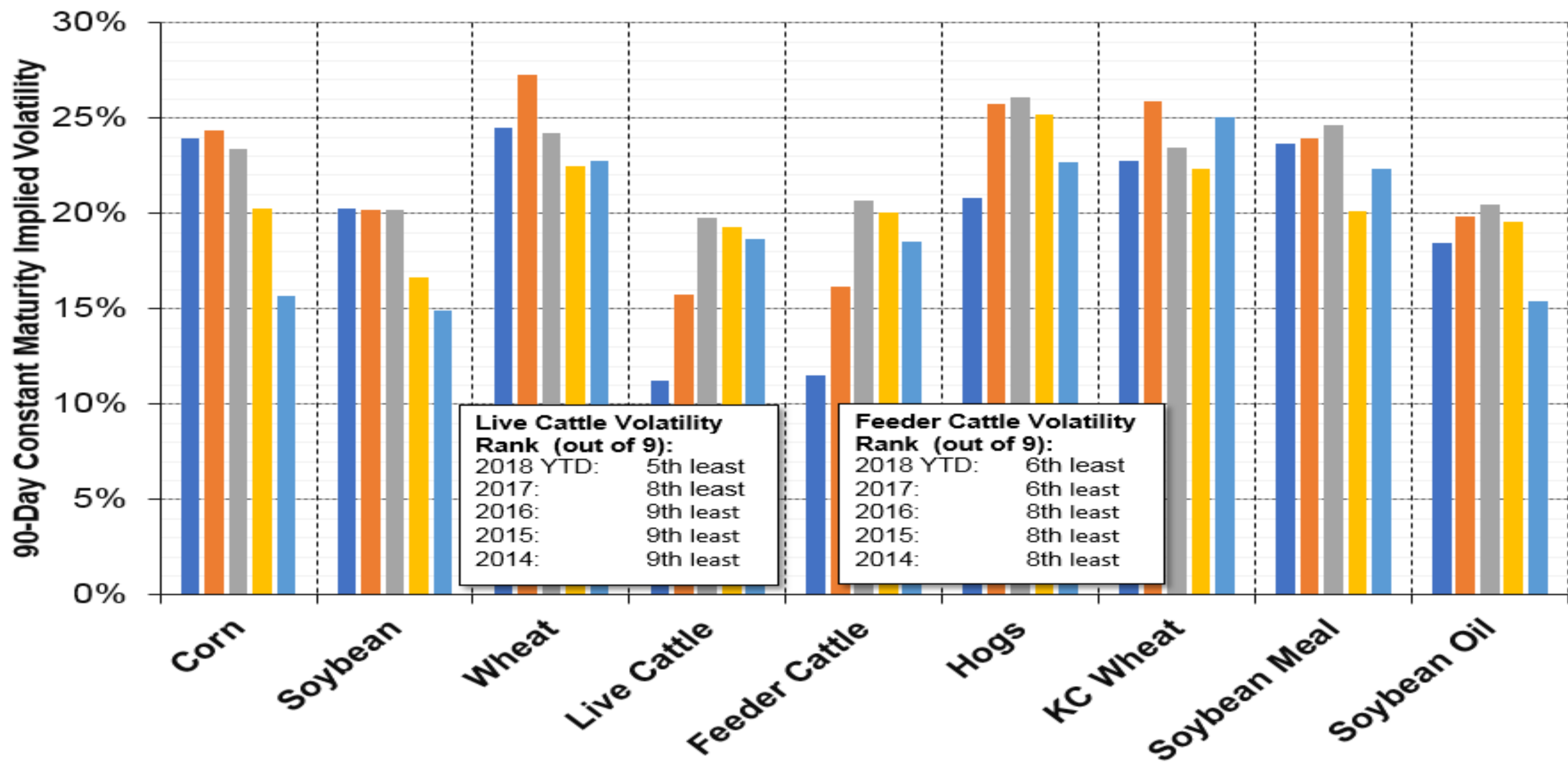
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Bartlett Cattle Company

Evaluation

- 1) The Live Cattle contract is correlating more tightly to cash than over most periods in that past two decades.
- 2) Liquidity is adequate to allow for timely hedge execution.
- 3) Volatility is less than most other major agricultural futures.
- 4) Live Cattle futures are less volatile than cash boxed beef and cash live cattle.
- 5) Conventional risk managers are largely pleased with function of the contract.

Agricultural Futures Volatility-By Commodity

■ 2014
 ■ 2015
 ■ 2016
 ■ 2017
 ■ 2018 YTD



Types of Transactions

Cash

- **Flavor 1:** Negotiated base prices
[aka: cash transactions]
- **Flavor 2:** Derived base prices
[aka: formula transactions]
- **Other Flavors**

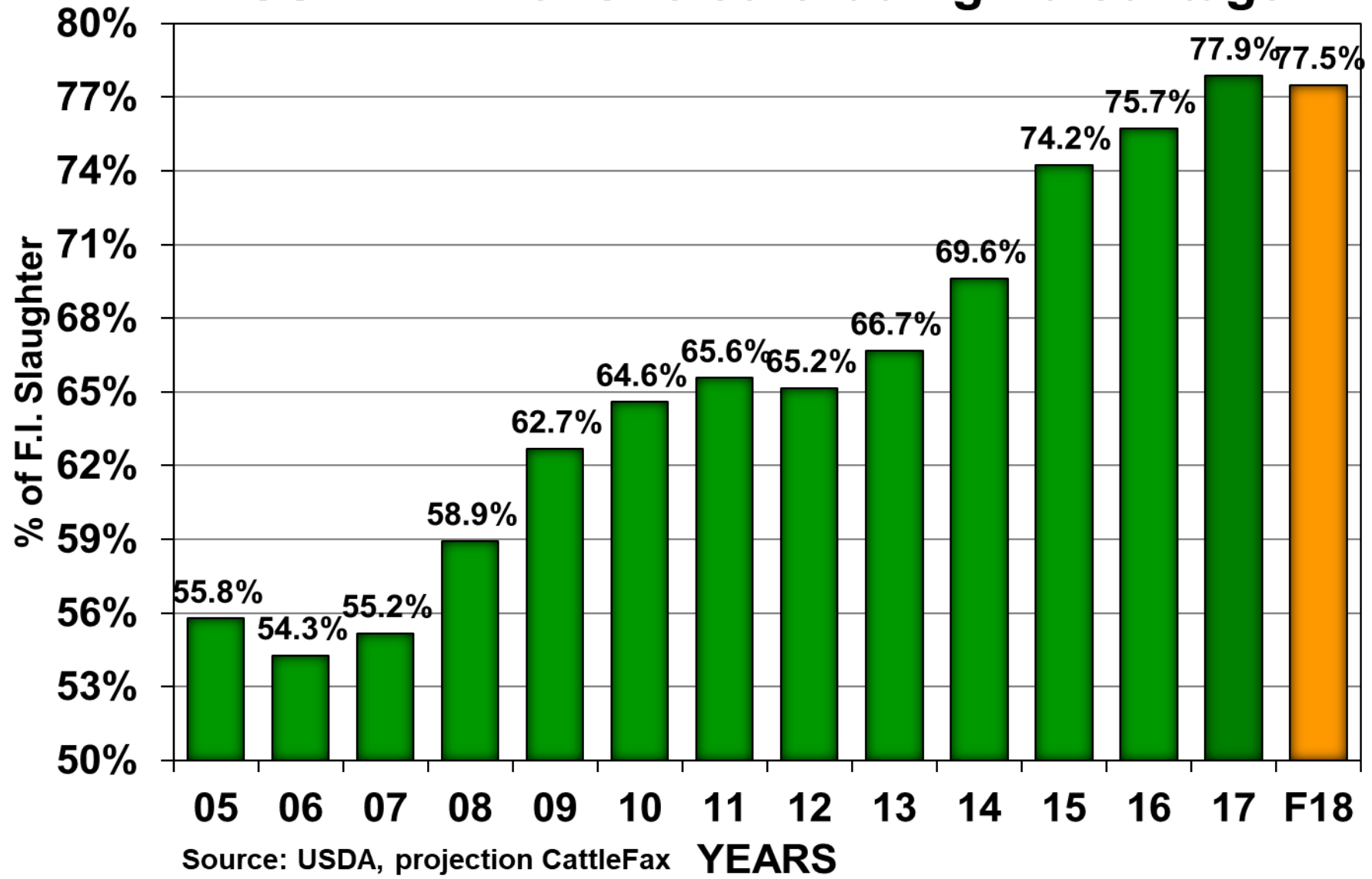
Futures

Quality of Convergence

“A **common mistake** in cattle markets is to compare the futures price with the average cash market price and then make statements about convergence. **Rarely does the quality of the average cash market cattle exactly equal the futures contract specifications.** Thus it is important to quality-adjust the average cash market price before judging how well the futures market converged to the cash market.”

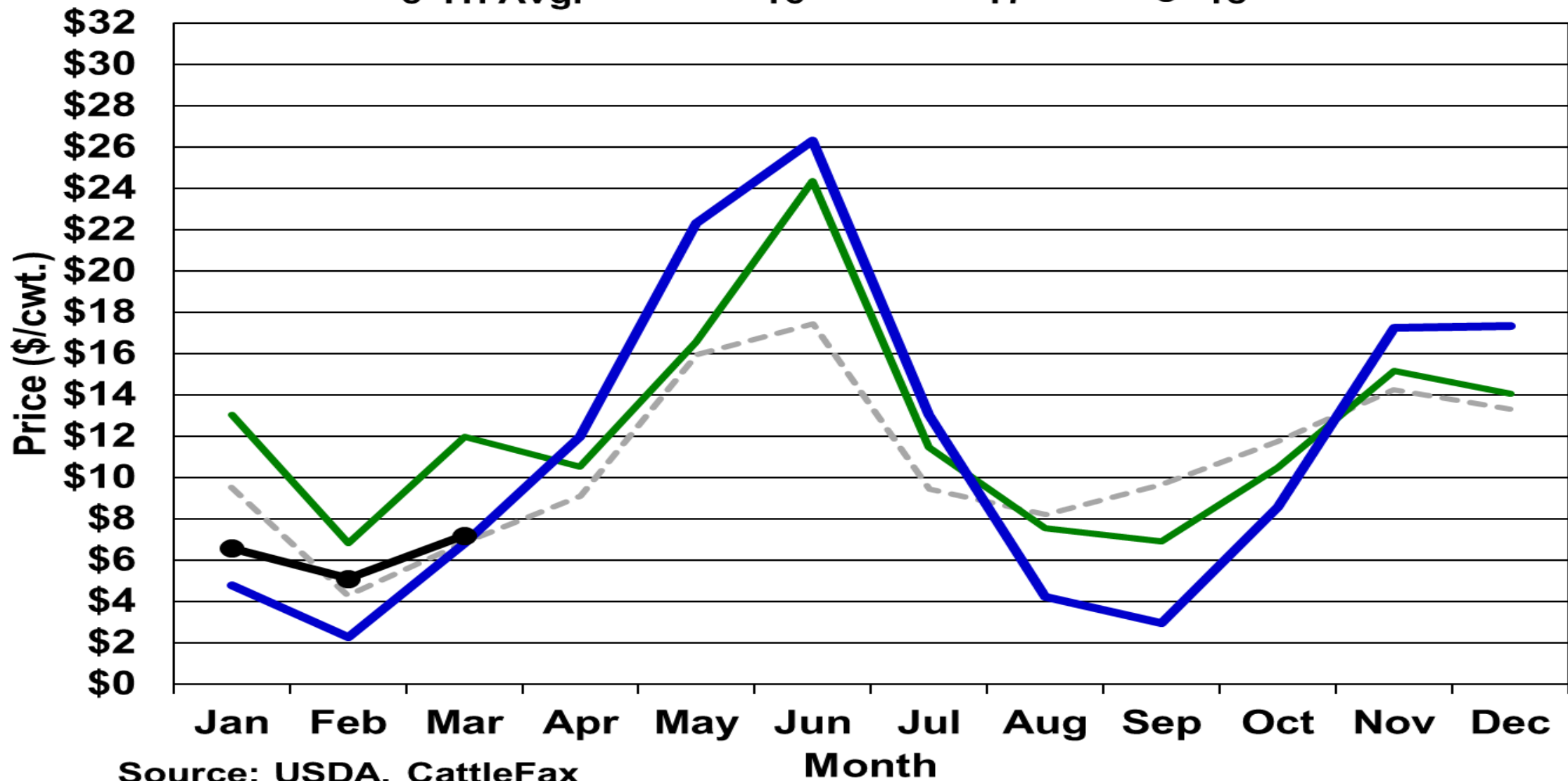
-CME 1997: “An Examination of an Industry Proposal to Cash Settle the Live Cattle Contract”

USDA Prime+Choice Grading Percentage



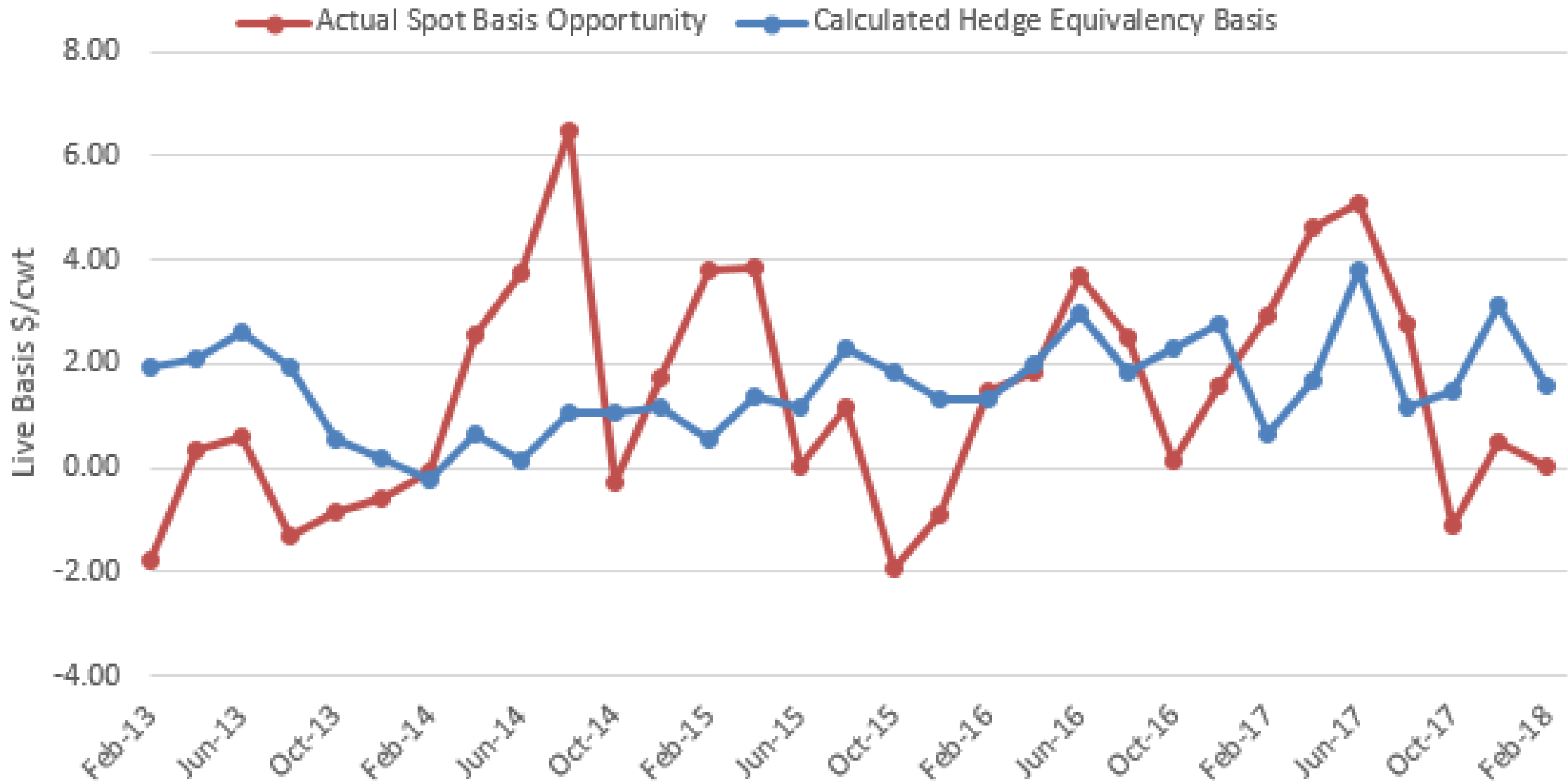
USDA Spot Choice-Select Price Spread

--- 5-Yr. Avg. — 16 — 17 —● 18



Source: USDA, CattleFax

Actual and Calculated Basis: SW KS



Average Difference: \$0.18/cwt (calculated higher than actual spot)

LM_CT150

St. Joseph, MO Mon Mar 26, 2018 USDA Market News Service

5 AREA WEEKLY WEIGHTED AVERAGE DIRECT SLAUGHTER CATTLE Texas/Oklahoma/New Mexico; Kansas; Nebraska; Colorado; Iowa/Minnesota feedlots (Includes all transactions regardless of delivery day)
For: Week Ending Sunday, 3/25/2018

Confirmed: 120,137 Week Ago: 104,711 Year Ago: 94,924

LIVE FOB BASIS - Beef Breeds

	Head count	Weight Range	Price Range	Avg Weight	Wtd Avg Price	
STEERS						
Over 80% Choice	17,971	1,265-1,580	124.00-130.00	1,477	126.30	
65 - 80% Choice	16,940	1,185-1,575	122.00-126.50	1,403	125.49	
35 - 65% Choice	9,936	1,200-1,480	123.00-126.00	1,268	125.85	
0 - 35% Choice	-	-	-	-	-	
Total all grades	44,847	1,185-1,580	122.00-130.00	1,403	125.90	
HEIFERS						
Over 80% Choice	12,612	1,100-1,450	120.50-127.50	1,302	125.75	
65 - 80% Choice	6,833	1,125-1,350	122.00-126.00	1,241	125.36	
35 - 65% Choice	1,609	1,100-1,270	125.00-126.00	1,194	125.68	
0 - 35% Choice	-	-	-	-	-	
Total all grades	21,054	1,100-1,450	120.50-127.50	1,274	125.62	

Timely
Trusted
Thorough
Tidy
Public

Livestock Mandatory Price Reporting

For Discussion

- 1) Settlement Method
- 2) Use/understand/improve
- 3) Cross Hedging
- 4) Supply Chain Optimization
- 5) Cattle Futures: Thank God!
- 6) Cash Price and Futures Spread Price Volatility