Marketing Strategies for the 2016 Calf-Crop

Now is the time to create a marketing strategy for your 2016 calf crop. Cow-calf producers who have an idea about the expected value of their calves can evaluate price offerings and decide among marketing at weaning or retaining ownership. Another issue is deciding whether to just watch and take a cash price at some point or get some price protection in place.

With October 2016 feeder cattle futures trading around $138 per cwt, producers can use basis to find an implied calf price or value. In October 2015, the basis on 500 to 600 pound steers in Iowa was $31 per cwt (figure 1). However, this year the basis has been averaging 52% weaker than in 2015. If this basis pattern holds for October, calves for October marketing would be valued at $153 per cwt.

Figure 1. Iowa Feeder Calf Basis (Cash – Futures), 500-600 lb Steers, Medium & Large 1

Specific to calves, producers can also look at deferred feeder cattle futures prices. The feeder futures are inverted. The nearby contract month and contract months closer to expiration trade at higher prices than the more deferred months (figure 2). The January 2017 contract, for example, is trading around $130 per cwt. The deferred months would indicate the ultimate value of a calf today that may weigh 700 to 800 pounds in early 2017.
October futures, with a basis adjustment, suggest a 550-pound steer calf would be valued at $841.50 per head in October. January 2017 feeder cattle futures suggest a 750-pound feeder steer would be worth $975.00 per head in January. If you can put on the extra 200 pounds of gain for less than $133.50 per head, the fall market currently is offering to reward you for doing so.

What should sellers do? Sellers who know expected cost of gain can compare their costs with the expected market values to estimate margins. Expected margins will be sensitive to adjustments in cost of gain driven by changes in feed prices and actual daily gain realized over the backgrounding period. Furthermore, producers marketing calves should be cautious with price expectations in light of changing market conditions. From today until producers actually market their calves, prices could rise, fall or hold steady.

Consider forward pricing

If forward bids are at or better than levels implied by the futures market, then consider forward contracting. USDA’s Superior Livestock Report (AM_LS753) for the Northcentral states (CO-WY-NE-MT-ND-SD-IA) shows that in recent weeks 500 to 600 pound steers with an October delivery date traded in a range from $143 to $167 per cwt and at a weighted-average price of $153.83 (figure 3). For those interested in 700-800 pound steers with a January delivery date the range was from $122 to $130 per cwt and at a weighted-average price of $129.29 per cwt.

If the forward bids are at or lower than levels implied by the futures market, consider hedging with futures or options. If you expect the price to rise and can manage the risk, then waiting may be the best choice for now. If prices rise or hold steady then price risk management will likely cost more than what it is worth. However, if prices decline then there could be several dollars never captured due to the price decline.
No single retained ownership decision or pricing strategy will be right for all producers. Also, consider tax ramifications when selling cattle in the following tax year. The best strategy for any one producer will also likely vary year by year. Over this next year, the general level of calf prices is likely to be closer to many producers’ breakeven prices than we have seen in recent years. Tight margins make it critical for producers to examine several alternatives and select the one that will yield the best return for them. As market conditions change over the next several months prior to weaning and marketing calves, the best strategy may change several times. Producers are encouraged to begin evaluating cattle marketing strategies earlier rather than later.

Lee Schulz

Searching for a Price Bottom

As we enter September, the markets have absorbed record projections for supply and demand, from both private industry and USDA, a good amount of crop moving at the end of the marketing year to clear out bin space, and a relatively benign finish to the summer. That combination of factors took corn prices to new lows and cut the prospects for soybean prices. Whether these prices will be the lows for the harvest season depends on potential production in the U.S. and the willingness of international markets to dive into the crop markets this fall.

With the August reports, USDA released its first field-based estimates for the 2016 crops. When the enumerators were out in the fields around Aug. 1, their focus was on plant populations, as the crops were not far enough along to assess much about the ears or pods themselves. But those plant population counts, in
combination with the yield estimates from farmer surveys, resulted in projected record yields and production for both corn and soybeans.

Figure 1 displays the projections for corn. States shaded in blue are projected to have higher yields than last year. States shaded in red are projection to have lower yields. As the map shows, the core of the Corn Belt is expected to have higher yields, while the states surrounding the core are expected a few bushels less. Overall, the national corn yield estimate is 175.1 bushels per acre, which is 6.7 bushels higher than last year and 4.1 bushels higher than the record from 2014. With over 94 million acres planted to corn, that yield translates to 15.15 billion bushels of corn nationwide. That would top the previous record harvest by over 800 million bushels.

Some of the private industry estimates (for example, Informa and FCStone) have reached roughly the same numbers for the corn crop. But there has been some discussion in farm country that the corn yield and production numbers may work their way down from these lofty projections. As part of the August release, USDA also provided some of the background data behind the yield estimates. Figure 2 contains that data. As it shows, ear counts for this year’s crop are below the levels for the past couple of years. But the implied ear weight is set at record level. As I mentioned earlier, the August observations are limited to plant counts as the crops are not mature enough for any ear measures. The implied ear weight incorporates the information from the farmer surveys. And what the implied ear weight shows is that farmers estimated big yields.

Going forward, I expect that the ear weight will retreat from this projected record. There have been a number of reports of tip-back issues as producers entered the fields over the last couple of weeks. And as the enumerators reenter fields over the Labor Day weekend, those issues will eventually show up in the USDA estimates. However, a record corn crop is likely. Given where we stand currently, even if the corn yield retreated 10 bushels to 165 bushels per acre, production would still exceed the 2014 record.
A very similar tale can be told for the soybean crop. August estimates show record yields and production. The core producing areas are set for higher yields, while more marginal areas are experiencing a slight pullback. With the national soybean yield projection at 48.9 bushels per acre, soybean production would exceed 4 billion bushels for the 1st time. But late August observations show some issues with the crop are emerging. The relatively cooler and wetter August has sparked some incidents of sudden death syndrome. But again, as with corn, the national yield estimate could fall by over a bushel and a half and we would still have record production.

Figure 3. Soybean yield projections (Source: USDA-NASS).
Luckily, the yields and production were not the records being projected. Crop usage continues to build to record levels as well. The growth across the livestock sector continues to spur feed demand. USDA’s projection for feed and residual usage is 475 million bushels higher for 2016 crop. Corn exports are expected to continue their march higher as well, adding another 150 million bushels compared to last year. And the ethanol industry’s use of corn is expected to jump another 75 million bushels. As Figure 4 shows, corn usage for ethanol has been at or near record levels over the past few weeks. A little strength in the oil market and the low corn prices have supported ethanol margins recently.

**Figure 4. Corn usage for ethanol production.**

For soybeans, usage is up across the board as well. Domestic crush use is projected to be 40 million bushels higher with the growth in the livestock sector (and the associated need for soybean meal) and another solid year of biodiesel production. But the largest increase in usage is expected in the export market. Current projections have exports increasing another 70 million bushels, to a record 1.95 billion bushels. And as figure 5 indicates, advance soybean export sales are moving along at a fairly brisk pace, slightly behind the pace set in 2014, but ahead of last year.

So the record usage is limiting stock build-up, but stocks are projected to increase. And season-average prices for the 2016 crops remain well below estimated production costs for both crops. USDA’s current price estimates have corn prices in the $3.15 per bushel range, while soybean prices are set around $9.10 per bushel. Futures prices, going into the Labor Day weekend, indicated season-average prices slightly below those estimates. And looking forward to the 2017 crops, the margin picture will likely remain troublesome. While the corn market is showing some carry between the crop years, soybean futures have taken another step down for the 2017 crop. Current futures point to 2017 season-average prices of $3.50 per bushel for corn and $8.80 per bushel for soybeans. And as figure 6 shows, those prices would put 2017 crop margins $75 per acre below production costs.
So the challenge for farmers this fall is the same one they faced for the previous two falls, bringing in record crops, while searching for better prices. And like with the last two years, producers may have to wait until late in the spring for those better pricing opportunities. But with usage still growing, any cuts in production, whether in our harvest or from South America’s next crops, could spur some upward price movement.
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