

WESTERN CORNBELT LEAN HOG BASIS, 1996-2000*

FOR THE 51-52% LEAN CARCASS CONTRACT (Dollars/cwt)

Market Period	Contract For Basis	Five Year Basis Low	More Negative 15% of Time	Expected Basis	More Positive 15% of Time	Five Year Basis High
Jan- 1st half	February	-9.22	-7.48	-4.73	-1.99	3.33
Jan- 2nd half	February	-6.37	-4.77	-2.40	-0.03	2.76
Feb- 1st half	February	-5.84	-3.73	-1.88	-0.03	1.55
Feb- 2nd half	April	-8.29	-5.39	-2.83	-0.28	1.09
Mar- 1st half	April	-8.27	-5.23	-2.57	0.10	1.10
Mar- 2nd half	April	-9.34	-5.17	-2.82	-0.46	1.60
Apr-1st half	April	-6.30	-4.09	-1.98	0.14	3.52
Apr- 2nd half	June	-15.12	-12.70	-8.88	-5.07	8.89
May-1st half	June	-10.56	-8.47	-5.73	-2.99	0.80
May- 2nd half	June	-8.01	-5.19	-2.17	0.85	4.07
Jun- 1st half	June	-7.23	-4.98	-2.76	-0.54	0.28
Jun- 2nd half	July	-4.85	-3.07	-1.31	0.45	3.79
Jul- 1st half	July	-4.20	-3.09	-1.54	0.02	2.60
Jul- 2nd half	August	-5.61	-1.98	0.70	3.39	5.43
Aug- 1st half	August	-4.36	-2.61	-0.86	0.90	7.20
Aug- 2nd half	October	-2.87	3.78	6.59	9.39	12.33
Sep- 1st half	October	-1.18	-0.05	1.89	3.82	6.03
Sep- 2nd half	October	-1.76	-0.61	1.27	3.15	5.88
Oct- 1st half	October	-3.92	-1.75	0.11	1.97	3.48
Oct- 2nd half	December	-7.53	-3.21	-0.20	2.81	5.25
Nov- 1st half	December	-10.83	-7.14	-3.48	0.19	3.08
Nov- 2nd half	December	-9.30	-6.30	-3.47	-0.64	2.43
Dec- 1st half	December	-7.32	-4.71	-2.73	-0.75	2.33
Dec- 2nd half	February	-14.02	-10.79	-6.62	-2.45	2.57

* Western cornbelt lean hog basis for the first half of January through the first half of August is calculated as a 5 year average of prices from January 1996 through the first half of August 2000. The second half of August through the second half of December is calculated as a 5 year average of prices from August 1995 through the second half of December 1999.

- 1/ Basis is calculated as Cash-Futures. A negative sign means that futures are greater than cash.
- 2/ Market periods were divided as follows: 1st half includes the first 10 trading days of the month, 2nd half includes all remaining days in the month.
- 3/ 1995-1996 futures prices were converted from a live to a lean value by dividing the CME price by 0.74 and adding the difference between the Iowa-Southern Minnesota 51-52% lean carcass and the 47-48% lean carcass cash values.
- 4/ Values for the more negative 15% and more positive 15% columns are figured as one standard deviation from the expected basis. Basis is expected to be outside of these values approximately 15% of the time.

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Hedging Example Using New Lean Hog Futures

Assume the February Lean Hog futures contract is trading at \$54.50 and you have 420 hogs to be marketed in the first two weeks of February.

I. Determine the Western Cornbelt lean price using the historic basis. Compare this price to cost of production and price objectives.

A. Add the Lean Hog Basis to futures price to arrive at the Western Cornbelt reported lean carcass price for early February (See Basis Table).

$$\$54.50 + (-1.88) = \$52.62/\text{cwt carcass weight.}$$

B. Add net premium (lean premium + sort loss) you typically receive compared to the Western Cornbelt reported lean price to arrive at your expected net lean price.

C. Multiply by your typical dressing percent to estimate live price

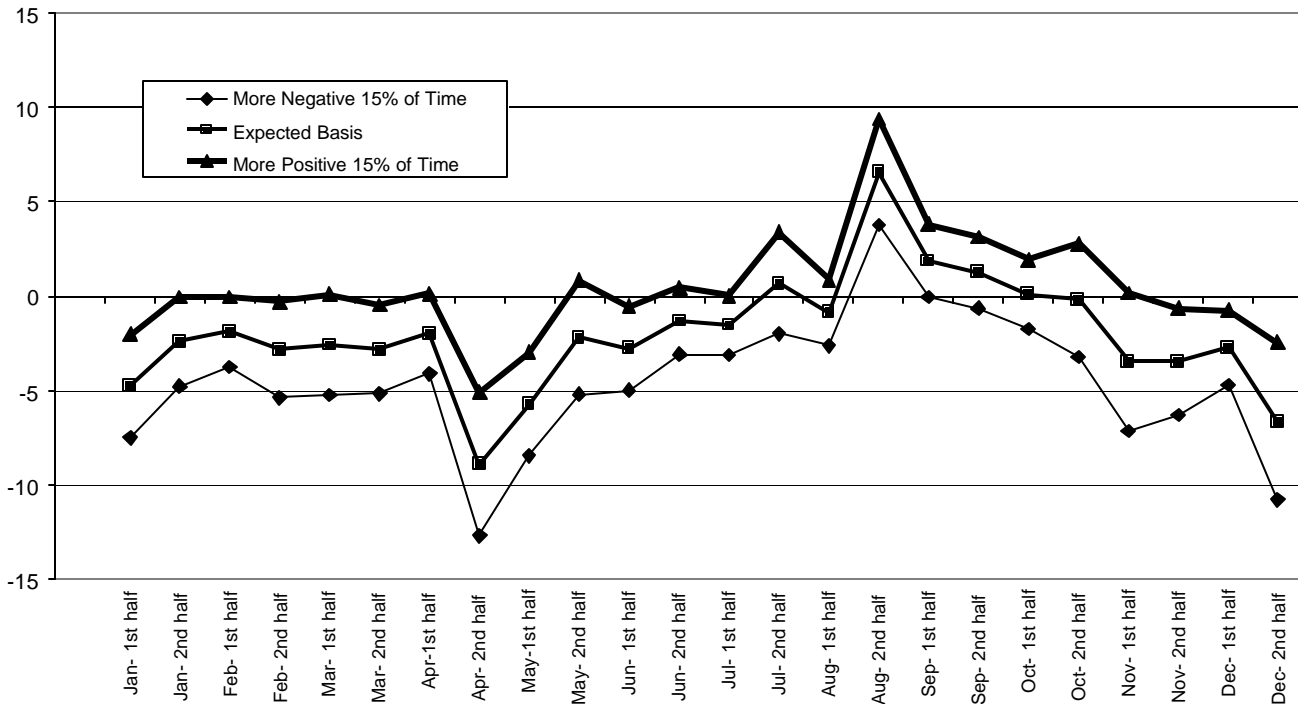
$$(\$52.62 \text{ net} + 1.50 \text{ premium}) * 0.7425 = \$40.18 \text{ cwt live}$$

II. Determine how many Lean Hog contracts you need to hedge your production.

Example: Number of hogs (420) x Average market weight (260) x Expected dressing percent (74.25)

$$420 \times 260 \times 74.25\% = 81,081 \text{ carcass pounds} = \text{approximately two } 40,000 \text{ lb. contracts}$$

5 Year Average Basis and One Standard Deviation



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