Fed Cattle Pricing Mechanics

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Objectives

Discuss packer pricing of fed cattle
↗Live weight bids
↗Dressed weight or "in the beef" bids
↗Basis forward contract bids

General Pricing Process

Meatpackers estimate meat and byproduct sales, subtract slaughter-processing costs and a profit target, and what remains is how much they can pay for fed cattle.

Packer Pricing of Fed Cattle: a Two-Stage Process

- A head buyer determines a daily buy order
- Field buyers execute the buy order as they purchase cattle from feedlots

More Specifically -

Packers begin with a basic profit equation:

(1) Profit = Total Revenue - Total Costs

This can be shown as:

(2) Profit/head = [(Price of Meat x Quantity of Meat) + (Price of Byproducts x Quantity of Byproducts)] - [(Price of Livestock x Quantity of Livestock) + Costs of Slaughtering/Fabricating]

Packers Rearrange the Profit Equation into a Bid Price Equation

(3) Bid Price of Fed Cattle = [(Price of Boxed Beef x Quantity of Boxed Beef) + (Price of Byproducts x Quantity of Byproducts)] - [Cost of Slaughtering/Fabricating - Profit Target] / Quantity of Fed Cattle

Live Weight Price Bid Example

Cattle Weight		**1200 lbs.**
STEP 1: Compute Adjusted Boxed Beef Price		
"Projected" Boxed Beef Price (Ch 1-3, 700-850)		**$110.00**
Less Discounts:		
% Select x $ Discount	**(50% x $5)**	**-$2.50**
% YG4-5 x $ Discount	**(10% x $10)**	**-$1.00**
% Light/Heavy x $ Discount	**(10% x $15)**	**-$1.50**

Live Weight Price Bid Example

Sum for Adjusted Boxed Beef Price		**$105.00**
STEP 2: Convert Boxed Beef Price to Liveweight		
Adjusted Price x Dress %	**($105.00 x 63.5%)**	**$66.68**
STEP 3: Add Byproducts Value		
Step 2 + $8.40/liveweight cwt.	**($66.68 + $8.40)**	**$75.08**
STEP 4: Subtract Processing Costs Plus Profit Target		
$75.00/Head Cost (Slaughtering - Processing)		
+ $10.00/Head Profit Target		
= $85.00/Head 12.0 cwts	**($75.08 - $7.08)**	
Bid Price		**$68.00/cwt.**

Dressed or Carcass Weight "in the beef" Bid Example

Cattle Weight		**1200 lbs.**
STEP 1: Compute Adjusted Boxed Beef Price		
"Projected" Boxed Beef Price (Ch 1-3, 700-850)		**$110.00**
Less Discounts:		
% Select x $ Discount	**(50% x $5)**	**-$2.50**
% YG4-5 x $ Discount	**(10% x $10)**	**-$1.00**
% Light/Heavy x $ Discount	**(10% x $15)**	**-$1.50**

Dressed or Carcass Weight "in the beef" Bid Example

Sum for Adjusted Boxed Beef Price		**$105.00**
STEP 2: Add Byproducts Value (on a dressed weight basis)		
Step 1 + $8.40 / .635 dressing %	**($105.00 + $13.23)**	**$118.23**
STEP 3: Subtract Cost Plus Profit Target (on a dressed weight basis)		
$75.00/Head Cost (Slaughtering - Processing) + $10.00/Head Profit Target = $85.00/Head / 7.62 cwts	**($118.23 - $11.15)**	**$107.08**
Bid Price		**$107.08/carcass cwt.**

Basis Forward Contract Bid Example

"Expected" Cattle Weight (October)		**1200 lbs.**
ASSUME AVERAGE QUALITY CATTLE		
STEP 1: Estimate an October Basis		
"Estimated" Average October Basis		**-$0.55**
STEP 2: Subtract a Risk Transfer Premium		
Step 1 - $1.00		**-$1.55**
Basis Bid (from October Live Cattle Futures)		**-$1.55/cwt.**
STEP 3: Feeder Picks the Live Cattle Futures Price		
"Estimated" Highest October Live Cattle Futures		**$77.00**
Sale Price ($77.00 - $1.55)		**$75.45/cwt.**

Conclusions

- Often we hear that the best offense is a good defense
- Marketing means understanding your customer and his/her business
- Therefore, cattle feeders must understand how packers' price cattle
- The pricing process, while simplified here, is basically a straight-forward process