CPM Group

Market Commentary

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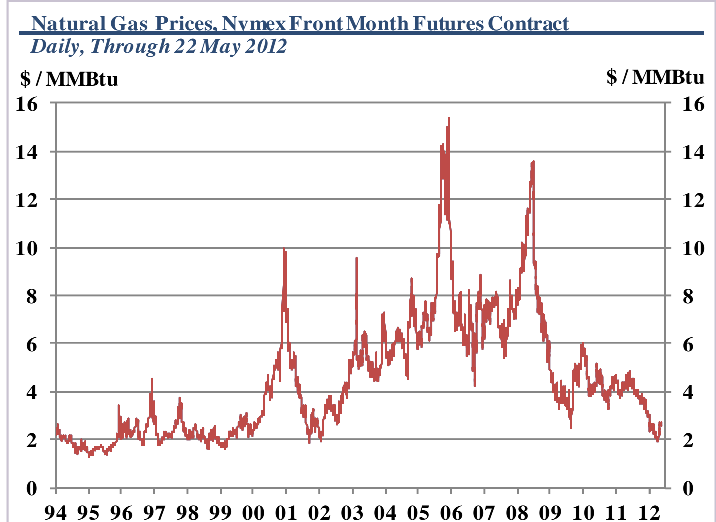
How Manufacturers Can Hedge Their Natural Gas Input Costs

Natural gas prices recently have fallen to their lowest levels since the 1990s. This has provided manufacturers that use natural gas in their factories an opportunity to lock in the lowest prices in more than a decade. Indeed, one of the major forces behind the rise in natural gas prices from around $2.00 to $2.70 over the past three weeks has been consumer hedging, along with CTA short covering.

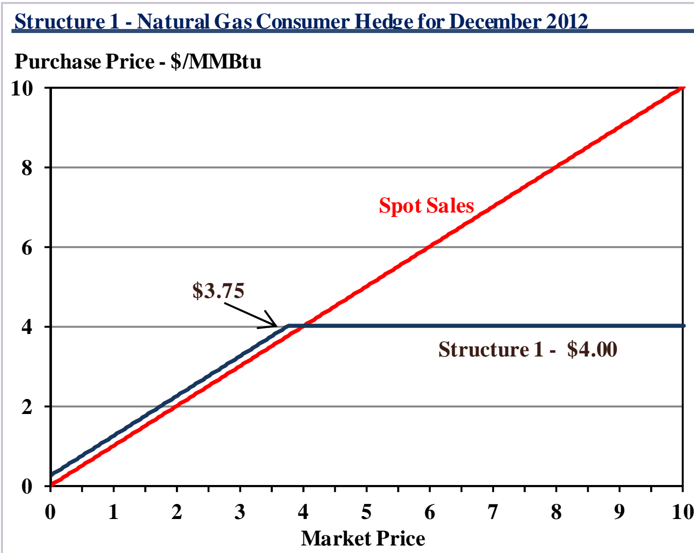
CPM Group structures, prices, places, and manages these hedges for its customers, often using CME options. Our preferred hedges provide consumers with a ceiling or maximum price they will pay for natural gas during the life of the hedge. There is no outlay of an initial premium. If prices are below the ceiling the consumer pays a price slightly above the market price, but the maximum marked to market variance is minimized using CPM Group's strategy and pre-determined before the hedge is put in place. There are no unpleasant surprises. CPM Group is not a broker, but works as an advisor for its clients.

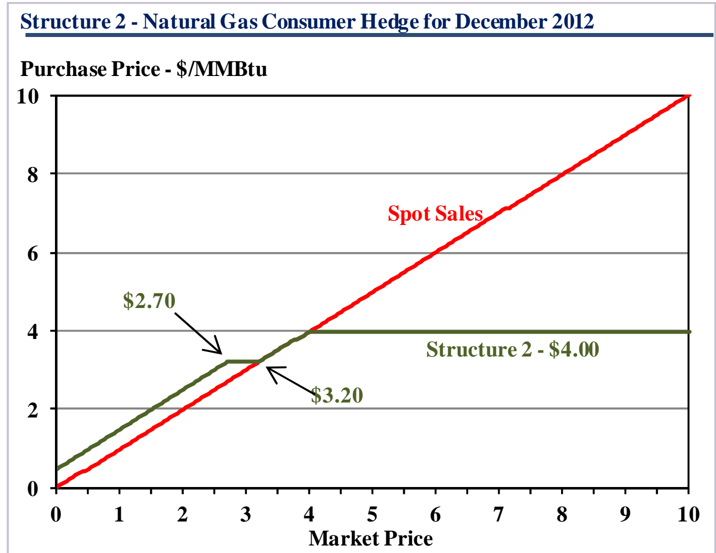
Two examples are shown here, each showing a hedge for December 2012. Longer dated hedges are possible. In the first hedge a consumer of natural gas can lock in $4.00 natural gas. If prices are above $4.00, as they have been for 72.5% of the time since January 2000, the consumer pays $4.00. If prices are below that, the consumer pays the market price plus 25 cents. If prices stayed at $2.75, the consumer would pay $3.00. If prices rose to $5.00, the consumer would pay $4.00.



In the second hedge the consumer locks in a ceiling on its natural gas purchase price of $4.00. Between $3.20 and $4.00 the consumer pays the market price, and below $2.70 the consumer pays the market price plus 50 cents.

Companies interested in using CPM Group to hedge their natural gas consumption should contact Matt Taub at 1-212-785-8320, or mtaub@cpmgroup.com





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