

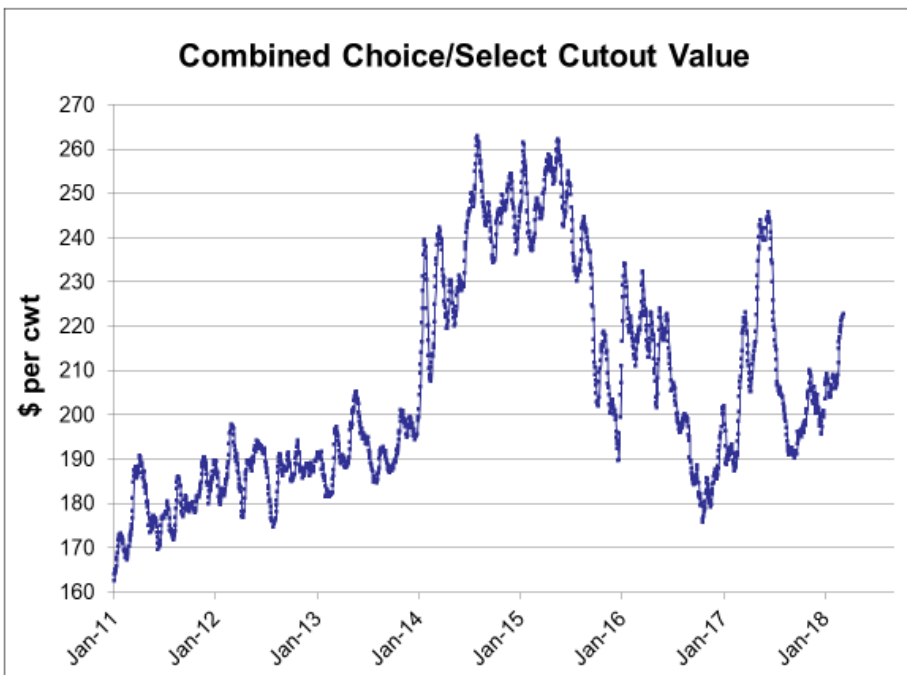


MEAT MARKETS *UNDER A MICROSCOPE*

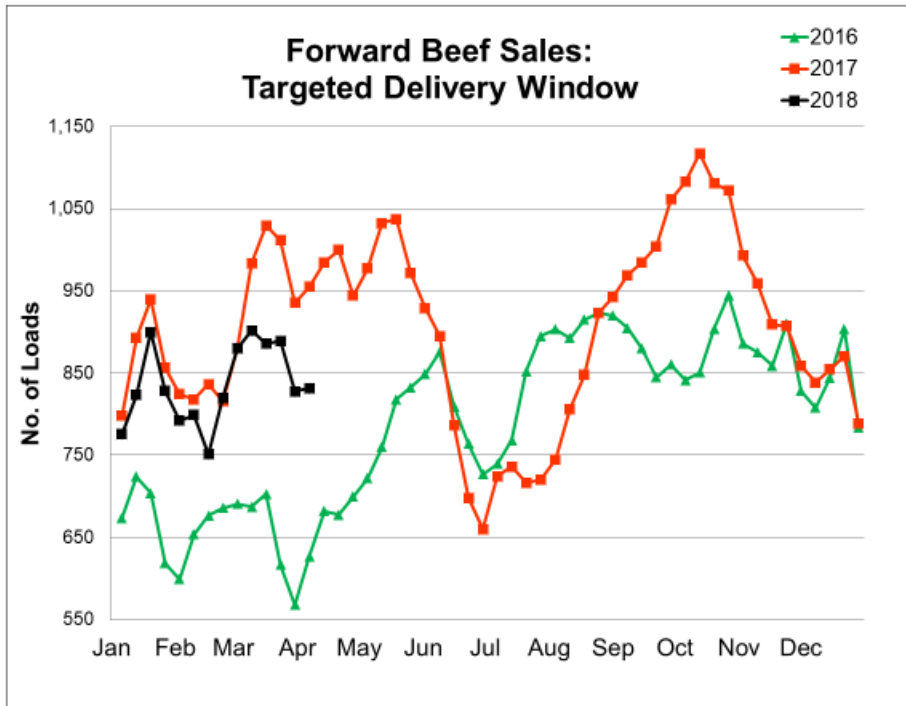
A perspective on the red meat markets by Kevin Bost...sometimes wrong, usually scientific, but always candid

March 10, 2018

The general consensus seems to be that the combined Choice/Select cutout value is topping out right about now, and with that notion I cannot disagree. First, I consider that it has reached a meaningful resistance level on the chart, this being the price that turned back rallies in March 2017 and before that, in June 2016.... and prior to that, it was an important area of support in April/May 2014. Should this resistance level give way, the next would be in the neighborhood of \$235 per cwt (\$12 above the current quote), which could be achieved in June *if* demand surges as it did last year at that time. Second, I notice that forward bookings for delivery between now and the first week of April are unimpressive, as I show in the picture at the top of the next page. These are only rough approximations, but they do indicate that packers will have a fair amount of meat to sell into the spot market over the next four weeks—not really conducive to higher prices. As for the seasonal track record, the beef market does not exhibit a bias in either direction during the three-week period leading up to Easter; but I notice that it has gained ground significantly in only four of the last 12 years.



There is another, more nebulous observation that may be relevant. This time around, the seasonal increase in cutout values is a bit more “long in the tooth” than it normally is by the first week of March. It has been four weeks since the combined cutout made its most recent low. In the past 15 years, only three times has the rally been four weeks old by the first week of March (2012, 2010, and 2008).



Perhaps more significantly, there was no meaningful setback during February this year. The combined cutout averaged 2.9% higher in February than in January. This has happened only four times in the last 15 years: 2012 (+2.8%); 2011 (+0.5%); 2010 (+0.9%) As usual for this time of year, the middle meats have led the way on the recent rally in cutout values.

There two years in

which the cutout value has endured no meaningful decline in February *and* in which the late-winter rally has been this far along by the first week of March were 2010 and 2012. What happened subsequently in these two years? Well, in 2010 the cutout value gained another \$11 per cwt by the end of March; in 2012, it lost another \$11 by the end of March. Oh well. I have not bothered to investigate what else was going on in 2010 that brought about such a strong performance during March. But intuitively, it still makes sense that these conditions would heighten the chances of a setback.... does it not?

OK, so among the “strong arms” in the beef market are the strips. How much more upside potential do they have in the near term? I’ll take a guess. The average price of Choice 0x1 strips in the first week of March (this past week) was the second highest on record for this point on the calendar and \$.35 per pound higher than a year ago. This would seem to be a limiting factor. However, the initial early-spring peak last year was \$8.09 per pound (March 20). I’m not going to bet against that happening again this time around. Similarly, 0x1 short loins are still almost \$1.50 per pound below their March 2017 peak, and these are much more moderately priced for this time of year from an historical perspective. Select-grade strips and short loins also appear to have a fair amount of upside potential. Select 0x1 strips are trading about \$.45 per pound below a year ago and are \$1.75 below their March 2017 peak; however, there is a formidable resistance level about \$1.00 above the current market, at \$6.50. Select 0x1 short loins are \$1.50 below their March 2017 peak, although their *practical* peak was \$6.50 (They spent only two days above that level).

In the case of Choice boneless ribeyes, meanwhile, the near-term upside potential seems more restricted. They are already priced \$1.25 higher than a year ago and are nearly matching their all-time high for this date. There is a prominent resistance level on the chart around \$8.75, \$.85 above the current quote. Select-grade ribeyes have not traded above \$7.50 per pound in more than two years, and Friday’s quote stood at \$7.35.... enough said.

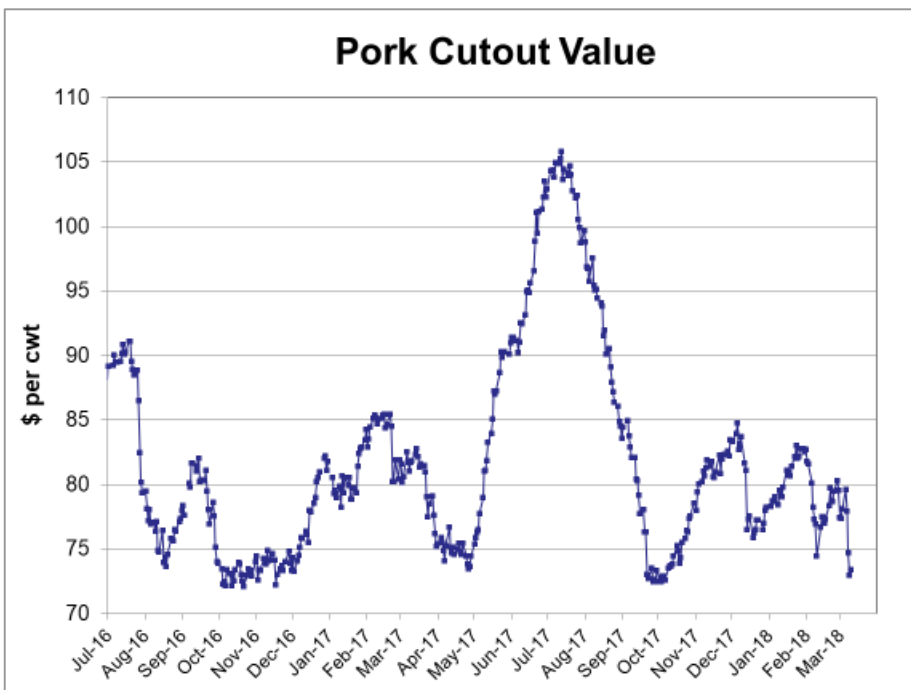
Select top butts made it up to \$4.00 per pound in early spring 2017 and 2016, and I don't know why they could not repeat that performance again this year; the same goes for Choice top butts. Both of these markets have been marking time in the \$3.50 area since the first of the year, so there have been no recent price shocks that would frighten away buyers.

OK, so let's summarize. The pre-Easter upside potential among the major middle meats appears to be something like this:

| | |
|-------------------------|-----------|
| Choice 0x1 strips | \$1.50/lb |
| Choice 0x1 short loins | \$1.50 |
| Select 0x1 strips | \$1.00 |
| Select 0x1 short loins | \$1.00 |
| Choice boneless ribeyes | \$.85 |
| Select boneless ribeyes | \$.15 |
| Choice top butts | \$.50 |
| Select top butts | \$.50 |

If all of this potential is realized, then chucks, rounds, and briskets will have to lose an average of about \$.25 per pound by then in order to hold the combined cutout value steady. Obviously, I think that can be accomplished. But it makes me think that we should not expect a material downturn in the cutout for at least another couple of weeks...

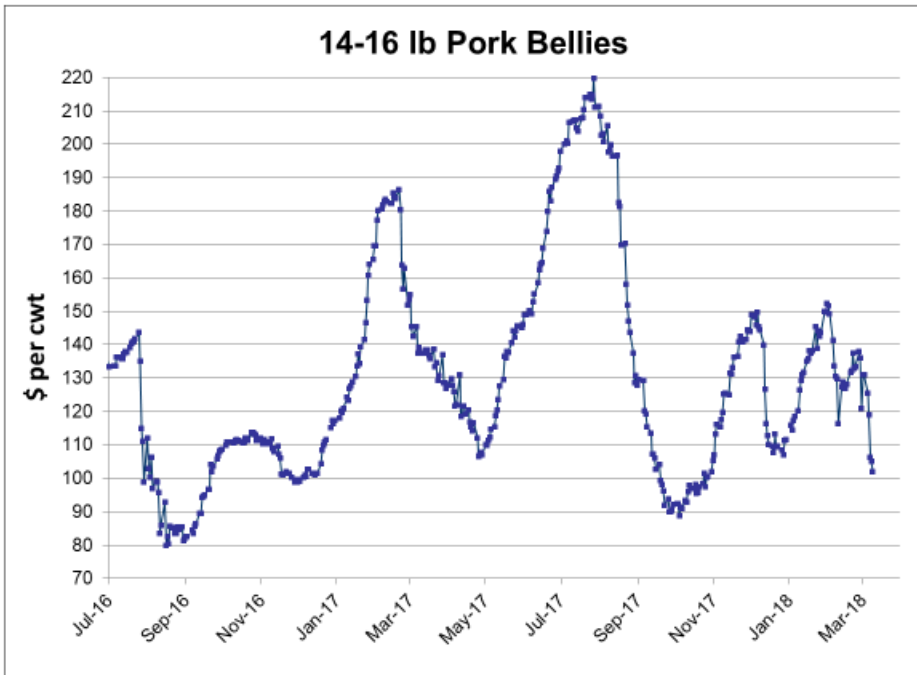
The pork belly market has fully “rebooted”, and therefore the pork cutout value has done likewise. I think this term best describes the sudden, sharp drop that we saw this past week, because it was not the beginning of a protracted decline. In fact, there is a good chance that the cutout value is on bottom right now.



The notion of a bottom in the cutout value right about here is supported not only by the picture at left, by the likelihood that the pork belly market has *probably* gone as low as it needs to go in order to keep supply and demand in balance through the spring. But prices will have to remain subdued for several weeks in order to generate enough forward bacon sales to

allow prices to appreciate normally into the summer. In the meantime, the flow of fresh bellies into the freezer will, no doubt, accelerate at these price levels. It remains my guess that frozen

belly stocks will increase by about 20 million pounds between February 1 and May 1 this year, leaving the May peak at 65 million vs. 34 million a year earlier.



Ham prices also fell backward significantly this past week, and I am reading this as faint but valid evidence that there may not be any extraordinary overseas shipments to be made in April and May.... and that therefore, the ham market is headed down to \$.55 per pound by the end of the month. The most vociferous members of the Sewing Circle have

been noticeably quiet on this subject lately. I understand, thanks to a diligent colleague, that pig prices in China have reached four-year lows, and so one has to wonder what the motivation would be for China to come into the U.S. ham market in a big way.

I'm ranking hams at the bottom of the totem pole in terms of price strength over the next three weeks, and bellies just one rank better. In the middle would be spareribs and pork butts, which I do not expect to move at all. In the top three rungs would be loins, trimmings, and boneless picnics—the latter two because they have already shown some “spark” within the past week; and the former because pork loins—especially the kind without a bone in them—are arguably the single best value in the entire Meat World.

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