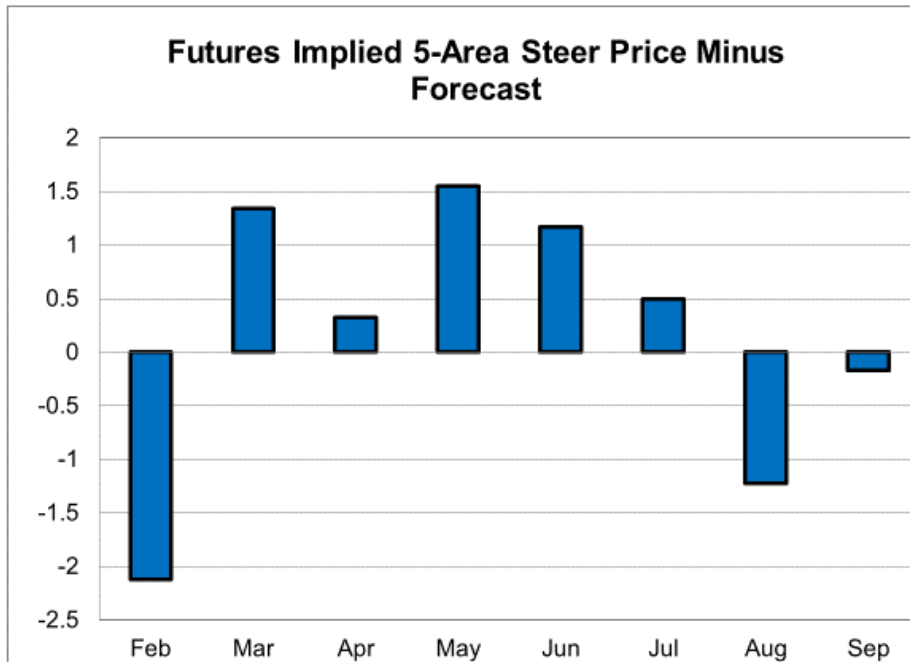


Trading Cattle

.... from a meat market perspective

A commentary by Kevin Bost

January 16, 2018



I do not have any money on the table in the cattle market right now. I have some interest, by virtue of the chart at left, in the long February/short June spread, but there is nothing urgent about the proposition.

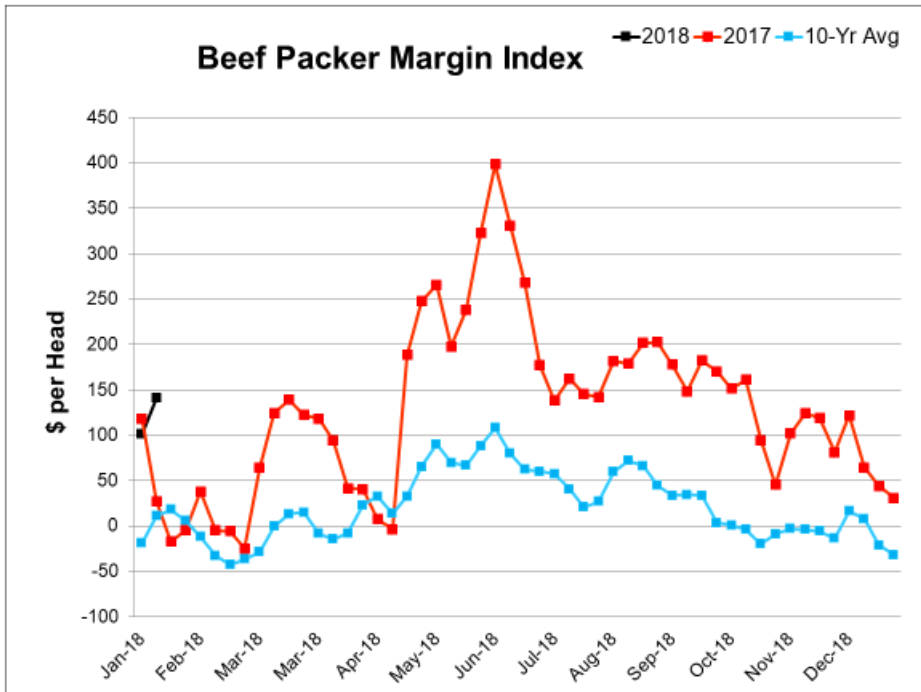
I am willing to wait because of the \$12 per cwt drop in the combined

Choice/Select cutout value which appears to be in the offing over the next three weeks or so. While I expect that most of this decline in product prices will be absorbed via tighter packer margins rather than lower cattle prices, I can't say that I'm supremely confident about that. Being a Meat Guy, it is always difficult for me to hold an outright long or bull spread position when the beef market is losing ground day after day. But if the spot packer margin index falls from this past week's reading of \$140 per head down to \$50 as I anticipate, then a \$195 per cwt *bottom* in the combined cutout value in mid-February (vs. yesterday's quote of \$206.84) would align with a Five Area Weighted Average Steer price of \$118-plus; the cash cattle market would average \$120 during February.

I acknowledge that this spread might actually work better (i.e., the front end gaining on the back) in a downward-moving futures market, since the fund-type selling would be more concentrated in the April and June contracts than in the February contract. However, I also acknowledge that a lower futures market could drag the cash market downward (yes, this really happens!) and nullify one of the main underpinnings of the spread. Anyway, I prefer to enter the February/April spread after the presumed drop in the cutout value is well underway.

Finally, the spread chart has not issued a convincing signal that it is ready to mover higher just yet. For the past four days it has been attempting to build a base around \$6.00 per cwt (premium to the February contract), but a bottom has yet to be confirmed. Until it *is* (confirmed, that is), I have to think that an entry point just above \$5.00 could be "in the cards". That would make for a considerably better risk: reward proposition, since my objective would be a February premium of

\$8.50. That target seems quite realistic; it traded there as recently as December 29, and it is pretty conservative in the sense that in each of the last four years, the February premium has stood at \$10 or more in the middle of February.



Otherwise, I don't see much in the way of opportunity in this market. An outright long position in February cattle—or a short position in February \$114 puts are still possibilities, but only if there is another leg down. The market did not fall precipitously

following its close below \$117.57 last Monday, as I thought it might, but then again, it has not done anything of much consequence to indicate that it is finished going down. For the reasons already mentioned—the impending downturn in the beef market—I can certainly afford to wait for this door to open. If it does not, then so be it.

Forecasts:

	Jan*	Feb	Mar	Apr	May*	Jun
Avg Weekly Cattle Sltr	601,000	590,000	602,000	608,000	632,000	646,000
Year Ago	576,100	581,400	596,800	599,600	606,400	637,900
Avg Weekly Steer & Heifer Sltr	473,000	468,000	481,000	487,000	511,000	526,000
Year Ago	456,000	458,000	476,500	481,100	490,600	514,200
Avg Weekly Cow Sltr	117,000	112,000	111,000	110,000	109,000	108,000
Year Ago	111,900	114,000	110,200	107,700	104,600	111,000
Steer Carcass Weights	900	893	885	870	863	876
Year Ago	894.0	881.3	871.8	849.0	837.8	854
Avg Weekly Beef Prodn	501	490	498	496	511	530
Year Ago	474.8	475.6	485.5	478.6	477.6	509.6
Avg Cutout Value	\$205.50	\$198.00	\$207.50	\$206.50	\$211.00	\$209.50
Year Ago	\$192.21	\$190.41	\$213.29	\$208.39	\$232.95	\$232.42

5-Area Steers	\$120.75	\$120.00	\$123.00	\$122.00	\$118.50	\$113.00
Year Ago	\$119.90	\$120.62	\$127.39	\$130.04	\$136.78	\$126.59

**Includes holiday-shortened weeks*

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