

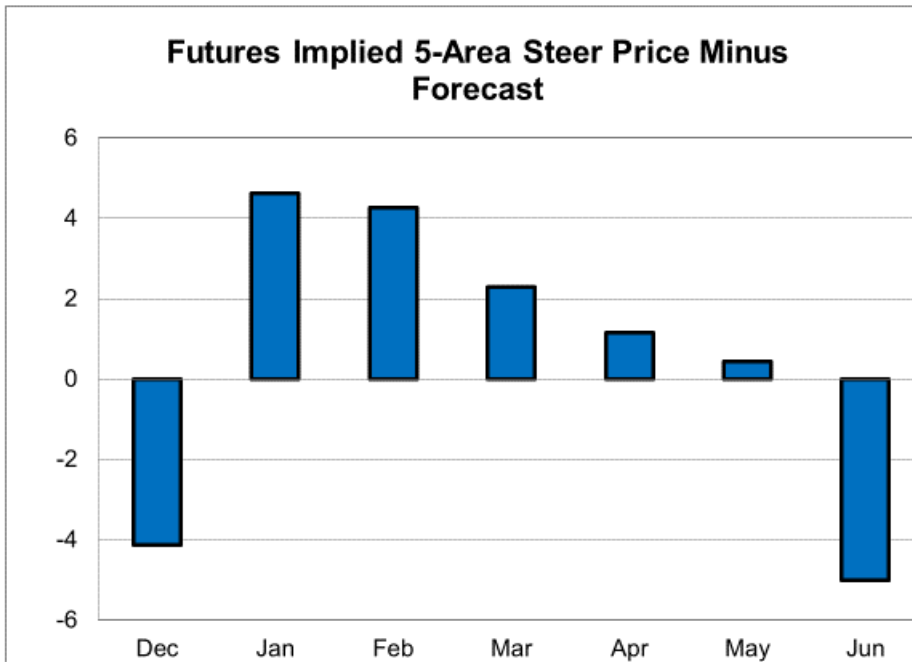
# Trading Cattle

## .... from a meat market perspective

A commentary by Kevin Bost

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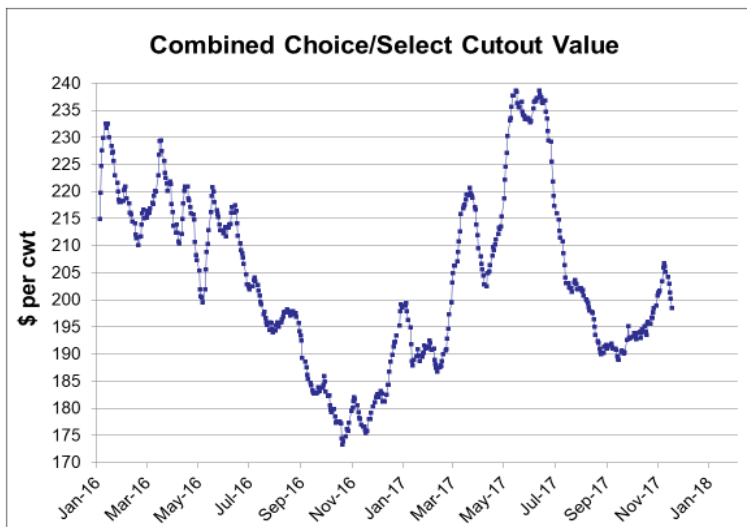
November 20, 2017



I currently hold minimal positions in both the long side of the December contract and the long December / short February spread.

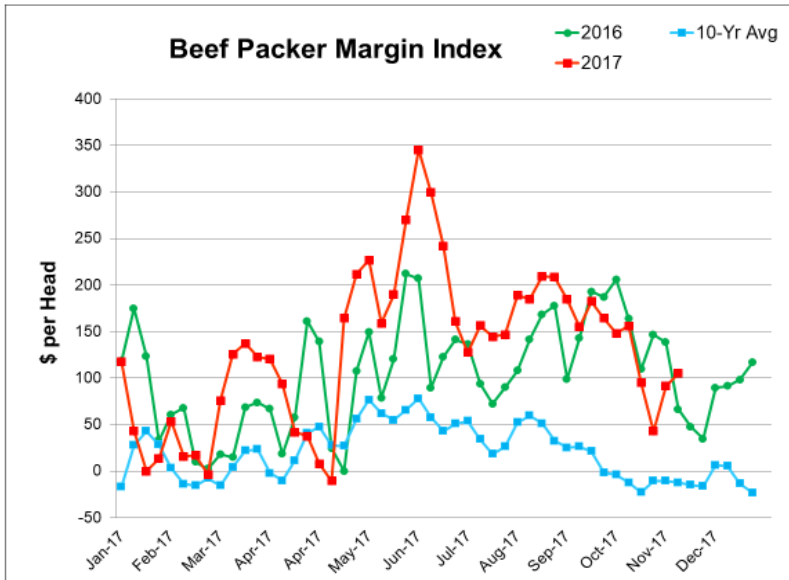
The upside potential in the December contract may not be great, but as objectively as I can discern, it should ultimately be

worth somewhere in the low \$120's per cwt. This humble opinion is grounded in the notion that the combined Choice/Select cutout value will claw its way back to about \$202 per cwt by the middle of December—up from Friday's quote of \$198.50—and that spot packer margins at the same time will be roughly \$25 per head narrower than they are now.



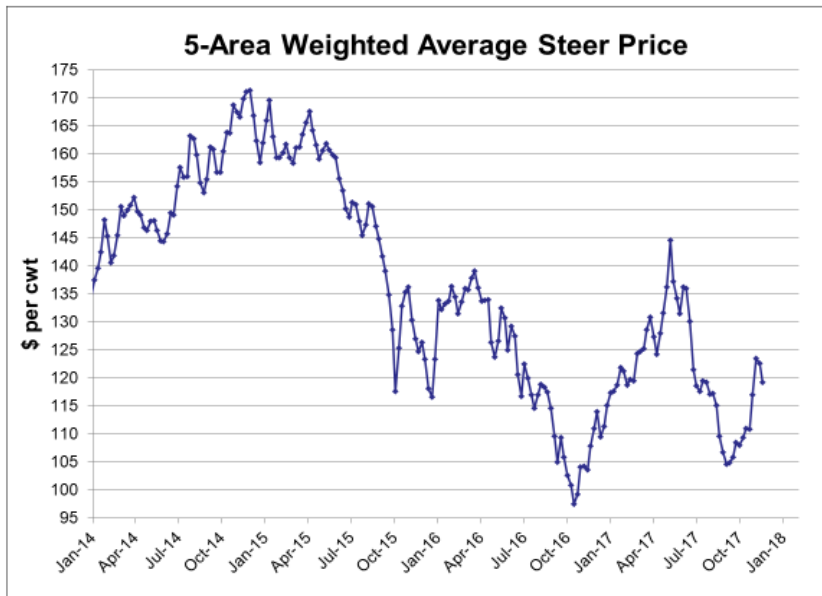
In regard to the cutout value, my basic assumptions are that weekly steer and heifer kills will be running near 485,000 after Thanksgiving (vs. 505,000 this past week), and that wholesale beef demand will trace a typical seasonal path through the balance of the year. Both are what I would describe as "middle-of-the-road" assumptions, with more bullish and bearish projections lying equidistant

from the center of the probability curve. A rather extreme bearish possibility would be a cutout of \$198.50 in the middle of December, precisely where stands today. That, of course, would require a significantly higher rate of production than suggested by the inventory of cattle on feed 90 days or longer and/or a significantly weaker-than-normal change in demand.



As for the spot packer margin, which is always a moving target, front-end cattle supplies are current enough to swing bargaining power over to the cattle feeder....as has been demonstrated in the past four weeks. Regrettably, though, sometimes the board can dictate the cash market instead of the other way around. In any case, this past week might have been the packer's best chance to push cash cattle prices downward until the next round of

holidays....which they did, of course, bringing the Five Area Weighted Average Steer prices back down to what was formerly a major resistance area, and therefore now seems a likely place for major support:



OK, so what if the spot packer margin does not tighten at all from this point, and the combined cutout value simply stays where it is (or loses some ground in the meantime and then returns to \$198.50 in mid-December)? That combination would result in a Five Area Weighted average price of \$117.50. This I regard as a "practical worst case" scenario for December cattle.

It is difficult to identify a meaningful support level between Friday's close and \$115.50 on the chart, and so any stop-loss point between here and there would have to be somewhat arbitrary. But it doesn't make good sense from a money management standpoint to risk 350 points on a trade in which I can only expect to profit as much. Therefore, I will have to take my clues from the cash market; heavy downward pressure on the beef market and a steady or lower cash cattle trade this week would come as unpleasant surprises.

I am treating the long December / short February spread as a position. This spread could be a winner even in a “down” market—in fact, it may perform more favorably in a down market, because the February contract is presumably more susceptible to a round of long liquidation than the nearby contract. As of last Tuesday, long positions among large speculators accounted for more than 20% of the total “pie”, the largest percentage in almost two and a half years. My objective is somewhere in the neighborhood of \$4.00 per cwt (premium to the February), a level that was traded just two weeks ago.

Finally, because of the picture at the top of the first page, I am somewhat interested in the long December / short February / long June butterfly spread. I am a bit hesitant about this proposition, though, because it is a cousin to the two-legged spread in which I already participate. But if the market affords the opportunity to enter around \$-15.00 per cwt, I will probably take it. It finished Friday at \$-12.85.

Forecasts:

	Nov*	Dec*	Jan*	Feb	Mar	Apr
Avg Weekly Cattle Sltr	620,000	577,000	600,000	586,000	591,000	604,000
Year Ago	604,000	574,900	576,100	581,400	596,800	599,600
Avg Weekly Steer & Heifer Sltr	491,000	457,000	474,000	467,000	472,000	486,000
Year Ago	482,000	459,300	456,000	458,000	476,500	481,100
Avg Weekly Cow Sltr	118,000	112,000	117,000	110,000	108,000	107,000
Year Ago	112,200	107,200	111,900	114,000	110,200	107,700
Steer Carcass Weights	901	895	891	885	877	862
Year Ago	915.6	903.3	894.0	881.3	871.8	849.0
Avg Weekly Beef Prodn	512	475	492	481	481	486
Year Ago	507.4	479.0	474.8	475.6	485.5	478.6
Avg Cutout Value	\$201.00	\$203.00	\$203.50	\$201.50	\$214.50	\$215.00
Year Ago	\$179.30	\$189.19	\$192.21	\$190.41	\$213.29	\$208.39
5-Area Steers	\$120.75	\$122.50	\$121.00	\$121.50	\$126.50	\$126.50
Year Ago	\$108.22	\$113.37	\$119.90	\$120.62	\$127.39	\$130.04

\*Includes holiday-shortened weeks

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