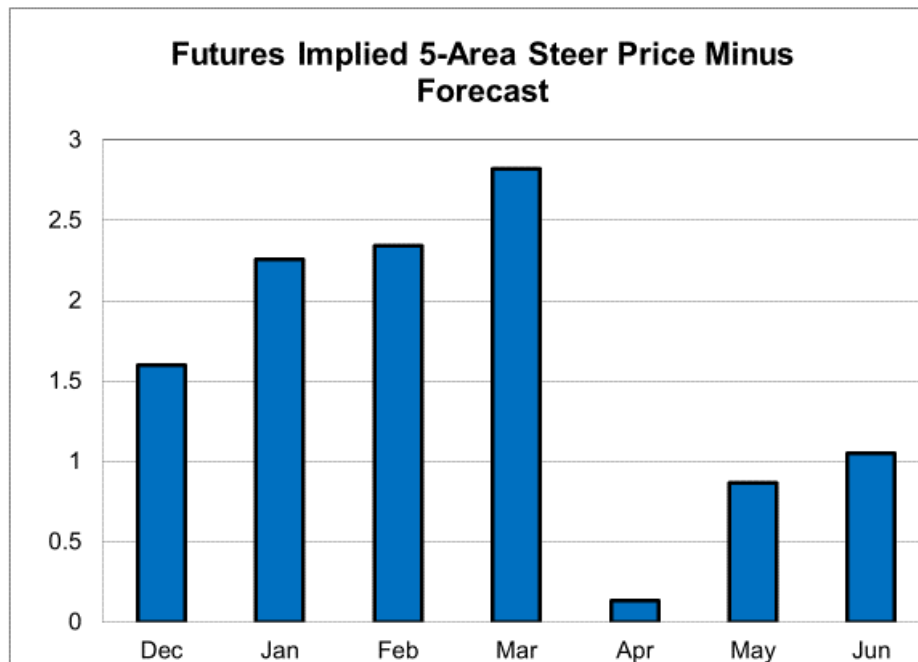


Trading Cattle

.... from a meat market perspective

A commentary by Kevin Bost

December 19, 2017



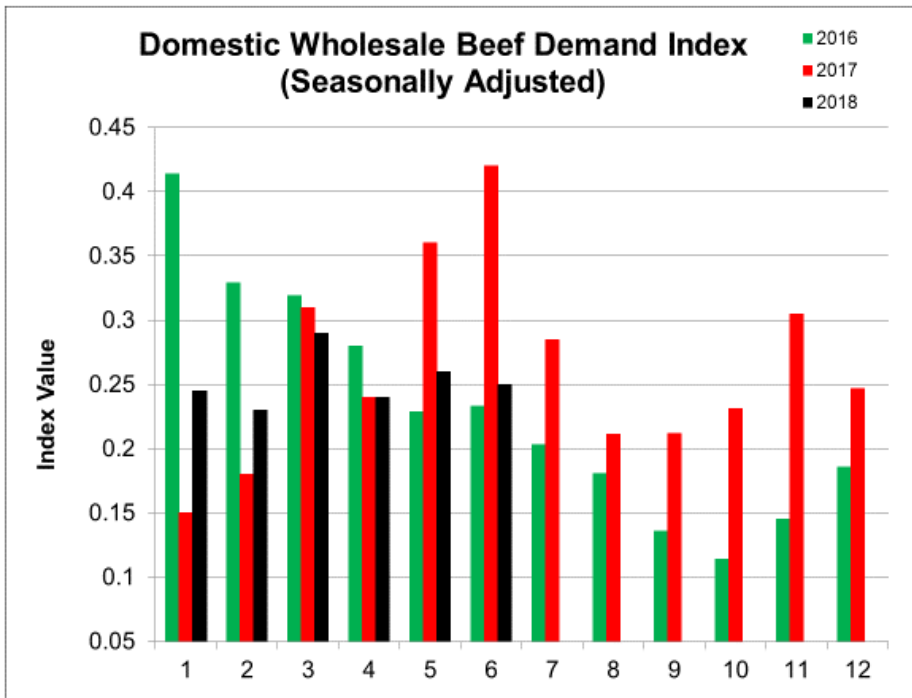
From a purely objective, fundamental standpoint, the cattle market does not offer much of a profit opportunity at the moment. The first three options appear to be fairly priced, or nearly so....within the margin of error, you might say. Mine is pretty wide.

I suspect that the February contract will reach a point at which a short position would be justifiable, but that point is not today. I have two reasons for saying so. One is that the beef market should work its way upward over the next three to four weeks. My guess is that the next peak in the combined Choice/Select cutout value will be about \$8 per cwt above yesterday's quote, but well short of the nearest major resistance level on the chart. But since the presumed upturn is just now getting underway, I don't want to underestimate its potential. The other reason is that the daily chart completed a pretty reliable bottom formation last Friday which, even if this turns out to be just a minor correction, should at least lead to a test of the downtrend line extending from the contract high. Today, that trend line passes through approximately \$123.00. There really isn't any resistance to speak of between here and there. Finally, I also notice that the five-day moving average has crossed above the ten-day MA for the first time in about two weeks.

And so my posture toward the cattle market might be described as "leaning toward the short side but allowing it some room to run".

I am leaning toward the short side mainly because the month of January does not look like it will be a very good one for wholesale beef demand. This notion, in turn, is based on the unimpressive volumes that have been booked for delivery after the first of the year, suggesting that beef will not be actively featured in supermarket ads at that time. There is also the more nebulous suggestion that wholesale beef demand reached a cyclical peak in November, and therefore will be in a downward phase during January, headed into bottom in February.

Since the assumption regarding beef demand (along with packer margins, of course) is particularly critical to the outlook for cattle prices, I'll show you once again those which I am factoring into the pricing equation:



As you can see, I am not making any bold assumptions, perhaps conservatively thinking that after reaching a cyclical bottom, the seasonally adjusted demand index will more or less flatten out through the second quarter. The situation in retail prices and retail margins is

generally supportive of wholesale beef demand, but not nearly as bullish as they were at this time last year. Hence, the expectation that the dramatic increase in May and June 2017 is unlikely to repeat itself this time around. But if it were to do so, then we would be looking at a cash cattle market in the upper \$120's per cwt in June.

As for the supply side, I keep in mind that while marketing rates have been aggressive throughout the fourth quarter, by February we should soon be getting into the heavier placements of September (up 13% from a year earlier). Also not too far in the back of my mind is the question of cattle supplies vs. slaughter capacity—not an issue until laste spring, but possibly a bearish factor to be reflected in packer margins. Last summer, practical slaughter capacity was challenged with steer and heifer slaughter running in the neighborhood of 515,000 per week; I think that front-end cattle supplies indicate a rate of 525,000 in June (and beyond).

And so, as I consider a short-side bet, I will be paying close attention to the more bullish extremes (such as in beef demand); and as I consider a long-side bet, my attention will be focused on the more bearish extremes....

Forecasts:

	Jan*	Feb	Mar	Apr	May*	Jun
Avg Weekly Cattle Sltr	607,000	593,000	600,000	612,000	630,000	647,000
Year Ago	576,100	581,400	596,800	599,600	606,400	637,900
Avg Weekly Steer & Heifer Sltr	478,000	469,000	476,000	488,000	507,000	524,000
Year Ago	456,000	458,000	476,500	481,100	490,600	514,200
Avg Weekly Cow Sltr	120,000	115,000	114,000	113,000	112,000	111,000
Year Ago	111,900	114,000	110,200	107,700	104,600	111,000
Steer Carcass Weights	893	887	879	864	857	870
Year Ago	894.0	881.3	871.8	849.0	837.8	854
Avg Weekly Beef Prodn	500	488	491	494	504	525
Year Ago	474.8	475.6	485.5	478.6	477.6	509.6
Avg Cutout Value	\$199.00	\$193.50	\$209.00	\$208.00	\$211.00	\$209.50
Year Ago	\$192.21	\$190.41	\$213.29	\$208.39	\$232.95	\$232.42
5-Area Steers	\$118.50	\$118.50	\$123.00	\$124.50	\$121.50	\$115.00
Year Ago	\$119.90	\$120.62	\$127.39	\$130.04	\$136.78	\$126.59

**Includes holiday-shortened weeks*

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