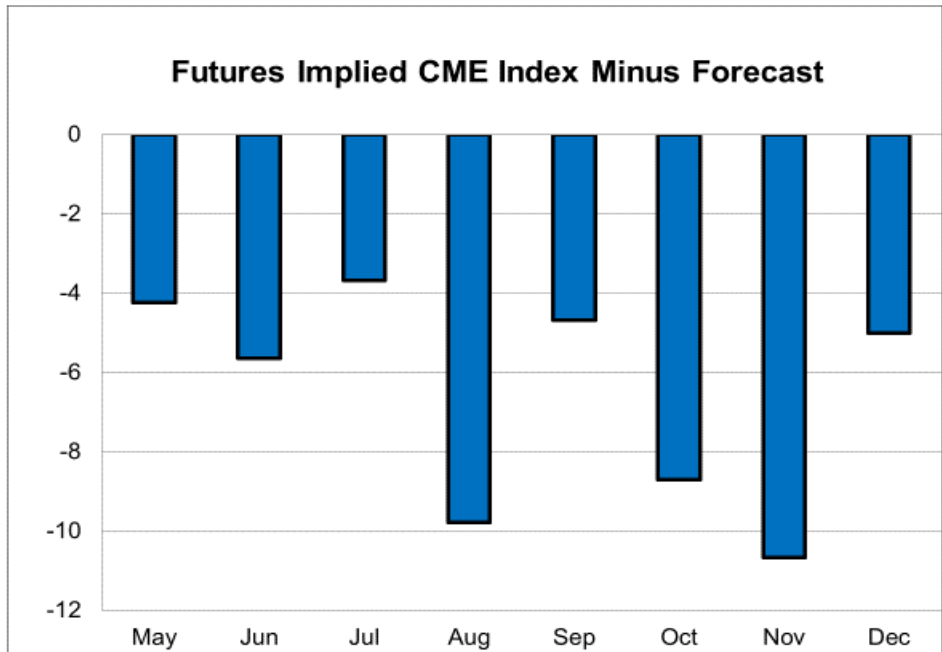


Trading Cattle

.... from a meat market perspective

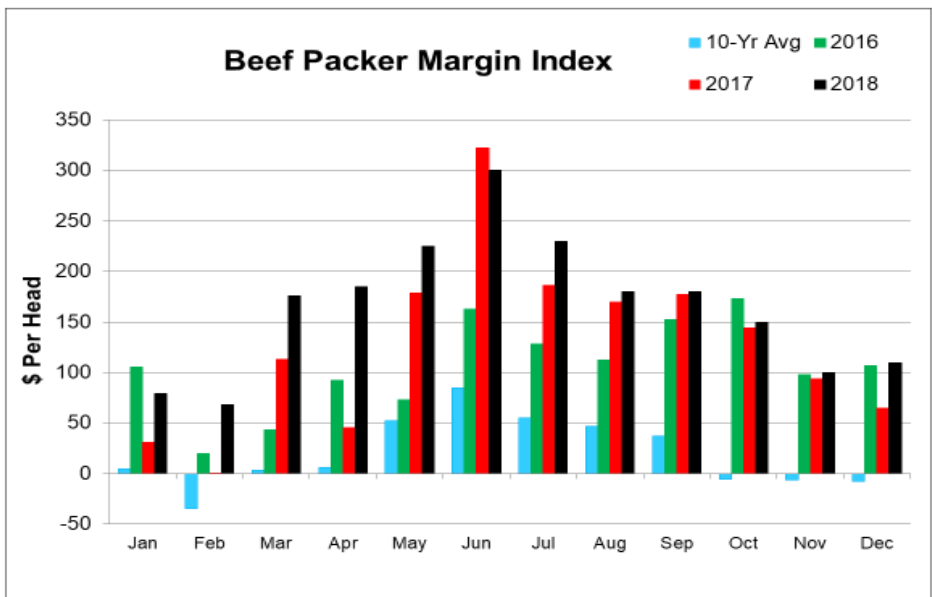
A commentary by Kevin Bost

April 17, 2018



My focus remains on the August contract, for reasons made obvious in the picture at left. Applying what I consider to be objective assumptions regarding beef demand and packer margins, the August contract appears to be ultimately worth about \$117 per cwt.

Am I *really* being objective in thinking that packer margins will be about the same as year earlier in August? It is this factor that poses the greatest downside risk to my forecast.

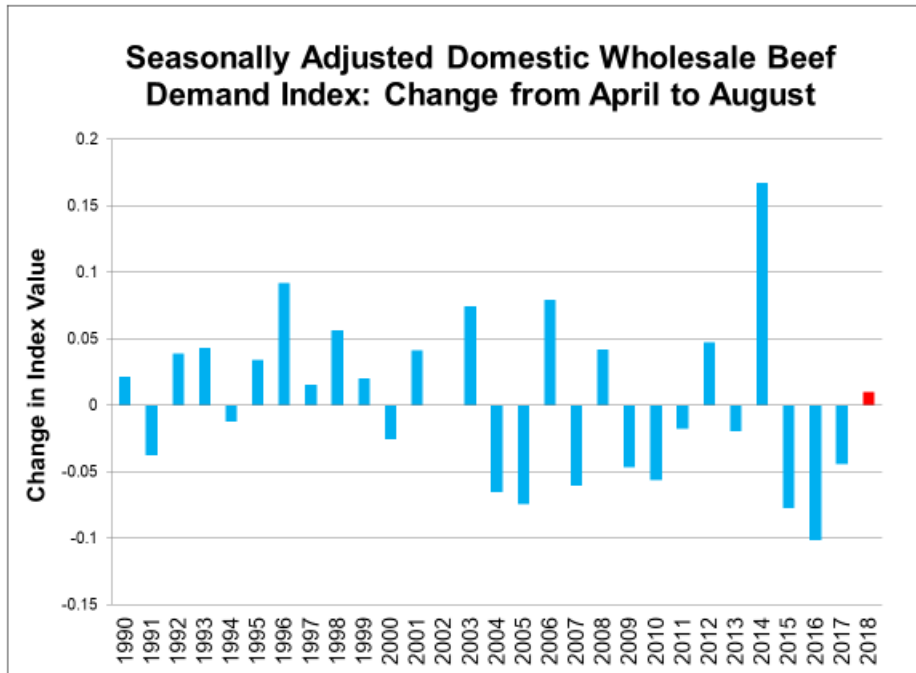


Well, the margin index value of \$180 per head that I am applying to my August pricing formula is pretty close to its March and preliminary April readings, which lends some degree of credibility to this projection.

Now, it is a bit disconcerting that more often than not, spot packer margins widen from March-April to August—but not *a/ways*. In seven of the past 15 years, they have either held steady or contracted. Also, the inventory of cattle on feed 90 days or longer should be 6% larger than a year earlier on August 1 (it was up 17% on April 1). This assumes a 12% decline in placements during March, followed by an 8% decline in April, and a 6% decline in May; and average weekly steer and heifer kills of 521,000 in May, 535,000 in June, and 507,000 in July. But front-end cattle supplies should be tapering off by August.

Finally, I consider that if the October contract still carries the sort of premium over the August contract that it does today, there should be an incentive for cattle feeders to slow marketing rates in late summer.... which should cause packers to compete more intensely for cattle.

As for beef demand, my assumption is simply that any material change between April and August will be of the normal, seasonal ilk. This is the most objective assumption I can make. About the only thing I can think of that would make for an extraordinary slowdown in wholesale demand into late summer would be if there were an extreme rally in beef prices prior to Independence Day—which is what happened last year. But if this is to be the case, then a long position in August cattle would probably make money in the interim. Last year, the combined Choice/Select cutout value jumped \$31 per cwt between mid-April and mid-June, and during that stretch, the August contract gained \$16. I doubt that the same will happen this time around, because roughly one third of the May/June 2017 rally was attributed to 50% lean beef trim. But forward bookings for late May and June delivery have picked up considerably in the last couple of weeks....



I still think that if the August contract is able to close above \$105.00, it will greatly enhance the likelihood that a major low was made at \$101.80 last Wednesday. The market this week has made two attempts to do so, and failed on both.

Originally I had not planned to buy the first close above \$105.00 in August cattle, but I have changed my mind about that. After two failed attempts, such a close would now be more meaningful. I would have to risk the position down to a close below \$101.80, which would presumably pose a risk of about 400 points. If the ultimate objective is \$117, then a 400-point risk would be in acceptable proportion. This buy signal might very well be followed by a pullback to \$105.00, but who knows? I would do well just to correctly identify where the road leads, let alone the path it takes to get there.

Forecasts:

	Apr	May*	Jun	Jul*	Aug	Sep*
Avg Weekly Cattle Sltr	618,000	649,000	664,000	632,000	642,000	636,000
Year Ago	599,600	606,400	637,900	603,800	633,800	624,400
Avg Weekly Steer & Heifer Sltr	489,000	521,000	535,000	507,000	510,000	503,000
Year Ago	481,100	490,600	514,200	488,800	511,000	502,100
Avg Weekly Cow Sltr	118,000	117,000	117,000	114,000	120,000	122,000
Year Ago	107,700	104,600	111,000	104,400	111,000	111,200
Steer Carcass Weights	861	849	862	877	889	901
Year Ago	849.0	837.8	854.0	868.5	884.6	896.0
Avg Weekly Beef Prodn	497	516	535	514	526	527
Year Ago	478.6	477.6	509.6	487.6	517.9	515.8
Avg Cutout Value	\$213.00	\$217.00	\$218.50	\$207.50	\$209.50	\$203.00
Year Ago	\$211.23	\$238.12	\$238.48	\$209.64	\$196.81	\$192.17
5-Area Steers	\$119.00	\$118.00	\$113.50	\$112.00	\$117.00	\$113.00
Year Ago	\$130.04	\$136.78	\$126.59	\$118.41	\$110.72	\$106.83

*Includes holiday-shortened weeks

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