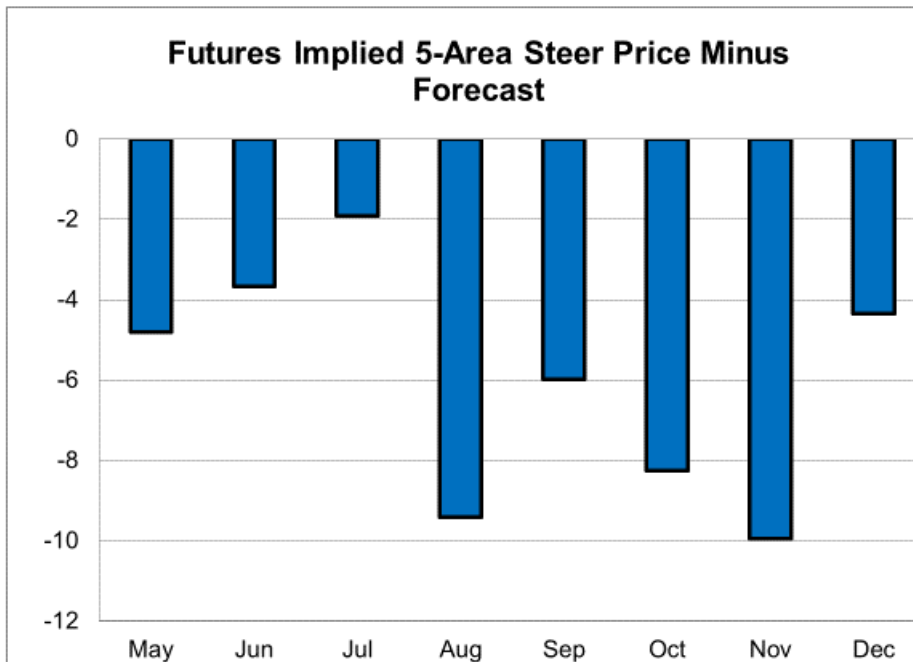


Trading Cattle

.... from a meat market perspective

A commentary by Kevin Bost

April 25, 2018



I feel as though I'm repeating myself, but such is the nature of strategy planning—check all systems, then do it again tomorrow and the next day. August cattle appear to be vastly

overvalued on the board and present the best trading opportunity. I remind myself that I am a better trader when I focus on the ultimate destination of a futures contract, and do not become preoccupied with the “noise” in the interim.

OK, so let's say that my assessment of ultimate value is correct. Proper money management requires that I still have to consider how much of an adverse move the market could make between now and—in this case—August, and take my bet off the table whenever a signal is given that a sizeable drawdown in equity is imminent. More often than not, failure to do so has been my downfall in the excessive losses that I have taken periodically throughout my career as a trader.

So, then, if August cattle are indeed destined for \$117 per cwt, how much lower could they go in the meantime? First of all, I notice that in the months of June and July, when the cash market is likely to be bottoming out, the August contract has carried discounts of as much as \$11.70 and \$7.74 respectively, on a weekly average closing basis. If the Five Area Weighted Average Steer price reaches down to \$105, which the chart on the next page suggests is a realistic possibility; and if this were to happen in early June; then August futures *could* be as low as

\$93-something at that time. If it were to happen in early July (which is more likely), then the August contract could be trading at \$97. Thus, a test of the contract lows at some point is not *that* hard to imagine.... even if it is to wind up at \$117.



It is equally likely, though, that a major low was established last Friday at \$101.72. I am willing to bet on this possibility. It is a bit disturbing that the August contract will probably fill the gap

that it left on the daily chart on Monday at \$103.95, and this price is significantly below the ten-day moving average, which has supported the market each day this week. Also, the five-day moving average, in that case, would be in danger of crossing below the ten-day average for the first time since April 9. This, in turn, could trigger the type of seemingly random sell-off that we saw last Thursday, setting up a move down to the \$102 area. However, one reason I am willing to bet on the support at \$101.72 is because there is not a lot of potential long liquidation from large speculators in this market. The *short* position among “large specs” is, in fact, the largest it has been in two years.

As for the bearish fundamental extremes, the packer margin poses the greatest threat among the key variables. Judging from 2017 steer and heifer kills, which peaked at 98,000 on weekdays and 52,000 on Saturdays during non-holiday weeks, the practical slaughter capacity appears to be around 542,000 per week. Keeping in mind that steer and heifer kills could *average* near that rate in June, the spread between cattle prices and cutout values could become surprisingly wide. Now, I am factoring into the equation an extremely wide spot packer margin of \$320 per head, on average, in June, but who knows what it could do? Yet, this is likely to be a factor only in June and not in August.

Forecasts:

	May*	Jun	Jul*	Aug	Sep*	Oct*
Avg Weekly Cattle Sltr	648,000	665,000	631,000	642,000	628,000	625,000
Year Ago	606,400	637,900	603,800	633,800	624,400	629,500
Avg Weekly Steer & Heifer Sltr	522,000	537,000	508,000	511,000	495,000	486,000
Year Ago	490,600	514,200	488,800	511,000	502,100	500,900
Avg Weekly Cow Sltr	115,000	116,000	113,000	119,000	121,000	128,000
Year Ago	104,600	111,000	104,400	111,000	111,200	117,800
Steer Carcass Weights	851	864	877	888	899	905
Year Ago	837.8	854.0	868.5	884.6	896.0	897.8
Avg Weekly Beef Prodn	518	538	515	527	520	518
Year Ago	477.6	509.6	487.6	517.9	515.8	518.4
Avg Cutout Value	\$218.50	\$218.00	\$207.50	\$209.50	\$205.00	\$206.50
Year Ago	\$238.12	\$238.48	\$209.64	\$196.81	\$192.17	\$197.04
5-Area Steers	\$119.00	\$111.50	\$110.50	\$117.00	\$114.00	\$117.50
Year Ago	\$136.78	\$126.59	\$118.41	\$110.72	\$106.83	\$112.08

**Includes holiday-shortened weeks*

Trading Cattle is published weekly by Procurement Strategies Inc., 99 Gromer Road, Elgin IL 60120. For subscription information, please contact Kevin Bost at (847) 212-7523; or visit our website at www.procurementstrategiesinc.com.

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