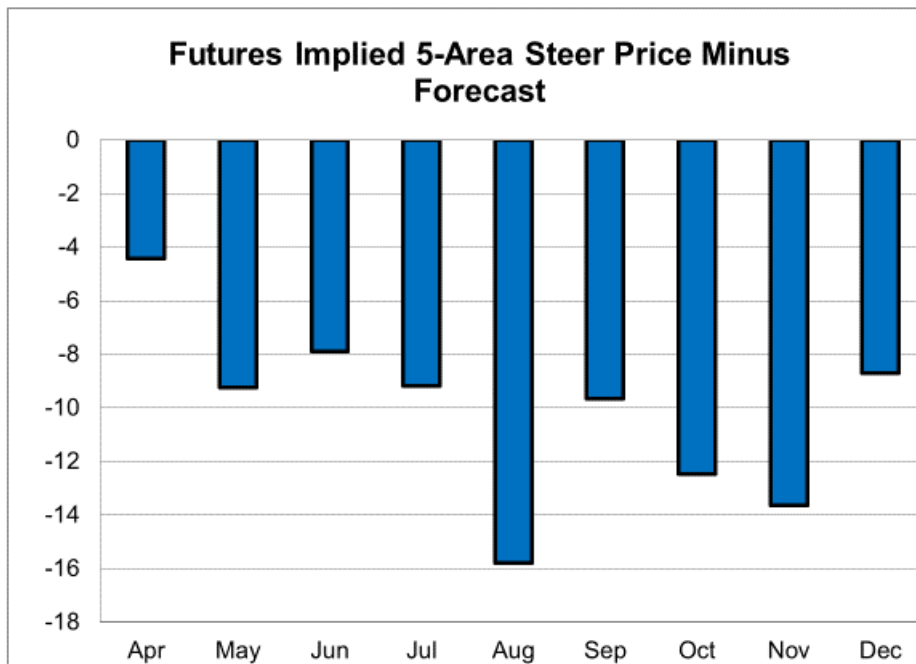


Trading Cattle

.... from a meat market perspective

A commentary by Kevin Bost

April 3, 2018

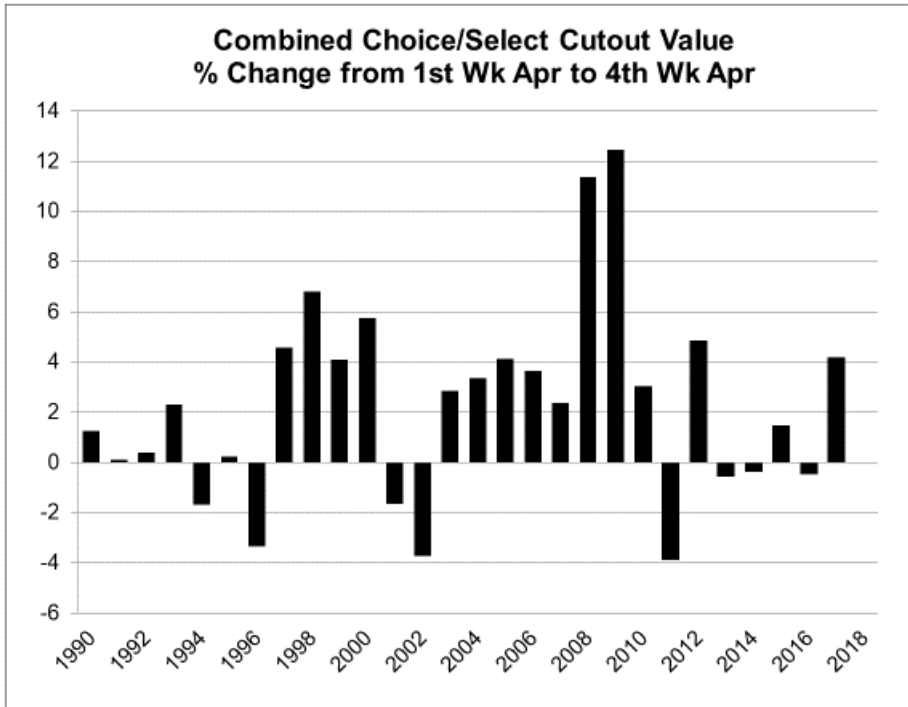


I have taken on a modest long position in the August contract, but whether the direction is upward or downward, I do not plan to hold this position for very long. Despite the fact that it appears to be vastly undervalued, I am not ready to bet that the market has established

its ultimate bottom. I am, however, willing to bet on a “bounce”, and in this case, that bounce could be sizeable. At yesterday’s close, the August contract stood about 400 points below its ten-day moving average (which today crosses near \$104.00 per cwt). The nearest meaningful resistance level lies at last Thursday’s high of \$105.65. And if my forecasts are not totally insane, then a return to the “breakdown point” at \$107.50 could be regarded as an intermediate objective; that could be achieved without doing any real damage to the downtrend, as a 50% retracement from yesterday’s low would be \$108.00.

As we all know, the cash cattle market is headed downward. But it’s not difficult to envision a period of temporary stability along the way. The beef market is actually performing a bit better than I had anticipated. It’s losing ground, but not at a breakneck pace. Now, in view of the abundance of meat being offered in the spot market, the rate of decline will probably accelerate. But there is a decent chance that the combined Choice/Select cutout value will find a temporary bottom sometime next week. That bottom could be as low at \$210 per cwt—the location of its major support level, and \$8 below Monday’s quote. On the next page I show the track record of the cutout value from the first week of April to the fourth week of April. It’s pretty rare that the latter has been any lower than the former; thus, the history suggests that there is likely to be some firmness in the market after the middle of the month. I must admit that the tepid forward booking volumes for April delivery cast a dark cloud over the near-term demand outlook. Yet, my guess of a \$115-\$117 combined cutout value in the final week of April assumes that demand will underperform relative to the seasonal norm.

The point is that with \$18-\$19 per cwt discounts in the June and August contracts, any sign of stability in the cash market likely would prompt a recovery in the futures market.



Perhaps this is not of immediate concern, but the composition of the futures market has changed dramatically over the last several weeks. As of last Tuesday, when June cattle were still above \$105, long positions among large speculators made up only 12% of the total "pie", the

smallest share in two years. The short position among large speculators was not huge, but its share of the total was the largest since November 2016. Potential long liquidation from speculators has diminished, while potential short-covering has grown.

Anyway, if the combined cutout value stands at \$115 at the end of the month, and if spot packer margins expand even further from last week's reading of \$218 per head to \$225 per head in the meantime, then the Five Area Weighted Average Steer price will still be above \$117, a significant support level on the chart.



In any case, I promised myself that I would make this bet only with a tight stop-loss in place, and by my definition, that would be a close below \$100.00 in the August contract. No exceptions.

Forecasts:

| | Apr | May* | Jun | Jul* | Aug | Sep* |
|--------------------------------|----------|----------|----------|----------|----------|----------|
| Avg Weekly Cattle Sltr | 617,000 | 648,000 | 663,000 | 631,000 | 641,000 | 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 | 116,000 | 116,000 | 113,000 | 119,000 | 121,000 |
| Year Ago | 107,700 | 104,600 | 111,000 | 104,400 | 111,000 | 111,200 |
| Steer Carcass Weights | 859 | 849 | 862 | 877 | 889 | 901 |
| Year Ago | 849.0 | 837.8 | 854.0 | 868.5 | 884.6 | 896.0 |
| Avg Weekly Beef Prodn | 496 | 516 | 535 | 514 | 526 | 527 |
| Year Ago | 478.6 | 477.6 | 509.6 | 487.6 | 517.9 | 515.8 |
| Avg Cutout Value | \$215.00 | \$218.00 | \$216.00 | \$207.00 | \$210.50 | \$203.00 |
| Year Ago | \$211.23 | \$238.12 | \$238.48 | \$209.64 | \$196.81 | \$192.17 |
| 5-Area Steers | \$119.00 | \$117.50 | \$111.00 | \$113.00 | \$118.00 | \$114.00 |
| Year Ago | \$130.04 | \$136.78 | \$126.59 | \$118.41 | \$110.72 | \$106.83 |

**Includes holiday-shortened weeks*

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