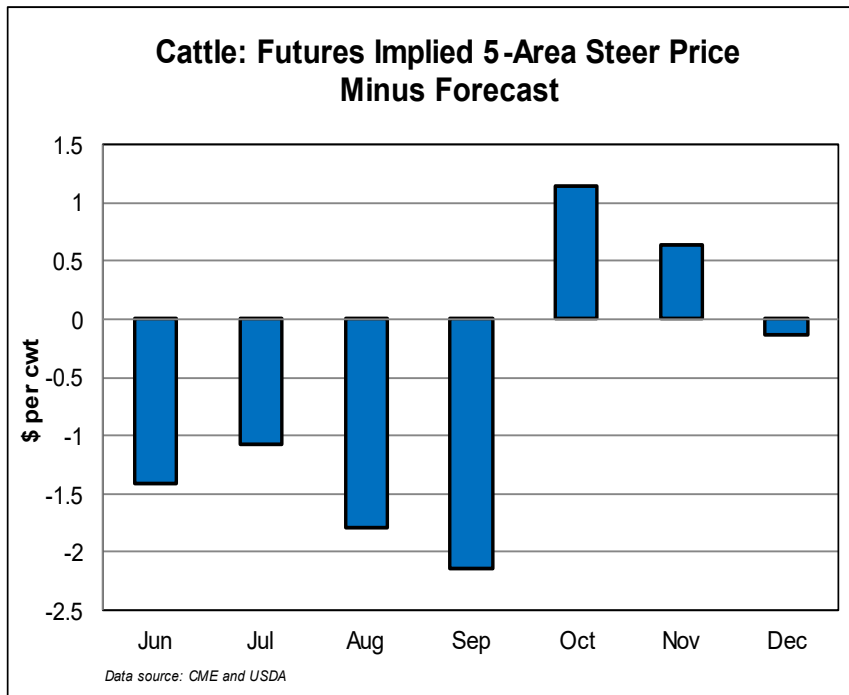


Trading Cattle

.... from a meat market perspective

A commentary by Kevin Bost

May 24, 2021



The picture to the left is uninspiring. While there are unusually broad ranges surrounding my forecasts at the moment, compared with the *most objective* forecasts I can come up with, the futures market appears to be pretty fairly priced. And so I have no immediate plans to lay a bet on the table.

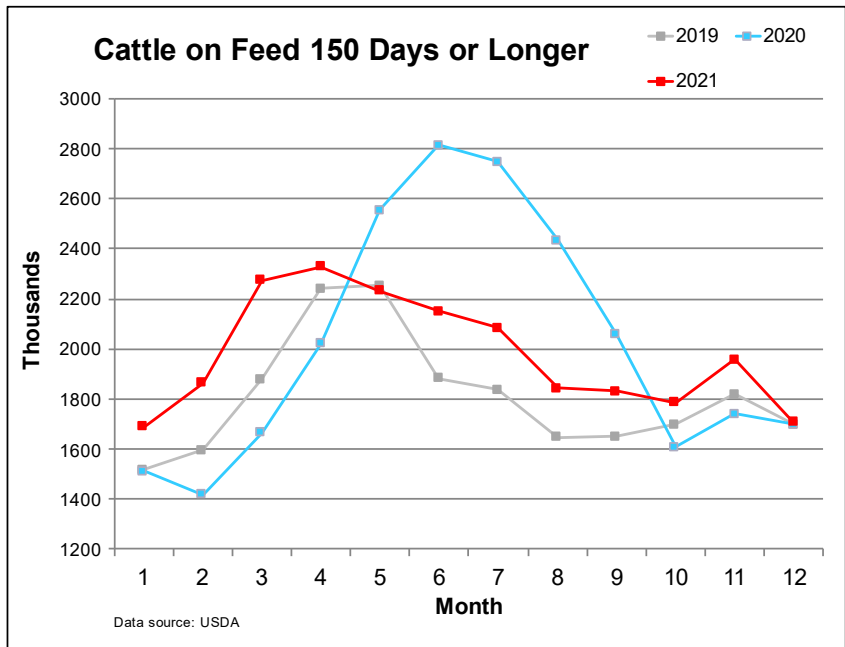
I prefer to approach the market from the long side, though, for a couple of reasons. One is simply the vague notion that the cattle market may be going through its toughest times right now, with front-end cattle supplies exceeding practical slaughter capacity. Generally speaking, there is hardly a more bearish condition to deal with than this, as it relates to cash cattle prices. The other is the chart of the Five Area Weighted Average Steer price, which is trending upward and looks as though it is headed for \$125—although the chart does not tell us when it will get there. It's not difficult to imagine a trade down to \$115 first.

Up to this point, I have been reluctant to play the long side of this market because of the likelihood that cutout values will take a major "hit" in the weeks ahead. But it seems that this is now widely anticipated; at least, it's not going to surprise anyone when it starts coming down in big chunks. And if we're all wrong—if beef prices manage to hold their ground somehow—that would be bullish.

And so the subject inevitably turns to packer margins. They *will* eventually come back down to Earth at some point, but frankly, I haven't much of a clue just how far off in the distance "eventually" might be.

My intuition tells me that cutout values cannot drop dramatically without packer margins narrowing at the same time. To put it another way, once a vacuum underneath beef prices is encountered, they will come off faster than will cash cattle prices. Yet, as long as competition among packers for live cattle supplies remains minimal, margins will remain extraordinarily wide; cash cattle prices could be “walked downward”, perhaps back to \$115 in the near term. At this juncture, I would have to bet against a more competitive environment developing before July.

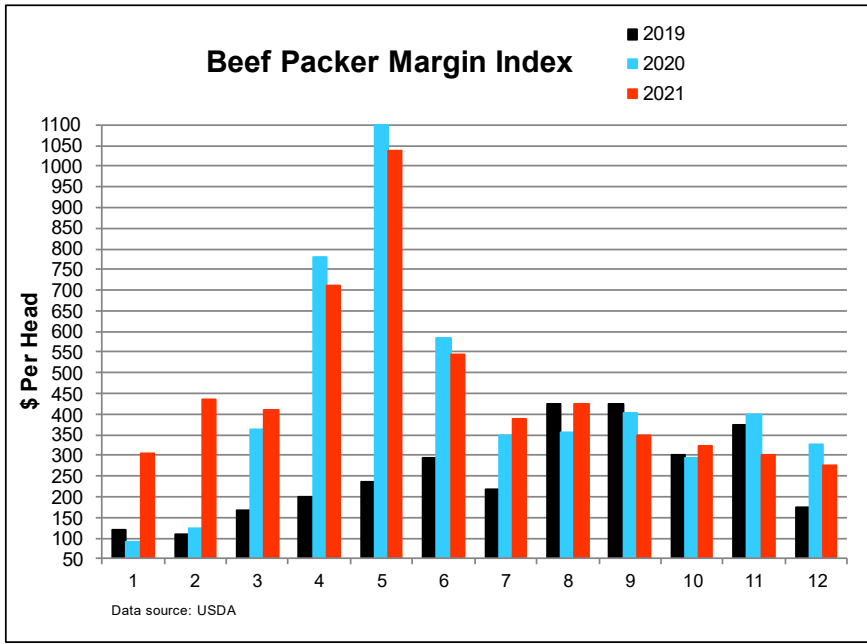
Last week’s jump in fed cattle slaughter (to 535,000) was a good start, but with labor shortages being such an issue, it is questionable whether or not this rate of production can be sustained week after week. It would need to happen, though, in order to prevent the apparent backlog from spilling over into July. I notice that between the end of March and the first week of May (which was the most recent official reading), steer carcass weights actually increased by two pounds; this compares with a ten-year average decline of 13 pounds over the same period. This says something about the industry’s “currentness”, doesn’t it?



I’m expecting that competition for live cattle supplies will be considerably greater by the time we get to August, based on the projection of cattle on feed 150 days or longer shown in the graph to the left. This projection assumes that steer and heifer kills will average 532,000 during the four non-

holiday weeks of June, and 517,000 in the three non-holiday weeks of July. Judging from their recent pace, this could be a challenge.

My guess is that the spot packer margin index, which I show at the top of the next page, will drop down to an average of \$545 per head in June; \$390 in July; and \$425 in August. I came up with these numbers by taking my forecast of cutout values and looking at where the margin index stood the last time cutout values traded at the same price. For example, I am forecasting an average combined Choice/Select cutout value of \$254 per cwt in June; the last time it traded at that level (in early April), the margin index stood at approximately \$540. It’s crude, but the logic seems fairly sound.



Packer margins make a big difference in the determination of live cattle prices, and there is enough doubt surrounding my margin projections that I want to keep in mind the range of possibilities. A couple of weeks ago I showed you a matrix of packer margin index values and the corresponding

cash cattle prices, and I think it would be a good idea to take a glance at it on a regular basis....with special attention to the more bearish possibilities, since my next bet will probably be on the long side of the table:

June		July		August	
Margin Index	Cash Cattle	Margin Index	Cash Cattle	Margin Index	Cash Cattle
\$750/hd	\$105.00	\$650/hd	\$101.00	\$650/hd	\$105.50
\$700	\$108.50	\$600	\$105.00	\$600	\$109.50
\$650	\$112.00	\$550	\$108.50	\$550	\$113.00
\$600	\$116.00	\$500	\$112.00	\$500	\$116.50
\$550	\$119.50	\$450	\$116.00	\$450	\$120.50
\$500	\$123.50	\$400	\$119.50	\$400	\$124.00
\$450	\$127.00	\$350	\$123.50	\$350	\$128.00
\$400	\$131.00	\$300	\$127.00	\$300	\$131.50

The major trend in the August contract is sideways, and so rule number one would be to aim for an entry price near the bottom of that range (roughly \$116). But as I mentioned last week, this is such an obvious support level, and has been thoroughly tested on three previous occasions that I'm not sure I trust it to hold up a fourth time....

Forecasts:

	Jun*	Jul*	Aug	Sep*	Oct	Nov*
Avg Weekly Cattle Sltr	656,000	634,000	649,000	636,000	641,000	636,000
Year Ago	645,700	630,500	645,300	636,500	645,000	634,600
Avg Weekly Steer & Heifer Sltr	521,000	504,000	515,000	500,000	498,000	495,000
Year Ago	513,500	508,700	520,600	506,200	507,700	499,100
Avg Weekly Cow Sltr	123,000	119,000	123,000	125,000	132,000	131,000
Year Ago	120,600	111,200	113,400	119,000	126,300	125,700
Steer Carcass Weights	900	914	926	938	945	946
Year Ago	893.5	901.0	910.3	921.0	928.5	924.5
Avg Weekly Beef Prodn	542	530	547	540	545	542
Year Ago	534.3	524.0	537.9	534.3	542.5	532.7
Avg Cutout Value	\$254.00	\$236.00	\$243.00	\$237.00	\$232.00	\$234.00
Year Ago	\$240.10	\$201.66	\$214.29	\$218.06	\$208.35	\$224.87
5-Area Steers	\$120.00	\$120.50	\$122.00	\$124.00	\$122.50	\$125.50
Year Ago	\$103.46	\$96.62	\$104.52	\$104.01	\$106.27	\$108.94

*Includes holiday-shortened weeks

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