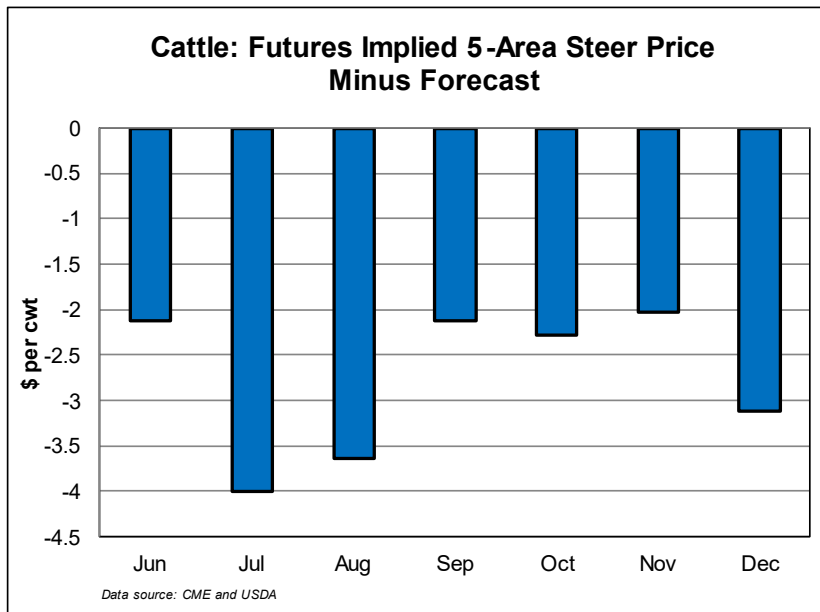


Trading Cattle

.... from a meat market perspective

A commentary by Kevin Bost

May 31, 2021



Cattle futures have covered a range of “only” 327 points over the last eleven sessions which, by today’s standards, is relatively small. But it looks as though the market will be shaken up on Tuesday by the apparent shutdown of all JBS’ slaughter and processing operations due to a cyber attack. As I’m writing this report, it is yet uncertain whether

the North American plants will be idled (as its Australian meat works were on Monday), but it appears to be headed in that direction. If so, then this development will trump all others for a while.

While this will be a temporary concern—unlike the fire at Tyson’s plant in Holcomb, Kansas in August 2019—we can only guess at how long “temporary” may be. In any case, the timing could hardly be worse as front-end cattle supplies are already exceeding practical kill capacity. And it comes on the heels of a surprisingly light kill last week (495,000 steers and heifers) and a holiday-shortened schedule this week.

And so, even though my preference is to trade the cattle market from the long side, since it is hard to imagine conditions being more bearish than they are now, I am willing to sell into a close below \$116.00 in the August contract. As I explained last week, I do not sell a market that is not overvalued unless the technical signals are overwhelming. And after three serious tests of the conspicuous support level at \$116.00 since February 1, a breakdown of that support would have some ominous consequences. The daily trading limit is scheduled to expand to 500 points on Tuesday (God knows why), so \$116.00 in the August contract is well within tomorrow’s reach.

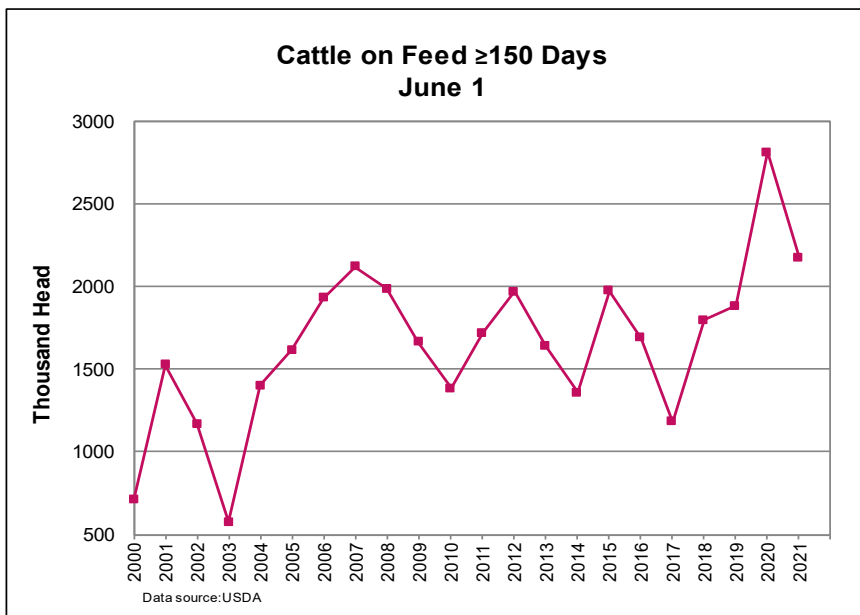
If it is confirmed that JBS’ North American plants will be idled, my intention is to sell a modest quantity of August cattle out of the gate on Tuesday and hold them if they close below \$116.00.

I have not forgotten that there remains a gap on the daily chart of August cattle at \$109.12. Assuming that this will not turn out to be a lingering issue, I would allow the market only a few days to fill this gap. Whatever the extent of the damage, the recovery should be a fierce one.

Although the charts could be reconfigured in the week ahead, I have to maintain my long-term perspective and keep my focus on ultimate fundamental value. It could turn out that the longer-term trading opportunity from the long side of the table will be greater than the short-term selling opportunity. In other words, the real value of a potential selloff could be that it creates a better buying opportunity.

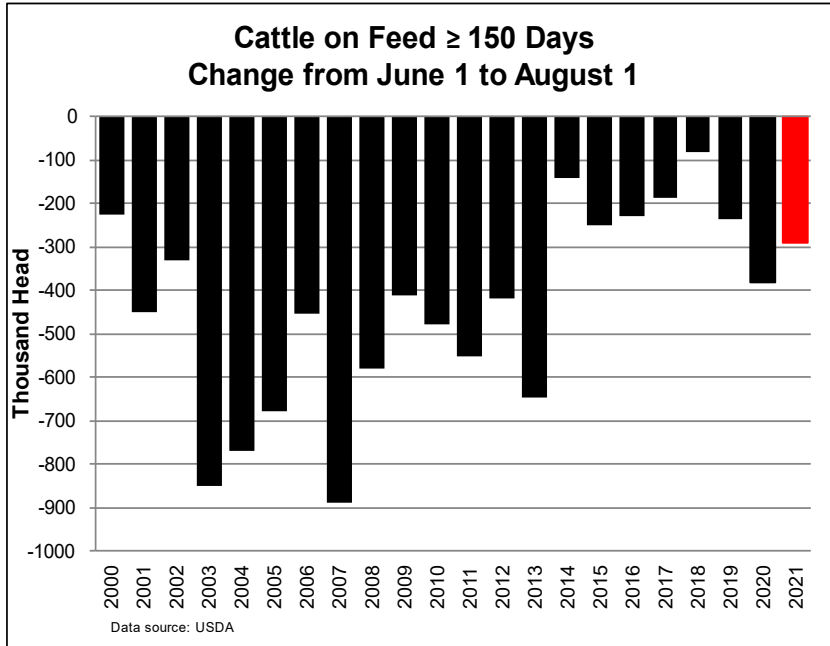
The cattle market has been operating under an unconventional set of rules lately, as the disconnect between cash cattle and beef prices renders the beef market less relevant than usual. Having said that, I have bumped up my projections of wholesale beef demand in view of its very impressive performance during May. Even so, it is highly likely that cutout values will drop sharply over the next 30 days; it's just a question of degree. Rapidly rising retail prices will not go unnoticed by supermarket shoppers, and product movement in this sector will slow down. There is a good chance that the increase in retail beef prices in June will be a record, or close to it. If the seasonally adjusted demand index pulls back to where it stood prior to April, then the combined Choice/Select cutout value will drop from Friday's quote of \$326 per cwt down to \$240 by early July. It seems likely that if that happens, then cash cattle prices will be pulled down along with it—not to the same extent, but I would expect packers to be less willing to support the market at \$119-\$120 if cutout values are falling that rapidly. This is not a good environment in which to be betting on higher prices.

The central issue remains the packer margin. Until packers have to compete for cattle supplies again, natural market forces will not drive cash cattle prices upward....which would be the foundation of a long position in the futures market. It is still not very clear to me, though, when that turning point will be reached. I look to the inventory of cattle on feed 150 days or longer for clues.



The picture to the left shows where it stands now. Next to 2020, it is a record-large supply for this date. My guess is that some measure of competition will return to the cattle market by August 1, but I am not highly confident of that prospect. On one hand, the 150-day

inventory on August 1 should still be the second largest on record for that date, and the decline in this inventory from June 1 to August 1 will be nothing spectacular; on the other hand, the August 1 inventory should be back down to about where it stood in February, when there was at least *some* trace of competition for live cattle.



Eventually, the contraction in packer margins will become a bullish factor—especially if it comes along in late summer, when beef prices should be recovering from their (presumed) June-July plunge. This is one reason why I am focused on the August contract....but waiting until the time is right.

Forecasts:

	Jun*	Jul*	Aug	Sep*	Oct	Nov*
Avg Weekly Cattle Sltr	653,000	634,000	648,000	634,000	640,000	634,000
Year Ago	645,700	630,500	645,300	636,500	645,000	634,600
Avg Weekly Steer & Heifer Sltr	517,000	504,000	513,000	497,000	496,000	493,000
Year Ago	513,500	508,700	520,600	506,200	507,700	499,100
Avg Weekly Cow Sltr	124,000	120,000	124,000	126,000	133,000	132,000
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	539	529	545	538	543	540
Year Ago	534.3	524.0	537.9	534.3	542.5	532.7
Avg Cutout Value	\$273.00	\$242.00	\$246.00	\$238.00	\$235.00	\$237.00
Year Ago	\$240.10	\$201.66	\$214.29	\$218.06	\$208.35	\$224.87
5-Area Steers	\$119.50	\$121.50	\$122.00	\$123.00	\$125.00	\$128.00
Year Ago	\$103.46	\$96.62	\$104.52	\$104.01	\$106.27	\$108.94

*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.

Information herein is derived from sources believed to be reliable, with no guarantee to its accuracy or completeness. There is a substantial risk of loss in trading futures and options especially when not hedged against a cash position. Opinions expressed are subject to change without notice. Each investor must consider whether this is a suitable investment. All funds committed should be risk capital. Past performance is not necessarily indicative of future results.