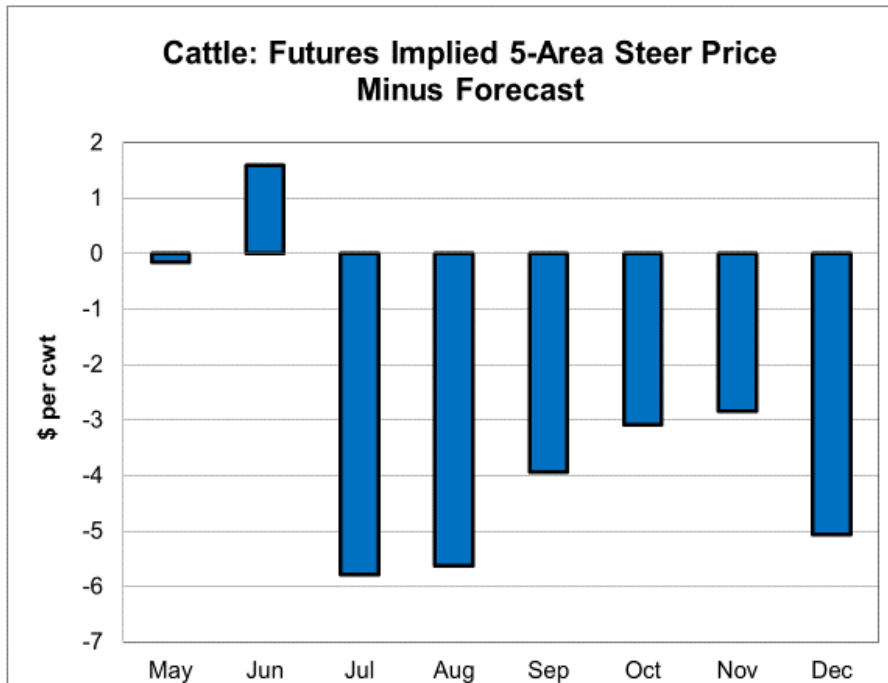


Trading Cattle

.... from a meat market perspective

A commentary by Kevin Bost

May 8, 2019

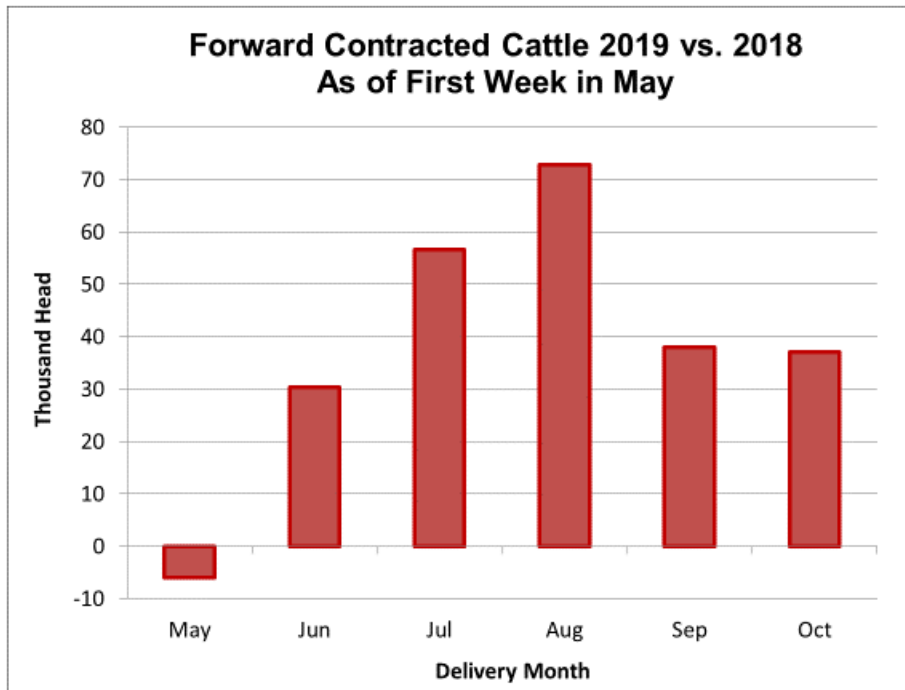


Although the board appears to have priced in an exceedingly bearish set of conditions, I am still avoiding the long side of the market. While I had expected a weaker than normal change in beef demand from April to

May, I did not look for the bottom to fall out the way it has. And in view of the relatively light volume of product that was forward-booked for May delivery, it looks as though the market still has a considerable amount of work to do to bring supply and demand into balance.

I consider also that spot packer margins will probably widen by \$100 per head or more before they peak--meaning, of course, that cattle prices should lose ground relative to beef prices in the weeks ahead. Apart from the seasonal tendency for packer margins to widen into June, I notice that the number of cattle already contracted for June delivery is about 30,000 head greater than it was at this time last year. The difference is even greater for July and August deliveries, as I show on the next page.

It's a good bet, then, that the futures market will have to absorb a lot of bearish news over the next several weeks, and I don't care to be holding a long-side bet and waking up to adversity every day. Oh--and there is the fact that the seasonal decline in cattle prices is only three weeks old, and at this point we're just guessing about where the bottom may lie.



And so I am waiting for the June contract to make an earnest attempt to recover, into which I would sell. What would qualify as an “earnest attempt”? Well, the Fibonacci numbers are always fun to play

with. Measuring from the April 16 high of \$122.97 to today’s low, a 38% retracement would take the June contract to \$115.52; the 50% retracement target is \$116.95; and the 62% retracement target is \$118.37. There is a gap on the daily chart just below the latter, at \$118.17. But if the market were able to rally all the way up to \$118-something at this stage of the game, then I probably would not want to sell it. That likely would require some sort of game-changing bullish development in the cash market. I am inclined to be a modest seller at \$115.50, saving enough ammunition to sell an equal amount near \$117.00. Of course, these parameters will change if the market moves substantially below today’s low before it tries to recover. As always, if no such bounce occurs, then I won’t play.

In the meantime, I am holding the short June/long August spread. I initiated this position last Thursday at a June premium of \$3.50 per cwt, thinking that it would serve as a proxy for an outright short position in the June contract and that the barrage of bearish news would weigh most heavily on front leg. I was nearly stopped out on Monday (my close-only stop-loss trigger is \$4.75). I still hold this opinion, though I am puzzled that it has not worked in my favor so far.

I am hoping that the June and August contracts move to even money, which seems like a very conservative target according to my assessment of “fair value” as shown in the picture on the first page. That would not be at all unusual from an historical perspective, either. True, the June premium never fell below \$1.00 after the second week of May in any of the last four years; but in nine of the past 15 years, it *did*. We’ll see. In any case, a 125-point risk coupled with a 350-point profit potential meets my standards from a risk/reward standpoint.

Forecasts:

	May*	Jun	Jul*	Aug	Sep*	Oct
Avg Weekly Cattle Sltr	653,000	660,000	626,000	644,000	637,000	648,000
Year Ago	642,200	654,000	623,900	643,400	632,200	641,500
Avg Weekly Steer & Heifer Sltr	522,000	531,000	500,000	514,000	508,000	514,000
Year Ago	517,100	526,100	499,100	512,600	504,500	505,500
Avg Weekly Cow Sltr	119,000	116,000	114,000	118,000	117,000	123,000
Year Ago	113,800	116,200	114,000	119,600	117,100	125,000
Steer Carcass Weights	854	866	880	894	906	911
Year Ago	848.4	857.5	870.0	884.8	897.0	898.0
Avg Weekly Beef Prodn	520	532	509	531	530	542
Year Ago	510.2	523.2	503.3	525.3	522.0	528.0
Avg Cutout Value	\$221.00	\$221.00	\$217.50	\$218.50	\$212.00	\$210.00
Year Ago	\$224.53	\$217.10	\$204.61	\$207.50	\$204.18	\$205.70
5-Area Steers	\$117.75	\$112.00	\$115.50	\$116.50	\$114.50	\$114.50
Year Ago	\$116.36	\$110.39	\$111.87	\$110.02	\$109.89	\$112.06

*Includes holiday-shortened weeks

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