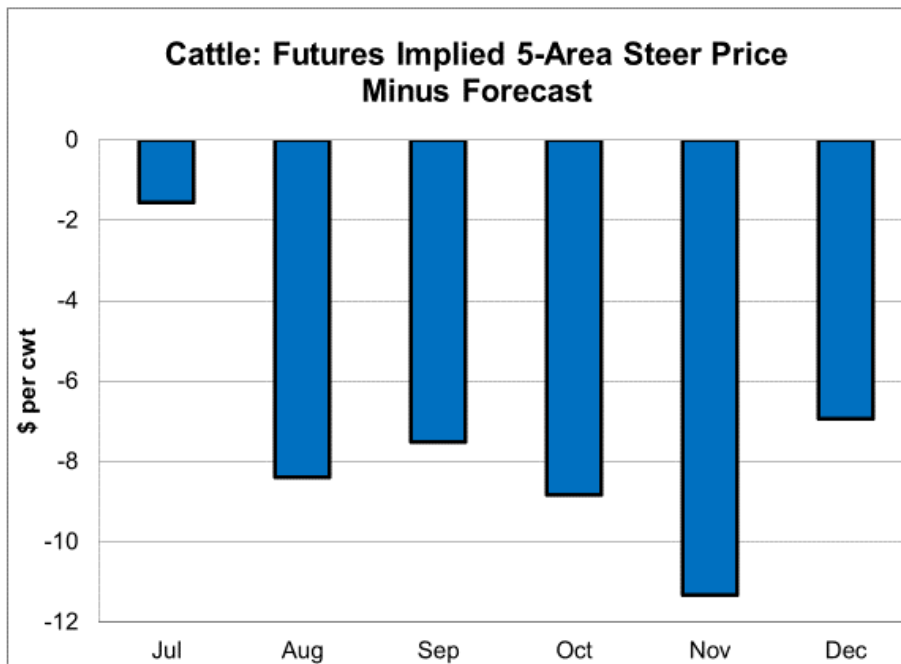


Trading Cattle

.... from a meat market perspective

A commentary by Kevin Bost

June 30, 2018



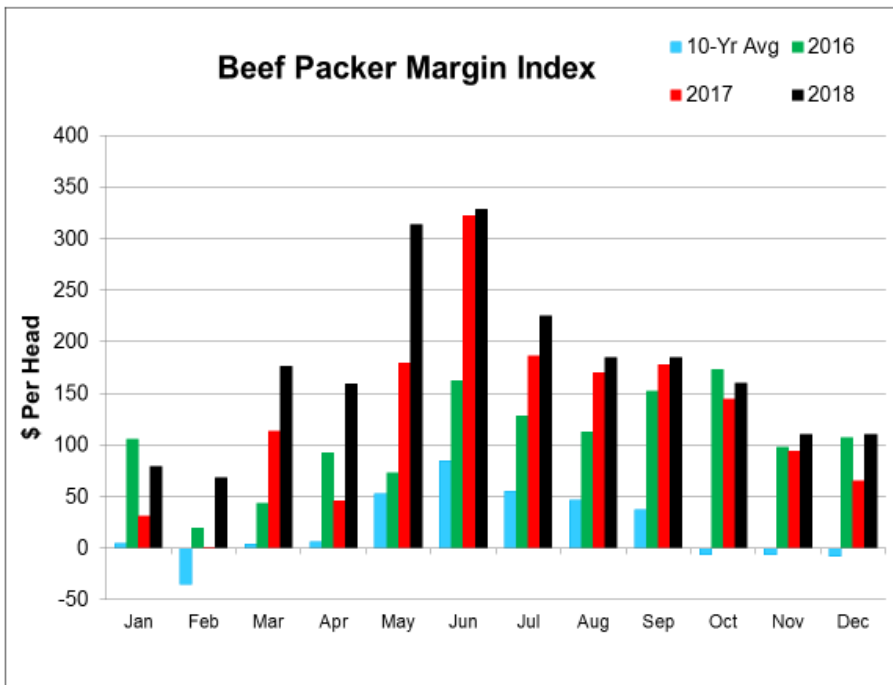
I continue to hold a fairly aggressive long position in August cattle, just waiting to either be stopped out (on a close below \$100.40) or to receive a signal that my cash price forecast is materially off-target.

You're probably weary of listening to me recount these same key variables, but I have to do it. "Checking my premises" over and over again is a mandatory discipline when I have a bet on the table. Losing money because my assumptions are wrong is acceptable; losing money due to lack of attention is not. So bear with me.

First, and most critical, is the packer margin. The first real test of my assumption that it will shrink dramatically during July will come next week, partly because packers will be buying for a full slaughter schedule with a holiday landing right in the middle of the week. But what I am mainly counting on is that a shift in the basis and a perception that the bottom is near will encourage feedlots to be more discriminating toward packer bids. And they can probably afford to do so, since slaughter rates and carcass weights indicate that front-end supplies are "current". [Since they bottomed in the week ended May 19, steer carcass weights have risen ten pounds vs. the 15-year average increase of 12.4.] I'm betting that packers will be willing to compete a bit more intensely to secure the "first cut" of cattle, because they will still be very profitable. And so, if the spread between

cattle and beef prices does not narrow significantly next week I will be concerned.

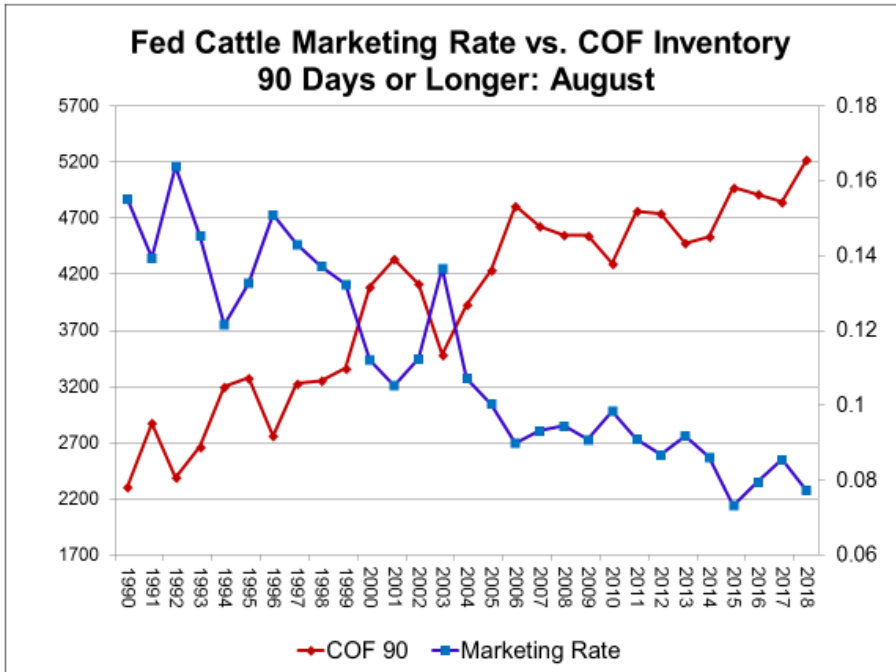
But if the spot packer margin index *does* narrow from this week's value of \$330 per head to \$185 in August, it will cover up a lot of sins in the forecast of the cutout value. My best guess, as I show in the table below, is that the combined Choice/select cutout value will average \$210.50 per cwt in August; if I am \$5.00 too high, a \$185 spot packer margin index would still align with a cash cattle market of \$113.50.



I am encouraged by the fact that the average packer margin index in June was virtually the same as a year ago; my projection of a \$185 per head index value in August is about \$15 above a year earlier.

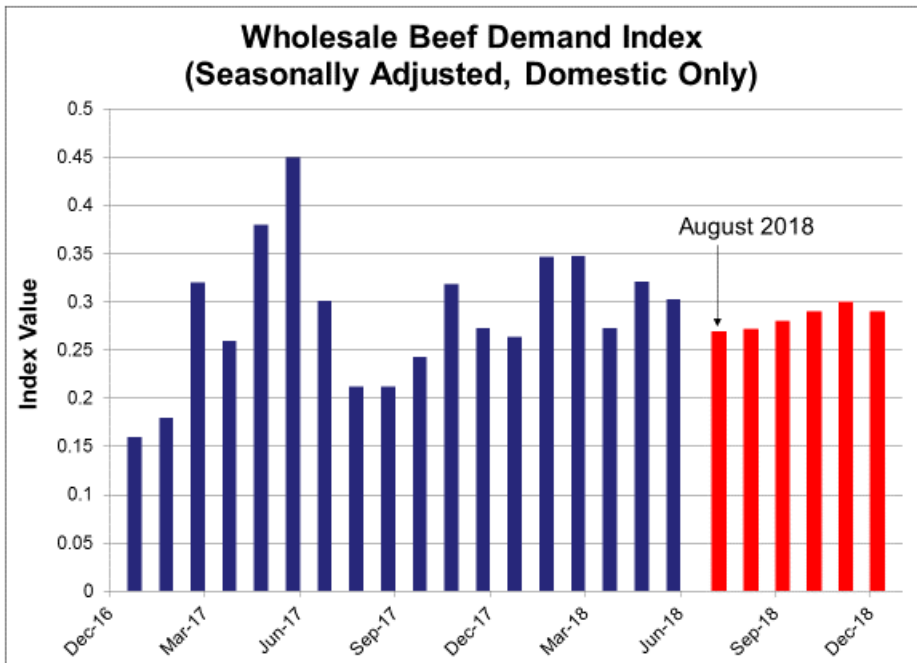
Second is the related issue of production. I'm factoring in a rate of steer and heifer slaughter that is 14,000 head per week lower than a year earlier in August—which is difficult to explain, given that the inventory of cattle on feed 90 days or longer will be 7-8% larger. There is always room for this variable to be over- or understated, since there are so many factors involved. All I can say is that a rate of 497,000 per week is actually a bit generous in view of the strong (inverse) correlation between the "90-day" inventory and fed cattle slaughter, as I show on the next page. When I insert into the equation a kill rate that is equal to a year earlier, though (511,000), it reduces the forecast of the combined cutout value by about \$3 per cwt, to \$207.50....which still aligns with a cash cattle price of \$115 if the packer margin index is \$185 per head.

Finally, I am assuming that the decline in wholesale beef demand will be greater than the seasonal norm, which is a pretty conservative assumption, I think. Forward bookings for August delivery have so far been quite active. Apart from



the fact that the wholesale demand index is due for a short-term cyclical low in July/August, I really have no reason to think that there will be anything other than a typical seasonal change in demand from June to

August...in which case, the combined cutout value would average \$215 and the cash cattle market \$120, all else remaining the same.



Forecasts:

	Jul*	Aug	Sep*	Oct	Nov*	Dec*
Avg Weekly Cattle Sltr	619,000	628,000	606,000	615,000	607,000	592,000
Year Ago	603,800	633,800	624,400	629,500	625,700	593,800
Avg Weekly Steer & Heifer Sltr	496,000	497,000	474,000	477,000	469,000	462,000
Year Ago	488,800	511,000	502,100	500,900	498,600	472,600
Avg Weekly Cow Sltr	113,000	119,000	121,000	127,000	128,000	121,000
Year Ago	104,400	111,000	111,200	117,800	116,700	111,600
Steer Carcass Weights	868	879	890	896	896	891
Year Ago	868.5	884.6	896.0	897.8	902.6	902.8
Avg Weekly Beef Prodn	500	510	496	504	499	487
Year Ago	487.6	517.9	515.8	518.4	519.2	495.3
Avg Cutout Value	\$206.25	\$210.50	\$209.50	\$210.00	\$210.00	\$207.00
Year Ago	\$209.64	\$196.81	\$192.17	\$197.04	\$205.15	\$199.67
5-Area Steers	\$111.50	\$117.00	\$116.50	\$119.00	\$122.50	\$120.50
Year Ago	\$118.41	\$110.72	\$106.83	\$112.08	\$121.03	\$120.00

**Includes holiday-shortened weeks*

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