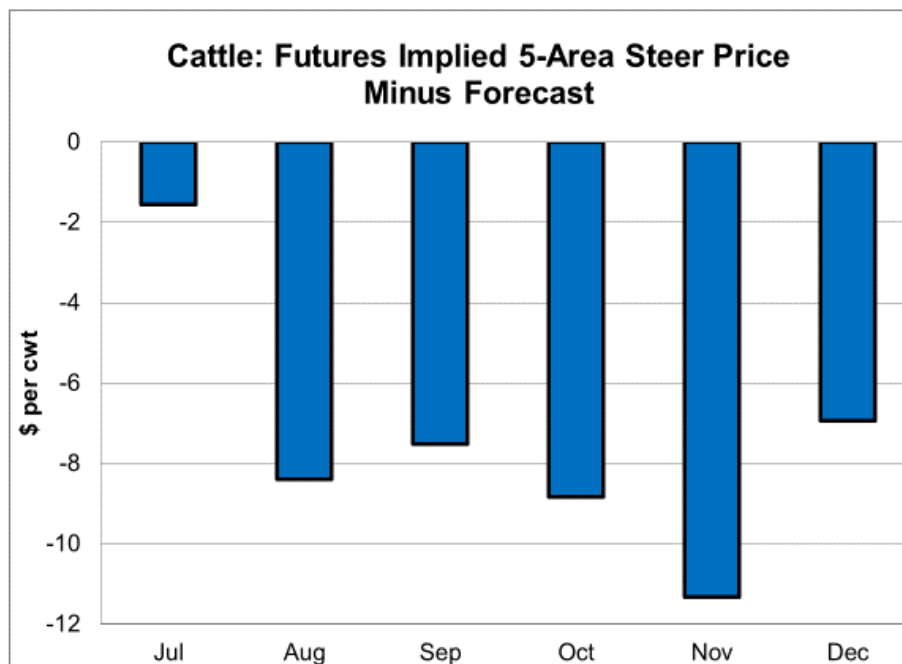


Trading Cattle

.... from a meat market perspective

A commentary by Kevin Bost

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I remain long of August cattle with a close-only stop at \$100.40 per cwt. The market has established two important support levels above that price (one of which was yesterday's low of \$102.70),

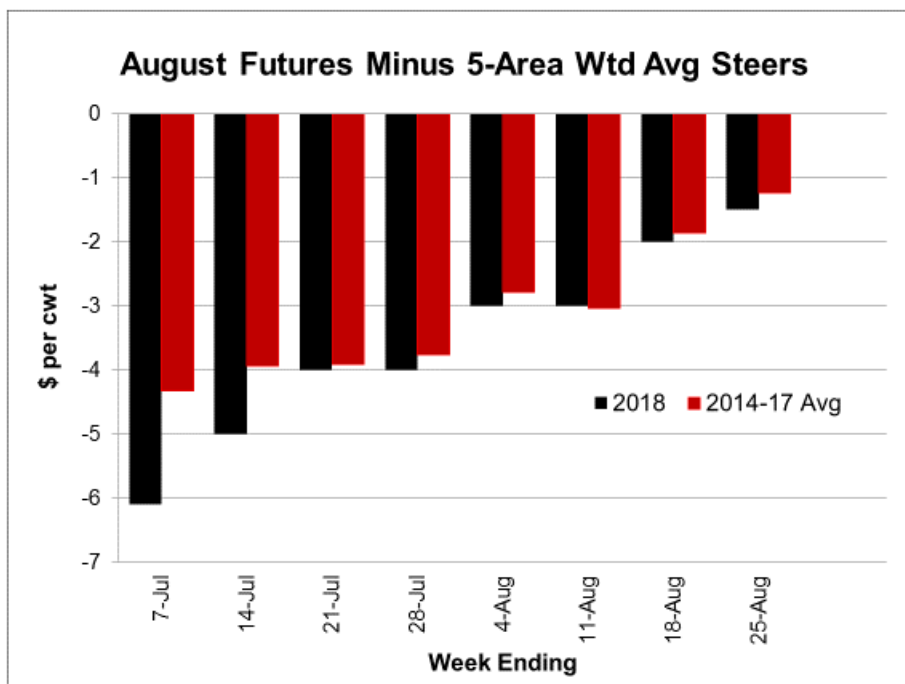
but I do not consider these to be critical—i.e., if they were taken out, it would not deliver a lethal blow to my expectations of the cash market; a drop below the big outside range/reversal of June 15 *would*. It's too late in the game for that to be happening if my forecasts are any good.

What sort of basis can we expect between now and the time the August futures contract expires? Well, the basis has reflected a bearish sentiment toward the August contract all year long, and I have no reason to think that this will change. Last week's settlements averaged \$6.10 per cwt below the Five Area Weighted Average Steer price, which was the second-steepest discount on record for the first week of July. I noticed that discounts in the August contract have become the norm in the July-August time frame over the last four years, which sets them apart from most other years. And so, the four-year history is as good a guide as any....with one caveat: theoretically, there is nothing in the delivery mechanism that limits the futures discount until the final days of contract life. As long as deliveries can be initiated only by the guy on the short side, this will always be the case. But that is another discussion for another time.

Anyway, here is the history of the futures-minus-cash difference beginning in the first week of July:

	7/7/18	7/14/18	7/21/18	7/28/18	8/4/18	8/11/18	8/18/18	8/25/18
2014	-5.38	-4.58	-6.78	-7.14	-4.12	-3.25	-4.70	-2.57
2015	-1.29	-1.69	-1.18	-.92	-2.58	-2.29	-1.33	-.74
2016	-7.74	-6.34	-4.69	-3.56	-2.34	-1.73	-2.85	-2.15
2017	-2.88	-3.15	-3.01	-3.45	-3.30	-4.41	-1.27	-.72
2018	-6.10							

Based on this history, I have some guesses about how the blank boxes might be filled:



It looks reasonable enough. It might be fair to say, then, that the board is pricing in a \$110 cash market this week. If I can believe my own forecasts of the cash cattle market, and if these basis projections

are accurate, then I should expect August futures to push through their resistance at \$108 next week, and reach \$116 by the third week of August. In any case, I'm pretty sure that I'll have to hold this position well into the month of August in order to realize my profit objective.

Apart from a close below \$100.40 in August cattle, the other signals that my cash market forecasts are veering off-course would be the usual suspects: a failure of packer margins to contract another \$50 per head or so by the end of July; a failure of the combined Choice/Select cutout value to form an unequivocal bottom by the same deadline; and/or a failure of steer and heifer kills to fall below 500,000 by the first week of August.

So far, none of the key variables in the equation has misbehaved. The spot packer margin index has narrowed more than \$100 per head from its June readings; the beef market has worked its way down at its expected pace and is showing traces of firmness in the right places (chuck and round cuts, trimmings, and grinds); and I don't have a real good idea where this week's steer and heifer kill will land, but it looks as though it will be 510,000-515,000. Until something goes wrong, the only reason I would have to do anything other than sit still would be to let go of my long position in the hopes of re-establishing at a lower price. The market has given me two good opportunities to do that already. There probably will be a third, but I'm not good at trading in and out of a position to try to enhance the ultimate outcome.

Forecasts:

	Jul*	Aug	Sep*	Oct	Nov*	Dec*
Avg Weekly Cattle Sltr	619,000	628,000	607,000	620,000	615,000	602,000
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	482,000	477,000	472,000
Year Ago	488,800	511,000	502,100	500,900	498,600	472,600
Avg Weekly Cow Sltr	113,000	120,000	122,000	128,000	129,000	122,000
Year Ago	104,400	111,000	111,200	117,800	116,700	111,600
Steer Carcass Weights	869	878	891	897	899	895
Year Ago	868.5	884.6	896.0	897.8	902.6	902.8
Avg Weekly Beef Prodn	499	510	497	509	507	497
Year Ago	487.6	517.9	515.8	518.4	519.2	495.3
Avg Cutout Value	\$205.00	\$210.50	\$209.50	\$208.50	\$207.50	\$204.00
Year Ago	\$209.64	\$196.81	\$192.17	\$197.04	\$205.15	\$199.67
5-Area Steers	\$112.50	\$117.50	\$116.50	\$118.00	\$121.50	\$118.50
Year Ago	\$118.41	\$110.72	\$106.83	\$112.08	\$121.03	\$120.00

**Includes holiday-shortened weeks*

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