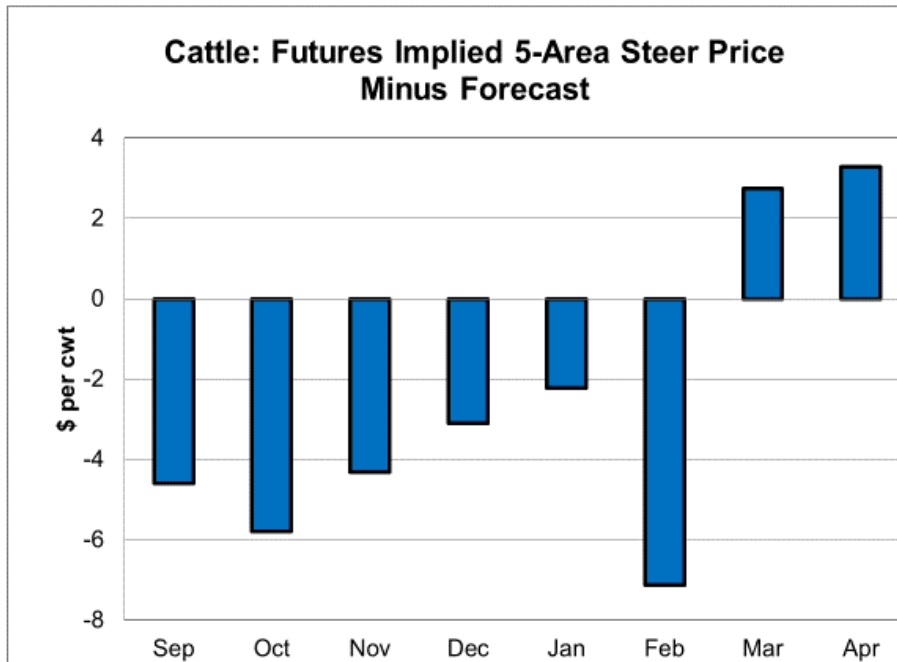


Trading Cattle

.... from a meat market perspective

A commentary by Kevin Bost

August 29, 2018

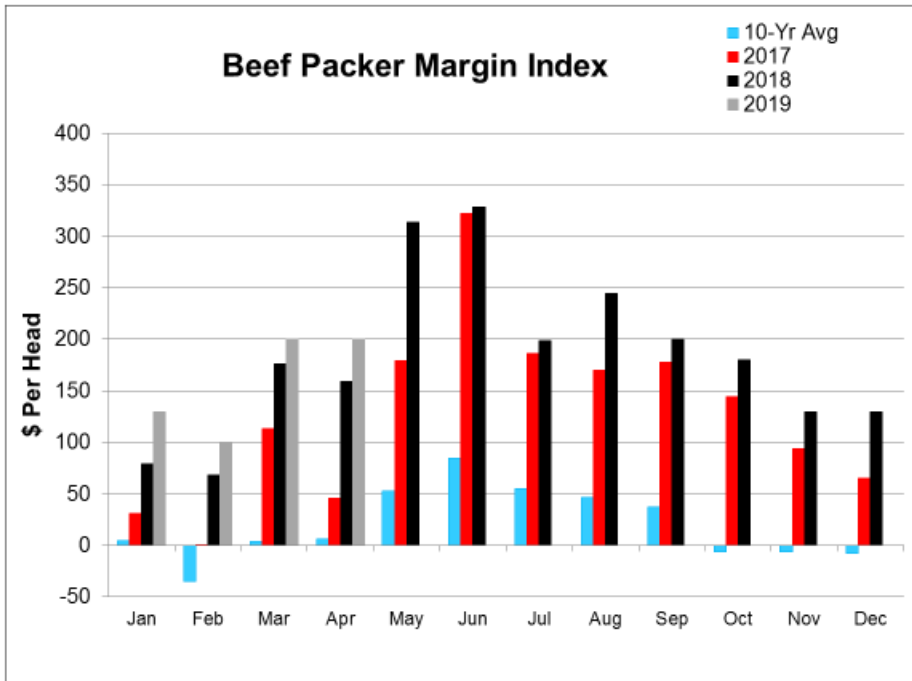


I have no commitment in the cattle market at present, having made a brief attempt at the long side of the October contract. I plan to make another.

Naturally, my interest in the long side of the

market is rooted in the picture above. The most objective assessment I can muster suggests that the October contract is worth about \$114 per cwt. True, I thought that the August contract would also trade up to that level. Obviously it did not, and it is easy to pinpoint the variable in the equation that “broke bad” on me: it was the packer margin. Whether that was a case of the futures market dragging the cash cattle market downward or a simple case of too many “front-end” cattle available, we’ll never know. But let’s look at the bearish possibilities in regard to packer margins down the road.

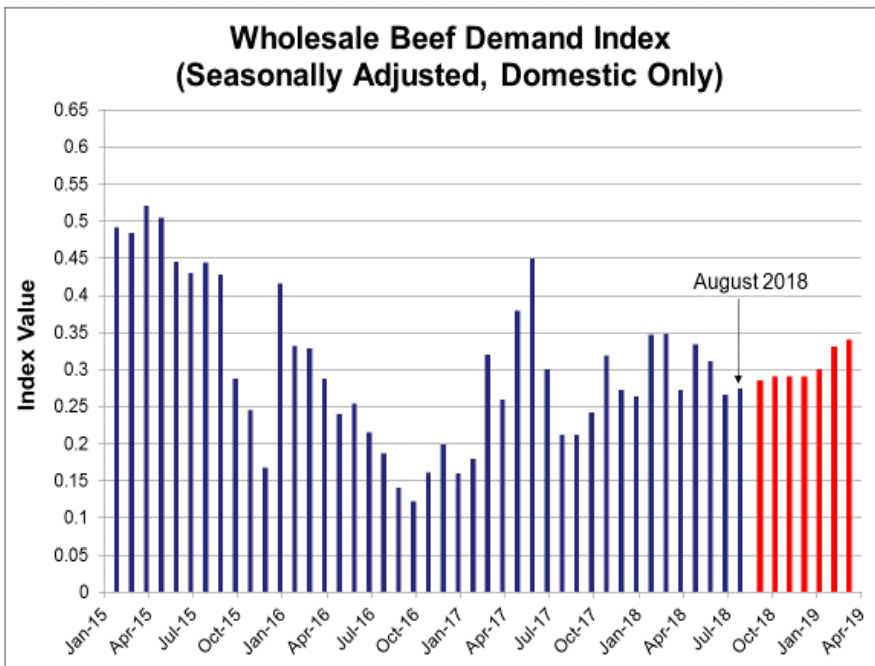
As I show on the next page, the spot packer margin index is going to wind up averaging nearly \$250 per head here in August, compared with \$170 a year ago. [All else being equal, that made the difference between a \$116 cash cattle market in August and the \$110 average that was realized.] Now, there is a pronounced seasonal tendency for spot packer margins to narrow significantly into the fall; that has occurred in 13 of the last 15 years. My projection of the packer margin index (a fairly generous one, I think) in October is \$180, still \$36 wider than a year earlier.



What if it were to remain right where it averaged in August? Unrealistic as it may be, the forecast of the cash cattle market would be lowered to \$110.

That assumes an average

Choice/Select cutout value of \$205.50 per cwt in October, which in turn assumes an average weekly steer and heifer kill of 492,000 and only a slight improvement in “core-level” demand from the cyclically low August reading, as I show below:



OK, then, what if the demand index were to drop back to its most recent low point, in July? In that case, the combined cutout would average \$202 and, with the packer margin index at \$245, the cash cattle market would be \$107.

There is no such thing as

a “worst-case” scenario in commodity trading, but this comes pretty close.

I will approach the October contract as a sideways market for the time being, bounded essentially by \$105 and \$112. I have two choices: one is to buy it near the low end of Monday's outside range/reversal, which was \$106.20, and use a close-only stop below that level; the other is to establish a small long position at that point and add to it as closely to \$105.00 as possible and place a close-only stop on the entire position below \$105.00. The risk on the latter will be acceptable if the position size is managed appropriately. My target with either option would be \$110.00, where the market left a tiny gap on the daily chart last Wednesday.

Forecasts:

	Sep*	Oct	Nov*	Dec*	Jan*	Feb
Avg Weekly Cattle Sltr	626,000	631,000	621,000	601,000	609,000	605,000
Year Ago	624,400	629,500	625,700	593,800	595,400	594,200
Avg Weekly Steer & Heifer Sltr	494,000	492,000	483,000	471,000	472,000	473,000
Year Ago	502,100	500,900	498,600	472,600	466,400	465,800
Avg Weekly Cow Sltr	121,000	128,000	129,000	122,000	128,000	123,000
Year Ago	111,200	117,800	116,700	111,600	120,400	119,500
Steer Carcass Weights	896	902	904	900	892	885
Year Ago	896.0	897.8	902.6	902.8	892.8	884.0
Avg Weekly Beef Prodn	517	522	516	500	502	498
Year Ago	515.8	518.4	519.2	495.3	492.5	488.1
Avg Cutout Value	\$204.50	\$205.50	\$203.50	\$202.50	\$211.00	\$209.50
Year Ago	\$192.17	\$197.04	\$205.15	\$199.67	\$206.72	\$212.70
5-Area Steers	\$112.00	\$114.00	\$116.50	\$116.00	\$121.00	\$122.50
Year Ago	\$106.83	\$112.08	\$121.03	\$120.00	\$123.36	\$127.65

**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.

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