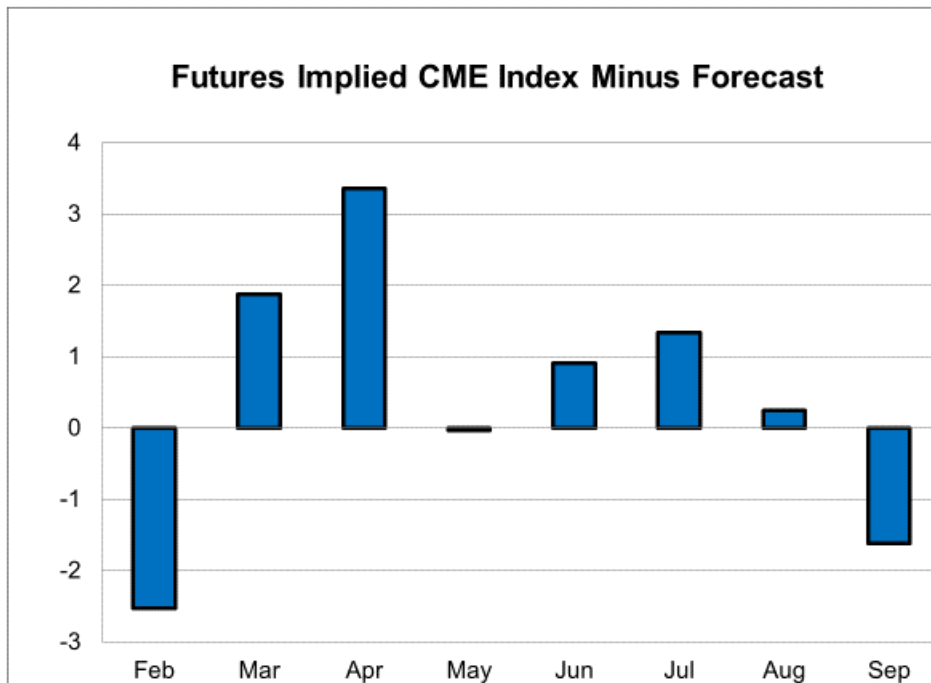


Trading Hogs

.... from a meat market perspective

A commentary by Kevin Bost

January 18, 2018



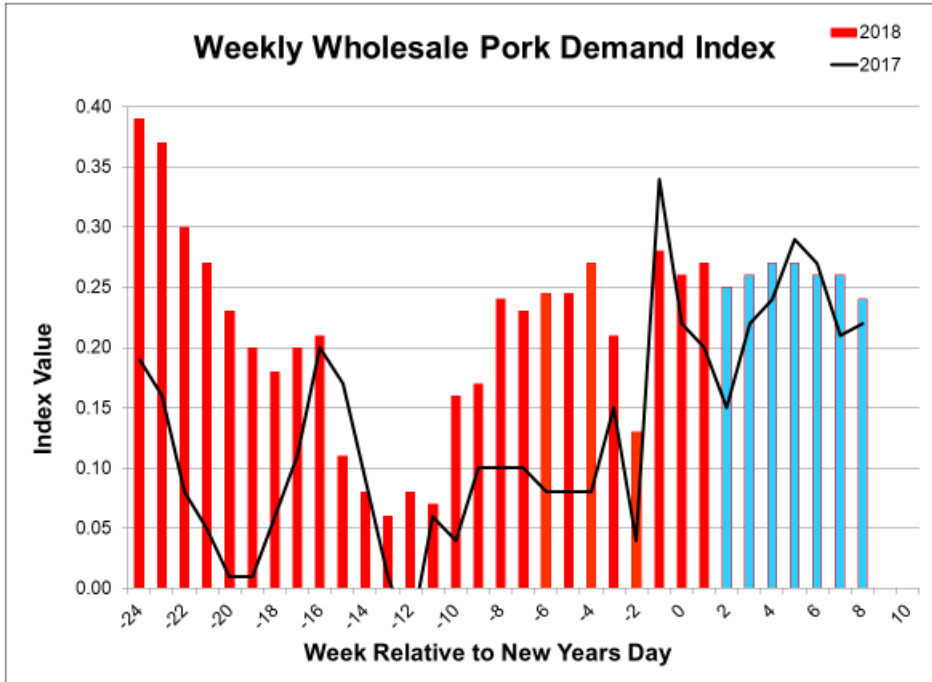
I am long of the February/April spread, with reason to think that it will continue to favor the nearby contract throughout its remaining life.

Based on the crude notion that the cash market will remain strong in the near term but wind up establishing a major high in February, I

am interested in the short side of February \$71 puts, as well as the short side of the April contract outright.

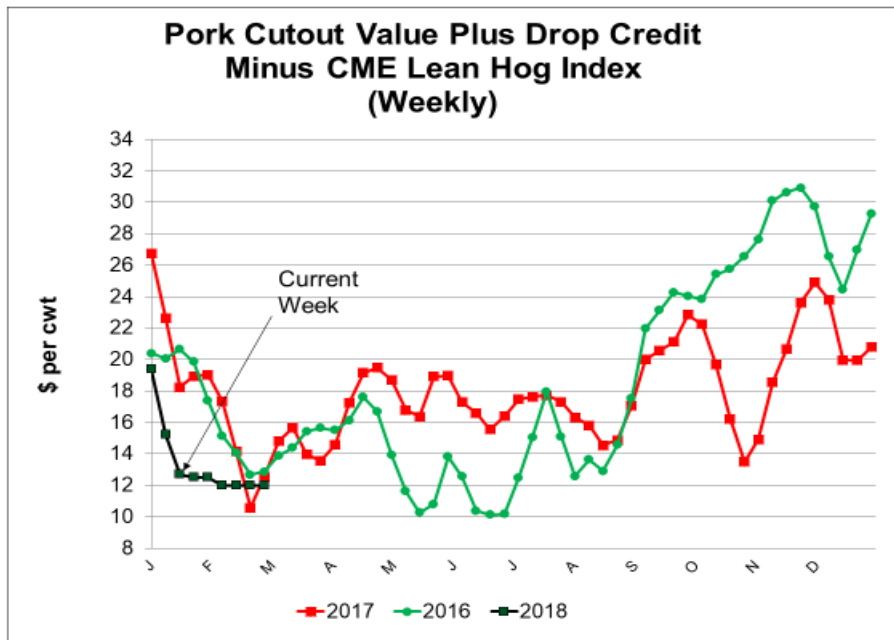
I cannot see anything on the horizon that would cause the cash market to veer from its current course. As best I can tell, hog slaughter will be declining for the next three weeks, into a practical February low of 2,370,000. Meanwhile, I cannot think of a good reason why wholesale pork demand would do anything seasonally odd in the near term. A "seasonally normal" path would be reflected by a seasonally-adjusted demand index which stays perfectly flat from this point forward. And demand has been pretty decent lately, as I show in the picture on the next page. In that picture, the first blue bar represents the current week, and the remaining blue bars represent my humble projections through the end of February

Anyway, when I combine that sort of production with seasonally normal changes in wholesale pork demand, the result is a cutout value of \$82.00-\$82.50 per cwt in mid-February, compared with yesterday's quote of \$80.95.



Packer margins, meanwhile, have dropped off a bit more sharply than I had anticipated. I show this in the second graph on this page. If the quoted gross packer margin remains essentially where it stands today, then an \$82.00-\$82.50 cutout

value would align with a CME Lean Hog Index of around \$75.50 in mid-February. But there is a distinct historical tendency for packer margins to shrink between now and then. If the quoted margin were to fall to, say, \$10 per cwt vs. this week's \$12.70, then the CME index would be closer to \$77.50 when the February contract expires. Am I suggesting that February hogs might ultimately be worth \$77.50? Yes, that's what I'm saying. By the way, the nearest resistance on the chart of the CME Index is the February 21, 2017 high of \$77.82 per cwt.



And so, even though a \$2.00 discount of the February contract to the April contract is a natural technical objective on the daily chart, I notice that there have been occasions on which the February contract traded at least equal to

the April, during the month of February—not many, only four times in the last 15 years—but it's not unprecedented.

For all the same reasons I just laid out, I am willing to sell \$71 February puts at \$1.00 per cwt or more. I am opting for the short put position because at this juncture it seems a bit aggressive to own both the bull spread *and* the outright long. I would prefer to add to the spread position instead.

As for the short April proposition, I am waiting for a convincing signal that the top is “in”. The market has become comfortable trading in a price range that not long ago it could not hold, and the major moving averages remain clearly, bullishly aligned. The primary trend remains upward. I will be impressed by a downtick (or two) in the CME Index, and I would be impressed by a downturn in pork belly prices—the Standard-Bearer of the pork market right now. Until such signals are delivered, I will avoid the short side.

Forecasts:

	Jan*	Feb	Mar	Apr	May*	Jun
Avg Weekly Hog Sltr	2,425,000	2,377,000	2,373,000	2,362,000	2,323,000	2,278,000
Year Ago	2,361,900	2,327,100	2,326,700	2,285,400	2,250,200	2,183,400
Avg Weekly Barrow & Gilt Sltr	2,358,000	2,310,000	2,305,000	2,295,000	2,255,000	2,210,000
Year Ago	2,297,700	2,262,400	2,260,900	2,220,200	2,185,200	2,117,200
Avg Weekly Sow Sltr	61,000	60,000	61,000	60,000	61,000	61,000
Year Ago	59,900	58,400	58,900	58,100	57,900	58,800
Cutout Value	\$80.50	\$82.00	\$79.00	\$80.00	\$85.50	\$89.50
Year Ago	\$80.18	\$84.08	\$80.20	\$74.86	\$84.92	\$97.04
CME Lean Hog Index	\$71.25	\$75.25	\$72.50	\$72.00	\$80.50	\$84.00
Year Ago	\$63.80	\$74.16	\$71.50	\$62.60	\$72.28	\$86.09

**Slaughter projections exclude holiday-shortened weeks*

Trading Hogs is published weekly by Procurement Strategies Inc., 99 Gromer Road, Elgin IL 60120. For subscription information, please contact Kevin Bost at (847) 212-7523 (cell), (224) 227-6281 (office) or Kevin_Bost@comcast.net; 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. 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.