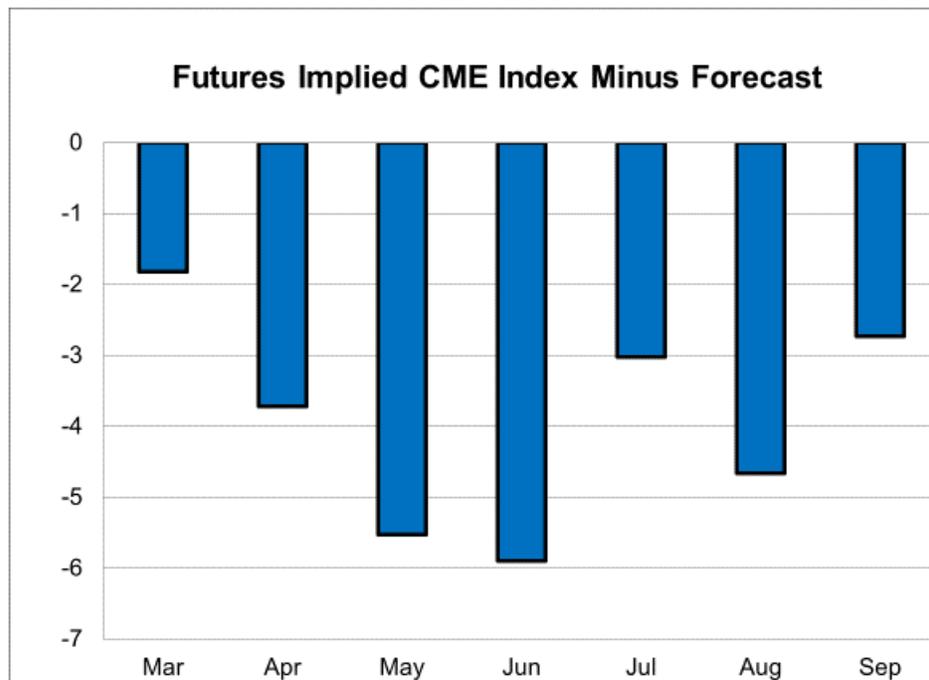


Trading Hogs

.... from a meat market perspective

A commentary by Kevin Bost

February 8, 2018



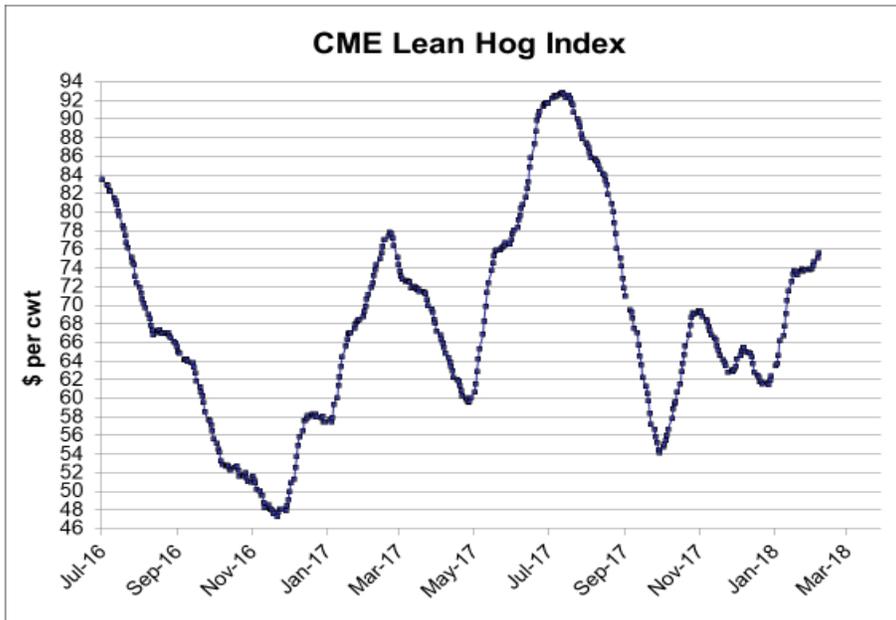
Trumping all else, the price action in the April, June, and July contracts is seriously bearish. It doesn't take a technical wizard to figure out that much. And so, I can approach this market only from the short side for the time being. An eventual move in April hogs down to

\$67 seems inevitable, now that a massive top formation has been completed. What to do, then?

Nothing right away. The board is obviously oversold, having come straight down 500 points in three trading sessions. An outright short position would have to be risked up to \$72.00 or higher, and at current trade levels, the risk-to-reward relationship does not justify a bet.... sort of like loading up on a "win" ticket at 3:5 odds. I just don't do it. I mention \$72.00 because a close back within last Friday's big outside range—which spanned from \$74.12 to \$71.67—would signal a test of the upper end of that range. My stop-loss trigger, therefore, will be placed at \$71.67 close-only. If \$67.00 is the downside target, then an entry point at \$70.50 would be needed in order to bring the potential profit:loss ratio above 2:1. That entry price makes sense from another angle, as \$70.62 was the previously major support level from which the market broke down.

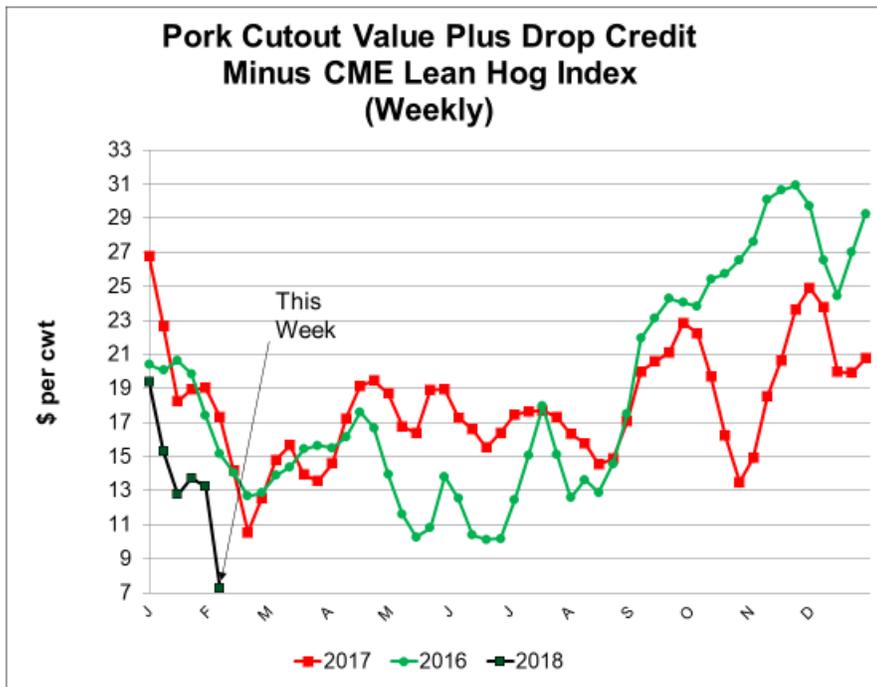
And then there is the picture above. Measured against the most objective cash price forecasts I can muster, the board is significantly undervalued at Wednesday's closing prices. Very seldom do I consider a short position when the market lies in "undervalued" territory. The technical signals must be overpowering in order to justify "jumping on the bandwagon". In this particular case, they are.

I am further encouraged to sell April hogs on a minor rebound because the “news” emanating from the cash market is likely to be negative for the next two to three weeks. Pork belly prices have begun a major, protracted correction, which means that the pork cutout value has registered a major top as well. The single-day Index value is peaking today at approximately \$76, and the nearest discernible support on the chart below stands at \$70.



There is a pretty good chance that it can get there before the end of the month. How so? It would require a continuation of the break in belly prices down to \$1.10 per pound, along with a slight widening of the packer margin. If the belly market trades at

\$1.10; lean trimmings and boneless picnics slip a few cents; and all else remains unchanged, then the cutout value will lose about \$4.50 per cwt from the current quote, down to about \$73.



Gross packer margins have collapsed this week, down to about \$6.50 per cwt as of yesterday. Applied to a cutout value of \$73, a margin of \$8 per cwt would result in a \$70 CME Index. It's not a far-fetched possibility.

But isn't there a long-side opportunity

somewhere in the works? At some point, yes. But this market needs plenty of “line”, and plenty of time for market sentiment to swing preponderously over to the bearish side. Perhaps that point is at \$66.35 in the April contract (I notice that there is a gap on the daily chart at that price) or around \$76.50 in the June contract. Among the major elements in the forecasting equation, pork demand holds the greatest downside risk. My assessment of “fair value” in the April contract assumes that it will be somewhat stronger in April than it was in the last three years; if it were to equal that of a year ago, then the CME Index would average \$67-\$69....

Forecasts:

	Feb	Mar	Apr	May*	Jun	Jul*
Avg Weekly Hog Sltr	2,357,000	2,363,000	2,362,000	2,323,000	2,278,000	2,291,000
Year Ago	2,327,100	2,326,700	2,285,400	2,250,200	2,183,400	2,211,300
Avg Weekly Barrow & Gilt Sltr	2,290,000	2,295,000	2,295,000	2,255,000	2,210,000	2,225,000
Year Ago	2,262,400	2,260,900	2,220,200	2,185,200	2,117,200	2,149,300
Avg Weekly Sow Sltr	60,000	61,000	60,000	61,000	61,000	59,000
Year Ago	58,400	58,900	58,100	57,900	58,800	55,000
Cutout Value	\$74.50	\$76.75	\$79.50	\$85.50	\$91.00	\$89.00
Year Ago	\$84.08	\$80.20	\$74.86	\$84.92	\$97.04	\$103.48
CME Lean Hog Index	\$71.25	\$70.00	\$73.00	\$80.50	\$85.50	\$83.50
Year Ago	\$74.16	\$71.50	\$62.60	\$72.28	\$86.09	\$91.47

**Slaughter projections exclude holiday-shortened weeks*

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