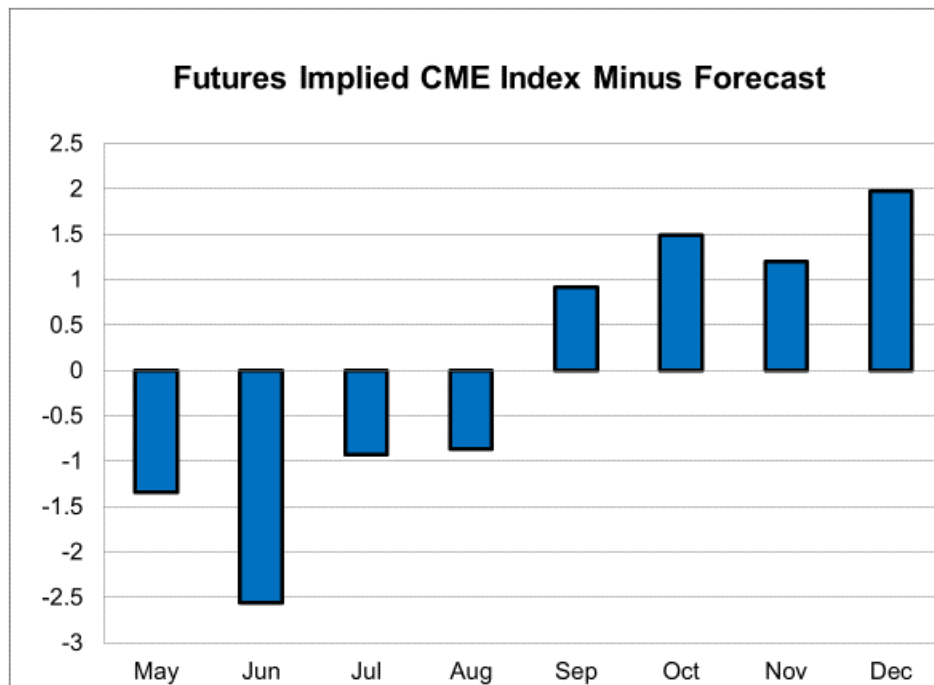


Trading Hogs

.... from a meat market perspective

A commentary by Kevin Bost

May 3, 2018



I remain long of the June / October spread, risking the trade down to two closes below \$7.70 (premium to the June) and targeting a move up to approximately \$12.00. I remind myself that in four of the last six years this spread was between \$11.50 and \$16.50 at the time the June

contract went off the board, and my humble assessment of "ultimate values" in the two contracts places them about \$14 apart. And so, what I'm asking from this spread is nothing wildly unusual.

June Hogs Minus October Hogs:



Otherwise, none of the 2018 hog contracts appears to be greatly over- or undervalued. There could still be a play on the long side of June hogs, though, if it is executed and managed carefully. This is no “home run” that we’re talking about here. My best guess at this point is that the CME Lean Hog Index will be trading around \$77 in the second week of June, and so this would be my upside objective. The stop-loss would have to be placed no higher than \$72.20 on a close-only basis. Prior to Monday, I was unwilling to trust any support level above the contract low of \$70.25; but after what looked like a trip down to the contract low last Friday, the downward momentum suddenly dried up.... which probably reflects a market composition that is leaning a bit too far to the short side. I also consider that if the June contract is indeed to work its way up to \$77 within the next six weeks, it probably should not again fall below \$72.20. OK, so if the upside objective is \$77.00 and the risk is down to \$72.20 (call it \$72.00), then the entry point of a long position must be \$73.50 or lower in order to bring the potential profit-to-loss ratio above 2:1.

I must mention that there is an enticing gap on the daily chart of June hogs at \$79.85. I generally place less trust in the filling of gaps in the nearby contracts than in more deferred options; but the July contract also has a conspicuous gap at \$79.87, and these two contracts tend to move more or less in tandem between now and early June.

A strong surge in the pork cutout value seems quite possible over the next three to four weeks, as long as hog slaughter behaves as it should—i.e., it does not significantly exceed the rates prescribed by USDA’s fall pig crop estimate. So far this spring, it has not. I am assuming, then, that weekly kills will hover near 2,350,000 between now and Memorial Day. Because hams, loins, and bellies are all situated at price levels that could readily be regarded as “cheap”, there is a good chance that demand for pork at the wholesale level will increase faster than the seasonal norm between now and the holiday. If the seasonally adjusted demand index simply returns to its early March standing, the cutout value will rise to \$80 per cwt by the end of May (today’s mid-day quote was \$69.55). In order to get there, we would have to see bone-in loins at \$1.10 per pound; hams at \$.62; and bellies at \$1.10, all else remaining unchanged.... a bit ambitious, perhaps, but in Memorial Day week of 2017, loins were trading at \$1.17; hams at \$.66; and bellies at \$1.47.

Meanwhile, gross packer margins have leveled out this week, and currently stand just above \$12 per cwt. If they remain there, then an \$80 cutout value would place the CME Lean Hog Index at \$73.... right about where I am willing to buy the June contract. I think it is safe to say that June futures will still be holding a premium at the end of May.

Forecasts:

	May*	Jun	Jul*	Aug	Sep*	Oct
Avg Weekly Hog Sltr	2,289,000	2,264,000	2,216,000	2,397,000	2,480,000	2,581,000
Year Ago	2,196,100	2,183,400	2,127,700	2,304,600	2,420,500	2,503,700
Avg Weekly Barrow & Gilt Sltr	2,222,000	2,195,000	2,150,000	2,330,000	2,410,000	2,510,000
Year Ago	2,133,800	2,117,200	2,068,800	2,241,600	2,357,500	2,436,800
Avg Weekly Sow Sltr	60,000	62,000	59,000	59,000	62,000	63,000
Year Ago	55,300	58,800	52,100	55,500	55,500	59,300
Cutout Value	\$76.50	\$85.50	\$86.00	\$87.00	\$78.00	\$76.00
Year Ago	\$84.92	\$97.04	\$103.48	\$91.67	\$77.89	\$74.51

CME Lean Hog Index	\$69.00	\$77.50	\$78.00	\$78.00	\$65.00	\$63.00
Year Ago	\$72.28	\$86.09	\$91.47	\$81.41	\$62.02	\$61.73

**Slaughter projections include holiday-shortened weeks*

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