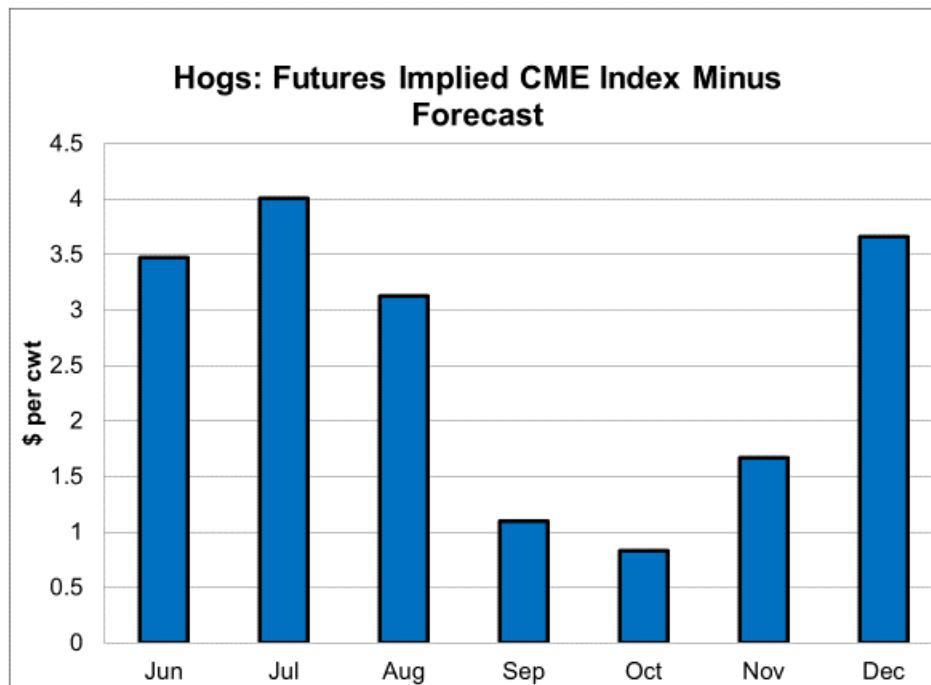


Trading Hogs

.... from a meat market perspective

A commentary by Kevin Bost

May 31, 2018



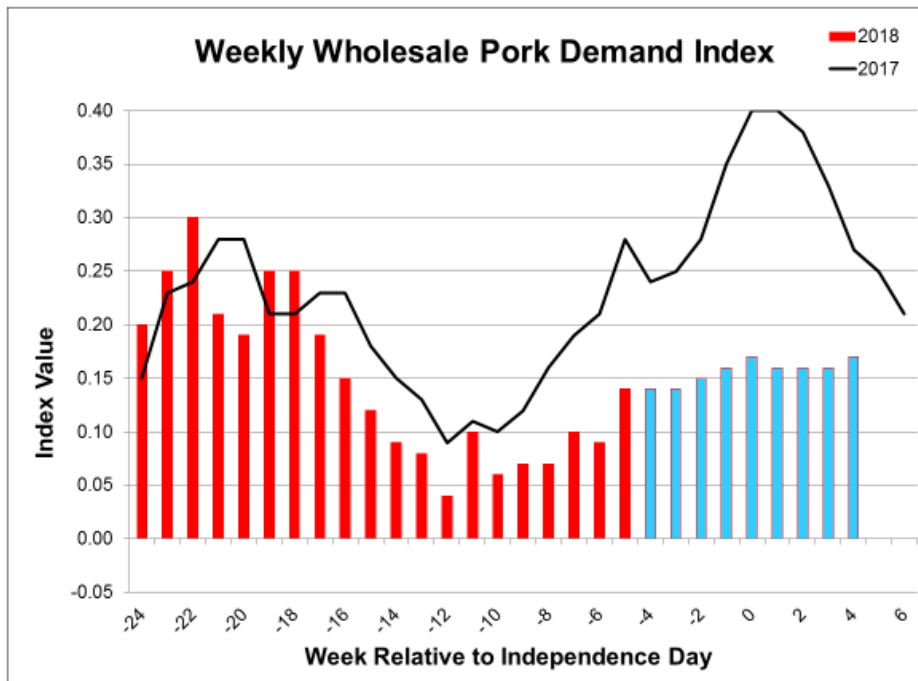
I currently hold a moderate position in the short August / long October spread. I took on this position as a proxy to an outright short-side bet in the August contract, since it appeared that I was not going to be able to sell August hogs with an acceptable risk: reward

ratio. That price would be approximately \$79.50 per cwt, from which a close-only stop at \$81.00 would make for a likely risk of 200 points and a profit potential of 500 points. [In case you're wondering, I have raised my sights a bit for the ultimate value of August futures, due to the apparent jump in wholesale pork demand this week. I'll come back to this subject in a minute.] Anyway, I intend to remove the long October leg of the spread if August hogs trade up to \$79.50. This, of course, would transform the spread into an outright short position.

In the meantime, I am retaining the bear spread with a target of \$11.00 (premium to the August) while risking two consecutive closes above \$14.27. I expect this spread to move in my favor if the August contract has a downward bias—which it will, if my assessment of ultimate value is correct. Conversely, I would not expect the August contract to lose ground against the deferred contracts if the cash hog market were to have more “gas in the tank” than I think it does.

I am somewhat impressed by the upturn in the wholesale pork demand index this week, which I show in the picture on the next page. I have been cautiously watching for *some* sign of a meaningful recovery, since the market has been in a demand-building mode for some time now. Perhaps this is it. But even if this turns out to be a “flash in the pan”, I have to give it the benefit of the doubt....and so I have raised my projection of pork demand in the summer months.

In the graph below, the final red bar represents the current week, which is the fifth week prior to Independence Day; the blue bars represent my humble projections for the period beginning next week and extending through the final week of July:



Under this assumption, along with weekly kills that average 2,277,000 in June; 2,212,000 in July (including the holiday week); and 2,395,000 in August—in other words, taking USDA’s winter pig crop estimate at face value—the pork cutout value is headed for a

peak of about \$85 per cwt, and in that case, the CME Lean Hog Index should be topping out at about \$77. As best I can tell, today’s Index value stands at approximately \$70.25. By the way, the \$7 per cwt premium that the August contract holds to the CME Index today would be the third largest on record for the first week of June. [In 2014, a year that had practically nothing in common with conditions this year, it stood at \$17; and in 1999, the inaugural year of the carcass weight-based futures contract, it was \$10.]

If pork demand is to be much stronger or hog supplies much smaller than I anticipate, then the market will tell me....and I will respect its opinion.

There are simply not any great trading opportunities in the hog market, at least none that I am able to perceive at the moment. And so, I am aiming for relatively small profits and commensurately small risks.

I cannot leave without saying something about gaps on the daily charts. There is one in the October contract at \$67.35, which seems a mile away....but then, so did the gap at \$79.87 in the July contract just a little more than a week ago, and it was filled yesterday. With short speculators accounting for an unusually large percentage of total open interest in the hog market—and with commercial positions leaning toward the bullish side of the boat—it may not require any monumental development in the cash market to push October hogs up to that mark. At that point, I would become quite interested in a short-side bet.

Forecasts:

	Jun	Jul*	Aug	Sep*	Oct	Nov*
Avg Weekly Hog Sltr	2,277,000	2,212,000	2,395,000	2,476,000	2,577,000	2,608,000
Year Ago	2,183,400	2,127,700	2,304,600	2,420,500	2,503,700	2,422,100
Avg Weekly Barrow & Gilt Sltr	2,210,000	2,150,000	2,330,000	2,410,000	2,510,000	2,540,000
Year Ago	2,117,200	2,068,800	2,241,600	2,357,500	2,436,800	2,357,600
Avg Weekly Sow Sltr	60,000	55,000	57,000	58,000	59,000	60,000
Year Ago	58,800	52,100	55,500	55,500	59,300	57,300
Cutout Value	\$81.50	\$83.00	\$83.50	\$78.00	\$75.50	\$72.00
Year Ago	\$97.04	\$103.48	\$91.67	\$77.89	\$74.51	\$81.18
CME Lean Hog Index	\$73.50	\$74.50	\$74.00	\$64.00	\$62.50	\$57.00
Year Ago	\$86.09	\$91.47	\$81.41	\$62.02	\$61.73	\$65.88

**Slaughter projections include 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 or Kevin_Bost@comcast.net; or visit our website at www.procurementstrategiesinc.com.

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