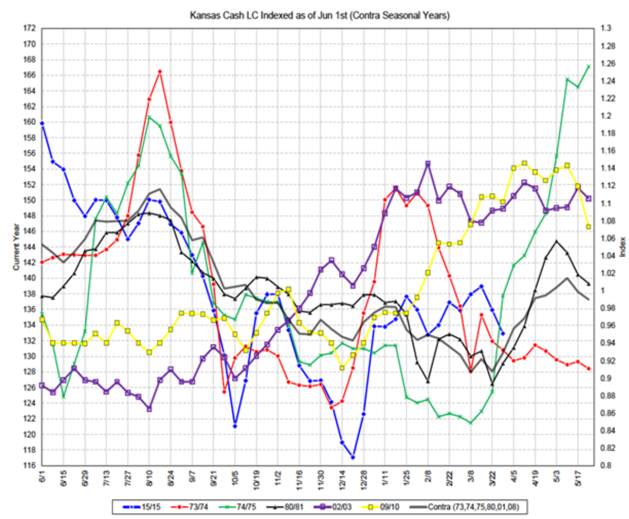
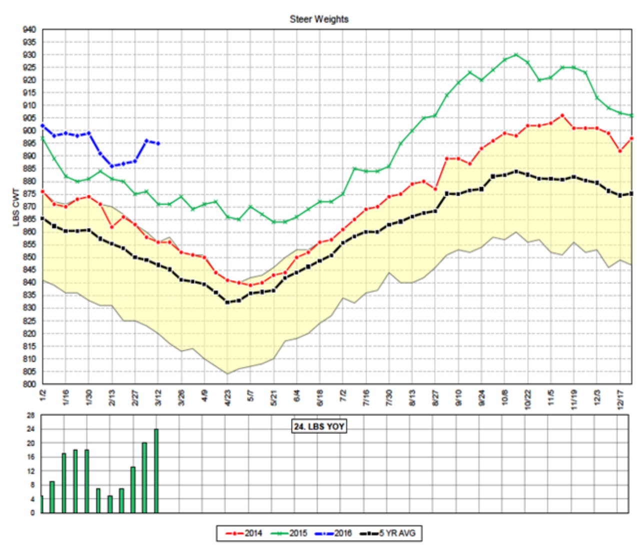
M & R Capital LLC

March 2016 Monthly Commentary

March was a first half bull and last half bearish environment with cash and futures both breaking $4.00 from beginning to end. Technical as well as index fund buyers were seen early in the month but gave way to packer kill reductions and lower beef prices mid to late month as they set up their month end contract (input costs) pricing for the coming months supply. As a result of this, all of the early month buyers were seen as aggressive sellers the last week of the month. The commercial long that was seen reducing positions during late February and early March reengaged the market. This would seem to be an effort to lock in record forward margins or roughly $200 per head given the boards discount to cash and seasonal increase in beef demand that should follow in the coming weeks and months.

- March's cash cattle prices moved from $138 to $134.
- Futures started at $137 rallied to $140+ then sold off to end the month at $133.
- Basis moved from par to +$1 or +$2.
- Beef prices moved -$4 from $217 to $212. Retailers continue to do a good job buying beef on dips and will use this to lower prices. Forward sales continue to increase by packers. Grinds and middle steak cuts are now a value as we start the demand season. Ground beef specifically is under priced.
- Slaughter levels are running a bit larger than expected as cattle are being pulled ahead from May and June.
- US Exports will continue to grow as the year unfolds as the affects of Australia continue to shorten the world supply. Imports into the US will continue to decline for the same reason.
- Weather has been and is good. Combine this with cheap feed and it will counter balance the decline in weights that will come from pulling cattle ahead. Weights will continue to decline into May and should be under a year ago by the end of this summer.
- China is starting to increase purchasing patterns for US pork vs last year adding select items that were not previously included in last year purchases.





Trading futures contracts and commodity options involves substantial risk of loss, and thus is not appropriate for all investors. Investors should carefully consider the inherent risks of such an investment in light of their financial condition.

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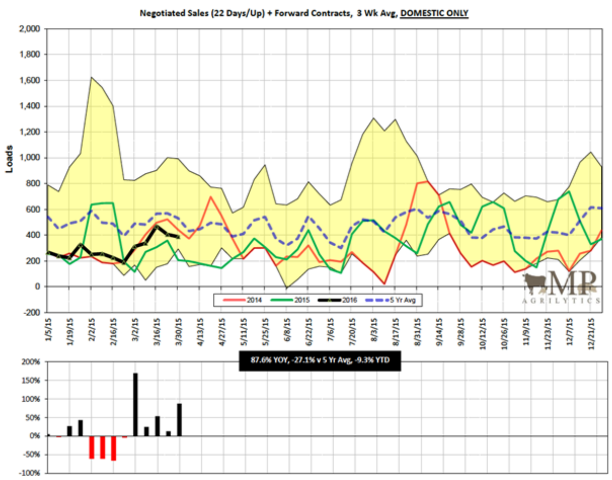
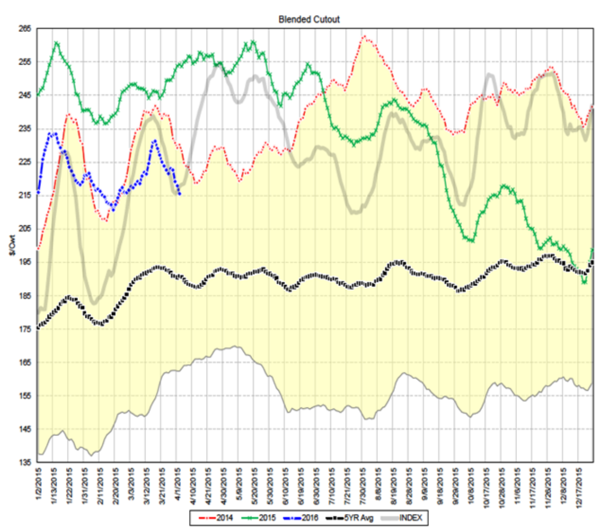


Cash prices started March at $137-$138 and ended $133. Beef prices dropped comparably to the $212 area. Beef prices are expected to bottom by the middle of April as demand gets better, weather improves, and supplies fail to increase as much as expected. In a world where nothing seems to be normal anymore, a normal rally in prices from here would imply a retest of the $225 area into May and June. This implies cash cattle prices at roughly $145 assuming zero margins and $135 assuming $100/hd margins. Seasonal average for margins in April is roughly -$20/hd to zero and for May it ranges between zero and +$75/hd.

What is interesting about these normal margins is that when you calculate the normalized beef price for the coming 8 weeks and then that of the June futures, the forward margin is in excess of $200/hd. This would be an all time record and something that will certainly not remain. When you inject record margins into any market you expect things will change. Therefore, we need to look at what will change in order to pull that number back down into something statistically likely. When we do that we come up with a beef market that can range from $210 lows to $235 highs and a cash cattle prices that can range from $130 on its lows to $145 at its highs. April futures are at $132 and June futures are at $121. Both of which seem to be too cheap by comparison.

The market is currently very busy pulling cattle ahead in order to move them out of the feedyard now at $135 vs waiting for the futures market at $124-$120. This tells us that we are starting to move cattle out of a period where the market is expecting to see a lot of them. Despite pulling cattle ahead, packers are still buying cattle for quick ship delivery—in some cases for next day arrival. Supplies are very tight in the spot, estimated to be roughly 10,000 hd short of current harvest needs per week. Forward beef sales continue to grow. Adding all this up and we conclude that futures prices are over estimating the impact of the pending supplies this summer especially now that we are moving them out of that projected spot. At a minimum the market will remain in a choppy trading range. Weights have not fallen off as much as we expected but now that cattle are being pulled ahead we expect the USDA data, which lags reality by 2 weeks, will show us a continued decline over the coming month of new data points. Even though supplies are being pulled ahead we anticipate a much smaller than normal seasonal increase in supplies is expected to be seen over the coming 45 days.



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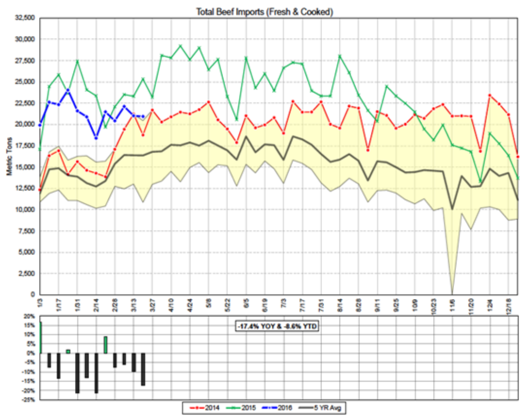
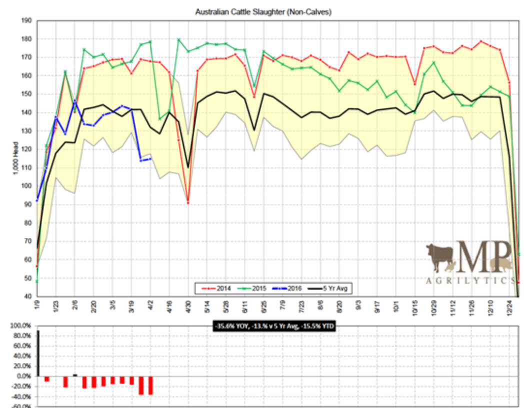
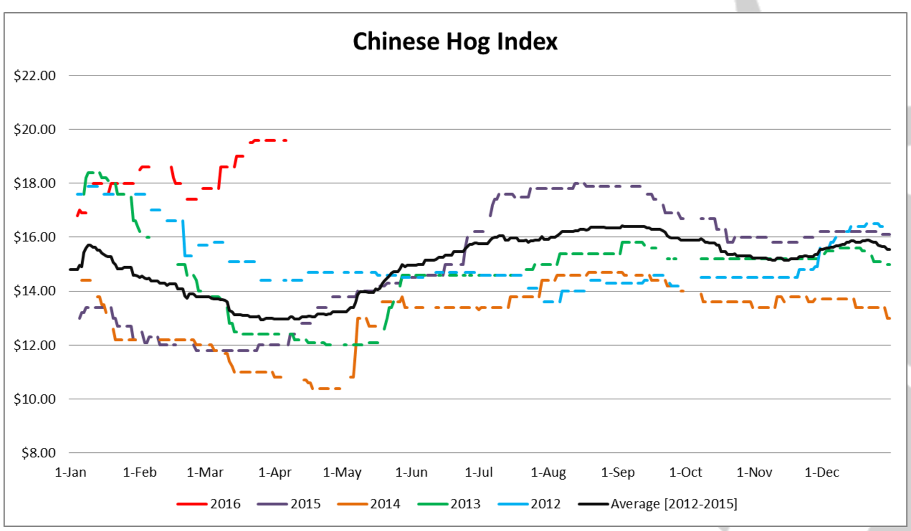




The Australian markets continue to evolve as we have expected with harvest rates being approximately 18% below a year ago in March. Trends look to be running around -20% or greater through the summer. Imports, as a result, are running lock step with this decline in supply posting between -10% and 20% from time to time. Imports are expected to continue very short of a year ago as we move through the summer.

We would like to make mention of Chinese pork prices this month as it is becoming something of a concern. Especially when we account for Australian beef supplies being very short of last year's marks we need to factor in better export demand to fix this situation. Tight supplies have pushed up pig and pork prices while feed costs decline. China's sow inventory has declined for 30 consecutive months according to JCI data. As of the end of March domestic pig prices have increased some 60% from last year. Pork prices are up 37% and piglet prices are +113%. This is leading some insiders to estimate that Chinese imports will increase 20% or more to over 1 million MT in 2016. This is the equivalent of 14 million live pigs. Everyone knows live pigs don't export but it will be meat cuts like hams or carcasses that they take. As an example, items are starting to move today that we have not previously sold to them. In this case whole heads are moving instead of just ham production. In the chart below you can see that the current Chinese index is well above recent years and the five year averages.



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Despite over estimating the objective for the rally effort during the month we were able to maintain a positive performance for the month in a period where prices actually closed lower. Our positions were able to weather the storm of the decline due to in part because of some options and in part because of spreads. Both of these risk management focuses paid off and protected us from what would have otherwise been a negative month. The market is evolving slower than we expected to see and clearly this is a function of pulling cattle ahead. If this continues it will mean some big things for the early summer's supplies getting moved around and something we will continue to monitor. It should be no surprise to understand that we remain bullish into the spring and early summer. Despite what you will read from others, we do not believe that the market will be going to zero. Like we did in March, you should expect that our trading activity will increase as we move forward as the markets like to go through many fits and starts and trading these actions is important. We will also be looking to shift our strategies as we look forward to trade against the potential increase in placements that should be coming now that pen conditions and weather allow feedyards to start placing cattle at profitable levels. This may come from spreads and this may come in the form of options.

The data is starting to tell us things are moving around for the future. But while feeders rush to pull cattle ahead this could create lots of confusion as to where those cattle actually reside. Fixing the spring supplies short fall is something that is still very difficult and any effort to do so will pull head away from June. Placements were up 10% in February and are up again in March but they will likely be down in April. Keep in mind this year we have 1 extra day in each month as compared to 2015. This accounts for roughly 4% of the comparable supply when you are looking to build weekly supply forecasts. Demand will get better into the spring and summer supplies shouldn't be consistently over a year ago until we can get into later summer months. Australia is in and will continue to be short of supplies all year.

Regards,

Scott Shepard

4/7/2016

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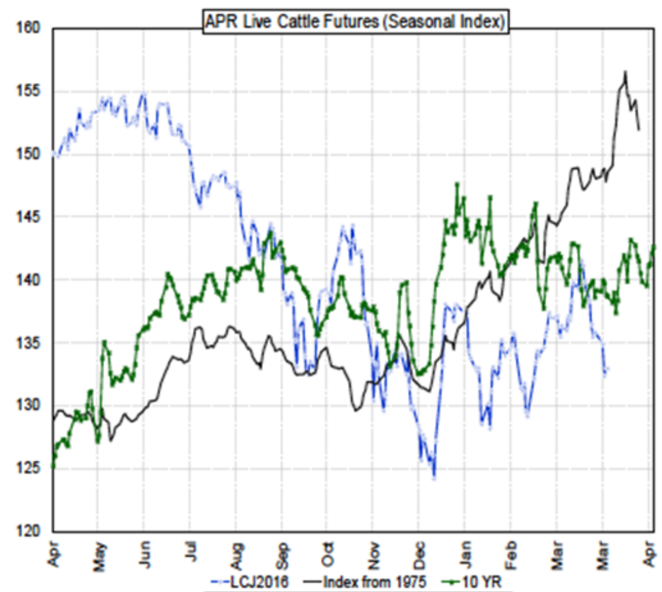

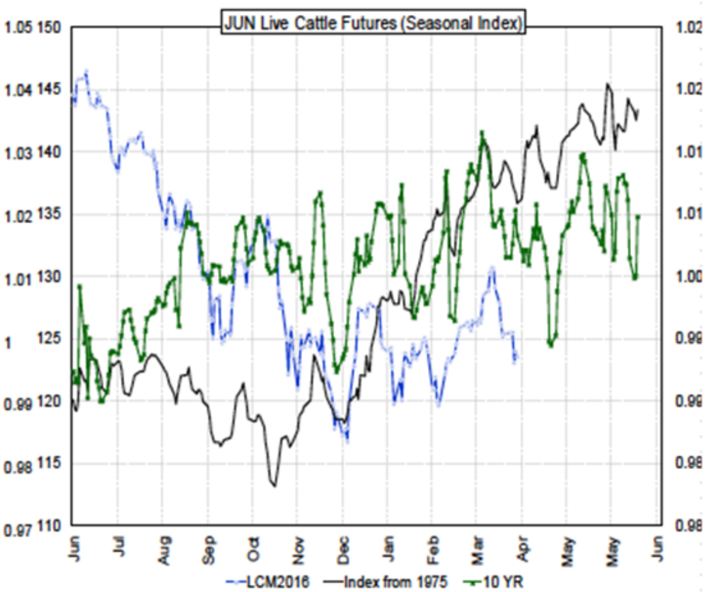

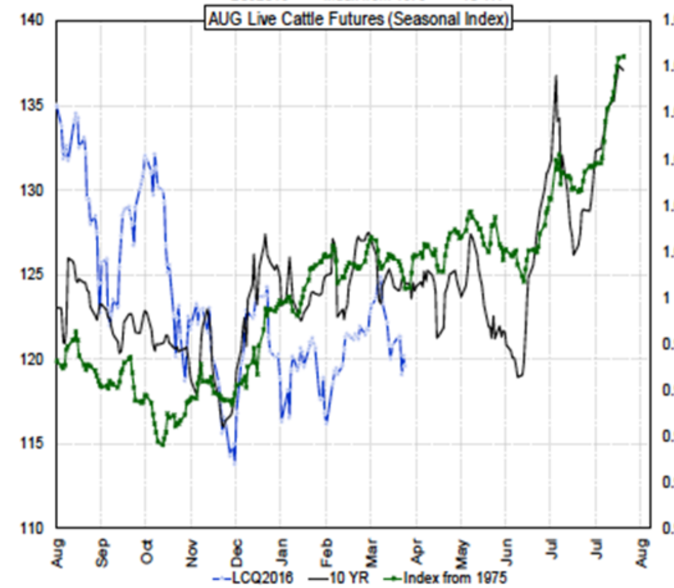

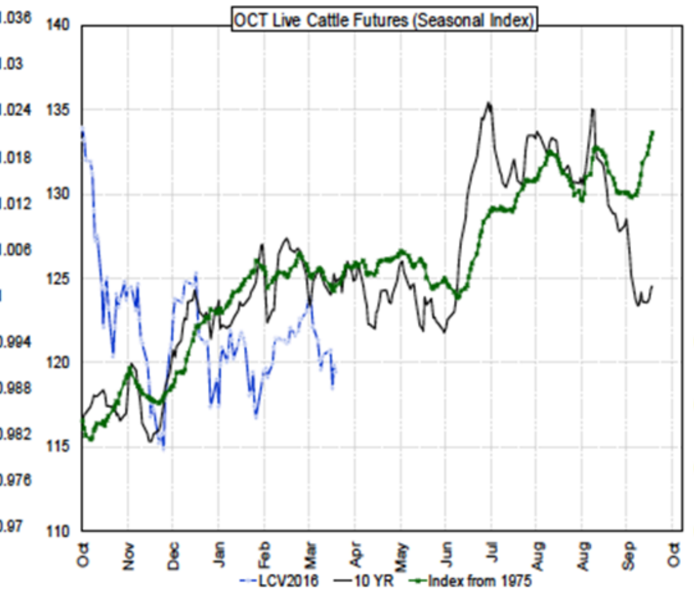

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