M & R Capital LLC

January 2017 Monthly Commentary

Notes of interest on prices:

	Week Ending 4-Feb		Week Ending 31-Dec
Kansas Cash Trade	119.00	1.00	118.00
Blended Beef Price	190.67	-7.42	198.09
February Futures	116.90	0.85	116.05

- Cash cattle prices advanced all throughout January before settling back towards steady at month end. Increased packer demand early in the month followed by decreased packer demand at month end was the reason for prices easing back. Live supplies remain tight seasonally, and packer harvest rates seem to be the only thing keeping prices from moving back in the lower $120s.
- Beef prices eroded throughout the month as packers continue to want to kill more than the available supply and certainly more than the seasonally poor demand that always plagues early to mid February. We need to watch exports like a hawk as they have been VERY strong. If buyers are buying ahead based on political fears surrounding NAFTA uncertainly and potential tariffs we need to understand this implication looking into the spring and summer when supplies start increasing again. While we are expecting prices to top out in February we believe the industries current patterns of over killing the available supply in January and the extreme current-ness of the feedyards means that prices may not yet be ready to stop moving higher.
- Packer margins have corrected lower as they seasonally do and are currently running around +$35/hd. Beef prices, however, feel heavy as we look into the poor demand that always happens in February. The packers breakeven with beef prices at a $190 blended beef price is roughly $122.
- We said last month that at $118, things have hit our base line forecasts. Since then the board went up just over $121 and broke back to just under $115 while cash ranged $118-$123. The board's discount to cash assumes that more cattle will be coming in 2017 as the cattle on feed reports and cattle inventory reports predict. However, the cattle seem to be coming this summer while spot supplies remain tighter than expected and supplies still muddy in the north. As a result a choppy trade or more movement in spreads could be seen. The USD has collapsed taking away a month and a half of gains all in three weeks time.
- Placement levels have increased in November, December, and in January estimated to be up another 10% or more. As a result, the January 1st Cattle On Feed will be back up over a year ago and pretty close to 101% YOY. Supplies still remain on the lowest end of historical comparisons for beginning inventories while cattle placements being added will be coming this summer.
- Imports continue to be down running 17% under a year ago for a 3 week average. The percent of imports being grinding materials is the smallest to start the year in the entire data set at -25% (3 wk avg). Australia remains weak at -41% (3 wk avg) but strength from Mexico at +32% (3 wk avg) and Brazil at +59% (3 wk avg) is making up ground in recent weeks. By comparison Australia's imports are almost the same as Mexico's with Mexico almost twice what they were two years ago while Australia is 50% of what they were 2 years ago. Export shipments remain strong at +24% over a year ago with outstanding sales yet to ship a shocking 30% over a year ago. Japan, China, and Mexico are the standouts. The US is expected to be a net exporter for most of 2017 and certainly for all of 2018.

Upcoming Data and S&D Thoughts:

- The long index and speculative roll will be the largest we have seen in over 3 years. This will affect the February contract especially if the packers reduce their demand in the coming weeks.
- The next Cattle On Feed report is expected to post another strong placement figure at +10%. This has us on the defensive looking for a correction in prices still. With total Cattle On Feed at 101% of a year ago, we have to be conservative in our forecasts.
- Spot supplies of cattle will continue to be small through February but are now starting to show that we are placing good numbers of cattle for next summer. However, we shouldn't expect placements to grow beyond March which means December forward supplies are not likely to match up.
- We have to be watching any political affects of NAFTA. First, would be if exports are strong today because buyers are buying 6 months of inventory in these recent 3 months. Second, would be to remember that 3% of the total US beef production curve comes form Mexico in the form of feeder cattle.

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- There are two smaller plants coming on line later this month and early this spring. One in Canada and one in Idaho. This means that cattle should be moving from Nebraska to the Northwest this spring more than normal. Also, Canadian supplies remain very tight and we need to monitor that situation.
- Weather has been a bad issue with mud and yields but this should be cleaning up in the coming week with a little sun and wind.
- We still see the average slaughter availability ranging in the 575,000 hd area for February. We will look at April, June, or August contracts to play the larger placement data.
- The long index and speculative roll will be the largest we have seen in over 3 years. They have to move some from April to June but the largest affect is likely to be the June and August contracts back to the October and December contracts this spring. Inflation is going to be a hot button for the speculative and index community as they firmly believe in a weaker USD and higher interest rates pulling ALL commodities higher in 2017.
- A disturbing trend has been put into action with certain packers shying away from the Holstein breed based on a large retailers shift in demand. This has a very large percentage of this supply going to two packers and reducing their demand for live supplies in general. We will monitor this situation for impacts on near term prices as well as the impact to future supply patterns. The larger affect will likely come this summer.
- There is also a labor shortage fear with more beef as well as pork plants coming online in 2017.

Expectations and Comments:

Now that the market has seen its mean reversion we will focus on a correction in price and trade in the near term. The index fund rebalancing and roll will be excessive. We wanted to get bear spread for this but did not due to year end volatility concerns. This is something we will look into as we start the new year. We believe the index funds have bought all their rebalancing needs and will merely focus on rolling a bigger number throughout the roll period in early January. This will be followed by the largest fund rolling of longs we have seen in over two years. As a result, it will be most likely that bear spreads rule the trade for the early part of the year. If kills are reduced to match supply with demand we will fall back towards the $110 area. Shorts have come out of ALL of their miscalculated positions since we accelerated up towards $118. Commercials are now the big short in the market. Speculators putting on new longs have increased the funds position up to a record 100,000 contracts. We still view cash as a $105-$120 item into early 2017. We will begin to test the bearish waters of pricing as well as bear spreads to start out the year. Hog prices have hit all objectives and are now moving into over priced areas. As a result, we will test the bearish waters in that market as well as it approached $72 in April and another over $80 in June. Bear spreads are likely the best way to trade this market.

Regards,

Scott Shepard
February 7th, 2017

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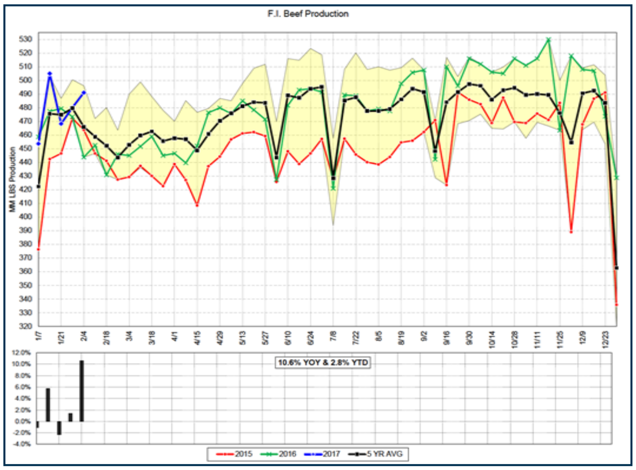

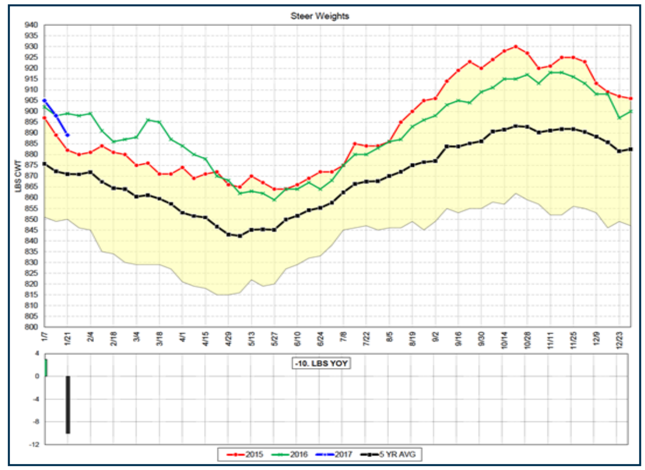

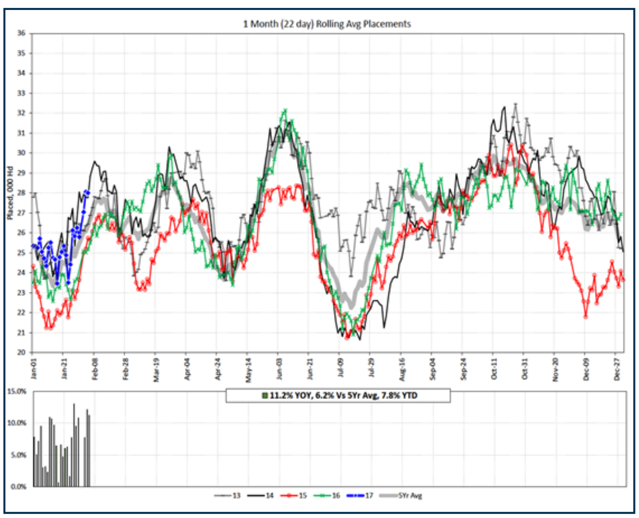

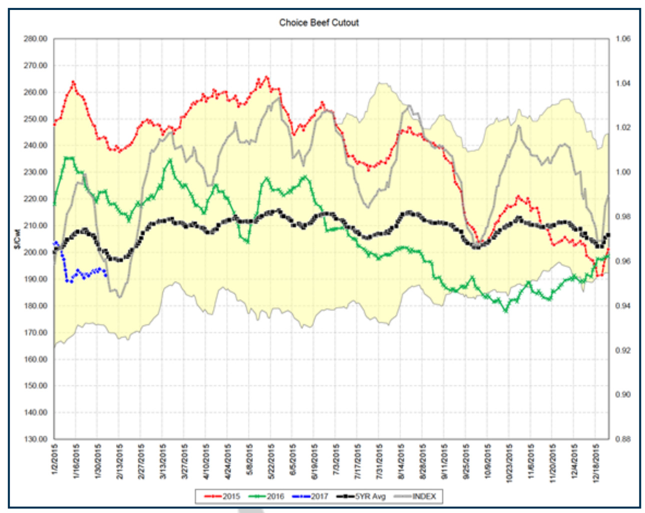

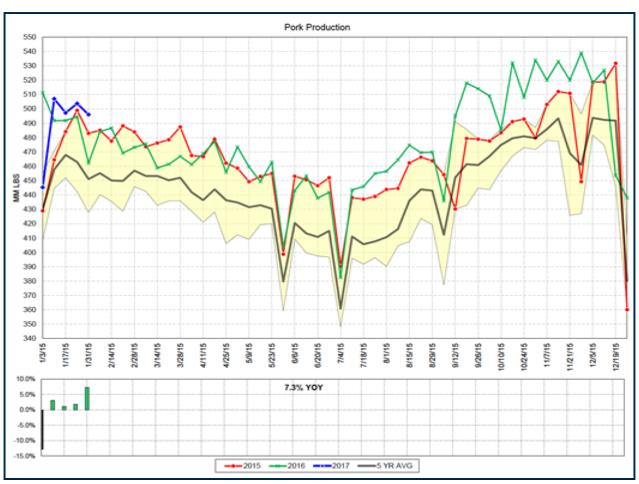

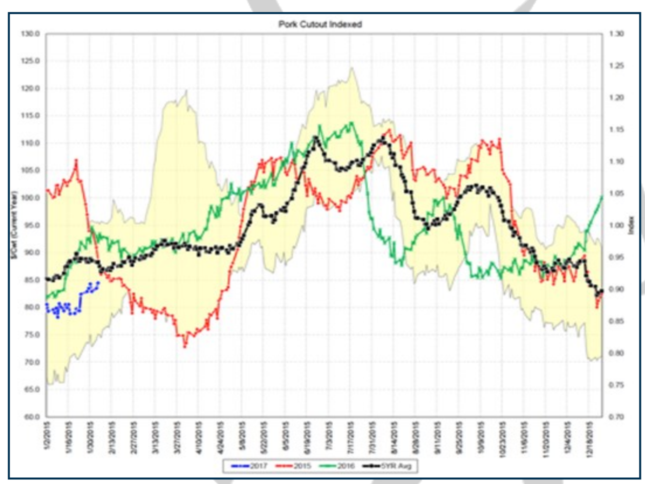

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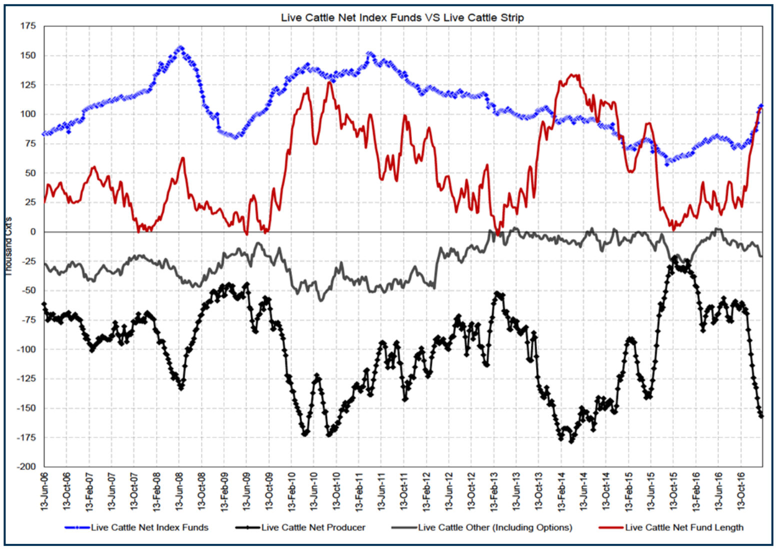

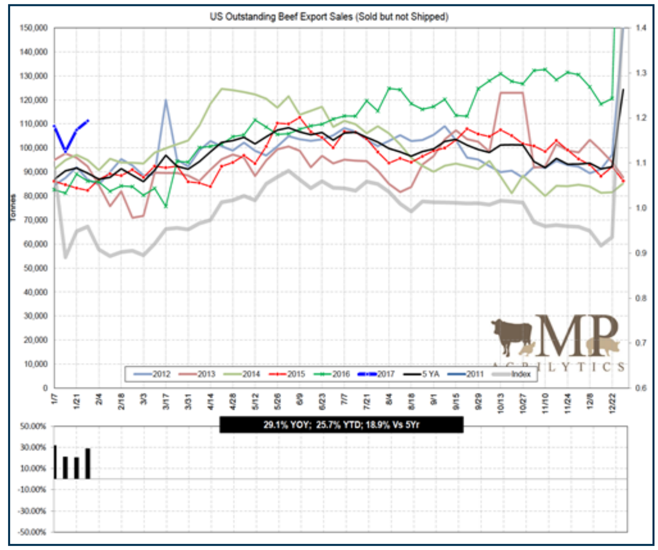

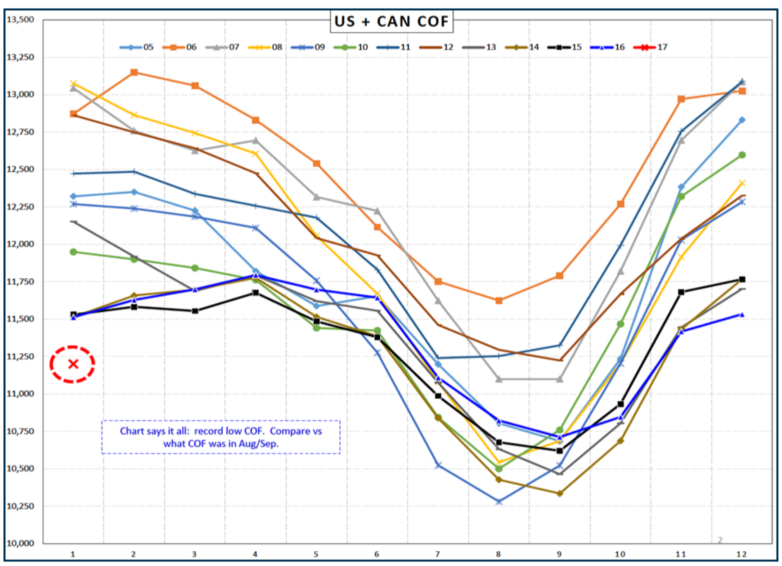

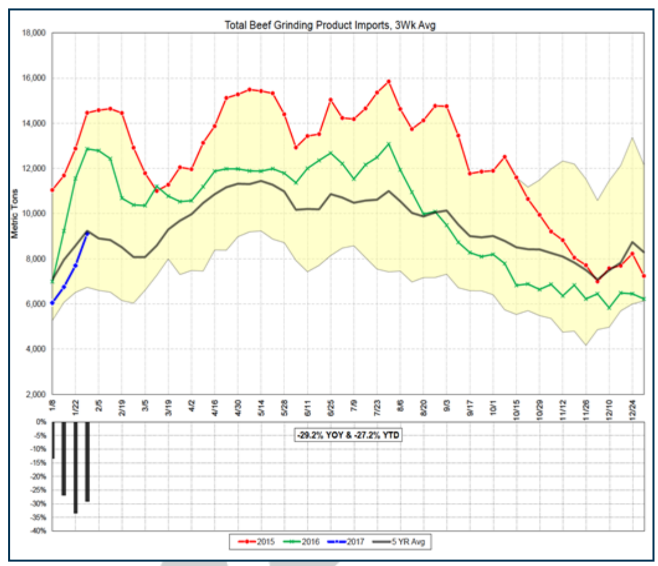

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