May 2017 Monthly Commentary

Monthly Recap:

	Week Ending 3-Jun		Week Ending 30-Apr
Kansas Cash Trade	137.00	0.70	136.30
Blended Beef Price	231.40	16.67	214.73
June Futures	129.00	8.95	120.05

- The month of May was troubling for a few reasons. I can assure you I am working on fixing a few items to insure that we do not have to endure the pullbacks we saw this past month. During the month volatility increased almost 3 times more than we have seen in the past. As such it is important that the program look to utilize optionality on both ends of the market. We did not have this in place to start the month, as we were deterred by option premiums. What was troubling this month is that spreads acted like outright spot markets as they moved greatly. Spreads have always been utilized to mitigate risk, but it did not help us enough this past month. We first saw this when the front end contracts scrambled higher while the deferred months remained steady, and in other cases where the deferred months were actually lower in the session(s). We are looking back at past indicators and overlaying today's new *"mayhem index"* which is giving us a profile for spillage. This will help us wait cautiously in order to pounce at the right time. It has become **very clear** in the wake of May's unwarranted price actions that we must employ immense measures in order to trade these current markets.
- Cash cattle prices started the month at $137-$140 then dropped to $130-$132 leading into the smaller Memorial Day holiday harvest schedules. They closed out the month at $137 immediately following the return from the holiday. At face value it seemed like one or two packers bought cattle in the forward and spot markets leaving another behind in the dust.
- Beef prices moved up into the holiday demand period as you would expect. However, prices have failed to correct despite many expectations that they would. Demand has been better than expected and many retailers are now short bought looking into their reduced July and August plans. The price of beef is at the 2nd highest price in history. Despite being at prices that have crushed demand in the past, things seem to be holding on better than expected. An all-time record price for rib-eyes and 50% beef trimmings are two items that have out performed everyone's expectations.
- Placement rates have been much stronger than expected with March and April at +11% and May looking very similar at +10% to +12%. Feedyards are full and will continue to focus on basis and marketing these supplies. December through April placements have been +835,000 hd higher than 2016. Cattle On Feed is growing rapidly from a 5 year low to a 5 year high in 6 months. We have a record change in supply from Q1 to summer supply.
- Weights remain lower but have seasonally bottomed. We expect them to gradually increase through the summer and peak in the fall. Weights should remain about 15 lbs. under a year ago in 2017.
- The futures markets have become extremely volatile and liquidity has become increasingly more challenging. As previously mentioned, we have decided to reduce exposures to spreads, options, and smaller outright positions until market dynamics can adjust. Placement patterns point towards more supplies (6% more) laying in the late part of June, all of July and August time frame with less coming as we enter into the end of the year and early 2018. This would point to the ideas that the value of the late 2017 and early 2018 supplies should be worth much more than 2017's later summer supplies. Yet the market is pricing in the opposite.

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Supply and Demand Factors:

- Spot supplies of cattle will be larger with weekly harvest rates likely to be around 620,000 head for all of June, and 630,000 head for July and August starting the week of June 5th. Margins are very strong at the packer level and negative at the retail level. As a result retailers are only buying short term and are not extending prices while packers are looking to extend prices.
- June through July will find ample supplies. With inventories being so current, the front-end supply of market ready cattle is manageable. Basis will remain strong. Look for prices to trend lower as the market moves through the larger supplies and seasonally softer demand.
- August through October will have above year ago levels of inventory due to the much larger placement patterns we discussed above. Seasonally, beef usage is soft in the heart of the summer. Large protein supplies are also a concern especially from pork.
- Seasonally, we should find about a 20% break in prices from the spring highs to the late summer/fall lows. This means $140-$110 should be a range we expect to trade. However, after an all-time record rally in prices from the 2016 lows there is a risk that 2017s break could be larger than expected.

Chinese Imports Announcement:

- Details surrounding US exports to China are expected to be released in early June. Regulations are expected to include traceability, hormone, and synthetic vs natural implant restrictions. Because of these restrictions this is expected to raise prices substantially vs the product they are currently importing from other countries. View these restrictions as a “Whole Foods” type of product, effectively pricing out the viability of American beef. Interesting enough is that this same trade deal allows China to import chicken into the US—yet this is not being discussed.

Thank you to our friends at MP Agrilytics for their data and charts.

Regards,

Scott Shepard
June 5, 2017

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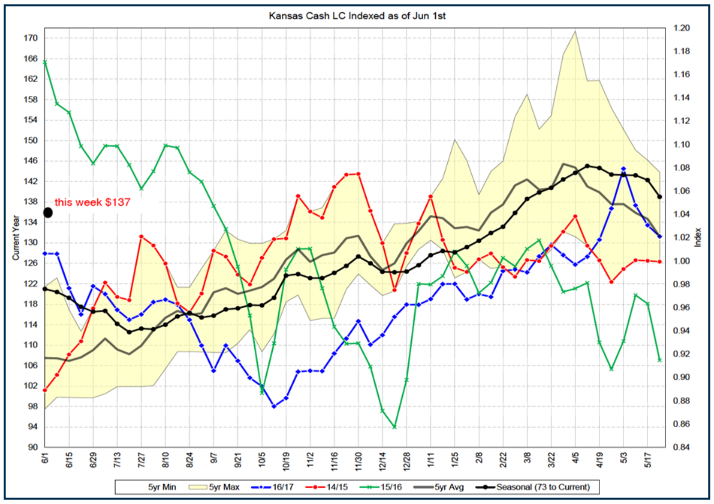

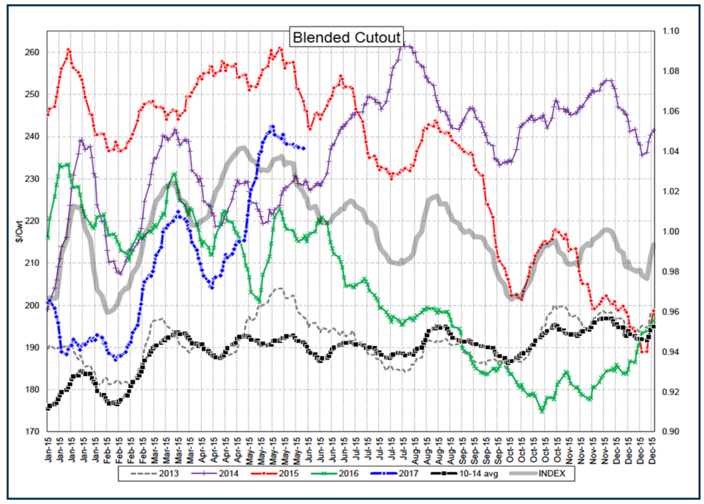

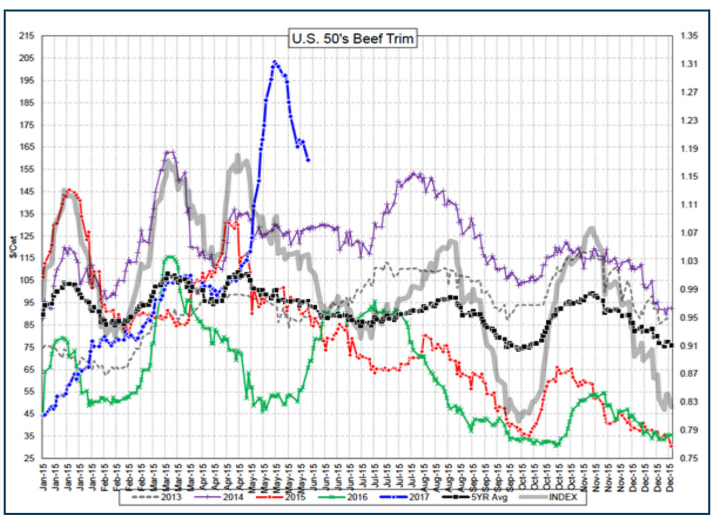

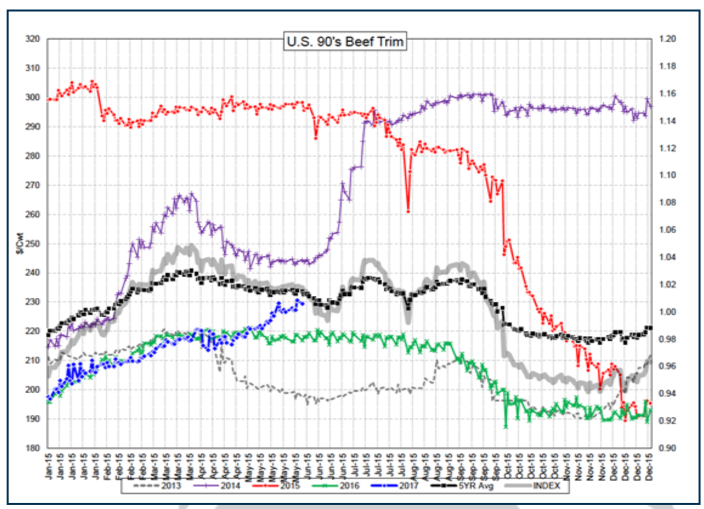

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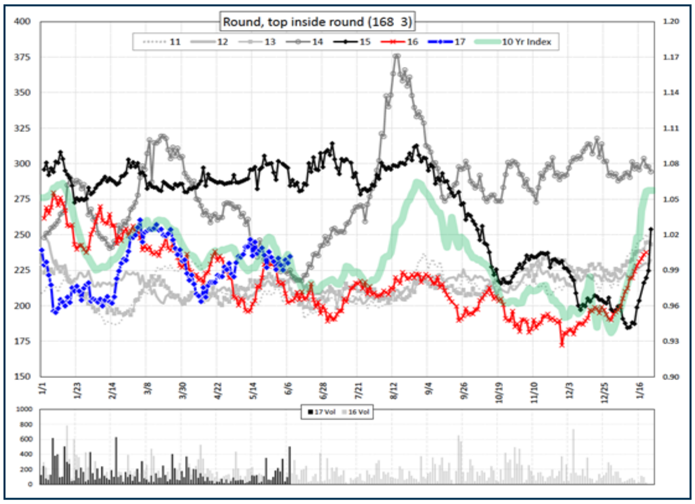

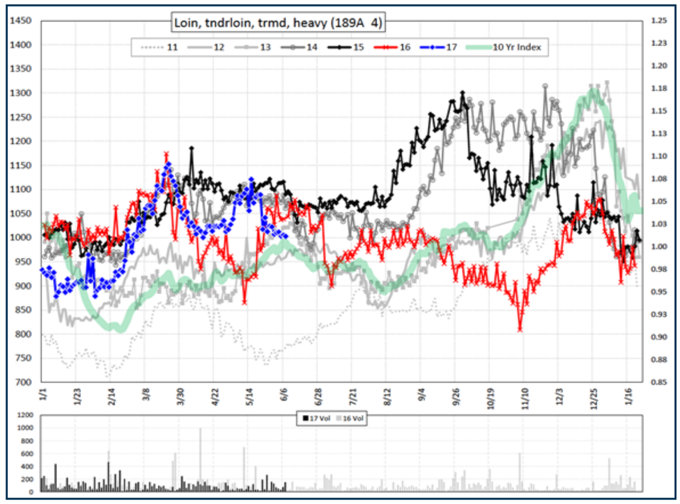

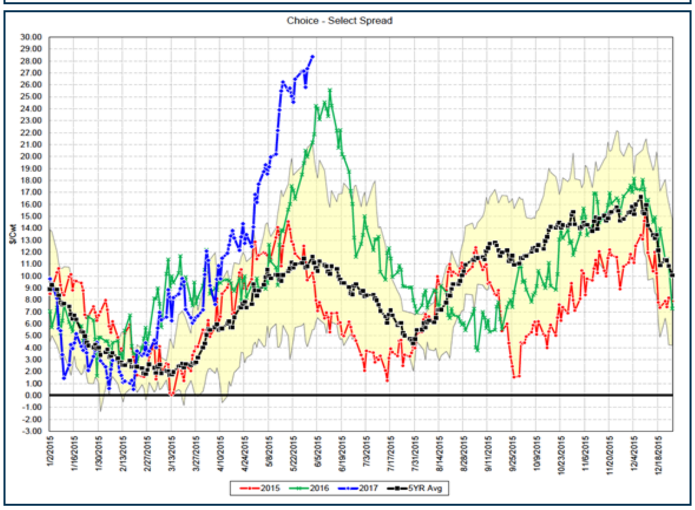

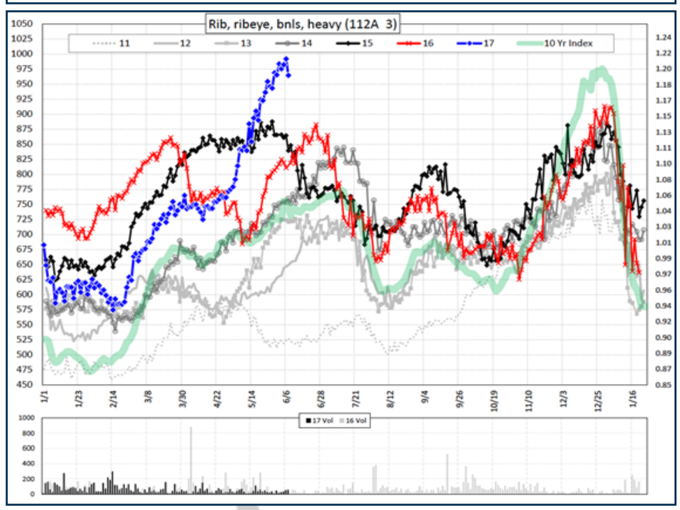

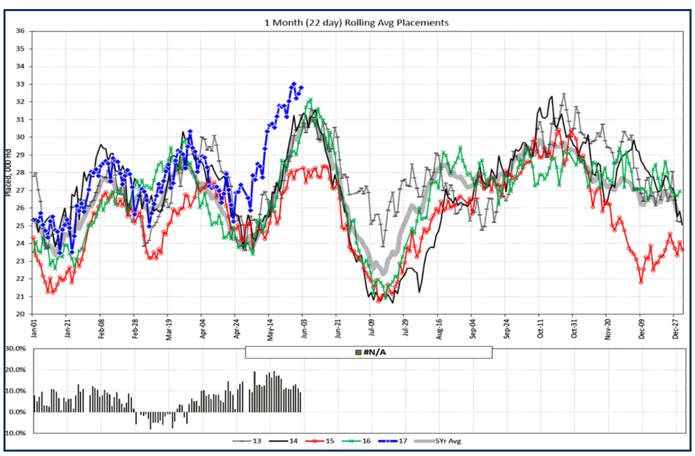

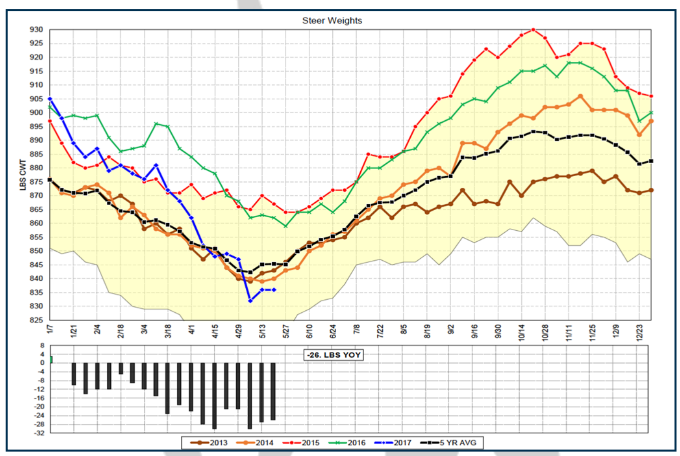

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