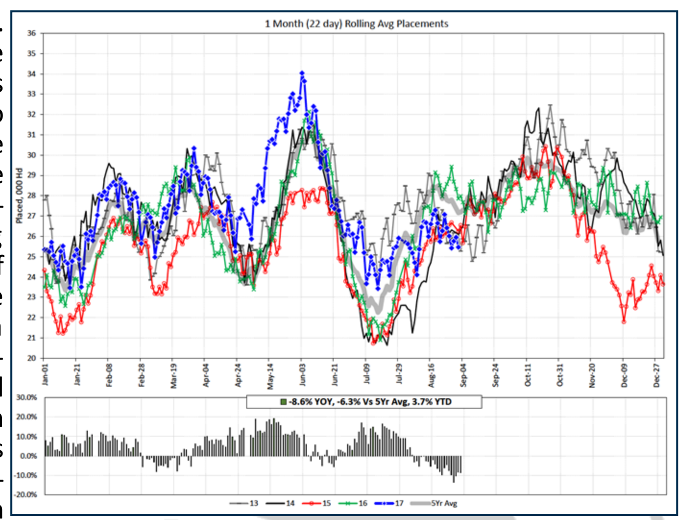
August 2017 Monthly Commentary

- Cash cattle prices started the month at $117 and eroded through the month down to $105. Prices moved lower based on the cattle feeders desire to move cattle early this summer instead of carrying them into the fall like they did in 2016. Their desire to sell with the very strong basis early in the month gave them an extra $50-$70/hd of encouragement. However, by the end of the month this encouragement was gone as basis moved from +$4 to -$1. This shift is even greater when looking into December at -$4 and February at -$8. Remember when futures were all $10 or more under cash? This told cattle feeders to market cattle ahead at a record pace this summer, which they did. Now with futures at a premium that selling pace has stopped and should mark our seasonal lows with this late August level at $105. Lighter placement patterns and better demand is expected to lift prices from here forward. The only question is from where? 2017 has been a big year for pulling cattle marketings as well as feeder cattle placements ahead.

	Week Ending 2-Sep		Week Ending 29-Jul
Kansas Cash Trade	105.00	-12.50	117.50
Blended Beef Price	191.07	-10.45	201.52
October	105.25	-7.17	112.42

- Beef prices continued to move lower finding no seasonal increase into Labor Day. The unexpected affects of Hurricane Harvey on Houston and larger harvest rates kept prices depressed. This has affectively increased demand with retail margins record large and features aggressive across the country. Prices are the lowest they have been since last fall with retail features prices in spots of the country even lower than last year's. Amazon/Whole Foods announced they were lowering prices for a laundry list of items including ground beef by some 30%-40%. Long hedging activity against the futures and forward long term purchases by end users surged late in the month. Export bookings and forward purchases data moved out to an all-time record high level. Demand is strong at these levels so this should imply that beef prices have bottomed and will begin their seasonal climb from here into holiday trade.

- Placement rates in July were less than expected at approx. 1.6M/hd while the marketing rate was at or just over the placement rate at 1.7M/hd. Total Cattle On Feed supplies posted at 104.3% or 1% less that most were expecting to see from USDA. However, what is interesting is that since we have been marketing so many cattle ahead of schedule this year because of basis that when you take the upcoming August placement rates at -10% and add the marketing rate at +5% you have total cattle on feed at only 1.8% as of Sept 1st. If you repeat that trend thru September then we will have Oct 1st Cattle On feed supplies at 99%-100% of a year ago. This will show us an all time record low placement rate for August and one of the quickest drops in total On Feed supplies that we have seen in a long time. When you combine this aggressive drop in total on feed supplies with the aggressive growth in demand you have the makings for the potential for a much stronger market than most are thinking today and certainly than the futures are pricing. Everyone is expecting a very large feeder run this fall but what if we have pulled a lot of these cattle ahead already? What if competition is greater than the market is expecting? Today's cash market is at $105 and with the next replacement costs being $115 it doesn't make sense to aggressively market ahead any longer. The cheapest feeders in the country are now the ones in the feedyard. February averaged $120 in 2017 and April averaged $128, this compares to 2018 that are both priced at $114.



9047 Poplar Avenue, Suite 101 • Germantown, TN 38138

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M & R Capital LLC

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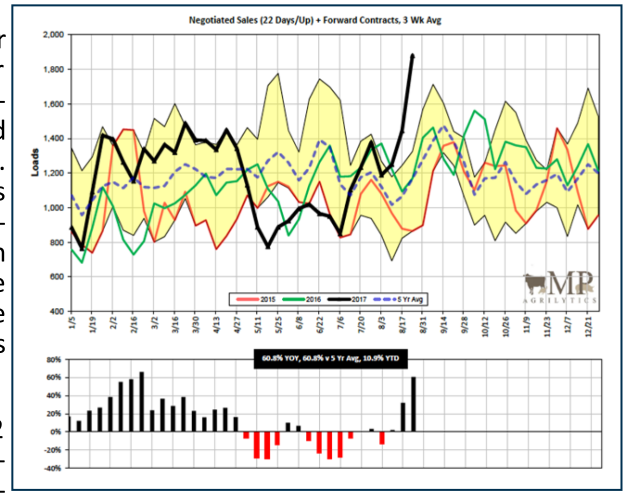
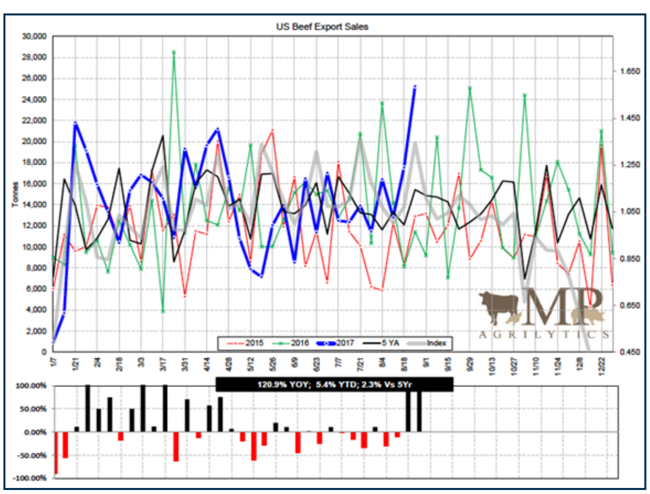


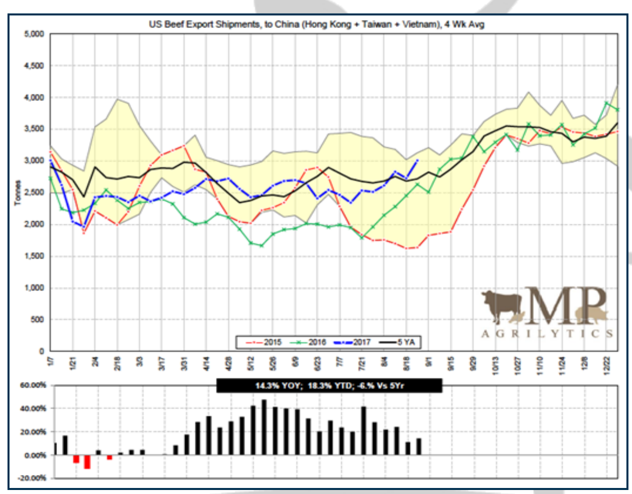
- The market has done a great job chewing through the larger inventories and creating better demand. We don't have a labor problem like many have feared we might. We are currently harvesting 630,000 hd with ease. This is a testament of demand that has increased year over year and is expected to continue. Peak supplies are right now here in August and September. As we outlined above, supplies will be declining beyond September. Seasonally, we are expecting cash and futures to bottom right now or the middle of September at the latest. For the time being supplies are matching up with demand but in the future there is the reality that demand will out stretch supply. This comes from domestic as well as exports.

- The market eroded lower than we expected from $110-$112 down towards $105. But now that basis has turned, long hedging has started up again, forward sold positions are the strongest they have ever been, and placement rates are now falling. Packer margins are still very strong so there is a lot of ground the market can cover as a result of that. Packer break-evens would be $120 as an example.

- Exports remain strong with the greater Asian destinations growing along with Mexico and Canada. Seasonally, New Zealand and Australian exports will erode so US exports to China should grow. And with the new US regulations finally in place we should see growth for this market as well as the continued strength in the "grey" market for China as well. Demand is good and more US supply is expected to be in even more demand as we look ahead. A declining U$ dollar continues to make the US market an attractive value.

- The funds spent the entire first half of the year growing their longs, peaking open interest and their length in early June. Since then, the funds have sold out of everything they are going to sell for now. Open Interest is off 120,000 contracts since the 6/6 peak in prices. October futures were $123 then and today they are $105. Long hedgers are now engaging the market growing open interest some 9,000 contracts over the last 10-days as they start locking in these implied beef prices. Speculative interests have stopped selling longs and focused on rolling back over the past 10 days while some quick turning funds have actually started in on a new short position campaign. $107-$108 is likely to be the pivot point for these new shorts while $111-$112 will be the level we need to get back over to encourage the recent longs to come back into the game again. As you can tell by our forecasts we expect this will happen.





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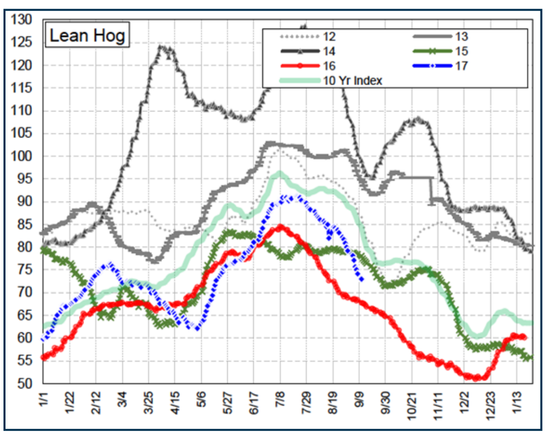
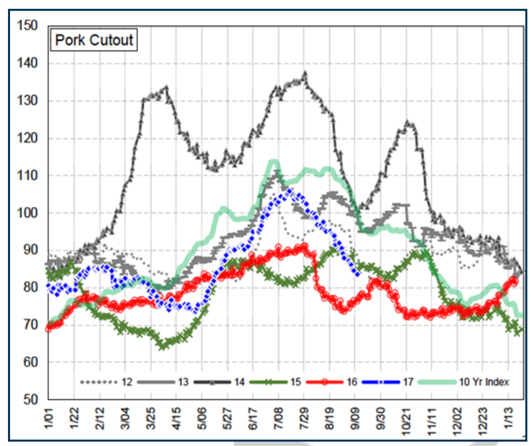
August 2017 Monthly Commentary

- We spent the entire month being long and wrong but sized our positions small enough so as to have protection from any sizeable loss and are now ready to fully engage the market here forward. Because the 10% to 15% growth in demand and with supplies moving from their peak here in September to something fewer as we look into early 2018 we fully expect 2018 prices to better than those that were seen in 2017. The market is still focused on last year's pricing performance. 2016 price action was created by basis that told feeders to hedge and carry cattle into the fall. 2017 has seen quite the opposite as we have pulled a lot of cattle ahead this year. This should lead to a late summer low in 2017 vs the late fall low we saw in 2016.

Hogs:

The seasonal decline in hogs that we expected came true. Prices dropped in the cash market ending the month down to roughly the $68 level while futures rallied from $65 to $71, but then collapsed from $71 to $60 late in the month. Speculative funds are still very long but seem to have liquidated roughly 25,000 longs from $64 to $60 in the recent days. As we discussed last month, we should see more cash weakness in the weeks ahead with value something around $55 to $60 for the market as we look into early October for the lows. The last big fund long liquidation sell off was seen this spring when prices went from $83 to $68 or a $15 decline in prices. That comparable decline today would imply October futures at $56. Typically we find a $30 break from the summer highs to the fall lows, which would imply a price at $60. Hence our call for a $55-$60 market this year. If trade retests the $68 level again we would look to re-engage shorts maybe as part of a larger cattle-hog spread relationship.





Regards,

Scott Shepard

September 6, 2017

9047 Poplar Avenue, Suite 101 • Germantown, TN 38138

newaccounts@mnrcapital.us • Tel: 901-766-4446 • mnrcapital.us