November 2017 Monthly Commentary

	Week Ending 2-Dec		Week Ending 3-Nov
Kansas Cash Trade	120.00	-5.00	125.00
Blended Beef Price	194.80	-5.91	200.71
December Futures	117.32	-7.00	124.32

Cash cattle prices started the month at $125 and eroded through the month down to the $118-$121 area in the later part of the month. Packers were able to pull contracts and cut kills into the holiday to reduce demand enough to break prices. Starting the month in December at $121, prices are expected to act in a similar fashion as packers are likely to reduce kills before and during the holidays to pressure prices into the end of the year. The shortages for choice cattle what were seen into the peak holiday demand are behind us. Prices did not get up to where we thought they would at $125-$130 for this time period. This is a sign that demand is a bit softer than expected and supplies a little larger as well.

Beef prices moved higher into the early part of the month as retailers scrambled to gather holiday supplies. However, as the month unfolded, prices crashed right around and after the holiday. This stemmed from more purchases of forward inventory and freezer stocks having been booked this year versus the past few years which limited the panic spot buying that packers are so accustom to seeing. Exports have been very supportive for trade but we are expecting the month of December to be very soft as players wind down their year and count inventory. All of the changes to industry grading cameras that happened in the middle of October are resolved and behind us now. There is choice beef everywhere now vs late October when there was roughly 10% less in certain regions. As a result, the choice select spread has topped and expected to erode from current levels.

Placement rates in November were much larger than expected at +6% as feeders continue to get cattle back into their feedyards after pulling so many cattle ahead this past summer. Since placements have been so large in through the summer and fall, the yards are full—we have plenty of cattle. These cattle are primarily coming in the spring and summer months and something we are already trading. Any rallies will be used to increase positions.

As we discussed in past write ups peak supplies were in September and eroded into what we see today. Supplies are expected to increase into January but dip again in February before marching ever so higher into this spring and summer. I don't have an answer to how we are going to overcome the supply given the capacity issues we might have in 2018. If cattle do not move forward into the early spring from the spring and summer we will have troubles. What is scary is the futures markets are not giving the producers the incentive to do this, instead they are giving them the opposite. Futures market spreads should be moving out to all-time record wide levels in the December and February vs the April, June, and August but are not. This is something we will be looking to trade and strategize around.

Packer margins have collapsed to roughly $25/hd. This means packers will attempt to get cash prices down closer to $114 in the coming weeks in order to get their margin back. Hence they will cut kills into the coming weeks, the long holidays, and at year-end.

You have heard us talk about $130 as an objective. The December failed to get there but the February and April did. We thought December had the power to get up towards $128 and the February closer to $134 before breaking. We did exit our longs nicely over $125, which helped us lock in our profits. However, since the trade was still undecided we haven't had much of a bias in recently. This is in part because of the holiday trade and waiting to fully understand the packers' intentions. Last week showed us those intentions and they were much softer and lower than expected. While demand remains to be pretty good we are not hearing much from exports and we are hearing better supplies of cattle coming down the pipeline this spring. As a result, I think we are looking at some very contra-seasonal trading patterns

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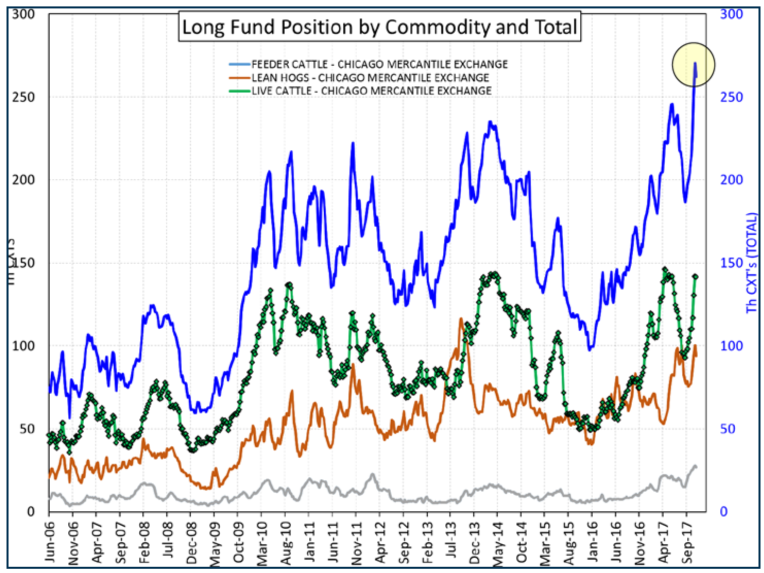
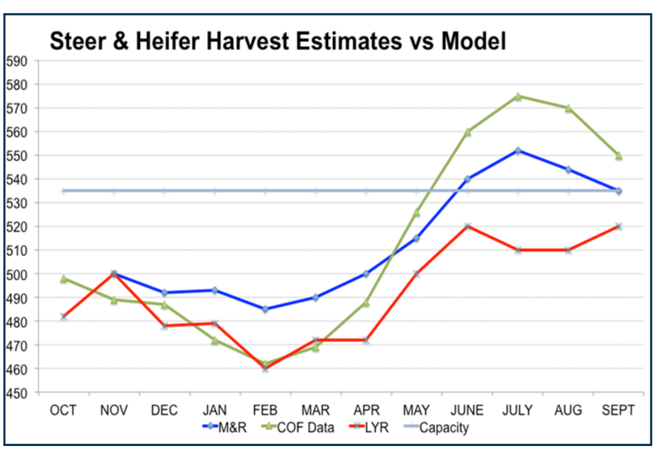
from early December through the spring and summer that we are going to be attacking. The funds still have a massive long position on and will be rolling that into the April and June contracts. The fundamentals clearly are telling us they are backwards. Hence our decisions to take them on here in late November. Selling rallies is the plan for the coming 6-12 months as I believe the focus should be primarily on the spring and summer contracts. The summer months are the ones that are in most jeopardy longer term and where we will carry our bias.

The funds will need the market to move back down under the $115 to $112 area like they did before when they sold out of 60,000 longs and took prices down to $104; however, this time they have 140,000 contracts.

The $104 lows that were made in August held us so far as prices reached a $127+ peak in late October and $121 here again in November after testing $117. Any declines in prices for the immediate time frame should be held to the $110 area. Seasonal rallies should be capped by the $125-$130 area for February and April. As for the summer lows, we will wait for our year end modeling work to give us more data but suffice to say we are concerned about where things might be headed and unless we increase demand, a lot prices are moving down in 2018. We will still have a decline in supply into the first quarter of 2018 from the 4th quarter of 2017. However, it is very important that feeders sell spring cattle ahead of schedule. I am expecting basis to widen out a lot to encourage this and forecasting that it will happen. This will come from the funds selling futures down more than the cash declines or rallies so basis should move cash premium to futures contra-seasonally early this year.





Basis led prices lower this summer and basis led us higher into the fall. Now basis is most likely going to lead prices back down again. Trade should correct back lower into Decembers expiration and possibly all they way into January before the stage gets set for the spring rally. However, we must have our eyes on the idea that if we keep placing cattle this fall we will most likely have a burdensome supply come this next summer.

We are increasing our risk platforms as we focus on the above strategy.

M & R Capital LLC

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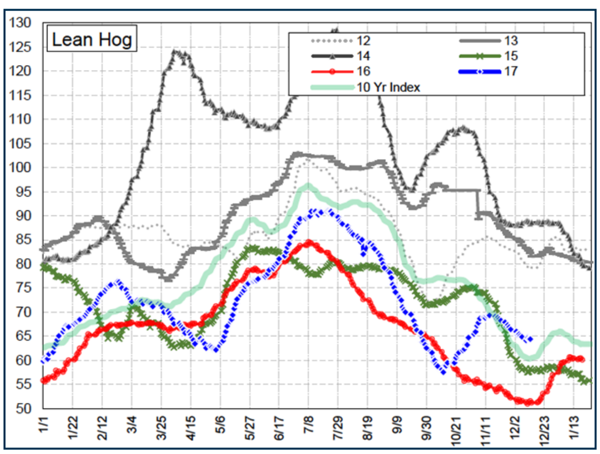
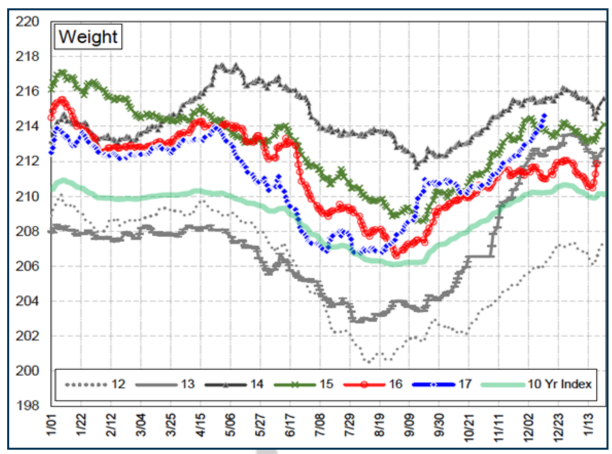
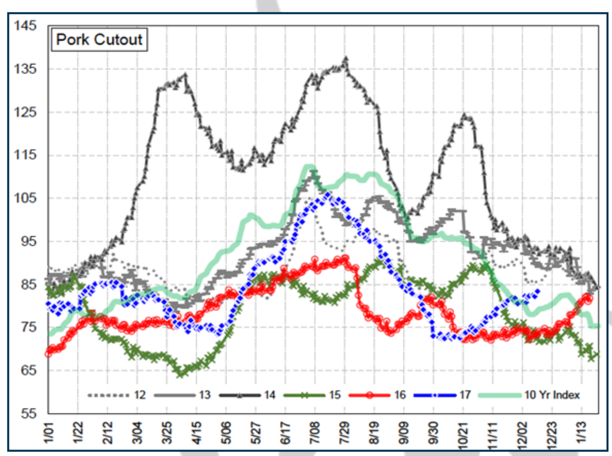
Hogs:

The market has surprised most bears this fall with cash prices finding support from $55 to $60 on hogs and $80 on pork when most models were looking for prices to be $55 to $50 and mostly $70 on pork. This better than expected pricing situation comes not because of better demand but because the USDA and many of us missed supply by roughly 4%. USDA was calling for 4% more pork production this fall while most analysts were looking for closer to 2% more. Reality was steady to 2% less. This short fall in supply comes from productivity troubles with the breeding herd as the industry seemed to have tried to do too much with too little of sow base and productivity suffered as a result. Weights are rising as producers attempt to make up for the headcount shortage with more pounds. So hogs are not backed up, they are merely bigger in order to make up for a tonnage shortfall at the factory farm.

Looking ahead we shouldn't carry this production mishap too far forward as the industry is very good at fixing these issues. Therefore I don't want to raise summer or fall prices of 2018 for a problem that was created in early 2017 and is likely fixed today. As a result we should expect seasonal price appreciation like normal with early 2018 prices being $75 and summer hogs $90.







Regards,

Scott Shepard

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