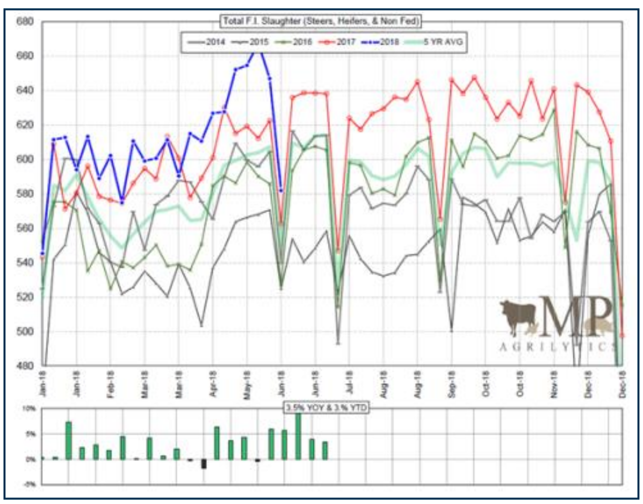
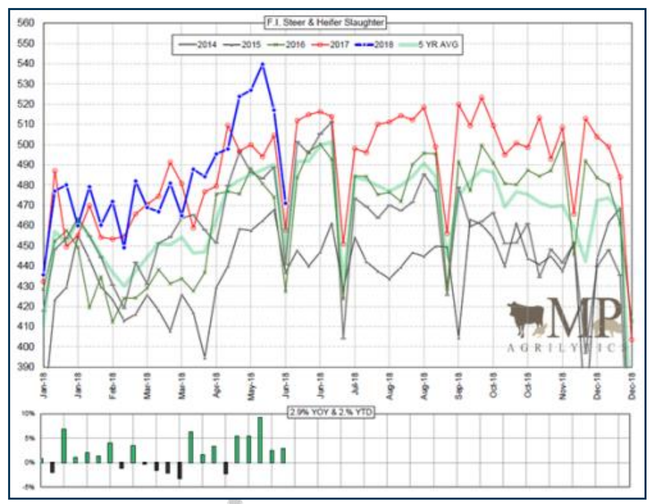
May 2018 Monthly Commentary

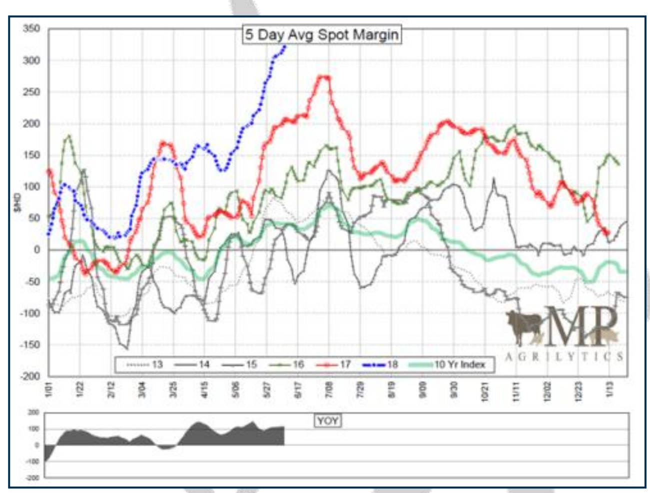
	Week Ending 1-Jun		Week Ending 27-Apr
Kansas Cash Trade	111.00	-15.00	126.00
Blended Beef Price	218.71	3.84	214.87
June Futures	104.90	-2.32	107.22

Cash cattle prices started the month at $126 and dropped to $110 by month end. Increased basis (forward) sales of cattle, fears of the summer supply, and a $7 collapse in futures prices into mid-month drove cash trade sharply lower. Packers' leverage was strong. Basis collapsed and packer margins surged as cash prices remained at their lows while futures prices rallied back into month end. Retail demand remains strong as beef prices held up despite the sharp increase in slaughter rates this month. Demand is strong. Cattle were pulled ahead selling into mid-June by the middle part of May. However, as basis collapsed late in the month the desire to sell cash lower (in order to capture basis profits) has been eliminated thus shutting the gates for this part of the supply—perhaps until this fall. Exports came back on strong and retail demand continues to impress. News that China is adding a few more plants in June and rumors that traceability requirements might be removed for future exports seems to possibly be their next move.





Packer margins have surged to our forecasts of $300/hd and thus the discounts for futures are now worth an investment as basis should move from the board's big discounts to more on par with cash levels. Cash could prove to have bottomed seasonally. As you have been reading for months, we have been calling for an early summer cash low and packer margins moving to $300/hd. We are here now. After setting the table for months it's time to capitalize. This means any drop in cash from here should mean the board is steady, at worst, and any steady to higher move in cash will require the board to work twice as hard to narrow basis. Margins will narrow from here and should be close to $100/hd. At a $195 cutout value and $100/hd margins this means cash will be $115 at the lowest and possibly back over $120. Futures today are $103-$105 by comparison.



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M & R Capital LLC

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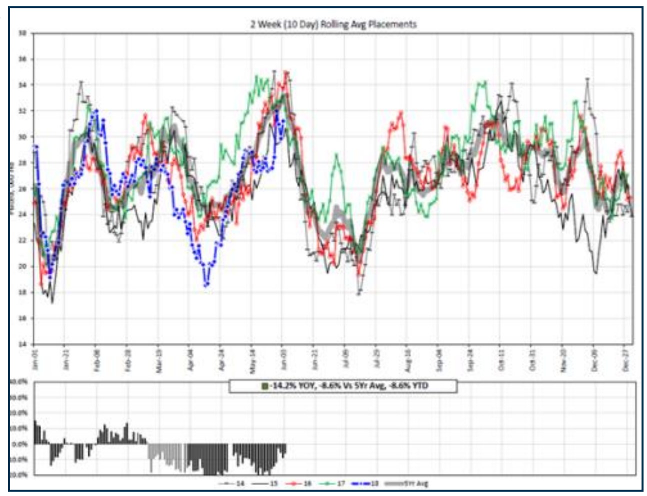
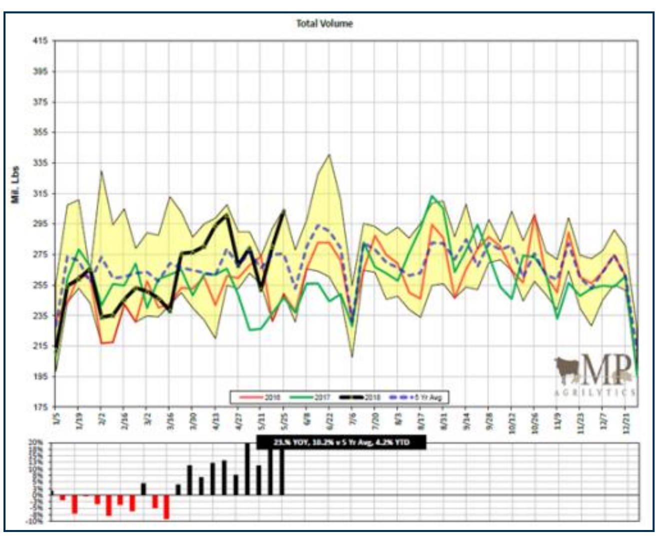
We have been worried that packers could not kill the cattle supplies this summer but we have proven we can hit 540,000 steer & heifer kills and with cows still strong. Assuming 125,000 kills for June, that implies we can get to 665,000 with ease. This means we have no real issue with capacity to fear. With the board discount to cash that probably doesn't need to be the case anymore.

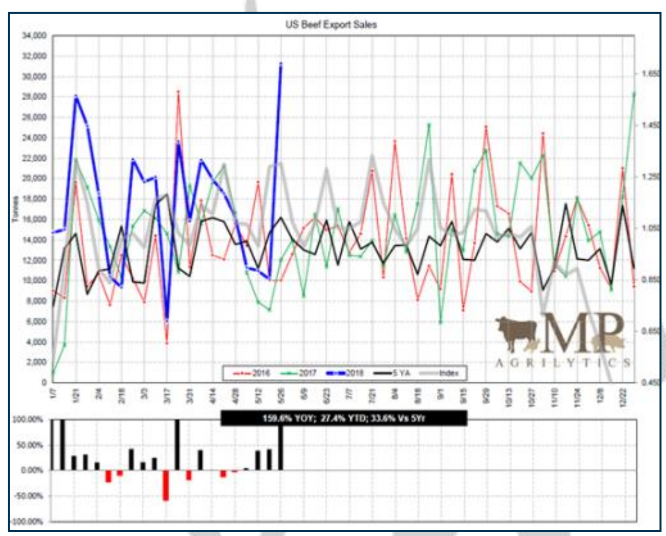
Cash prices dropped and as a result of strong margins and beef moving very well it seems like cash prices have bottomed for the summer. If this is an accurate statement cash should rally back to $115-$120 and futures should be able to rally back from $105 to $115 as well. The degree of upside for the trade will be determined by the funds' desire and aggression with their nearly 70,000 shorts— near record positon for them.

Placement rates have been falling since March. Averaging -10% for March, April and now May, this means the total cattle on feed supplies should be back to par with a year ago. By July and August slaughter rates could possibly be around -1%. Since demand is running so strong this summer and supplies subsiding we might have a stronger market later this summer than many are currently expecting.



We have long discussed peak supplies being around early July. However, as basis changes I am expecting that we will start moving some of these July and August supplies out into the fall. This will remove supplies from the later part of the summer and add them on to the fall supplies, which are falling at this time based on recent placement patterns. This should be very supportive to prices into the later part of this summer but level off supplies from crashing too much this fall.





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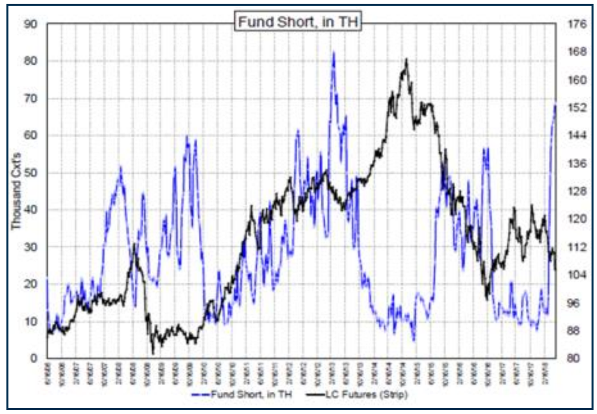
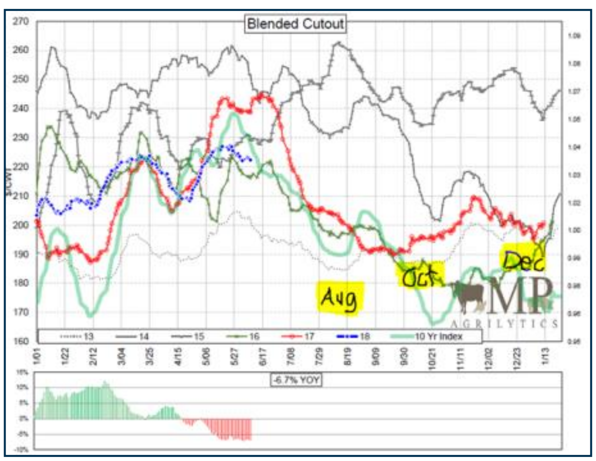
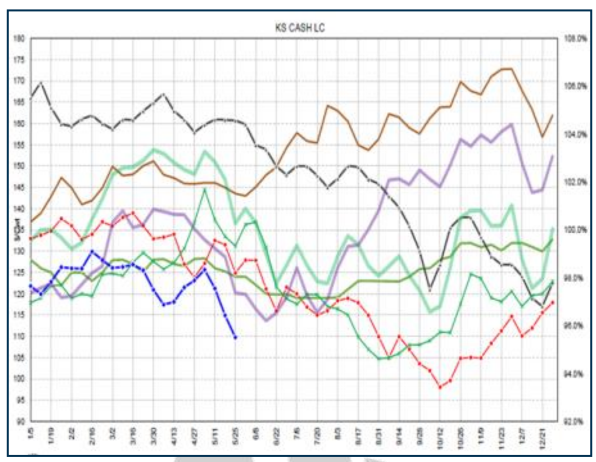
Speculatively, the funds are pushing the envelope of risk with selling and shorting the market. There have been very few times that they have been this short. It has resulted in roughly a $15.00 rally in prices before the situation was changed. The index funds (both passive and active) have now likely finalized their 3 months of selling they needed to accomplish. This should reduce one of our larger selling pressures against futures. With the nearly 70,000 short speculative positions we have the makings for a decent rally. Commercial buying has been big since pushing through $105 the first time and this buying has been aggressive on this second push down in recent days. This is tied to demand, hedging, as well as feeders cashing in on record basis profits. All of which should encourage more demand and less supplies as we look into the later part of the summer.



Volatility will continue to be excessive especially with the funds positioned short and the index funds now done selling their longs. Therefore we will continue to be big traders of options to limit our over-all risk exposures relative to our positions. We have found our reason to be long the August and October and have done so. We are comfortable being long volatility again. We will look at the June contract into the spot month as a risk worth trading for as this basis convergence is a great risk reward especially with demand being so strong. We will be able to do this with zero risk of delivery.

Cattle On Feed supplies are dropping fast and should be at a year ago by July or roughly a 7% drop in 4 months time. Hence, why we are prepared to increase our risk parameters.





Regards,

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

Scott Shepard

June 6, 2018

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