

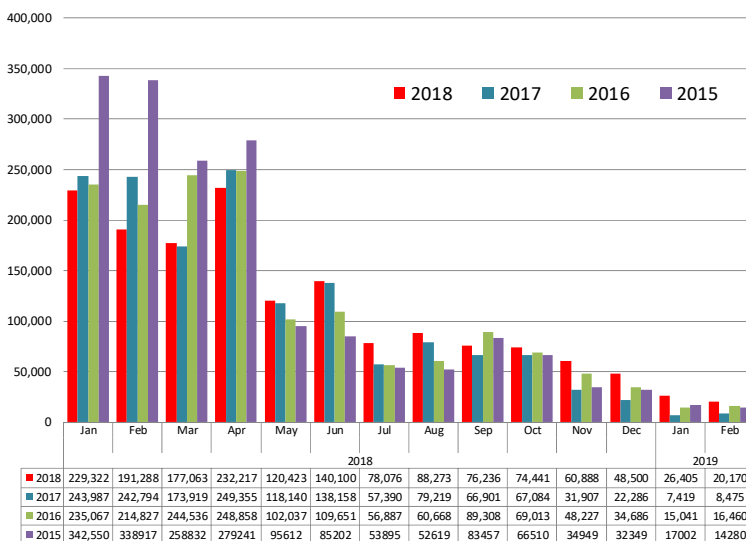
Will the current shakeout in the cattle futures cause packers to increase the number of cattle they contract for forward delivery?

In part this will be dictated by the ability of packers to sell product forward but also their general view/attitude/perception of supply risk. The mandatory price reporting system provides some data in this regard but the volume of information is quite substantial and one needs to spend a fair amount of time making sense of it. It is also important to understand what is and is not included. Let's start with some of the latest statistics as reported by USDA. The information on packer forward cattle purchases is included in a weekly report (LM_CT153). One can also use the MPR query system to collect and analyze historical information. For the week ending January 7 the report shows that 392,509 head of cattle slaughtered were reported into the system. For the most part this is fed cattle but there were probably some non-fed cattle included as well. Not all cattle slaughtered are captured by the mandatory price reporting system. According to USDA, total cattle slaughter for that week was 541,000 head and fed cattle slaughter for the week was 431,000 head. Therefore, **the slaughter reported into the mandatory system represented 91% of the national fed cattle slaughter and 73% of the total cattle slaughter.** These ratios have been fairly stable over the years and are quite representative in our view.

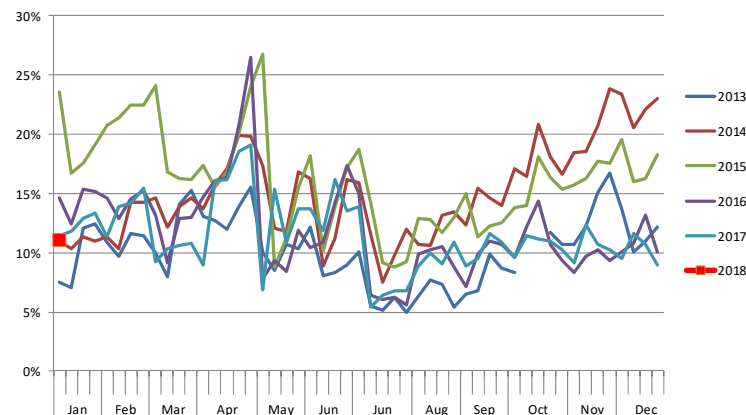
The report then breaks down the slaughter reported by marketing type. Not all cattle slaughtered last week were purchased last week. And a very small portion of those were done via direct negotiation. About 95,289 head were purchased via direct negotiation between packers and the feedlot operators, or 24.3% of the total cattle reported in the system. Over the years we have seen a steady decline in the share of cattle traded on a negotiated basis although the ratio has stabilized in the last year. Most cattle that were slaughtered last week were purchased on a formula basis (59.7%) and another 11% were purchased at some point in the past. This last piece of data is one that tends to move around quite a bit and what we started this discussion with. The report provides an indication of what those forward purchases on a cumulative basis. For instance, at this point packers have purchased 191,288 head of cattle for delivery in February 2018. Last year, at this point they had purchased around 245,292 head of cattle for delivery in that month. Fed cattle availability is expected to be higher during Q1, something that is evident to anyone that has looked at on feed inventory numbers. The packer is aware that it should be a bit easier securing cattle and thus has reduced their forward coverage. The decline in forward cattle purchases may also reflect the decline in forward beef

Cattle Forward Contracted for Delivery in a Given Month

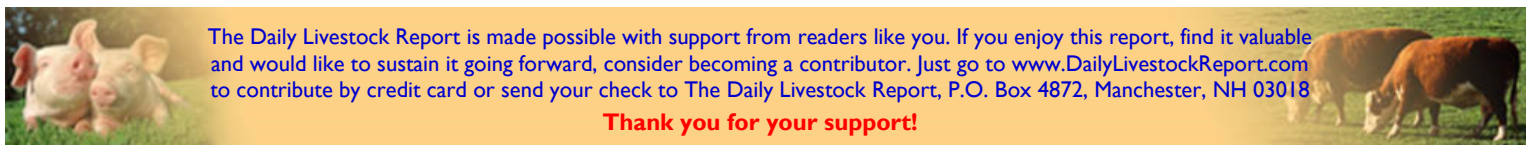
Supply Cumulative as of January 8, 2018 and Comparable Period in Previous Years. Source: USDA MPR System



Forward Contracted Cattle as % of Domestic Slaughter Reported in the LM_CT153 report
Data Source: USDA Mandatory Price Reporting System



sales, especially for product that will delivery in March and April. The first chart above illustrates the packer forward cattle position in the last four years during the first week of January. What quickly stands out is that the packer has less coverage in February, March and April but more coverage in May and June, when beef demand tends to improve.



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