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WEEK ENDING MAY 20, 2022

THE BEEF WRAP

The cash cattle market started to eased further this week, dropping a little over $2 to average $140.26. The beef cutouts were higher, with the Choice gaining $4.07/cwt and the Select up $2.61. Given that this week was the sweet spot for last-minute buying ahead of Memorial Day, it was somewhat surprising to see the chuck primal leading the Choice cutout higher. Ribs and loins did post some modest gains, but not nearly to the degree that is normally expected right ahead of the start to summer. It does make me wonder what will happen as we move deeper into summer and the end cuts are more likely to become a drag on the cutout rather than a supporting factor like they were this week. The combined margin chart tells us that beef demand is still in a downcycle and it is approaching the zero line for the first time since January, 2020. I would like to think that the zero line will be the point where it makes a bottom and turns higher, but my fundamental forecasts have it continuing lower toward a bottom around -$170 near the end of June.

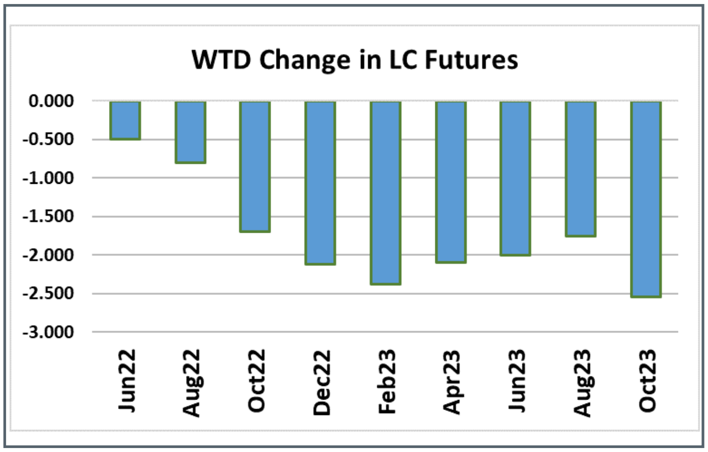
With the cash cattle market now in decline, the feedyard margins should only get worse from here and as far as the packer margin goes, this weak showing heading into Memorial Day leads me to forecast the cutouts lower in June and July and that will probably limit the upside potential for packer margins. When consumer demand fades, there is simply less margin to be shared among the supply chain participants. That softening in consumer demand is being helped along by a sharply lower stock market, which will make consumers feel poorer pretty quickly. Over the past few years, a greater percentage of the population has become involved with equity markets. That was great while equity prices were going up, but now that they are coming down it means that a larger swath of the population will feel the pain. Combine that with rampant price inflation in the economy and it is easy to see why consumers might pass by the $15/lb ribeye in the supermarket. So, even though the cutouts ticked up a bit this week, I remain a demand bear.

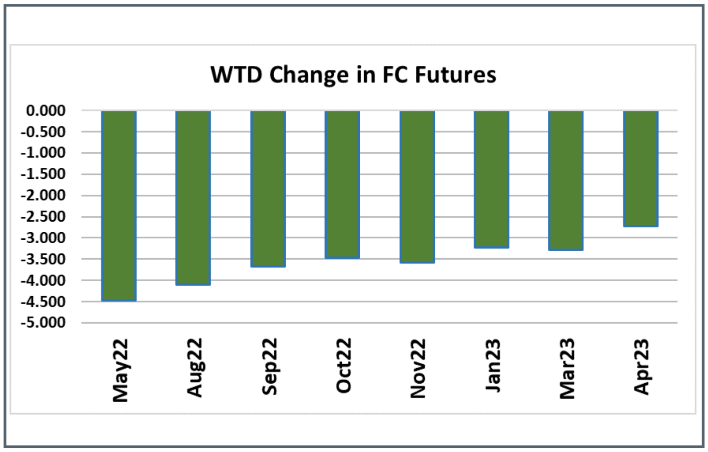
On the supply side, packers put together a huge kill this week, with fed slaughter coming in at 533k. That was 22k larger than last week. Some of that additional meat could be meant to fill orders already on the books for next week, but I suspect that pushing that big of an increase through the system will likely result in softer cutouts. Of course, we will have a short kill for Memorial Day week, so that could help to limit the supply pressure briefly in early June. However, after Memorial Day the flow model is telling me that weekly steer and heifer slaughter should be above 520k per week and might even exceed 530k. By then, carcass weights should be on the rise also. This week USDA reported steer weights down 3 pounds for the first week in May, but weights normally bottom around mid-May, so the supply side won't be getting help from declining weights much longer. The big kill should help to improve feedyard currentness, but it is important to remember that packers bought a lot of cattle with time a few weeks back and they will likely be working through those in the near future, taking some demand out of the spot cattle market.

And of course, we can't talk about the supply side without discussing this afternoon's Cattle on Feed report, which showed April placements down only 0.9% when analysts had been looking for a 4.3% decline. This is the second month in a row where placements came in well above expectations. When this happened last month, the futures dropped $3/cwt the following Monday. A similar result is likely this time, but maybe to a lesser degree since the futures have been beaten down pretty hard already. All of the contracts lost ground this week, but it was the very deferred issues that lost the most. Those are the ones that have been showing up as way over-priced on the weekly mis-pricing charts and it does seem that traders are now starting to adjust their price expectations for late 2022 and early 2023 downward. Today's COF report showed May 1 feedyard inventories up 2% and the largest for this time of year since the series began in 1996. That is pretty bearish in itself, but when we also consider that it is happening at a time when demand appears to be softening and carcass weights will soon be increasing, then it becomes an even bigger stumbling block for prices this summer.

Fed slaughter in May has lined up very well with what the flow model suggested and gives me a higher degree of confidence that June and July kills will also come in close to the projection. If there is a miss, I think it will miss to the downside because I could envision a situation where packer margins deteriorate more than expected and packers throttle back on the kill. If that happens, then it just pushes the supply problem further into the future and probably adds to carcass weights also. For much of this year, it seems that all the market pundits wanted to talk about was how cattle supplies were going to get seriously tight because cow kills have been elevated and we have been liquidating the beef herd. Well, here we are almost to June and we have record numbers of cattle on feed in a declining demand environment.

There will come a time when cattle supplies get tight and drive prices higher, but that moment is a long way off from the present. Right now, the industry needs to be focused on surviving the next few months of big supplies and softer demand. It would really help if retailers would aggressively lower price levels, but they are typically slow to do that and not inclined to do it in May/June when historically consumer demand has been the best. I'd look for bigger retail price reductions in July and August. Next week, we will be watching closely to see how the market handles this week's big production. I'm forecasting the cutouts a little lower and the cash cattle market to pull back another couple of dollars. Monday's futures market reaction to the COF report should help get the ball rolling in that direction.


WTD Change in LC Futures
0.000
-0.500
-1.000
-1.500
-2.000
-2.500
-3.000
Jun22
Aug22
Oct22
Dec22
Feb23
Apr23
Jun23
Aug23
Oct23


WTD Change in FC Futures
0.000
-0.500
-1.000
-1.500
-2.000
-2.500
-3.000
-3.500
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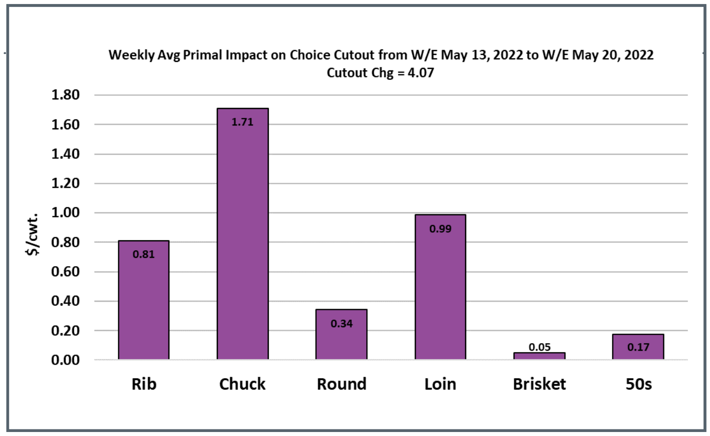
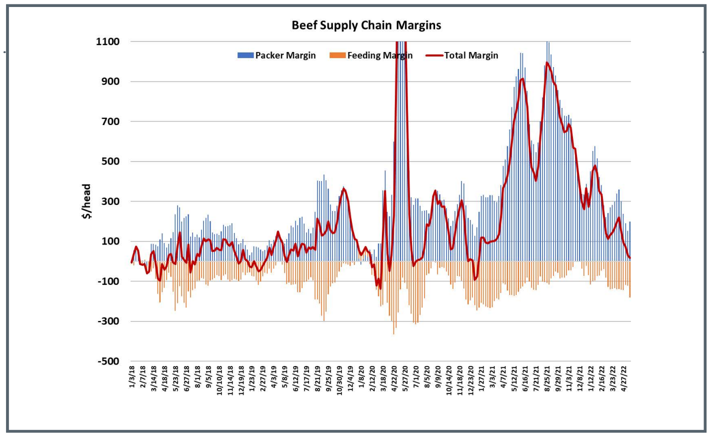
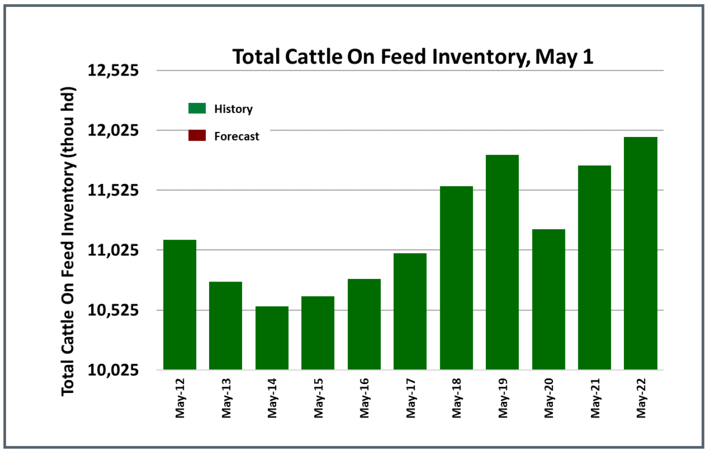
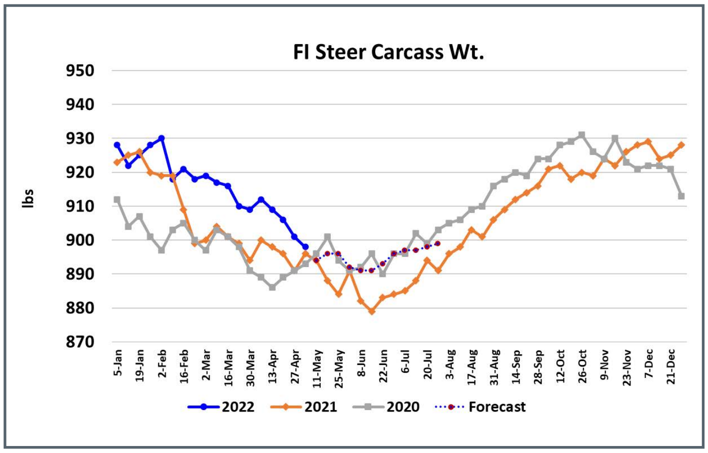
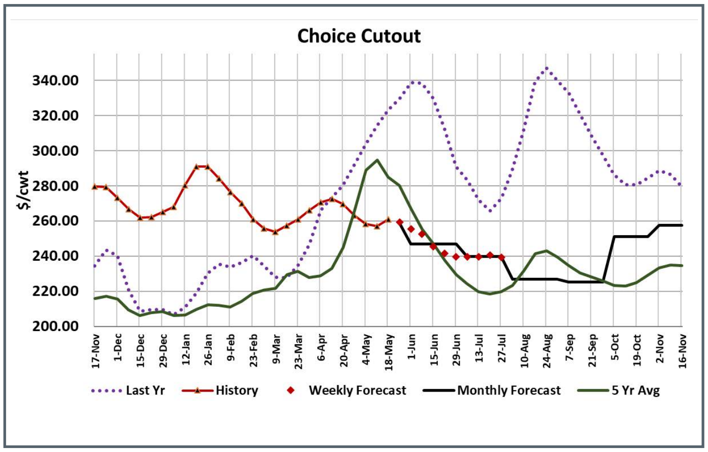
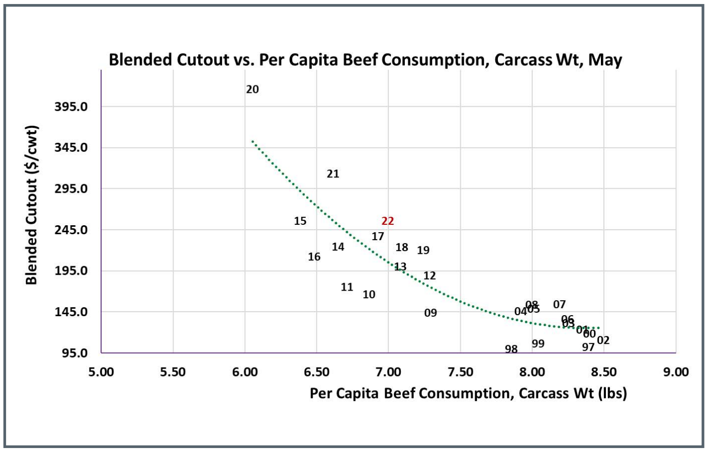

Weekly Avg Primal Impact on Choice Cutout from W/E May 13, 2022 to W/E May 20, 2022
Cutout Chg = 4.07
$/cwt.
1.80
1.60
1.40
1.20
1.00
0.80
0.60
0.40
0.20
0.00
0.81
1.71
0.34
0.99
0.05
0.17
Rib
Chuck
Round
Loin
Brisket
50s


Beef Supply Chain Margins
Packer Margin
Feeding Margin
Total Margin
$/head
1100
900
700
500
300
100
-100
-300
-500









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Dr. Rob Murphy is an agricultural economist and business leader with over 29 years in the industry. He has a wealth of experience in the North American meat and livestock industries studying, analyzing and predicting market movements.