



WEEK ENDING OCTOBER 28, 2022

# THE BEEF WRAP

The seasonal increase in beef prices got underway in earnest this week, with the Choice cutout gaining \$9.26/cwt. and the Select cutout up \$7.69/cwt. Of course, when cattle feeders saw that, they wanted their piece of the pie, and they got it. Cash cattle prices advanced almost \$2/cwt. to finish the week very close to \$152/cwt. Since the beef moved up more than cattle, packer margins expanded and are now back close to \$95/head. It is considerably easier to get packers to pay up for cattle when the boxes are advancing rapidly as they did this week, but I suspect that when the boxes turn lower a few weeks from now, that cattle feeders will not want to give back any of the ground they have gained in the cash market. At the moment, neither packers or feeders are too concerned about it because both markets are rising, but the cutout normally makes its seasonal top just before Thanksgiving and the calendar will turn to November next week.

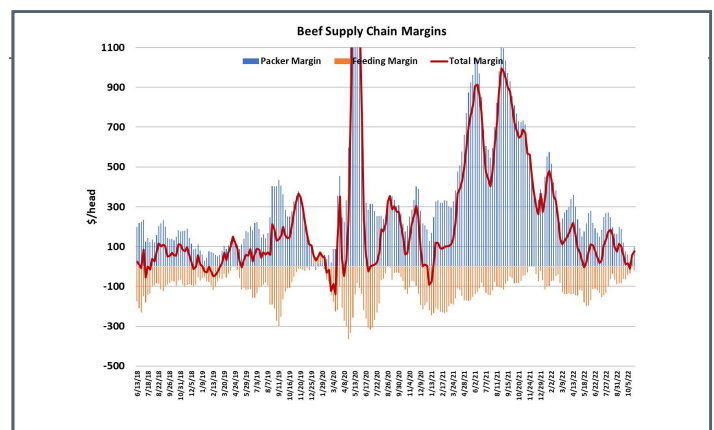
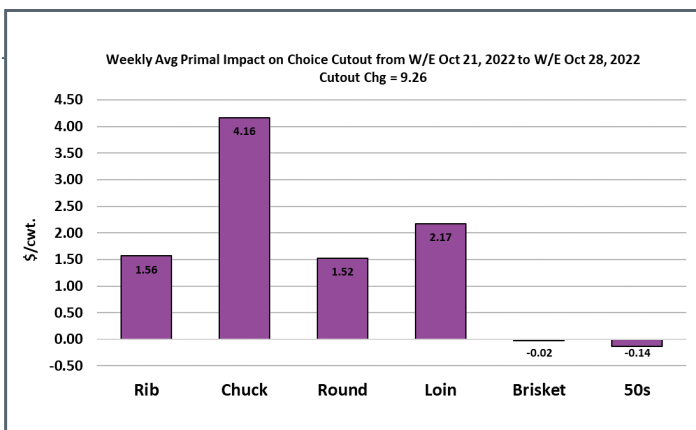
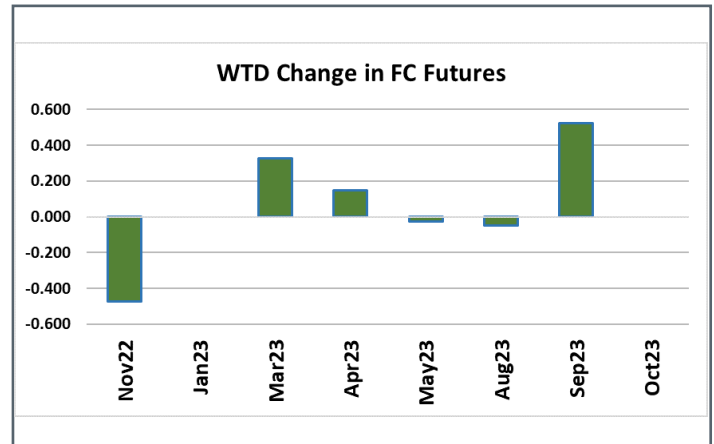
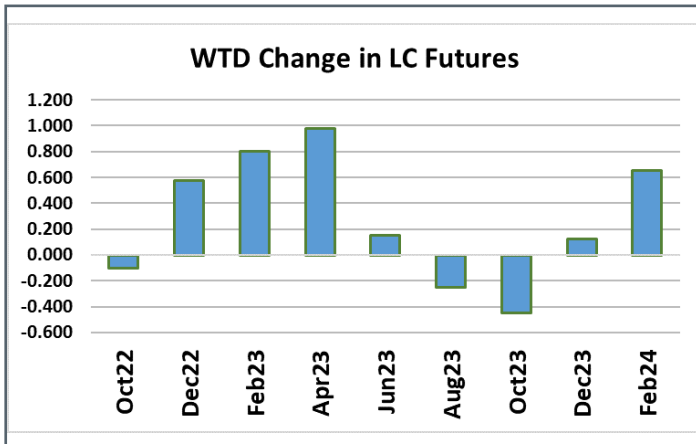
That means there might only be 2-3 more weeks of seasonal increases in the beef before the cutouts falter force packers to make some tough decisions about how they are going to reset cattle feeders' price expectations. I think that packers hands are going to be tied over the next couple of weeks due to the fact that they have forward sold a lot of beef that will need to be delivered in the second half of November (see attached chart). When packers have a big forward book to fulfill, slowing down the kill is not a viable option so they normally end up paying what cattle feeders want. That means we could be looking at another couple of weeks where the cash cattle market advances \$2 or \$3 per week. However, once the orders have been delivered, the cutouts are likely to be in the process of turning lower and that will give packers a lot of financial incentive to reverse the gains in the cattle market.

That is when the fight is likely break out. Normally, packers have the upper hand in those types of price skirmishes because they can always slash the kill, but for some reason packers have been reluctant to bring out that powerful weapon in the last few months. If they don't get a better handle on the cattle market they are likely to have some serious margin woes as we move into next year. Beef demand in Jan/Feb is usually way softer than in Nov/Dec and that means considerably lower cutouts early next year. However, the futures market is now pricing cattle in February \$3 higher than in December. If packers allow that to come true, we could see significant red ink on packer income statements in Q1. This week's gains in the cutout were more spread out across the carcass than expected.

The middle meats were expected to contribute a nice chunk, and they did, but the surprise was that the chucks and rounds also showed strength. My feeling is that the ends won't be able to keep pace with the middles in the next few weeks and we will likely see the ribs take a bigger leadership role. Beef demand is in and upcycle now and the combined margin is confirming that, but I'm a little concerned that this upcycle will be shorter than most and fail to reach the tops that have been common in recent cycles. Further, the next downcycle will likely coincide with the completion of the holiday business and thus it might be deeper than in recent lows. The macro picture still looks pretty dark and the odds of a recession remain relatively high. The stock market has recovered a bit lately, so that might help consumer confidence heading into the holidays, but I'm more concerned about what will happen once we are beyond the holidays.

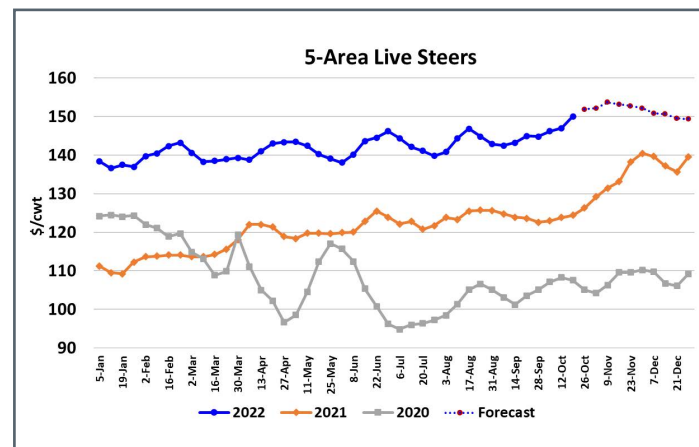
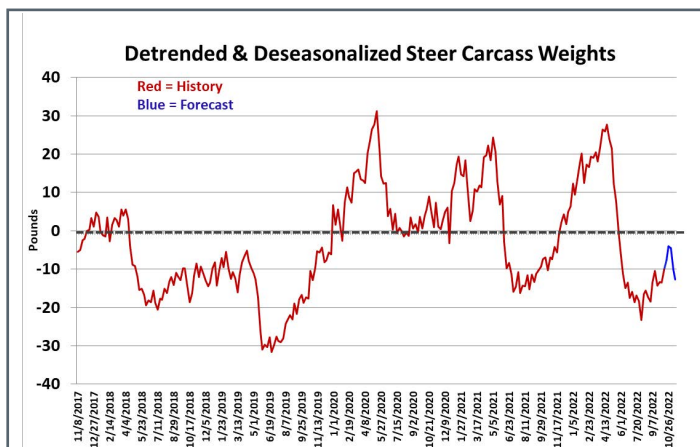
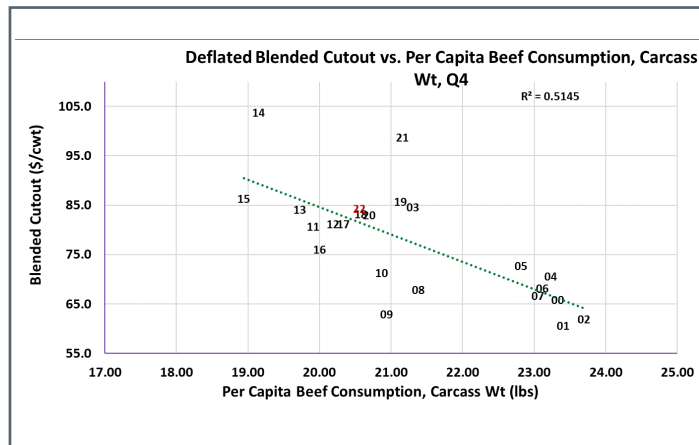
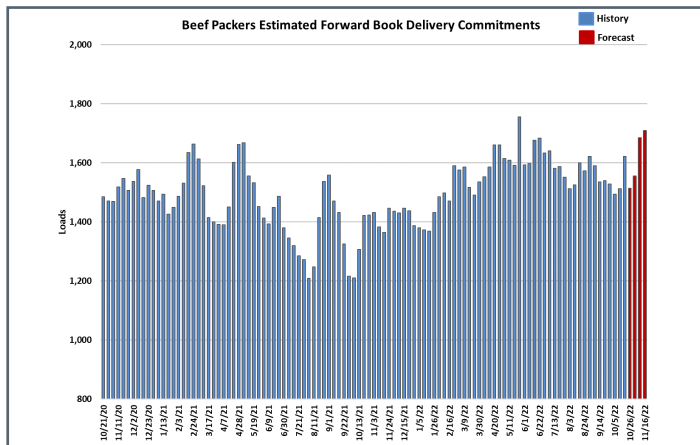
The supply side of the market looks pretty good at present. This week's steer and heifer kill clocked in at 515k, still about 10-15k more than what our model suggests should be available. Steer carcass weights were up four pounds this week and that is helping add to the beef supply. However, weights are only a few weeks from topping and turning lower. The DTDS weights have risen a bit in the past few weeks and that seems to support the idea that feedyards are becoming less current, but that is at odds with the fact that we are seeing larger-than-expected fed kills week after week. Maybe packers have been borrowing some cattle from November to fuel big kills in October.

The flow model suggests that November fed kills should be around 510k in the non-holiday weeks, but with the big forward book coming due, there is a decent chance that early November kills will exceed that level. Beef exports seem to be holding up well and we will find out more next Friday when USDA releases the trade data for September. Overall, I'd say the market seems to be in good balance right now and behaving more normal than it has in the past three years. There are still a few quirks that seem odd, like packers refusing to cut the kill in the face of tight margins, but taken as a whole the market seems to be performing smoothly. Next week, watch for the gains in the middle meats to outpace the ends and lead the cutout higher. Cash cattle are likely to advance again and the futures market will probably applaud again.



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