VOLUME 5, ISSUE 10
EN | FR | ES

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THE MONTHLY

OCTOBER 2022

RED MEAT OUTLOOK: CATTLE & BEEF

September saw boxed beef values move lower, with the Choice cutout dropping from around $260/cwt. at the end of August to about $245/cwt. near the end of last week. The price decline can be at least partially attributed to normal softening of domestic demand as consumers transitioned from summer activities back to a more normal work and school routine. Unfortunately for beef packers, cash cattle prices were rising while the cutouts were declining. Cash cattle stayed within the narrow trading range they have been in for most of the year, but added about $3/cwt. during the month of September. Falling beef prices, simultaneous with rising cash cattle prices, meant that packer margins tightened up and we are now seeing some of the smallest beef packing margins of 2022 (less than $100/head by our calculation). Of course, while a $100/head margin seems very small in the context of where margins have been for the past three years, it is still a very large margin by historical standards if we look back prior to 2018 (see **Figure 1**). This margin compression is a natural part of the cattle cycle and signals that cattle numbers are slowly shrinking to the point where they are better aligned with packing capacity, thus packers are having to compete a little more vigorously for animals to fill their kill schedules. This is just the beginning of an even greater tightening phase in cattle numbers that will occur over the next 2-3 years and thus we can expect to see further pressure on packer margins over time. At some point in the next couple of years, it would not be surprising to see one or more major slaughter facilities close in order to keep the relationship between capacity and the available cattle supply balanced.

Packer margins are compressing and approaching levels that were typical before the pandemic

SUPPLY PICTURE

Fed cattle slaughter during September averaged around 520,000 head per week in the non-holiday weeks. That was a little smaller than what our flow model suggested would be available based on past placement patterns. As a result, that will make more cattle available for slaughter during October than might otherwise have been the case and that will be helpful since market-ready cattle numbers are expected to shrink as we move into October. It appears that fed kills during October should range between 500,000 and 510,000 head per week. That downshift in beef production will be occurring right at the time of year when we normally expect improved demand ahead of the holiday season, so this is likely to lead to higher beef pricing by the end of the month.

Carcass weights should continue to increase seasonally throughout October, so that should provide a bit of relief in the face of smaller fed cattle slaughter. Steer weights have been tracking close to last year since they bottomed back in early June and aren't likely to reach a top until November. The de-trended and de-seasonalized carcass weights are still at very low levels, which suggests that feedyards remain relatively current in their marketings and that likely played a role in the cattle feeders' ability to move cash cattle prices higher in September. Further, cattle are not grading very well compared to recent years and that is making it more difficult for packers to find adequate supplies of cattle that will qualify for the Choice or better grades that are coveted by consumers these days. That is also a sign that feedyards are in a strong bargaining position in their dealings with the packers.

The drought that has plagued most of the Western US for the last year or so has eased in some spots and thus we have seen pasture prospects improve. With more grass becoming available for grazing, that should eventually slow the movement of animals into feedyards, but so far that hasn't materialized. Feedyard placements during August were up about 0.5% from the year before and total on-feed inventories as of September 1 were 0.4% over last year. So, the cattle supply is just a little more plentiful than last year, but seasonally the number of cattle that become market ready should decline in Q4 relative to Q3. That, along with what should be seasonally improving demand during Q4, should support stronger beef pricing over the next couple of months.

DEMAND SITUATION

Perhaps the most unsettled portion of the current market has to do with domestic demand. The macroeconomic situation in the US and other parts of the world has darkened, and equity markets have moved lower as a result of this rising demand uncertainty. Inflation looks like it may be making a top, but is still relatively strong at near +8.3% YOY on the last reading. Food price inflation is one of the strongest components. Energy prices have fallen considerably, but US consumers could be facing very high heating bills this winter as the NATO allies work to keep Europe supplied with natural gas now that Russia has cut the flow into that region. The Federal Reserve has indicated that they will keep pushing interest rates higher until meaningful reductions in inflation occur and that has raised concerns that the economy will move into a recession as a result. Recessions are never good news for beef demand, so there is naturally some concern building about how well domestic demand will hold up in a high interest rate environment. The one saving grace is that unemployment remains very low in the US at 3.7% and most of the ill effects of a recession on beef demand come from rising unemployment. One thing that is apparent to us now is that domestic beef demand has now shed all of the boost that it got from the pandemic. **Figure 2** shows our calculated beef demand indexes by quarter and the "demand bubble" that occurred during the pandemic, and particularly during 2021, has now dissipated. These demand indexes take the inflation level into account because simply looking at raw price levels can cloud our ability to see what is really going on with beef demand when inflation is high, as it is now. This is normally the time of year when we advise buyers to take coverage on holiday middle meat items in order to avoid price hikes as the holidays approach. We think that middle meat prices will rise in normal seasonal fashion during Q4, but don't look for prices on holiday middle meat items to exceed last year's level. Cattle are grading poorly however, and that may make availability of prime and upper Choice product a bit tighter than it has been in past holiday seasons.

International demand is another area of concern. So far, export numbers have held up well, but the US dollar has strengthened a lot lately and that raises the cost of US beef to our overseas trading partners. Further, other parts of the world face most of

Cattle are grading poorly,
making it more difficult to source high quality middle meats

the same macro headwinds that exist in the US and so there is risk that international demand, which has been a bright spot over the past year or so, might start to erode in Q4. The strength in the US dollar is largely due to investors using that currency as a safe haven that has become more attractive as US interest rates rise. It is doubtful that the conditions that have caused the dollar to strengthen will change any time soon, so international beef traders may well have to contend with that adverse factor for many months, if not years. China is a particular concern since the growth in US beef exports to China has been hugely supportive over the past couple of years, but covid lockdowns and slowing economic growth inside China make us a little worried about China's ability to maintain their purchasing of US beef at the levels we have grown accustomed to since 2019.

SUMMARY

US beef prices have been on the defensive during September, but that is expected to change in Q4 as buyers begin to seek out high quality middle meats for the holidays. With grading down from recent years, buyers might face a little more difficultly sourcing the high-quality product they desire. Cattle supplies are adequate and carcass weights will be increasing seasonally, so we don't expect a huge increase in prices as the market moves toward the end-of-year holidays. Demand has now reset lower from the frothy levels that it experienced during the pandemic and there are some concerns that problems in the macroeconomy such as high inflation and rapidly falling equity markets will make consumers feel poorer and thus spend less on beef. Export demand for US beef has been strong all year long, but that too could decline as the US dollar is now at very strong levels relative to most other currencies, thus raising the cost of US beef to overseas buyers. Beef packer margins have declined precipitously in recent months and that is likely to continue for the foreseeable future as the cattle herd continues to shrink, making it more difficult for packers to fill existing processing capacity. The tightest cattle numbers probably won't arrive until 2024 or 2025, but buyers should start thinking about the potential for considerably higher beef prices a couple of years down the road. Our near-term price forecasts for cattle and beef are provided in **Table 1**.

Figure 1: Monthly Average Beef Packer Margins, 2016-Present

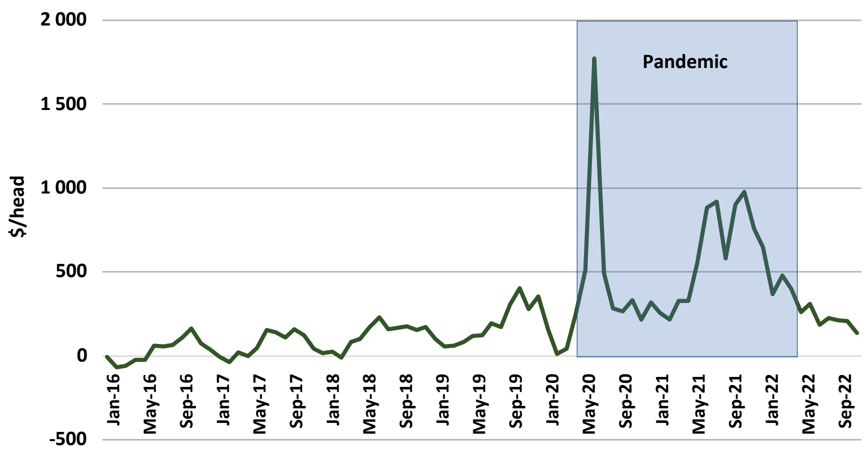

Figure 2: Demand Indexes Using Inflation-Adjusted Data, Blended Cutout
(shaded is forecast)

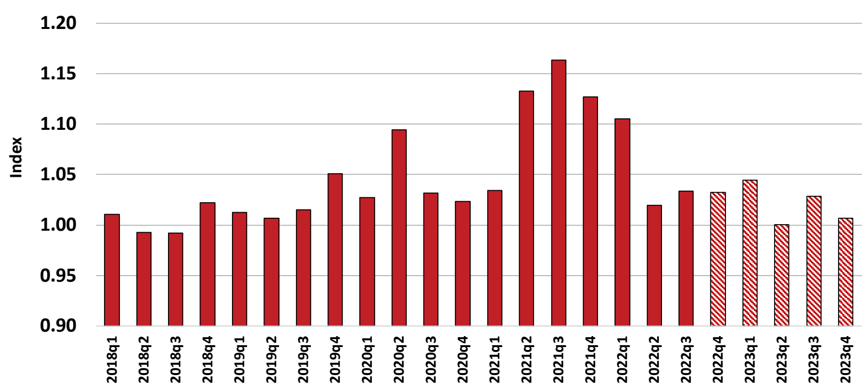

Table 1: JSF Cattle and Beef Price Forecasts

	12-Oct	19-Oct	26-Oct	2-Nov	9-Nov	16-Nov
Choice Cutout	248.5	252.6	255.3	256.0	257.0	256.9
Select Cutout	221.7	225.5	225.9	227.7	229.4	228.9
Choice Rib Primal	420.1	433.2	445.1	452.6	464.0	466.5
Choice Chuck Primal	195.7	199.0	202.0	201.4	199.1	195.5
Choice Round Primal	218.9	220.3	222.2	221.1	222.0	223.0
Choice Loin Primal	322.4	326.4	325.5	327.0	328.6	331.2
Choice Brisket Primal	199.0	203.2	208.8	208.1	207.3	208.0
Cash Cattle	143.5	144.2	145.0	145.4	145.7	145.0

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