VOLUME 6, ISSUE 4

J.S. FERRARO

THE MONTHLY

APRIL 2023

RED MEAT OUTLOOK: CATTLE & BEEF

After rallying hard in February, the cutouts drifted lower throughout March, but still remained stronger than last year. At the end of March, the Choice cutout was registering $282/cwt., about $14/cwt. (5.4%) over the same week in 2022. However, there is a big difference between this year and last. In 2022, the strength in the cutout was driven largely by very strong demand while here in 2023 tight supply appears to be providing considerable support. Last week's action in the cattle market was a good example of tight cattle supplies as packers paid almost $169/cwt., a full $4/cwt. higher than the week before. Packers are starting to gear up for the post-Easter grilling season business and they have forward commitments to deliver upon. Choice middle meats will once again be in focus as grilling season heats up and there is some concern that, much like last fall, packers will over-kill the available supply of cattle as they seek out the Choice middle meats that consumers seem to prize so highly. Cattle grading naturally slides lower as summer approaches, so those buyers needing high quality middle meats would be wise to cover all or at least a portion of their needs as soon as possible. Unfortunately, this is going to be the new reality for the next couple of years as cattle inventories shrink and price levels rise. The supply of cattle in US feedyards is down about 4-5% from last year's level and there could be times in the second half of 2023 when that deficit reaches 9-10% below 2022.

The cash cattle market surged $4 to near-record highs last week as packers geared up for grilling season

SUPPLY PICTURE

Fed cattle slaughter in March averaged about 493,000 head per week. That was mostly in line with the 490,000 head per week that our flow model was indicating. Past placement patterns point to similar availability during April, with numbers at the beginning of the month being tighter than near the end of the month. Available fed cattle supplies are not likely to be consistently over 500,000 head per week until the middle of May and that means that packers must constrain their appetite for large spring slaughter levels or else they run the risk of boosting cash cattle prices even higher in the process. We fear that, as packers strive to fill orders for high quality middle meats this spring, they will over-kill the available supply and thus, in addition to raising cattle prices, they will "borrow" cattle from June to support large May kills and thus supplies may remain tight right through early summer.

Past placements suggest **fed kills will remain below 500,000 head per week** in April

So far, the only indicator of supply tightness has been increasing cash cattle prices. Carcass weights are now about 11 pounds below last year (for steers), but the de-trended and de-seasonalized carcass weights have been creeping higher and don't seem to be signaling that feedyards are exceptionally current. We know that feedyards in the Northern Plains had a rough winter and muddy, cold feeding conditions caused cattle performance to be below normal. That has made cattle availability tighter up north and is starting to manifest some modest price premiums in the North compared to the South. It will take probably another 4-6 weeks before cattle in those northern feeding areas get caught up and start gaining normally again, but the risk of further bad weather in all regions is fairly limited at this point in the calendar.

Tight cattle availability this spring really seems to be more a function of the shrinking cattle herd than of any particular

jsferraro.com | 130 Adelaide Street West, Suite 3302 Toronto, Ontario M5H 3P5 | 416.306.8788

weather anomaly. Feeder cattle supplies are shrinking and cattle feeders are having to pay much higher prices to procure animals to put into feedyards. Last week the CME Feeder Cattle Index, which measures cash feeder cattle prices in the Central US, topped $193/cwt. for an 800-pound animal (**Figure 1**). The last time cash feeder cattle prices were that high was in October 2015 when the US cattle inventory was near its low point. This time however, we are not even close to the low point in cattle numbers. That might not occur for another two years. We think this liquidation phase will run longer than most expect, with cattle numbers getting tighter than expected, and thus cash cattle and beef prices getting very high as this cyclical process plays out over the next couple of years. Those $193 feeder cattle that were bought last week will need to bring at least $175/cwt. in the cash fed market this fall just to cover their cost of production. Right now, the October live cattle futures are only trading near $165/cwt., so cash cattle prices need to rise a lot, or else cattle feeding margins will be deep in the red this fall.

DEMAND SITUATION

Domestic beef demand in March held together quite well. **Figure 2** is an example of the type of scatter diagram that we use to evaluate domestic beef demand. The green regression line indicates the average position of the beef demand curve during March since the year 2000. Data points above the line are years where demand was stronger-than-average and those below the line indicate weaker-than-average demand. The data point for March 2023 clearly indicates stronger-than-normal demand in March, but not as strong as in 2021-2022. We use the Consumer Price Index (CPI) to deflate the cutout values in this diagram so that we don't accidentally misread price inflation in the macroeconomy as strong beef demand. Speaking of inflation, it seems to be slowly cooling in the US, with the most recent CPI release showing overall inflation running 6% per year. That is down from a peak of 9.1% last summer. It's good news for consumers that inflation isn't getting any worse, but price levels still remain very elevated and that is forcing consumers to make some hard choices about where and how they spend their disposable income. Consumers near the top of the income pyramid are not having much trouble affording high quality beef and thus demand in that segment remains very strong. It is the other end of the income spectrum where the most pain is being felt by consumers. A lot of lower income shoppers recently lost the boost in food stamps they received as a result of the pandemic and that has a direct negative impact on demand for lower quality beef items. Prices for ground beef have struggled recently and that could be related to softer demand at the lower income levels. Those financially strapped consumers are likely trading down to cheaper sources of protein. Thus, domestic US beef demand has become bifurcated, with wealthy consumers continuing to exhibit strong demand for high quality beef items while lower income consumers struggle to afford lower cost items. This situation is likely to persist for the foreseeable future and creates a quandary for packers because when they increase slaughter in an effort to meet the high-quality demand, they also produce a large amount of lower quality beef that must clear the system at lower prices.

The weekly data that USDA provides on beef exports seems to be suggesting that international demand for US products is starting to soften. Movement into the major markets of Japan and S. Korea appears to be down considerably from last year. Fortunately, shipments into Mexico remain relatively strong, but that doesn't completely cover for the deficit to the Asian nations. As US beef prices rise this spring on the back of domestic grilling demand, it is likely that international buyers will opt to purchase less beef and thus the YOY shortfall in exports may become pronounced. This is good news for domestic buyers as it will help keep availability in the US market a little larger than it might be otherwise this spring. The decline in exports is a normal feature of the US cattle cycle. As animal numbers shrink and prices rise, export volumes tend to decline as well. What we are starting to see now is probably the beginning of a long string of YOY declines in US beef exports.

Beef exports are beginning to show signs of **softening**

SUMMARY

As the calendar transitions beyond Easter, the spring grilling season will get underway. That generally means improving beef demand and higher beef pricing. We think that demand this spring for high quality middle meats will be exceptional, but demand for lower quality items might be less robust because lower-income consumers are becoming increasingly stressed by inflation in the macroeconomy and wages that are not keeping up. Cattle and beef availability isn't expected to expand much, if any, during April and thus as demand improves that likely points to higher pricing throughout the complex. Packers recently had pay near record prices for fat cattle and you can be sure they will try to pass that increased cattle cost along to consumers in the form of higher beef prices in the next few weeks. Feedyard inventories are close to 5% below last year

Figure 1: CME Feeder Cattle Index

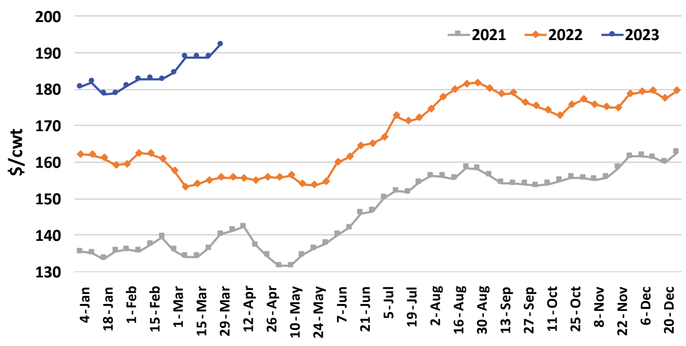

Figure 2: Deflated Blended Cutout vs. Per Capita Beef Consumpton, March

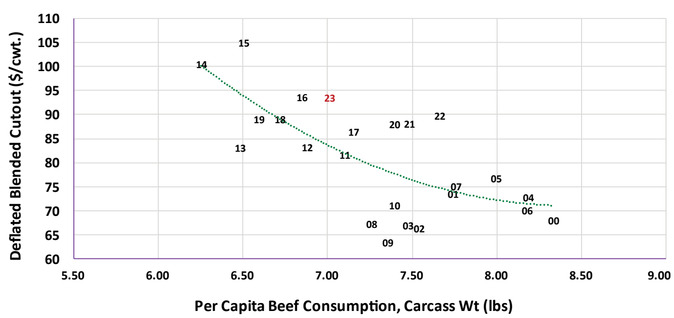

Table 1: JSF Cattle and Beef Price Forecasts

	12-Apr	19-Apr	26-Apr	3-May	10-May	17-May
Choice Cutout	282.5	283.3	284.5	285.5	285.6	285.7
Select Cutout	266.0	264.8	264.3	262.1	260.0	256.8
Choice Rib Primal	472.3	477.3	476.3	482.1	490.0	499.1
Choice Chuck Primal	219.6	217.3	218.0	216.3	215.1	213.2
Choice Round Primal	217.4	214.6	215.2	215.6	212.7	210.8
Choice Loin Primal	396.6	403.7	408.1	411.6	413.7	415.1
Choice Brisket Primal	224.1	228.7	232.9	236.0	239.7	237.9
Cash Cattle	168.7	169.8	169.5	168.7	168.0	166.8

and that deficit could grow even wider in the second half of the year. Beef buyers need to be making plans now for dealing with smaller beef supplies and higher pricing in the months ahead. From a long-run perspective, we think that the current liquidation phase of the cattle cycle will be longer than most expect, resulting in very tight beef supply a couple of years down the road. The industry will need to contract and price levels will get much higher in the process. The hand-to-mouth purchasing strategy is likely to be a loser in this environment and buyers need to be shoring up their hedging and forward pricing expertise in order to best navigate the market over the next couple of years. Our near-term price forecasts for cattle and beef are provided in **Table 1**.

DR. ROB MURPHY BS, MS, PhD Agri Economics,
Executive Vice President, Research & Analysis,
J.S. Ferraro

E: Rob.Murphy@jsferraro.com

Dr. Rob Murphy is an agricultural economist and business leader with over 32 years in the industry. He has a wealth of experience in the North American meat and livestock industries studying, analyzing and predicting market movements.