VOLUME 6,
ISSUE 8

J.S. FERRARO

THE MONTHLY

AUGUST 2023

RED MEAT OUTLOOK: CATTLE & BEEF

July was mostly a month of bad news for packers, with cutouts moving lower and the price of cash cattle moving higher. The Choice cutout dropped almost $30/cwt. over the course of July and is now trading not too far from the $300 mark. At the same time, cash cattle prices moved from about $181/cwt. at the beginning of July to around $185/cwt. last week. Thus, packer margins, which were running close to $150/head at the end of June, are now approaching -$115/head today (**Figure 1**).

Packer margins have collapsed to -$115/head, **the lowest level** so far in 2023

To be sure, the drop in the beef market was a retreat from a very sharp price increase that occurred in early June, so one might surmise that this latest move was just the market returning to more normal price levels. The relentless strength in cattle pricing is simply a result of tight cattle supplies relative to packer capacity and that is a theme that is going to be present in the cattle market for at least another two years as the nation's cattle herd continues to decline and packers battle to maintain market share in the at environment. USDA issued their mid-year cattle inventory report recently and it showed the US cattle population down 2.7% YOY and the beef cow inventory down 2.5%YOY. The number of heifers being held as herd replacements was down 2.4%, which signals that the industry has not yet started to rebuild the herd and thus liquidation is expected to continue. When herd rebuilding does begin to take place, it will result in sharp reductions in feedyard placements of heifers, thus restricting beef production even more. We think that is at least a year away and maybe two years into the future. For beef buyers, that means that the next couple of years are going to be characterized by reductions in beef availability and higher pricing.

The mid-year cattle inventory **report showed a 2.7% YOY drop**, confirming producers are still liquidating the herd

SUPPLY PICTURE

The last time cattle prices rose and squeezed their margins, packers simply raised prices to beef buyers and met with little resistance because demand was very strong in early June. This time around, however, demand in early August isn't strong enough for them to force beef prices higher simply by asking buyers to pay more. This time, packers recognize that they will need to tighten up beef availability by restricting the kill in order to push prices higher. Our flow model suggests that there should be enough cattle available to support fed kills in the 510-515,000 head range, but for the past couple of weeks packers have restricted the kill to 485,000 head per week. That has slowed the decline in beef prices, but it has yet to exert much pressure on cash cattle prices. That may take another couple of weeks and thus negative packer margins are likely remain in place for much of August.

One factor that may complicate packers' goal of lowering cattle prices is that some exceptionally hot weather has developed recently in the midsection of the country. Feed consumption typically declines when temperatures rise and that can lead to slower weight gains and prompt cattle feeders to want to hold those animals on feed a little longer before marketing them. With the de-trended and de-seasonalized carcass weights already at very low levels, this has the potential to keep weights lower than normal, thus further reducing beef production. Preliminary data suggests that last week's fed beef production was down over 5% from last year.

The most recent *Cattle on Feed* survey showed placements into feedyards during June were up 2.7% YOY and that comes on the heels of a 4.6% increase in May. We think this is largely a function of much better cattle feeding margins that started back in April and continues to the present. Feeding margins last week are calculated to be near $400/head. Cattle feeders have paid dearly for the privilege of refilling their pens however, as cash feeder cattle prices have soared over the past few months. The CME Feeder Cattle Index, which stood near $180/cwt. when the year began, is now over $240/cwt. These sharply higher input costs will eventually need to be recouped from consumer's wallets. Retailers are doing their part in that effort by keeping retail beef prices on an upward trajectory, with little sign that will change in the near term.

Cattle feeding margins are now close to $400/head, **the highest since spring of 2017**

DEMAND SITUATION

Beef demand was red-hot during June but cooled quite a bit during July. Some of that cooling was related to normal seasonal patterns, but some was also driven by buyers recoiling from the sharp price increases during June. The market has moved back into better balance now and is moving through the "dog days" of summer where consumer interest is somewhat tepid. The next big demand event on the horizon is Labor Day, and we should see an uptick in interest for middle meats and grinds during early August as retailers prepare for the holiday that marks the end of summer. However, we don't think that is going to be enough to send the cutouts upward in a big way, but rather might just provide some speed bumps to slow the decline in a market where sub-$300 Choice cutouts are likely to be a feature from the middle of August through September. The current forecast points to a low in the Choice cutout around $285/cwt. near the middle of September. After that, demand should start to strengthen markedly, as buyers start gearing up for the year-end holidays. We are currently in the midst of a demand downcycle that began in the middle of June and may carry through Labor Day. However, if packers keep the fed cattle kill constrained beyond August in an effort to fix their margin problem, then that might also keep beef prices and cutouts somewhat above our current forecast. In October, student loan payments will restart after being suspended for three years due to the pandemic. That will take a big slice of spending power away from millions of consumers and won't be good for beef demand. Will those borrowers slow their spending in August and September in anticipation of the payment re-start in October? That is a possibility and must be recognized as another potential demand headwind. Despite the potential breather that demand might take in the near-term, we recently made major increases to demand expectations for 2024 under the idea that as supplies shrink, those buyers that must have beef in order to operate (think steak house or quick serve restaurant), will exhibit very strong demand as they vie for that shrinking supply. The current forecast has the Choice cutout topping next spring near $380/cwt. (**Figure 2**), with risk that it may move significantly above that.

International demand for US beef suffered during June as prices spiked and has yet to recover much now that prices are well off their highs. Mexico continues to show strong YOY growth, but most of the Asian destinations are taking less beef than they did last year at this time. That could be due to slower economic growth out of Asia recently. However, the phenomenon of shrinking US beef exports is likely to remain in place as long as US cattle supplies are in decline and price levels are generally high. We see total exports in 2023 down 9.5% and project another 5-10% decline in 2024. It is reasonable to assume that higher prices in the US will attract increasing beef imports in the next couple of years, but that probably won't be enough to fully offset the loss in export volume.

SUMMARY

Packer margins have come under pressure recently due to falling beef prices and gains in the cattle market. Those operators are attempting to correct that problem by restraining kill levels. That seems to have slowed the decline in beef prices but doesn't guarantee that they will turn higher. The recent smaller kills have yet to impact cattle prices because feedyards are very current on their marketings. A new heat wave might hurt weight gains and thus further reduce their sense of urgency in marketing cattle, so there is no guarantee that the kill reductions will be successful at lowering cattle prices. Retailers continue to push consumer-facing prices higher and that is slowing consumption, bringing it into better alignment with the number of cattle that are available. Expect demand to continue to cool during August and September, but there could be some modest price gains as retailers prepare for Labor Day features. The re-start of student loan repayments in October creates some risk for near-term beef demand as well as for the economy in general. The recent cattle inventory survey made it abundantly clear that the US beef herd is continuing to shrink and there are no signs yet of rebuilding. When that rebuilding effort begins, likely late next year or in 2025, buyers will face acute reductions in beef availability as heifers are diverted from feedyards and back into the breeding herd. Buyers should be honing their forward pricing skills in anticipation of what could be a very difficult market in the next couple of years. Do not become complacent if demand takes a bit of a breather this fall and prices retreat, but rather use that as an opportunity to get ahead of what could be a very explosive price environment in the spring of 2024. Our near-term price forecasts for cattle and beef are provided in **Table 1**.

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

Figure 1: Estimated Beef Packer Margins, 2023

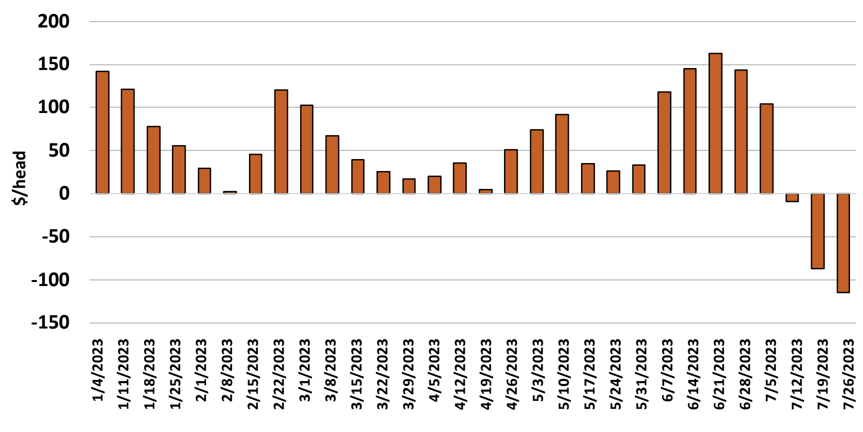

Figure 2: Choice Cutout

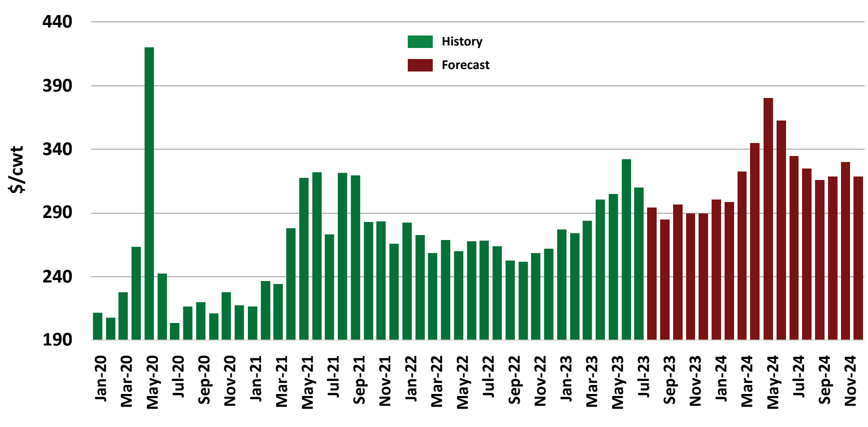

Table 1: JSF Cattle and Beef Price Forecasts

	9-Aug	16-Aug	23-Aug	30-Aug	6-Sep	13-Sep
Choice Cutout	297.4	293.7	291.6	288.4	286.1	283.5
Select Cutout	271.1	269.5	268.6	265.1	261.6	257.7
Choice Rib Primal	455.7	461.2	467.0	463.3	457.4	459.6
Choice Chuck Primal	250.1	245.8	240.6	238.5	237.4	233.5
Choice Round Primal	236.6	233.9	235.8	235.3	232.4	229.6
Choice Loin Primal	404.8	396.4	391.5	383.9	381.2	378.8
Choice Brisket Primal	255.2	257.0	253.8	249.6	247.3	245.8
Cash Cattle	183.6	181.0	180.1	177.8	175.1	174.5

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.