April 2013 – Livestock Market Update
Public Policy Department
Budget & Economic Analysis Team

In this edition:

- Livestock Update: John Anderson, Deputy Chief Economist
- Dairy Outlook: Bob Young, Chief Economist

Recommended links:

- Recent Analysis and Presentations on SILO

Next Market Update:

- Crop Market Update: Week of May 13th

Livestock Update

Cow Slaughter Picks up Steam

For most of this year, beef cow slaughter has been well below year ago levels. This has not been surprising. For one thing, with a smaller cow herd to work with, even the same rate of slaughter (as a percent of cows available) would show up as a smaller absolute number of animals going to slaughter. Beyond that, reasonably favorable profitability in the cow/calf sector over the past couple of years should have been expected to result in more interest in herd expansion, which generally shows up as lower cow slaughter. That interest in expansion has also likely been reinforced by widespread understanding that meat production in general is fairly tight, contributing to expectations of support for prices from the supply side of the market for the foreseeable future.

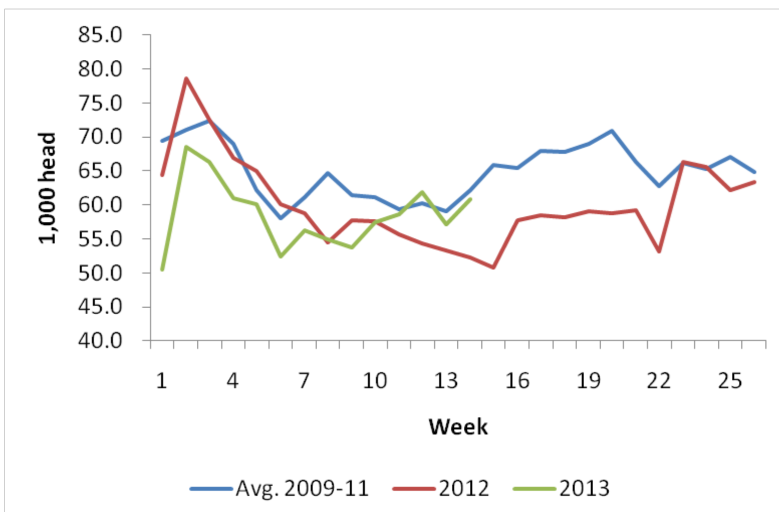


Figure 1. Weekly Beef Cow Slaughter in H1
Data Source: USDA Agricultural Marketing Service via LMIC

In spite of the arguments for holding onto cows, in recent weeks, beef cow slaughter has surged. Figure 1 shows weekly beef cow slaughter for 2013 along with weekly slaughter for Q1 and Q2 for 2012 and for the 2009-11 average.

In the four week period ending April 6 (most recent data available on slaughter by class), beef cow slaughter consistently ran above the prior year level. For the last week of that period, beef cow slaughter was almost 17 percent above year-ago. Beef cow slaughter has actually been about in line with the 2009-11 average level, despite the considerably smaller cow herd now relative to that time period.

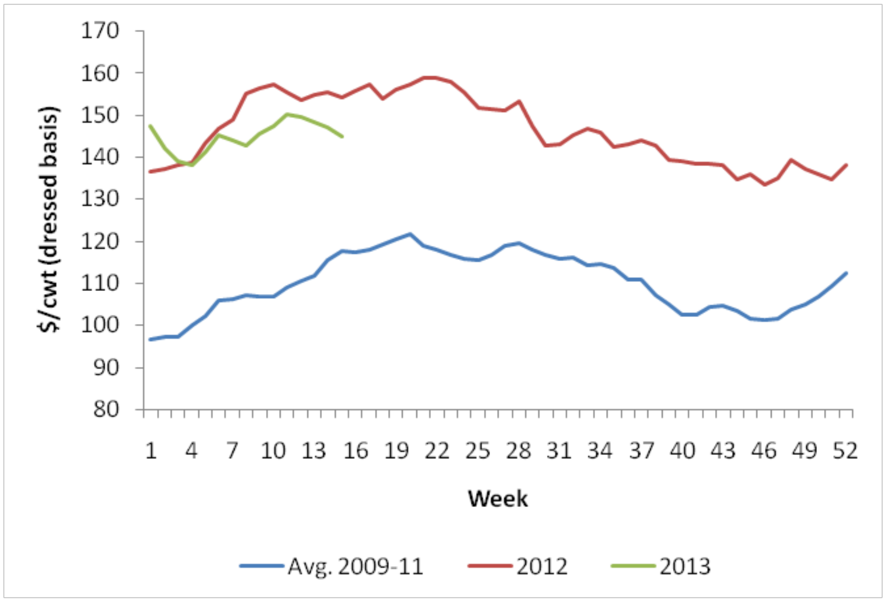


Figure 2. Weekly Direct Negotiated Breaker Cow Prices (75% Lean, 500+ lbs)
Data Source: USDA Agricultural Marketing Service via LMIC

Why the increase in cow slaughter? From the demand perspective, prices have done little to affect a significant year-over-year surge in liquidation. Cull cow prices have, in fact, improved some since earlier this year. For example, breaker prices averaged a little over $140/cwt (dressed) in January compared with almost $149 in March. However, the cull cow market has actually been unseasonably weak compared to past experience. This is shown in figure 2, which shows weekly average direct negotiated breaker prices reported by USDA. Note the seasonal tendency for prices to rise steadily through the first three or four months of the year. That has not occurred this year.

The most likely explanation for the surge in beef cow slaughter is on the supply side. This year's harsh late winter weather would appear to be encouraging producers to pare their cow numbers even further than they already have. Feed prices and availability have been challenges for a long time now – fairly acute challenges since last summer. March weather was unseasonably cold in much of the country. Where it wasn't cold, it was dry. Unfortunately, this dry area included regions of the Plains that have been plagued by drought since 2011. It seems entirely reasonable that the harsh late-winter season has contributed to increased culling activity among producers who were either unwilling or unable to locate and pay for supplemental feed to finish out the long winter.

Cattle on Feed Summary

At this point, the impact of increased cow slaughter on beef herd expansion is difficult to ascertain. Part of the reason for this is that we have a long way to go before we get another read on inventory and slaughter rates can ebb and flow quite a bit between now and then. Another reason is that increased beef cow slaughter can be offset by reduced heifer slaughter. To some extent, this appears to have been happening in recent weeks. Heifer slaughter as a percent of total slaughter has been consistently below year-ago levels for most of this year. Also, the January *Cattle* report indicated a 2 percent year-over-year increase in the number of beef replacement heifers held in inventory. The question moving forward is how many of those replacements will actually make it into the cow herd. The same factors that have encouraged increased culling of mature cows will also encourage increased liquidation of heifers that could have potentially served as replacements. Last week's Cattle on Feed report suggests that some of those potential replacements may have made their way to the feedlot in March. Table 1 shows the headline numbers from last week's Cattle on Feed.

Table 1. April *Cattle on Feed* Summary: Actual Figures vs. Pre-Report Estimates

	1,000 head	% of Previous Year	Pre-Report Estimates* Average	Range
March Placements	1,899	106.0	99.1	92.1 – 103.2
March Marketings	1,771	92.3	93.5	92.4 – 95.1
April 1 On-Feed	10,909	95.0	93.9	92.7 – 95.5

*Source: Dow-Jones Newswires via LMIC

Note that all of the numbers in the report were on the bearish side of expectations. The on-feed inventory figure was at the high end of the pre-report range. Marketings were just outside the low end of pre-report estimates. Marketings were expected to be below last year's level partly because this March had one fewer business day than last March, but the drop in marketings was larger than most had anticipated. Finally, placements were substantially above even the largest pre-report estimates. Among the major feeding states, the largest increase in placements was in Texas, which notched a 26 percent year-over-year increase. Kansas also saw a large increase: 13 percent year-over-year. This may indicate that deteriorating conditions caused some producers to cut backgrounding programs short, placing cattle in March that they had planned on holding over until April or May. Additionally, the larger than expected placements may indicate that a good many females that had been held for possible replacement duty were put on feed instead. Given how big the miss was on placement expectations, there is probably a bit of both going on.

Retail Meat Prices

While cattle and hog prices have been disappointing so far this year, retail meat prices have continued to increase. The average retail price for Choice beef reported by USDA Economic Research Service hit a record $5.30/pound in March. Pork retail prices have been a bit less impressive. The average Choice retail pork price in March was $3.466/pound. That is about a dime less than the record level set in September 2011, but it is up from just over $3.40/pound in January. So if retail pork and beef prices are higher, why haven't wholesale prices been pulled along with them? A look at the spread between wholesale and retail prices suggests that in historic terms, retail prices aren't yet really out of line with wholesale prices. Figures 3 through 5 show the wholesale to retail price spread (retail price minus the wholesale price as reported monthly by USDA-ERS) as a percent of the wholesale price for beef, pork, and broilers, respectively.

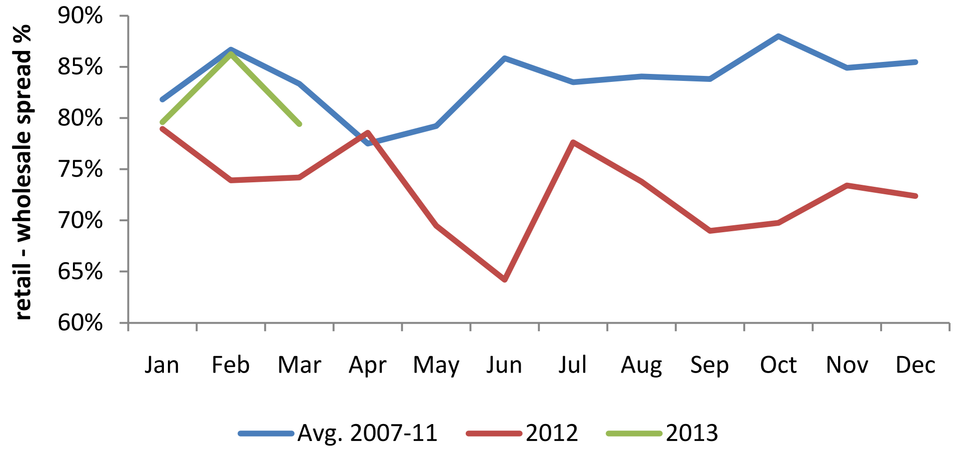


Figure 3. Wholesale-to-Retail Price Spread as a Percent of Wholesale Price: Beef
Data Source: USDA Economic Research Service

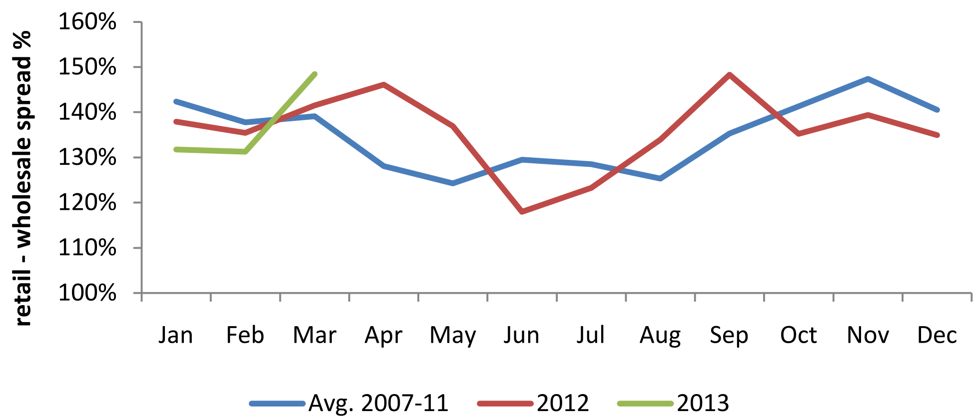


Figure 4. Wholesale-to-Retail Price Spread as a Percent of Wholesale Price: Pork
Data Source: USDA Economic Research Service

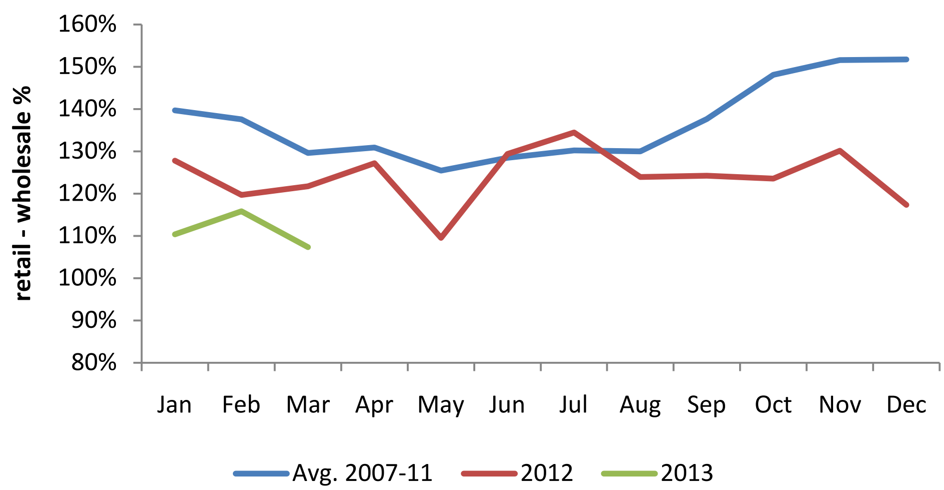


Figure 5. Wholesale-to-Retail Price Spread as a Percent of Wholesale Price: Broiler Composite
Data Source: USDA Economic Research Service

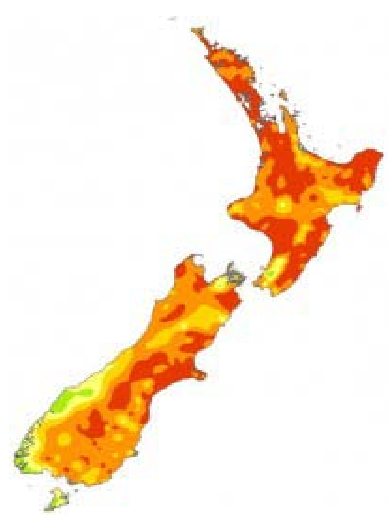
For beef, the spread between retail and wholesale prices is about in line with the 2007-11 average value. For pork, the March spread jumped above the historic average due to a fairly sharp drop in the reported wholesale price for March. Prior to that, the spread had been below the average. For the broiler composite, the wholesale-to-retail spread remains well below the 2007-11 average. The point of this is that retail prices haven't really gotten out of line with the wholesale market at this point. It appears, rather, that retailers are basically playing catch-up – at least on beef and pork. Having absorbed higher wholesale prices in the past, they now seem to be trying to move back to more normal margins. With respect to broilers, those margins appear to remain fairly tight as wholesale prices remain on an upward trajectory.

Dairy Outlook

The last couple of months have witnessed a significant turnaround for the dairy industry. Class III milk prices that were touching on \$17/cwt in March are now trading at or above the \$19/cwt mark. At the same time, corn futures have dipped more than \$0.50/bushel. You'll never see dairy folk smiling, but they are at least a little less grim than was the case a couple months back.

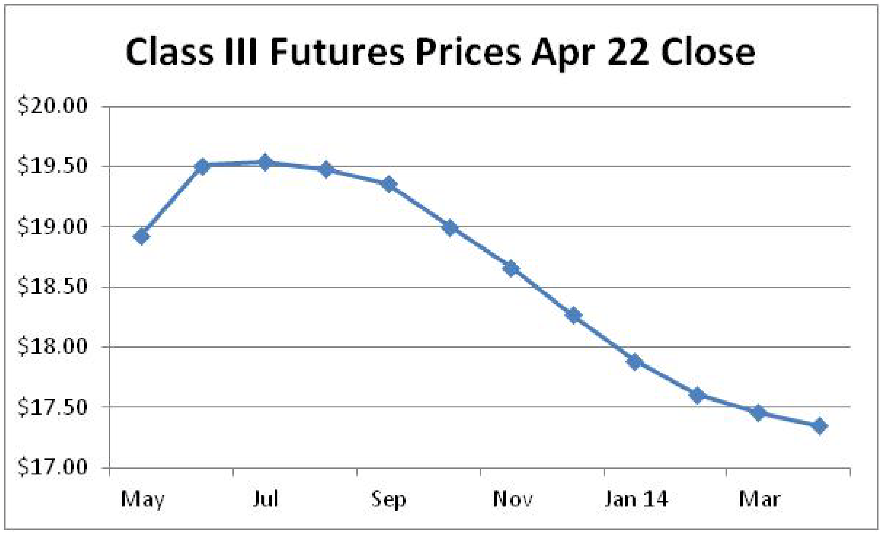
The causes for the dairy price move have come from supply concerns, both here and abroad. Milk production reported for February was officially down 3.3 percent, but after adjusting for the leap year differences, it was essentially unchanged from last year, which was the case for March as well. Production in California was down in March by more than 3 percent this year, but was offset by a 3 percent increase in Wisconsin.

One of the challenges in the March data, however, is the shift in reporting methodology National Agricultural Statistics Service (NASS) will use, due to the loss of survey information brought on by the sequester. NASS had originally said they would stop the milk production report all together, but several letters and other comments from the industry induced them to continue with the report, but to do so in a modified manner. Past reports have actually gone out and surveyed dairy farmers, getting a handle not only on milk production, but cow numbers directly and then been able to calculate production per cow. NASS, in order to continue to put out some kind of official estimate of milk production, will now lean on 'administrative' sources of data. Expect this data to come under question should anything unexpected show up.



The other production issue has been in New Zealand. Recall that their production is almost entirely grass-based. Unfortunately the included graphic did not bring across the legend, but the dark orange regions mean the same thing there that they would if this were a map of Texas – very dry conditions. Some reports are suggesting this is the worst drought in 30 years. Milk production is expected to be off 20 percent from last year's levels as the end of the season unfolds. And as one looks around the world to make up these shortfalls, about the only available supplies available are in the United States. This has been one of the causes for the uptick in cheese and powder prices over the last couple months.

Prices on the futures markets are reflecting some of this expected tightness and are holding fairly firm for the summer. Class III prices are above the $19/cwt level for the next several months which should translate to All-Milk prices well above the $20/cwt level. Price levels for the fall and into next year, however, reflect expectations of supply coming back both here and in the rest of the world.



The question is whether or not that expectation will be realized. Looking at weekly dairy cow slaughter data one gets the idea that so far this year at least, dairy producers are cutting back slightly. The combination of lower milk prices and higher feed costs would certainly have driven producers in that direction, but the recent movements may well be generating different ideas. The next few weeks are going to be critical in trying to suss out where prices might go toward the end of the year.