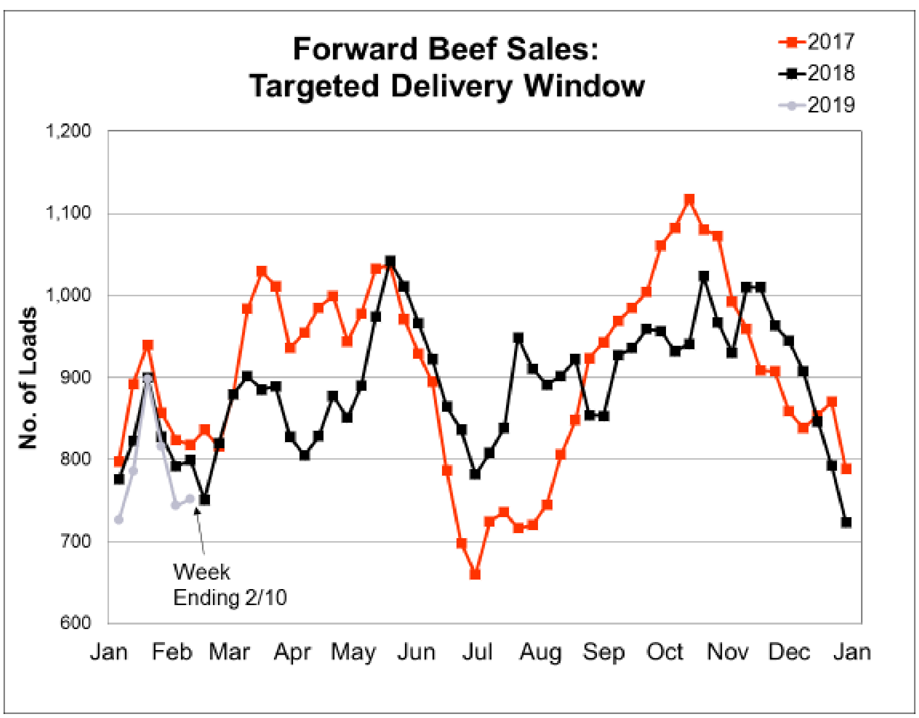
MEAT MARKETS
UNDER A MICROSCOPE

A perspective on the red meat markets by Kevin Bost...sometimes wrong, usually scientific, but always candid

January 9, 2019

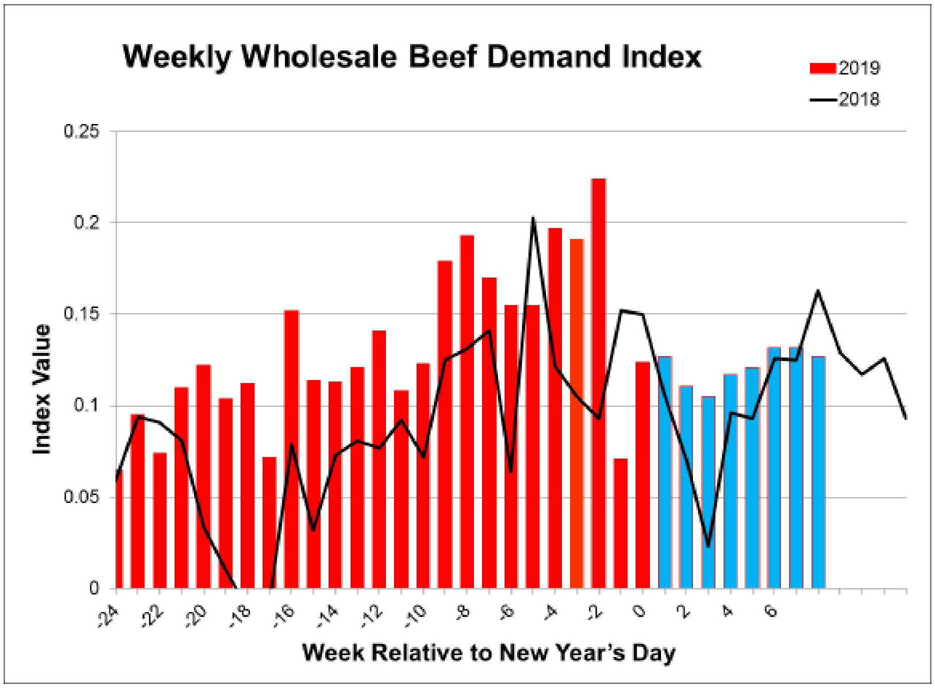
I was taken in by the impressive status of beef demand during December and the consistent tendency toward higher prices in January—not to mention the stubbornly bullish behavior of the futures market—and erred toward the notion that the market would mount a decent rally in January. But over the past week it has become evident that this is not going to happen.

The items that normally lead the charge in cutout values at this time of year are sputtering. I'm talking about bottom round flats and eyes, shoulder clods, ground beef, knuckles, and chuck rolls, in that approximate order. Normally, all of these show substantial gains between the immediate pre- and post-holiday periods; not so this time around.



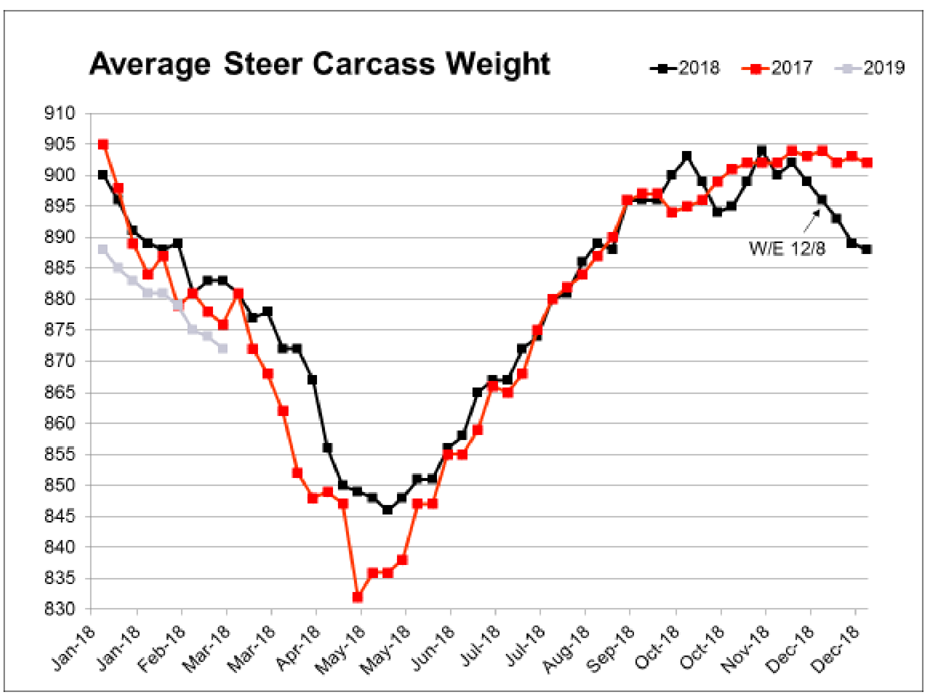
The most likely explanation for the sup-par performance is that supermarkets have backed away from beef features. We saw hints of such an impending "retraction" in the forward booking statistics over the last several weeks. It looks as though the volume of product booked for deliveries through early February have been below a year ago, while fed beef production *should* be up approximately 2.1% over the next four weeks. [This depends partially on carcass weights; I'll return to that subject in a second.] This is reason to think that demand will remain relatively sluggish through the end of the month.

Just what I mean by "relatively sluggish" is shown in the picture on the next page.



The first blue bar in this picture represents the week we are in right now. My assumption, then, is this: now that the short-term demand index has fallen back to where it stood in October, it will remain in that neighborhood at least into February. Expressed in English, now that demand has made a downward adjustment, it will undergo normal seasonal changes from this point. If this is to be the case, then the combined Choice/Select cutout value should move sideways between now and early February, not straying far from the current quote of $213 per cwt.

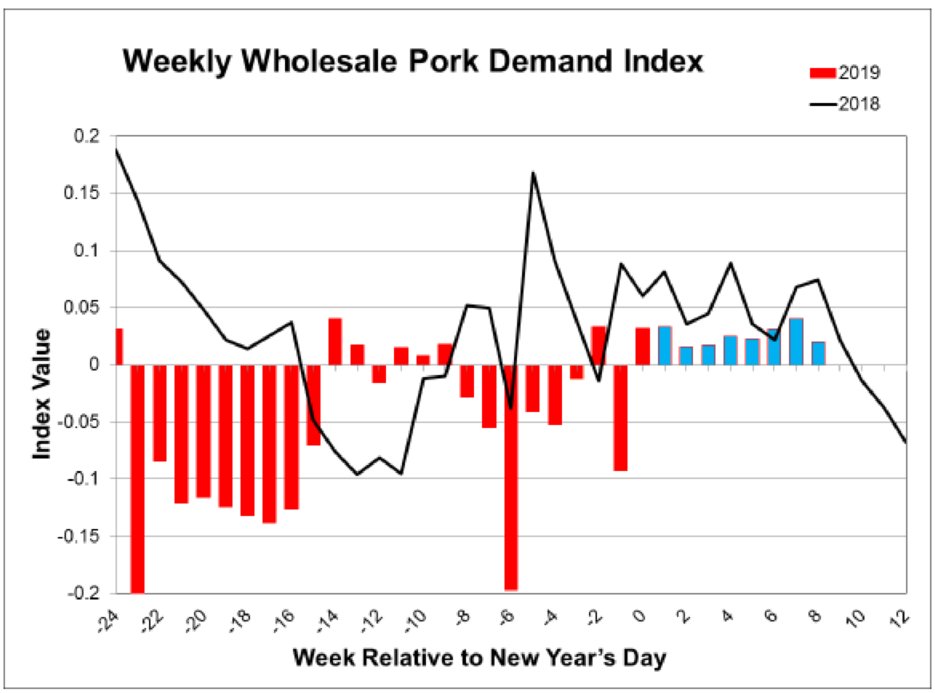
OK, so what *about* carcass weights? I hear a lot about terrible feedlot conditions and lighter-than-expected "weigh-ups", but these are subjective terms. We have not seen any official carcass weight data since the first week of December, and so we are left to guess. Here is mine:



Without going overboard, I'm factoring in a steeper-than-normal drop in carcass weights beginning in the second half of December, such that steer weights would average nine pounds below a year ago in January and February; heifer weights would be down 13 pounds. This is the best I can do until our government is back up and running.

I am anticipating that as beef struggles to move through the pipeline and "out-front" asking prices come down, retailers will step up their buying for second half February and March deliveries, and launch a major leg up in cutout values. Presently I am forecasting a peak in monthly average cutout values near $230 per cwt in May. This forecast assumes that net domestic beef supplies will be roughly 1.5% smaller than a year earlier in the first half (due to lighter carcass weights and a 5% increase in exports), and that wholesale beef demand will be significantly stronger than a year earlier. And yet, I wonder: why, really, should wholesale beef demand be any better than a year earlier? About the only reason I can think of is that it has been so since last August. But competition form the pork and chicken markets is more intense; retail beef prices are higher; and no one in the Beef World is talking about the possibility of a slowdown in the economy from its currently robust status….

In contrast, there are several reasons to expect wholesale pork demand to strengthen. As of the most recent reading, retail pork are down significantly from a year earlier, and retail margins are wider. Supermarket features should be both prominent and consistent through the winter, and there is a good chance that "everyday" sticker prices will be reduced as well. This would mainly benefit loins, butts, and ribs. One would *think* that cheap prices in just about all parts of the carcass except bellies would spur demand from foreign buyers, despite the continued existence of tariffs in Mexico and China. Finally, opposite the situation in the beef market, wholesale demand is recovering from depressed levels:



I am not really including much of a recovery in demand through February in the pricing equation, and even so, I am coming up with a cutout value of roughly $75 per cwt by the end of the month (compared with this afternoon's quote of $69.67).

The loin market still seems to possess the greatest upside potential, for obvious reasons. The track record of this market shows a consistent tendency to rally over the upcoming three-week period, and it seems reasonable to think that the extent of a rally this time around could go well beyond the average. The greatest appreciation in bone-in loin prices over this time frame has been 27.5%, that occurring in 2016; and in 2016 the market stood 12¢ per pound higher coming out of the New Year's holiday than it stands today. Extreme, perhaps, but possible? Why not? To spare you the sophisticated number-crunching, a 27.5% rally would carry prices up to $.96.

Hog slaughter should be a supportive influence on the entire pork market in the weeks ahead. It looks as though this week's kill will wind up near 2,550,000, 4.5% above a year ago. If USDA's summer pig crop estimate was on the mark, then next week's total should drop to 2,500,000 and remain there through the end of the month; that should be followed by an average of 2,440,000 in February.

Meat Markets Under a Microscope is published weekly by Procurement Strategies Inc., 99 Gromer Road, Elgin IL 60120. For subscription information, please contact Kevin Bost at (847) 212-7523, or visit our website at www.procurementstrategiesinc.com.