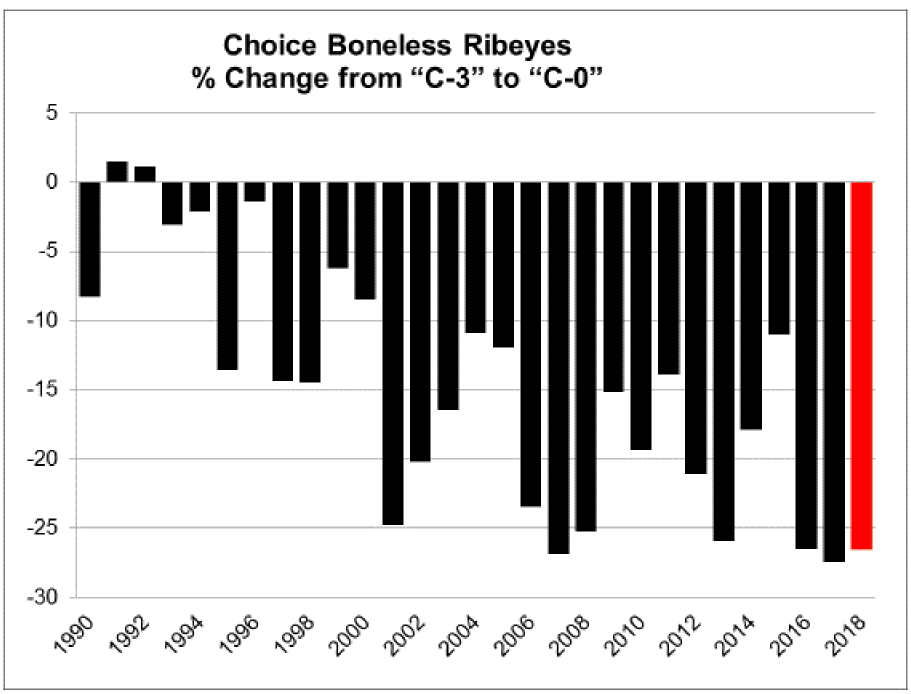
MEAT MARKETS
UNDER A MICROSCOPE

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

December 5, 2018

While the beef market remains fairly well-balanced for the time being, it looks as though cutout values should be back-tracking over the next couple of weeks. Of greater consequence, though, is that the prospects for wholesale demand in January are not exactly "rosy".

Of course, the near-term downward pressure will be mainly driven by rib cuts and tenderloins. How much downside potential is there?

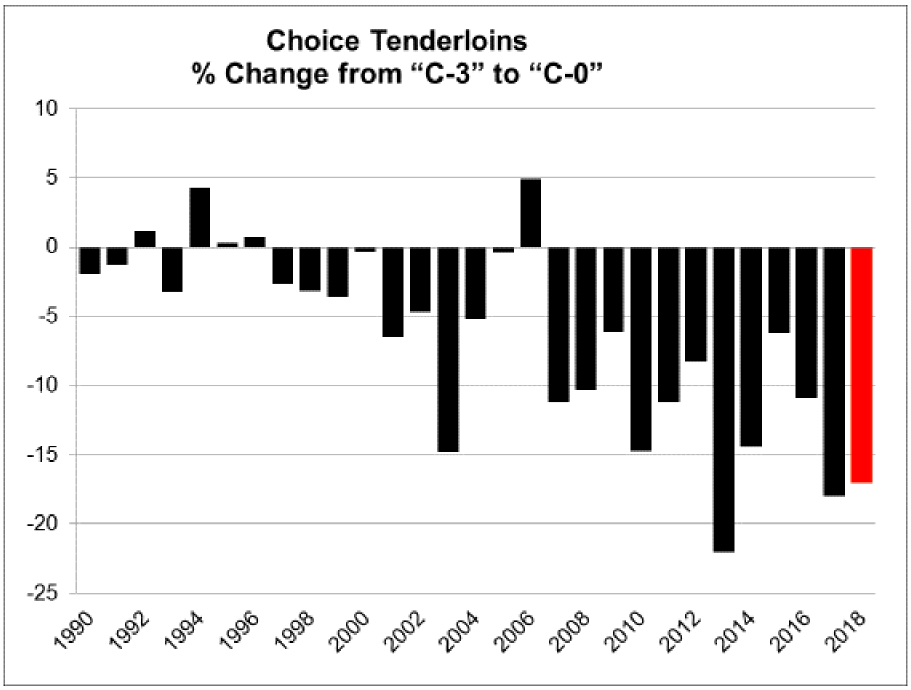


Even though the economy is unquestionably strong, I can't think of a good reason why the seasonal decline in rib prices would be any different than usual. Thus, something on the order of 26% would seem to be a reasonable expectation. If we call this week's market $8.85 per pound, then a 26% decline would take it down to roughly $6.50. Last year it averaged $6.28 during the week of Christmas, and so the notion that robust consumer spending should hold prices above a year earlier remains intact.

The prospects for their Select-grade cousins are somewhat different. The equivalent picture (as that shown above) for Select boneless ribeyes suggests that a pullback of 12-13% is likely. That would place them just above $6.00 per pound, which approximately 50¢ above their trade levels of Christmas week 2017.

Prices of these sorts for boneless product would align with Choice bone-in ribeyes at about $6.10, and Select at $5.35.

As for the tenderloins, a decline of 17% between now and Christmas would clearly be steeper than average, but it would make sense from the standpoint that it would carry this market down to about $9.75, which is the nearest discernible support level on the chart. Plus, it would still place the "PSMO" about 50¢ above its trade level during Christmas week 2017….and it would practically match last year's performance:



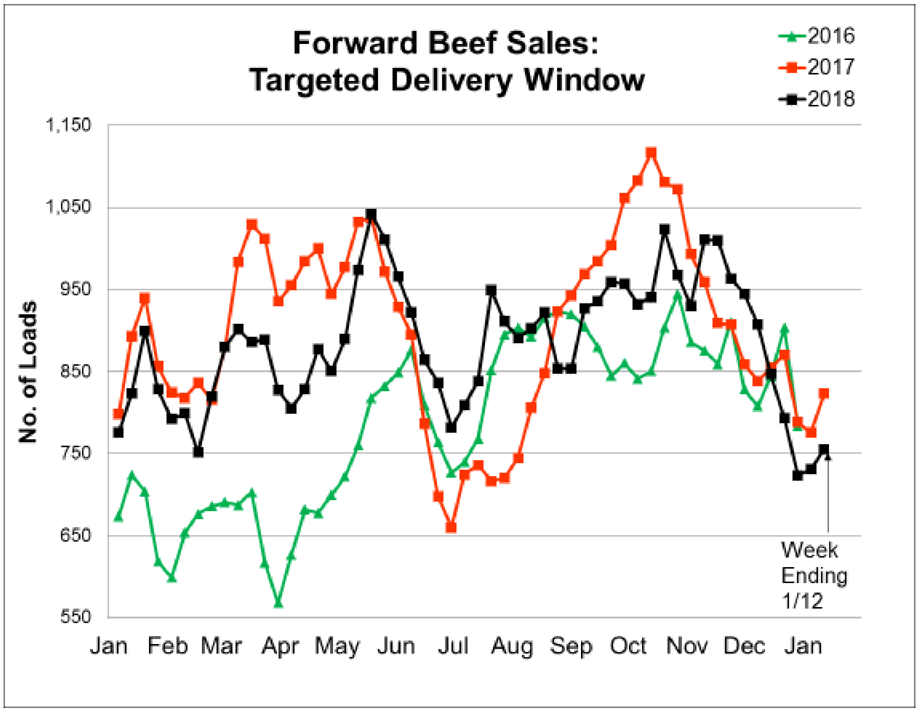
In the case of Select-grade tenderloins, my best guess is that these are headed back to $9.25, *maybe* $9.50. This would make for a record drop over the upcoming three-week period, and I am usually hesitant to predict such things; but I notice that in each of the past three years, Select tenderloins have wound up at $9.15-$9.20 during the week of Christmas. True, this item is trading *way* above a year ago right now. But if I can say with a straight face that the Choice version will be worth $9.75, then I have to believe that the Select equivalent will be no higher than $9.50.

A third item that I expect to pressure cutout values in the near term is 50% lean trim. I must say that this market's recent resilience has surprised me. I didn't think it would still be clinging to $.70 per pound at this time. However, its track record shows a bit of a downward bias over the upcoming three-week period, and prices have not been this high in the first week of December since 2014. A simple average decline would take them down about a nickel, but four times in the last 15 years they have lost between 10¢ and 20¢.

So then, if we slot the Choice boneless ribeyes at $6.50; Select ribeyes at $6.15; Choice tenderloins at $9.75; Select tenderloins at $9.50; and 50% lean trimmings at $.65, then together this group would shave roughly $10 per cwt off the combined Choice/Select cutout value by Christmas—if all else were to remain the same, that is.

But all else will not remain the same. All chuck and round cuts, as well as briskets, have a remarkably consistent track record of trading higher during the week of Christmas than three weeks prior. Ditto for top butts. Both Choice and Select-grade strips/short loins show an historical bias toward the upside as well, although it is not as pronounced. Thus, it's hard to bet against higher money in any of these items. Together, they should offset most of the negative impact on cutout values delivered by the rib cuts, tenderloins, and "50's". How much? My guess is 60-70%....which would place the next low at $206-$207 per cwt in the week ending December 22.

Forward booking volumes for January delivery have been quite unimpressive so far. Here is an updated look:

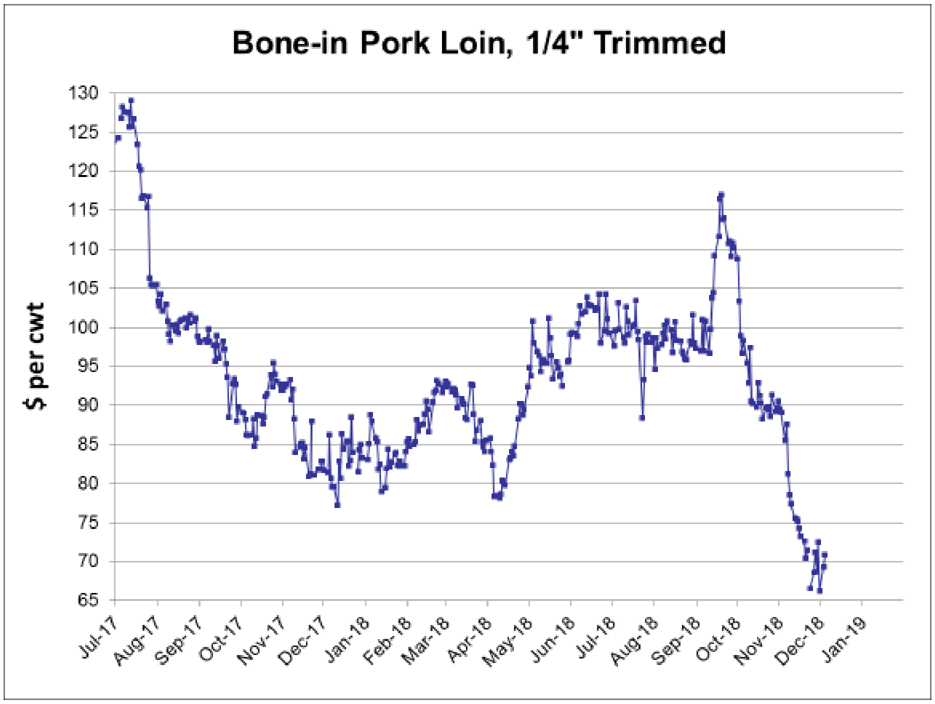


What this does, of course, is sedate the prospects for the seasonal rally in cutout values that typically begins during the holiday weeks and extends through mid- or late-January. The chart to the left suggests that retailers are *not* planning to feature beef as prominently as they did last year. This makes sense, as the opposite situation seems to be developing in the pork market.

Keep in mind that fed cattle slaughter will—in my humble estimation—exceed a year earlier in January by 10,000-15,000 per week, or about 3%. Indications are, then, that packers will have more product to sell in the spot market, which is not bullish of prices. At the moment, I'm thinking that the combined cutout value will make its way back up to its most recent high ($215 in the first week of November), but not beyond….not until February, anyway.

Bone-in pork loins are a candidate for Best Value on the Planet right now. I don't need to show you a picture of the seasonal history of this market, because you already know what it looks like. Boneless loins also have a distinctly upward bias into the holidays. But the extent of the presumed rally should be magnified this time around, because of the cheap price level. Naturally, the low product costs have caught the attention of meat buyers, and the word in the Sewing Circle is that supermarket features will be focused on pork loins, butts, and ribs (but especially loins) both prior to and beyond the holidays.

I consider that a 20¢ per pound rally in the bone-in loins would be worth about $5 to the cutout value. And the potential is greater than that, since a rally from $.70 to $.90 per pound would do nothing to deter promotional plans that are already in place.



For the reasons I just described, it would be safe to say that pork butts and ribs, though not having the same amount of upside potential, should be well-supported over the next several weeks (and perhaps into January as well).

The belly market could be described similarly. Having risen 10¢ per pound over the past week, it has clearly demonstrated that the fourth quarter low is "in". Setting aside the speculation on first-quarter upside potential for now, I think it's fair to say that there is no material downside potential in this market through the end of the year.

What makes the near-term outlook for the pork cutout value different from most years is that there is *probably* not as much of a post-holiday drag stemming from the ham market this time around. And this is simply because prices have not been this cheap at this point in time since 2003. There is hardly any "air" to be let out of the balloon, so to speak. If the market begins to perceive—or even guess—that stronger exports to both Mexico and China are just around the corner, then the next major low in ham prices will probably only match the weekly low established in the second week of November, at $49.50 per cwt. I'm assuming this to be the most likely scenario. In such case, the decline in ham prices would not offset the rally in the loin market, let alone the strength that could be coming from other parts of the carcass. Odds are that the cutout value will be a couple dollars higher at the end of the month than it is right now….and by "a couple" I mean two. This would be a rare occurrence indeed. Only three times in the last 22 years has the pork cutout value gained any ground over the upcoming three-week period.

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.