

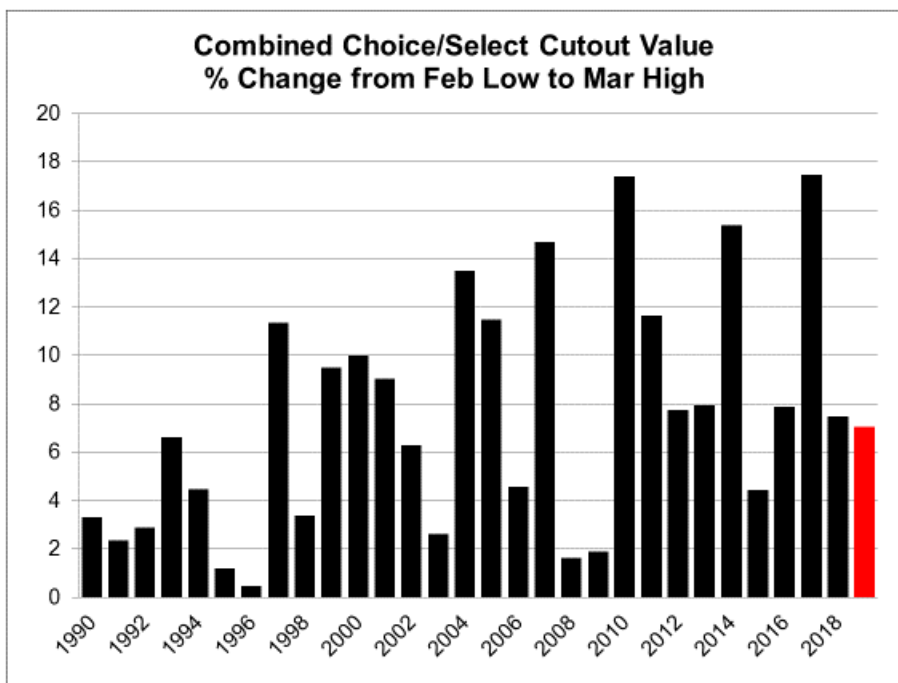


MEAT MARKETS UNDER A MICROSCOPE

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

February 9, 2019

Beef cutout values have an obviously consistent tendency to rally into March, and so it would be hard to bet against it happening again this time around. As one who is waiting for the right time to bet on the short side of the April and June futures contracts, my focus at the moment is on the extent of that rally. Naturally, it is an important consideration.



I include my humble forecast in the picture to the left, which is for a slightly smaller increase from the February low to the March peak than we witnessed last year, and which places the highest weekly average in March at about \$228 per cwt. I am assuming that the February low will be near \$213, which could be registered this coming week. It was quoted Friday at \$216.68.

As you probably know already, the Choice-grade middle meats are typically most important in determining the course of cutout values between now and the end of March. The 20-year correlation between this group and the combined cutout from the February low to the March peak is 70%; it is 51% for the “thin meats”; 46% for the Select-grade middle meats; 37% for the Choice end meats; and just 27% for the ground beef/trimmings complex.

I should explain that the composites I am using to calculate these correlations are defined as simple (unweighted) averages of the following groups:

Middle Meats: boneless heavy ribeyes, 0x1 strips, top butts, and tenderloins

Thin Meats: briskets, ball tips, tri tips, flap meat, flank steaks, outer skirts, and cap meat;

End Meats: Shoulder clods, chuck rolls, knuckles, bottom round flats, XT inside rounds, and round eyes;

Ground Beef/Trimnings: 81% lean ground beef, 50% lean trim, and 90% lean grinding beef.

I realize that lumping these together without weighting each product by its share of the carcass weight is not as precise as it could be, but it serves its purpose. It is Kindergarten analysis, but at its most sophisticated level.

Anyway, I notice that the Choice and Select middle meat composites, as well as the thin meats, are priced substantially higher than they were at this time last year....and I suspect that this will leave less room for appreciation in these items into March.

	Last Week	Year Ago	Mar '18 Peak
CH Middles	\$6.66/lb	\$6.17/lb	\$7.08lb
SL Middles	\$6.43	\$5.86	\$6.61
CH Ends	\$2.45	\$2.42	\$2.41
CH Thin Meats	\$3.82	\$3.46	\$4.05
Grinds/Trim	\$1.50	\$1.57	\$1.63
Combined Cutout	\$216.13/cwt	\$207.53/cwt	\$223.04/cwt

More specifically, I have to wonder how aggressively supermarkets will try to feature ribeyes or strips of either "flavor" in March, in view

of the product costs they will be facing. As best I can tell, forward price offerings for March delivery of Choice rib cuts have been at least 50¢ per pound above a year ago; in the case of Choice strips, they have been at least 30¢ higher. Remember, forward booking activity for March delivery, in general has been just OK....not slow, really, but short of a year earlier.

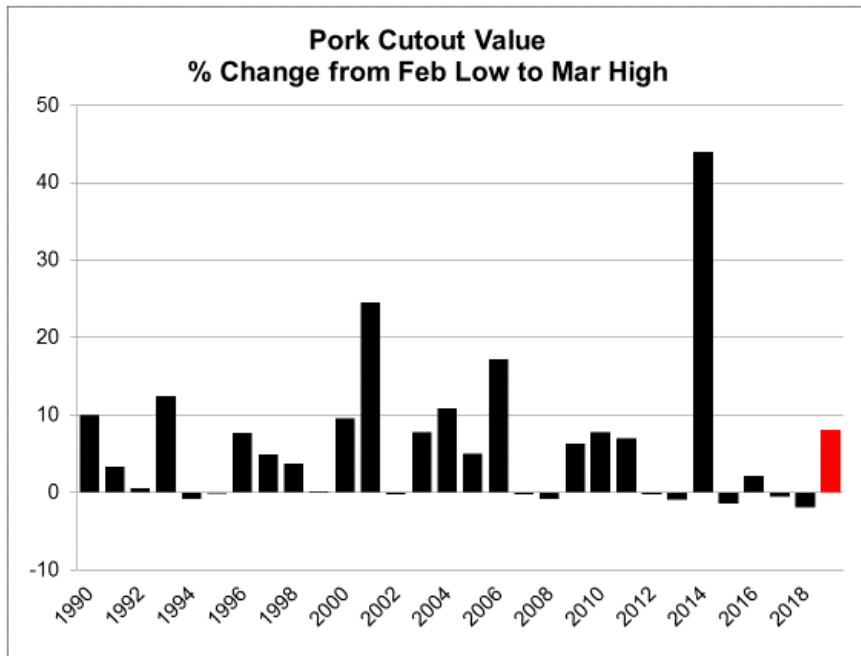
	Last Week	Year Ago	Mar '18 Peak
CH Bnls Ribeyes	\$7.59/lb	\$6.80/lb	\$8.20/lb
CH 0x1 Strips	\$5.40	\$5.10	\$6.73
CH 0x1 Short Loins	\$5.01	\$4.68	\$5.79
CH Top Butts	\$3.62	\$3.48	\$3.46
CH Tenderloins	\$10.02	\$9.30	\$10.06
SL Bnls Ribeyes	\$7.02	\$6.36	\$7.60
SL 0x1 Strips	\$5.21	\$4.41	\$5.55
SL 0x1 Short Loins	\$5.13	\$4.48	\$5.53
SL Top Butts	\$3.55	\$3.44	\$3.53
SL Tenderloins	\$9.93	\$9.24	\$9.82

Why should prices this March be capped at last year's peaks? I'm not saying that they have to. I'm just saying that they may not extend much beyond those peaks. I'm

looking for steer and heifer slaughter to average near 480,000 per week in March vs 470,000 a year earlier. As it relates to whole-muscle cuts, the "piece count"—and therefore the slaughter rate—is more important than carcass weights and total tonnage.

Finally, a weekly peak of \$228 per cwt and a monthly average of \$225 or so in March assumes that wholesale beef demand will be modestly stronger than a year earlier, and from that angle, my forecast might even be a bit optimistic. So far, the demand index in February is shaping up to be equal to a year ago.

The opposite condition exists in the pork market. Prices are cheap, and I would *think* that this would be reason to expect demand to improve as we go along. The demand readings since mid-January have been quite unimpressive. And my forecast of a greater-than-normal increase in the pork cutout value from the February low to the March high does *not* include any material improvement in demand. It probably *should*, but I must admit that I am “snake-bit”—and a little lighter in the wallet—because of the market’s recently poor performance. I am assuming that the cutout value, quoted at \$64.82 per cwt on Friday, is essentially on bottom right now. On that subject, although hog slaughter is now tracking a bit high in relation to USDA’s summer pig crop estimate, it is still likely to drop down to 2,470,000 within the next couple of weeks from this past week’s total of 2,516,000. Naturally, that will be supportive.



As it stands—i.e., without much help from the demand side of the equation—my guess is that weekly average cutout values will reach \$71 or slightly above in March. That would still fall about \$5 short of the March 2018 peak. As long as we’re comparing with year-ago numbers, I should acknowledge that it net domestic pork supplies should be about 2.5% larger than a year earlier in March. This projection

includes an average weekly kill of 2,470,000; a small net out-movement of freezer stocks vs. a small increase in March 2018; and total exports of 563 million pounds vs 538 million last March. The increase in exports, by the way, is accounted for by Japan, Korea, Columbia, and Australia—not China or Hong Kong. It looks like that’s going to be May or June before we can expect much of an acceleration in exports to China. However, based on the comic books that I read, there is a decent chance that Mexico’s 20% tariff will be removed sometime in April.

	Current	Year Ago	Mar '18 Peak
Bn-in Loins	\$.82/lb	\$.87/lb	\$.91/lb
Strap-on Bnls Loins	\$1.15	\$1.13	\$1.14
Butts	\$.78	\$1.01	\$1.02
Spareribs	\$1.38	\$1.43	\$1.48
23-27 lb Hams	\$.44	\$.56	\$.62
Bellies	\$1.19	\$1.30	\$1.11
Bnls Picnics	\$.60	\$.78	\$.80
72% Lean Trim	\$.54	\$.69	\$.68
42% Lean Trim	\$.30	\$.28	\$.44
Cutout Value	\$65.98/cwt	\$77.41/cwt	\$75.73/cwt

Clearly, the items holding the greatest upside potential are butts and hams, and boneless picnics and lean trimmings are also trading far below year earlier levels.

Further on that subject, the fact that pork belly prices started to break in the third week of January enhances the possibility that retail bacon featuring will become more active in March. Last year, this market was just now peaking at this time (at \$1.51 per pound), capping a 40¢ rally after the holidays; retailers were backing away from March promotions, which probably contributed to the crash in prices during March. I'm not real confident about this, but it makes some sense, does it not?

As for the main drivers of the cutout value into March, the correlations with boneless and bone-in loins are the strongest at 80% and 78% respectively. These are followed by lean trimmings at 73%; bellies at 69%; boneless picnics at 68%; hams at 63%; and butts at 51%.

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