MEAT MARKETS
UNDER A MICROSCOPE

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

March 19, 2018

First of all, I wish to apologize for running behind my publishing schedule. I have been preoccupied with satisfying the onerous regulations of the National Futures Association in order to maintain my registrations. Perhaps they are not such a burden for a large trading firm, but for a guy like me, doing business out of a shed in the back yard, this process takes up a lot of time. I dream of upgrading to a Boiler Room someday….

The huge supply of cattle eligible for slaughter in the second quarter has become well-advertised. It is being described as a "Wall of Cattle", which makes me cringe because I have heard this metaphor many times before in my career, and often the wall turns out to be not so high. But whenever it fails to materialize, it is because cattle feeders and meat traders make preparations for it in advance, and thereby dampen its impact. Specifically, cattle feeders tend to market cattle aggressively during such times, knowing that bigger supplies lie ahead and seeing the discounts in futures prices. This is precisely what I expect to happen this spring.

That will not alleviate the supply-side pressure on the market in the second quarter; in fact, it will add to it. Sooner or later, the larger supply must be absorbed…. if later, then cattle supplies will become backlogged and the consequences will be more severe. This is a less likely outcome, I think.

So, then, I am expecting that fed cattle slaughter will increase from 467,000 per week so far here in March to an average of 485,000 in April; 515,000 in May; and 530,000 in June. The increase from first to second quarter would match the greatest of the past ten years. As a reminder, the reason for this steep rise is the large number of feeder cattle that were placed in feedlots last fall and through the winter. Fourth quarter 2017 placements were up 9% from a year earlier, and in January-February they were up 5%. [It looks very much as though they will fall below a year earlier in March through June, because placements have been "pulled forward"; but that is a different topic for another time.]

The increase in net domestic (per capita) beef supplies, after including carcass weights, cow slaughter, and imports/exports in the equation, will be substantial. My humble projections are shown on the next page, along with a detailed breakdown of expected U.S. beef exports by country of destination. As always, if you find anything absurd in these numbers, I trust that you will tell me where I've gone astray.

Oh—and I should point out that in these supply projections, I am assuming that carcass weights will follow a seasonally normal path, even though a combination of more "calf-feds" (lighter in-weights) and aggressive marketing rates would seem to argue in favor of a steeper-than-normal decline in slaughter weights, as we saw last year. I'm still pondering this question.

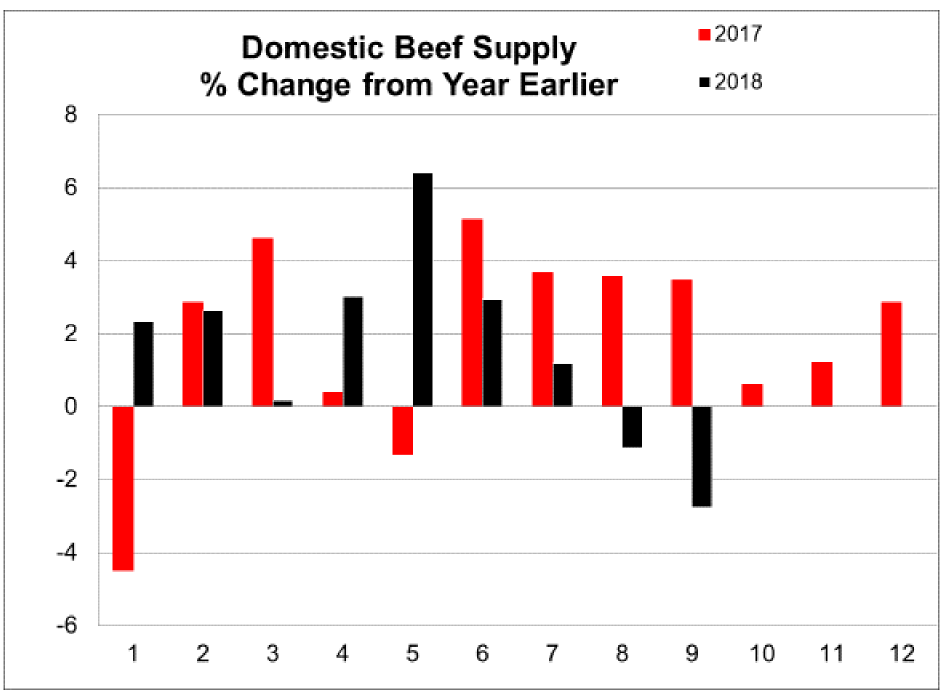
U.S. Beef Exports in Million Pounds and Change from Year Earlier

	Q1		Q2		Q3	
	Volume	Change	Volume	Change	Volume	Change
Japan	210	+6%	238	+17%	239	+2%
China/Taiwan/HK/Vietnam	133	+32%	127	+9%	133	+12%
Korea	122	+16%	115	+8%	132	+5%
Mexico	97	+2%	104	+4%	112	-1%
Canada	74	-6%	82	+9%	75	-5%
Total	713	+10%	748	+10%	776	+4%

…. and as long as we're at it, here are the imports:

U.S. Beef Imports in Million Pounds and Change from Year Earlier

	Q1		Q2		Q3	
	Volume	Change	Volume	Change	Volume	Change
Australia	156	+10%	195	+17%	215	+2%
Canada	174	+15%	180	-6%	202	-4%
New Zealand	195	+20%	215	+20%	132	-4%
Mexico	135	-8%	153	+5%	158	+6%
Total	756	+8%	849	+5%	817	0%



Notice that as far as I can tell, the U.S. is buying, and will continue to buy, more beef than it sells to foreign countries. [Most of the imports consist of grinding beef, while whole-muscle cuts account for most of the exports.]

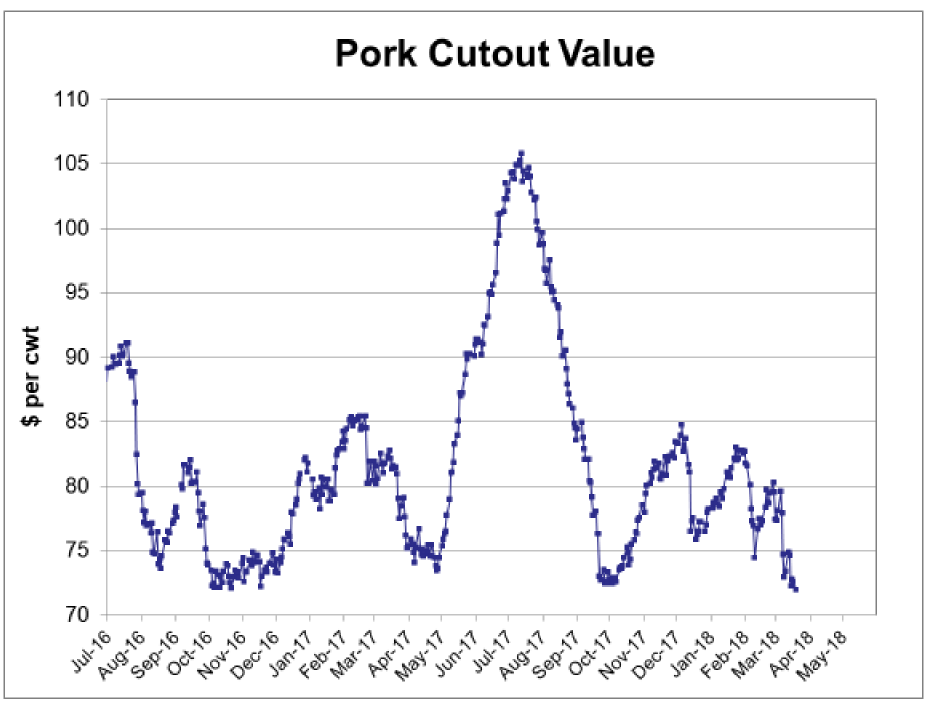
Anyway, as I stated a little while ago, the market will have to absorb the large supply either sooner or later, and it will do so by keeping prices subdued. For the past ten—going on eleven—months, demand at the wholesale level has been considerably stronger than a year earlier. That's long enough to conclude that this is enduring strength, not the product of an ephemeral "wave" or cycle…. which may have something to do with the robust economy, to state the obvious.

Having said that, it seems quite unlikely that wholesale beef demand will match the extreme spikes that we saw in May and June 2017. I notice that the ratio of wholesale to retail prices, as reported by USDA, is narrower than it was at this time last year, and it has been so for the past twelve months. And I hear from pretty good sources that retailers are generally dissatisfied with their margins in the meat department. Thus, it seems doubtful that supermarket beef features will be very aggressive, at least for the next couple of months.

If wholesale beef demand merely follows a typical seasonal course from this point forward, then the combined Choice/Select cutout value should average about $217 per cwt in April; $219 in May; and $216 in June. It was quoted this afternoon at $223.50.

If the pork cutout value is not on bottom right here, then it is this [ ] close. My reasoning is simple:

- As the chart below shows, it currently lies in an obviously major support level, one which has not been penetrated in 26 months;
- Hog slaughter should take another step downward starting next week, to 2,350,000 from the current rate of 2.4 million-plus;
- The seasonal track record shows no bias in either direction into Holy Week from the week prior, having slipped backward seven times in the last 15 years; gained ground six times; and held steady twice. From the week of Good Friday to the following week, it has lost ground only three times in the last 15 years;
- The most frequent timing of the "Post-Easter" low in the ham market is the week ending with Good Friday;
- Pork belly prices and ham prices are currently quoted only 3¢ and 2¢, respectively, above their natural support levels of $1.00 and $.50 per pound. As best I can tell, none of the other major pork products shows a weakening undertone.

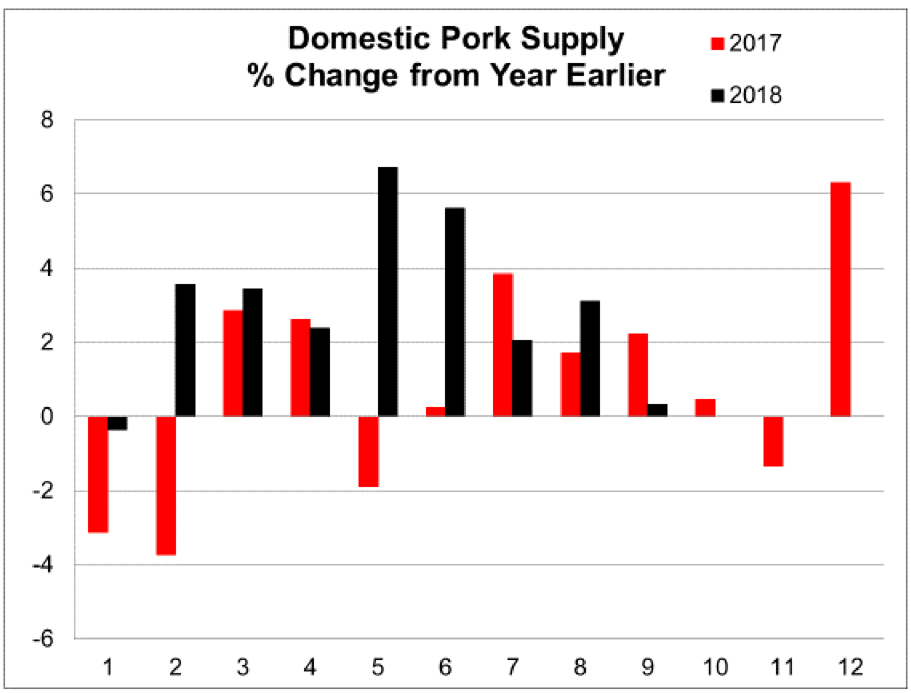


There is another individual item on the menu that is worth mentioning, and that is the pork loin. In spite of the substantial year-over-year increase in domestic pork supplies that I show on the next page, the loin market is subject to a surprising rally, one which may "launch" a bit earlier than normal ("normal" would be the second half of April). This item is particularly wellsuited for retail promotions. Bone-in loins are matching a 19-year low for this point on the calendar, and they trade 15¢ per pound below a year ago; and prices have hardly budged since early February.

I'll finish today by showing the pork equivalents to the table and the graph on the second page:

U.S. Pork Exports in Million Pounds and Change from Year Earlier

	Q1		Q2		Q3	
	Volume	Change	Volume	Change	Volume	Change
Mexico	453	-3%	442	+4%	457	+8%
Japan	329	+3%	318	+3%	295	+6%
China/Taiwan/HK	149	+10%	168	-6%	96	0%
Korea	172	+10%	148	+11%	90	+18%
Canada	123	-1%	132	+3%	140	0%
Australia	66	+8%	58	+25%	48	+18%
Colombia	52	+20%	46	+22%	50	+14%
Total	1476	+3%	1463	+3%	1312	+7%



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