

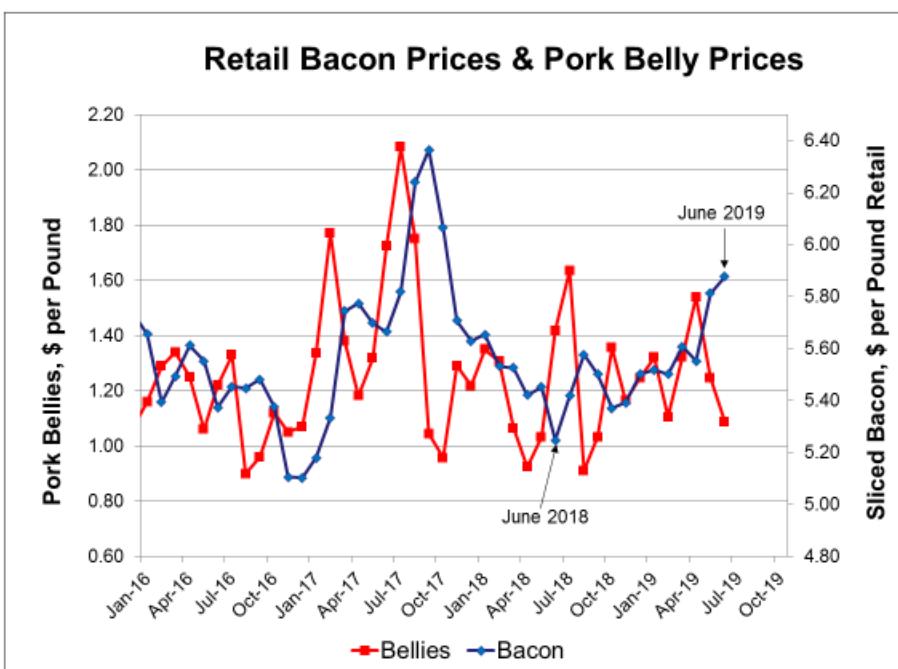


MEAT MARKETS UNDER A MICROSCOPE

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

July 17, 2019

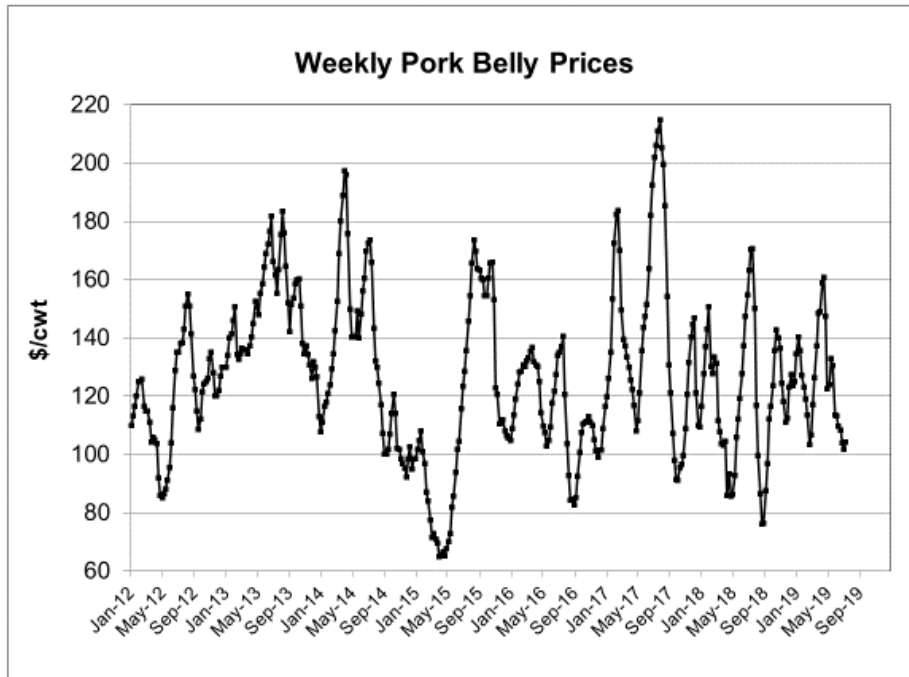
I'm going to pick up where I left off last week, and that was on the subject of pork bellies. It's not that I have an obsession with pork bellies, but let's face it: the path taken by the pork cutout value over the next two months will be dictated by the pork belly more than any other single component.



A look at retail bacon prices helps explain why this market has been so weak lately (along with the carcass weight issue that I discussed last week). The U.S. Commerce Department reports that retail prices of packaged bacon averaged 63.1¢ per pound above a year ago in June, after having risen 32.6¢ over the last two months.

I think the central consideration here, as it relates to the price outlook, is the *direction of the next significant change* in retail prices. And the key is probably the retail margin--which has become very wide. I'll spare you the additional graph, but the ratio of pork belly prices to retail bacon prices is approaching a three-year low. The wide margin leaves room for supermarkets to drop their sticker prices--arguably, the competition forces them to do so--which, in turn, speeds up the rate of flow through the pipeline and increases demand for pork bellies. Whereas the quantity demanded from the foodservice sector is relatively constant, it is more volatile in the supermarket sector; thus the supermarket channel acts as the primary regulator in the short run. I am told that bookings for mid- and late summer are quite active, which makes perfect sense from this angle.

And so the belly market is probably coiling up for a big rally. It is hardly a bold prediction, given that prices have not been this cheap in the middle of July since 2009. The fact that this presumed rally will be launching so late in the season likely means that it will extend late into month of August this time around. And if that turns out to be the case, then pork bellies will be a bearish influence on the pork cutout value in September. Last year, the situation was quite the opposite: prices peaked in the week we are in right now, and they plunged about \$.85 per pound by the middle of August.



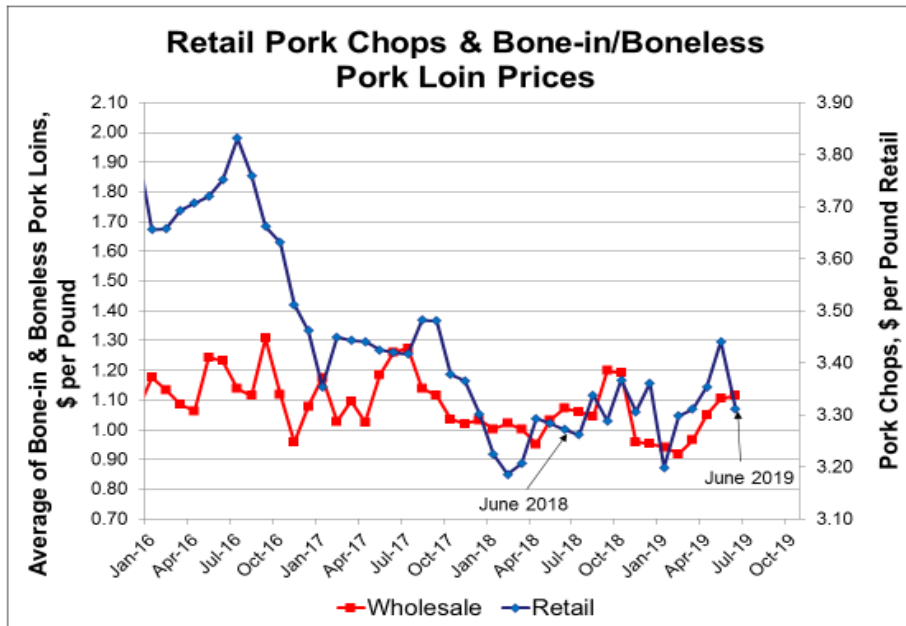
This summer's peak is naturally difficult to call, but the long-term chart seems to suggest that something in the \$1.80 per pound range could be within reach. Why not, if export business ramps up as expected? A move from \$1.10 to \$1.80 would add roughly \$11 per cwt to the pork cutout value.

Let's extend this discussion to pork loins.

On the next page I show the equivalent picture of wholesale and retail prices. In this case I am comparing the simple average price of $\frac{1}{4}$ " trimmed, bone-in loins and boneless, strap-on center-cut loins with the retail category labeled as "All Pork Chops".

This picture is not nearly as bullish of demand at the wholesale level as it is for bellies. While retail pork chop prices did drop 12.9¢ per pound from May to June, they are still 4.0¢ higher than a year ago; and more importantly, the spread between wholesale and retail prices is relatively narrow. I'm interpreting this to mean that we are unlikely to see a significant decline in retail prices through the summer, meaning that demand for pork loins should follow a seasonally typical path between now and Labor Day.

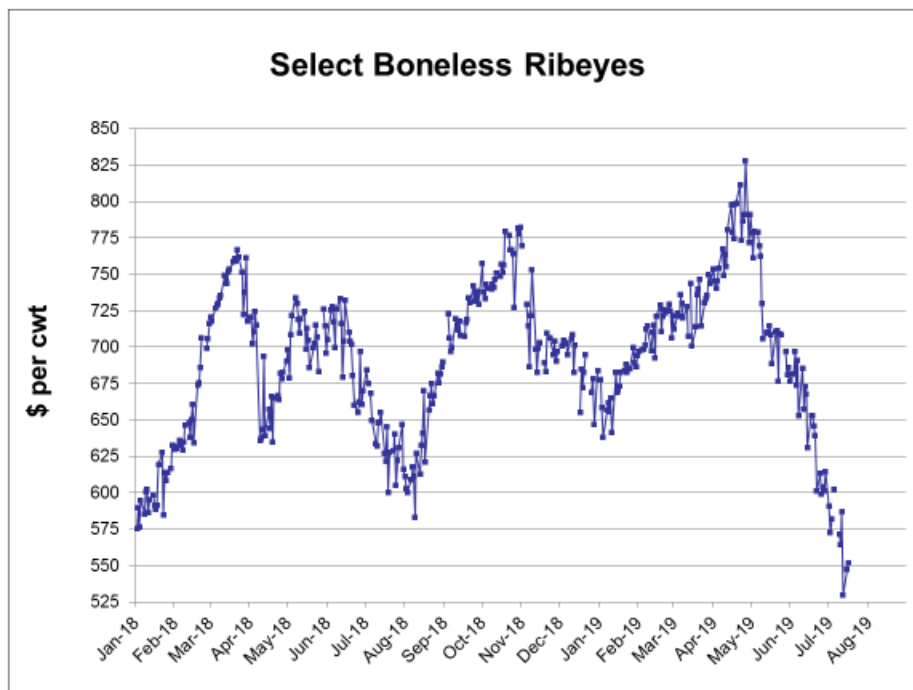
And what does *that* mean, exactly? Well, my approach is to assume that pork loins will continue to carry a relatively small share of the total cutout value--the ratio of the former to the latter has clearly been trending downward over time--and yet loin prices should benefit from the "rising tide lifts all boats" phenomenon, as they did in March. My guess is that $\frac{1}{4}$ " trimmed, bone-in loins will average \$1.05 per pound in August, and strap-on boneless loins will average near \$1.25. Ho hum.



I won't drag you through the same degree of detail, but the near term demand indicators in the beef market are generally neutral right now. Retail margins have widened out over the last two months, but currently they stand in only "moderate" territory....leaving some room for more aggressive

retail featuring in August, but not a whole lot. Likewise, forward booking activity for August delivery has been OK--not great, not bad, just OK. This past week's volumes were excellent, but when they are combined with the previous couple of weeks, the total is not terribly impressive.

One thing that *is* impressive, and certainly worth noting, is how cheap Select-grade middle meat prices have become.



I'm showing you the Select boneless ribeyes, but the picture is similar for strips and short loins. I don't think I'd be going out on a limb to say that this market is probably making its low for the rest of the year right now. Just by looking at 15-year average prices for each week, one would conclude that the seasonal bottom is not "due" until the middle of September. However, the

pattern has changed in recent years. In the last two years it landed in the second week of August, and in both instances the low was in the neighborhood of \$6.10 per pound; last Friday, the daily weighted average quote reached down to \$5.30. Not since 2013 has the August-November low been below the prices that are trading today. It's not really common for this market to show a material improvement between now and Labor Day, but think about it: Select boneless ribeyes at \$5.30; Select 0x1 strips and 0x1 short loins at \$3.60; Select top butts at \$2.50....why would those who carry Select-grade product *not* use these items to attract customers with steak features in August?

COPYRIGHT NOTE: To those of you who subscribe to my reports, I thank you sincerely. And I ask you kindly, please do not forward this report to anyone outside of your immediate subscriber group. I appreciate your loyalty, and I hope you will respect my efforts to treat everyone else fairly as well. Thank you!

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.