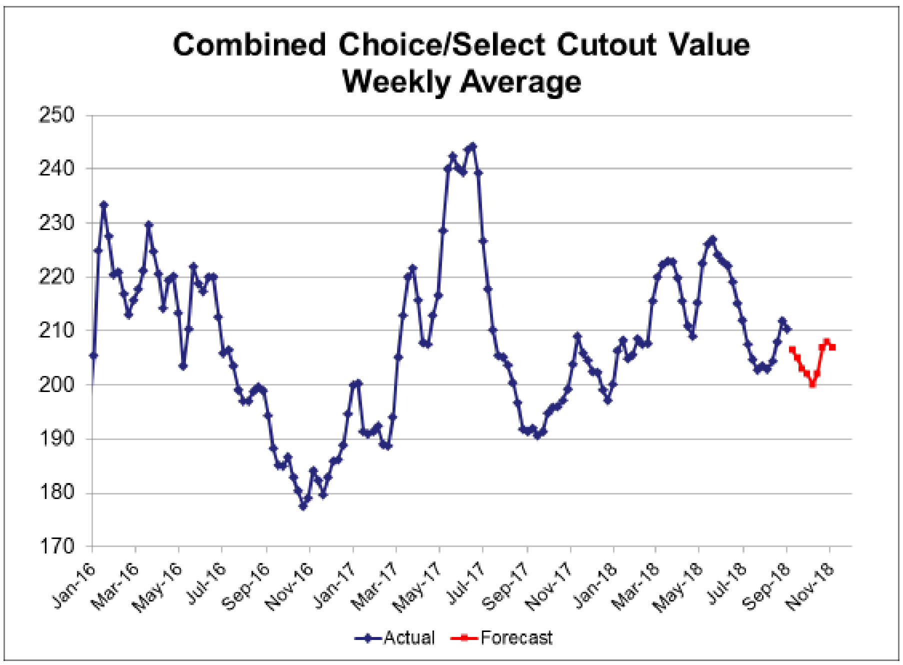
# MEAT MARKETS
# UNDER A MICROSCOPE

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

September 5, 2018

**The combined Choice/Select cutout value is turning downward pretty much on its typical seasonal schedule.** If nothing odd pops up from either the supply or demand side of the equation, then I think we're headed for a pattern that looks something like this:

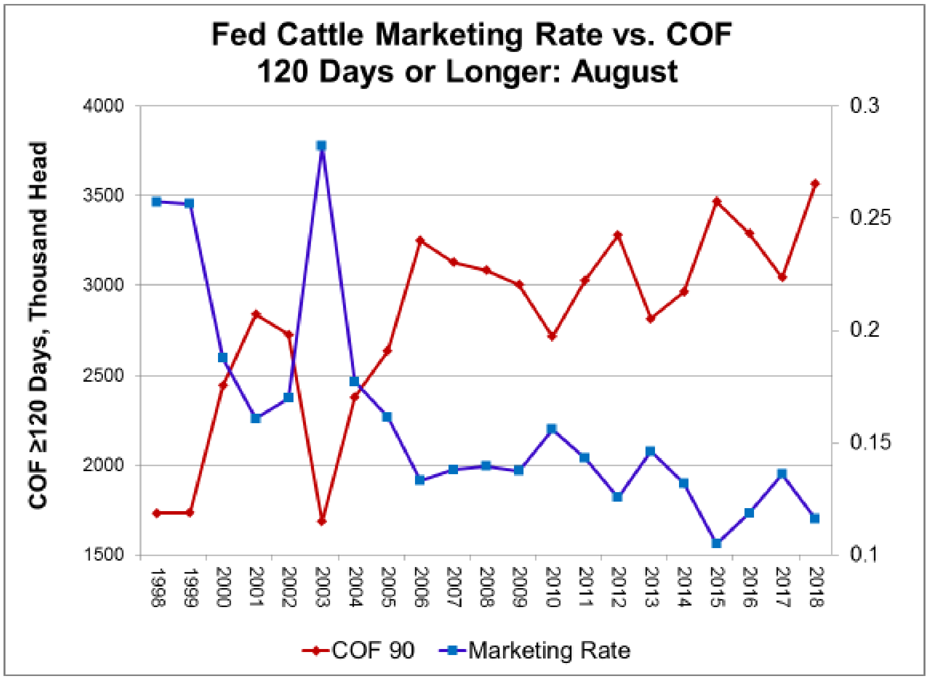



I'm talking about a five-week decline into a bottom in the first week of October, followed by a brief but substantial rally from that point into the second half of the month. The low weekly average should be in the neighborhood of $200 per cwt, with the ensuing peak several dollars below the most recent one on August 24.

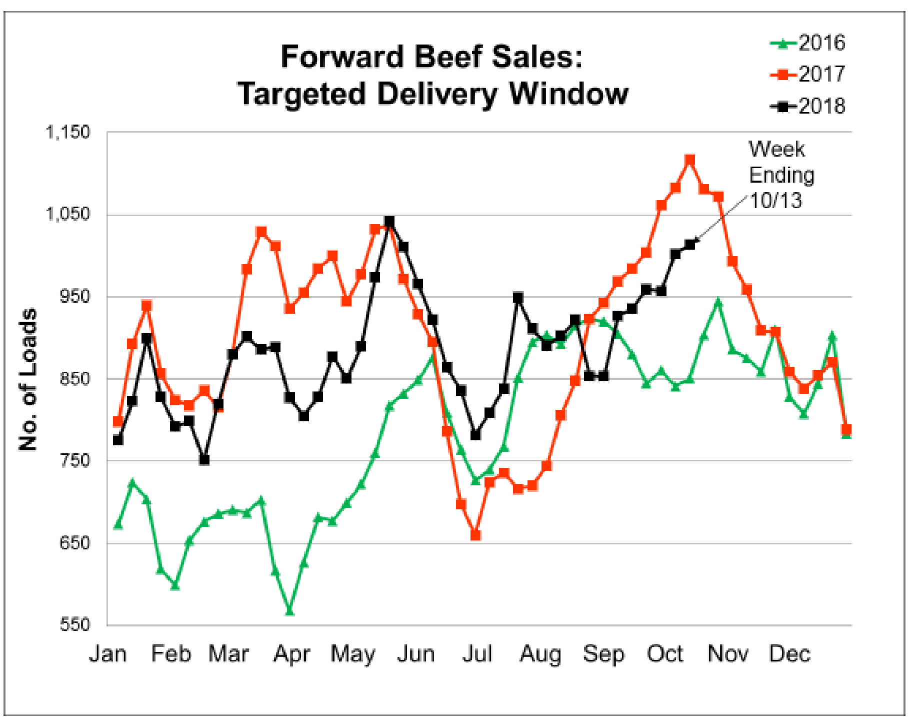
"Something odd" in this case would be a departure from the normal seasonal path of beef demand within the next two months, or else a major change in cattle feeders' willingness to move cattle. I'll begin with the latter.

Up to this point, feedlots have sold cattle rather liberally. As I view them, the statistics indicate that marketing rates have been fully adequate to keep pace with the available cattle supply. One conventional measurement are carcass weights, whose indications are fairly reliable….and presently neutral. As of the latest official reading—for the week ended August 18—steer carcasses were tracking two pounds heavier than a year ago, but lighter than each of the two previous years. Their increase since the first of July has matched the pace of 2014, 2016, and 2017….but has been considerably slower than the same period in 2015, the last time that cattle became veritably backlogged heading into the fall.

Likewise, the ratio of marketings relative to the inventory of cattle on feed 120 days or longer was significantly higher in July and August than it was in 2015:




No doubt, the extraordinary packer margin and suppressed futures prices encouraged the healthy marketing rate in August. But if this same general marketing posture persists for the next two months, then fed cattle slaughter will be in the 505,000-510,000 range during the three non-holiday weeks of September (compared with 504,000 in the past two weeks), and will drop to around 495,000 in October—which, by the way, would be a bit more than 1% *below* a year earlier.




I do not perceive anything in the works that would cause wholesale beef demand to veer from its typical seasonal course in either direction. Forward bookings for delivery throughout September and in the first half of October have been solid, suggesting that: a) supermarket beef featuring will be fairly active; and b) packers will be in a pretty good "forward-sold" position during this time frame.

On that subject, I suspect that round cuts will be one of the main targets of upcoming retail features. As a group, they are cheap compared with the rest of the beef market, as they have been for some time now. The simple average price of the four prominent members of the family stands at $2.12 per pound (vs. $2.24 at this time last year) heading into what is normally one of the strongest demand seasons for end meats. I notice that bottom round flats and eye of round (I'm still not comfortable calling them "round eyes", even though that may be the proper description) have a particularly consistent seasonal tendency to appreciate between now and the first week of October. Anyway, together the trimmed round cuts comprise some 13% of the total carcass weight, and so strength in this sector could go a long way toward offsetting the widely expected slump in strips, short loins, and top butts.

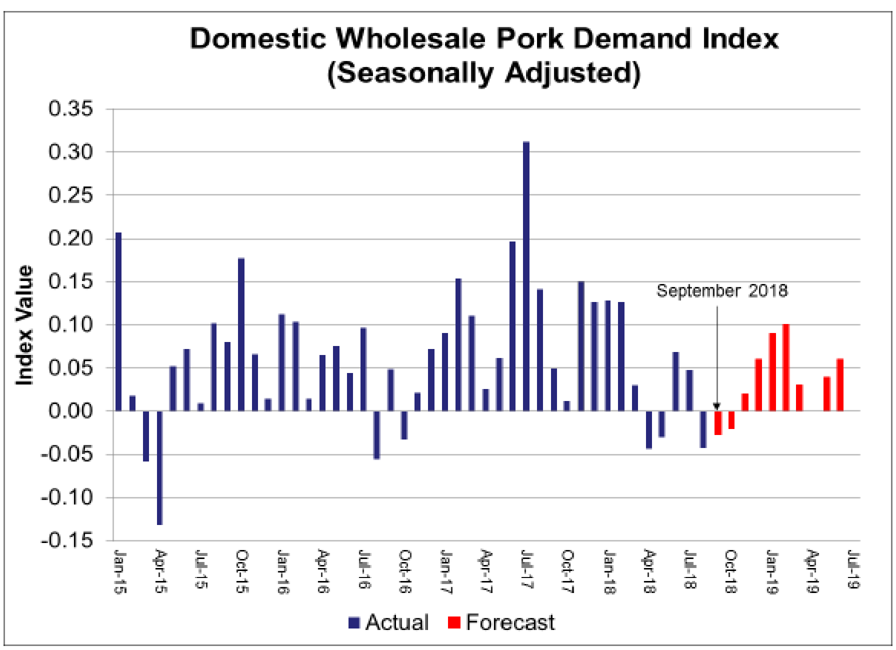
As for the latter group, my guess is that major support will be uncovered at somewhat higher price levels than it was a year ago….namely:

| | |
|---|---|
| CH 0x1 Strips | $5.00 |
| CH 0x1 Short Loins | $4.50 |
| CH Top Butts | $2.70 |
| SL 0x1 Strips | $4.00 |
| SL 0x1 Short Loins | $4.00 |
| SL Top Butts | $2.50 |
| 50% Lean Trim | $.60 |

I added 50% lean trimmings to the list because this is the only other item that looks like it could lose a substantial amount of ground over the next four weeks….it has done so in each of the last ten years.

And so, if all of these descend to the presumed support levels shown in the table and nothing else changes (which seems unlikely), then they will remove roughly $4 per cwt from the combined cutout value. From this angle, the prospect of a $200 cutout value a month from now seems kind of pessimistic, doesn't it?

**Meanwhile, the pork cutout value has bounced almost $5 per cwt from its August 24 low, and my guess is that it will now shift into a sideways pattern for several weeks. There should be another leg downward beginning in the second half of October, but there is a realistic possibility that the August 24 quote ($64.18) marked the practical bottom for the rest of the year**. It seems foolish to make such a declaration with hog slaughter headed for 2,600,000+ per week this fall (compared with the August average of 2,421,000), but there is a good chance that wholesale pork demand will make a rather strong recovery by November.




Why? Because of persistently low prices and expectations for more of the same in the fourth quarter….and in some cases, the ability of end-users to actually lock in low product costs through the end of the year. This will allow retail prices to come down further, which will accelerate the rate of product movement through the "pipeline"—not only in the supermarket sector, but in the restaurant sector as well. It is this response to a material change in prices that produces the short-term cyclical swings in wholesale demand. And as illustrated in the picture above, demand probably reached a cyclical bottom in August.

Actually, the sort of recovery in the wholesale demand index that I suggest in the graph, while substantial, is not *all* that dramatic in the broad scheme. Yet, it would make for a November average cutout value of $67-$68 per cwt, even with weekly kills reaching 2,650,000 at that time.

When I take a $67.50 cutout value and apply a projection of how each individual product might trade in relation to the cutout value, I come up with the following guesses for average prices in November. The projections of each product's share of the total cutout take into account how those relationships have performed in the last couple of months, and how they change seasonally between now and November:

November Average Pork Prices with a $67.50 per cwt Cutout Value:

| | |
|---|---|
| Bone-in Loins | $.84 |
| Boneless Loins, Strap-on | $1.10 |
| Butts | $.85 |
| Spareribs | $1.14 |
| Bellies | $.99 |
| 23-27 lb Hams | $.60 |
| Boneless Picnics | $.63 |
| 72% Lean Trim | $.49 |



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