



# ANALYSIS AND COMMENTS

Livestock Marketing Information Center

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## **CATTLE SITUATION AND PRICE OUTLOOK: Tight Beef Supply and Uncertain Demand**

Cattle and beef markets face a number of crosscurrents in 2008; demand aspects will likely dominate prices producers receive for cattle over the next two years. Consumer demand for red meats languished at times in 2007 due to sluggish economic conditions. That situation could become an important headwind for cattle prices in 2008, especially if the U.S. economy falters.

Overseas demand for U.S. beef improved some in 2007 even though several Asian countries continued to throw-up barriers and mishaps occurred with U.S. shipments, especially to South Korea. Further growth in exports and rather modest levels of beef imports are forecast for 2008. Cowherd numbers in Canada, Australia, and some South American countries are on the decline which could assist U.S. beef exports.

Drought has become a major issue for many U.S. cattle producers and the impacts on the cattle market could continue to linger. As of January 1, 2008, expectations are for a small decline in the U.S. beef cowherd. Overall, the major uncertainty for 2008 is the macroeconomic environment. To say that there are mixed signals regarding the likelihood of a recession. Even without recession, will consumer demand for beef falter? In 2008, beef market participants should carefully watch several factors, including: 1) the extent of U.S. beef sales to foreign markets, especially in Asia; 2) increases in competing meat supplies (pork and poultry); and 3) feed grain and forage production conditions and prices.

For the calendar year of 2007, slaughter steer prices averaged about \$6.50 per cwt. above 2006's, and were record high. For the year, in the Southern Plains yearling and calf prices averaged about \$0.75 and \$2.25 per cwt. below 2006's, respectively. But were a little above 2006's in the fourth quarter even with surging feed grain prices. U.S. beef production in 2007 was about one percent above a year earlier and 2008 is forecast to be about unchanged. Ratcheting-up of corn prices due to ethanol production will continue to cap calf and yearling prices relative to slaughter animal prices in coming years.

### Beef Cow Numbers Decline

In 2007, drought in the southeast states and record high national average hay prices resulted in larger cow slaughter numbers, which resulted in a contraction of the cowherd. Thus, the U.S. cattle inventory declined in 2007.

According to USDA, as of July 1<sup>st</sup>, all cattle and calves in the U.S. totaled 104.8 million head, 400 thousand head or about a half percent below 2006's and modestly lower than 2004's. At mid-year, the number of beef cows was reported at 33.4 million head, 100 thousand head less than in 2006. Of importance was the number of heifers 500 pounds and over held for beef replacements which totaled 4.7 million head, down 6 percent (300,000 head) from the prior year.

U.S. cow slaughter in the second half of 2007 remained above a year earlier with heifer slaughter also up in 2007. So, as of January 1, 2008, USDA is expected to report another year-to-year decline in the U.S. beef cow inventory. That will translate into another small calf crop in 2008. USDA estimated the 2007 U.S. calf crop at slightly less than the prior year and 2005's. So, feeder cattle supplies will remain tight. In fact, to stabilize the size of the U.S. beef cowherd more heifers will need to be retained by cow-calf operations for breeding purposes.

Besides cowherd declines in the U.S., the same situation is occurring in other important countries. Importantly, the Canadian beef cowherd declined in 2007 and did so at a faster pace than in the U.S. In key South American countries, cowherd numbers are under pressure as pastureland continues to be converted into cropland due to high crop prices. Finally, Australia has suffered from ongoing severe drought as well.

### Pork and Poultry Production Increasing

One of the biggest factors influencing beef and therefore cattle prices in the next two years may be competing meat prices. Production of pork and poultry ramped-up dramatically in the fourth quarter of 2007 and those trends will continue for at least well into 2008. U.S. pork production in the fourth quarter of 2007 was nearly 10 percent above a year earlier. In addition, preliminary calculations put fourth quarter 2007 U.S. poultry (chicken and turkey) production more than a 5 percent above 2006's.

In 2008, the largest annual increases in pork and poultry production are forecast to occur in the first half of the year. Even with a growing population and increased exports, on a per capita basis, U.S. total red meat and poultry consumption (retail weight basis) will increase in 2008 compared to 2007. Estimated U.S. per person retail red meat and poultry consumption (retail weight) in 2007 was about 0.5 pounds less than in 2006. In 2008, the preliminary forecast is for a significant increase in per person red meat and poultry supplies and consumption in the U.S. (up over 1 pound). In fact, due to surging pork and poultry production in the U.S., retail weight per person consumption of red meat and poultry is forecast to be record large. Of course, if U.S. exports of pork and poultry grow even more than expected, the increase in per person meat and poultry supply will be moderated. In 2009, preliminary forecasts suggest per capita red meat and poultry consumption will be rather stable.

### A Look Back at Prices 2007

Overall, cattle prices held up quite well in 2007, especially feeder cattle prices given very high feedstuff prices. But cattle feeders suffered red ink for the most of the year.

For calendar year 2007, slaughter steer prices were record high, averaging about \$92.50 per cwt. The monthly price peak was in April (about \$97.50 per cwt.) and on a weekly basis, prices peaked in early April at just over \$100 per cwt. From mid-April into June, fed cattle prices eroded falling to the mid \$80's in late June. Fed cattle prices were above a year earlier for the balance of the year mostly due to very small packer gross margins. In fact, beef packers lost a lot of money in 2007, especially during the last six months.

During the first quarter of 2007, calf and yearling prices at major markets were slightly below a year ago due to high feedstuff prices. Southern Plains feeder steers (700-to 800-pounds) averaged about \$100 per cwt. in the first quarter, while steer calves (500-to 600-pounds) averaged slightly under \$119 per cwt. With very good spring grass conditions, in the second quarter, calf and yearling prices in the Southern Plains strengthened compared to the first quarter and were well above a year ago. During the first six months of 2006, feeder steers (700-to 800- pounds) averaged just over \$105 per cwt., while steer calf prices in Western Kansas averaged nearly \$123.00 per cwt.

By summer, in terms of pasture and range conditions, U.S. drought conditions were better than 2002's very severe conditions but were deteriorating quickly in the southeastern states. Cowherd liquidation in many states in the southeast was occurring in the second half of 2007 and nationally

feed grain prices were high and hay prices were record high. The weight of high cost of gains and red ink by cattle feeders began to dampen feeder cattle and calf prices in the fourth quarter of 2007.

In the fourth quarter of 2007, calf and yearling prices were below summer levels but remained mostly above 2006's. In the Southern Plains, 700-to 800-pound steers averaged about \$110.00 per cwt., with the lowest prices posted in December. Steer calves (500-to 600-pounds) in the last quarter of the year were about \$118.00 per cwt. in the Southern Plains, about \$2.75 per cwt. above a year earlier.

### Outlook for 2008

In late 2007, USDA reported that the U.S. monthly on-feed inventory was slightly above a year ago. The year-to-year increase was mostly due to placements of lightweight calves into feedlots and imported Canadian feeder cattle. Still, U.S. Commercial cattle slaughter is expected to be below a year ago in much of 2008 and may be down about one percent for the calendar year. Tight supplies of beef and cattle will be supportive of cattle prices. In the supply-demand arena, both domestic and foreign demand will be the issue. The U.S. economy is expected to slow-down and consumers will be faced with increased supplies of pork and poultry. Foreign sales of beef are forecast to grow in 2008, but trade barriers and economic conditions overseas are unknowns.

The major uncertainty for calf and yearling prices, just as in 2007, will be feedstuff costs, especially corn prices. U.S. ethanol production will demand even more corn in 2008 and 2009.

U.S. slaughter cattle prices are projected to be stronger than a year earlier for 2008. The only yearly decline on a quarterly basis is forecast for the summer quarter, by that time beef packer margins should move toward more historical levels rather than the depressed situation of 2007. For the year, slaughter steer prices in the Southern Plains are projected to average \$93.00 to \$96.00 per cwt., setting another record high.

U.S. feeder cattle imports from Canada surged in the second half of 2007 due to several factors but most directly a higher cost of gain in Canada compared to U.S. feedlots. Declining Canadian cattle numbers may moderate those flows some as 2008 progresses. A small year-to-year decline in U.S. imports of Mexican feeder cattle may also happen in 2008.

If another large U.S. corn crop materializes in 2008, prices for yearlings will generally remain above the \$100.00 per cwt. level in the Southern Plains. Overall, yearling prices may be similar to 2007's. High corn prices will persist and calf prices will be impacted relatively more than yearling prices. Preliminary forecasts, assuming normal moisture conditions and significant drought relief nationwide compared to 2006 and 2007, put 500-to 600-pound steer calf prices in the Southern Plains \$1.00 to \$8.00 per cwt. below 2006's. Any yearly decline will in large part be attributable to high corn prices.

Feedlots and beef packers will likely continue to struggle at least into the second quarter of 2008. Many operators in those segments of the beef industry will need to make some difficult decisions in 2008.

### Looking Ahead 2009

Many of the factors that have impacted the beef and cattle markets in 2007 will continue to influence the market throughout 2009. Most of the price surprises, both positive and negative will arise from the demand side of the market. For the beef and cattle markets, those demand factors that will influence prices are underpinned by overall U.S. domestic economic conditions, foreign demand for beef and byproducts, and competition from competing meats and poultry.

On the supply side, the lingering impacts of the 2006 and 2007 U.S. droughts coupled with higher feedstuff prices have reduced the rate of cowherd growth, which will be supportive of cattle prices throughout 2009. Cow-calf operations should keep an eye on feedstuff prices as demand for corn will remain quite strong and hay supplies will once again be tight nationwide. U.S. commercial beef production is forecast to show modest annual decreases in 2009, as a result of

reduced slaughter numbers, especially of cows and heifers. Preliminary forecasts are for a year-to-year decline in U.S. beef production in 2009 of one to two percent.

Export markets will remain a vital factor influencing beef and cattle prices. In fact, export markets beyond beef will be critical, especially for pork and chicken. U.S. beef export tonnage is not expected to return to pre-2003 levels until after 2009, however in the next few years further growth in export tonnage is expected as trade restrictions are relaxed. Thus, overseas markets will likely be supportive of U.S. cattle prices.

Worldwide beef production potential may not grow as fast as in recent years due to lack of cowherd growth in key countries. So, U.S. beef imports from foreign countries will be rather constrained in 2009. Further, the U.S. is expected to continue regaining beef markets in Asia and elsewhere.

The major factor that could dramatically dampen calf and yearling prices in 2009 would be further surges in corn prices. Grain prices will remain volatile, causing potentially large price swings in calf and yearling prices. Continued growth in ethanol production will require corn prices high enough to attract large plantings in 2008 and 2009. Any shortfall in U.S. corn production will have a strong and immediate negative impact on calf prices.

The stage is set for record high annual slaughter steer and cull cow prices in 2009. Unless the U.S. and/or world wide economy falters dramatically, Choice steer prices in one or more quarters of 2009 could for the first time eclipse \$100.00 per cwt. For the Southern Plains, forecasts put calf (500-to 600-pound steer) prices for 2009 similar to slightly less than 2008's due to spillover from the feed grain market. With high feedstuff costs persisting, yearling cattle will remain in good demand by feedlots.

## ANNUAL AVERAGE CATTLE PRICES

