

CattleFax Outlook Presented

CattleFax predicts market shock is nearly over, turbulence still ahead.

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Recent price shock in the market and insights about the turbulence ahead were explained Jan. 28 to more than 2,000 beef producers at the CattleFax Outlook Session convened during the 2016 Cattle Industry Convention & NCBA Trade Show.

The downward spiral in price from record-high cattle prices has been a rough ride for many in the business, but CattleFax CEO Randy Blach said the market correction has mostly occurred. He explained how tight global protein supplies and a strong export market in 2014 and 2015 led to the “perfect storm” of market peaks and significant drops seen in recent extremes. Animal health challenges in both poultry and pork production led to tight supplies in 2014, which saw the tightest per capita protein supply in the last 20 years.

“We are coming off of historic peaks in the cattle market, created by unique conditions in the global beef and protein markets,” said Blach. “Dynamics, specifically global beef supply, led to a large correction in price. That big market downward swing is nearly over now. However, the cycle shows prices continuing to trend lower in 2016, 2017 and 2018.”

Analysts predicted the cattle feeder will lose about \$200 per head, stocker operators will have tight margins, and cow-calf producers will have profitable margins. The team of economists expect fed-cattle prices averaging \$130-\$145 during the next year.

“The cow-calf margins will still be profitable, but substantially lower than in the past two years,” said Kevin Good, senior analyst and fed-cattle market specialist, CattleFax. “We predict the cattle feeder will have tight margins for the year overall with potential for profit mid-year.”

A two-year *El Niño* weather pattern has replenished moisture conditions across the country, specifically the West Coast, which



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► Commenting on continued cattle market volatility, CattleFax Market Analyst and CEO Randy Blach blamed part of the problem on inadequate price discovery.

saw some relief in 2015. The weather outlook appears favorable, especially moisture conditions for grasslands, according to the weather outlook from Art Douglas, professor emeritus at Creighton University.

“As we head into 2016, a split jet stream pattern will favor above-normal precipitation from California to the Southern Plains and the Southeast through March,” said Douglas. “In the Corn Belt, spring will be wetter than normal, which will be accompanied by slower spring warming.

Delays in fieldwork and planting dates are likely to result.”

Analysts predicted \$294 added value per head in exports for the year ahead, a \$66 drop per head from 2014

values. This decrease in export potential is caused by a combination of a strong

U.S. dollar, slowdown in global market and challenges with market access. Russia and China are still the biggest opportunities for U.S. beef, but trade restrictions will continue to limit potential in the year ahead.

Imports of beef are predicted to be down

8%, since domestic cow kill will increase. In recent years the United States was in a rebuilding stage and females were held back for the cow herd. Imports of slaughter cows from Australia were available because of drought, but improving moisture conditions in 2016 will keep females in Australia for herd rebuilding. Analysts predict the growth in the U.S. cow herd will slow in the coming year and predict a 600,000-head cow herd increase, which is down from a 1.1 million increase in 2015.

— by NCBA staff

Angus Media drills into analysts’ presentations in the following segments.

Supply, price shocks should be past

“The supply shock was last year (2015). It’s important to realize we’ve had the supply shock and, with that, we’ve had the price shock,” CattleFax’s Kevin Good shared during the CattleFax Outlook Session. “The market has absorbed the bulk of that shock.”

Good noted that favorable weather and cattle prices led to rapid expansion the last couple years. As an indicator of this, in 2015 heifer slaughter was down 12%, adding 1 million head to the cattle inventory.



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“We’ll continue to expand in 2016, but at a slower pace,” Good said. The 2016 total cattle inventory was up 3.2% — equal to 2.8 million head — larger than last year. This is the biggest increase since 1981. The 2016 beef cow inventory was 1 million head larger than last year, totaling 30.3 million head.

With these numbers, Good said, “Expect more placements [on feed]. 2016 will have tight supplies early, but there is the potential to have increasing supplies the second half of the year.”

Overall, the production forecast for 2016 has all meats up — beef up 3%, pork up 2.7% and poultry up 1.3%.

Regarding demand, Good said 2015 retail demand was strong — up 8% on average, but the overall picture for the year shows a slightly different story. Demand was robust the first half of the year and declined in the second half. Retail prices peaked in July and declined through the last six months of the year.

With pork and poultry prices 40%-50% cheaper than beef in 2015, beef demand is estimated to pull back 3%-5%. As supplies increase, retail prices are likely to dip. Average retail price for beef is projected in the \$5.80s. In 2015, retail beef price averaged around \$6.04.

Building demand will continue to be important. CattleFax data suggests each 1% increase in retail beef demand is worth \$80 per head to the cattle market.

Good reported that beef in foodservice has trended positively the last few years, with sales in fine dining doing extremely well.

Said Good, “We do think the domestic economy will continue to grow, but at a



► Art Douglas discussed CattleFax weather predictions for 2016.

slower pace. However, foodservice should continue to do well.”

Good noted that beef exports have been the biggest challenge the past year. He said he anticipates beef export volumes to improve, but it won’t be as good as previous years. The decline in U.S. beef, hide and offal export values alone was worth a loss of \$118 per head to the cattle market from fall 2014 to fall 2015.

Given the robust supply and lagging demand both domestic and global, CattleFax projects prices on all classes of cattle will

work lower during the next three to four years. For 2016, Good said price averages will likely be as follows: calves \$195 per hundredweight (cwt.); feeders \$165 per cwt.; and feds \$130-135 per cwt.

Regarding bred cows, Good said, “We should all recognize 2015 bred cow prices were extreme. Expect that to pull back and anticipate \$1,600 to \$1,900 per head as calf prices soften.”

—by Kindra Gordon, field editor

Grain, energy prices trend lower

Lower prices for grain and energy can be expected throughout 2016. That was the message CattleFax analyst Chad Spearman shared during his remarks.

Ample supplies of grain — corn, wheat and soybeans — and an oversupply of oil will limit upside price potential in the coming year. Spearman also said the strengthening U.S. dollar and slower growth for China will limit grain export demand.

Spearman said corn supply is expected to remain steady with the upcoming growing season. It is projected farmers will add 1.5 million corn acres, resulting in a steady to larger supply moving into 2017.

Regarding prices, CattleFax anticipates the spot corn futures price average for the year will be \$3.75 per bushel (bu.) compared to \$3.77 per bu. in 2015. However, a wider range from the average is expected. For the first quarter of 2016, CattleFax says corn prices will find support from \$3.35 to \$3.45 per bu., with resistance from \$4 to \$4.10 per bu. May to December price lows are being projected at \$3 to \$3.30 per bu.

Soybean acreage for 2016 is expected to gain 1.3 million acres, while wheat acreage is expected to be down 2.7 million acres, mostly due to reduced winter wheat plantings. Spearman said the combination of cheaper energy and protein feeds combined with the recovery in hay stocks should keep hay prices under pressure for the year as well.

An oversupply of energy products is expected to continue in 2016. The United States has decreased rig count, but domestic production has remained strong. As a result, U.S. crude oil imports are the lowest they’ve been since 1995.

In 2015, domestic crude oil production averaged 9.3 million barrels per day. In 2016, that number is projected to be 9.1 million barrels per day.

As a result of the strong supply, West Texas Intermediate (WTI) crude oil averaged \$49.96 per barrel in 2015, a 48% price decline from the previous year. A range from \$25 to



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► Ample supplies of grain — corn, wheat and soybeans — and an oversupply of oil will limit upside price potential in the coming year for these commodities, said Chad Spearman, CattleFax analyst.

\$48 per barrel is expected for WTI crude oil in 2016.

Retail gasoline prices averaged \$2.54 per gallon in 2015 and are expected to range between \$1.90 and \$2.40 per gallon in 2016. Additionally, retail diesel prices in 2015 averaged \$2.72 per gallon and are estimated to be \$2.10 to \$2.65 per gallon in 2016.

Based on these projections, Spearman said a couple takeaway messages can be observed:

- With retail fuel prices coming down, the miles traveled per capita is picking back up. This should be supportive to U.S. ethanol production, according to Spearman. Some might also say that with increased travel, consumer spending could boost the economy along with restaurant beef sales.
- Cheaper protein and energy feed costs, along with lower fuel prices will help lower input costs for cattle producers. Spearman calls the ample grain supplies a “great thing for livestock feeders.”
- With the massive oil production outstripping demand, Spearman acknowledges, “Now oil prices are so low, we’re concerned about the economy.” The continuing concern to watch going forward will be global demand and the impact of economic growth and geopolitics.

— by Kindra Gordon, field editor

Where’s the beef?

Boasting the highest volatility since the bovine spongiform encephalopathy (BSE)

crisis a decade ago, today’s markets have producers on the edges of their seats. Despite this volatility, CattleFax market analyst and risk-management specialist Mike Murphy said we should expect to see exports increase and an overall trend of positivity in the 2016 cattle market.

During the fourth quarter of 2014 through 2015, prices of feeder cattle, fed cattle and calves dropped off sharply, falling from a record high of \$167 per hundredweight (cwt.) at the end of 2014 to \$128 per cwt. by the end of 2015.

While the cattle market remains positive, Murphy said it’s important to realize the beef industry isn’t immune to the volatility of the grain markets.

“Our markets, in some form in the commodity business, are all intertwined,” he said. “It’s pretty amazing when you step back and you evaluate those correlations.”

Commodity markets are cyclical in nature, he said. The cattle industry skipped the traditional 10-year cycle as supplies have, on average, been in decline since and prices have been, on average, going up since the mid 1990s.

“You can trace these relationships in the markets back to equities,” Murphy explained. “They typically are going in opposite directions of each other. Where commodities are declining, equities are improving and vice versa.”

After the significant push in commodity prices in 2008, those raised prices stimulated production. In the last year, we’ve seen

significant corrections to the crude oil and hog sectors, fueled by large increases in production. Demand for those commodities has fallen, pumping the brakes on global demand.

So, what does the United States export market for protein look like in the future?

It’s not too shabby. Murphy said the United States is in “really good shape compared to the rest of the world” and that he can see no concern of a recessionary year.

Countries around the world are lowering interest rates to spark economic growth. Murphy said this act did have a positive effect, but that effect has worn off. Now, interest rates are scraping the bottom of the barrel and nations are devaluing their currency in hopes of stimulating exports.

Russia has seen a 56% decline in the last 18 months due to the deflationary concept. Brazil’s export market is raising eyebrows in the United States as countries around the world have the opportunity to buy their beef cheaper.

“It’s a different type of product that we ship versus what they ship in terms of quality,” Murphy said, noting the difference in the United States’ high-quality, grain-fed product compared to Brazil’s lower-quality grass-fed beef. However, when economies are leveling off rather than growing, cheaper is better.

“The challenge the U.S. is faced with is that we’re a stable economy,” Murphy said. “There’s no fear of risk, of seeing a decline in

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► During the last four to five years, the United States has exported about 2.5 billion pounds (lb.) of beef on a fairly consistent annual basis — roughly 10% of our production, said CattleFax’s Mike Murphy. Maintaining that export level, “even throughout all the chaos,” is a big positive for our industry, he said.

PHOTO COURTESY OF NCSA

the state of our economy, at least not in the short term over the next one to two years. These other countries are taking over what they need, devaluing their economy and trying to stimulate growth. That hurts us because now we're less competitive."

For the supply side of the ledger, Murphy has one word: contraction.

"With beef in particular, we've got small increases in global beef production in 2016 — about a 1% increase," he said. "Go back and look at the last several years: It's a tight, tight supply."

That tight supply is due to the anticipation of expansion. Australia and Canada will likely contract their production in 2016 to prepare for herd expansion in the future, Murphy said.

Beef imports have seen a decline of about 8%, Murphy said. There's also been a decrease in the value of lean beef, which makes up the majority of imports into the United States.

During the last four to five years, Murphy said the United States has exported about 2.5 billion pounds (lb.) of beef on a fairly consistent annual basis — roughly 10% of our production. Maintaining that export level, "even throughout all the chaos," is a big positive for our industry, he said.

"When we start to look at beef production, numbers globally get a little bit bigger in 2016, most of that growth is going to come from the United States," he said. "That's going to put us in the position where we should still be able to command better demand from a

global standpoint and export a little bit more product."

Keep monitoring the markets, Murphy urged. After those record-high cattle prices of 2014, the correction has finally come, and come quickly. We may see slow growth in global demand, but prices will likely remain lower in 2016.

— *by Shelby Mettlen, assistant editor*

Blach summarizes CattleFax outlook

Who knew it would happen so fast? Even he was surprised by how rapidly the cattle market correction came, said Blach.

"We anticipated that increased protein supplies would move the market lower," said Blach. "Boy, it happened quick!"

In his presentation, Blach reviewed what he called the third-largest market rally in history. That was in 2014-2015, when prices climbed 37% in 15 months.

“In the last 12 months, we’ve seen the third-largest break in prices — a drop of 32%,” he said. “For some, \$500- to \$600-per-head profits shifted to \$500 to \$600 losses.”

Blach said the contributing factors included a staggering increase in U.S. protein supplies led by record-large pork and poultry production. Exports struggled through 2015, meaning more product needed to be consumed here at home, and domestic beef demand softened.

Commenting on continued cattle market volatility, Blach blamed part of the problem

on inadequate price discovery. He noted how the cash market for cattle continues to shrink, with only the Central and Northern Plains regions contributing to price discovery.

Looking ahead, Blach said expansion of the national cow herd is expected to continue in 2016, 2017 and probably through 2018, albeit at a more moderating pace. Increased feeder-cattle supplies should foster increased beef production in 2016. Annual per capita net beef supplies are expected to increase for the first time in a decade. Beef exports are expected to struggle during 2016, and perhaps through 2017.

“Exports must grow and markets expand or the domestic beef supply is likely to become burdensome,” warned Blach.

Factors point toward lower cattle prices. However, Blach said cattle producers also have some good things going for them. Weather has been more favorable in many cattle-producing regions. Grain and forage supplies are ample and fuel costs are relatively low.

Warning that easy profits won’t be found anytime soon, Blach said, “We’ve got to get back to doing business, in every segment of the industry.”

— by *Troy Smith, field editor*



Editor’s Note: For additional coverage of the 2016 Cattle Industry Convention & NCBA Trade Show, visit the Newsroom at www.4cattlemen.com.