CattleFax Offers Annual Outlook

Calling the beef industry market environment a rocky road for everyone in 2012, analysts predicted much of the same for 2013.

The weather outlook for the spring and summer should be brighter for some this year, yet bleaker than last year for the Central Plains, predicted Art Douglas, Creighton University professor emeritus. Fittingly, Douglas presented the weather outlook to kick off the CattleFax Annual Outlook Seminar Feb. 8 at the 2013 Cattle Industry Convention in Tampa, Fla.

The development of La Niña, though in transition, means that predictions are indecisive, but they likely favor continued drought in the center of the country, he said. The cold east Pacific and warm Atlantic favor widespread drought in the United States. These patterns are classic of La Niña.

Douglas predicted improved moisture in the Ohio Valley, Great Lakes and Northern Plains, which should help a portion of the Corn Belt. The pressure systems have been causing large storms on the East Coast, but moisture hasn't ventured farther inland.

This winter was forecasted as being mild, though observed temperatures have been colder than originally thought. The spring should be dry for the Southeast, West Texas and much of the West Coast. It also will be warm, except in the Northwest and some moisture in the North. Some good news for the Corn Belt, he said normal moisture patterns and warm weather should encourage early planting.

Summer looks mild without big pressure systems in the Pacific, Douglas predicted. "It won't be a repeat of the severe heat like last year." Dryness will persist, though an above-normal hurricane season could bring more moisture in the late summer and early fall.

Globally, he said, India is in good condition, as is much of South America. Improved moisture should occur in Brazil and Argentina. Australia is facing incredibly dry conditions.

Douglas explained that Arctic ice has been less lately, leading to much of the global-warming discussion. However, he added, there has been recent recovery. What doesn't reach the news is that Antarctic ice has increased significantly.

"There is no way you can have global warming … and have the Arctic get warm and the Antarctic get cold," Douglas said. "Either the whole globe warms up or it doesn't. What this really tells us is we're looking at regional climate anomalies."

— by Kasey Miller, associate editor

►Creighton University's Art Douglas provided the CattleFax weather outlook.

Ethanol, Oil and Gas Outlook

Fuel demand remains soft, and prices should struggle to trade much higher than year-ago levels, said Chad Spearman and Mike Murphy, CattleFax analysts.

Inverted futures markets have resulted in rationing of corn for ethanol, Spearman said. There is a smaller demand for U.S. exports because of supply in South America and Ukraine. Production levels have dropped and the price incentive has left. Ethanol production has been rationed, but the use of it has not. U.S. refinery net ethanol inputs continue to run near year-ago levels.

Blenders will have to use ethanol stocks more aggressively, and the United States will have to be a net importer of ethanol to meet the Renewable Fuels Standard (RFS) mandated usage, said Spearman. Imports have jumped to the highest level since 2008. The United States can't import enough to reach the mandate level to offset the lack of ethanol production.

The incentive for blenders to use ethanol will have to be displaced by the use of Renewable Identification Number (RIN) credits instead of physical ethanol, he explained.

U.S. gasoline prices are likely to trade in a seasonal manner, with a peak in the spring. Oil prices are up 116% since 2007, said Murphy. The global recession has reduced oil production, and 2012 has especially shown a sharp decline in usage.

Murphy mentioned that \$3-\$4 per gallon should be the expected trading range. There is a lot of consumer resistance at the \$4 range, so market signals in usage should push it to the lower end of the range. This should serve as support to economic growth, as consumers won't have to spend as much money on energy costs.

The market is telling producers to make more oil and less natural gas. Prices should improve in 2013.

— by Kasey Miller, associate editor

Feedgrain Outlook

Continued rationing of corn coupled with better weather conditions and a significant increase in corn production should pressure corn prices sharply lower by fall 2013, said Spearman, a grain market specialist.

For the September 2012-January 2013 period, projected corn stocks averaged a record low 5.8%. This is expected to range from 5.0%-7.0% through April 2013.

Corn feed/residual usage is expected to decline only 100-200 million bushels (bu.) compared to last year, despite higher corn prices, he said, and corn export demand is being rationed.

Corn for ethanol production is also being

►CattleFax analyst Chad Spearman offered the outlook for feedgrain production and pricing.

rationed, but the usage of ethanol by the blender is not.

For February to June 2013, Spearman predicted that resistance could be in the range of $7.65-$7.75 per bu., finding support from $6.85-$7.00.

The 2012-2013 carryover is expected to remain historically low, which supports historically high prices. This has the potential for extreme basis risk in the third quarter of 2013. U.S. crop acreage continues to grow, and 2013 corn acreage is expected to rise 1-1.5 million acres, from 97.2 million acres to 98 million acres in 2013. Additionally, 2013-2014 the projected stocks-to-use ratio is expected to rise to 10%-12%, so prices could potentially be lower.

Spearman predicted a transition period from June through September-October and, with it, prices in the $6.80-$5.80 per bu., and fourth-quarter risk down to the $4.50-$5.50 range.

Global soybean stocks-to-use levels should remain near the 10-year average, though U.S. stocks levels are still historically low. He explained that they expect U.S. soybean acreage to increase from 72 million acres to 79 million acres this year.

Hay stocks on Dec. 1, 2012, were at the lowest level since 1957, Spearman said, adding he expects hay prices to remain high this year.

Wheat, like soybeans, has stayed near the 10-year average, both domestically and worldwide. Spearman predicted that wheat acreage would increase from 55.7 million acres to 58 million acres.

— by Kasey Miller, associate editor

Demand Outlook

Domestic beef demand has a dismal outlook, said Murphy. He reported that no significant growth in the nation's gross domestic product (GDP) is expected for 2013. "It will stay positive but only grow at 1%-2%, and that is some concern for beef demand in 2013," Murphy told convention attendees.

He attributed this to the fact that a lot of the country is still unemployed and carrying a heavy debt load. The $4-per-gallon gas price is also a factor dragging on beef demand, he said. "More disposable income going to fuel means less money to spend on other items such as beef."

He noted that high gas prices offer another lesson for the beef industry, as well. Murphy pointed out that as gas prices have increased, consumers have decreased their travel and use of fuel. With retail beef prices steadily increasing, Murphy said, "This is something the beef industry must watch as well" — hinting that beef demand and consumption could taper off domestically.

Murphy said the bright spot in the 2013 picture is that the GDP in emerging and developing countries like Vietnam and China will grow, which could help boost meat exports to those countries.

Murphy said the recent announcement allowing expanded beef access to Japan is a "big deal." He noted this will be positive for beef exports in general, but explained that the real positive will come on the variety meats. "That's where we'll be able to add a lot of value to the bottom line," he said.

Regarding Russia's ban on U.S. beef, Murphy said, "We don't see a quick resolution to that situation."

Given the tight beef supplies in the United States, Murphy explained that beef imports will likely be up 12%-15% from a year ago, as well.

— by Kindra Gordon, field editor

Supply Outlook

Addressing the supply situation and looking at rebuilding of the U.S. cow herd, CattleFax's Kevin Good noted that fewer cows are being slaughtered and said, "Don't be surprised over the next couple years if [fewer] heifers are going into feedlots as more are being used for replacements."

He acknowledged much depends on Mother Nature.

"The economic incentive is there to expand," Good said, "and we do expect to see that as soon as Mother Nature cooperates."

For the first quarter of 2013 Good said the cattle are there to be placed into feedlots, which would create a larger beef supply for summer. Despite that, CattleFax estimates anticipate retail beef prices will be up 4% in 2013, which could hinder beef purchasing by consumers.

— by Kindra Gordon, field editor

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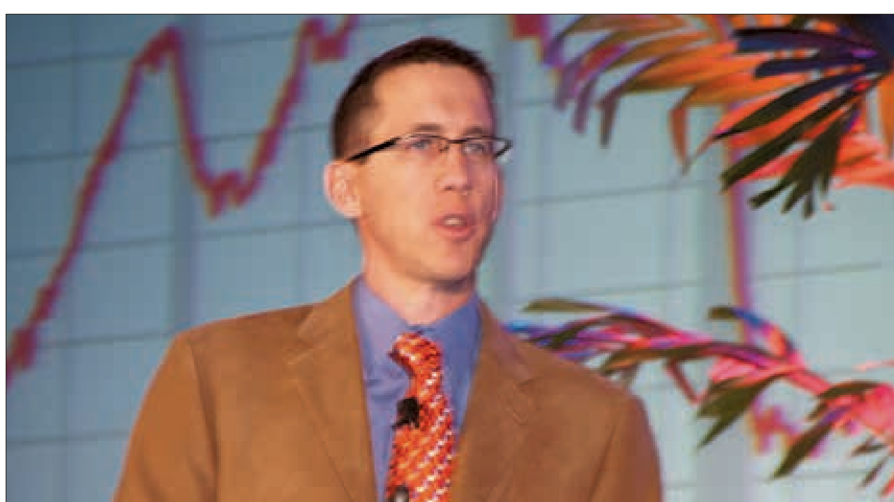

►CattleFax analyst Mike Murphy reported that no significant growth in the nation's gross domestic product (GDP) is expected for 2013.

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Cattle, Beef Price Outlook

Prices for U.S. cattle and beef are expected to reach record-high levels in 2013, CattleFax analysts agreed as they talked about forces expected to influence prices, naming drought as having a huge impact on beef supplies.

They talked about how the Southwest's lingering drought spread last year to parch an even larger portion of cow country. The result was lower forage production on grazing lands and lower yields of harvested forage, which further boosted already-high feed prices. Despite chances for regional relief in 2013, forecasters said drier-than-normal conditions may persist in some areas and particularly in the Central Plains area.

The current lack of moisture and only slim chances for significant improvement mean U.S. cow numbers are likely to decline further from the current tally of just more than 29 million head — the lowest since 1952. A smaller supply of cattle translates to a reduction in beef supply. While domestic beef demand has slipped a bit, export demand for U.S. beef has grown. Access to new foreign markets and expanded exports to others means global demands should more than make up for any diminished domestic demand.

"Global beef supplies (excluding India) are expected to drop by 2%," said Good. "That will drive our outlook."

Declining fed-cattle numbers, stronger exports and higher prices for competing proteins should support higher beef cutout prices in 2013, he said, adding that he expects prices to average $196 per hundredweight (cwt.), which is 4% higher than the year prior. Good said fed-cattle prices should average higher for the fourth consecutive year, ranging from $116 to a high near $134 per cwt., and averaging around $126. The price spread between Choice and Select beef is expected to widen.

Tighter supplies of feeder cattle and excess feeding capacity mean prices for feeder cattle may increase by nearly 6% this year. Good expects considerable price volatility, however, in response to shifts in prices for corn and futures contracts. He looks for a range of $140 to perhaps $165 per cwt., and an average price of $155 per cwt. for 750-pound feeder steers.

While the impact of drought will influence profitability for many cow-calf producers, Good's forecast for calf prices was positive. At the top end, prices could exceed $200 per cwt., with 2013 prices averaging $175.

— by Troy Smith, field editor

►Expect price volatility for feeder cattle, a wider Choice-Select spread and record prices, says analyst Kevin Good.

Profitability Expectations Mixed

While forecasts for cattle and beef prices were higher, expectations for profitability were mixed. CattleFax market analysts said profitability could vary among industry segments. The outlook is not rosy for beef retailers, packers or cattle feeders. Profitability for stocker and cow-calf producers could depend on drought's effect on each operation's input costs.

CattleFax CEO Randy Blach said food retailers are "featuring" beef less often, as margins have been squeezed. Both grocers and restaurants will struggle to increase profits in 2013. The reason is a decrease in domestic demand as a result of decreased real income among consumers. Prices for pork and poultry were up, but beef prices increased more. Price resistance suggests consumers are keeping tighter grips on their wallets.

That would pressure beef and cattle prices lower were it not for increased sales of U.S. beef abroad. Blach said the value of exports contributes $280 per head to the value of a finished steer. In the current environment, that doesn't necessarily translate to profitability in all of the beef business.

"The cattle feeder, the packer and the retailer didn't make any money. They've been pushing up against a price ceiling for several months," said Blach. "It's been a little tough for margin operators."

The beef industry faces a continuing struggle with excess capacity in the beef-packing and cattle-feeding sectors. Excess packer capacity reached 15% in 2012, resulting in the lowest margins in five years and forcing the closing of a Plainview, Texas, packing plant.

Blach said the beef industry faces a continuing struggle with excess capacity in the beef-packing and cattle-feeding sectors. Excess packer capacity reached 15% in 2012, resulting in the lowest margins in five years and forcing the closing of a Plainview, Texas, packing plant. He said there could be more plant closings, followed by contraction in the feeding segment.

"We estimate a 25% to 30% excess in cattle-feeding capacity. Cattle feeders are chasing a declining supply of feeder cattle. Losses in the feeding segment were nearly $100 per head in 2012, assuming no risk management," added Blach. "There's a high probability of feeding losses during the coming summer."

Prospects for high feeder-cattle prices are good, and that bodes well for stocker operations, said Blach. However, they are margin operators, too. Profitability could be hard to achieve if drought continues to affect availability and costs of grazed and harvested forages. Some cow-calf operators may be in the same boat. However, if their feed situation is good, cow-calf producers are in the driver's seat and should be profitable in 2013.

Blach said drought relief would aid chances for everyone. Persisting drought will likely lead to more beef herd contraction and continuing high prices for feedstuffs. However, numbers indicate that producers in some areas of the country are expanding. The Pacific Northwest and Northern Plains were cited as regions where increased heifer retention and cow herd expansion are evident. It shows what a difference adequate precipitation makes.

— by Troy Smith, field editor

Issues Shaping the Future

Domestic demand for beef could be described as steady to slightly soft. It's a reflection of tight beef supplies and resulting higher beef prices, but also a 1% decline in consumers' per capita disposable income. According to CattleFax market research, a 1% change in real income creates a 1% change in beef demand. Blach discussed beef supply and demand, the U.S. economy and other issues likely to shape the future market outlook.

According to Blach, higher beef prices in 2012 rationed a limited supply of product. The supply will tighten a bit more in 2013, begging the question: "How much are consumers willing to pay?" There probably is a limit, as suggested by consumer resistance to gasoline sales at $4 per gallon.

Blach said he believes beef will struggle to remain price-competitive with pork and chicken, even though prices for those alternative protein sources are predicted to increase, as well. Beef will still cost more, and the gap may widen.

While he does not expect the U.S. economy to backslide into recession, Blach doesn't see much up-side either. He said government policy will heavily influence income levels in 2013. Based on current figures, incomes and GDP (market value of all U.S. goods and services) have the potential to decline by as much as 3%.

Fiscal cliff concerns have subsided, but policymakers have yet to balance public concerns related to tax cuts and deficit spending by government. During 2013, Blach expects little improvement in the domestic economy, and the possibility of buyer resistance to higher beef prices. Internationally, however, emergence of new markets and expansion of existing markets should result in aggressive bidding for U.S. beef in 2013.

"As personal incomes in developing countries increase, so does the demand for a higher-quality diet. Global beef consumption is climbing," said Blach. "We will see (global) population growth of 700 million to 800 million people in the next decade. We'll see more demand for meat and more opportunity to export beef."

Blach said exports will play a big role in whether the U.S. beef industry is able to grow, citing the current $280 contribution to the value of a finished steer that is a result of the collective export market. That's $100 per head more than in 2003, before the U.S. lost valuable foreign-market access.

Blach said he thinks the big push in agricultural land markets may be about to run its course.

Record-high prices have driven the conversion of more acres into corn production. CattleFax analysts expect corn prices to remain historically high through the first half of 2013, but demand rationing for ethanol production and exports, plus an increase in corn production, could pressure prices sharply lower by fall.

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Noting how uncertainty creates market volatility, Blach said increases in both capital requirements and risk, without increasing returns, will hinder the cattle industry. Returns to the cattle-feeding segment, in particular, have been exceeded by operating investment and the consequences of price volatility over the last decade. Emphasizing how credit needs have "skyrocketed," Blach warned that access to capital will be tested. He expects continued volatility will lead more producers to develop risk-management plans.

Pointing to a thinning cash market for fed cattle, with more cattle moved through alternative marketing arrangements, Blach said selling cattle "with the hide off" is shaping into a long-term trend that challenges price discovery.

"Be careful," advised Blach. "Yes, we're seeing record prices, but it may be difficult to make money because we also have record breakevens. Manage your risk."

Urging the audience to contrast current CattleFax reports with those of 20 years ago, and note how reports now cover many more issues in greater detail, Blach said it's because cattle producers must consider the effects of many more issues.

"Your business demands it," he concluded.

— by Troy Smith, field editor

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