

The Value of Quality

Cattle-Fax sets “value of quality” at half a billion dollars a year.

by Steve Suther

You can do something because it “feels right” or because you figure it will pay off some day. Out of necessity, most people are grounded in what pays off today, but you can’t always sort out the economics.

You may wonder what’s it worth to aim for a high-quality beef target such as the *Certified Angus Beef*® (CAB®) brand, especially if, like 90% of producers, you are in the cow-calf business. We asked Cattle-Fax to help answer that question, and the result is a July 2007 white paper titled, “Value of Quality Analysis.”

To get at how much value is added by quality grade categories, Cattle-Fax considered, “What would prices do if all premium quality categories and brands went away?” It turns out that a quality focus has added about half a billion dollars a year to all cattle values each year since 2004 (see Fig. 1).

Although some have speculated that the added value would decline in the face of greater supply, the Cattle-Fax model actually shows the only threat to increasing beef value is a decline in the number of higher-quality cattle. Here’s the study in its entirety:

Methodology

Based on the Choice-Select cutout, the analysis used the U.S. Department of Agriculture (USDA) reported composite cutout for Choice and Select grades to create a composite price based on the grade percentages of each, then grossing the total to equal 100%.

This is the baseline cutout (with price and percentage examples):

Choice: \$150 cutout, 54.3% grading
Select: \$143 cutout, 37.3% grading
91.6%

91.6% graded:
 $54.3\% \div 91.6\% = 59.2\%$ adjusted Choice
91.6% graded:
 $37.3\% \div 91.6\% = 40.7\%$ adjusted Select
100%

Adj. Choice
 $59.2\% \times \$150$ (Ch cutout) = \$88.80
Adj. Select
 $40.7\% \times \$143$ (Se cutout) = \$58.20
Baseline cutout: \$147.00

The “premium” cutout calculation was created using the same type of grade percentage and cutout calculations, first dividing into these five categories:

- ▶ Prime
- ▶ CAB
- ▶ upper 2/3 Choice (non-CAB)
- ▶ lower 1/3 Choice
- ▶ Select

From the National Beef Quality Audit (NBQA), Cattle-Fax and Certified Angus Beef LLC (CAB) data, grade composition was determined (see Fig. 2).

Cutout prices on each category were estimated from the Urner-Barry CAB cutout value for CAB and upper 2/3 non-CAB and the Choice-Select baseline cutout for the lower 1/3 of Choice. These new cutout values and percentages were rolled up with Prime and Select cutout values to create a “premium” composite cutout. That cutout was compared to the baseline Choice-Select cutout to calculate quality premiums (see Fig. 3).

Fig. 2 shows the spread between the two cutouts.

At first glance, the spread between these prices appears very small. However, when considered on a per-head basis, these spreads are of particular significance (see Fig. 4).

A quality focus has added about half a billion dollars a year to all cattle values, each year since 2004.

Cattle-Fax also conducted sensitivity analysis of increasing Choice and decreasing Select in the model with several key findings.

Every percent increase in Choice grade makes the premium cutout worth:

- ▶ 20¢ per head more than the baseline
- ▶ 3¢ per hundredweight (cwt.) of carcass more than the baseline
- ▶ 2¢ per cwt. live more than the baseline

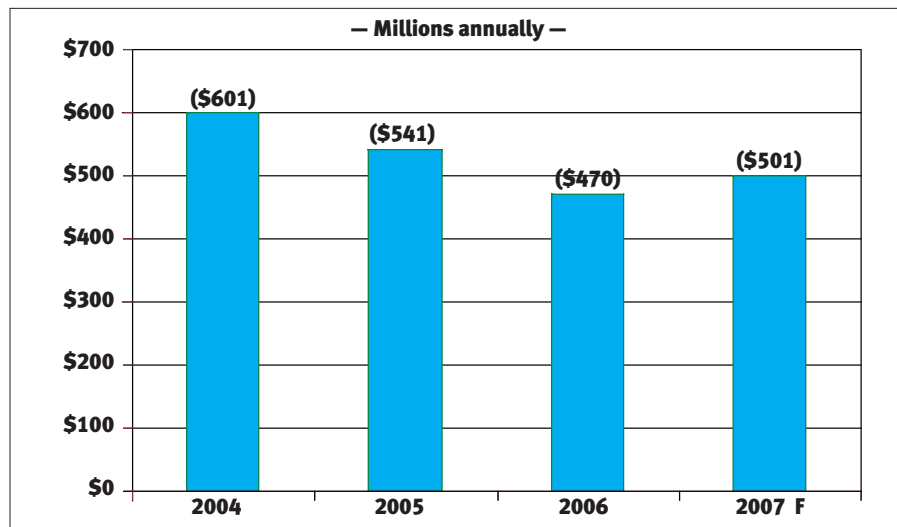
The inverse is also true, so that every percent decrease in Choice grade makes the premium worth 20¢ per head less, for example.

Conclusion

Cattle-Fax concluded that programs and classifications that add value above the Choice-Select blended cutout value have added \$17 to \$22 per head on an average basis since 2004, with an average of \$19.91 per head. This is the equivalent of \$2.59 per cwt. carcass, or \$1.58 per cwt. live.



Fig. 1: Total industry value of premium grade categories



Source: Cattle-Fax, USDA, CAB