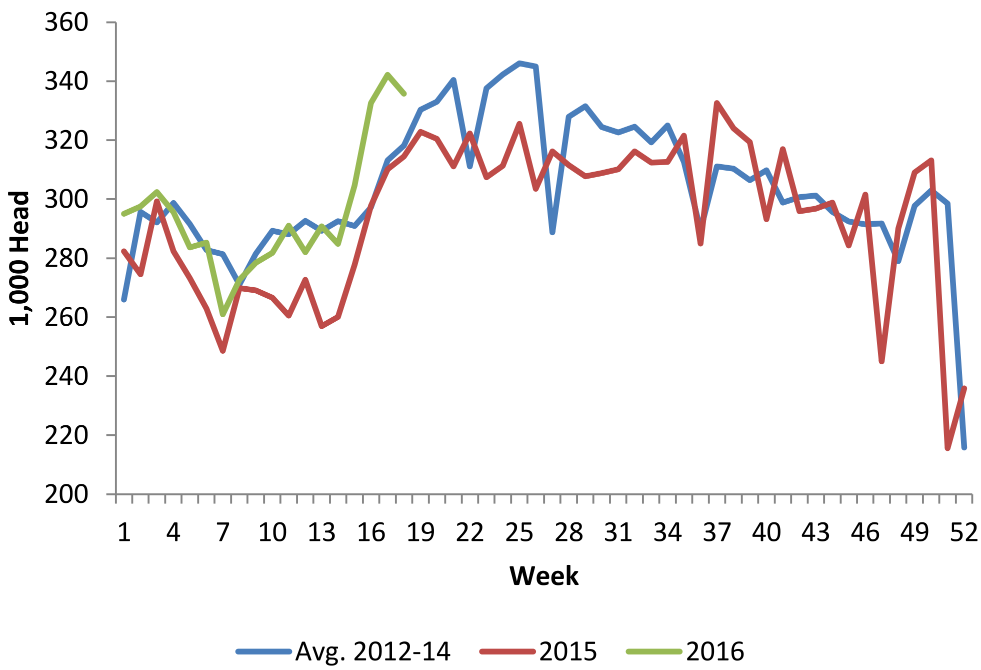
May 2016 – Livestock Market Update
Public Policy Department
Budget & Economic Analysis Team

Beef Demand Improving?

Beef production over the last few weeks has been remarkably large. Weekly federally inspected beef production has exceeded the prior year's level by at least three percent in every week since the beginning of April. Larger production has mostly been due to big year-over-year increases in weekly cattle slaughter—more specifically, in weekly steer slaughter. Figure 1 shows weekly steer slaughter for 2016 compared with the prior year and with the 2012-14 average.

Figure 1. Weekly Federally Inspected Steer Slaughter



Data Source: USDA Agricultural Marketing Service through Livestock Marketing Information Center

As this figure shows, steer slaughter has been well above not just the prior year, but also at or above the 2012-14 average for some time. The weekly slaughter data suggest that quite a few fed cattle have been pulled ahead in the supply pipeline. That is, it looks as though the normal summertime increase in fed cattle slaughter has occurred early this year. Weekly dressed weight data also lend support to this idea. For the first week of May (most recent data available), the average steer dressed weight worked out to 862 pounds. That is 8 pounds less than a year ago, marking the first year-over-year decline in weekly steer dressed weight since mid-June 2014. This suggests that feedlots are more current in their marketings than they have been in a good long time.

The behavior of wholesale beef prices during this period of increasing production has been interesting. The daily choice boxed beef cutout topped out at just under $2.35 per pound in mid-

March. After that, it began an almost-uninterrupted slide lower, finally bottoming out at $203.74 at the end of the first week of May. In the last two weeks, though, the choice cutout has climbed by more than $20 (even accounting for a bit of a drop to close the week last week). This strong rally in the wholesale beef market even as production has remained quite large is encouraging, suggesting that the market is in a good position to accept larger beef supplies. It has been a while since the market has seen abundant beef supplies. Retailers have not really had very attractive beef feature options in a long time. It's too early, I think, to conclude that beef demand is doing great—load counts have definitely slipped as wholesale prices have soared. But the wholesale market has rallied in the face of strong production, competing meat prices are moving up and front-end fed cattle supplies are as cleaned up as they have been in many months. All in all, those fundamentals don't sound too bad.

So far, the cattle market has not been all that impressed with improving fundamentals. While the rally in wholesale beef prices has been impressive, the performance of the fed cattle market has been far less so. From the last week of April through mid-May, fed cattle prices added about $9—rising from a low of $123.79 to $132.56. Last week, however, cash prices slipped back down by almost $2, with the weekly 5-area weighted average price working out to $130.75. This is some improvement, of course, but it seems that stronger fundamentals are having a hard time overcoming the seasonal bias toward weaker prices.

What has been true of cash cattle prices has been even more significant for cattle futures. Despite strong positive movement in wholesale beef prices, cattle futures have mostly remained on the defensive. Last week, the nearby Live Cattle contract finished the week at $121.05. Against last week's 5-area weighted average price, basis works out to +$9.70. Now, basis in May tends to be seasonally wide as late spring cash prices are being weighed against a summer futures contract, but the current basis is remarkably strong. This is further incentive for aggressive marketings.

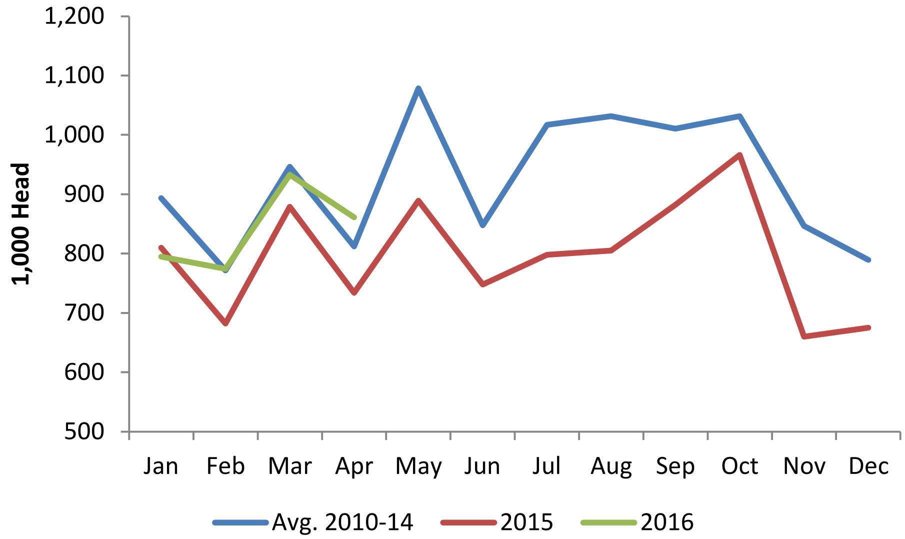
As of Monday, following a surprisingly bearish Cattle on Feed report (more on that below), Live Cattle contracts through April 2017 were down the $3 daily limit. This makes it likely that cash business will take place at lower prices this week. Basis really does look out of line though, even before Monday's big sell off, which suggests that today's futures market reaction may be a bit overblown.

Cattle on Feed Surprise

In contrast to the rosy situation described above, Friday's Cattle on Feed (COF) report included a bit of a nasty surprise. According to the latest COF, April placements were up by 107 percent compared to the prior year. This was a pretty big miss for the pre-reports, which had mostly expected placement to be down at least a couple of percentage points from last year.

Placements for April were expected to be down in large measure due to the fact that placements in February and March had been relatively large, suggesting that cattle had been pulled ahead to some extent. April is kind of an interesting month in terms of cattle placements. Typically, April placements are small in comparison to the months on either side of it. This has a lot to do with the placement of wheat pasture cattle in the Southern Plains. Generally, feeder cattle come off of wheat pasture by mid-March (if the wheat will be harvested for grain) or they come off in May (if the wheat is grazed out for the full season). This year, though, it looks like Southern Plains placements have been at least somewhat atypical, with April placements that seem a good deal bigger than the usual monthly pattern would have suggested. This is evident in Figure 2, which shows combined monthly placements for Kansas, Oklahoma and Texas.

Figure 2. Number of Cattle Placed on Feed: 1,000 head capacity lots in Kansas, Oklahoma, and Texas



Data Source: USDA National Agricultural Statistics Service through Livestock Marketing Information Center

In the three primary states of the Southern Plains, April placements were up by 17 percent from the prior year. Placements in these states were over six percent higher than the 2010-14 average—a period during which feeders cattle were generally considerably more abundant than they are now. By contrast, placements in the major Corn Belt states (Iowa, Nebraska and South Dakota) in April were about steady with a year ago (up 0.2 percent) and were 3.4 percent lower than the 2010-14 average.

The question now is what any of this implies for May placements, particularly in the Southern Plains. With generally good grazing conditions, it's not clear why cattle would have been pulled out of graze-out programs early, even though the pattern of placements suggest some of that was probably going on. Confounding that story a bit is the fact that in Texas (the one Southern Plains state for which placements by weight category are reported), placements in the lightest weight category were up by 14 percent—so it wasn't all heavy feeders pumping up the placement figures. At this point, I think my best bet would be that May placements will not hold up to the current pace. Of course, that's what most people were betting on for April, and that is reason last week's report was so bearish.

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The EU's Biotech Freakout, Glyphosate Mess

Back in March 2015, the World Health's Organization, International Agency for Research on Cancer (IARC) issued a statement that re-classified glyphosate as "probably carcinogenic to humans." IARC's system of making determinations ignores probability and dosage, which leads it to make determinations that are counter to almost every other scientific body. Despite the fact that glyphosate's lethal dosage measure is about that of common table salt, some consumer groups and even some countries reacted strongly.

Predictably one of those who reacted strongly was the European Union. Consumer groups in the EU were quick to launch into campaigns that linked "poisonous" glyphosate to "poisonous" biotechnology. On that linkage, in April 2015 the EU Commission adopted a proposal which would have allowed member states to restrict or prohibit the use of genetically modified food and feed in their territory. Concerns about threats to the single market and the potential for significant negative economic impacts won out, however, and in October, the European Parliaments overwhelmingly rejected a proposal.

Now, here we are in May 2016 and another attack on biotech is underway. This time, consumer groups are taking the fight directly to glyphosate. Every 15 years, products need to be renewed by the commission and glyphosate is up for renewal this year. The commission needs to decide by June 30 whether to renew marketing authorization for the pesticide. If they do not, after a six-month grace period, countries would be obliged to pull it from the market.

The vote would come after months of delay and pressure from environmental and consumer groups to limit the use of the herbicide because of concerns it could cause cancer. Since most biotech crops are genetically engineered to withstand treatment with the chemical, the reauthorization has escalated into a high-profile fight in the war over GMOs in Europe.

A vote in March on glyphosate's reauthorization was postponed on these concerns, but a vote had been expected to vote on the relicensing during a May 18-19 meeting. The EU Commission had made clear that it needed a solid qualified majority of its 28 member states to proceed to a vote on glyphosate, but that was not forthcoming after Germany and several other EU countries failed to indicate their voting intentions, so no vote occurred.

So what now? No one really knows. Without a clear qualified majority, officials have yet to determine how they plan to move forward.

More importantly, why do we care? The political wrangling over glyphosate in Brussels has ensnarled the approval of three soybean GMO varieties that have gained sign-off in other major export markets: Monsanto's Roundup Ready 2 Xtend soybeans, which are resistant to glyphosate and the herbicide dicamba; the company's Vistive Gold variety, which is high in oleic acid, producing oil that doesn't need to be partially hydrogenated and thus avoids a major source of trans fat in food; and Bayer Crop Science's Balance GT soybeans, which are tolerant of glyphosate and the herbicide isoxaflutole.

The wait continues.

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