

MONTHLY MARKET PROFILE: FEBRUARY, 2010
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“Where’s the market headed?” That question has been increasingly frequent in the past few months. More-often-than-not, it’s probably asked with an underlying intent: “Please tell me some good news.” My response always includes, “Well, that depends on the consumer.” Over the short-run resilience / survival is the predominant theme for the market. But more important are the long-term business implications of beef demand trends.

That theme served as the focus of last month’s Monthly Market Profile which reviewed the long-term trends relative to consumer expenditures for beef, pork, and poultry. My summary of those circumstances last month was as follows: “Per capita spending [for beef] is forecast to decline in the coming years – those projections by USDA released a year ago and developed before full manifestation of the financial crisis (this year’s numbers may look worse yet)...the battle for tastes/preferences and comparative price/value relationship has never been more important...” Potential opportunities for growth and increased market share, over the long-run, hinge upon the economy. Some perspective of the macro-picture of the economy, recovery and consumer behavior helps to serve as a foundation for decision-making going forward.

The recession and financial crisis has left no industry untouched - the entire global economy is going through fundamental restructuring. Within that scenario is the mandate for many Americans to repair their personal balance sheets. That condition coupled with associated anxiety, worry and trepidation about excessive debt will likely establish some lasting consequences. The legacy effect will prove significant - consumer spending will likely be permanently altered. Add unemployment and plunging home values to the mix and you’ll find persons who vow to never again base personal spending on their respective ability to borrow. In the future, the “new normal” for spending behavior will increasingly be dictated by real savings.

Perceptions of uncertainty are underscored by CNBC’s December consumer survey. The aggregate view of the economy remains unchanged from the previous year: 91% of those surveyed are pessimistic about current economic conditions and only 2% were changed in their attitude about the future (52% were pessimistic versus 54% in 2008). Stagnant home values, unemployment concerns and the need to shore up personal savings will limit growth going forward. William Dunkelberg, Chief Economist, National Federation of Independent Business explains the current state of the consumer and recovery like this (*Bloomberg on the Economy*, Dec 10, 2009):

...all the stimulus stuff that was done from January on, very little really was stimulating the consumer. And the consumer is what we’re missing. 50% of consumption [consumption being 70% of GDP]... comes from the top 20% of the income distribution. They’re the ones who stopped buying cars – they still have their jobs, they still have their incomes but they aren’t spending. They, of course, shot their wad with using a lot of debt from their home value and so on. So they’re not spending - They need to get back into the game. Nothing has been done but threaten them with higher taxes.

It’s also important to note that housing is now confounded with unemployment; people are reluctant to pick up and move to take a new job if their mortgage is underwater. The implication being, at least over the short-term, the consumer remains under pressure.

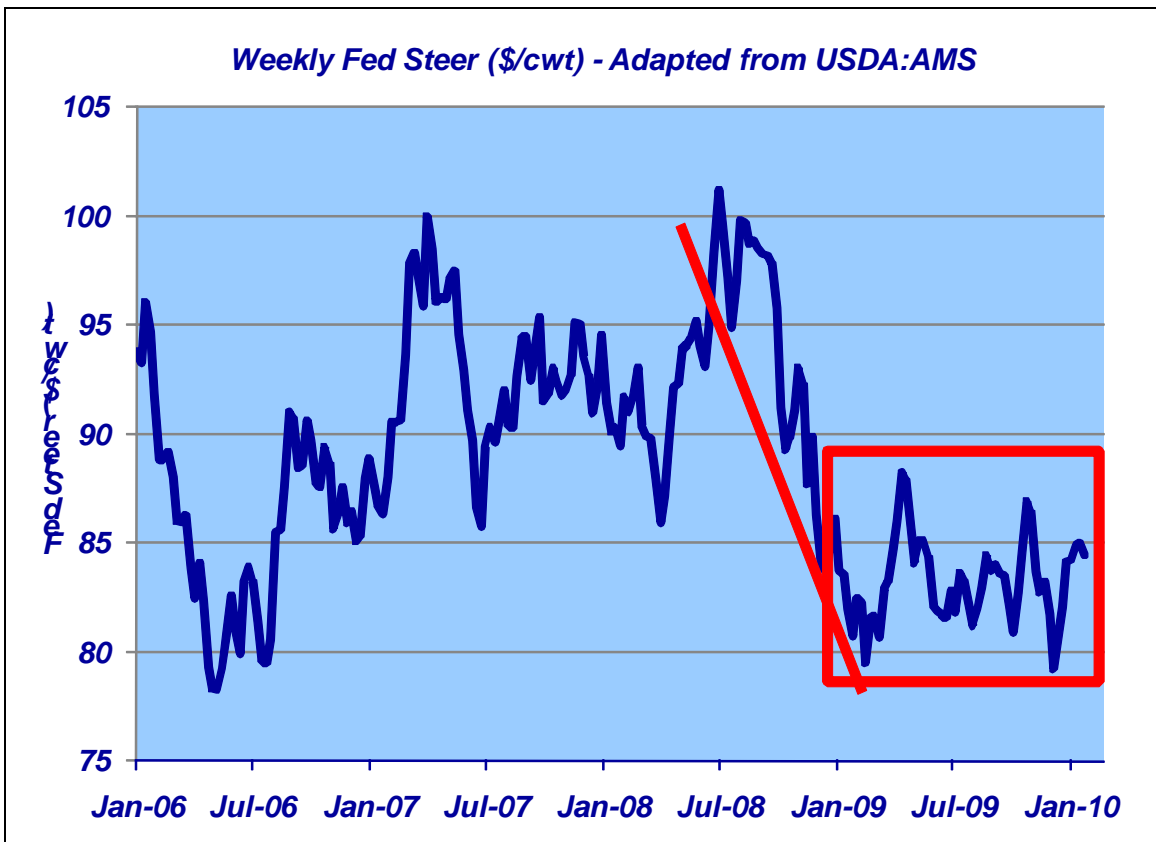
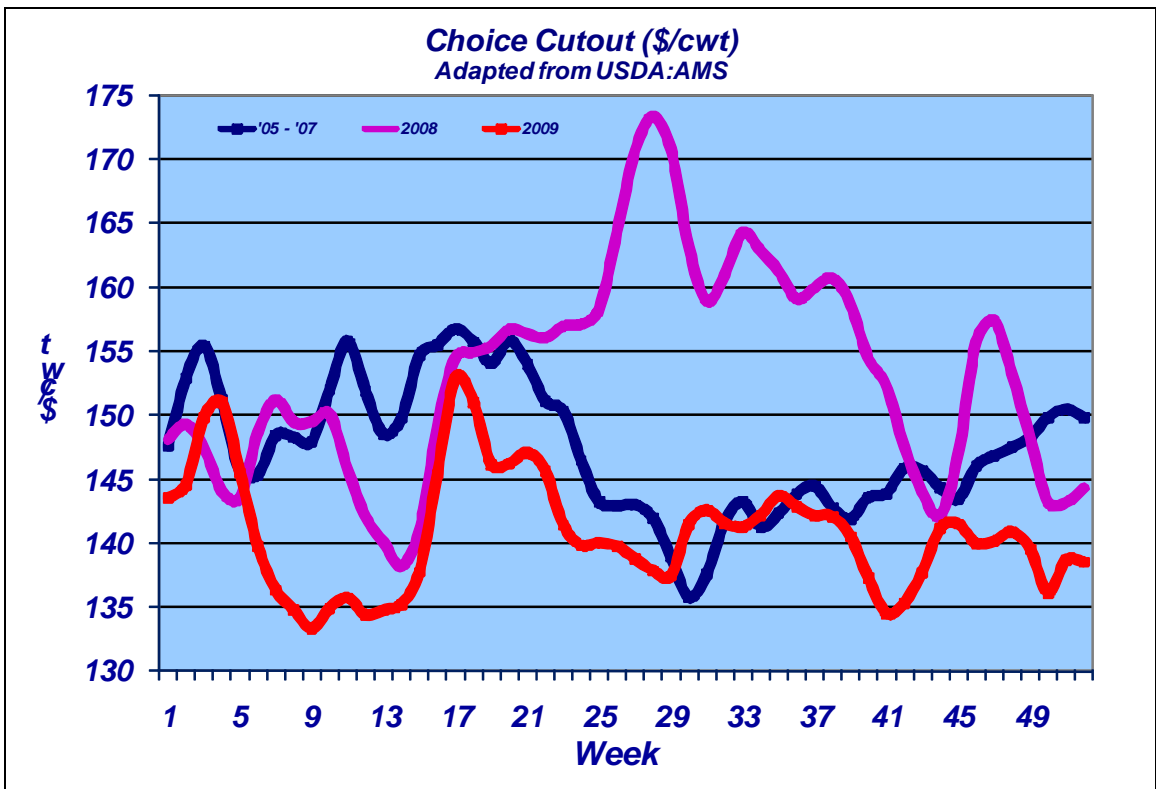
For the beef industry that means consumers are trading down (in favor of pork and poultry) and across (switching from restaurants to retail). That reality has made it difficult for the market to find traction; that’s been the case for most of 2009 and played out again this past week. Cutout values continue to find strong resistance at \$140-5. That directly impacts the fed cattle

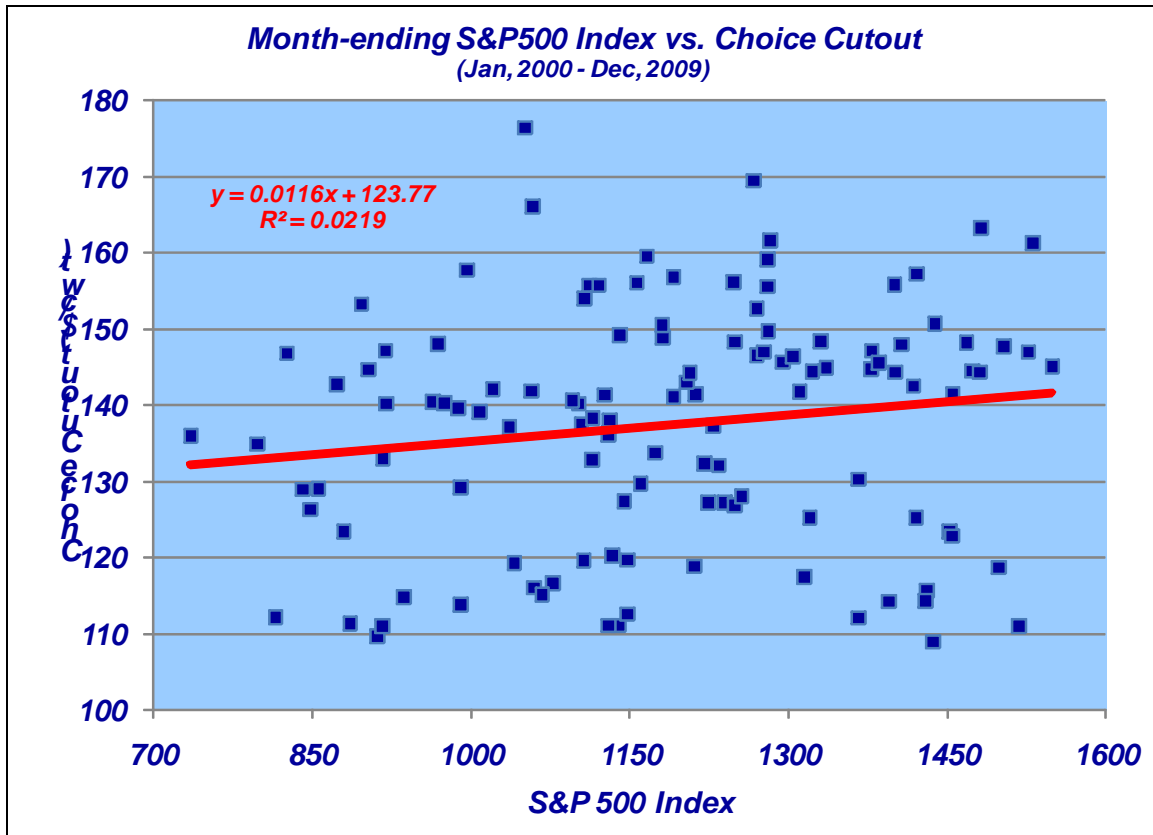
market. Spurred by government stimulus checks in 2008, fed cattle prices experienced a mid-year, contra-seasonal peak at \$101; the market subsequently experienced lower prices over the span of eight months and established a near-term low (\$79) almost a year ago – the difference representing \$275/head. Since that time, fed prices have been stuck in a relatively narrow trading range (see graphs below).

Conventional wisdom generally assumes that beef spending is positively influenced by the “wealth effect” or positive economic growth. At the consumer level that’s usually reflected by various measures including income, home values and investment portfolios. The graph below indicates the beef industry can’t simply rely on an improving economy – it doesn’t automatically equate to better beef sales. (The relationship between the S&P500 index and cutout values is nearly non-existent. And we witnessed a divergent trend in economic growth and beef demand between 2004 and 2007). Given the data and the trends mentioned above, beef sales are not guaranteed to pace GDP growth. Economic recovery is more appropriately viewed as opportunity or a foot-in-the-door to regain market share.

Meanwhile, forecasts for higher prices in coming years are promising – but those need to be interpreted with some caution. Higher prices, based on dwindling supply, don’t necessarily mean more market share and/or new opportunities for producers (nor do they take into account the offsetting effects of inflation and rising costs). In the end, only improved demand - consumers buying more beef at higher values (versus pork and poultry at both the restaurant and retail level) - will provide business growth for producers.

The upshot being that creative promotion and product innovation has never been more important. It also reinforces the need for the beef industry to obsessively manage its cost structure to remain competitive. In the end, back to the original question about the market, perhaps the best wisdom of all comes from Clarice Bean (my daughter’s favorite book character) who puts it like this: “Always remember: it’s the worry you haven’t thought to worry about that should worry you the most.” Or stated another way, amidst the uncertainty and turbulence of a “new normal”, it’s better to worry (i.e. manage risk and monitor costs) and not need to than to not worry and wish you had.





PRICE SUMMARY

WEEK ENDING:

| | 5-Feb | 29-Jan | 22-Jan | 15-Jan | 8-Jan |
|----------------------------------|--------|--------|--------|--------|--------|
| Slaughter Steers (\$/cwt) | 85.76 | 83.23 | 84.30 | 84.53 | 84.17 |
| Choice Cutout (\$/cwt) | 139.34 | 141.40 | 144.95 | 144.91 | 140.23 |
| Select Cutout (\$/cwt) | 136.85 | 137.98 | 140.46 | 139.65 | 134.97 |
| Hide and Offall (\$/cwt) | 9.55 | 9.53 | 9.41 | 9.38 | 9.31 |
| USDA Slaughter Weights (lb) | 1294 | 1296 | 1296 | 1297 | 1297 |
| USDA Steer Carcass Weights (lb) | 836 | 839 | 841 | 843 | 841 |
| CME Feeder Cattle Index (\$/cwt) | 98.43 | 97.62 | 97.01 | 97.26 | 94.90 |
| Cow Cutout (\$/cwt) | 114.03 | 114.71 | 115.76 | 117.49 | 115.63 |
| Corn (basis Omaha: \$/BU) | 3.35 | 3.36 | 3.40 | 3.47 | 3.99 |
| Cattle Harvest (000 head) | 642 | 629 | 665 | 652 | 640 |
| Beef Production (million lb) | 496 | 487.3 | 515.6 | 505.6 | 497 |