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Record Prices, but Will They Last?

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Many key beef production and consumption areas across the world are currently experiencing high or record prices for beef or cattle. In our feature article, we explore what is driving this and whether it will last. Many other issues are also affecting global beef markets at present.

Covid-19

The rollout of vaccines, the transition to robust economic growth, and the advance of the northern hemisphere summer see many areas experiencing lower Covid case numbers and higher economic activity. With restrictions being eased, foodservice sales are also starting to pick up. Figures for China indicated foodservice sales in March were higher than in January 2020, and foodservice sales in the US for April were just below January 2020 numbers. The continued reopening of foodservice should support ongoing demand for beef. On the flip side, low labor availability is starting to restrict operations at some plants, especially in the US.

Argentina suspends exports

Argentina announced in mid-May that it would impose a 30-day ban on the export of beef to alleviate rising domestic beef prices. As Argentina supplied 22% of China's imports in Q1 2021, this could be bullish to trade prices for beef, depending on how long the ban stays in place.

Sustainability momentum rolls on

In late March, JBS, the world's largest animal protein company, announced a commitment to achieve net-zero greenhouse gas (GHG) emissions by 2040. JBS joins a growing list of animal protein companies that have set ambitious targets for GHG-emission reductions.

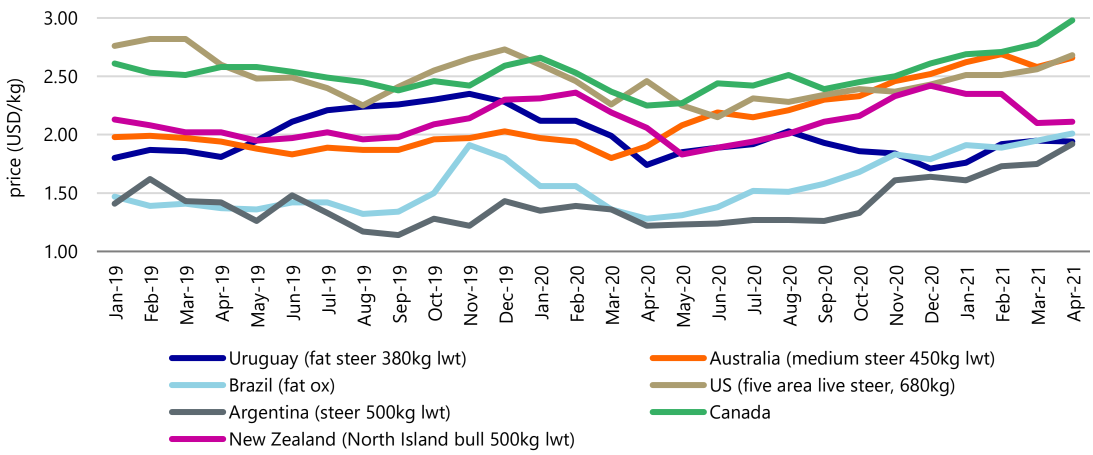
Commodity price hikes drive higher cost of feeding

In April, agri commodity prices pushed to levels not seen since 2011-13, raising concerns about the cost of feed. Rabobank forecasts wheat, corn, and soy prices will remain high – a concern for US cattle awaiting processing and Brazilian cattle faced with poor pasture availability.

Rabobank global cattle prices

Strong demand and limited supplies are driving cattle prices to record levels (see feature article). The Rabobank Seven-Nation cattle price index shows finished cattle prices across all regions – except Uruguay and New Zealand – rose through March and April (*see Figure 1*).

Figure 1: Rabobank global cattle prices, Jan 2019-Apr 2021



Source: Macrobond, AgriHQ, MLA, Rabobank 2021

Feature: Will High Prices Kill High Prices?

Many regions are experiencing either high cattle prices or high beef prices, which raises the question of whether markets are operating at sustainable levels or whether high prices will eventually kill high prices. While there are some common factors, such as strong demand from China, local drivers are arguably more important in creating the record cattle and beef prices we see around the world. We believe many of these local factors will correct and cause an adjustment in prices. However, with China's demand expected to remain firm, we also believe that the market has seen a fundamental step up.

These record prices – whether cattle or beef – also highlight the pressures of a very tight market. Given the growth in demand and global trade, pressures created in the current system mean that seasonal conditions that may have once been considered slightly abnormal are now causing major shifts in markets. While we believe there is underlying strength in the beef market, the tight market and the associated volatility mean planning and managing beef supply chains are even more important.

Strong Demand-Driven Beef Prices – US

Renewed competition between foodservice and retail, triggered by the reopening economy, combined with grilling season, all-time-high consumer income and savings, and strong exports have put the US beef sector squarely in a demand-driven market. In April, beef prices were 18.5% higher at wholesale and 11.5% higher at retail compared to levels seen in 2019 (avoiding comparisons to supply disruptions and panic buying in 2020). While part of the beef price spike in Q2 2020 was driven by reduced production (down 11% vs. 2019), 2021 beef production through April was up 6% against 2019 and up 7% against 2020.

Historically, there is a strong relationship between beef demand and consumer income, with short time delays between changes in consumer income and changes in willingness to pay for beef at the wholesale and retail level. That relationship appears to be holding true in the current market (*see Figure 2*).

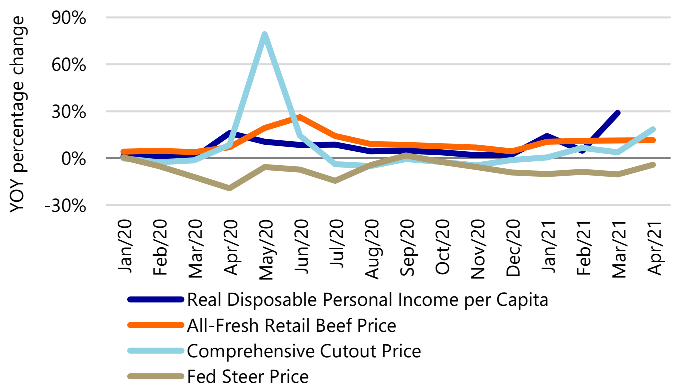
Unfortunately for cattle producers, the imbalance between fed cattle supplies and operational packing capacity has prevented high beef prices from filtering through to cattle prices. We estimate that fed cattle supplies have averaged 120% of operational packing capacity since April 2020. Thus, despite record strong beef demand, cattle prices have been depressed throughout the pandemic.

Moving forward, US retail beef prices could see increases through much of May and even June, as high wholesale prices are passed on to consumers. Wholesale prices should begin to moderate in the near future as the peak of grilling season purchases subsides, restaurant supply chains are filled, and consumer stimulus money is spent or reallocated. That said, cutout prices could remain 5% to 10% higher than pre-pandemic levels for much of 2021. If fed cattle supplies can fall back under packing capacity constraints in Q3, cattle producers will get a larger share of the beef dollar throughout 2H 2021.

Seasonally Delayed Slaughter in a Charged Export Market – Brazil

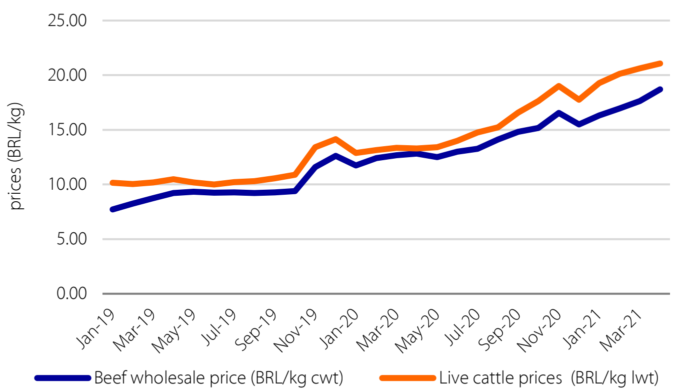
The main driver of higher Brazilian cattle prices has been the delay in seasonal rainfall in a Chinese-charged export market (*see Figure 3*). An inconsistent rainy season led to poor pasture growth and an inability to finish cattle (approximately 50% to 60% of Brazilian cattle are fattened exclusively on pasture). Meanwhile, Covid-related disruptions and a delay in rolling out financial aid to part of the population led to softer domestic demand. However, producers chose to delay the sale of cattle until they reached the desired weight, and supply dropped below demand, forcing slaughterhouses to offer better prices to meet their slaughter planning. Adding to the situation is the requirement that only cattle under 30 months of age can be exported to China (China makes up about 40% of Brazilian exports). The delayed sale of

Figure 2: US YOY change in incomes and prices, Jan 20 – Apr 21



Source: USDC BEA, USDA AMS, USDA ERS, LMIC, Rabobank 2021

Figure 3: Brazil cattle and beef prices, Jan 19 – Apr 21



Source: MDIC, Rabobank 2021

cattle by producers created a bigger squeeze on the availability of cattle that meet Chinese market specifications. High cattle prices have also encouraged breeders to hold females – given the increased value of calves – further limiting the supply of cattle.

Cattle prices started to soften at the end of April following an increase in supply, although reduced supply will limit any further price reductions. Future live cattle prices indicate higher prices in 2H, which should favor margins and improve profitability of the second feedlot campaign.

Low Supply-Driven Prices – Australia

Successive years of drought and large livestock liquidation have resulted in the Australian beef cattle herd being at its lowest point in over 30 years (*see Figure 4*). With such low numbers, the improved seasonal conditions in early 2020, which have carried into 2021 for many cattle-producing areas, saw intense competition among producers looking to restock properties and generate value out of increased pasture production. Young cattle prices jumped almost 30% YOY in February 2020 and rose another 20% in February 2021.

Australian nominal cattle prices loosely follow a pattern of prices stepping up every five to ten years, generally triggered by a local seasonal factor and subsequent recovery of the market. We believe that current cattle prices will ease as cattle numbers increase and producer demand dissipates. However, as the supply chain overcomes the disruption and consumers adjust their price expectations, the market will adapt and a new, higher baseline will be established.

Strong Demand Supports Beef Prices – China

China's beef cattle prices increased steadily entering 2021, and were up 9% YOY in April (*see Figure 5*). This is a big contrast to stagnant poultry prices and declining pork prices. Compared with the same period in 2018 (pre-ASF era), cattle prices have seen even stronger growth, rising over 30%. In previous decades, China's beef prices escalated to a new level every four to six years. The key driving force behind this price escalation has been the slow growth of domestic production, which has not been able to keep up with the strong growth in consumption. This has led to rising beef imports by China in past years.

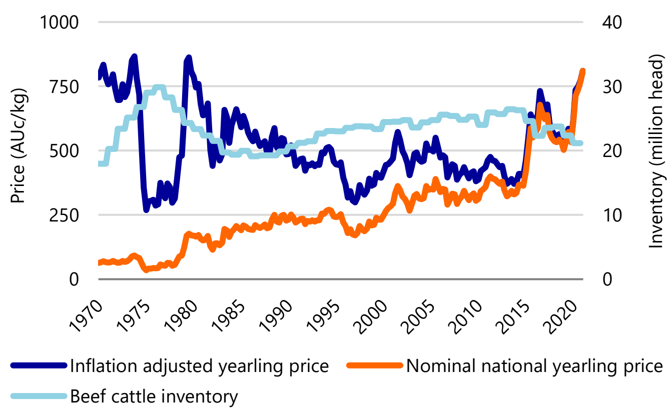
The current round of price increases was first triggered by ASF outbreaks in 2019, as beef was substituted for pork on some occasions. Covid-19 saw disruptions to beef supply, but beef consumption remained resilient, shifting partially from foodservice to at-home consumption. As a result, beef imports have continued rising to cover the gap between local supply and demand despite Covid.

Following the normalization of the economy and consumer behavior that is expected after the pandemic, beef consumption outside of homes will recover. However, we believe the habit of cooking beef at home established in the past two years will persist and become a new channel for beef consumption. While a portion of beef consumption will shift back to pork when pork production recovers, we expect strong beef demand to remain as new markets will have been established. This will continue to drive imports from the global market.

Reduced Supply Lifts Prices – Europe

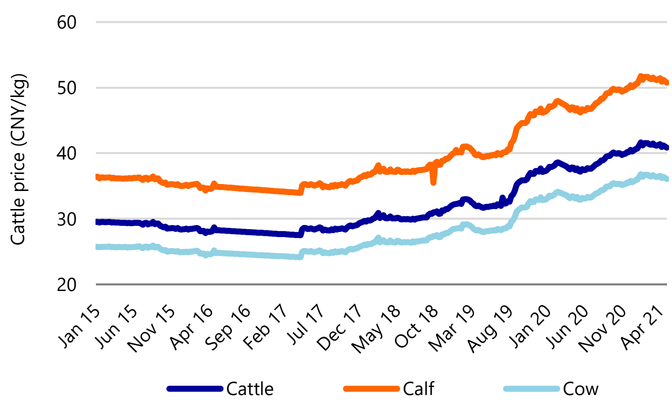
EU beef carcass prices have been firming since Q4 2020, with the average EU beef carcass price currently up 7% on the same period last year. Cow prices are even higher, up 15% YOY, indicating a shortage of slaughter cows. However, this is compared to a relatively low base, as Covid heavily affected prices in this period last year. Still, prices show strength and have moved against the declining seasonal trend in the first couple of months of this year, driven by reduced cattle supplies across the EU. Low profitability in the past year likely reduced the numbers brought in by beef finishers, leading to low cattle availability in 1H 2021. Although an increase in supply is expected in 2H 2021, prices will likely be held up by increased demand as foodservice reopens.

Figure 4: Australian cattle prices and inventory, 1970-2021



Source: ABARES, ABS, Rabobank 2021

Figure 5: Chinese cattle prices, Jan 2015-Apr 2021



Source: Chinese Ministry of Agriculture, CAAA, Rabobank 2021

Regional Outlooks

Australia: The Pendulum Is Swinging

In an indication that we might see producer demand ease soon, the balance of buyers in the weaner cattle market is starting to return to normal. Local producer demand has driven cattle prices to record levels as they look to restock paddocks. But among the lower numbers of cattle currently on offer, a more normal balance is returning, with producers dropping back and feeders taking a more active share of the market (*see Figure 6*). Compared to 2020, when producers were the largest buyers in the category for many months, the first three months of this year have seen them occupy, on average, 39% of the market compared to feeders at 50%.

But producers are still paying the premiums – about 6% above the market average. This continues to support cattle prices, and after reaching a new record of AUD 9.10/kg cwt on April 20, the EYCI dipped slightly before recovering to AUD 9.02 on May 14. Producers generally occupy a large part of the market until July, and without major seasonal change, the strong producer demand should continue to support prices through Q2.

Slaughter numbers remain very low. East coast weekly cattle slaughter for the four weeks of April were down 30% YOY and down 31% from the five-year average.

Reflecting lower production, beef exports also remain low. April exports (72,502 metric tons swt) were down 22% YOY and down 11% from the five-year average. With fewer cull cows in the system, higher prices and different product offerings have seen Australia's export customers shift focus slightly. China has dropped its share of total exports from 24% to 17%, and the US has dropped from 20% to 15% between 2019 and year-to-date 2021. Meanwhile, volumes to Japan and South Korea have lifted slightly for the first four months of 2021.

Brazil: Production Improves Slightly, and Cattle Prices Ease

Poor pasture conditions caused a short-term increase in the supply of slaughter cattle at the end of April. This has relieved upward pressure on live cattle prices, but we do not expect larger slaughter numbers and price declines to continue.

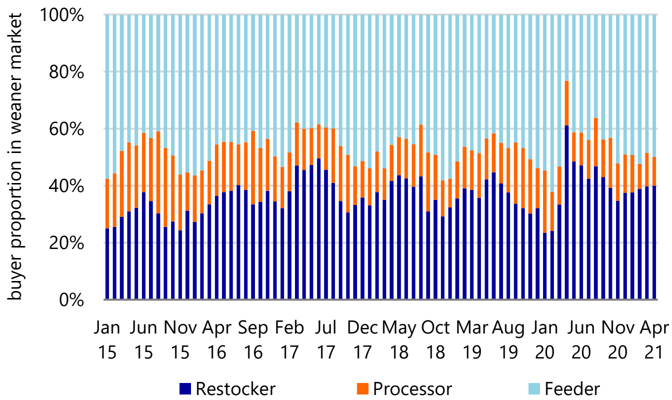
Below-average and irregular rainfall in important producing regions through Q1 2021 reduced pasture availability and capacity to fatten cattle, leading to lower slaughter numbers. Despite higher numbers at the end of April, we believe these poor conditions, together with continued drier seasons, will see fewer cattle fattened on pasture this season. Furthermore, female retention in the herd – which has also contributed to lower slaughter numbers – has also led to atypical cattle price increases in Q1, despite the seasonal fall in beef demand.

Wholesale beef prices remain bullish, but some daily price drops in early May suggest they may start to fall. On the other hand, the return of financial aid in April has lifted domestic demand, which may support prices in the short term. Although bullish, wholesale prices – which have risen 46% YOY – have tracked below live cattle prices, which have risen by 58% YOY. The strong export demand is reducing the need to pass through all the livestock price increases to domestic consumers.

Exports registered good volumes in March and April, and are 2% higher YTD (*see Figure 7*). China continues to lead national shipments, with a 23% increase in year-to-date purchases. Hong Kong remains the second largest importer despite the 13% drop in sales in the same period. In addition, Chile and the US took the third and fourth place in Brazil's export market, due to the strong retraction in exports to Egypt (-46%).

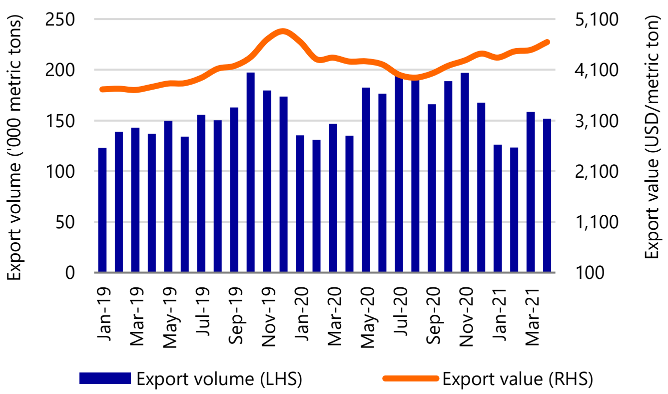
Beef production in 2020 was severely constrained by low domestic consumption and recorded an 8% decrease in slaughter numbers and a 5% decline in weight.

Figure 6: Buyer proportion in weaner cattle (EYCI) market, 2015-2021



Source: MLA, Rabobank 2021

Figure 7: Brazilian beef exports, Jan 2019-Apr 2021



Source: MDIC, Rabobank 2021

Canada: Beef Supply Chain Avoids Covid Impacts

As of early May, Canada was in the midst of a third Covid-19 wave, with much of the country under restrictions. Against this backdrop, multiple meat and poultry packing plants have faced temporary Covid-related shutdowns in recent months. Fortunately, the major beef packing plants have remained in operation, with year-to-date weekly cattle slaughter (up to April 24) up 5.7% compared to 2020 and flat compared to 2019. Year-to-date weekly average dressed steer weights were only 8lb above 2019. It seems Canada's fed cattle supply is closer to being current than the US. As a result, beef production is up 7.9% and 1.5% YTD compared to 2020 and 2019, respectively.

In late April, Alberta fed steer prices were down 2% in CAD terms compared to 2019 (*see Figure 8*). But due to a strengthening CAD, prices were up 6.7% on 2019 in USD terms. In USD terms, Alberta fed steer prices are typically at a discount to the US five-market average. However, a stronger CAD and ample US fed supplies have shifted this relationship. Since early December 2020, Alberta prices averaged nearly USD 5/cwt above the US market. This price premium has driven the 10% YOY decline in cattle exports from Canada to the US in Q1. At the same time, imports from the US reached 100,000 head for only the fifth time since 1988.

Strong demand from the US, Japan, and Mexico helped lift Q1 exports 12% YOY. Meanwhile, high US beef prices, ample Canadian supplies, and a restricted economy kept Q1 imports down 7% YOY.

With beef cow inventory down nearly 17% since 2010, Canada's expanding cattle feeding sector is increasingly dependent on US feeder cattle imports. Thus, if Covid challenges at plants subside, Canadian cattle prices stand to rise on reduced North American cattle supplies and strong US beef demand, but profitability will be limited by high feed costs. Cattle on feed was down 1% YOY, but up 8% against the 2015-2019 average in April.

China: Beef Prices Remain Strong

China's beef prices have been resilient despite weak pork prices that have continuously declined since February 2021. Retail beef prices declined only slightly in April, to CNY 87/kg, down 3% from the peak in February, but up 4% YOY. Meanwhile, pork prices fell 26%, and white broiler dropped 4% (*see Figure 9*).

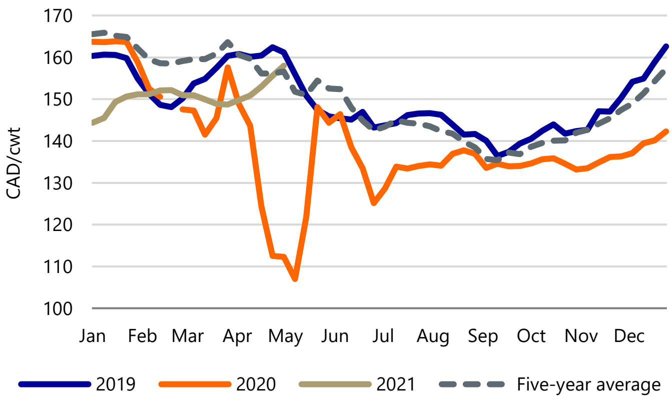
Beef supply is improving. Imported beef that had previously faced extensive delays at ports due to testing and inspections is now flowing faster and is being distributed into the market. Domestic beef production also increased 6% YOY, to 1.65m metric tons, in Q1 2021, according to China Statistics Bureau. Given this lift in supply, we believe the strong beef prices mainly reflect strong consumer demand.

We expect China's beef production growth to slow for the rest of 2021. Cattle withheld from slaughter in 2020 due to lower consumption are now believed to have been worked through the system. Local supply will remain limited in the coming months.

On the demand side, foodservice has nearly recovered from the declines that followed lockdowns imposed due to the pandemic. But higher beef and sheepmeat prices have forced restaurants to seek out lower-priced cuts. Meanwhile, we believe the rise of beef consumption at home is a structural change, leveraging the rapid growth of modern retailing, especially online shopping.

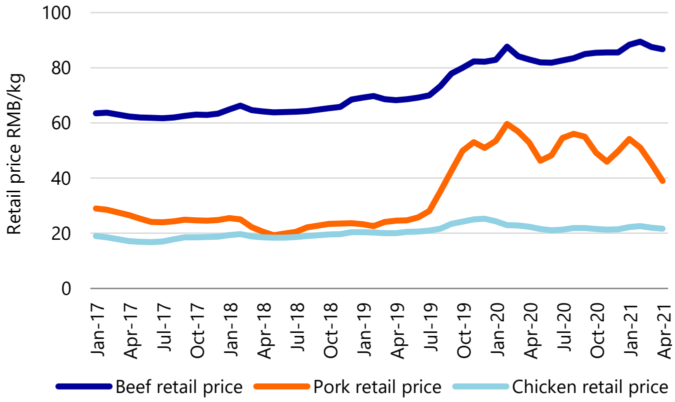
China's beef imports were strong in Q1, reaching 617,000 metric tons, up 20% YOY. Brazil strengthened its lead position, lifting its share to 40% of China's total imports. Brazil is followed by Argentina (22.5%), Uruguay (14%), New Zealand (9%), and Australia (7%). Australia's position has fallen from the third largest supplier to fifth, due to high export prices of Australian beef and limited supplies. We expect lower imports from Australia will continue in the coming months, and the US will likely fill in the void by shipping more beef to China.

Figure 8: Alberta fed steer prices, Jan 2019-May 2021



Source: Canfax, Rabobank 2021

Figure 9: Chinese retail meat prices, Jan 2017-Apr 2021



Source: Chinese Ministry of Agriculture, CAAA, Rabobank 2021

Europe: Weak Production, Strong Prices

In the EU-27+UK, limited cattle supplies resulted in a sharp 9% YOY contraction of beef production in the first two months of the year, with production declining in most markets. We have seen the largest declines in Ireland (-20% YTD), Poland (-19%), the Netherlands (-14%), and Germany (-13% YTD). Although we generally expect lower supplies to persist through the year, production will likely gather pace in the coming months, as consumption is expected to pick up in 2H 2021.

Beef trade also slowed in the beginning of the year. For the first two months of 2021, EU-27+UK beef exports fell by 11% (down 9,000 metric tons). Increasing volumes to the Philippines, Bosnia and Herzegovina, and South Africa could not compensate declines to other destinations, such as to Ghana, Côte d'Ivoire, and Hong Kong. Beef imports to the EU-27+UK were also down by 26%, as demand is still impacted by Covid-19-related lockdowns in many parts of Europe. Volumes from Brazil and Argentina were down by 24% and 38% YOY, respectively, for the first two months of 2021.

Brexit-related trade frictions had a significant impact on two-way trade between the EU and UK. EU-27 beef imports from the UK declined by 68%, whereas EU-27 exports to the UK declined by 39%, with volumes from Ireland to the UK contracting by 26% in the first two months compared to the same period last year. Lower product availability as a consequence of lower throughput possibly also played a role in Ireland's weak exports to the UK.

Even though restrictions in foodservice continue to impact demand, the contraction in supply is firming up prices. The EU average beef carcass price is up 7% YOY and up 2% compared to the five-year average in week 17 (*see Figure 10*). We expect prices to trend above 2020 levels into Q3 2021. In 2H 2021, the expected reopening of foodservice may provide further support to prices. However, higher feed prices coupled with dry weather conditions may reduce farmers' margins.

Mexico: Drought Starting to Bite

With nearly 85% of the country in some level of drought at the beginning of Q2 2021, the beef herd is showing signs of decline. Between 2015 and 2020, the Mexican beef cow inventory grew at a 3.3% CAGR, but from 2020 to 2021, annualized growth declined to 0.6%. The share of heifers in feeder cattle exports to the US in April was at 27% compared to the 2015-2020 average of 19%, signaling a slowdown in replacement heifer retention. Under current conditions, beef cow inventories may start to decline for the first time since 2013-2014.

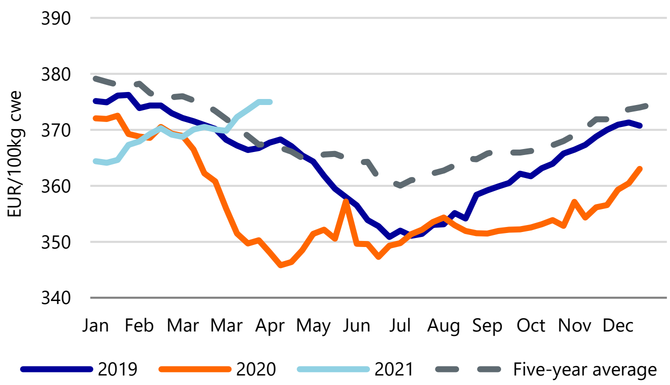
Q1 beef production (504,000 metric tons cwe) is up 2% YOY. With the 2020 calf crop up 1% compared to 2019 and feeder cattle exports to the US down 6.6% YOY for April, beef production will likely continue above 2020 levels. Although drought conditions and high feed costs have potential to reduce carcass weights, these same conditions could also spur liquidation, adding to slaughter numbers in the short term.

The finance ministry has lifted its expectations for total 2021 GDP growth to 5% YOY based on the reopening of both its domestic economy and its largest trade partner, the US. Reported Covid cases have fallen dramatically since January, and restrictions continue to be loosened.

Ample beef production in the US, a Mexican peso closer to pre-Covid strength, and the gradual reopening of Mexico's economy shifted beef trade closer to pre-Covid norms (*see Figure 11*). While Q1 2020 beef exports were up 14% vs. 2019, Q1 2021 was only up 8% against 2019. High US beef cutout prices in February helped boost March exports to the US, up 8.5% YOY.

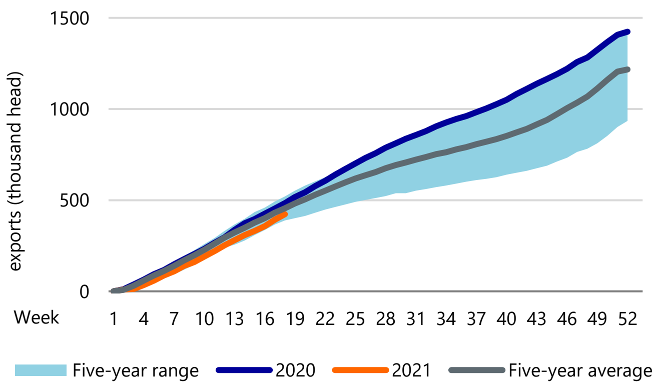
Cattle prices are strong year-on-year, with March #1 and #2 feeder cattle prices up 11% and 19% (in MXN/kg), respectively. But against 2019, prices were flat to 10% lower. High feed costs could make further price appreciation a challenge. On the other hand, high US beef prices and the reopening of Mexico's economy boosted March hot carcass prices – up 25% YOY and up 15% compared to the five-year average. As long as high feed prices and strong beef demand are in play, this disparity is likely to continue.

Figure 10: Average EU carcass price, Jan 2019-Jan 2021



Source: European Commission, Rabobank 2021

Figure 11: Mexican net cattle exports, 2020-2021



Source: TDM, St. Louis FRED, Rabobank 2021

New Zealand: Cattle Prices Starting to Lift

Rabobank expects farmgate prices to hold steady during May, with the reduced competition from Australia assisting New Zealand product in finding a home with the change in seasons in the US. But, the recent news of Argentina ceasing beef exports, together with low supplies from Australia and New Zealand's position to supply chilled beef to China create definite upsides for farmgate prices.

Total beef production for the season to date (April 17 - week 28) is up 7.8% on the same period last year. The increase has been driven by an increase in steer and heifer production (up 17.6% and 20.4%, respectively) and an increase in bull beef production (up 3.6%) – which has offset a 2.1% decline in cow beef production. North Island cow production dropped 8.1%, while South Island cow production increased 11.7%.

Farmgate prices showed signs of life and nudged upward in April 2021 (*see Figure 12*). As of the end of April, the AgriHQ North Island bull price was 6% higher compared to the same period in 2020, at NZD 5.15/kg cwt. The AgriHQ South Island bull price was also higher at NZD 4.60/kg cwt over the same period.

NZ beef exports rose 5%, to 266,875 metric tons, for the seven months to April 2021. However, the value of exports (in NZD terms) fell 9.2%, with a much stronger NZ dollar contributing to some of this fall. Volumes to China and the US were up 4% and 12%, respectively, compared to the same period last year.

New Zealand farmgate returns have benefited from less competition from Australia in key markets – particularly the US. US demand for manufacturing beef has lifted in line with the changing of the seasons, with some warmer weather bringing out the barbecues, along with the reopening of eateries, as vaccinations become more widespread and restrictions ease in some states. These dynamics will continue over the next month, helping to maintain New Zealand farmgate prices.

US: A Market Out of Balance

Demand for US beef continues to be exceptional, both in the domestic and the export markets. At the very same time, fed cattle prices continue to be a huge disappointment. This imbalance is due to limitations in slaughter capacity – especially in the fed slaughter sector.

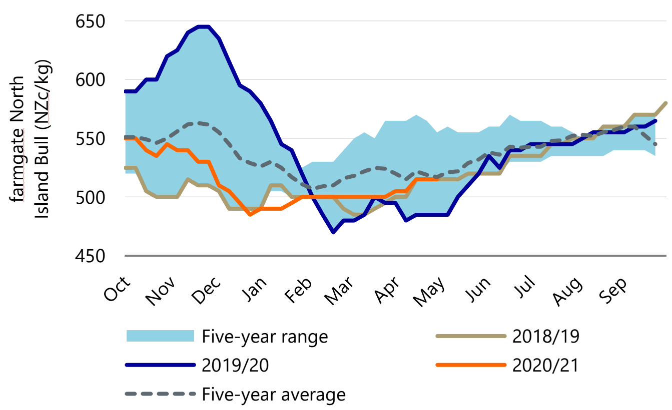
An already insufficient fed cattle slaughter capacity is being further hamstrung by a number of factors, the biggest factor being a shortage of labor. Furthermore, the Covid-19 health and safety protocols and spacing requirements implemented a year ago are restricting the productivity of available labor. And, larger-than-normal slowdowns due to weather and plant maintenance issues have also compounded capacity constraints.

Strong demand for finished product and insufficient means to get cattle harvested is driving the leverage index in favor of the packer (*see Figure 13*). At this time, fed cattle price is 41% of beef cutout values. The inability to harvest cattle on a timely basis is holding carcass weights and beef tonnage above projected levels, making cleanup of excess cattle supplies even more challenging and adding additional pressure to the leverage index. Year-to-date fed cattle slaughter is up 4.5% from a year ago, while beef production is up 9%. The bottom line is the long-anticipated cleanup of excess fed cattle supplies just keeps hanging in front of the market.

Despite increased feeding cost, demand for replacement cattle remains stronger than earlier expectations. 2021 is the third year of cow liquidation, and it is starting to force a reduction in feeder cattle supplies. Reduced feeder supplies and sharply higher production costs are forcing a reduction of feed yard placements. We expect this will reduce fed cattle supplies in late Q3 and into Q4.

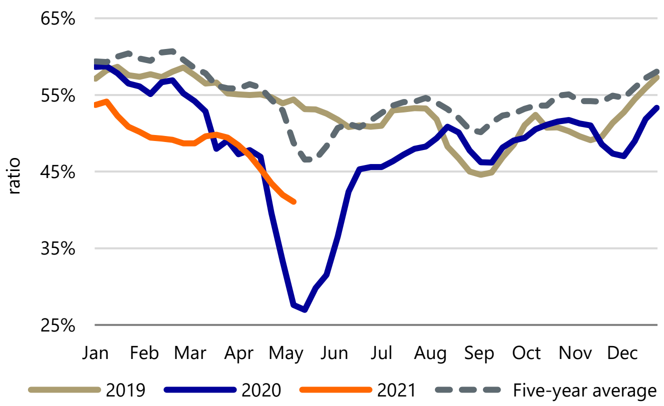
Year-to-date cow slaughter is up 2.5% from a year ago. Continued drought conditions across the western US, rapidly escalating feed cost, and tight hay supplies are forcing the sale of cows. The escalation in domestic cow slaughter is buffering the domestic market from high international prices for lean trimmings.

Figure 12: NZ cattle price, 2018-2021



Source: AgriHQ, Rabobank 2021

Figure 13: US fed steer price to Cutout ratio, January 2019-Feb 2021



Source: USDA, Rabobank 2021

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