Making the Best of Less

Industry trends affect supply for the brand.

Story by
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The year 2012 will go in the books as yet another epic period for the cattle industry. It began with an outlook of optimism in most sectors, as it appeared nationwide cow numbers would begin to stabilize and corn-planting intentions foretold more manageable feed costs. Mother Nature had plans of her own, however, and the many impacts cannot be repaired with a few good inches of rain.

Supply and demand drive commodity markets, and we've been tearing down the cattle supply for some time now. The southern U.S. drought of 2010-2011 created advanced liquidation of cow numbers in that important cow-calf region. Expectations a year ago would have seen a halt to cow liquidation simply due to a recovery or stabilization in the south, while cow-calf revenues should have also buoyed cow numbers in states with better moisture coupled with high calf prices.

However, the wider spread of drought across the country in 2012 has further deteriorated cow numbers in what has become a five-year trend of cow-culling rates greater than 10% of the Jan. 1 cow herd inventory, according to economist Derrell Peel of Oklahoma State University. Increasing land values and the advancing average age of cow-calf operators compound the herd decline.

Bright spot

Retention of replacement heifers appears to be the only bright spot in the breeding-female population, as the 2012 fed-cattle harvest has been composed of 36.5% heifers compared to the 2011 figure of 37.1%. Even so, this is a historically high share of heifers being fed to finish rather than retained for breeding. That percentage of retained heifers is being compared to a smaller and smaller U.S. cow herd total.

Fig. 1: USDA weekly boxed beef prices, 2012

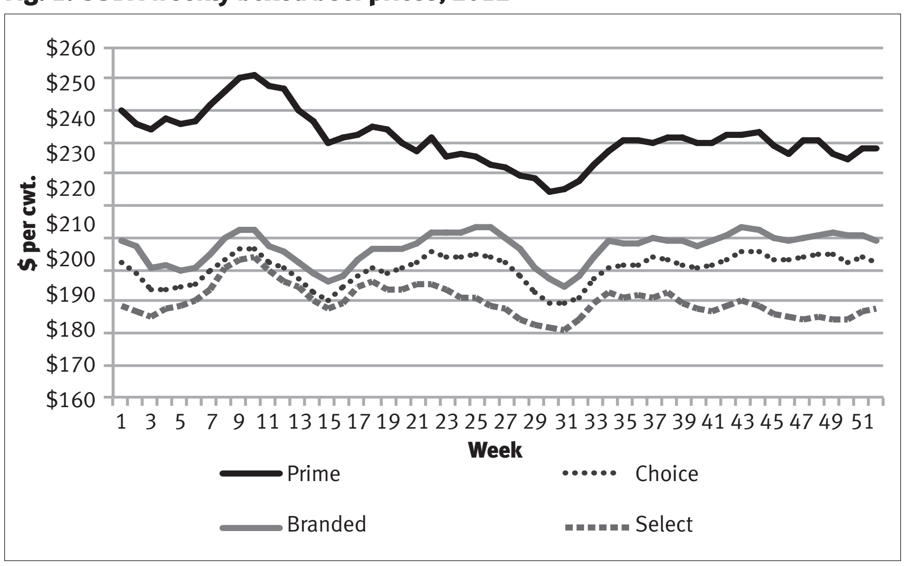
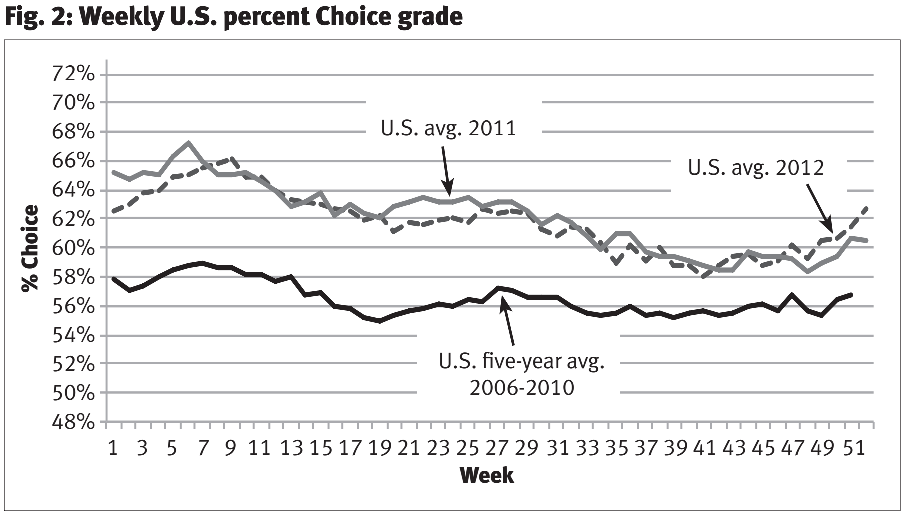


Fig. 2: Weekly U.S. percent Choice grade



To summarize the supply story that's been developing all year, the overall U.S. harvest for all classes of cattle was down 3.59%, or 1.2 million head. Fed cattle averaged 78.4% of the federally inspected cattle harvest, compared to 78.3% a year ago. That was not a numerical gain, and harvested head counts were reduced on the fed-cattle share, down 3.31% for the year.

Profitability in the feedlot sector was scarce in 2012 as feed costs caught many off guard, particularly those leaving their corn needs unhedged.

Even so, carcass production tonnage saw a setback of only 1.08% on the younger fed cattle due to monumental and consistently higher carcass weights throughout the year. Steer carcasses were 18 lb. heavier than in 2011, with a 52-week average of 858 lb. on the rail, hitting a maximum of 880 lb. in the months of October and December.

Heifers weren't to be outdone, as they finished the year 19 lb. heavier than the last year's average, with the heaviest reported average of 815 lb. That new record came during the second week of November, much higher than the previous record of 806 lb. set in October 2009.

A year ago we celebrated what had been the highest achievement in carcass quality grading that the industry had ever seen. 2011 topped a five-year run-up in the percentage of Choice-grading carcasses, culminating in an aggregate move from 51.7% Choice in 2006 to 62.1% in 2011. We gave a little back over the past year. The data indicates the Choice grade lost about half of a point to average 61.78%. Although annual improvement has subsided, at least for now, we should bear in mind that the current figure still ranks as the second highest in USDA data history.

Sourcing supply

To offset the smaller available pool of beef-type domestic fed cattle, packers and feeders had to reach outside of their normal supply to achieve any semblance of steady throughput of harvest-ready cattle. As a result, higher percentages of fed cattle came from domestic Holstein steers, Mexican feeder cattle and Canadian feeder and fed cattle.

Those outside sources contained fewer black-hided beef animals, so a residual effect was a decline in the share of fed cattle eligible for the many Angus branded-beef programs. Once eligible, such cattle are evaluated for further carcass specifications, such as those imposed by the *Certified Angus Beef*® (CAB®) brand. That point is summarized in the USDA's 2012 figure showing a black-hided percentage of fed cattle at 61.17% vs. 62.87% last year. Still, the portion of Choice grade stamped with USDA-certified premium-Choice brand for all labels was steady at 24.87% on the year.

Although they've underpinned carcass weights and overall beef tonnage, the beta-agonist feed additives that have permeated the feeding industry in a few short years are known to depress quality grade by a few critically important marbling score points. Cattle feeders and nutritionists have learned better strategies for use of these compounds since their introduction, and quality genetics have advanced enough to keep pace. That's seen in late 2012, with carcass weights at all-time highs at the same time quality grades picked up: their fourth-quarter push saw Choice trending in line and ahead of the 2011 pattern. Meanwhile, the share of Prime went to 4.09% in late October and averaged 3.87% through the end of the year, compared to 3.28% for the same period in 2011.

Profitability in the feedlot sector was scarce in 2012 as feed costs caught many off guard, particularly those leaving their corn needs unhedged. The upside for feeders of quality cattle came in the form of grid premiums, at least in the second half of the year. From July through December, the Choice-Select price spread averaged $13.52 per hundredweight (cwt.) on a carcass basis, compared to $6.63 per cwt. for the first half of the year, according to USDA. Values for the Prime grade in 2012 were even stronger as boxed beef in that category commanded a $40.94-per-cwt. premium over Choice, a clear indicator of demand for the most highly marbled products.

Similarly, USDA reported that grid payments from packers to feeders marketing CAB brand carcasses averaged $3.89 per cwt. over Choice, with the highest-ever reported average coming in the third week of November at a weighed value of $5.14 per cwt. Some of the dynamic grids that change weekly based on market signals were quoted to offer as much as $9.00 per cwt. for a CAB premium during strains on the supply and demand balance.

Editor's Note: *Paul Dykstra is a beef cattle specialist and author of the weekly "Rearview Mirror on Quality" column for Certified Angus Beef LLC.*