Market Gleanings

Navigating the Upside

by ***Wes Ishmael***

New and existing market dynamics.

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Barring an unforeseen cosmic unraveling, cattle supply fundamentals set the stage for a sustained period of higher cattle prices, perhaps eclipsing the historical heights achieved in 2014-15.

There are certainly similarities. Primarily, it's the significant herd liquidation forced by drought, even more this time around than about a decade ago. As then, steadily increasing prices will likely shift into overdrive when enough folks begin retaining females to rebuild the herd (see Simmer, Page 44).

There are plenty of differences this time around, too, from the higher cost structure to generational shifting and a variety of market-altering influences from outside the industry.

Here are a couple of old and new dynamics to keep on the radar.

Flatter cattle cycles

Despite many suggestions of its demise over the years, the venerable cattle cycle is alive and well. It still guides producers to increase or reduce the national cattle inventory as production ebbs and flows, pushing prices one direction or another far enough to incentivize response.

Given cow biology — one calf per year, hopefully — and the time it takes that calf to enter the marketplace, an entire cattle cycle typically encompasses 9-13 years. That's from the beginning, when cattle numbers are the lowest, through peak numbers and then back to the trough when another cycle begins. The current cattle cycle began in 2014. It peaked in 2019 and is still in the process of discovering the bottom side.

With all of that said, cattle cycles have changed dramatically over the last seven decades, according to *An Updated Evaluation of the U.S. Cattle Cycle,* authored by Glynn Tonsor, agricultural economist at Kansas State University (K-State) and agricultural economics graduate students Jaime Luke and Andrew Anderson.

In a nutshell, the authors explain cattle cycles have grown less pronounced over time — the difference between cattle inventory highs and lows is less — as the industry churns out increasing levels of beef production per cow in the inventory.

"For example, average annual beef production in the current cycle is 15% greater than it was in the 1967-1979 cycle although the beef cow inventory is 22% smaller," say the authors. Much of that stems from the genetics and management that enable ever-increasing fed cattle carcass weights.

The less pronounced cattle cycle also impacts the associated price cycle, which suggests heifers purchased through the low part of the price cycle are producing calves through the high part of the price cycle and vice versa. So, market timing may carry more weight when there's the chance to build back this time.

"Market timing will be huge," says Rick Machen, the Paul C. Genho Endowed Chair in Ranch Management at the King Ranch Institute for Ranch Management (KRIRM), Kingsville, Texas. "Higher prices won't stay forever. The quicker you can get in, the better off you'll be."

Machen and KRIRM students recently conducted an analysis for one cow-calf client. In every scenario tracking net present value over the next 10 years, the quicker females went into production, the more the profit potential (see Rethink, Renew and Reshape, Page 1).

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"The cattle inventory cycle has three phases — expansion, liquidation, and turn-around. Each phase has unique price relationships and profit opportunities. The optimum production strategy differs among phases," explains Lee Schulz, Extension livestock economist with Iowa State University in the December Ag Decision Maker.

Schulz goes on to provide heifer price perspective.

"In November 2022, heifers bred to calve in spring 2023 sold at 1.71 times the value of 500-600 pound heifers. This is the lowest this ratio has been in the last four Novembers. The ratio can spike during expansion years. In November 2014, bred heifers reached $3,250. Some sold for even higher, usually based on genetics," Schulz explains. "In November 2014, the combined Nebraska auction price of 500-600 pound, Medium and Large No. 1 heifers averaged $270 per cwt. Thus, bred heifers were worth 2.19 times the value of heifer calves. Given where bred heifer values are currently and where they could be going, they may be presently undervalued a bit."

New and expanded packing capacity

As more marketing leverage returns to producers — as there becomes too much packing capacity chasing too few cattle — plenty of plans are in the works to expand capacity further through new construction and expansion of existing facilities.

Tonsor offered an update at the Kansas Department of Agriculture Ag Summit last August. At the time, 13 entities had announced plans to grow packing capacity by approximately 23,000 head per day, a combination of fed cattle and cull cows. Some of those plans have since been shelved, in part because of surging construction costs, and some others appear to be headed that way. Currently, an inexact and generous estimate suggests 15,000 head per day is the potential topside for new capacity. Past experience suggests the reality will be less.

For the sake of argument, let's say new capacity amounts to 9,000 more head per day, not all at once, but over time. Let's also assume current existing capacity remains in production.

"Generally, more plants mean more competition, but supplies will be tight enough that I'm not sure you'll be able to tease out the differences for a while," says Katelyn McCullock, director and senior economist with the Livestock Marketing Information Center. Regionally speaking, she says how the cow herd builds back in the area, and which new plants are built and where, will determine the price impact.

"I think the larger impact could come from the cow-kill plants that are being built," McCullock says. In the Southern Plains, for instance, she notes the volume of cows moving through existing capacity has depressed cull cow values compared to the rest of the nation.

"Until we pull capacity away, it will be supportive to fed cattle prices," Tonsor says. "Let's say 9,000 head capacity is added. I think we'll see other existing capacity mothballed within three years." He believes shuttered capacity could come from outdated facilities owned by the larger packers and from small independents who can no longer afford to chase higher-priced cattle through this stage of the cycle.

Given the enormous economic cost to build per-head capacity, Derrell Peel, Extension livestock marketing specialist at Oklahoma State University, says anyone building or expanding currently will face challenges.

"If these plants get built, the capacity won't go away, but the ownership will likely change if history is any indication." Typically, he observes that it is about the third owner of a packing plant that can finally make it pencil — after the original investment has been discounted significantly a couple of times.

So, new capacity could offer some added price support for a time. Five years down the road, though, the industry might still be hunting more shackle space. **HW**