Up and Then Some

Market conditions suggest cattle price strength for an extended period.

by ***Wes Ishmael***

No matter how stubborn the beads on your own abacus, cattle prices continue to run higher and faster than many anticipated. Given what appears to be ongoing beef cow herd liquidation and the dearth of replacement heifers, this is only a prelude of markets to come.

"We're 18 to 24 months from the price highs," says Lance Zimmerman, senior protein analyst at RaboBank. "The expansion timeline is currently similar to 2012. We haven't begun to retain heifers. We still have our foot firmly on the gas pedal of beef cow slaughter."

Likewise, Dave Weaber, protein analyst for Terrain believes the peak in the current price cycle comes in 2025-26, a year later than he anticipated originally.

"We expect further tightening of feeder cattle and calf supplies during the second half of 2023. Improving moisture conditions across much of the Central Plains and West combined with now-record fed cattle prices have feedyards chasing replacement cattle and driving prices markedly higher," Weaber explains.

In June, Weaber and Terrain forecasted the 2023 price range for feeder steers (700-900 pounds, Central Plains and West) at $235-$270 per hundredweight (cwt.) Price projections for fall-delivery steer calves (500-600 pounds) were $275-$300, depending on quality.

By way of comparison, USDA's Economic Research Service (ERS) pegged the third-quarter feeder steer price (750-800 pounds, Oklahoma City) at $224 per cwt. in the June *Livestock, Dairy and Poultry Outlook*. ERS forecast the fourth-quarter price at $226 for a 2023 average price of $210.62. Next year's annual average price was projected to be $226.50.

On the other end of the scale, ERS projected the fed steer price (five-area direct) to be $173 in the third quarter and $174 in the fourth quarter for an annual average of $171.73. Next year's annual average price was forecast to be $180.

Weaber explains cash fed cattle prices (five-area direct) were record high in the second quarter this year, exceeding prices at the peak of the last cycle. He points out part of the strength in fed cattle prices came from a couple of novel factors.

One was the new sow housing and handling requirements (Prop 12) that became law in California on July 1. Weaber explains the new regulations mean there is a significant shortfall of 'compliant' pork to serve the state's consumers. Retail grocers and food service outlets scrambled to fill the void with beef and poultry.

Increased competition for fewer cattle will be the rule for a while as the national herd finds the cyclical trough. These Hereford and baldy feeders were selling at Mitchell Livestock Auction, Mitchell, S.D.

"We expect wholesale beef and fed cattle prices to overperform our previous expectations as California meat demand transitions and must compete with the rest of the market for beef supplies amid an already tightening supply situation," Weaber says.

At the same time Weaber points to growing demand for beef fat to use in producing renewable biodiesel. "If renewable diesel demand for fat continues, cattle will have more value, and we will have another product to sell at or above the cost of gain," Weaber says.

Katelyn McCullock, Livestock Marketing Information Center director and senior economist, expects cattle prices to approach where they were during the previous cyclical summit in 2014. She notes peak prices last time only lasted for about a quarter; high prices for about two years.

"I wouldn't be surprised to see a pattern similar to last time, and it could be longer this time because of the number of heifers in the feedlot," McCullock says.

At the same time, McCullock explains, "We will continue to be concerned about demand destruction. Everything is so much more expensive today. You have to wonder when consumers will show more price fatigue."

Given the likely extended horizon for herd rebuilding, Weaber believes expansion could occur at a more manageable pace than the last time, without the steep short-lived price spike followed by a hard fall. Instead, prices could remain elevated for longer.

Expansion road bumps

"This kind of price activity is expected to further drive expansion plans at many cow-calf operations and create even tighter feeder cattle and calf supplies," according to Weaber. "We expect feeder cattle and calf supplies outside of feedyards to be down 5% to 7% during the second half of 2023. The reduction is a function of 4% fewer beef cows calving and 5% fewer beef replacement heifers expected to calve in 2023 combined with accelerating beef replacement heifer calf retention at the ranch level."

Even so, key factors in the current market are starkly different than conditions in the 2014-15 time period that so many want to equate to currently reality.

McCullock explains the U.S. economy was emerging from a soft, shallow recession (2011). The domestic economy was expanding as herd rebuilding began, interest rates remained historically low and there was little inflationary impact. The opposite is true for all of those today.

Start with interest rates. The prime rate was 3.25% in the heart of 2014 when expansion began last time, according to Zimmerman. Today, it is 8.25%. In broad terms, he says the 5% increase in interest rates equates to about $500-$550 more interest rate expense in a bred heifer purchased today than about a decade ago (see Replacements — How High is Too High?).

"We need to ask ourselves how a higher interest rate affects not only expansion but how it affects the attitude toward taking risk, be it retaining cattle through the feedlot or building and remodeling facilities," Zimmerman says.

Speaking of which, some producers are nearing retirement; others of a certain age could view the high-price environment as an historical opportunity to exit the business.

"Everyone wants to know when the peak prices will come. It's more important, to me, to know when prices will stop increasing."

— Katelyn McCullock, Livestock Marketing Information Center

Thinking about cattle businesses ceasing or changing generational hands, Zimmerman says, "It's also the transfer of knowledge and networks." He encourages younger producers to consider intentionally seeking out those who have been successful over a lifetime and seeking their knowledge.

Weaber expects the industry to rebuild beef production during the coming expansion phase, but likely with fewer cows. That's possible due to the average annual growth in carcass weights that has occurred for decades and shows no signs of slowing. Markets continue to incentivize heavier carcasses, while technology and management prowess provide the means.

However, while still too early to know, Zimmerman says consumer beef demand the past couple of years, and so far in 2023, sets the stage to begin considering if an overall demand shift is occurring. In other words, could the efforts by producers and the collective industry across decades have pushed the demand curve forward in such a way that some of the old rules no longer apply or apply differently? For instance, as McCullock mentioned above, many economists continue to expect consumers to trade down within their beef purchases or substitute more lower-priced competing proteins. That has occurred historically, but not this time, so far.

"If demand has truly shifted, are we at a time where we can support more beef operations?" Zimmerman wonders.

Navigating the road ahead

"Everyone wants to know when the peak prices will come. It's more important, to me, to know when prices will stop increasing," McCullock says.

Part of that has do with higher input costs today and likely narrower margins compared to a decade ago. Plus, McCullock notes, "The last five years have shown us there are a lot of shocks we can't anticipate."

"We are operating in an environment that is increasingly more volatile than ever before, from moonshot rallies to drought," Zimmerman says. "We have to be more agile. We need a business plan, but we also need to invest in things that give us the opportunity to pivot. If we over-commit to a single plan it could sink us."

Likewise, McCullock encourages producers to identify ways of increasing operational flexibility, be it figuring out ways to cut hay cost or increase marketing options.

"You need to be a low-cost producer all of the time. Once those pennies get away, they don't come back," Weaber says. **B***A*