International Agri Insights with Prof. Bill Bailey

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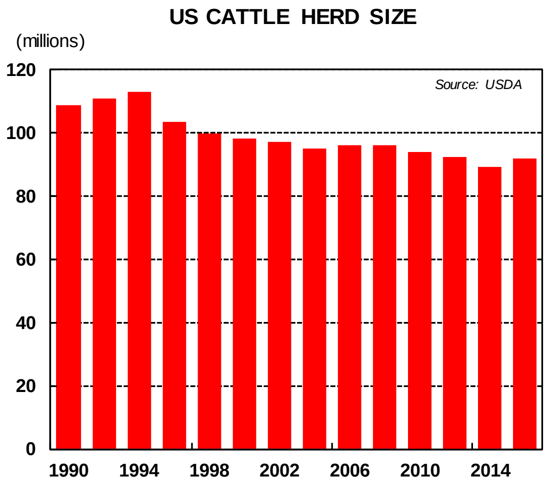
US Beef Market: All good things come to an end

- **The US beef herd, after shrinking to near a record low size, has started to get bigger again.**
- **As the US herd grows over the next five years, beef prices will decline, exports increase and imports drop.**
- **Lower prices should lead to higher US per capita beef consumption, particularly for more expensive cuts.**
- **The herd will increase in size, assuming normal weather, until 2020, and then start to shrink.**

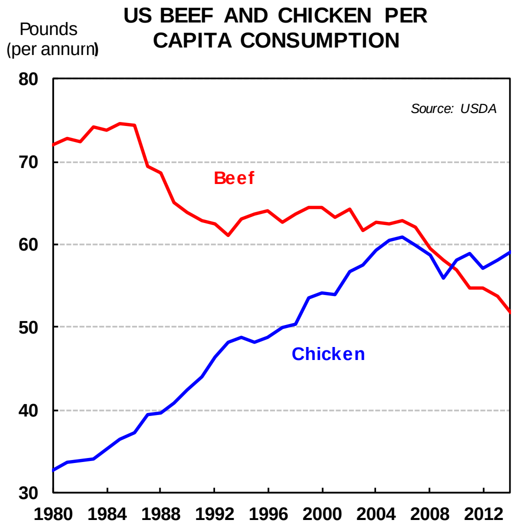
Introduction

The United States has the world's largest fed-cattle industry in the world and is the world's largest producer of beef. Although it is the world's 4th leading beef exporter (New Zealand is right behind at 5th), it is also the world's largest beef importer. The key factor in this rather ironic situation is the type of beef that changes hands – the US produces and exports high quality grain fed beef while importing lower value beef destined for food chains or further processing.



Cattle Cycle – Increasing the size of the US herd

Beginning in 1994, the size of the US beef herd slowly declined. An attempt to increase the size of the herd in 2004 was unsuccessful because hot and dry conditions in the southwest combined, with high corn prices in late 2006, limited herd growth. In contrast, today, most pastures around the US are in good shape and corn prices have declined nearly 50% from levels seen in 2006. The consequence of these positive feeding conditions, when combined with record high beef prices, is that potential exists for the sector to experience the largest increase in the US beef herd for at least 25 years.



Unlike some industries, cattle producers are unable to instantly respond to either high or low prices. The biological constraints involved in growing the size of the US herd means about 5 years are required to initially grow the herd. As the herd grows in size, eventually prices will decline sufficiently to create an environment that encourages herd reduction. But things can get in the way of these changes, as was seen in 2012 when high feed prices, plus drought, kept the herd from growing. This time around, the US herd showed its first intent to respond to high prices when, in 2015, the US herd grew 3% from 2014 levels. Assuming continued low grain prices and normal weather, the US herd should grow until 2020 and then, following the traditional cattle cycle pattern, start to shrink.

US Beef Consumption

US per capita consumption of beef has been in a steady decline since 1985. That decline has taken place despite growth in the fast food industry, an important source of beef to a significant part of the US population.

Benefiting from this decline in the demand for beef is the poultry industry, which, since 1980, has experienced a 40% growth in per capita consumption compared to beef's 30% decline. One reason for the decline in US beef consumption was its high cost compared to poultry. Over the past 3 years, beef prices increased from twice the price, per pound, of poultry to currently three times more expensive than poultry. Last June, retail beef prices hit an all-time high, with that record high coming in just before major summer holidays.

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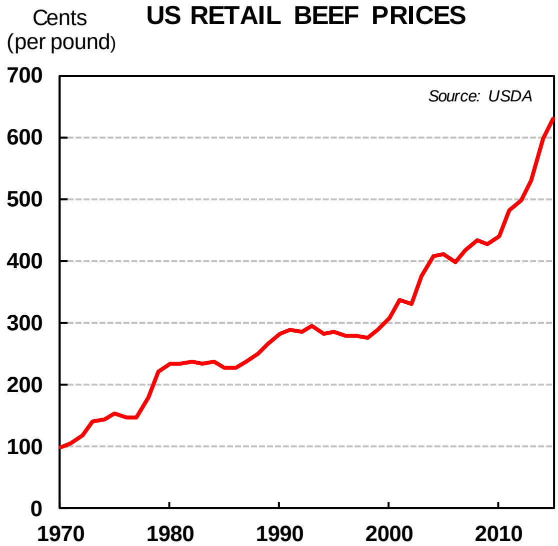
Consumers responded to the high prices by purchasing less beef last summer than the previous summer. As the cattle herd increases in size, retail beef prices will decline. It is expected the price decline will do two things:

1. Encourage increased consumption by those consumers who kept beef in their diet rather than shifting to pork and poultry; and
2. Lure those consumers back who had turned to poultry and pork because of the high price of beef.

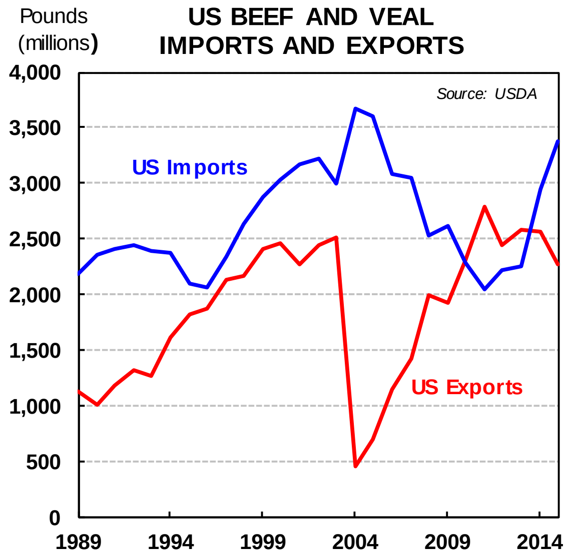
It is expected that the increase in consumption will focus on higher quality cuts of beef rather than less expensive, and often imported, processed beef and hamburger. With 2015 per capita consumption slightly higher than 2014, an increase in consumption in 2016 could mean beef consumption increased in the US for two consecutive years – the first time this has happened since 1998 and 1999.



Exports and Imports

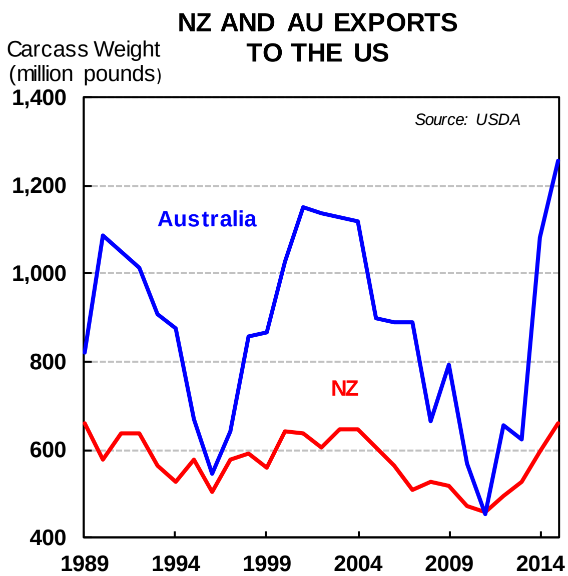
In 2015, US beef exports declined 12% from 2014 levels. The export decline was broad based, affecting all major trade partners other than South Korea.

The two major factors slowing US beef exports were the strong US dollar and the high domestic prices exporters needed to bid against to secure product. While important, but not as significant of a constraint as a strong dollar and high domestic prices, increased competition from Australian and New Zealand beef suppliers also slowed US exports.



While 2015 was not the best year for US beef exporters, 2016 will be much better – world beef demand is expected to strengthen and, with higher US beef production resulting in lower prices, beef exports are expected to increase almost 10% from 2015 levels. However, the strong US dollar will remain an <u>export</u> constraint during 2016.

While the US Department of Agriculture (USDA) sees stronger US beef exports in 2016, the beef import picture is the reverse. That said, the strong, and potentially even stronger, US dollar will lower the price of US beef imports, tempering the pace and or magnitude of any import decline. While US beef exports declined in 2015, beef imports increased almost 15% from 2014 levels. Good demand for lower value beef and available supplies from both Australia and New Zealand, when coupled with a strong US dollar, resulted in a 16% increase from 2014 levels of Australian beef entering the US with New Zealand origin beef imports up 11%. 2015 US imports from those countries reached their highest level since at least 1989.



The USDA forecasts 2016 total US beef imports to drop 16% from 2015 levels and sink to their lowest level since 2005. With less domestic demand for imported beef and new players such as Brazil and Uruguay entering the picture, the US imported beef market will become quite competitive during the next 3-4 years. All up, this signals lower beef export prices for New Zealand beef producers over the next several years, as the US cattle cycle runs its course.

About the author:

William C Bailey was Chair of Agribusiness at Massey University for 13 years. He has written weekly world dairy market columns for ASB Bank for almost 15 years. He currently is Dean, College of Business and Technology, at Western Illinois University, in Macomb, Illinois. Bill spent 5 years in the US Marine Corps and received his PhD in Agricultural Economics from the University of Missouri. Before shifting to New Zealand, Bill was Chief Economist for the US Senate Committee on Agriculture, Nutrition and Forestry, served as Deputy Undersecretary of Agriculture and was Vice President and Director of Research for World Perspectives in Washington, DC. His beer of choice is Tui.

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