August 2012 Cattle Report

Drought and the Cattle Industry

The beef industry has already experienced a number of difficult years characterized by falling cow numbers and declining per capita beef supplies. There was hope in the first-half of this year that this downward production phase was coming to an end. But the drought of 2012 has erased those hopes. So, where is the cattle industry today, and what do we know about the impacts of this year's drought?

The mid-year *Cattle* inventory report from USDA indicated that beef cow numbers had dropped by an additional three percent over the past year. Since 2006, beef cow numbers have dropped by eight percent due to much higher feed prices and to the long drought in the Southern Plains. The 2012 calf crop is expected to be down about two percent, and also down eight percent from 2006. This year's drought likely means further decreases in cow numbers over the next 12-14 months.

The impacts of the drought are just beginning to show up in some of the national data, but we do know the direction, but not the final magnitude of those impacts. The cattle industry is negatively affected by feed costs and lack of availability of forages. Higher corn and soybean meal price have dropped the value of calves and feeder cattle that will eventually go to the feedlots. Lack of pasture is also causing some early movement of cattle.

Since feed prices started rising in mid-June, corn prices have increased around 60 percent and soybean meal 25 percent. Forage conditions have been horrible across the Midwest. At the end of July pastures that were in "very-poor" and "poor" condition totaled from 82 percent to 98 percent for the states of Indiana, Illinois, Arkansas, Missouri, Iowa, Kansas, Nebraska, and Colorado (USDA:NASS). There have been many reports of producers forced to feed hay that was intended for this winter's forage supply. Those producers are hoping for late-summer rain that may restore some pasture this fall. If that does not come, then a deeper liquidation of cows can be expected.

In the wake of high feed prices and uncertainty regarding forage availability, calf and feeder cattle prices plummeted. Oklahoma steer calf prices in mid-June were $173 per hundredweight and collapsed to $138 by late July. How much loss of value is that? A $35 per hundredweight decline on a 550 pound calf is nearly $200 per head reduction in value. Multiplying that across a national calf crop of 34.5 million head totals a potential decline in value of over $6 billion. It is still too early to count the actual damages, but this illustration shows it is likely large.

Reduced value of calves and feed uncertainty will most likely result in further declines in cow numbers this fall and winter. National slaughter data so far during this drought indicate only modest increases in cow slaughter. However most Midwest producers have had hay to feed helping them to avoid panic liquidation. How the drought unfolds in coming months will influence how much cow liquidation occurs. More rain and thus grass will reduce liquidation. Continued drought will increase fall and winter cow culling.

The largest negative financial impacts of the drought will be felt by cow-calf producers and by feedlot managers who did not have feed prices locked in at lower spring levels. Assuming most large feedlots are primarily hedged on feed and feeding margins, this means that moderate and small sized family feedlots are the primary category that have suffered large losses. Some of those family farms may also have large losses from crops, especially if they did not have crop insurance, and thus could be in financial difficulty.

The message for cow-calf producers is to hold on to the cows if possible. The short-term losses of the next 12-14 months will be replaced by large profits in late-2013, 2014, and 2015. These anticipated "golden" days are based on continued reductions in per capita beef supplies which will mean higher-and-higher retail beef prices; on a return to more normal crops in 2013 and beyond; and thus record high calf prices and profits in late-2013 and beyond. The problem for some producers in a weakened financial condition is that they have to survive the pain in the short-run to secure the prize in the long-run. The message for family feedlot managers is "risk management."

Any thoughts of industry-wide expansion are pushed off for another year to late-2013 when pastures are restored and feed prices drop. The exception are producers in areas of the country that have abundant forages. For them buying cows sold this fall from distressed owners appears to be a strategic move.

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