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Better Supply-Demand Balance Expected in 2004 Dairy Markets

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Overall, dairy markets are expected to be better balanced in 2004. Demand is projected to grow more than milk production, commercial stocks are expected to be smaller, and commercial exports of nonfat dry milk might substantially trim the recent surplus. However, this basic improvement might not generate higher farm milk prices. Much of the modest farm price recovery in 2003 was caused by a misalignment of cheese and other dairy product prices. Cheese buyers are likely to make quicker and more vigorous adjustments in 2004 that will prevent a repeat.

Beef markets continue the adjustment process as prices moved to record levels in 2003 to allocate a tightening supply of high quality beef. Beef production was down 12 to 16 percent from a year earlier in October/November as fed cattle marketing dates could not be moved forward anymore to sustain the strong demand for higher quality beef. Although cattle and boxed beef prices have declined from the record peaks of early fall, prices remain well above a year earlier. Retail prices continue to rise as the retail and hotel/restaurant sectors have absorbed a formidable share of the price increase since mid-summer, and pass the higher prices on to consumers.

Fourth-quarter prices of live-equivalent 51-52 percent lean hogs are expected to range between $37 and $38 per hundredweight (cwt), almost 20 percent higher than a year ago. A continuation of weekly hog slaughters of 2.1 million head since the first week of October will bring fourth-quarter slaughter to only slightly below 1998, when hog prices collapsed. With an expected slaughter of about 27.4 million head, and dressed weights of 199 pounds, fourth-quarter pork production could be record-high at about 5.45 million pounds, 3 percent greater than last year and 4 percent more than in 1998. Retail pork prices are expected to finish 2003 averaging in the mid-$2.60s per pound. Retail prices in 2004 will likely average 1 percent higher. Through October, pork exports ran more than 6-percent above last year. Japan, Mexico, Canada, and smaller Asian countries were the primary destinations for U.S. pork products. The United States imported 14 percent more pork products, primarily from Canada and Denmark. The U.S. Department Agriculture (USDA) issues the *Quarterly Hogs and Pigs* report on December 30th.

Fourth-quarter federally inspected broiler slaughter is forecast at 8.2 billion pounds, an increase of 3 percent from the same period last year. Increased fourth-quarter production is expected to come from gains in the number of birds slaughtered and higher average weights. U.S. broiler exports for the third quarter of 2003 were 1.2 billion pounds, down 2 percent from the previous year. This, coupled with a lower forecast for fourth-quarter exports, lowers the estimate for 2003 to 4.8 billion pounds, about even with 2002.

The wholesale N.Y. price of grade A large eggs is expected to average more than $0.88 per dozen for 2003, an increase of almost 32-percent over last year. Prices in the fourth quarter are expected to average almost $1.13 per dozen, 49-percent above last year. Higher prices are attributable to both demand and supply factors: strong seasonal demand and higher prices for substitute animal proteins on the demand side; and, slightly lower production from disease problems and compliance with animal welfare restrictions on the supply side. Production is expected to increase about 1 percent next year, but strong consumer demand will keep the average wholesale price for the year more than 3-percent above 2003.

Choice lamb prices at San Angelo, Texas are expected to average around $92 per cwt in 2003, 27 percent above last year. The sharp boost in lamb prices this year is due to an expected 9-percent decline in lamb and mutton production and a 2-percent drop in imports. A continuing decline in production and only a slight increase in imports will likely keep average lamb prices in the low $90s in 2004.

Dairy

Low Milk Prices May Persist in 2004

Strong orders for the late holiday season and declining commercial stocks brought some stability to cheese prices following their late October-early November drops and lifted butter prices to their high for the year. However, this modest price strength probably will be overwhelmed by normal seasonal weakening in coming weeks.

Overall, dairy markets are expected to be better balanced in 2004. Demand is projected to grow more than milk production, commercial stocks are expected to be smaller, and commercial exports of nonfat dry milk might substantially trim the recent surplus. However, this basic improvement might not generate higher farm milk prices next year. Much of this year's modest farm price recovery was caused by a misalignment of cheese prices with other dairy prices. Cheese buyers are likely to make quicker and more vigorous adjustments in 2004 that will prevent a repeat.

Milk Production About Steady

Milk production remained just slightly below a year earlier in early autumn, as declines in milk cow numbers picked up and milk per cow failed to sustain its recovery. Output has been near or below a year earlier since May because of very low returns since early 2002. Even so, milk production has not yet shown signs of a significant downturn and is expected to stay relatively close to a year earlier through 2004.

Milk cow numbers turned down fairly sharply late summer. After peaking in late winter, cow numbers slipped during spring. Farm expansions had been deterred by the low returns, and most of the earlier expansions had been brought up to capacity. Even though milk prices rose as summer began, the long period of low prices began to take its toll on weaker producers. Farm exits picked up in earnest at the start of autumn, probably when leftover 2002 forage supplies were exhausted. Between March and October, milk cows in the 20 major States fell 91,000 (1.2 percent). The proportional decline for all 50 States was probably even larger.

The August-October drop may prove particularly significant. Normally, a disproportionate share of expansions are brought on line in September and October. This results in relatively strong August-October cow numbers. This year's decline was affected by cooperative actions to trim cow numbers but also might indicate that the expansion phase caused by the high returns of 1998-2001 is truly over.

Although recent changes in cow numbers were dominated by structural effects, high slaughter cow prices probably also contributed. As cull cow prices shot over $50 per cwt, the difference between dairy and salvage value fell to its lowest level in 5 years. A larger share of the cows in exiting herds probably went to slaughter rather than being sold as replacements.

Growth in milk per cow in the 20 States hit a low in May, recovered a bit through July, but then backslid through October. The October level was less than 1 percent higher than a year earlier, and the increase from the average of the previous 5 years was at only about a 1-percent annual rate, half the trend growth. Milk-feed ratios have been quite unfavorable, encouraging dairy farmers to be conservative about increasing concentrate feeding. In addition, forage quality in 2003 was spotty, with quality problems particularly pronounced early in the season.

Feed conditions could not explain all of the recent weakness in milk per cow. Average milk per cow probably did not receive its normal boost from the exit of farms with relatively low herd averages. In addition, the cow herd probably had an unusually large share of first-calf heifers because of the 2002 heifer shortage. However, it also seems likely that the very low milk prices may have caused some farms to limit use of bovine somatotropin or to feed their poor forage instead of seeking better supplies.

The pattern of widely divergent changes in milk production across States remains. In general, output in recent months was stronger in the West than in the Midwest, which in turn was stronger than the Northeast. However, exceptions to this general pattern were quite easy to find.

Milk cow numbers are expected to decline at a fairly rapid clip through 2004. The recent higher prices probably were perceived as temporary and are not projected to have a significant impact on farmers' long-run plans. Dairy farm exits probably will be more common than in several years, and farm expansions likely will be fewer and cautious. Also, cull cow prices are projected to stay strong as the beef industry seems poised to undergo a cyclical turn. Milk cow numbers are expected to run 1 to 2 percent below 2003 throughout next year.

Milk per cow probably will remain relatively weak in 2004 but could post some recovery from this year's poor showing. Concentrate feed prices are projected to remain high next year, holding milk-feed price ratios to very low levels. Feed grain prices might run about the same as this year, but protein will be expensive. Farmers probably will stay conservative about boosting concentrate feeding, particularly compensating for poor forage with extra protein meal.

Forage conditions remain a mixed bag in most important dairy areas. Dairy farmers commonly had quality (and quantity in some areas) problems for part of the forage season. Commercial hay supplies seem ample, but good quality can be hard to find. Forage quality may continue to threaten milk per cow, particularly if low milk prices deter farmers from seeking out good hay.

On the other hand, weakness in milk per cow due to the 2002 heifer shortage should become a thing of the past. In fact, passage of this year's large heifer cohort into their second lactation should be positive for gains in milk per cow. Daily average milk per cow is projected to rise slightly more than 2 percent in 2004, just slightly recovering toward the long-run trend line.

Milk production throughout 2004 is expected to run a bit less than 1 percent above 2003 (on a daily average basis). Such stability in milk output would tend to temper milk and dairy product prices next year. However, there might be higher odds for milk production to be weaker than now expected than for it to be stronger.

Lower milk production during September-October slightly reduced supplies of milk for manufacturing. The reduction in supplies was not enough to keep strong cheese prices from boosting cheese production, particularly in September. However, Cheddar output in September-October managed only a tiny increase, and growth in production of most other varieties stayed moderate. Meanwhile, production of butter and nonfat dry milk fell.

Supplies of milk for manufacturing are projected to be slightly larger than a year earlier during the first half of 2004. Cheese output is expected to rise while butter production stays near a year earlier. However, production patterns will be quite sensitive to developments in butter and cheese demand and to possible commercial exports of nonfat dry milk.

Butter Stocks Finally Moderate

The dairy industry's long ordeal with huge butter stocks may be coming to an end. Holdings on October 1 and on November 1 were below a year earlier for the first times since 2001. In addition, fairly good holiday season movement reportedly is helping to trim stocks further. However, butter holdings still are quite large and may remain a problem. The biggest contributor to reduced inventories was the large drops in production while milk was being diverted into cheese production, an adjustment that is unlikely to continue. Unless sales have picked up briskly, butter stocks may continue to weaken prices through winter.

Commercial cheese stocks have remained moderate. On November 1, holdings of American varieties were down slightly from a year earlier, while stocks of other types were slightly higher. Although pipeline cheese stocks might have built between late spring and early autumn, cheese did not significantly back up in warehouses. Manufacturers' stocks of nonfat dry milk on November 1 were similar to the modest holdings of a year earlier.

In total, commercial stocks on November 1 were equivalent to 9.6 billion pounds of milk on a milkfat basis, slightly less than a year earlier but more than 1 billion pounds above 2 years ago. On the other hand, stocks of skim solids were very close to both of the preceding years. If growth in butter stocks can be held to modest levels through the end of winter, commercial stocks should cease to have important price effects.

Recovery in Dairy Demand Ragged

Brisk growth in the economy during spring and summer has not yet translated into sustained recovery in dairy product demand. Despite generally modest prices, commercial use of milkfat rose only fractionally during August-October while sales of skim solids slid more than 1 percent from a year earlier. Use in 2003 probably was stronger than these comparisons imply, since 2002 movement was brisk during these months before faltering considerably in the last months of the year. In contrast, 2003 use probably has grown throughout the holiday season, and cheese buyers may have restrained purchases during August-October in anticipation of price declines.

This year's holiday season use appears to have developed considerable late strength. If so, this would be the first year in several to have fair strength at both ends of the holiday season. The restaurant business reportedly finally started to recover, helping sales of both cheese and butter. Thanksgiving retail butter sales evidently were brisk, leading to sizable post-holiday orders. Retail sales of natural cheeses reportedly also were good. Information on ingredient use of milkfat and skim solids is scanty, but there were indications that the holiday production season was extended due to better-than-expected orders.

Dairy demand in 2004 may move out of its 2-year stagnation. The economy is projected to grow at a fairly good clip, the employment picture is improving, and consumers seem to be returning to more typical spending patterns. Relatively low prices of dairy products should spur some additional use. Commercial use of milkfat and skim solids is projected to expand substantially next year. However, dairy demand is not likely to match the extraordinary strength of the 1999-2001 period.

The surplus removed under the price support program was fairly modest in recent months. Net removals during September-November were only 0.1 billion pounds, milk equivalent, milkfat basis and about 0.6 billion pounds on a skim solids basis. Small exports under the Dairy Export Incentive Program (DEIP) made up all the removals of butter and cheese.

DEIP removals of nonfat dry milk during September-November were similar to those of a year earlier. Purchases also ran close to year-earlier levels but the level of purchases was somewhat misleading. A significant share of this year's purchases was fresh powder displaced by older products from Government stocks that had been swapped for pudding and processed cheese for use in domestic donation programs. Taking this into account, net removals of nonfat dry milk fell by almost half during September-November. Even if the full displacement of fresh powder did not occur by the end of November, the surplus of nonfat dry milk definitely has begun to wane.

The 2004 surplus of milkfat is projected to be quite small. Increases in use are expected to surpass growth in milkfat production, creating somewhat tight milkfat markets. On the other hand, the surplus of skim solids will stay large. Ingredient use of skim solids has not yet responded very much to the sharply lower powder prices. However, economic growth should spur some ingredient use, particularly for upscale versions of some foods. The skim solids surplus is projected to decline next year to a level well below those of most recent years.

International Prices Rise

International market prices for dairy products have risen because of continued tightening of market conditions and a weaker U.S. dollar. In early December, butter prices were up about $200 per ton from early summer and about $300 from a year earlier. Similarly, skim milk powder prices had risen about $150 and $400, respectively. Prices for whole milk powder rose the most, with early December prices about $300 per ton above those of early summer and about $450 above a year earlier.

Import demand has generally strengthened. Economic growth has boosted demand by some important buyers, conditions are somewhat more settled in the Middle East, and demand has picked up seasonally in the Northern Hemisphere. Milk powders have seen the most improvement.

Although Russia has increased butter imports and some recovery may be occurring in the Middle East-North Africa, butter demand remains a bit sluggish.

Early-season supplies from Oceania have been fairly limited. Australian milk output continues to suffer ill effects from last season's drought. New Zealand expects a small increase in milk production this season, but rainy conditions cut early production in some areas, and stocks probably were tight at the start of the season. Reportedly, little beyond preseason commitments was available from these countries until quite recently.

Supplies from the European Union (EU) also have been a little tight. Fairly brisk internal demand has absorbed most of the seasonally reduced supplies. Domestic market tightness has limited the EU export subsidy response to the rising value of the euro.

International market prices might slip slightly in early 2004. Production prospects for the second half of the Oceania season are favorable, and Northern Hemisphere demand will be seasonally softer. In addition, U.S. supplies of skim milk powder are quite competitive at current exchange rates, and large U.S. supplies may trim international prices. However, EU supplies may not become heavy until at least later in the year, and the improvement in international demand is expected to continue. Price decreases are expected to be modest.

U.S. imports of dairy products ran somewhat smaller than a year earlier during spring and summer. Smaller imports of American cheese in excess of the tariff-rate-quotas (TRQ) provided the bulk of the decrease, as most major product imports were similar to a year earlier. The high-tariff cheese imports in 2002 probably had not been profitable in the short run, and much tighter Oceanic supplies deterred shipments this year. In addition, the gaps between international and domestic prices have steadily narrowed as 2003 has progressed, particularly for products utilizing skim solids.

Imports during the last quarter of 2003 may stay below a year earlier because of relative small expected price differences. However, the declines are not expected to be sizable. Most imported products are marketed under a long-run strategy that is fairly insensitive to modest short-run swings in profitability. In addition, gradually improving cheese demand might boost imports of relatively expensive cheeses.

Dairy exports thus far in 2003 have been mixed. Nonfat dry milk exports were considerably larger than during January-September 2002. Exports under the DEIP were slightly smaller but commercial exports rose. U.S. prices have been relatively competitive during most of the year. Butter exports rose because of the use of DEIP for milkfat this year. On the other hand, cheese exports slipped in spite of slightly larger DEIP exports.

Nonfat dry milk exports could become large this winter if the recent weakness of the U.S. dollar persists. Recent strength in powder prices may ease, but a weak dollar probably would keep the U.S. competitive in at least some important markets. In addition, ample supplies ready for export are assured—something that is not true for the EU and Oceania until at least later in 2004.

Butter and Cheese Price Strength Likely Temporary

Exchange prices of cheese have pretty much stabilized following the late October-early November drops. The adjustments were triggered by increasing cheese production, the easing of concerns about sharp declines in milk production, and the lack of aggressive growth in cheese use. The decreases were then stemmed by the strength of late-season cheese movement, at least for natural cheese. Similarly, brisk butter sales, continued declines in production, and falling stocks brought butter prices generally higher through November, reaching the highest levels of the year in mid-December.

Recent price strength is unlikely to last longer than the holiday season. With milk production expected to be near or slightly above a year earlier, ample products should be available to meet seasonally low winter needs, even if demand continues to recover. However, cheese and butter prices are projected to run above those of the first half of

2003. Growth in demand is expected to exceed increases in production, and commercial stocks likely will be smaller.

Nonfat dry milk prices are expected to stay near the support purchase price during the first half of 2004 under the pressure of a sizable continuing surplus. If vigorous export demand develops, price prospects could change for powder, particularly if export sales coincide with recovery in domestic ingredient use.

Second-half price prospects are uncertain. Supply-demand conditions, in most ways, probably will be somewhat tighter than during 2003. Prices of many products are projected to run somewhat above a year earlier. However, cheese prices may well be a key exception. In 2003, cheese buyers generally did not attempt to protect themselves against price rises until it was too late in the season to have much effect. More aggressive building of pipeline stocks during the spring of 2004 probably will forestall a repeat of the 2003 price pattern.

With 2003 farm milk prices staying well above a year earlier through yearend, farmers will receive an average of about $12.60 for 100 pounds of milk, 50 cents more than they did in 2002. Although price recovery was quite modest, it did help improve dairy farm returns a bit from the very low 2002 level.

Farm milk prices are expected to average above a year earlier during the first half of 2004. The current market balance probably will be somewhat tighter, commercial stocks will be lower, and the skim solids surplus is projected to be less. In addition, larger quantities will go into pipeline holdings to meet second-half needs. However, second-half milk prices are expected to fall short of this year's. Precautions taken during the first half are expected to prevent a large gap in the value of milk for cheese and for butter-powder.

The average price of all milk in 2004 is projected to slip slightly. In general, market fundamentals, although healthier than during the preceding 2 years, are not expected to have adjusted enough to end the recent period of weak dairy prices. However, the odds of weaker-than-expected production (or stronger-than-expected demand) triggering substantial advances across the spectrum of product prices probably are higher than since 2001.

Retail dairy prices during October-November were up about 3 percent from a year earlier, about the same rise as for all food prices. The early autumn farm-to-retail price spread was considerably lower than a year earlier as increases in retail dairy prices failed to keep pace with rises in farm milk prices. Fluid milk price increases were the sharpest among dairy products in early autumn.

For all of 2003, retail dairy prices are projected to be about unchanged, with the higher farm prices absorbed by a lower spread. The farm-to-retail spread is expected to recover in 2004, pushing retail prices up 3 to 4 percent. Even so, dairy prices will have risen at an annual rate of only about 1 percent during 2001-04.

Boxed Beef/Cattle Prices Moderate as Markets Adjust to Tight Beef Supplies

Beef demand continued strong into 2003, particularly for higher quality fed beef. However, the beef sector has been forced to make adjustments throughout 2003. During winter through mid-spring adjustments stemmed from poor feeding conditions resulting in light slaughter weights and very tight supplies of higher quality beef. Although retail prices began a record path in February, fed and feeder cattle prices rose but remained below record levels. Discovery of bovine spongiform encephalopathy (BSE) in a single cow in Canada on May 20 resulted in a ban on imports of live ruminants (cattle, sheep, goats, deer, and elk) and ruminant products and byproducts from Canada. This tightened supplies even more and the industry reacted by marketing cattle out of feedlots ahead of schedule and, aided by large feedlot profits and dry conditions, placing more cattle on feed. Consequently, third-quarter steer and heifer slaughter rose 2.5 percent, but beef production was slightly below a year ago, due to sharply lower steer and heifer dressed slaughter weights. Production would have been lower but cow slaughter rose 5 percent due to drought and poor grazing conditions in many areas.

A sharp turn of events occurred in September, October, and November. Steer and heifer dressed slaughter weights were averaging over 30 pounds lower than a year ago, resulting in even tighter higher quality beef supplies. Three factors began to come together this fall to limit climbing fed beef prices from rising even more on tightening higher quality beef supplies. First, the movement to a record monthly price of $176.06, up 51 percent from a year earlier, for light Choice boxed beef in November resulted as supplies declined. This forced some end users to switch to other products. Second, there was some improvement in slaughter weights as weekly slaughter levels dropped from third-quarter and year-earlier levels as days on feed increased. Typically steer and heifer slaughter weights peak in October-November, but this year weights have been steady to declining since August. Third, on August 8, boneless beef from cattle under 30 months of age was allowed to re-enter the U.S. market from Canada. After several weeks of adjustments to the new permit system, imports from Canada have been increasing. This combination of events, although taking some bloom off cattle/boxed beef prices, may help the industry preserve market share gained through the very strong consumer and export market that has evolved over the past few years. However, cyclical meat market share lost through tight supplies and high prices, typically is expensive to regain as cattle inventories and beef supplies expand. Supplies will tighten from present levels over the next couple of years as female stock are retained, but likely in mid-2006 beef supplies will again begin to rise with market share having to be regained.

Feedlots in December are less current and slaughter weights are likely to pick up from the summer lows. Boxed beef prices have declined from the mid-October peak near $194 a cwt to $155 to $160 a cwt in mid-December. Retail prices continue to rise, a situation likely to continue through early winter, as the live/wholesale/retail price spreads readjust to the rapid supply/price changes of 2003. The November retail price for Choice beef rose sharply averaging a record $4.32 a pound, up 10 percent from last month's record, and up 29 percent from a year earlier. The retail and hotel/restaurant sectors absorbed a formidable share of the price increase through October with the wholesale to retail spread falling from $1.63 in July to $1.22 in October before a rapid pass through in November. The November wholesale to retail spread rose to $1.74 a pound. Although fed cattle and boxed beef prices are off their highs, they remain well above any previous highs and will remain in these ranges for the next couple of years as supplies tighten further. December averages are likely to remain 25 to 30 percent above a year earlier.

The beef complex will be challenged over the next couple of years to maintain supplies for the various sectors of the domestic and export market. Market share will be lost to pork and poultry as the next expansion phase of the cattle cycle begins and more cows and heifers are retained. The more the industry can moderate the adjustments to declining higher quality beef supplies over the next couple of years, the less downward price adjustment will be needed to buy back market share.

Record Beef Prices Support Pork Sector Above Year-Earlier Levels

Fourth-quarter prices of live equivalent 51-52 percent lean hogs are expected to average $37-$38 per cwt, almost 20 percent higher than a year ago. Weekly hog slaughter since the first week of October has been a consistent 2.1 million heads or above, with the exception of holiday weeks. Given this weekly slaughter pattern, fourth-quarter hog slaughter will fall only slightly below 1998 when fourth-quarter hog prices were $22 per cwt. With an expected slaughter of about 27.4 million head, and dressed weights of 199 pounds, fourth-quarter pork production will be record high at about 5.45 million pounds, nearly 4-percent greater than last year, and 4 percent more than in 1998. If current price and production expectations are met, the market will be faced with higher hog prices and record-high pork production, a situation at odds with all those Economics 101 scenarios where prices are low when production is high.

It appears that the dynamics of another variable--Choice beef prices--explain higher hog prices at the same time that the industry is producing record quantities of pork products. Record-high cattle and beef prices have probably fostered a shift by consumers toward relatively lower-priced pork products. The shift in demand toward pork is signaled by the higher wholesale carcass cutout value, which averaged $58.08 during October-November, almost 8 percent higher than in the same period last year. The higher cutout provides an incentive for packers to pay higher prices for hogs while, at the same time, enabling them to maintain positive slaughter margins.

Stronger Retail Pork Prices Expected

Strong consumer demand for pork is expected to send fourth-quarter retail prices about 4 percent above same-period prices a year ago. Fourth-quarter retail pork prices typically drop below third-quarter prices. But this year the reverse is expected. Fourth-quarter prices are expected to be slightly higher than the third quarter price of $2.70 per pound. For 2003, retail prices are expected to average in the mid-$2.60-per-pound range, less than 1-percent above 2002. In 2004, with tight beef supplies continuing to drive pork demand, and slightly lower pork production, consumers can expect to pay about 1 percent more for pork than in 2003.

2003 Pork Exports Running Ahead of A Year Ago

In the first 10 months of 2003, U.S. processors exported 1.4 billion pounds of pork, more than 6-percent above the same period last year. As usual, the largest foreign markets for U.S. pork products this year have been Japan, accounting for 49-percent of exports, Mexico, accounting for 19-percent, and Canada, which has so far taken 11 percent of U.S. pork exports. Larger exports to smaller Asian countries--Korea, Taiwan, and Hong Kong--have compensated for slower shipments to Canada.

So far this year, Japan has imported 683 million pounds of American pork products, almost 6-percent more than in the same period last year. The increase has come despite Japan's imposition of the pork Safeguard on August 1. The Safeguard is a 25-percent increase in the minimum import price of pork, which is sanctioned by the World Trade Organization to protect Japanese pork producers from the price effects of import surges. The Safeguard has been imposed three times by the Japanese Government in the last three calendar years. It will be lifted April 1, 2004, the first day of the Japanese fiscal year.

With the Safeguard in place, Japan imports less pork. When Safeguard imposition appears imminent, Japanese traders import enormous quantities of frozen pork, accumulating huge stocks to supply domestic markets while the Safeguard is in place. Imports of frozen pork thus decline the most while the Safeguard is in place, and imports of fresh pork products take relatively less of a "hit". Consequently, Denmark, which for geographic/transport reasons can only export frozen pork to Asia, is affected by the Safeguard to a greater degree than the United States and Canada, whose exporters ship both fresh and frozen pork products.

Japanese import data indicate that U.S. pork has gained market share so far this year, at the expense of Canada and Denmark. Through August, the U.S. share of Japanese imports was 34-percent, a 6-percent increase from the same period in 2002. The market shares of both Canada and Denmark declined. Canada lost 5-percent, while Denmark lost 9-percent.

Japanese market share changes are likely due, in part, to relative exchange rate changes that have taken place this year. Since January, the U.S. dollar has depreciated against the Japanese yen by more than 8-percent, meaning (ceteris paribus) that U.S. products were 8-percent cheaper in November than at the beginning of the year.

Both the Canadian dollar and the Danish krone have appreciated against the yen since January, likely contributing to market share losses. In November, the Canadian dollar cost almost 8-percent more in terms of the yen than in January, and the Danish krone appreciated about 3-percent against the yen.

Exchange rate dynamics in 2003 have favored American pork products, making them cheaper to Japanese customers, while currency appreciation makes Danish and Canadian products more expensive. Favorable U.S. dollar-yen rates, and the U.S. ability to ship fresh pork products while the Japanese market is hindered by the Safeguard, are likely factors driving gains in the U.S. share of Japan's pork import market.

The current USDA forecast has Japan importing about 1 percent fewer pork products in 2003 than last year. In 2004, Japan is expected to import the same quantity of pork as in 2003, with the U.S. market share gains likely to continue.

U.S. pork exports to Mexico through October show a gain of almost 3 percent over a year ago. Mexico imported 266 million pounds of U.S. pork in the first 10 months of 2003 and remains the second most important market for exported U.S. pork, accounting for 19 percent. Through September, Mexican imports were running behind last year, which was not unexpected given the sensitivity of Mexican consumers' pork demand to macroeconomic activity, and the lackluster performance of the North American economy for most of this year. Recently however, economic activity accelerated, incomes improved, and demand for U.S. pork products pushed above year-ago levels. With the Mexican economy expected to grow at a rate of 3.6 percent in 2004, continued growth of demand for U.S. pork products is expected. The current USDA forecast has Mexican pork imports increasing almost 3 percent next year.

Canadian imports of U.S. pork products through October have declined more than 4-percent over a year ago. Canada remains the third most important export market for U.S. pork products, accounting for 11 percent of U.S. exports so far this year. One explanation for the lower Canadian demand--despite the lower valued U.S. dollar--is the loss of competitiveness of Canadian pork on international markets due to the appreciation of the Canadian dollar. A loss of competitiveness abroad increases the likelihood that more Canadian pork products are being marketed domestically, perhaps "crowding-out" U.S. pork. In 2004, Canadian demand for U.S. pork products is expected to stabilize and to recover somewhat. USDA forecasts a 4-percent increase in total Canadian pork imports next year.

U.S. exports to smaller Asian countries--South Korea, Hong Kong, and Taiwan--have increased almost 38-percent over the same period in 2002. Together these three countries account for almost 11-percent of U.S. pork exports, and more than compensate for export reductions to Canada. Moderate growth rates of these economies this year, together with the lower valued U.S. dollar, are the likely factors driving import demand for U.S. pork products. Current USDA forecasts have 2004 pork imports of the smaller Asian economies increasing by less than 1 percent.

Pork Imports Increase at 14 Percent Clip

The United States imported 813 million pounds of pork through October, an increase of 14-percent over last year. Canada continues to hold a share of the U.S. import market that ranges between 80 and 85 percent. Denmark accounts for between 10 and 14 percent, with the remainder going to the "Other" category, which includes products from Central and Eastern Europe and the European Union. Given the depreciation of the U.S. dollar against both Canadian and Danish currencies, the rate of U.S. pork import expansion is a bit surprising. But strong U.S. consumer demand for pork products and the sheer size of the U.S. market function as strong magnets for any country with pork to sell.

Live Hog Imports Accelerate

If current expectations are met, the United States will import almost 7.5 million head of Canadian hogs this year, 30 percent more than in 2002. Almost all import categories of hogs have increased, but in particular, slaughter hog imports have increased 18 percent, feeder pigs increased 24 percent, and sows/boars increased 33 percent. What are the major factors that have sent so many Canadian hogs to the United States? In a nutshell, U.S. hog finishers and packers are willing and able to pay more for hogs than Canadian finishers and packers. Low Canadian bids derive from weak slaughter margins that directly result from an appreciated Canadian dollar. The appreciated dollar has made Canadian pork more expensive and less competitive in foreign markets where it competes with lower priced pork from the United States and Denmark, in particular. For a country that exports almost half of its pork production, the appreciation of the "Loonie" (i.e., the Canadian dollar) in 2003 has had unambiguously negative consequences for the Canadian pork sector.

From a Canadian packer's perspective, the consequences of the high-priced Canadian dollar and lower export demand for Canadian pork products include--but are not limited to--low-to-negative slaughter margins, and reduced slaughter numbers. In fact, three small Canadian packers have declared bankruptcy this year: West Perth Packers, Brantford Packers in Ontario, and Les Viandes Abitemis in Québec. In addition, Springhill Packers recently re-opened with financial assistance from the Province of Manitoba after shutting down for a short period. Bruce Packers in Ontario has ceased operation, after being heavily damaged by fire in early November. Fewer packers mean less demand for slaughter hogs, and more slaughter hog exports to the United States. Moreover, fewer packers can also mean less competition for slaughter hogs, with remaining Canadian packers tending to bid less for hogs and driving more slaughter hogs south to the United States. Fourth-quarter slaughter for major hog producing provinces, through November, is 8-percent lower than a year ago in Manitoba, almost 4 percent lower in Ontario, and about even with last year in Québec. Fourth-quarter hog prices are more than 6-percent higher in Manitoba, 3-percent lower in Ontario, and almost 2-percent higher in Québec.

The Canadian breeding herd also appears to be responding to lower packer demand and lower returns on feeder pigs exported to the United States. Since August, weekly USDA data indicate that U.S. imports of Canadian sows and boars have increased almost 53 percent over the same period last year, suggesting at a minimum, that culling of the herd is taking place.

Poultry

U.S. Broiler Production Moving Higher

The estimate for broiler production in 2004 was increased by 160 million pounds to 33.6 billion pounds, as egg and chick placements have been running several percentage points above the previous year. The weekly *Broiler Hatchery* report continues to show increases in the numbers of broiler chicks being placed for growout. During the last 8 weeks (Oct. 18 through Dec. 6), the number of broiler chicks placed each week for growout has averaged 160 million, up 2.5 percent from the same period the previous year. The data for egg placed in incubators indicate that chick placements can be expected to continue to be above year-earlier levels as the number of eggs placed has been up by an average of 2 percent over the last 3 weeks.

U.S. broiler production in fourth-quarter 2003 is estimated at 8.2 billion pounds, about 3 percent higher than in fourth-quarter 2002. Broiler production in October was 3.04 billion pounds, an increase of 2.8 percent from a year earlier, and slaughter in November and December is expected to be higher than the previous year. This follows a third-quarter where production increased 2.5 percent compared with a year earlier. This gradual increase in production is expected to come from a slightly higher number of birds going to slaughter and continued growth in their average weights.

Broiler Stocks Down Sharply

With little or no growth in broiler production over the first half of 2003, stocks of broiler products held in cold storage have declined throughout the year. The estimate of cold storage holdings of broiler products at the end of October was 599.2 million pounds, down 30 percent from a year earlier and 5 percent lower than at the end of October 2001.

With lower stocks and only a small increase in production over the first 10 months of the year, domestic broiler prices have continued to strengthen. The November 12-city average for whole broilers was 64.5 cents a pound, up 21 percent from the previous year. Prices for most broiler parts have increased even faster. Prices for leg quarters were 29.6 cents per pound in November, up 64 percent from the previous year. Wing prices have risen 106 percent from the previous November to 94.13 cents per pound. Broiler prices are expected to remain strong over the next several months as a recovering economy, a brighter export outlook, and high prices in the beef and pork sectors combine to strengthen demand.

U.S. broiler exports in October 2003 were higher than expected at 553 million pounds, leaving exports for the first 10 months of the year at 4.1 billion pounds, 1 percent higher than in the same period in 2002. While domestic prices for bulk leg quarters in October were much stronger than the previous year, much of this strength is from domestic factors.

While overall exports have increased, shipments to the two largest markets are lower than the previous year. Over the first 10 months of 2002, broiler exports to Hong Kong have totaled only 257 million pounds, down more than 50 percent from the same period in the previous year. The decline in broiler exports to a number of Asia markets was offset by higher shipments to smaller markets and the NIS countries. Exports have also been growing to Mexico over the last several months and through October are 3 percent higher than the previous year.

Turkey Production Flat, Exports Higher

In November, the three-region price for whole turkeys (hens and toms) averaged 65.5 cents per pound, up 2 percent from the previous year. Most of the increase came from higher prices for toms as prices for whole hens were about even with the previous year. Wholesale prices for whole birds and parts are expected to remain close to their present levels as stocks of turkeys (whole birds and parts) at the end of October were considerably lower than the previous year, down 8 percent. Turkey production during the first 10 months of 2003 has totaled 4.8 billion pounds, making it almost exactly even with the previous year. While the number of birds slaughtered is down slightly from a year earlier, average weights are higher. However, just the opposite was true in October as the number of birds rose and the average weight declined slightly. Production over the next several months is expected to remain at or slightly below the previous year. Over the last 6 months, (May through October), the number of poults placed for growout has been down 1.4 percent from the same period in 2002.

U.S. turkey exports strengthened in the third quarter and continued to be strong in October totaling 50 million pounds, up 39 percent from the previous year. Most of the increase has come from an expansion in exports to Mexico. Over the first 6 months of 2003, exports to Mexico totaled 101 million pounds which was 9 percent less than in the previous year. During the third quarter exports to Mexico totaled 65 million pounds and shipments in October were an additional 29 million pounds, pushing exports for the first 10 months of 2003 to 397 million pounds, 6 percent higher than the previous year. With higher exports and no increases in production forecast, turkey prices are expected to gradually increase over the next several months, especially with relatively high prices expected in the rest of the livestock sector.

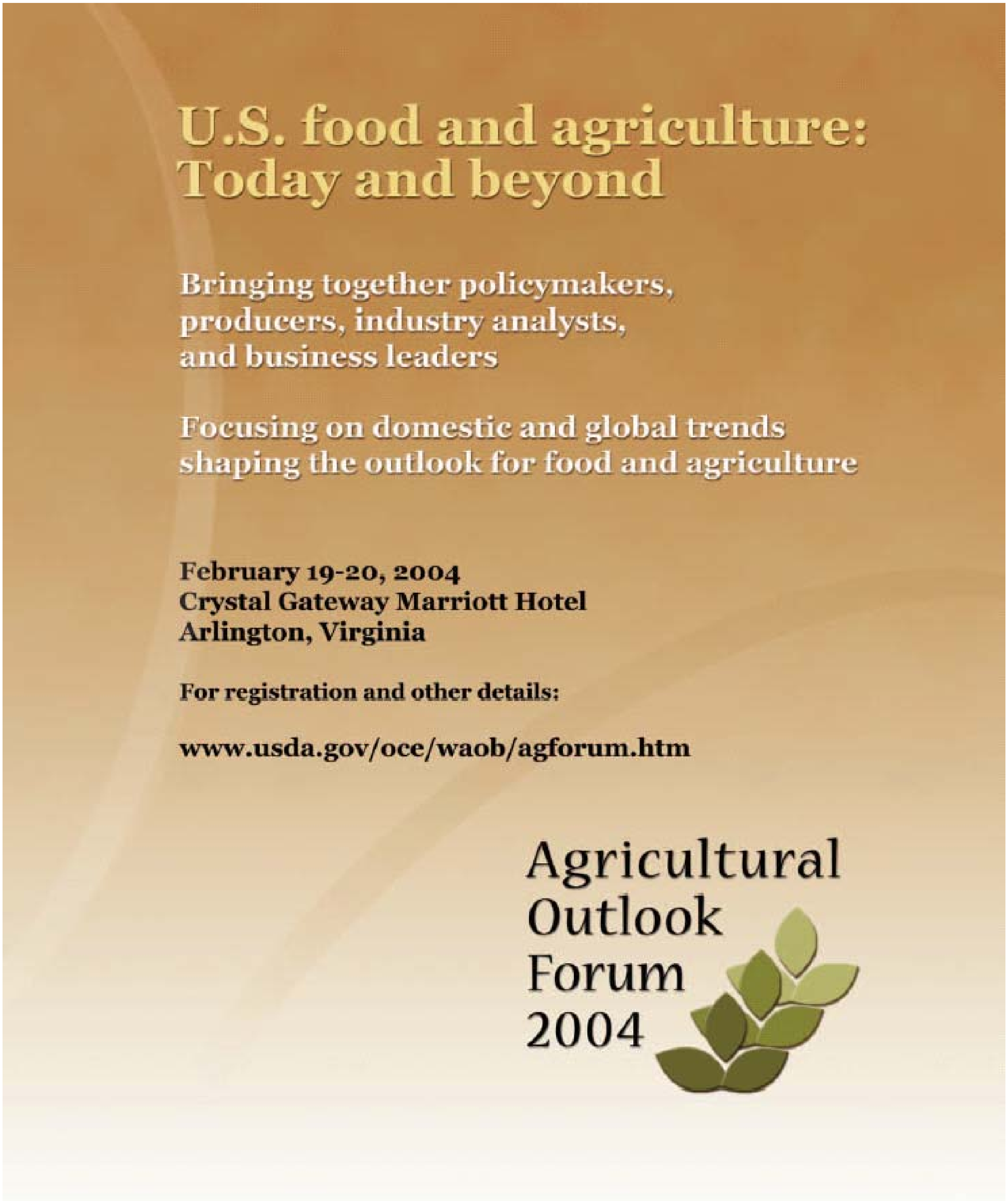
Sheep

Lamb Prices Up Sharply

Choice lamb prices at San Angelo, Texas are expected to average around $92 per cwt in 2003, 27 percent above last year. The farm price of lambs will likely average about $94 per cwt, a 28-percent increase from a year ago. The sharp boost in lamb prices is due to an expected 9-percent decline in lamb and mutton production and a 2-percent drop in imports. Continuing, albeit more moderate, declines in production and only a slight increase in imports will likely keep average lamb prices in the low $90s in 2004.

Fourth-quarter lamb and mutton production is expected to show its seasonal increase of more than 10 percent above the third-quarter level of 2003. Despite the expected seasonal increase, production is expected to be more than 5-percent below 2002 fourth-quarter levels. Lower production levels have resulted in fairly strong prices. Fourth-quarter choice slaughter lamb prices at the San Angelo, Texas market are expected to average nearly $10 per cwt above a year earlier. The fourth-quarter farm price for lambs is also strong and is expected to average $13 above the same period last year.

Strong lamb prices are further fueled by weaker-than-expected lamb and mutton imports as they have not increased to maintain the trend of stable per capita consumption. Lamb and mutton imports for the first 10 months reached 123 million pounds, down nearly 8-percent from the same period a year earlier. Imports reflect tight supplies in Australia, a primary U.S. supplier. Tight lamb supplies in Australia are expected to continue into 2004, hence, a small recovery in U.S. imports is expected. Imports in 2003 are expected to account for about 45 percent of U.S. consumption and an even higher import proportion is expected in 2004.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Related Article

The discovery of bovine spongiform encephalopathy (BSE) http://www.usda.gov/news/releases/2003/05/bg0166.htm in Canada resulted in the United States placing a ban on imports of ruminant animals and products from that country as of May 20. When the ban will be lifted is uncertain. The United States imports a substantial amount of cattle and beef from Canada.

USDA's **Outlook Forum** will be February 19-20, 2004, in Arlington, Virginia. The Forum provides the agricultural community with timely forecasts of farm prospects and insight into developments affecting the farm economy. Program details are available at http://www.usda.gov/oce/waob/agforum.htm.

Data

Retail Price Reporting for Meat
http://www.ers.usda.gov/Data/Meatscanner/ A new ERS database contains monthly average retail prices for selected cuts of red meat and poultry, based on electronic supermarket scanner data. While not based on a random sample, the raw data underlying the database are from supermarkets across the United States that account for approximately 20 percent of U.S. supermarket sales. Leland Southard, (202) 694-5187.

Web Sites

Animal Production and Marketing Issues, http://www.ers.usda.gov/briefing/AnimalProducts/
Cattle, http://www.ers.usda.gov/briefing/cattle/
Hogs, http://www.ers.usda.gov/briefing/hogs/
Poultry and Eggs, http://www.ers.usda.gov/briefing/poultry/
Dairy, http://www.ers.usda.gov/briefing/dairy
WASDE, http://www.usda.gov/oce/waob/wasde/latest.pdf

Red meat and poultry forecasts

	2001	2002		2003					2004			
	Annual	IV	Annual	I	II	III	IV	Annual	I	II	III	Annual
Production, million lb												
Beef	26,107	6,783	27,090	6,287	6,907	7,078	6,025	26,297	6,150	6,550	6,700	25,400
Pork	19,138	5,255	19,664	4,889	4,734	4,795	5,450	19,868	4,925	4,775	4,825	19,750
Lamb and mutton	223	56	219	49	50	48	53	200	49	48	47	194
Broilers	31,266	7,936	32,240	7,770	8,238	8,454	8,175	32,637	8,040	8,515	8,665	33,610
Turkeys	5,562	1,482	5,713	1,379	1,438	1,407	1,475	5,699	1,370	1,430	1,430	5,710
Total red meat & poultry	83,006	21,700	85,669	20,550	21,546	21,954	21,345	85,395	20,709	21,499	21,842	85,361
Table eggs, mil. doz.	6,077	1,573	6,184	1,511	1,514	1,546	1,570	6,141	1,525	1,520	1,550	6,170
Per capita consumption, retail lb 1/												
Beef	66.2	16.6	67.6	16.2	16.9	16.8	14.6	64.5	15.3	16.3	16.3	62.4
Pork	50.2	13.8	51.5	12.6	12.5	12.5	14.1	51.7	12.7	12.5	12.6	51.2
Lamb and mutton	1.1	0.3	1.2	0.3	0.3	0.2	0.3	1.1	0.3	0.3	0.3	1.1
Broilers	76.6	19.9	80.5	19.6	20.6	21.3	20.0	81.5	19.7	21.0	21.3	82.2
Turkeys	17.5	5.9	17.7	3.6	3.9	4.6	5.6	17.7	3.7	3.9	4.2	17.5
Total red meat & poultry	213.6	57.0	220.5	52.7	54.6	55.9	55.1	218.3	52.1	54.4	55.2	216.4
Eggs, number	252.6	64.6	253.6	61.9	62.3	63.1	64.1	251.4	61.9	61.7	62.8	250.0
Market prices												
Choice steers, Neb., $/cwt	72.71	69.10	67.04	77.82	78.49	83.07	102-103	85.47	93-97	84-92	79-85	84-91
Feeder steers, Ok City, $/cwt	88.20	83.08	80.04	78.48	82.49	94.90	104-105	90.09	97-101	89-97	86-92	90-97
Boning utility cows, S. Falls, $/cwt	44.39	35.39	39.23	40.53	46.52	49.84	50-51	46.85	47-49	48-52	47-51	47.25-50.25
Choice slaughter lambs, San Angelo, $/cwt	72.04	82.02	72.31	91.92	93.71	89.48	91-92	91.65	89-93	87-95	87-93	87-94
Barrows & gilts, N. base, l.e. $/cwt	45.81	31.34	34.92	35.38	42.64	42.90	37-38	39.61	39-41	39-43	40-44	39-42
Broilers, 12 City, cents/lb	59.10	53.70	55.60	60.30	59.60	63.40	63-64	61.70	60-64	61-67	63-69	61-66
Turkeys, Eastern, cents/lb	66.30	68.20	64.50	61.10	60.60	59.10	67-68	62.10	59-63	60-64	61-67	61-66
Eggs, New York, cents/doz.	67.20	75.50	67.10	77.20	73.90	89.90	112-113	88.40	93-97	82-88	86-94	88-95
U.S. trade, million lb												
Beef & veal exports	2,269	612	2,447	585	678	681	640	2,584	620	680	685	2,620
Beef & veal imports	3,164	708	3,218	810	741	619	690	2,860	835	950	905	3,430
Lamb and mutton imports	146	38	162	40	44	35	40	159	43	41	39	163
Pork exports	1,560	414	1,611	413	438	406	430	1,687	405	430	410	1,695
Pork imports	951	299	1,070	289	301	298	340	1,228	320	340	350	1,375
Broiler exports	5,555	1,220	4,807	1,200	1,166	1,182	1,240	4,788	1,215	1,240	1,275	5,030
Turkey exports	487	102	439	103	114	130	130	477	115	115	125	490

1/ Per capita meat and egg consumption data are revised, incorporating a new population series from the Commerce Department's Bureau of Economic Analysis based on the 2000 Census.

Economic Indicator Forecasts 1/

	2002			2003					2004			
	III	IV	Annual	I	II	III	IV	Annual	I	II	III	Annual
GDP, chain wtd (bil. 1996 dol.)	9,465	9,503	9,435	9,556	9,608	9,692	9,784	9,661	9,877	9,971	10,059	10,016
CPI-U, annual rate (pct.)	1.9	2.4	2.2	3.9	0.6	1.5	1.4	1.8	2.0	1.9	2.0	2.0
Unemployment (pct.)	5.7	5.9	5.8	5.8	6.2	6.2	6.1	6.1	6.0	5.9	5.8	5.9
Interest (pct.)												
3-month Treasury bill	1.6	1.3	1.6	1.2	1.0	1.0	1.0	1.1	1.1	1.3	1.6	1.5
10-year Treasury bond yield	4.3	4.0	4.6	3.9	3.6	4.2	4.3	4.0	4.4	4.5	4.8	4.6

1/ Source: Survey of Professional Forecasters, Philadelphia Federal Reserve Bank, August 2003.

Dairy Forecasts

	2002			2003					2004			
	III	IV	Annual	I	II	III	IV	Annual	I	II	III	Annual
Milk cows (thous,)	9,153	9,148	9,141	9,154	9,114	9,066	9,025	9,090	8,980	8,950	8,920	8,935
Milk per cow (pounds)	4,566	4,543	18,573	4,691	4,814	4,582	4,605	18,690	4,830	4,935	4,695	19,185
Milk production (bil. pounds)	41.8	41.6	169.8	42.9	43.9	41.5	41.6	169.9	43.4	44.2	41.9	171.4
Commercial use (bil. pounds)												
milkfat basis	43.8	43.9	170.5	41.2	43.0	44.7	44.9	173.8	42.3	44.1	45.3	176.7
skim solids basis	42.1	41.2	163.6	40.0	41.2	42.0	42.4	165.5	41.1	42.2	43.6	170.1
Net removals (bil. pounds)												
milkfat basis	0.1	0.1	0.3	0.4	0.6	0.2	0.1	1.2	0.1	0.1	0.1	0.4
skim solids basis	2.1	1.4	9.8	3.1	3.2	1.5	0.7	8.4	2.1	2.1	0.9	5.5
Prices (dol./cwt)												
All milk 1/	11.33	11.97	12.11	11.37	11.07	13.20	14.65 -14.85	12.55 -12.65	12.25 -12.75	10.95 -11.75	11.45 -12.45	11.85 -12.65
Class III	9.59	10.10	10.42	9.52	9.62	13.29	13.15 -13.35	11.35 -11.45	10.70 -11.20	9.95 -10.75	10.55 -11.55	10.65 -11.45
Class IV	10.36	10.52	10.81	9.89	9.74	10.05	10.15 -10.45	9.90 -10.10	9.75 -10.35	9.60 -10.50	9.95 -11.05	9.90 -10.80

1/ Simple averages of monthly prices. May not match reported annual averages.