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Cheese Markets Tighten, Other Dairy Markets Remain Soft

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Relatively weaken milk production and recovering sales led to significantly tightened late summer cheese markets while most other dairy markets stayed fairly soft. The cheese price increases are boosting milk prices. Production and market adjustments in coming months will test whether the prices can hold. The 2003 average price of all milk is projected to be similar to 2002's annual average ($12.19 per cwt) about $2 below the 1997-2001 average. Milk prices in 2004 are expected to be near this year's levels. Market adjustments leading to stronger prices could start to make a difference by late in 2004, but at least the first half of the year is threatening to be a lot like 2003. Milk production in 2003 is expected to total just barely larger than 2002's 169.8 billion pounds. Milk output may end the year again above the weakening levels of a year earlier. The projected recovery in milk per cow in 2004 would be enough to push 2004 production about 1 percent higher.

The ban on imports of Canadian beef and cattle by the United States since May 20 has created a shortage of market ready cattle. The continued strong domestic and international beef demand and tight beef supplies have resulted in U, S. cattle prices moving to record levels. Slaughter levels have remained relatively high to maintain beef production levels, but has sharply reduced slaughter weights and lowered the proportion of cattle grading Choice or Prime. Renewed imports of Canadian beef from cattle under 30 months of age will help ease the record setting price situation. Although prices are expected to decline as Canadian product reenters the market, prices are expected to remain strong as North American cattle inventories continue to decline due to continued drought in many areas.

Large hog exports by Canada have altered U.S. pork production and trade expectations for the balance of 2003 and the first half of 2004. Larger U.S. imports of Canadian slaughter hogs is the key factor pushing expected 2003 hog slaughter to nearly 99.3 million head, and pork production to 19.6 billion pounds. Higher slaughter hog imports will likely persist into 2004, lifting estimated slaughter for next year to 98.4 million head, and estimated production to 19.5 billion pounds.

Dairy

Weakened milk production and recovering sales led to significantly tightened late summer cheese markets while most other dairy markets stayed fairly soft. Adjustments in coming months will test whether recent cheese and milk prices can hold.

Recent price strength is not yet seen as a bellwether of a sustainable return to higher dairy prices. The delayed effects of the 1996-2001 period of generally high prices on milk production and the impact of a collapse in dairy demand probably have yet to be fully absorbed. Also, the quiet long-run trends in productivity and demand continue their effects.

Milk Production Softens

Spring and early summer milk production weakened from the large year-to-year increases that had persisted since the autumn of 2001. Heavily affected by low returns, milk cow numbers began declining from the winter peak and were below the rising numbers of a year earlier by late spring. More important, milk per cow was far below trend levels and rather erratic across States and months. Although decreases in milk cow numbers are expected to continue to weaken milk production in coming months, recovery in milk per cow, augmented by recent milk price recovery, could bring back small increases in milk production.

Very low milk prices and the highest concentrate feed prices in 5 years left first-half returns over concentrate costs at levels not seen in decades. Payments under the Milk Income Loss Contracts (MILC) significantly cushioned the impact for smaller producers receiving payments on all or most of their production. However, even these farmers had total returns much lower that in most recent years. The low returns and the relatively unpromising prospects for sustained price recovery led to a spring acceleration in the number of farm exits. Although the exit rate still is relatively modest, it contrasts considerably with the very low rates of the preceding 2 years.

Expansion by stronger producers has slowed, in part because of the low returns and in part because the momentum from the 1998-2001 returns finally appears exhausted. In addition, producers now have the option of expanding by buying discounted capacity of exiting farms rather than by adding new capacity to the industry.

July milk cow numbers in the 20 major States had fallen 0.6 percent from the March peak and 0.2 percent from a year earlier. Based on recent relative changes in 20-State and U.S. cow numbers, U.S. cow numbers in July probably were almost 1 percent below a year earlier. However, recent herd size was considerably less than 1 percent below the 5-year average, virtually no change by historic standards.

Milk-feed price ratios were relatively very low during the first half of 2003. Producers were not only cautious about the amounts of concentrates fed, but also reportedly cut back on some of the higher quality concentrates such as cottonseed. In addition, some producers probably opted to feed low-quality hay rather than seek out difficult-to-find and expensive dairy quality hay. This likely was an important factor in the very weak May milk per cow. Use of bovine somatotropin (BST) also may have been discouraged.

This year’s alfalfa crop is similar to last year’s: production is large but quality is erratic in most areas. Average prices are relatively modest because of the large supplies of mediocre alfalfa. However, supplies of good alfalfa stay tight. Making prime dry alfalfa hay has been particularly challenging in rain-drenched parts of the Midwest and Northeast. Corn silage prospects also are quite mixed.

Delayed effects of the 2001-2002 heifer shortage probably continued to weaken this year’s growth in milk per cow. As the heifer shortage eased last autumn, an influx of heifers into the milking herd began. This year’s disproportionate share of heifers in the herd lowered average milk per cow. This effect should reverse itself in coming months as these cows enter their second lactation.

Milk per cow in spring and early summer was virtually unchanged from a year earlier. Compared with the 5-year average, recent growth in milk per cow was only slightly more than 1 percent per year--barely more than half the long-run trend. The 20 States data indicate that May was the weakest month for milk per cow. By July, growth had recovered somewhat but remained quite weak. Recent milk per cow data have been quite erratic. Few regional patterns appeared, with both large declines and large increases common across the 20 States. In addition, month-to-month patterns have been unsteady, a characteristic that emerged last year.

Recovery in Milk per Cow May Boost Output

Summer strength in cheese and milk prices is not expected to significantly affect developing rates of structural change. The price recovery is likely to be fairly modest and possibly short-lived. Market tightness is pretty much restricted to cheese, with supplies of other products staying ample. Longer-run prospects probably will not be perceived as changed until there are clear signs of a broadly based market tightening. Only then are farmers likely to start altering long-run plans.

Relatively low returns are projected to keep milk cow numbers declining through 2004. Decreases from a year earlier are expected to exceed 1 percent by yearend, averaging about one-half percent for the year. Unless dairy product demand rises much more than now appears likely, declines in milk cow numbers could increase to almost 2 percent in 2004.

The recent price strength may have more impact on milk per cow than on cow numbers. Crop conditions remain quite uncertain, but the anticipated easing of concentrate prices now seems unlikely. Even so, milk-feed price ratios are not expected to return to the very low levels of late 2002-early 2003. Projected ratios will not rise to levels associated with trend growth in milk per cow but will allow farmers to be a bit more liberal with feed and BST.

Farmers probably have already begun reversing measures taken during the first half of 2003, and the effects may be apparent by this autumn. Fall is also when the large age cohort will start moving into their second lactations. Gains in milk per cow will accelerate this autumn and probably through next year. However, milk-feed price ratios are not projected to reach levels associated with trend increases in milk per cow, and forage quality probably will again be uneven. By late 2003, the increase in milk per cow from the weak level of a year earlier is projected to near 2 percent. But, the annual total likely will be only 1 percent above a year ago.

Recovery in milk per cow is expected to continue in 2004. Year-to-year increases are projected to be almost 3 percent as economic incentives improve slightly, and abnormal short-run circumstances fade. However, even this relatively large rise from a year earlier would leave milk per cow still below the long-run trend line. In addition, recovery may well remain uneven, as unambiguous forces for full recovery are unlikely.

Milk production in 2003 is expected to total just barely larger than 2002's 169.8 billion pounds. Milk output may end the year again above the weakening levels of a year earlier. The projected recovery in milk per cow in 2004 would be enough to push 2004 production about 1 percent higher.

Cheese Takes the Milk

Cheese production jumped 3 percent from a year earlier in July. Following the late-June boosts in cheese prices, cheese plants had a very large advantage in competing for somewhat tight milk supplies. The value of cheese exceeded the value of butter and nonfat dry milk by at least $3 per cwt of milk for most of July. In addition, nonfat dry milk and local cream was a very competitive alternative to raw milk for cheese.

Larger amounts of most cheeses were produced in July, with Italian varieties posting particularly large increases. However, milk supplies were not large enough, even with augmentation by powder and cream, to allow Cheddar to share the general increase. Cheddar production was still 3 percent below a year earlier in July, only a slightly smaller decrease than earlier in the year. Continued declines in Cheddar output were a major factor in firming cheese markets as summer progressed.

The amount of milk going into butter-powder plants fell substantially in early summer. Butter production dropped 16 percent from a year earlier in July, following a 13-percent decrease in June. Cream markets were additionally tightened by stronger ice cream output and more cream apparently going into foods other than dairy products. The decline in nonfat dry milk production was less, only 7 percent in July following 15 percent in June.

Supplies of milk for manufacturing are expected to stay moderately tight for the rest of the year, near year-earlier levels. Milk should be worth more in cheese than in butter and powder, at least until yearend nears. Cheddar production will remain a key factor in cheese prices. Sizable increases in Cheddar output would be an indicator of impending weakness in cheese prices.

Huge butter stocks remain a major barrier to lasting recovery in milk prices, although the problem appears to have stopped worsening. August 1 commercial butter stocks were only 31 million pounds above a year earlier, compared with increases of more than 100 million pounds earlier in 2003. The seasonal rise between April 1 and August 1 was only 26 million pounds in 2003, compared with about 55 million pounds in 2001 and 100 million pounds last year. Lower butter production and some increase in sales helped trim the growth in butter holdings. However, the kind of surge in butter use that could really bring stocks back into line is not yet evident.

August 1 commercial stocks of cheese were slightly smaller than a year earlier. Most of the 3-percent decline was due to lower holdings of American varieties. Reportedly, the most significant declines were for young Cheddar as a result of recent drops in Cheddar production.

August 1 manufacturers' stocks of nonfat dry milk were down about a fifth from the levels of the preceding 2 years. These holdings were larger than needed for the commercial market, but probably were fairly comfortable. Some stock swelling is inevitable during a continuing surplus period, and export deals under the Dairy Export Incentive Program (DEIP) require their own stocks.

On a milk-equivalent basis, August 1 milkfat stocks totaled 13.2 billion pounds, up only 3 percent from 2002 but almost a third larger than the lean 2001 stocks on that date. These holdings equaled 4 weeks of average commercial use of all dairy products. Skim solids stocks were a more moderate 9.7 billion pounds, slightly below a year earlier and slightly above 2 years earlier.

Commercial stocks of milkfat are projected to decline significantly during the second half of 2003. Any increases in milk production probably will be absorbed in the cheese markets, and retailing specials on butter may be more common. Even so, yearend stocks are projected to still be somewhat larger than needed. Market tightening this year has been insufficient to offset 2002's rapid stock accumulation. Ample stocks of butter are likely to remain a source of price weakness in early 2004.

Dairy Demand Creeping Back

Dairy demand continues its limping recovery. The economy has grown, although expansion has been uneven and with some nagging unemployment problems. Commercial use of dairy products generally has grown, although most of the recovery probably could be explained on the basis of low dairy prices. The restaurant sector remains in the doldrums.

Commercial disappearance of milk in all products was about flat in May and June before jumping about 4 percent from a year earlier in July. Both of these patterns may have been misleading. The May-June period was one of mixed signals concerning a production slowdown on one hand and a sales pickup on the other. Buyers probably were reluctant to step up purchases even though their pipeline holdings may have been unusually low for the time of year. The July surge was almost entirely the result of brisk cheese movement as buyers scrambled to build pipelines in a rising market. Another confusing feature resulted from the very large imports of American cheese (and resulting boost in commercial use data) during June-July 2002, cheese that probably did not move into final use until much later in 2002.

The most likely patterns of dairy product movement into final use during late spring-early summer included continued recovery in cheese use. Growth probably was stronger than earlier in 2003 or 2002, but that cannot yet be determined. Sales of butter and fluid milk stayed close to a year earlier. Disappearance of nonfat dry milk increased somewhat, but only to moderate levels. It is not clear that any increase in use outside the dairy industry itself has occurred.

Sales of dairy products are expected to grow at a slightly faster rate in late 2003 and 2004. Recovery in demand is expected to continue, although possibly raggedly. Prices, with the possible exception of cheese, likely will be attractive. Food processing use may pick up from last year's generally sluggish holiday season. For butter, there are some signs that autumn retail specials may be more common this year. Even so, growth in use is not projected to be extraordinary, and any price increases may quickly trim expansion.

Surplus About the Same

The small spring purchases of butter and cheese under the price support program quickly dried up once prices began to rise. Even though butter prices lost most of their original strength, supplies of current butter have not been in excess of market needs. On the other hand, purchases of nonfat dry milk continued relatively unabated. The level of powder purchases probably did not reflect just market conditions. Traders knew that USDA was planning to swap stocks of nonfat dry milk for process cheese and pudding for the school lunch and other domestic feeding programs. Sales to USDA under the price support program were made in anticipation of this powder's market effects. These swaps are expected to have put about 100 million pounds of nonfat dry milk on the market during the July-September quarter, with considerably more to come later in the school year.

New initial DEIP allocations, representing about a third of the annual limits, were announced in August. However, an invitation for bids was released only for nonfat dry milk. The nonfat dry milk allocation was exhausted fairly quickly.

Significant purchases of butter and cheese are not expected during the rest of the year, and it is uncertain whether an invitation for DEIP bids will be made. Therefore, net removals of butter and cheese are expected to be small and may even be negative if significant amounts are sold for unrestricted use. On the other hand, purchases of nonfat dry milk are expected to continue. The powder swapped for other products probably will not clear the market very quickly and likely will weaken demand for fresh production. In addition, DEIP removals will be sizable.

The surplus of skim solids is projected to be about 8 billion pounds, milk equivalent, down slightly from 2002 but still about 5 percent of marketings. The skim solids surplus has stubbornly remained above 3 percent since 1998. This year's surplus of milkfat is projected to be equivalent to only about 1 billion pounds of milk. Although this would be the largest in a number of years, it represents almost negligible amounts.

The surplus in 2004 is projected to decline. Surplus milkfat is expected to stay small and will hinge on DEIP activity. On the skim solids side, commercial use is expected to grow faster than production, leading to a modest drop in net removals. However, the surplus of skim solids is seen to be still sizable because sales growth has yet to show signs of a brisk response.

International Markets Quiet

International dairy markets have been mostly quiet since early 2003. In general, demand has been moderate. Dry milk importing has been steady but not aggressive, in part reflecting the somewhat mixed economic performance of major importers. Buyers know that large U.S. supplies of nonfat dry milk are available at only a slight premium to current international prices and have no need to import more than current usage. Butter demand has picked up a little with additional interest from Russia. However, overall demand remains relatively weak, in part because of less demand from the Middle East.

Somewhat tighter domestic markets in the European Union (EU) have lessened export supplies slightly. Supplies from the Southern Hemisphere will be very limited until significant quantities start to be shipped from the new season's production. Prospects for the new season in New Zealand and Australia are mixed, but quick recovery from the drought problems and low returns of last season does not seem likely.

Prices are expected to remain near current levels during the second half of 2003. Some seasonal strength in butter prices is possible toward yearend, but substantial improvement is not projected. Dry milk prices will be sensitive to recovery in Oceanic production, but cannot rise much in response to any shortfall because they are capped by U.S.

domestic prices. Even if southern production comes back rapidly, major price decreases probably would not occur until the seasonally largest amounts are shipped in early 2004.

Spring U.S. dairy trade was fairly stable. Milkfat imports were about 5 percent below a year earlier, while imports of skim solids fell about 15 percent. The proximity of international and domestic prices for nonfat dry milk discouraged imports of skim solids products, but the major factor in the declines was lower cheese imports. Considerably less American cheese was imported at the relatively high tariffs applied to imports outside the tariff-rate-quotas (TRQ), probably reflecting a change in business strategy on the part of the importer. Imports of other varieties subject to TRQ's were lower during April-June, but large July imports made up for them. Exports other than under the DEIP also were fairly steady, rising just slightly from a year earlier.

Dairy Prices Await Developments

Wholesale cheese prices have been steady in recent weeks. Stocks of American cheese are moderate, and sales have readily absorbed current production. Seasonal tightening of milk supplies around Labor Day reportedly was particularly pronounced this year. On the other hand, tightness in milkfat markets never really developed this summer in spite of fairly strong demand for cream for processing and limited supplies of fresh butter. Enough users shifted to the more-than-ample butter in storage to erode most of the rather feeble price increases.

Unless increases in cheese sales accelerate more than expected, small increases in milk production, the diversion of milk from butter-powder production, and increased use of nonfat dry milk in cheese production are likely to upset the rather delicate balance in cheese markets. The current price plateau might turn out to be the seasonal peak in cheese prices, with prices declining as yearend approaches.

Butter prices have the chance of posting some increases before the yearend holidays. Whether they do will hinge on the rate of decline in commercial stocks, which depends in turn on the briskness of sales. Even with brisk sales, such price increases likely would develop slowly and are unlikely to be more than modest. Nonfat dry milk prices, faced with large supplies of old powder and likely continuing sales to the Government, are not expected to attain any sustained increases. Even the normal seasonal premiums for fresh powder outside the West may be less than normal.

Farm Milk Price Increases May Not Hold

The jumps in wholesale cheese prices will boost farm milk prices during the second half of 2003. Farmers are projected to receive over $1.50 more per cwt of milk than they did a year earlier. Even so farm milk prices will stay much lower than those of the high-price years of 1998, 1999, or 2001. Because of the price strength, MILC payments will not be made on September and probably October milk. The MILC payment rate will rise if cheese prices start to crumble, but payments are not expected to return to high rates until well into winter.

The 2003 average price of all milk is projected to be similar to 2002's $12.19 per cwt, about $2 below the 1997-2001 average. Although the impact has been cushioned by the MILC (particularly for small producers), these prices represent a lengthy period of real prices lower than anything seen since before World War II.

Higher average milk prices in 2004 probably will require either accelerated improvement in dairy product demand or weakening in milk production, neither of which is considered likely. Recent improvement in cheese demand has been encouraging but shows no signs of being joined by strength in demand for other dairy products. Also, the economy is not expected to be robust enough to accommodate a surge in cheese sales sufficient to support significantly increased milk prices without contributions from other products.

Failure of milk per cow to show any recovery potentially could have a substantial impact on 2004 milk prices. However, the long trend growth in milk per cow is based on steady management and feeding improvements that are rarely interrupted for long. Although recent gains have been erratic and forage quality and concentrate prices are expected to fall short of ideal, conditions are not projected to be so unfavorable as to override pent-up trend forces.

Milk prices in 2004 are expected to be near this year's levels. Market adjustments leading to stronger prices could start to make a difference by late 2004, but at least the first half of the year is threatening to be a lot like 2003.

Retail dairy prices in July were more than 1 percent below a year earlier and slightly below most of the first half. Retail prices in July had not yet had much opportunity to respond to increases in wholesale and farm milk prices. Retail dairy prices will rise in coming months, particularly for cheese. However, rapid increases are not expected as the farm-to-retail price spread is likely to slip below a year earlier during the second half. The spread posted a moderate increase during the first quarter and was about unchanged in the second.

For all of 2003, retail dairy prices are projected to decline fractionally, the first decline in more than a decade. All of the decline would be due to a smaller farm-to-retail price spread as farm prices are expected to be unchanged. The spread is projected to bounce back in 2004, leading to a 2- to 4-percent increase in retail prices.

Cattle/Beef

Record Beef Prices Allocate Scarce Supplies of Quality Beef

The ban on imports of Canadian beef and cattle from the U.S. and world markets since May 20 when a single cow was discovered to have BSE (Bovine Spongiform Encephalopathy or Mad Cow Disease) exacerbated an already short supply of market-ready cattle. With continued strong beef demand both domestically and internationally, tight beef supplies have resulted in prices moving to record levels to pull fed cattle marketings forward. Slaughter levels have remained relatively high, to maintain beef production levels, but the cost has been sharply reduced slaughter weights and a reduction in the number of higher grading cattle. Renewed imports of Canadian beef from cattle under 30 months of age will help ease the record-setting price situation presently allocating very tight supplies of Choice and Prime beef within the export, hotel-restaurant, and a retail market increasingly demanding more consistent, higher quality beef. Although prices are expected to decline from present levels as Canadian product reenters the market, prices are expected to remain strong as North American cattle inventories continue to decline due to continued drought in many areas.

Recent Rains Raise Hope of Replenishing Forage Supplies

Recent rains throughout most of the country raised hopes for improved grazing conditions and at least some small grain grazing. Substantial rains in the late August should help the Central and Southern Plains in preparation for winter wheat planting. Late summer growth should also help late hay harvests; the next update on this year's hay crop will be released in the October *Crop Production* report. Additional rains and mild fall temperatures for additional pasture growth will be essential for over-wintering even the reduced cattle inventory. Producers in many areas have already been forced to supplement their herds on drought-reduced grazing with hay made earlier in the year.

Retail Choice Beef Prices Continue Record-Setting Pace

Market supplies of higher quality beef are extremely tight, at a time when even the retail market has been shifting toward a higher proportion of Choice beef in the meat case. Although the top end of Select beef can be an excellent value, in general Select beef does not have the consistency of the higher grades of beef. In August 2002 about 60 percent of the steer and heifer slaughter graded Prime and Choice, this year the proportion dropped to 50.6 percent. Record Choice boxed-beef prices are allocating the reduced supplies among users. Retail beef prices have been on a record/near record-setting pace since February as poor weather conditions slowed weight gains and tightened beef supplies. Then just as rates of feedlot gains began to improve in May, BSE was discovered in Canada eliminating this source of higher quality beef from the market.

The price surge continued in August with the Choice retail beef price averaging a record $3.74 a pound up from $3.66 in June and $3.65 in July. In the second week of September, with further supply tightening in higher quality beef, prices for Choice boxed beef rose sharply averaging a record $156.11 per cwt. Normally, slaughter weights rise through early fall and peak in late October-early November. As fed cattle have been pulled foreword and slaughtered with fewer days on feed this summer, weights have been relatively flat and well below the record weights of a year earlier. Even though third quarter beef production remains near to slightly below year-earlier levels, as cattle slaughter increased well above year-earlier levels, slaughter weights and the proportion grading Prime and Choice has declined. In July, federally inspected steer carcass weights averaged 25 pounds below last year, while heifer weights were down 19 pounds. The proportion of steer and heifer slaughter grading Prime and Choice was 61 percent last year, this past July the proportion was down to 54.5 percent. In August, steer carcass weights were about 30 pounds below a year earlier, while heifer weights were down about 25 pounds. The proportion of steer and heifer slaughter in August grading Prime-Choice was down to 52.6 percent, sharply below the 61 percent of a year earlier. The proportion grading Prime-Choice moved up to 64 percent last fall, but will remain far below that level this year unless the slaughter pace is slowed and cattle are kept on feed longer.

All Sectors of the Cattle Industry Profitable at Present

Typically, one sector of the cattle sector is profitable at the cost of another sector. At present, however, the ban on Canadian beef imports and the tight supply situation have resulted in industry scrambling to maintain the strong demand for higher quality beef and profits throughout the industry. At issue is how much higher prices can be pushed and still maintain profits in each sector. Clearly at present, some end users are not receiving the quality of beef their patrons have been receiving. Over the past several years satisfaction with higher quality beef has resulted in repeat business even at higher prices. In 1999 and 2000, retail pork prices were about 84 percent of beef prices. As demand for higher quality beef strengthened, this ratio deteriorated to near 80 percent in 2001 and 2002. With the present intense competition for the sharply reduced supply of Prime-Choice beef, the Choice beef/pork retail price ratio has declined to 72 percent. A similar situation has occurred with broilers. In the late 1990's the ERS retail young chicken composite price was about 55 percent of the Choice retail beef price. This ratio slipped to 46 to 50 percent in the early 2000's, and this spring the ratio was down to 44 percent. Although profits are extremely favorable throughout the cattle industry, a number of users are now paying extremely high prices for less than desirable quantities, and increasingly of lower quality of beef. Select beef prices have also risen rapidly over the past several months reflecting increased demand for all types of beef. Both pork and broiler supplies are expected to be near to above year-earlier levels over the next year, while beef supplies will be declining cyclically, particularly if forage conditions improve and herd expansion begins. Pork and poultry will become increasingly more attractive competitors, particularly to the retail market, if the alternative is a return to the inconsistent "lean beef" of the 1990's.

Quality Beef Supplies Continue to Tighten

Over the past decade, the North American beef industry has become increasingly coordinated. The two largest beef packers in Canada are also two of the largest packers in the United States. In recent years the United States has imported beef and cattle from Canada, and has exported both to Canada although in smaller quantities. About 8 to 10 percent of U.S. beef supplies are directly (boxed beef) or indirectly (fed cattle for immediate slaughter or feeder cattle for later slaughter) imported from Canada. With cattle herd liquidation occurring in the United States and Canada (as well as Mexico, an important source of feeder cattle) the present tight supply situation for high-quality beef is only going to get tighter until herd expansion results in increased beef supplies. Female slaughter has been large again this year due to dry conditions in many areas, and herd expansion has been put off for at least another year. At present even if more heifers are retained and bred in 2004, beef production will not increase before 2006, and supplies will decline even more in 2004 and 2005. In fact the stronger the expansion signals and the more female stock are retained; the tighter supplies will get over the next couple of years.

Canadian Beef Likely To Be Absorbed Fairly Readily

The first loads of Canadian boneless beef from cattle under 30 months of age and veal began to enter the United States in early September. Although the industry is concerned with the reentry of Canadian beef, end users will likely absorb the additional beef fairly easily. Certainly prices will decline from the feverish pace of the past several weeks, particularly for the higher quality beef, but the supply situation will remain very tight once the supplies begin to balance out. Initially larger quantities of higher quality beef are likely to enter from Canada because of their slaughter slowdown since May 20. This will allow fed cattle marketings in the U.S. to slow resulting in more days on feed for cattle in U.S. feedlots, a slowdown in slaughter and additional Prime-Choice beef to meet the growing demand for this product. Once the initial surge of higher quality beef from Canada is exhausted, much of the Canadian beef produced is likely to be lower grade due to the backlog of cattle they need to process. Typically about 50 percent of Canadian beef enters the export market. The U.S. and Mexico have opened their borders for Canadian veal and boneless beef under 30 months of age.

Cattle Prices Continue Record Pace

Fed cattle prices averaged in the low $80's in August, and in the upper $80's in early September. Even as Canadian beef reenters the United States, prices are expected to remain near $80 to the low $80's over the next year as cattle inventories tighten. Prices may go even higher depending on female retention and continued demand strength.

Similarly, feeder cattle prices have risen rapidly as feedlot operators attempted to maintain feedlot inventories following the rapid marketing pace of recent months. Yearling feeder cattle prices in Oklahoma City were averaging near $100 per cwt in mid September. Prospects for improved fall grazing conditions, particularly small grain grazing, are also increasing the demand for a tightening supply of feeder cattle. Although prices are expected to decline as beef supplies smooth out, prices are likely to remain in the upper $80's to the low $90's over the next couple of years

Utility cow prices remain very strong, with prices averaging near to slightly above $50 per cwt in late summer. Even as calf weaning begins and additional cows are culled from the herd, prices are expected to remain strong, as many herds have already been culled due to reduced forage supplies. Prices for 90-percent lean beef remain strong, averaging near $120 per cwt this summer, up from $102.60 in the third quarter of 2002. The tight supply of higher quality beef has similarly resulted in a sharp decline in supplies of fed beef trimmings, 50-percent lean, and a run at record prices. In summer 2002, 50-percent lean beef trimmings averaged $32.84 per cwt, but, as supplies of higher quality beef tightened, prices moved up beginning in April 2003, and with the reduction of trimmings from Canada, prices averaged $81.52 in August.

At present the entire market is short higher quality beef and the trimmings that are derived from this product. Prices for imported 90-percent lean beef, blended with 50-percent lean trimmings to add value, have languished in the $90 to low $100 range since spring. This has been an unusual year for the beef complex anyway one looks at it. The industry will be tested over the next couple of years as to whether it can continue to serve the strong customer base that it has developed with high-quality consistent beef for the retail, hotel-restaurant and export markets in the future. Prices relative to pork and poultry will be a key, particularly at the retail market. The retail market has shifted very successfully toward Choice beef and has been rewarded by consumers' willingness to pay higher prices for a consistent, quality product.

Hogs/Pork

2003 Pork Production Pulls Almost Even with 2002

Responses to the BSE situation in Canada by the U.S. and Canadian markets have altered expectations for U.S. pork production and trade for the balance of 2003 and the first half of 2004. Larger U.S. imports of Canadian slaughter hogs is the key factor pushing expected 2003 hog slaughter to 99.3 million head, and pork production to 19.6 billion pounds. Higher than average slaughter hog imports will likely persist through the first half of 2004, lifting estimated slaughter for next year to 98.4 million head, and estimated production to 19.5 billion pounds.

These upward adjustments in estimated slaughter and production leave very little daylight between 2002 slaughter and production, and estimates for this year, and 2004. Only 1 percent fewer hogs are expected to be slaughtered this year than in 2002. Production will likely be off by less than 0.5 percent if heavier year-over-year dressed weights continue for the rest of this year. Hog slaughter and pork production in 2004 are each expected to be less than 1 percent lower than 2003. Thus, breeding herd reductions of 2002 have largely been offset by larger hog and feeder pig imports from Canada, higher dressed weights, and small productivity increases.

Hog Prices Weaker, Retail Prices Steady

Record high prices in the beef sector finally spilled over into the pork sector last week. Although the Estimated Composite Pork Carcass Cutout averaged $64.21 from June through August, it had declined into the high $50 range in late August, and into early September. For the week ending September 13 the Cutout added more than $5 to the previous weeks close however, on the strength of higher wholesale demand for loins, butts, hams, and bellies. Retail pork prices appear to be on the increase as well. USDA reported an August composite retail pork price of $2.71, in increase of almost 2 percent from July. Higher beef prices and declining supplies of market ready cattle will likely provide continued support for both wholesale and retail pork prices well into the Spring of 2004. Adequate supplies of export-ready Canadian pork products as well as slaughter animals could moderate pork price increases.

U.S. Imports of Canadian Slaughter Hogs Up Sharply

U.S. imports of Canadian slaughter hogs have increased sharply since June. Live hog imports reported by USDA/APHIS indicate that U.S. imports of barrows and gilts for the period June-August 2003 increased 48 percent over the same period of 2002. Larger imports of Canadian slaughter animals is consistent with Canadian slaughter data, which indicate that Federal Slaughter for June-August is more than 7 percent lower than in the same period of 2002. The Canadian data further suggest that slaughter facilities in the western provinces have reduced slaughter numbers the most. For June-August 2003, Manitoba's slaughter is more than 19 percent lower than last year, and Saskatchewan's slaughter was 11 percent lower than last year.

Canadian Hog Slaughter at Federally Inspected Packing Plants

	British Columbia	Alberta	Sask.	Manitoba	Total West	Ontario	Québec	Atlantic Provinces	Total East	Total Federal Slaughter
	(head)	(head)	(head)	(head)	(head)	(head)	(head)	(head)	(head)	(head)
June-Aug 2002	102,379	659,355	291,072	1,160,160	2,212,966	1,047,327	2,071,533	142,733	3,261,593	5,474,559
June-Aug 2003	92,868	669,325	260,330	937,305	1,959,828	1,035,374	1,955,477	124,463	3,115,314	5,075,142
% change	-9.29	1.51	-10.56	-19.21	-11.44	-1.14	-5.60	-12.80	-4.48	-7.30

Source: Agriculture and Agri-Food Canada

Pork Consumption Lower in Canada in Response to BSE Situation

An important reason for lower Canadian slaughter-- and thus a greater supply of exportable hog-- could be weak demand for pork by Canadian consumers, since the onset of the BSE situation in late May. It appears that Canadian consumers have increased their consumption of domestic beef as a sympathetic response to the plight of the Canadian beef industry. Lower Canadian pork prices contributed to lower packer margins and subsequent cutbacks in Canadian slaughter, diverting hogs to the United States for slaughter. Larger imports of Canadian slaughter hogs will likely persist, until supply and demand balance has been achieved in Canada, and more normal pork consumption rates resume.

Fallout From Canadian BSE Situation Extends to U.S. Pork Product Imports

Weak consumer demand for pork products in Canada appears to have created attractively priced products for U.S. importers. Despite the lower valued U.S. dollar, June and July imports of Canadian pork products increased 14 percent over the same 2 month period last year. For the first 7 months of 2003, imports of Canadian pork products increased 16 percent over 2002.

Poultry

Broiler Production Forecast Increased

The U.S. broiler production forecast for third quarter 2003 has been increased to 8.43 billion pounds, up 150 million pounds from the previous estimate. This is a 2.1-percent increase in production compared to a year earlier and reflects an expected upward turn in the number of birds slaughtered as well as continued growth in their average weight. Broiler meat production is expected to show a seasonal decline in the fourth quarter, with production estimated at 8.1 billion pounds. Throughout most of the third quarter, the number of chicks being placed for growout has averaged only marginally higher than the previous year. This pattern is expected to change slightly going into the fourth quarter, with chick placements averaging slightly less than 1 percent higher than the previous year. In the most recent broiler hatchery report, the number of egg sets and chicks placed over the last 5 weeks (August 2 to September 6) showed little growth over the previous year. This is a strong indication that the number of birds available to processors through the middle of November will at best be only a little higher than in the same period in 2002. However, average live weights have continued to increase and are expected to be a major reason behind higher broiler meat production. Over the first 7 months of 2003, the number of birds slaughtered was down by 1.4 percent, but that decline was has been offset by a 1.4-percent increase in their average weights.

Broiler Exports Edge Higher

Second quarter 2003 broiler exports totaled 1.17 billion pounds, up 2.6 percent from the same period in 2001. The chief reason for the increase is a stabilization in the export situation with Russia. Exports to Russia were down 10.5 percent over the first 7 months of 2003, compared with same period in 2002. This amounts to a roughly 100-million-pound decrease in shipments. However, all the decrease was in the first quarter, with shipments in the remaining months slightly higher than the previous year.

Shipments to other top markets (Hong Kong, Mexico, and Korea) have also been markedly lower than the previous year. These have been almost totally offset by the growth in exports to a number of rapidly growing markets. In the Western Hemisphere, much of the growth has been in shipments to Cuba (up 62 percent) and Guatemala (up 30 percent). Other high-growth areas so far in 2003 have been direct shipments to China (up 104 percent), Angola (up 40 percent), and Taiwan (up 40 percent).

The forecast for broiler exports during the second half of 2003 calls for gradually increasing shipments. Total exports in the third and fourth quarters are expected to reach 2.6 billion pounds, up 5 percent from the previous year. Along with improvements in the Russian market, this forecast depends on improvements in exports to such markets as Hong Kong and Mexico.

Flat Production, But Lower Exports, Increases Turkey Stocks

Over the first 7 months of 2003, U.S. turkey production totaled 3.3 billion pounds, almost identical with the same period in 2002. Along with the minimal increase in production, the first 7 months of 2003 has seen a considerable decline in turkey exports (down 4 percent), chiefly due to lower exports to Hong Kong. These factors, combined with little increase in domestic consumption, have resulted in a continued buildup in stocks of frozen whole turkeys and turkey parts. Cold storage estimates at the beginning of August place turkey stocks at 742 million pounds, 5 percent higher than in 2002, but 39 percent higher than at the beginning of August 2001. Overall, most of the increase in turkey stocks has been in parts, which are 9 percent higher than at the same time the previous year. While stocks of whole birds are up only 1.4 percent, there is a large difference between the poundage of whole hen and whole toms in storage. Stocks of whole toms are up 14 percent from the previous year, but have been offset almost entirely by lower cold storage holding of whole hens (down 13.3 percent).

Eggs

Egg Prices Sharply Higher

In August 2003, wholesale table egg prices (NY grade A large) averaged 93.8 cents nominal per dozen, the highest ever recorded. For all 2003, prices are expected to average 81-83 cents a dozen, the highest since 1996, when wholesale prices averaged 88.2 cents per dozen, also the highest annual price ever recorded. In 1996, large export sales and the rising trend of eating breakfast were major contributors to high egg prices.

In 2003, however, high egg prices are likely due to tighter per capita supplies, resulting from poor profitability during 1999-2002, flock depopulations and rising demand for eggs that are "animal care certified." The U.S. United Egg Producers (UEP) voluntarily initiated Animal Husbandry Guidelines which includes increasing the assigned cage space per bird over several years. The Food Marketing Institute and the National Council of Chain Restaurants have endorsed these guidelines. Some grocery chains in the United States are requiring suppliers to be certified as using the guidelines.

In August 2002, the U.S. egg industry started with an initial space allowance of 56 sq. inches for white egg leghorn layers, and 62 sq. inches for brown egg layers. These space allowances, according to UEP, will increase gradually to a maximum of 67 sq. inches for white layers and 76 sq. inches for brown layers in 2008. Increased cage space allowance can increase the costs of buildings and equipment, but can improve feed conversion.

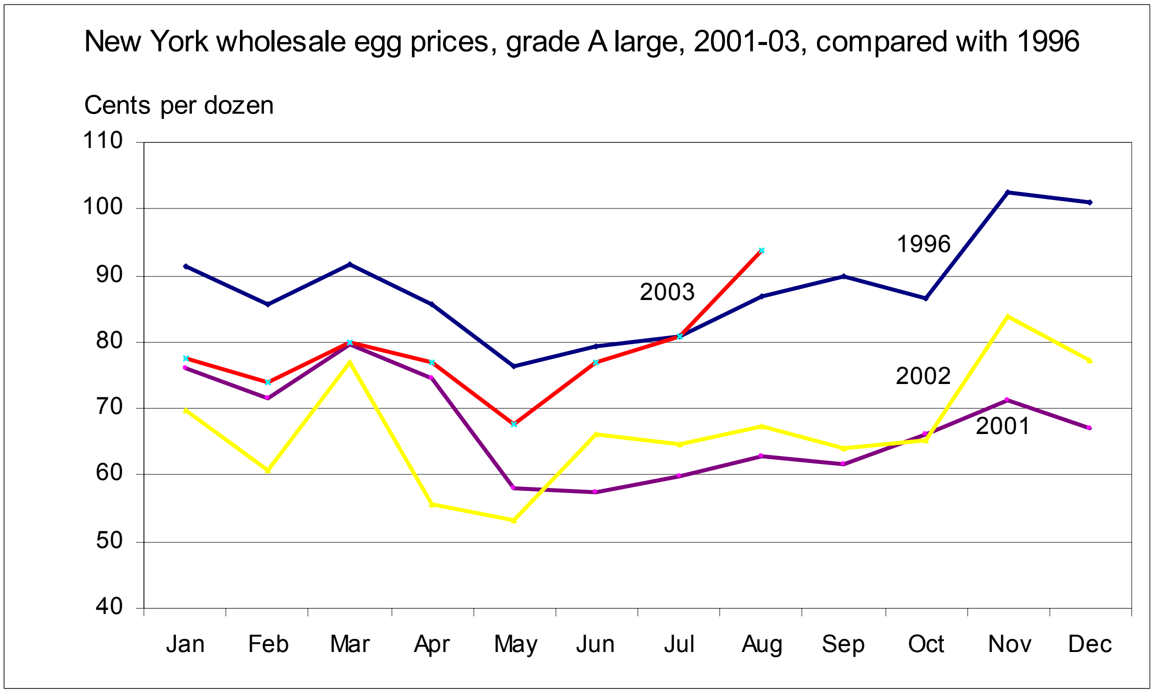
Wholesale egg prices increased sharply from an average of 67.7 cents per dozen in May to 93.8 cents in August (see figure). During August, prices reached as high as 98 cents for 5 consecutive days, before they headed down, ending the last day of the month at 95 cents per dozen. In 2003, wholesale egg prices are expected to average 81-83 cents per dozen and 77-83 cents in 2004.

For all of 2003, retail egg prices are expected to average about $1.15-1.17 per dozen, 12 percent higher than in 2002. If realized, the price would beat the record retail prices of $1.106 per dozen reached in 1996. However, prices are expected to drop about 2 cents per dozen in 2004.
In 2003, per capita egg consumption is forecast to decrease slightly, to 252 eggs and further decline by about 1 egg per person in 2004.

For 2003, due to the higher shell egg prices, the quantity of eggs going to the breaking market is expected to decline by 4 percent compared with 2002. The trends will most likely reverse course in 2004, as prices moderate.

Total U.S. egg production in 2003, table and hatching, is expected to rise to nearly 7.23 billion dozen, a fractional increase over 2002. Egg production is expected to increase by 1 percent in 2004, due to higher 2003 prices. Table eggs account for 85 percent of total production in 2003, and are expected to stay at that percentage in 2004. Hatching egg production in 2003 will be nearly unchanged, but is expected to rise by nearly 2 percent in 2004. The rise in 2004 will come mostly from higher demand by the broiler sector. Table egg production is expected to rise by less than 1 percent.

U.S. egg exports in 2003 are expected to reach 153 million dozen, down 12 percent from the previous year. The decline is mainly attributed to layer-flock recovery from avian diseases in the Netherlands, Belgium, and Germany, which imported more shell egg and egg products to compensate for their egg production lost in 2002. Shell eggs (for human consumption and hatching) accounted for nearly 55 percent of total U.S. exports. The remaining 45 percent were exported as processed albumen and yolk in dried or liquid forms.


New York wholesale egg prices, grade A large, 2001-03, compared with 1996
Cents per dozen
110
100
90
80
70
60
50
40
Jan
Feb
Mar
Apr
May
Jun
Jul
Aug
Sep
Oct
Nov
Dec
1996
2003
2002
2001

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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.

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	III	IV	Annual	I	II	III	IV	Annual	I	II	Annual
Production, million lb												
Beef	26,107	7,097	6,783	27,090	6,287	6,907	7,000	6,200	26,394	6,050	6,525	25,275
Pork	19,138	4,832	5,255	19,664	4,889	4,734	4,775	5,200	19,598	4,900	4,700	19,500
Lamb and mutton	223	51	56	219	49	50	49	51	199	49	48	194
Broilers	31,266	8,251	7,936	32,240	7,770	8,238	8,425	8,100	32,533	7,900	8,375	33,000
Turkeys	5,562	1,412	1,482	5,713	1,379	1,438	1,425	1,475	5,717	1,390	1,450	5,790
Total red meat & poultry	83,006	21,837	21,700	85,669	20,550	21,546	21,854	21,198	85,148	20,469	21,284	84,476
Table eggs, mil. doz.	6,077	1,551	1,573	6,184	1,511	1,514	1,555	1,580	6,160	1,520	1,530	6,205
Per capita consumption, retail lb 1/												
Beef	66.2	17.3	16.6	67.6	16.2	16.9	16.7	14.9	64.7	15.3	16.2	62.3
Pork	50.2	12.7	13.8	51.5	12.6	12.5	12.4	13.5	51.0	12.6	12.2	50.4
Lamb and mutton	1.1	0.3	0.3	1.2	0.3	0.3	0.3	0.3	1.1	0.3	0.3	1.1
Broilers	76.6	20.8	19.9	80.5	19.6	20.6	20.9	19.6	80.5	19.4	20.5	80.2
Turkeys	17.5	4.4	5.9	17.7	3.6	3.9	4.2	6.0	17.7	3.8	4.0	17.9
Total red meat & poultry	213.6	56.1	57.0	220.5	52.7	54.6	55.0	54.8	217.1	51.8	53.7	213.8
Eggs, number	252.6	64.0	64.6	253.6	61.9	62.3	63.6	64.5	252.3	61.6	62.0	250.9
Market prices												
Choice steers, Neb., $/cwt	72.71	63.29	69.10	67.04	77.82	78.49	80-81	78-82	79-80	78-84	79-85	78-85
Feeder steers, Ok City, $/cwt	88.20	78.87	83.08	80.04	78.38	82.49	94-95	94-98	87-88	92-98	90-96	87-96
Boning utility cows, S. Falls, $/cwt	44.39	37.69	35.69	39.23	40.32	46.52	49-50	47-49	46-47	45-49	48-52	47-50
Choice slaughter lambs, San Angelo, $/cwt	72.04	74.60	82.02	72.31	91.92	93.71	88-89	84-86	90-91	84-90	84-90	83-90
Barrows & gilts, N. base, l.e. $/cwt	45.81	33.86	31.34	34.92	35.38	42.64	42-43	38-40	39-40	39-43	41-45	41-44
Broilers, 12 City, cents/lb	59.10	56.40	53.70	55.60	60.30	59.60	63-64	60-64	61-62	57-61	59-63	58-63
Turkeys, Eastern, cents/lb	66.30	66.70	68.20	64.50	61.10	60.60	58-59	62-66	61-62	59-63	61-67	64-69
Eggs, New York, cents/doz.	67.20	65.30	75.50	67.10	77.20	73.90	87-88	88-92	81-83	77-83	72-78	77-83
U.S. trade, million lb												
Beef & veal exports	2,269	660	612	2,447	585	678	685	650	2,598	630	680	2,620
Beef & veal imports	3,164	839	700	3,218	810	741	640	700	2,891	860	975	3,530
Lamb and mutton imports	146	32	38	162	40	44	36	43	163	45	42	171
Pork exports	1,560	389	414	1,611	413	438	400	430	1,681	405	430	1,695
Pork imports	951	275	299	1,070	289	301	320	340	1,250	320	315	1,295
Broiler exports	5,555	1,202	1,220	4,807	1,200	1,166	1,250	1,300	4,916	1,250	1,275	5,200
Turkey exports	487	98	102	439	103	114	115	120	452	110	105	445

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		
	II	III	IV	Annual	I	II	III	IV	Annual	I	II	Annual
GDP, chain wtd (bil. 1996 dol.)	9,388	9,465	9,503	9,435	9,556	9,608	9,692	9,784	9,661	9,877	9,971	10,016
CPI-U, annual rate (pct.)	3.4	1.9	2.4	2.2	3.9	0.6	1.5	1.4	1.8	2.0	1.9	2.0
Unemployment (pct.)	5.9	5.7	5.9	5.8	5.8	6.2	6.2	6.1	6.1	6.0	5.9	5.9
Interest (pct.)												
3-month Treasury bill	1.7	1.6	1.3	1.6	1.2	1.0	1.0	1.0	1.1	1.1	1.3	1.5
10-year Treasury bond yield	5.1	4.3	4.0	4.6	3.9	3.6	4.2	4.3	4.0	4.4	4.5	4.6

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

DAIRY FORECASTS

	2002				2003					2004		
	II	III	IV	Annual	I	II	III	IV	Annual	I	II	Annual
Milk cows (thous,)	9,149	9,153	9,148	9,141	9,154	9,116	9,075	9,045	9,100	9,000	8,960	8,950
Milk per cow (pounds)	4,811	4,566	4,543	18,573	4,691	4,815	4,590	4,625	18,720	4,845	4,955	19,260
Milk production (bil. pounds)	44.0	41.8	41.6	169.8	42.9	43.9	41.7	41.8	170.3	43.6	44.4	172.3
Commercial use (bil. pounds)												
milkfat basis	42.2	43.8	43.9	170.5	41.2	43.1	44.5	44.8	173.6	42.6	44.5	177.6
skim solids basis	40.6	42.3	41.2	163.4	40.2	40.8	43.5	41.7	166.1	41.3	42.3	171.0
Net removals (bil. pounds)												
milkfat basis	0.1	0.1	0.1	0.3	0.4	0.5	0.2	0.1	1.1	0.3	0.1	0.7
skim solids basis	3.5	2.1	1.5	9.8	3.1	3.2	0.6	1.3	8.2	2.0	2.2	5.3
Prices (dol./cwt)												
All milk 1/	12.03	11.33	11.97	12.11	11.37	11.07	12.95 -13.15	13.20 -13.70	12.15 -12.35	11.30 -12.10	10.75 -11.75	11.40 -12.40
Class III	10.59	9.59	10.10	10.42	9.52	9.62	13.05 -13.25	11.40 -11.90	10.90 -11.10	9.65 -10.45	9.80 -10.80	10.15 -11.15
Class IV	10.73	10.36	10.52	10.81	9.89	9.74	9.90 -10.20	9.90 -10.50	9.80 -10.10	9.60 -10.50	9.40 -10.50	9.70 -10.80

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