

In The Cattle Markets

James Mintert, Ph.D.

Professor, Department of Agricultural Economics, Kansas State University

Narrow Processor Margins Have Supported Live Cattle Prices

Kansas slaughter steer prices are on track to establish a new record high of about \$93/cwt. in 2007. Current forecasts suggest that prices could set another record high in 2008. In that context, it's useful to look back upon 2007 to ascertain why prices were so strong.

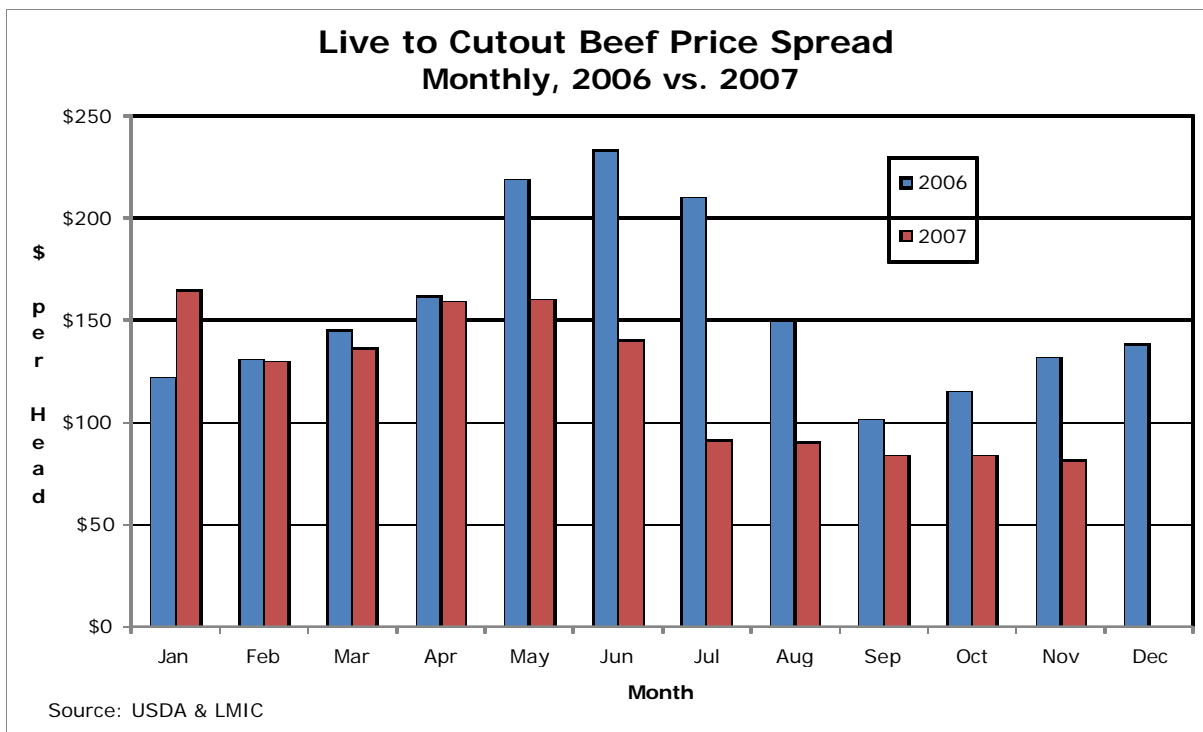
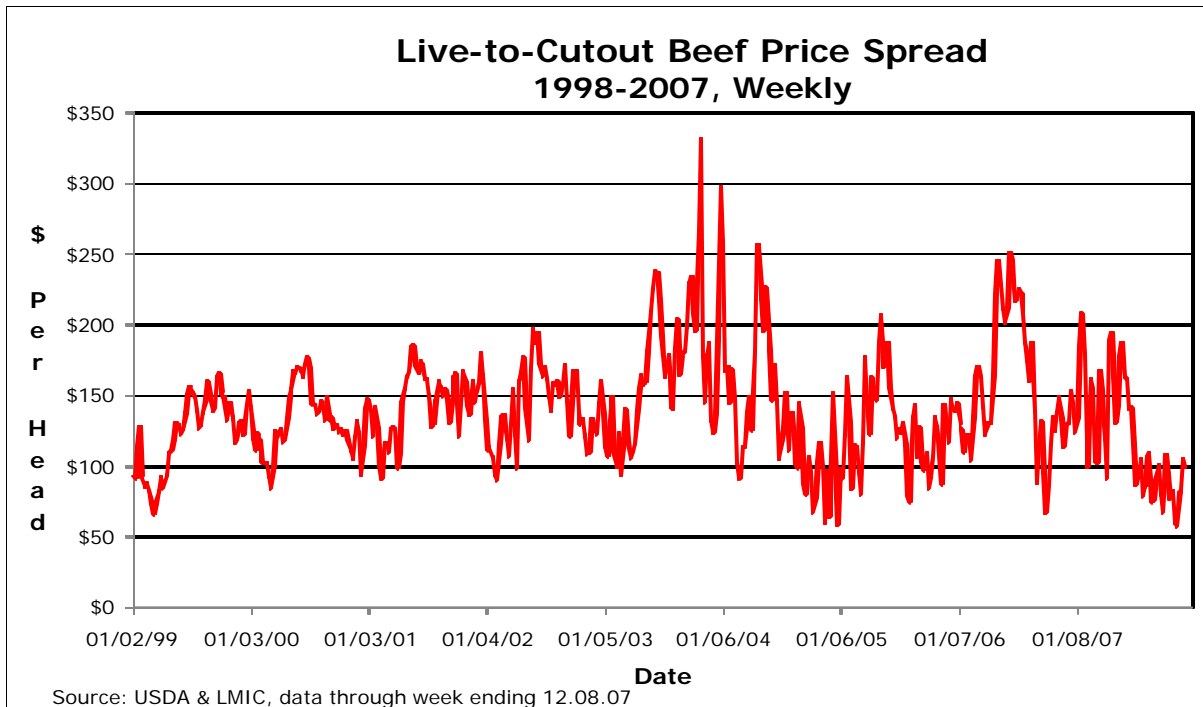
One of the key factors that helped support live cattle prices at such a high level during 2007 was a dramatic narrowing in the spread between wholesale beef and live cattle prices. This becomes more clear when year-to-year changes in wholesale beef and slaughter steer prices are examined. Through early December, Kansas live steer prices averaged \$92.94/cwt. up 7.9% from the same period in 2006 when they averaged \$86.13/cwt. In contrast, over the same time frame wholesale Choice boxed beef prices averaged \$149.87/cwt. in 2007, just 1.9% more than in 2006. It's clear from looking at the shift in the two price series that processor's operated with much narrower margins in 2007 than in 2006.

The Livestock Marketing Information Center (LMIC) calculates an estimated live-to-cutout price spread each week to help gauge shifts in processor operating margins over time. Over the last 10 years LMIC's estimated weekly margins have ranged from a high of well over \$300 per head to a low of just over \$50 per head.

Since estimated margins can be quite volatile from one week to the next, it's useful to average them over longer periods of time to make more meaningful comparisons. Monthly average margins in 2006 and 2007 tell an interesting story. The spread between live steer prices and wholesale Choice beef was actually wider than a year earlier during January and near 2006's from February through April. However, since May the spread has consistently been narrower than a year earlier.

A variety of factors influence margins, both from week to week and over long periods of time. But it appears that a key factor behind narrower processor margins in 2007 than in 2006 has been the processing sector's desire to keep slaughter plants operating near their optimum level, rather than reduce capacity to reflect the fact that the industry's annual slaughter volume in 2007 is much smaller than just a few years ago.

Looking ahead to 2008, it's clear that expectations for record high slaughter cattle prices in 2008 are at risk to what actually happens to the live-to-cutout beef price spread. Recently, several major processors have indicated that they plan on reducing hours of operation in response to poor processing margins. If they follow through with their announced intentions over a long period of time in 2008, it could lead to a wider spread between wholesale beef and live cattle prices. In fact, recent weekly margin estimates indicate the price spread has widened from about \$60 per head in early November to approximately \$100 per head in early December. So, processor margins could be a key to live cattle price strength in 2008.



The Markets

Slaughter cattle prices in Kansas and Nebraska weakened the week ending 12.14.07, averaging \$93.05/cwt. in Kansas and \$145.50/cwt. in Nebraska. There has been very little trade this week (week ending 12.21.07) through Thursday. Choice boxed beef prices declined moderately last week, as the Choice cutout averaged \$147.70/cwt. and the Choice-Select spread dropped back to \$15.55 from \$16.03/cwt. Trade this week (week ending 12.21.07) was higher on Monday and Tuesday, and despite some price weakness at mid-week, the weekly

average Choice cutout could wind up 1 to \$2 higher than a week earlier. Feeder prices weakened last week in both Kansas and Nebraska, although trade volume was light. Strength in corn prices and weakness in slaughter cattle futures, are the forces pushing feeder prices lower.

Cattle or Meat Category	Week of 12/14/07	Week of 12/07/07	Week of 12/15/06
Kansas Fed Steer Price, live weight	\$93.05	\$93.93	\$85.01
Nebraska Fed Steer Price, dressed weight	\$145.50	\$145.96	\$134.24
700-800 lb. Feeder Steer Price, KS 3 market average	\$104.22	\$106.23	\$103.07
500-600 lb. Feeder Steer Price, KS 3 market average	\$114.68	\$114.34	\$113.57
700-800 lb. Feeder Steer Price, NE 7 market average	\$102.99	\$111.46	\$101.17
500-600 lb. Feeder Steer Price, NE 7 market average	\$121.13	\$123.52	\$116.57
Choice Boxed Beef Price, 600-900 lb. carcass	\$147.70	\$148.33	\$143.40
Choice-Select Spread, 600-900 lb. carcass	\$15.55	\$16.03	\$18.08
Corn Price, Omaha, NE, \$/bu (Thursday quote)	\$4.16	\$3.87	\$3.36
DDG Wholesale Price, Iowa, \$/ton	\$142.50	\$140.00	\$127.50