How the beef and cattle market will look beyond COVID-19

As consumers' lives return to normal, expect continued cattle market volatility.

Burt Rutherford | May 27, 2020

The tide is turning. Maybe. Or perhaps it's more accurate to say the tsunami called COVID-19 is beginning to recede, leaving economies in shambles and pace of economic recovery in doubt.

Here are some sobering facts about the U.S. economy from John Penson, chief economist with Ag America Lending:

- The Dow lost 23% of its value in the first quarter, ending a record 11-year bull market run.
- The S&P 500 decline in March surpassed its decline in the Great Depression.
- Energy company shares fell more than 40%.
- Bank stocks fell more than 30%.
- An estimated $1.5 trillion loss in economic output was reported in the first quarter.
- According to the Commerce Department, consumer spending fell 8% in March, which accounts for 70% of GDP.
- There's an estimated annualized GDP decline of 25% to 30% for the second quarter, compared with the 26% decline during the Great Depression.
- Estimates further are that we'll see a 6% to 7% decline in real GDP for the entire year, compared with the 2.5% decline during the Great Depression.
- On the plus side, unemployment reached 14.7% as of April, compared with 24.9% during the Great Depression.

According to the AgAmerica Lending report, the above figures show unsettling similarities to the state of the U.S. economy during the Great Depression. Clearly, however, the economic world we live in now is very different from the economic world my grandparents experienced leading up to and during the Depression of the 1930s. But I'll place my bets on America. That's because we are the United by God States of America and American people, American business and the American economy are far too resilient to stay down for long.

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In addition, there are other significant and important differences.

One of those, and in my mind the biggest, is that the decline in the U.S. economy related to COVID-19 is due to self-imposed restrictions rather than a lack of consumer demand. "This signals the potential for a strong rebound in the second half of the year, estimated between 5% and 10% as businesses begin to reopen," Penson writes.

For agriculture, particularly beef, the rebound may be even greater in my opinion. I'm not an economist, so I can't validate that opinion with numbers.

But people have to eat. And we know they want to eat beef. The logjams at packing plants are beginning to break up and plants are running between 50% and 90% of capacity. That will allow the beef marketing chain to begin refilling grocery store meat cases. As states begin to relax their lockdowns, restaurant traffic will increase. That's good news.

Weighing on the market, however, is a backlog of harvest-ready cattle in feedyards at mind-boggling numbers. Estimates are that there around 1 million fed cattle backed up in feedyards with the number growing daily.

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In RaboResearch's Beef Quarterly Q2 2020 report, Rabobank protein analyst Angus Gidley-Baird writes, "Even if plants return to relatively normal processing capacity in June, it will likely be well into 2021 before the industry has fully digested the backlog."

That means marketing plans for the rest of this year and 2021 need to be carefully evaluated. The last two Cattle on Feed reports show reduced placements—March placements were down 23% year over year and April placements were down 22%.

Those feeders are still out there and will have to go on-feed sometime. "Such delayed feeder placements likely create a gap in fed cattle marketings in October, thus challenging bunk space for the fall calf run," according to the report. How will the market respond?

"As packing plant capacity disruptions are solved, the relative value between beef and live cattle will return to traditional levels, although the global macroeconomic challenges will weigh on the absolute price of both," according to the RaboResearch report. "Cutout price should fall dramatically as the panic around short-term beef supply shortages is relieved. Third quarter live cattle prices could trade near $105 per cwt, with potential for $110 to $115 in Q4."

The report says feeder cattle prices will track deferred live cattle futures, with slow fed cattle marketings and financial damage to cattle feeders curtailing demand in the short term. Long term, as pen space begins to loosen, we'll return to whatever our next normal will be as packers find their level of production in the post-coronavirus world. It's likely, given present packing plant capacity, we'll be around 80% to 85% of pre-COVID production.

Only time will tell. In the meantime, "Expect volatility moving forward as the market continues through unchartered territory," Rabo Research warns.