CME Group

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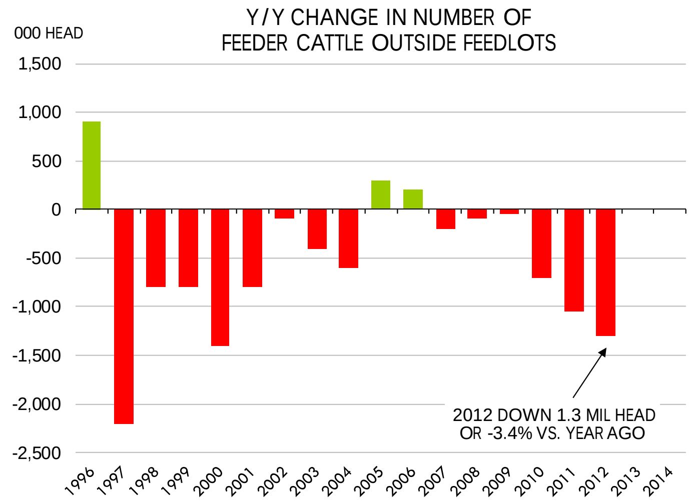
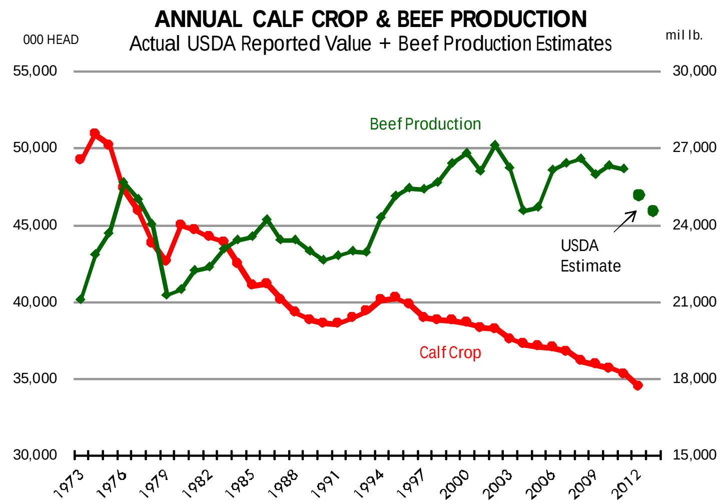
Market Comments

Live **cattle futures were modestly higher on Monday** as the latest USDA survey data pointed to dramatic reductions in both the number of cattle expected to come to market in the next few months (feeder supply) as well as the number of beef cows that form the base for future production. Feeder cattle futures, on the other hand, continued to drift lower as an inflationary feed outlook remains a negative for the complex. The supply of feeder cattle outside of feedlots (a measure of "pipeline supplies') was 37.5 million head as of July 1. This represents a 1.3 million head or 3.4% decline from the same period a year ago. The chart to the right outlines the change in feeder cattle supply numbers for the July inventory count since 1996 and the data is downright depressing. It shows an industry mired in a significant contraction, with feeder supply numbers increasing modestly in only three of the last 18 years. Feeder supplies have been declining steadily since 2007, with supplies down by a little over 1 million head last July and then down another 1.3 million head this year.

The latest cattle inventory data appeared to confirm that the feedlot sector is undergoing significant structural changes. A number of analysts, particularly those at the Livestock Marketing Information Center, have pointed out that the monthly feedlot inventory data likely overstates the number of cattle on feed. As some operations close while others expand to become profitable, this has skewed the sample size and it has given the appearance that there are more cattle on feed this year compared to last. The semi—annual survey gets around this issue since it polls all feedlot operations and not just those with a capacity of +1000 head. **The cattle inventory data pegged that total cattle on feed inventory as of July 1 at 12.3 million head, only 0.8% higher than a year ago**. This is almost 2% points lower than what the regular monthly feedlot survey indicated for July, a big difference which should put US feedlot supplies in better context.

The current drought conditions and lack of pastures will likely further exacerbate the liquidation of the US beef cow herd and reduce future calf crops. The USDA crop progress report published on Monday afternoon indicated that **26% of US pastures and ranges are now in very poor state**, about 8 points higher than the same period a year ago. Another 29% of pastures and ranges are in poor state. Some states, such as Missouri, show 74% of pastures in very poor state, a situation that will most likely force many producers to sell. High corn prices have made a difficult situation untenable but significantly reducing potential future profits.





March 2013 feeder futures were trading at around $164/cwt in mid June but have declined to the mid to high 140s currently. With high feed costs, poor pastures and lower out front prices for calves, the incentive will be to once again liquidate beef cows. Despite the shrinking calf crop, US beef producers have been able to sustain, and even increase, beef production since the 1980s. But as productivity gains hit an inflection point and calf crop declines, forecasts are for steady reduction in beef output.

The Daily Livestock Report is published by Steve Meyer and Len Steiner. To subscribe/unsubscribe visit www.dailylivestockreport.com.