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For Ag, It's Mostly Good News on the Demand Front

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For Ag, It's Mostly Good News on the Demand Front

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THE CROP and livestock markets have experienced significant swings over the past few years—record crop prices in 2012 and 2013 were followed by record livestock prices in 2014. Since then, prices have tumbled across the board. In most cases, price reductions have been driven by increases in supply, as opposed to drops in demand.

For the hog sector, the last five years have been very good from a packer demand perspective. As Figure 1 shows, packer demand for hogs surged in 2012 and has basically ridden that wave ever since, with only a slight setback in 2015. The downturn in 2015 occurred when hog prices dropped from record levels. Pork exports have been strong since 2011, supporting packer demand; and the near-term future looks positive as well, as the pork industry will add slaughter capacity over the next couple of years. The growth in packer demand for 2016 is a combination of larger pork supplies and higher real prices than a year ago.

Domestic demand for pork, measured at the retail grocery counter, has also strengthened over the past five years, despite the volatility in the hog market. Figure 2 displays the retail demand for pork. Domestic pork demand has not been this strong since 2004; however, the growth in pork demand has slowed over the last couple of years.

For the cattle sector, the packer demand over the past few years has been more variable, as can be seen in Figure 3. In general, packer demand has trended downward since 2011; however, there has been a couple of waves of demand growth, in 2013 and 2015. Packer demand in 2016 took the largest step back since 2009. While the amount of beef moving through packers has increased, the price decline more than offset the gain. Cattle prices during the 2nd quarter of 2016 were down nearly 14 percent from the previous quarter.

While packer demand for cattle has declined, retail demand for beef has trended higher, peaking as recently as 2015. Figure 4 shows retail demand for beef. While beef demand has slowed a bit, the 2nd quarter numbers show demand holding at the second-highest level since 2000. Compared to a year ago, beef consumption is higher and retail prices are lower; however, the decline in prices is bigger than the increase in consumption.

The mostly positive demand story for the livestock industries has also contributed to a stronger demand and usage story for the crop sector as well. Figure 5 shows the quarterly usage of US corn over the past five marketing years. The marketing year for both corn and soybeans begins on September 1 of the year when the crop was harvested. So, for example in the corn and soybean figures, "2011 Q1" refers to the 1st quarter of the 2011 marketing year, or September to November 2011. The 2nd quarter covers December to February, the 3rd quarter March to May, and the 4th quarter June to August. As Figures 5 and 6 show, livestock feed usage peaks during the 1st quarter of the marketing year. While that 1st quarter peak has not been quite as high over the past couple of years, the usage in the other quarters has provided support. On average over the five-year period, feed usage has increased by 11 million bushels per year.

The ethanol industry's usage of corn has grown significantly over the past couple of decades, such that it now

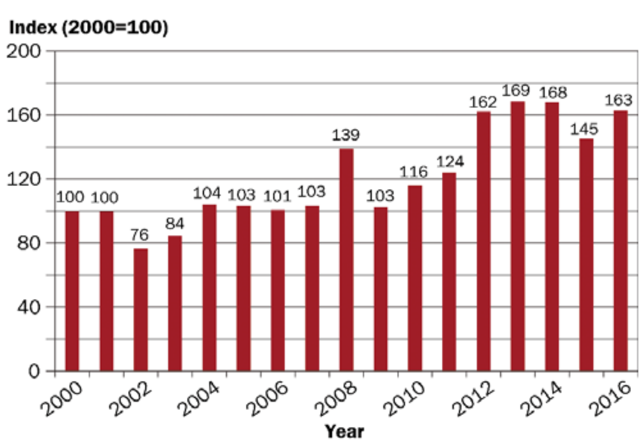

Figure 1. Second quarter (Apr-Jun) US packer demand for hogs index

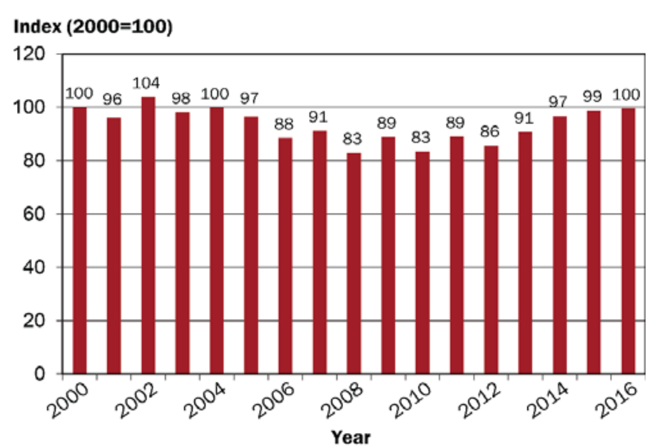

Figure 2. Second quarter (Apr-Jun) US retail pork demand

challenges feed as the largest usage category. While corn usage for ethanol declined in the 2012 marketing year, the general pattern has been slow and steady growth. From 2011 to 2015, corn usage for ethanol grew by 24 million bushels per year; however, the strongest annual growth rate for corn usage over the past five years has been in exports. The international market for corn has been absorbing, on average, an additional 39 million bushels per year. Much of the export gain has come from the Latin and South American countries, as the provisions of free trade agreements are enacted. Corn usage in other categories (corn sweeteners, industrial uses, etc.) has remained flat over the same period.

There has been similar growth in the components of soybean usage. Figure 6 outlines the usage of soybeans over the past five marketing years. Roughly half of the US soybean crop goes to international markets and the other half is used domestically. Like corn, soybean usage is loaded toward the front end of the marketing year. For domestic use, this is due to the need to crush soybeans to create soybean meal, a livestock feed product. Soybean oil is also created, which is often used for biodiesel production or other industrial processes. Both of these products can also be exported. The average growth rate for domestic soybean usage has been a 7 million bushel increase per year over the past five years.

Most of the growth for soybean demand over the past few years has come from exports. The Chinese market continues to expand its need for soybeans and that has driven US soybean exports to a steady stream of records. The projections for the 2016 marketing year continue that string. On average, soybean exports have grown by 20 million bushels per year. Given USDA's latest projections, this year soybean exports will rise by 45 million bushels.

Overall, the demand picture for crops and livestock is good. The issues the markets are having are more related to large supplies than declines in demand. For the livestock sector, the growth in supplies is slowing; however, the crop sector has not been able to pull back on production. In both sectors, prices will remain under pressure given the larger supplies. ■

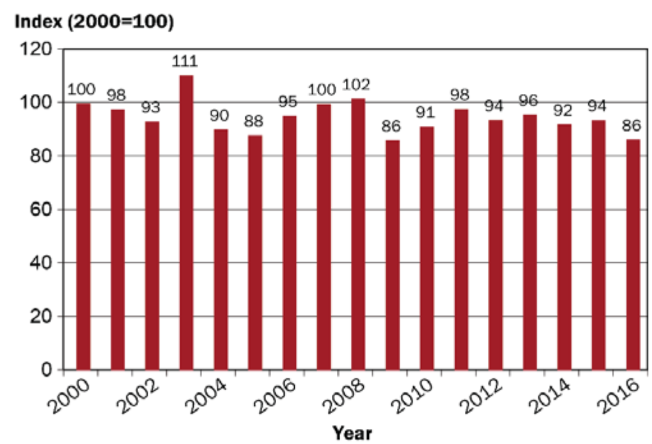

Figure 3. Second quarter (Apr-Jun) US packer demand for cattle index

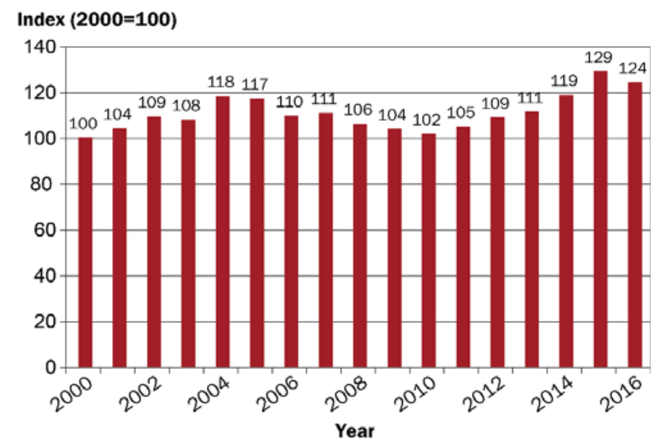

Figure 4. Second quarter (Apr-Jun) US retail all fresh beef demand

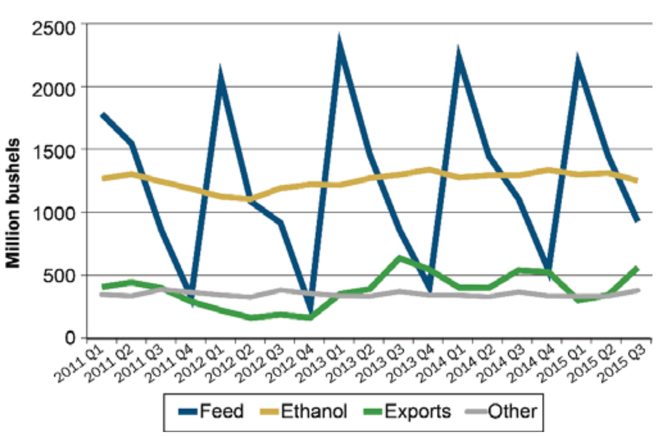

Figure 5. Quarterly usage of US corn 2011-2015

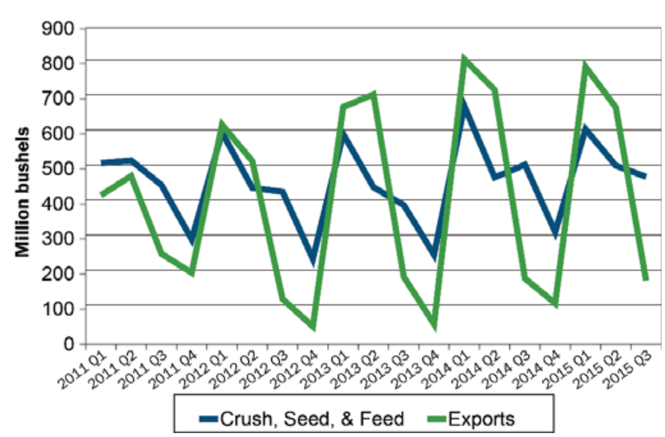

Figure 6. Quarterly usage of US soybeans 2011-2015