Make Informed Decisions
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Cow Prices and Value Diverge

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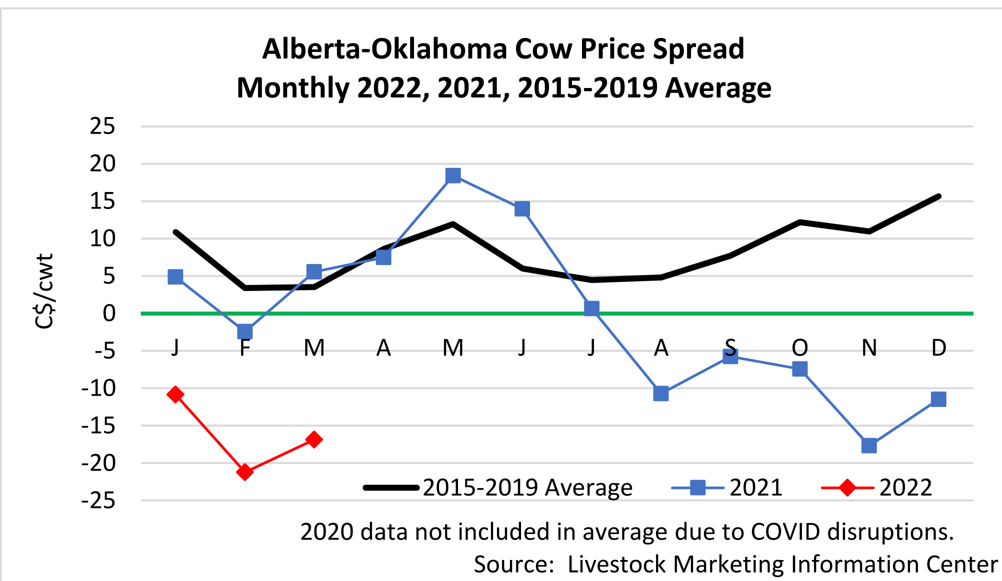
In prior reports, I showed how fed cattle prices and beef prices have been on divergent paths in recent years. The same appears to be happening regarding cow and cow beef pricing, particularly in Alberta.

Cow Spread Erosion

The Alberta-U.S. cow price spread has been performing well below average since the summer. During the first quarter this year, the Alberta cow price was C$16/cwt under Oklahoma. Last year in the first quarter, the average was positive by $2-3/cwt and the 2015-2019 Q1 average was nearly +$6/cwt.

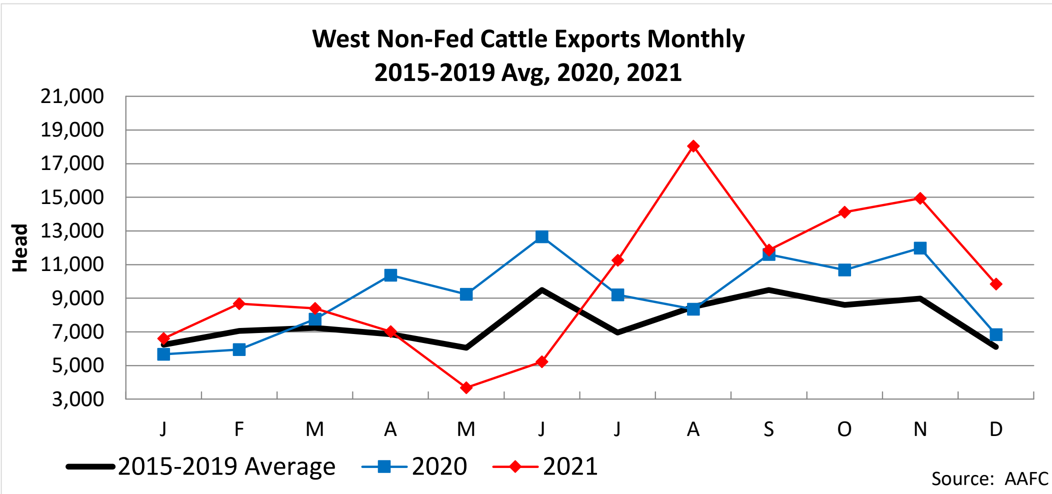


Drought Induced Marketing Glut

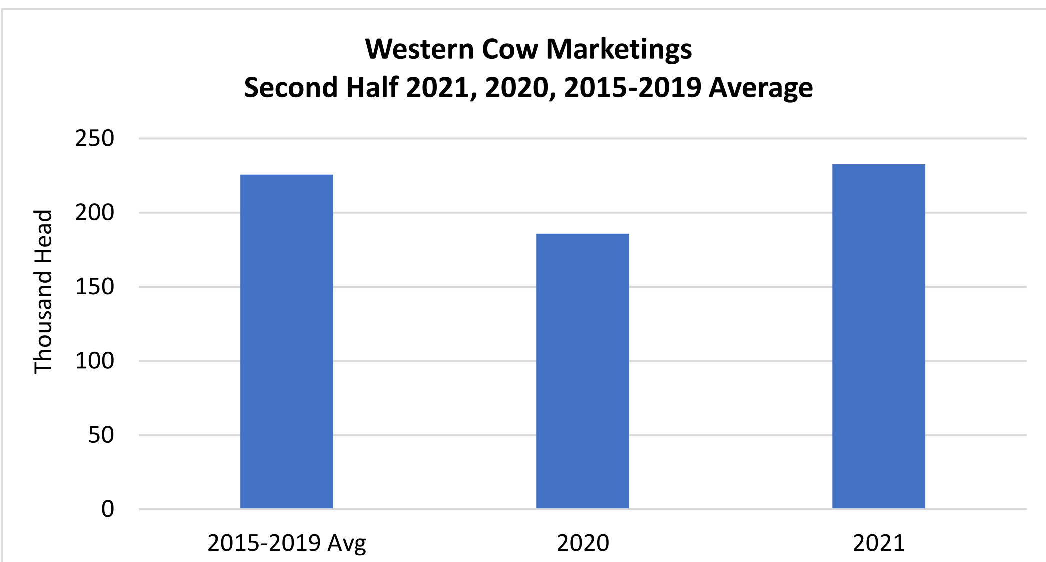
The steep erosion in the prairie cow market relative to the U.S. coincides with the 2021 drought and increased culling. During the final half of last year, Alberta cow slaughter was about 25,000 head more than the last half of 2020. That 25,000 amounts to about a 20% difference or about

1,000 per week, which is significant. With that noted, second half 2021 exports were about 15,000 head less than the 2015-2019 2H average.

The other point of note is that exports of cull cattle from Western Canada amounted to over 80,000 head in the second half of 2021. That compares to less than 60,000 in 2020 and 2015-2019 average exports of less than 60,000.



The net result of the slaughter and exports is that 2021 second half marketings were nearly 47,000 head more than 2020, and nearly 7,000 head more than the 2015-2019 average.

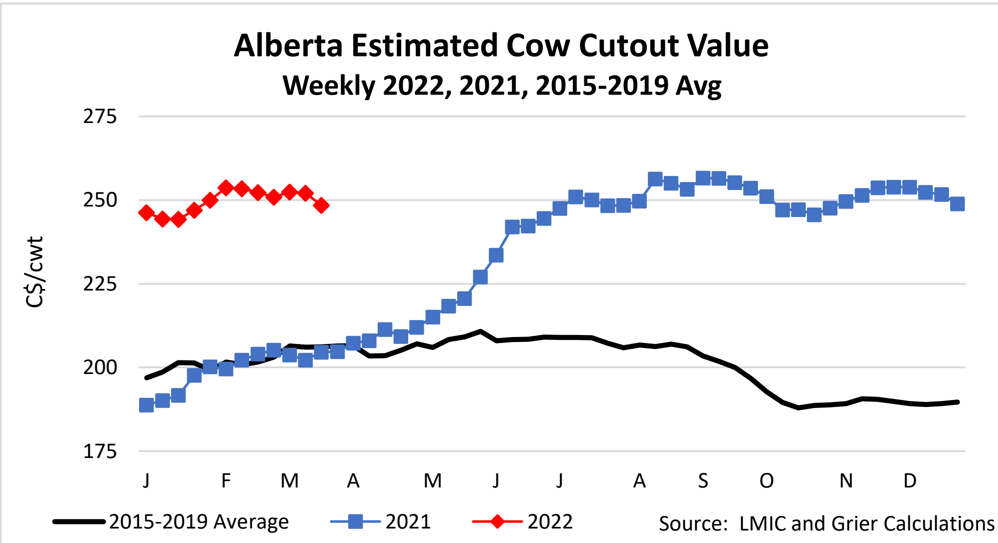


That 2021 2H versus the average differential does not seem like much until it is noted that the 2021 Western Canadian July cow inventory was 139,000 head less than the 2015-2019 average inventory.

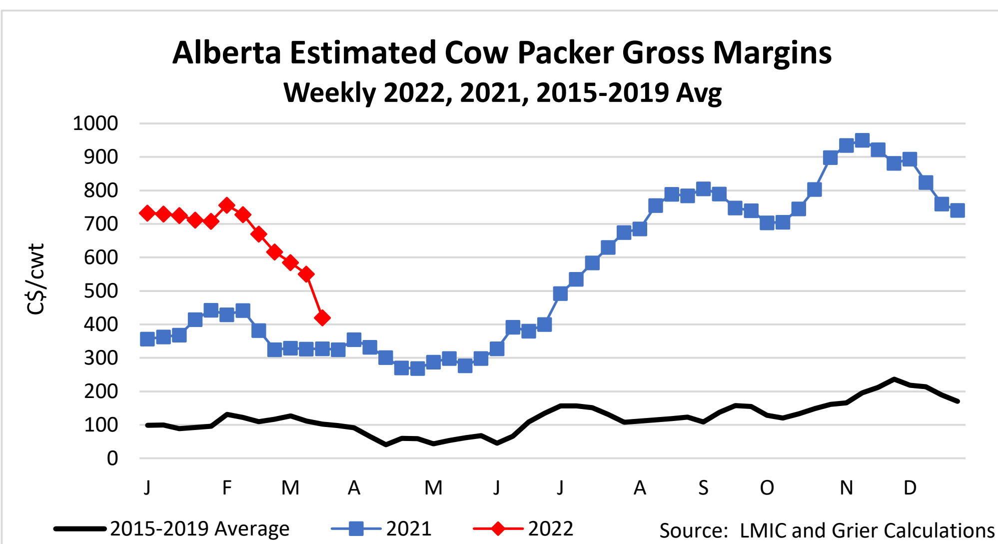
All of that was a long way of saying that cow marketings were and are significant and generally more than domestic packers are demanding. The net result is the material price erosion relative to the United States. Furthermore, while the Alberta cow price has been increasing sharply this year, it remains far below the 2015-2019 average.

Cutout Values Stay Strong

Meanwhile, although the cow price has been struggling, the value of the cow cuts has been remarkably steady at very high levels. The USDA publishes a cutter cow cutout value each week. I estimate a Canadian equivalent by adjusting for physical differences in the Canadian cutout. Due to differing cutting specifications, I reduce the U.S, value by 4%. In addition to that, due to transport cost differentials, I reduce the U.S. value by another 10% to return an estimated Alberta equivalent. With all of that noted, the Alberta estimated cutout has been trending far above average for several months.



Putting the costs and the cutout together leads to the conclusion that Alberta packer cow margins must be very good. To estimate a gross margin, the hide and offals, referred to as the drop credit, must added to the beef revenues. Drop credit is estimated by taking the USDA cow drop credit and reducing it by one half. That decrease is necessary because of Canada's antiquated SRM rules. Those rules take value out of the drop and reduce it to rendering. Taking those beef and credit revenues and subtracting the prior week's cow cost yields a gross margin. The gross margin is before operating costs such as labor and materials.



Of course, any given Alberta packer is going to have different cow margins than those shown on the graph above. Nevertheless, the assumptions going into the Alberta cutout and drop are reasonable and defensible. Furthermore, the methodology has been applied consistently over time. It shows that the average margins from 2015-2019 were very poor. At the same time, the methodology shows that current margins are excellent.

Due to Unusual Supply and Demand

As with the fed cattle and beef divergence which I described elsewhere, the cow and cow beef divergence causes are due to unusual circumstances and overall factors of supply and demand. The COVID production backlogs, the drought-induced forced marketings and ongoing feed shortages have driven cull cow supplies higher and prices lower. At the same time, excellent beef demand has kept cow beef prices very strong. The net result is a cow price and cow cutout divergence.

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A version of this note first appeared in the March 28, 2022, edition of Canadian Cattle Market Report. If you would like a free, two-month trial to the report, email me at kevin@kevingrier.com.