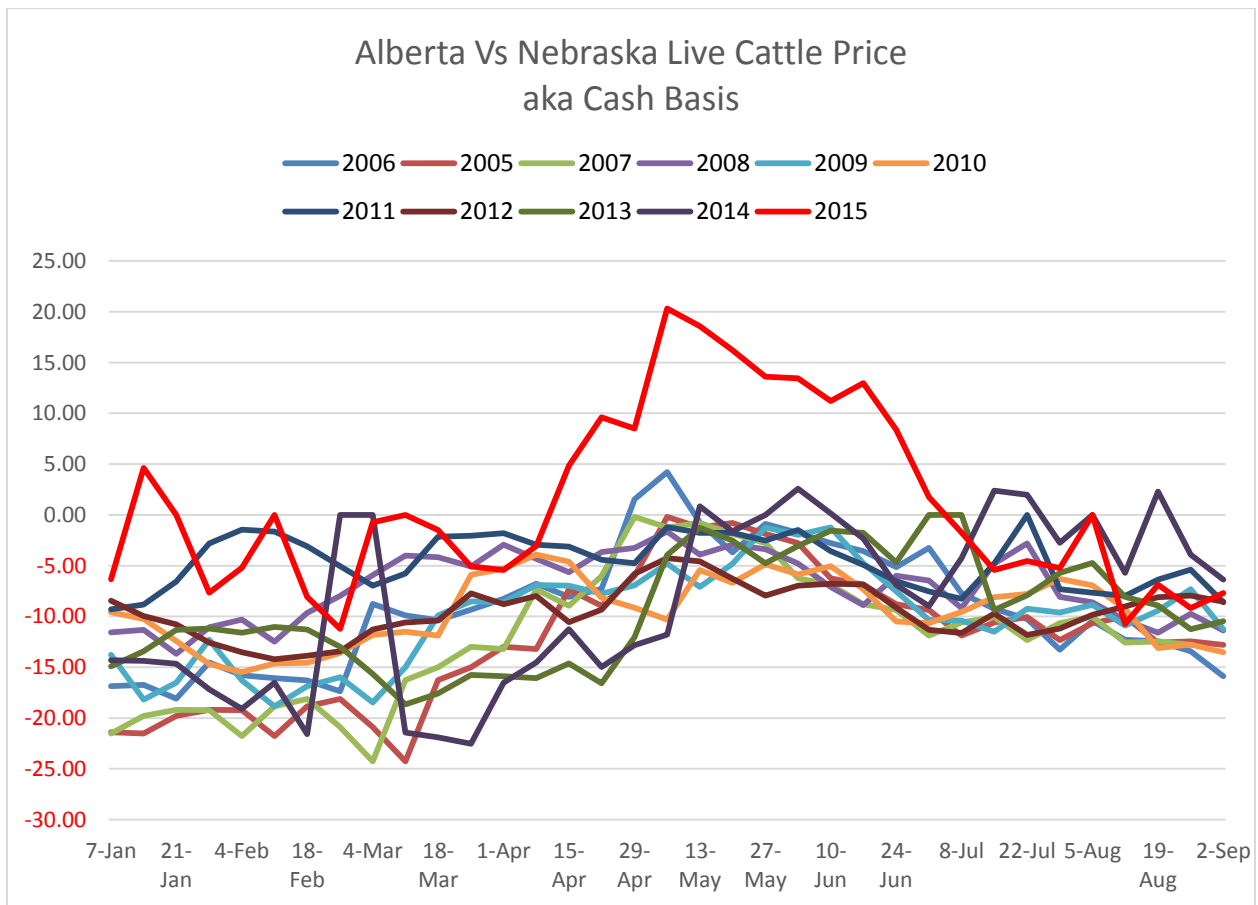


Arguments Point to Change Coming to Alberta Beef Packing

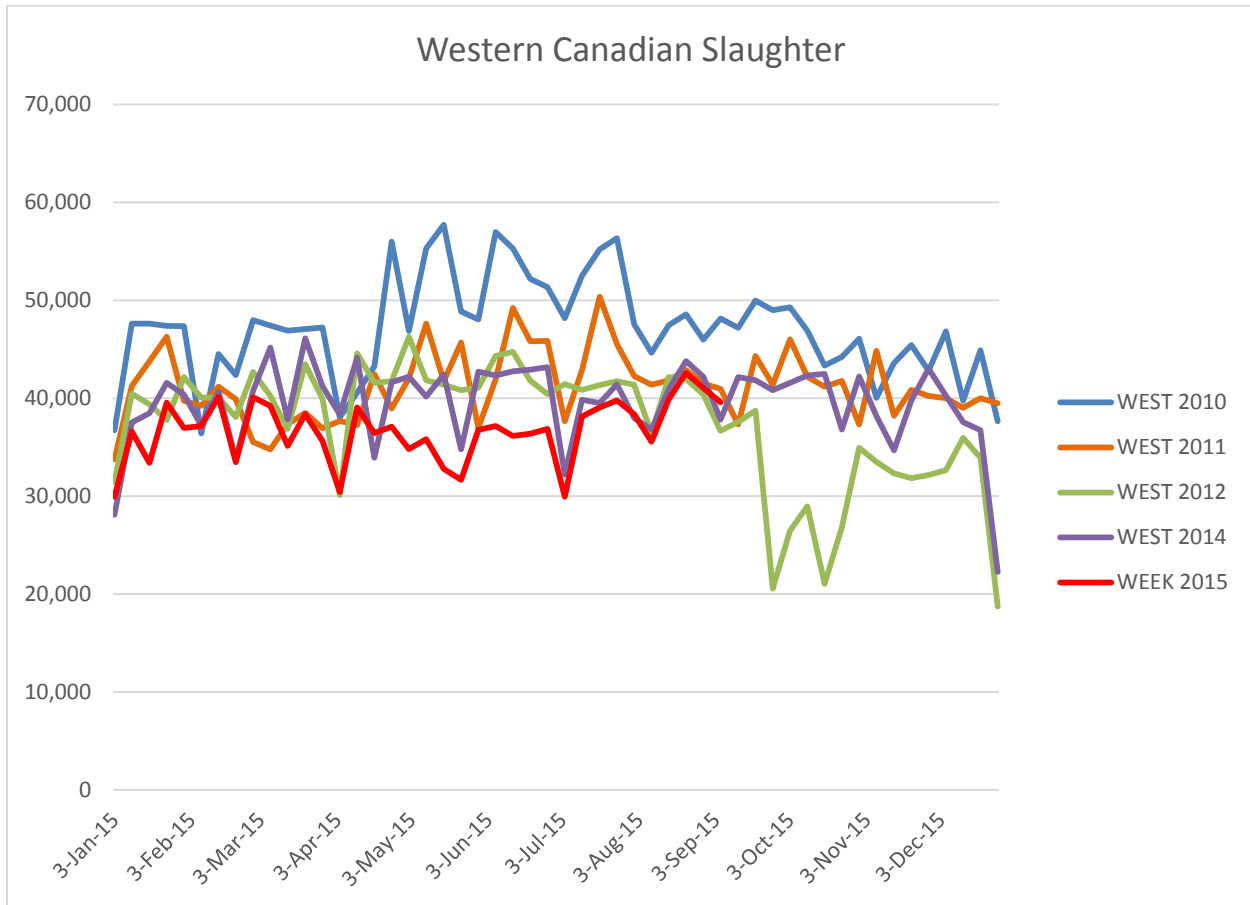
Well confusion reigns in the economics of the Canadian Calf trade. In 2016 we have experienced a significant increase of forwarded contracted calves. This is a new development in the industry as calf prices have reached a level producers are willing to accept offered prices and buyers are fearful of supply enough to want to secure supply earlier than normal. This is not unusual in the United States and is more of the norm for larger operators.

What isn't usual though is the significantly negative profit margin for the buyer created by current calf prices. Buyers are looking at these prices and wondering if the tightness of supplies warrants such a high price while the futures market has been acting rather poor for feeder prices this spring or fat prices this summer. However, given how aggressive Canadian packers were last spring/summer and the profitability experienced over the last 24 months buyers seem willing to take on substantial risk given the previous supply and demand environment.

Supply and demand in a particular region can be seen looking at the basis. Basis means the price in one region compared to either the futures market or the cash price paid in another region. The Live cattle basis in Alberta set historical records in 2015. This was a sign of extremely tight live cattle supplies and more than ample demand from Canadian plants.



Well the slaughter rate tells another story. As can be seen from the chart below fewer cattle were slaughtered in 2015 than any of the last 5 years.



This therefore must mean that demand wasn't the ignition that lit the price up in Western Canada to where Canadian packers were paying up to \$250/hd more than their counterparts in the US. It was in fact a true shortage of supply in the region. This begs the question, will this be fixed as it surely is not sustainable in the long-run. Everyone in the cattle business understands the biology of the cow means that it takes years to rebuild supplies.

This volatility of prices makes it extremely difficult for Alberta cattle feeders to know what to expect for a live cattle price in 2016. Therefore most look to the basis contracts or forward contracts offered by packers for future delivery during the spring/summer of next year. Most of these contracts being offered are near even the futures or even premium the futures exchange. This shows the Alberta packers are very aggressive in finding cattle against this same time period for next year.

The difficult economic equation which is very difficult to explain is can Canadian Packers pay more or even an equivalent price for live cattle as US Packers. Historically the answer has been no they cannot.

Evidence for this was the closure of Calgary XL, Moose Jaw XL, and the sale of Lakeside by Tyson. These closures and sales were done when the basis was much wider. Analysis needs to be done I believe to demonstrate how the economics for the Canadian packer has changed either through a change in kill cost or in the beef price received. This is highly important to determine if the environment is sustainable either to project future live cattle prices in Canada or most importantly if another Canadian packer needs to close or cut capacity?