

The latest chapter in the Zilmax saga unfolded on Friday when Merck Animal Health, the product's manufacturer, announced that it would suspend sales of Zilmax, its product containing zilpaterol. The move comes after two weeks of controversy and concerns over the impact of zilpaterol on the mobility of fed cattle that had received the beta-agonist to enhance lean muscle gain, growth rate and feed efficiency late in the feeding period. The controversy began when Tyson, as the result of several incidences of extremely lame cattle, announced that it would stop accepting cattle fed Zilmax on September 6. That announcement came on the heels of a meeting of beef industry participants in Denver during which some reportedly heated debate was held regarding animal welfare impacts of Zilmax. Reuters reported late last week that a video presented at that meeting by a JBS Swift official had shown cattle "having difficulty walking." That report confirms what we had heard the prior week. Our source indicated that the video was a major cause of the debate at the Denver meeting.

Merck Animal Health stated that the reason for the suspension was to "ensure effective implementation of our five-step plan" referring to the Five-Step Approach to Ensuring Responsible Beef that the company announced last week. That plan includes a scientific audit conducted by independent experts that will "monitor the process of feeding Zilmax and will follow identified cattle from the feedyard to the packing plant" according to the Merck news release.

What does this mean for the beef industry and, more immediately, beef and cattle markets? First, let's consider what Zilmax and Optaflexx, the cattle version of ractopamine, another beta-agonist, caused in terms of weights. The chart at right is purposely cluttered by more data than we normally present to show the sharp increase in fed steer slaughter weights in early 2012. The chart for heifer weights looks almost identical with the vertical axis being slightly different. Note that weekly slaughter weights for 2010, 2011 and the five year period from 2007 through 2011 are quite similar but that weights jumped dramatically in early 2012 — a time period that corresponds well with the widespread adoption of the beta-agonists by U.S. cattle feeders. The year-on-year increase averaged 19.08 pounds per head or 2.2% from February 1, 2012 onward and, as we pointed out last week, persisted even when feed prices jumped to record highs last summer. Weights were higher again for the first five months of this year and have been roughly even with last year since June 1. We think one has to conclude that beta-agonists were a primary driver of this year-on-year production increase of about 2%.

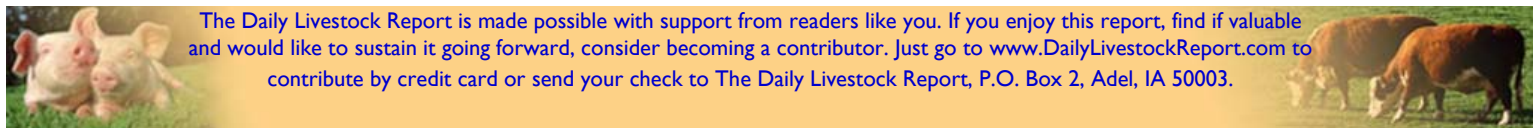
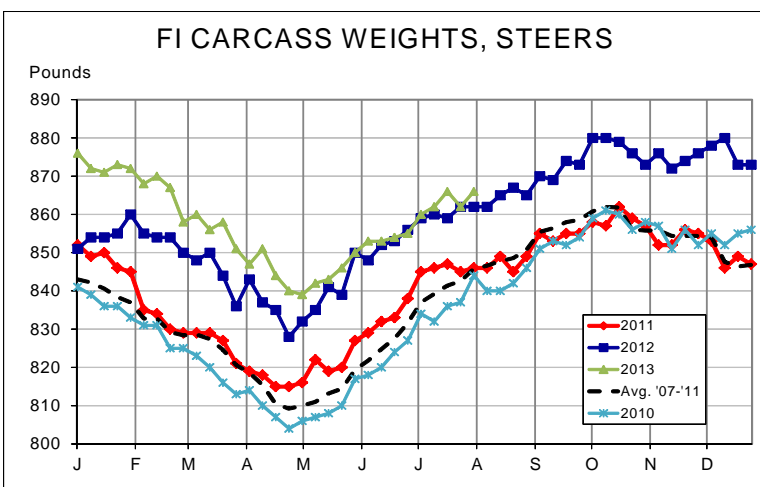
But remember that sales of only one of the two beta-agonist products is being suspended. The economic benefit of these products for both feeders and packers is significant and we expect feeders that currently use Zilmax to switch to Optaflexx. Therefore, not all of that 2% production increase will be lost. According to our sources, switching from Zilmax to Optaflexx will probably reduce weights by 6-8 pounds or about one-third of the increase observed in 2012. Carcass weights have made up for most—and in some weeks, all — of the

reduction in fed cattle numbers so far this year (YTD beef production is down 0.92%) so reducing the weight increase will leave us closer to and, most likely below, last year's output levels. Live cattle futures were up about \$1.20/cwt for the week — a reasonable response, we think, to what we know at present.

What does it mean for technology adoption in the beef industry and, by extension, the livestock and poultry sectors? Merck went through all of the protocols to get Zilmax approved by the FDA, which, according to another Reuters story on Friday, "requires drugmakers to report any adverse events." Lameness was apparently not an issue when the product was approved. USDA, though it monitors animal welfare situations in packing plants, had made no comments about the Zilmax situation and is apparently referring all questions to FDA.

The jury is definitely out on this question. Our initial response is that, to at least some degree, this is the way things should work. When the practical impacts of any product or practice appear to be negative to the well-being of animals, it seems logical to us that the animal's owner has the first responsibility to take action. That is not an indictment of feeders since any observed lameness could have been seen as a "one-off" occurrence. Packers, though, are in a position to see animals from many farms or feedlots and could, quite logically, be the first agents in the product chain to observe a pattern. That a packer observed this should really be no surprise.

The situation also underscores the times we live in. "I'm using an approved product according to the label!" is no longer an acceptable response to concerns over animal well-being. We economists would term approval and proper usage as "necessary but not sufficient" conditions in today's culture. Just as we no longer have the authority to "do what I darn well please" with the animals that we own, we also must judge the impact of approved, safe products on animal and human well-being and take actions appropriate for the times — whether we like it or not.



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PRODUCTION AND PRICE SUMMARY

Week Ending **8/17/2013**

| | Item | Units | Current Week | Last Week | Pct. Change | Last Year | Pct. Change | YTD | Pct. Change |
|--------------|---------------------------------------|---------------------|---------------|---------------|---------------|---------------|---------------|---------------|--------------|
| | Total Meat & Poultry Prod. | Million lbs. | 1706.4 | 1733.9 | -1.59% | 1709.2 | -0.17% | 55,046 | 0.82% |
| C | FI Slaughter | Thou. Head | 617 | 633 | -2.53% | 643 | -4.07% | 20,211 | -1.47% |
| A | FI Cow Slaughter | Thou. Head | 117.6 | 117.1 | 0.45% | 120.9 | -2.71% | 3,762 | 2.03% |
| T | Avg. Live Weight | Lbs. | 1310 | 1307 | 0.23% | 1300 | 0.77% | 1,309 | 1.01% |
| T | Avg. Dressed Weight | Lbs. | 797 | 795 | 0.25% | 794 | 0.38% | 793 | 0.79% |
| L | Beef Production | Million Lbs. | 490.6 | 502.6 | -2.39% | 509.3 | -3.67% | 15,948 | -0.92% |
| E | Live Fed Steer | \$/cwt live wt. | 123.86 | 122.45 | 1.20% | 120.51 | 2.78% | | |
| | Dressed Steer | \$/cwt carcass | 196.86 | 195.95 | 0.46% | 189.50 | 3.88% | | |
| & | OKC Feeder Steer | 700-800 Lbs. | 157.56 | 153.08 | 2.93% | 140.02 | 12.53% | | |
| | Beef Cutout | 600-750 Choice | 192.13 | 187.92 | 2.24% | 190.23 | 1.00% | | |
| B | Hide/Offal | \$/cwt live wt. | 14.18 | 14.14 | 0.28% | 13.24 | 7.10% | | |
| E | Rib | Choice | 299.34 | 288.15 | 3.88% | 279.53 | 7.09% | | |
| E | Round | Choice | 163.52 | 158.76 | 3.00% | 167.28 | -2.25% | | |
| F | Chuck | Choice | 161.55 | 157.48 | 2.58% | 157.09 | 2.84% | | |
| | Trimming, 50% | Fresh | 109.14 | 109.76 | -0.56% | 48.05 | 127.14% | | |
| | Trimming, 90% | Fresh | 201.36 | 199.88 | 0.74% | 210.61 | -4.39% | | |
| H | FI Slaughter | Thou. Head | 2177 | 2019 | 7.83% | 2176 | 0.05% | 68,280 | -0.01% |
| O | FI Sow Slaughter | Thou. Head | 58.0 | 55.3 | 4.95% | 62.9 | -7.75% | 1,731 | -0.08% |
| G | Avg. Dressed Weight | Lbs. | 203 | 203 | 0.00% | 201 | 1.00% | 206 | -0.25% |
| S | Pork Production | Million Lbs. | 441.4 | 409.9 | 7.68% | 437.5 | 0.89% | 14,071 | -0.24% |
| | Iowa-S. Minn. Direct | Avg. | 98.29 | 99.78 | -1.49% | 86.86 | 13.16% | | |
| & | Natl. Base Carcass Price | Weighted Avg. | 98.62 | 98.02 | 0.61% | 89.13 | 10.65% | | |
| | Natl. Net Carcass Price | Weighted Avg. | 101.21 | 100.64 | 0.57% | 91.66 | 10.42% | | |
| P | Pork Cutout | 200 Lbs | 103.57 | 104.96 | -1.32% | NA | #VALUE! | | |
| O | Hams | Primal Cutout | 83.22 | 81.95 | 1.55% | NA | #VALUE! | | |
| R | Loins | Primal Cutout | 105.79 | 107.41 | -1.51% | NA | #VALUE! | | |
| K | Trimming, 72% Lean | Fresh | 75.75 | 97.66 | -22.43% | 70.75 | 7.07% | | |
| | Bellies | Primal Cutout | 177.44 | 186.70 | -4.96% | NA | #VALUE! | | |
| C | Young Chicken Slaughter* | Million Head | 159.38 | 157.64 | 1.10% | 156.08 | 2.12% | 4,908 | 0.73% |
| H | Avg. Weight | Lbs., RTC | 4.20 | 4.33 | -2.93% | 4.20 | 0.00% | 4.3 | 1.46% |
| I | Broiler Production | Million Lbs., RTC | 669.7 | 682.4 | -1.85% | 655.8 | 2.12% | 21,629 | 3.15% |
| C | Eggs Set | Million | 202.1 | 199.7 | 1.16% | 193.0 | 4.72% | 6,406 | 1.71% |
| K | Chicks Placed | Million Head | 165.6 | 168.0 | -1.43% | 162.5 | 1.91% | 5,284 | 0.59% |
| E | National Composite Broiler | Composite | 91.36 | 90.9 | 0.50% | 85.19 | 7.20% | | |
| N | Georgia Dock Broiler | 2.5-3 Lbs. | 105.86 | 104.77 | 1.00% | 94.26 | 12.30% | | |
| | Northeast Breast | Skinlss/Bonelss | 182.18 | 180.64 | 0.90% | 143.48 | 27.00% | | |
| | Northeast Leg Quarters | | 51.43 | 51.86 | -1.70% | 49.21 | 1.70% | | |
| T | Young Turkey Slaughter* | Million Head | 4.35 | 5.61 | -22.54% | 4.58 | -5.15% | 137.8 | -1.79% |
| U | Avg. Weight | Lbs. | 24.09 | 24.78 | -2.81% | 23.27 | 3.51% | 24.7 | 1.12% |
| R | Turkey Production | Million Lbs. | 104.7 | 139.0 | -24.71% | 106.6 | -1.83% | 3,398 | -0.89% |
| K | Eastern Region Hen | 8-16 Lbs. | 99.00 | 99.00 | 0.00% | 108.18 | -8.50% | | |
| F | Corn, Omaha | \$ per Bushel | 6.04 | 5.87 | 2.90% | 8.07 | -25.17% | | |
| E | DDGS, Minnesota | \$ per ton | 211.50 | 217.50 | -2.76% | 302.50 | -30.08% | | |
| E | Wheat, Kansas City | \$ per Bushel | 7.01 | 7.00 | 0.14% | 8.59 | -18.39% | | |
| D | Soybeans, S. Iowa | \$ per Bushel | 14.36 | 13.57 | 5.82% | 17.08 | -15.90% | | |
| | SB Meal, 48% Central Illinois | \$ per Ton | 450.80 | 437.60 | 3.02% | 560.00 | -19.50% | | |

* Chicken & turkey slaughter, production and prices are 1 week earlier than the date at the top of this table. Cow & sow slaughter are for 2 weeks earlier

Source: USDA Agricultural Marketing Service, various reports