

Retail beef prices in March increased compared to the previous month but they were still about 5% lower than the previous year and down 7.9% from the peak in May 2015.

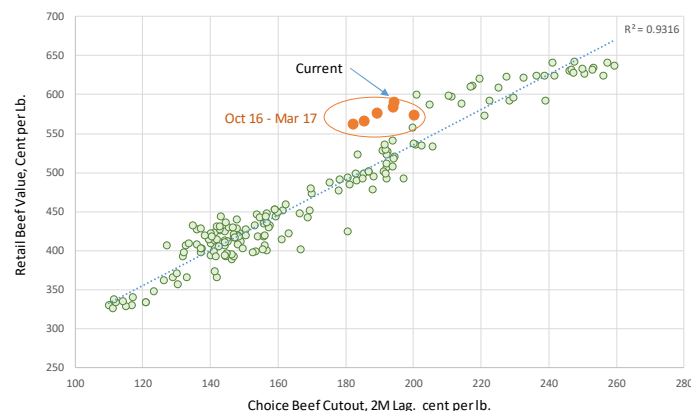
The decline in retail beef prices follows the decline wholesale beef prices at the end of 2016 and early 2017. The chart to the right shows the fairly strong relationship between wholesale beef values, as represented by the choice beef cutout, and the value of beef at retail. We have lagged the choice beef price by two months, in other words, relating the value of choice beef in January 2017 with retail prices in March 2017. What stands out in the last 12 months is that retail beef prices have been higher than one would expect given the long run relationship. Some of this may be due to the retail price data series itself, since it is not weighted by sales volume. The other reason may be due to the fact that wholesale beef prices last fall and winter declined at a fairly rapid clip and retailers have taken their time to adjust. Wholesale beef prices in February declined compared to the previous month but they rose sharply in March. The average choice beef cutout in March was \$216/cwt, 13% higher than the previous month but still about 4% lower than the previous year. So far in April the choice beef cutout has averaged \$210/cwt, 4% under last year's levels. Market participants in the futures markets are now likely pondering what effect the stronger than expected cutout values will have on retail prices and eventually the amount of beef consumers will buy. Because retailers took their time in adjusting prices lower, it appears unlikely to us that we will see a notable increase in retail beef prices this summer. Some of the speculation that higher prices will kill beef demand may be overstating the case a bit. What may be a bit more problematic for beef demand, especially once we move past the key summer holidays (Memorial Day, 4th of July) is the price of competing proteins and beef trade flows. So far this year beef supplies available in the domestic market have increased but not as much as one would expect if you were simply looking at the slaughter numbers. For now retailers and foodservice operators are in full swing preparing for the seasonal improvement in demand that comes from warmer weather. Consumer confidence is at the highest level it has been in almost a decade and consumer disposable income growth has returned to pre-recession levels. The unemployment rate is at 4.5%. In other words, these should be good times for beef demand and retailers could opt to keep prices in check (after all their margins are still good) and capitalize on consumer willingness to indulge as the grilling season gets underway.

Retail pork prices were sharply higher in March, largely due to the run-up in the price of bellies the previous month.

Pork retail value for the month of March was pegged at \$3.78 per pound, 3.8% higher than the previous month and 0.5% higher than the previous year. Bacon prices at retail have reset rather sharply and help explain what is now happening with belly prices at wholesale. It was a scenario that we considered back in February when belly prices spiked (remember the belly shortage brouhaha). What is unfortunate is that pork prices are above a year ago at

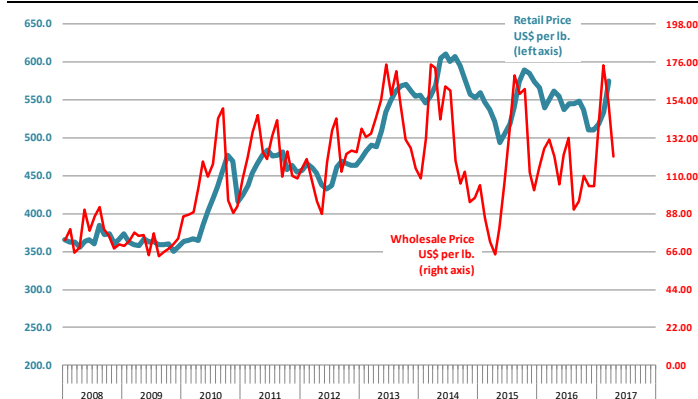
Choice Beef Cutout (Lagged 2Months) vs. Retail Beef Value. 2002-2017

Data Sources: Cutout from USDA MPR System. Retail Value Calculated by USDA/ERS



WHOLESALE PORK BELLY PRIMAL VALUE VS. THE PRICE OF SLICED BACON AT RETAIL

Data Source: USDA MPR Prices and BLS Retail Price Series



a time when pork production is up +6% and pork exports are about flat with last year (this is based on our forecast for April exports not exports in Jan/Feb). The result is continued weakness in the pork cutout, most of it due to the sharp deflation in the wholesale value of bellies. The chart above shows that bacon prices at retail generally move a bit higher even as wholesale prices start to decline, reflecting the lag in the price transmission through the supply chain. In the past we also have seen belly prices continue to decline through April but eventually the low price becomes attractive enough to get retailers to start featuring bacon again for the summer months. Right now futures are pricing a fairly bearish outlook for pork prices in June, July and August, with implied cutout values at around \$80/cwt (hogs at 72.9 for July). This would indicate a belly value around \$125, a very small premium to current market.

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