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US beef market poses threat to New Zealand returns this year – visiting expert

The likely forced slaughter of US cattle due to drought is set to pressure global beef trade and prices, posing a threat to New Zealand beef returns, a visiting North American cattle industry expert has warned local producers.

Rabobank's US senior animal protein analyst Don Close, who has been in New Zealand this week for a series of presentations, said forced herd liquidation in the United States – along with the risk of recessionary pressures in the US economy – would directly impact New Zealand producers.

"The US is both the dominant export destination for New Zealand beef, as well as a fierce competitor with New Zealand in other export markets, including Japan and South Korea, he said. "In addition, the United States and New Zealand, along with Australia, will potentially be fighting it out for market share in China in the future."

Too many cattle

Mr Close – who is based in St Louis, Missouri – said the US beef herd had staged an aggressive rebuild in recent years, with the majority of stock located in parts of the country under severe drought stress.

"After bottoming out at 28.7 million cows in 2014, there has been aggressive herd rebuilding and the US beef herd is now sitting at around 31.7 million head. And I estimate this cycle will peak somewhere between 32 million and 32.5 million head," he said.

"However, currently 70 per cent of our US beef herd are residing in areas of extreme drought. While we still have a window of opportunity for rain, the likelihood we will see some level of forced liquidation before the end of the US summer is very high. If we see cow slaughter rates increase because of forced liquidation, there is a very real risk that there will be too many cattle for the system."

Currently, beef cow slaughter rates are up 10.5 per cent above year ago levels, but this could rise to between 12 and 15 per cent, he said. Compounding the number of beef cattle on the market is the liquidation of dairy cows, with the poor economic returns for US dairy farmers.

Mr Close said with US production of beef – and also pork – up by five per cent, there was "a tonne of protein coming at us" in the US, but also globally.

"New Zealand is going to have to work harder to find a home for their product in the US," he said. "Already we have seen New Zealand and Australia's share of total US beef market fall from between 12 and 14 per cent, down to four per cent, because the US is generating more of its own beef."

US competition

US product is also generating a premium over New Zealand beef, Mr Close said.

Reducing the incentive to buy New Zealand product, he said, this was creating vulnerability for New Zealand's beef exports into the US, but also in key export markets.

"In 2017, the US exported 11.06 per cent of their beef production, a 'monster number' as beef exports have never been above 10 per cent, and we have broken through the glass ceiling that was limiting exports," he said.

"With total US protein now at levels we can't consume all at home, the US dependency on exports is becoming increasingly important."

And this will have a significant impact on New Zealand as an export-oriented producer, he said, with New Zealand exporting around 80 per cent of its production.

Recessionary pressures

While the US was currently enjoying its second-longest period of economic expansion in history (at 108 months), Mr Close said, the market would likely be "stress-tested" by recessionary pressures in the near future.

"I have very serious doubts that we will reach the all-time record of 120 months, as we are starting to see the yield curve flatten out close to parity or even discount, with virtually full employment creating inflation," he said. "So within the next year or 18 months, the likelihood of US recessionary pressure is very high."

Mr Close said this recessionary risk, together with increasing gasoline prices, was likely to impact US consumers' discretionary income, and their demand for beef – particularly more premium cuts – at a time when US beef production was on the rise.

Positive longer-term outlook

Despite the headwinds facing US and global beef markets, Mr Close remained bullish about the longer-term outlook for global beef, saying he had never in his 45-year career "seen the global marketplace as exciting and ready for change".

"While there will be downward pressure on beef prices this year, the global beef market remains dynamic, with increased activity in trade and changing suppliers as global demand for beef continues to expand," he said. "The overall direction will be driven by the increasing demand for animal protein. And we are talking about the 300 million in China's emerging middle class, but also South-East Asia and southern Africa – where the opportunities are incredible.

"We are also seeing rapid changes in consumer demand, and the insatiable demand for convenience. Rarely a day goes by without a new development in home delivery or meal kits."

Responsible for analysing the beef and animal protein sectors for Rabobank in the United States, Mr Close's wealth of experience spans high profile roles at Texas Cattle Feeders Association, AzTx Cattle in Hereford, Future Beef Operations and Pioneer Hi-Bred International.

Rabobank New Zealand animal proteins analyst Blake Holgate said while New Zealand manufacturing beef going into North America would be put under pressure by increased US cow kill and production, prime cuts exports would be sheltered to a certain degree by demand in the higher-value Asian markets, particularly China.

"Almost half (47 per cent) of New Zealand's beef exports (191,000 tonnes) went to the United States in 2017 – primarily in the form of manufacturing beef. China, New Zealand's second largest, export market accounted for 21 per cent of total beef exports," he said.

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