IOWA STATE UNIVERSITY
Extension and Outreach

Iowa Farm Outlook

Department of Economics
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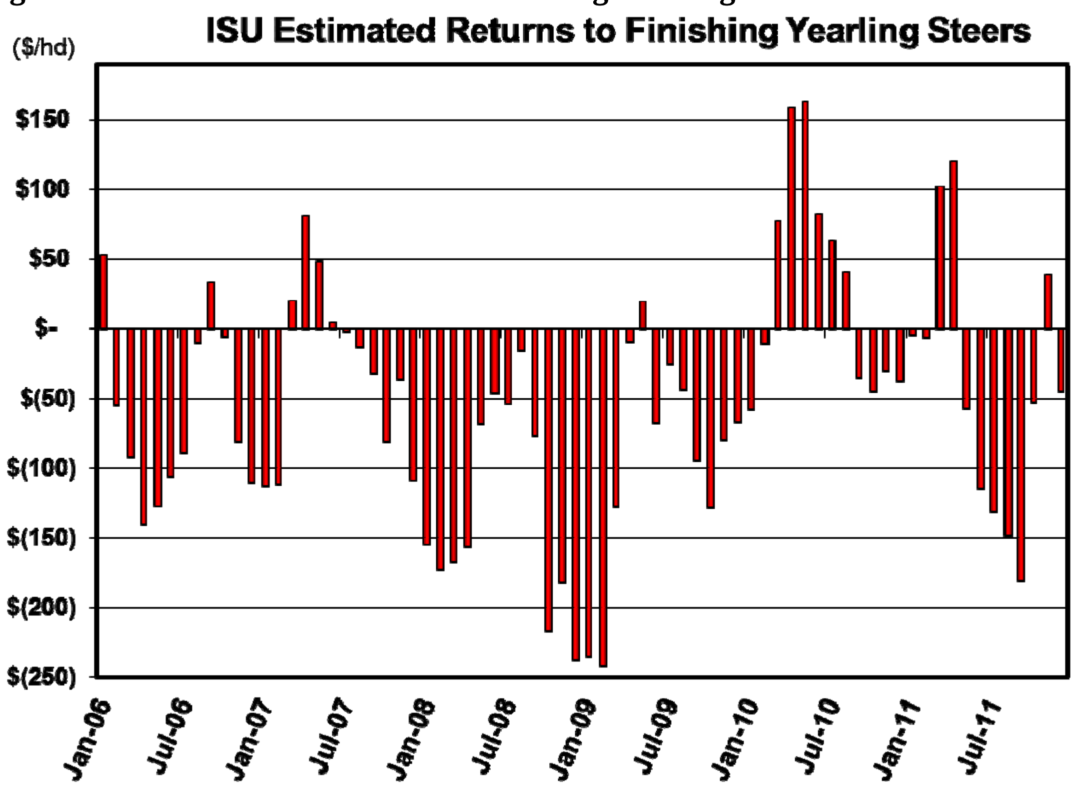
2012 Holds a Mixed Bag for Cattle Feeders

Feeding cattle had its high and low points of profitability last year. Based on the Iowa Estimated Returns, a barometer of economic profitability, finishing yearling cattle last year netted an average loss of $40/head. The brightest point of the year was during the spring when returns edged past $120/head profit for cattle sold in April. This short period of profitability was cut short by a combination of increasing feeder cattle and feed costs coupled with mundane fed cattle prices. Profitability hit a low point of a $180/head loss on cattle sold in September. Profitability returned for a fleeting moment in November when high quality beef cuts surged in value.

The choice-select price spread widened to more than $18/cwt. during October and November. This strong upsurge in beef prices made it difficult for retailers to feature beef cuts and still turn a profit. As a result the demand for beef has started out the year more like a lamb and less like the lion that many had anticipated a few months ago. Rather than continued strengthening of demand for beef in the coming year, a stable status quo is becoming more likely. At current prices, profit margins on retail beef sales are narrow at best, leaving incentive to increase sale volumes. For packers and feeders, the profitability situation is rather grey to start out the year, as neither sector is in a position to turn a profit at recent prices. Packers have been losing $35-45/head, on an operating basis, and they still have plenty of beef yet to sell. The choice-select spread has narrowed up to less than $10/cwt. as a strong supply of choice beef is getting ahead of demand. February and early March are usually when beef demand is at its weakest during the year, which leaves us with a continued bearish short-run cash market.

Figure 1. ISU Estimated Returns to Finishing Yearling Steers



Cattle that are currently on feed will likely to turn a modest profit, and as can be expected the cattle marketed in March through June will likely produce the largest returns for the year. Based on recent futures market prices, fed cattle may reach $130/cwt. during late April and May, and then remain north of $125 for the duration of the summer. By November there could be a reemergence of $130/cwt. fed cattle to finish out the year. Keep in mind that these cattle prices are likely to deteriorate with any major disturbance in the general economy. This remains the "800 pound bear in the room".

Adding bullish pressure to the market is the expected decline in beef production during the year. Despite the increased supply of beef currently being offered by packers, the actual quantity of beef being produced is expected to be lower in each quarter of 2012. Both fed cattle marketings and feeder cattle placements were predicted by analysts to be lower in December, while cattle on feed inventories remain about 3 percent greater than those of a year ago. The USDA January WASDE report predicts a 4.6 percent reduction on the production of beef in this year compared to last. The third quarter could see a 6 percent reduction in beef production compared to the same time period last year, as the current decline in placements will affect the availability of finished cattle during the late summer months.

The January cattle report for beginning of the year inventories reported the expected declines in total cattle numbers. There are now less than 91 million head of cattle in the US, and less than 30 million head of those are production beef cows. The supply of beef feeder cattle continues to decline, while cattle on feed inventories are slightly higher than a year ago. While numbers are up, the supply of finished animals is expected to be substantially lower nearly every quarter of 2012. Beef heifer retention was up slightly from last year but was still 4 percent lower than the quantity seen at the beginning of 2010. In short, cattle numbers are still lower, beef supplies will be down, and while there are early signs of an expansion beginning to phase in we may see declining beef supplies for the next 3 years. Table 1 contains a summary of the January cattle report.

Table 1. Summary of January 2012 Cattle Report

	Million Head	% Change
All Cattle	90.8	-1%
Beef Cows	29.9	-3%
Beef Replacement Heifers	5.2	+1%
Dairy Cows	9.2	+1%
Dairy Replacement Heifers	4.5	-1%
Other Heifers	9.6	-2%
2011 Calf Crop	35.3	-1%
Cattle on Feed	14.1	+1%

Shane Ellis

Dairy Outlook Overview

Milk price is driven by simple economics of supply and demand. United States milk supply continues to increase over time with increased milk output per cow and an expanding cow herd. Demand outlook for dairy products in 2012 is not favorable due to increased global milk supply and minimal growth in national demand. Producer profit margin outlook is marginal for 2012 due to suppressed milk prices and feed commodity markets remaining strong.

Milk Supply: Production continued to increase in 2011 with annual production closing out at 196,057 million pounds, 1.76 percent increase from 2010. Annual Iowa milk production ended the year at 4.345 million pounds, up 0.18 percent from 2010. Milk production per cow continues to increase at an average of 1.7 percent per year. For 2011, production per cow equaled 21,335 and 21,305 pounds for the U.S. and Iowa, respectively (approximately 73 pounds per cow per day tank average). Annual gain of milk production per cow comparison across states, Iowa ranked second among the 23 dairy states at 560 pounds behind Texas at 820 pounds.

The total number of milk cows in the U.S. is just under 9.2 million cows in December 2011, up 80 thousand cows from the year prior. Growth in cow inventory occurred in the southern high plains, western, and upper northwest regions. Replacement heifer inventory is down one percent at 4.5 million head. The largest two-year increase in heifer inventory since the early 1980's occurred in 2009-2011, at a gain of 250,000 head. Those heifers started to enter the cow herd in 2011 and those heifers will be freshening through mid-year.

Figure 1 Iowa Milk Cow Inventory vs. Annual Milk Production

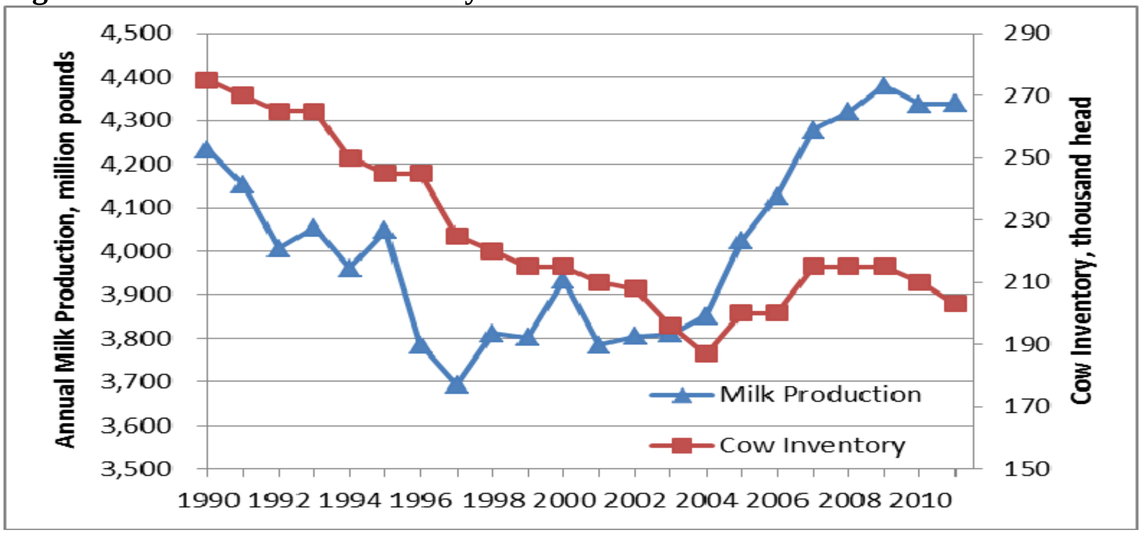


Figure 1 shows milk production and cow inventory for Iowa over time. Annual milk production has increased in the last decade with a slight decline after 2009. Cow inventory has subsided in the past few years to 203,000 head at the end of 2011; however increased milk production per cow has allowed milk production to remain steady.

Continued growth in milk production per cow, strong heifer inventory, and expected growth in cow inventory could increase U.S. milk production by up to 3 billion pounds. Factors that may decrease this influx in milk supply include current feed quality and availability across regions and weather cycles that will affect 2012 feed crops.

Milk Product Demand: Demand for milk commodities in 2011 was strong due to increased activity in the export markets; leading export markets are Mexico, Southeast Asia, and Canada. Total exports equaled $3.96 billion in export product; total export products are equivalent to over 13 percent of the milk solids at the farm level. Drivers behind export demand in 2011 were decreased global milk supply due to New Zealand and Australia experiencing drought conditions early in the year, increasing population and middle class in Asian countries, opportunities to enter into markets based on foreign policy decisions (South Korea market), and a weak dollar value. Protein enriched products and associated global demand from Asian countries in late summer months helped to drive dairy product prices and milk price received by producers.

The stated factors will continue to affect global demand into 2012. However, Australia and New Zealand are recovering from the drought and supplying more milk into the global market while the strength of the Euro and economy of the EU continues to be in question causing uncertainty in the strength in global exports for 2012. Product innovation for convenience, nutrition, and consumer needs in new markets may be vital to increase demand both nationally and globally to meet the increase in milk supply entering the market.

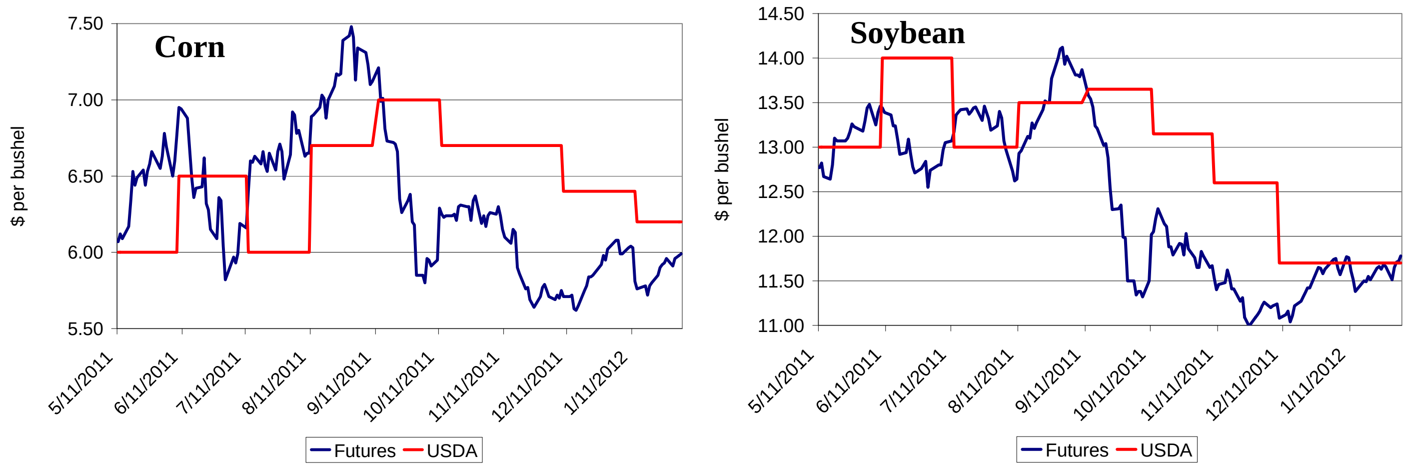
Dairy Profitability: The U.S. All Milk Price for January was $19.60 per hundredweight; a record high was set in August at $22.00. Iowa producers saw a $0.10 gain on All Milk Price at $19.70 in January. Iowa producers typically see about a $2.00 positive basis between All Milk Price and Announced Milk Price, based on CME closing futures price. Milk futures have taken a negative turn for 2012 in the past few weeks with prices in the $16-17 range. These milk prices with corn prices rallying in the $5.50-$6.50 range and reduced hay stocks will create tight margins for dairy producers in 2012. Producers may experience marginal positive gains on a cash basis, but net returns including debt, depreciation, and opportunity cost on investments may result in negative margins based on ISU Dairy Budget calculations. Margin management and maintaining or improving production levels will be important for producers to remain profitable in 2012.

Kristen Schulte

Another Profitable Outlook

The 2011 crop year will remembered for several reasons, the flooding along the Mississippi and Missouri Rivers, the drought that plagued the Southern Plains, and the myriad of weather events (hail, wind, freeze) that lowered crop yields and production nationwide. But despite all of those problems, 2011 will also be remembered as a very profitable year for Iowa crop producers. The 2011 Iowa corn crop had the 4th highest yield on record, the 3rd largest production, and, based on current prices, is the most valuable corn crop we have ever produced. Currently, the 2011 Iowa corn crop is projected to be valued at over $13 billion. The previous record is the 2010 Iowa corn crop at $11.7 billion. For Iowa soybeans, the 2011 crop had the 5th highest yield and only the 11th largest production, but is the 2nd most valuable soybean crop we have ever produced. The 2011 Iowa soybean crop is projected to be worth over $5 billion, only the 2010 soybean crop was worth more.

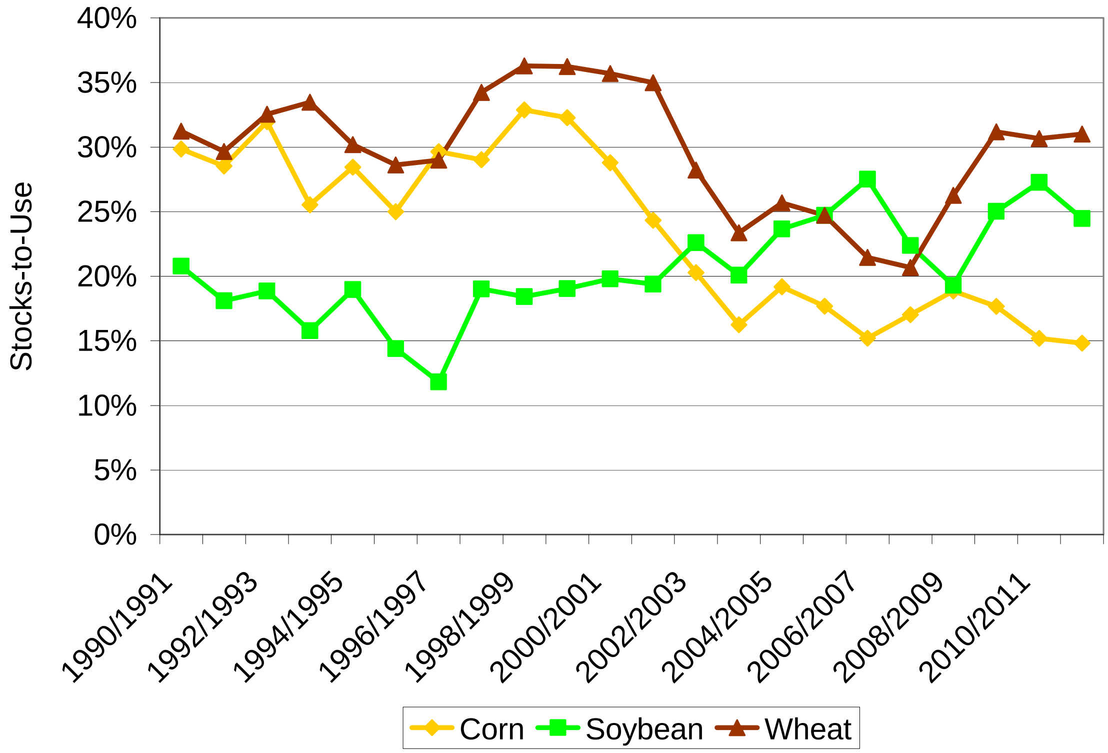
Figure 1. Projected 2011/12 Season-Average Prices



Using the ISU Extension production cost estimates as a guide, it costs roughly $4 per bushel to produce the 2011 Iowa corn crop and $9.67 per bushel for the Iowa soybean crop. So the projected season-average prices for the 2011 Iowa crops can cover costs and provide returns of over $1.50 per bushel for both crops. Based on those returns, USDA has forecast that U.S. agriculture will receive record net farm income in 2011, topping $100 billion for the first time ever. Iowa net farm income in 2011 will also likely be a record.

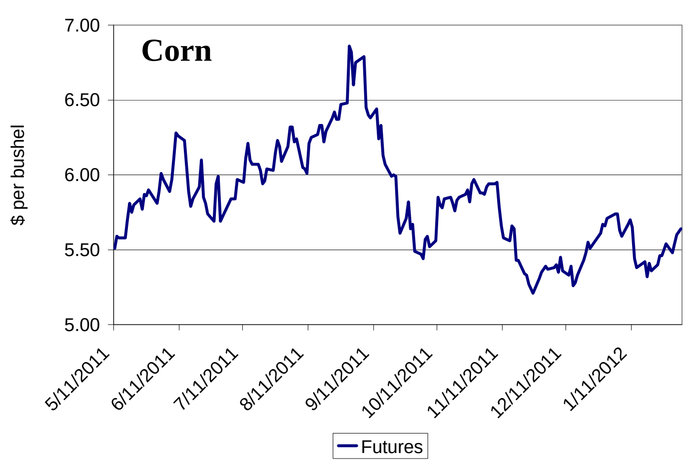
However, as Figure 1 shows, while returns are very good right now, they are also highly variable. Crop prices during the last half of 2011 have mostly been on the decline. Corcerns about the global economy, in combination with the U.S. harvest, sent crop prices tumbling through September and October. Since then, the corn market has oscillated between $5.70 and $6.40 and the soybean market has bounced between $11 and $12.50. As we move into the 2012 planting season, I see two big factors shaping crop prices. The first is the global economy. As we experienced this fall, the markets will react quickly and decisively if traders sense weakness in crop demand. The Europeans are still wrestling with debt problems; the Chinese are still dealing with inflation; and we continue to see slow job growth (although the latest numbers look promising). Crop demand has been the big driver of the crop markets over the past few years. With ethanol leading the charge for corn and exports doing the same for soybeans, demand for our crops has been enough to absorb all we could produce recently. But ethanol's growth has slowed and soybean export demand has fallen off with China's inflation problems. World crop stock levels are relatively high for most crops as well. As Figure 2 shows, the wheat stocks-to-use ratio has been high for the last couple of years. Soybean stocks have been on a general increase over the past decade. Only the corn stocks-to-use ratio would be considered low right now.

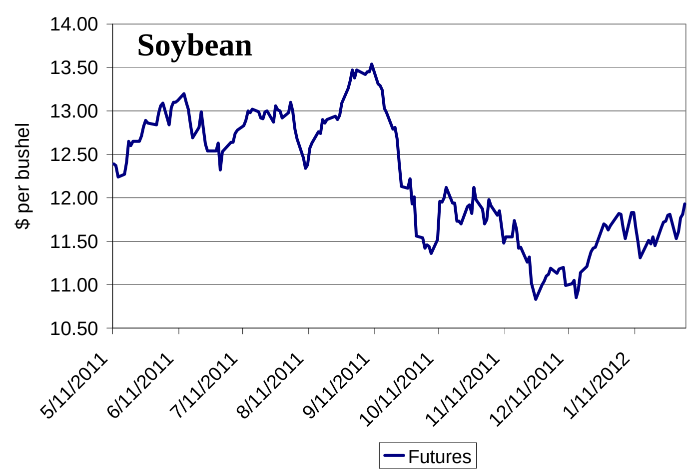
Figure 2. World Stocks-to-Use Ratios (Source: USDA-PSD)



At the same time though, there are significant questions on the supply side as well. Global weather is the second factor shaping crop prices. The La Niña that impacted last year's crops is still around, affecting the South American crops and setting up to possibly affect our upcoming crops. USDA's January estimates indicated the drought and high temperatures in Argentina have reduced potential production there. That production reduction helped spur crop prices higher in the later half of December and have continued to provide support as we move into spring. Meanwhile, here in the U.S. soil moisture is limited in the northern Corn Belt. Those conditions point to potential lower yields here this coming crop year and are providing upward price pressure.

Figure 3. Projected 2012/13 Season-average Prices





With these two factors pushing in opposite directions, the markets have been on a see-saw recently, up on weather news and down on economic news. As the economic and weather factors will not be resolved very soon, the near-term pattern is for the markets to continue to ride the see-saw. So we can expect continued high price volatility for awhile. Figure 3 shows the projected 2012/13 season-average prices, based on futures prices over the past eight months. As with the 2011 crops, projected prices were higher this summer and fall, but good prices are still available. ISU Extension's production cost estimates for 2012 are $4.41 per bushel for corn and $10.96 per bushel for soybeans. With 2012/13 season-average prices in the $5.60 range for corn and $11.90 range for soybeans, 2012 is shaping up to be another profitable year. But the swings in prices could be very dramatic this year, making risk management very important. Crop insurance is always a good risk management tool, but given the current weather situation and outlook, it may be doubly important this year. With the chance for lower yields also comes the likelihood for higher prices, so marketing tools that leave upside price potential should be attractive for 2012 as well. Options, while high priced given the price volatility, offer a quick way to put in a price floor and capture those possible higher crop prices.

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