IOWA STATE UNIVERSITY
Extension and Outreach

Iowa Farm Outlook

Department of Economics
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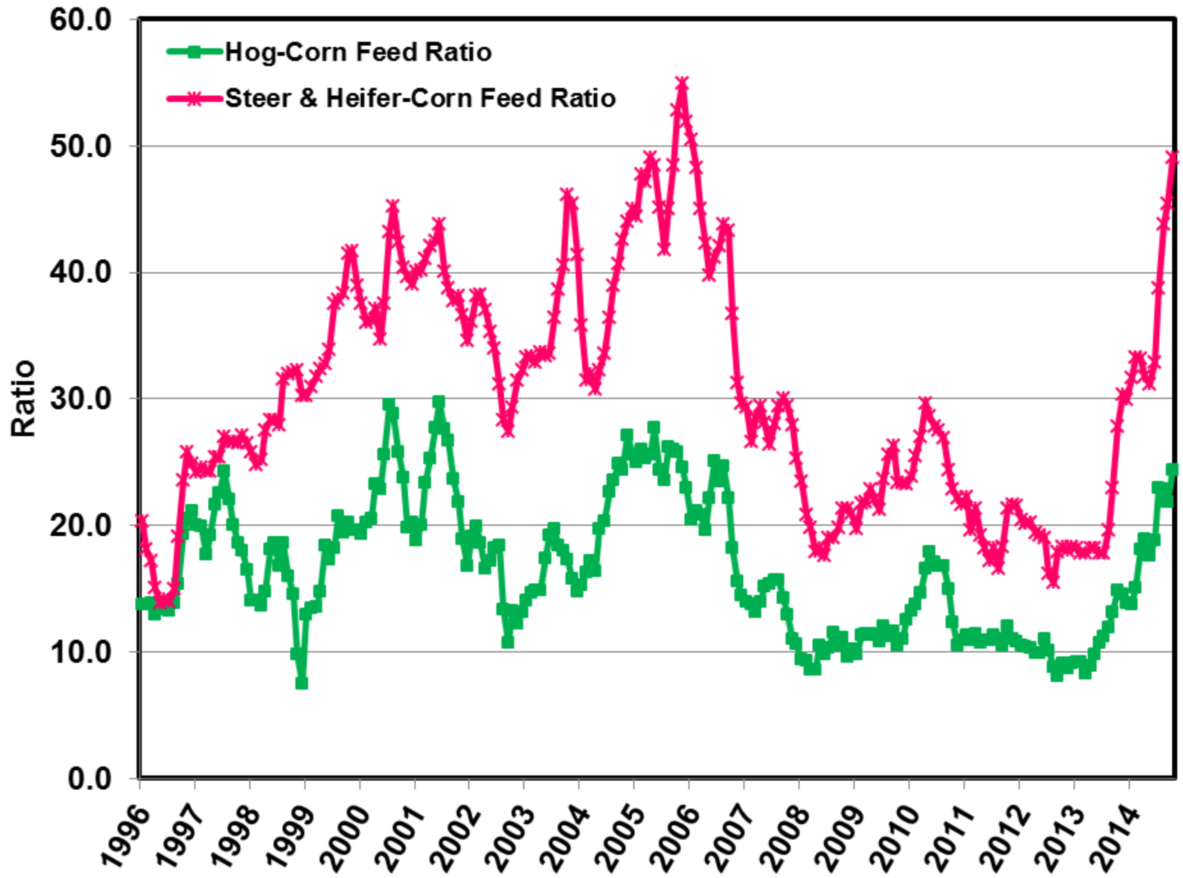
Profit Situation and Outlook in Cattle and Hog Finishing

Conditions in the cattle and hog finishing have improved dramatically in the past year after bouts of significant red ink during parts of the last several years. Those periods, of course, were characterized by significantly higher feed costs and, in some periods, relatively low output prices. Producers have long used ratios of livestock prices to corn prices or feed prices to gauge profitability. The steer & heifer-corn and hog-corn ratios have now returned to levels that, even relative to long-run historical levels indicate profits (figure 1). The October ratio for cattle was 77% higher than one year ago. The hog ratio was 64% higher than one year ago.

Figure 1. Cattle and Hog Price-Cost Ratios



Data Source: USDA-NASS.

Looking at the livestock price to feed price ratios most would conclude that it was a profitable year for cattle and hog finishers, and it certainly was. However, significant variation around the trend line makes it difficult, if not impossible, to predict profitability into the future from this method. Furthermore, these ratios fail to capture feeder prices which are a significant share of the total cost of production and are volatile, adding to a producer's risk. Given the current market environment, i.e., one of relatively tight feeder supplies, lower feed prices, and strong output prices, feeder cattle and pig markets are reflecting what a buyer "has to pay" for feeders as opposed to what a buyer "could pay" for feeders.

Cattle feeders have realized near record profits on closeouts this year but are in the process of bidding future profits into the feeder cattle market. Recent estimates of closeouts offered in the Iowa State University Estimated Livestock Returns Series — Finishing Yearling Steers — indicate steers sold in September at a profit of $218.05/head. This marks the ninth consecutive month of closeouts with profits exceeding $150/head. These positive returns essentially reflect the substantial increase in fed cattle prices relative to expectations when feeder cattle were purchased, at levels much lower than current prices. While this run of very strong returns so far in 2014 is certainly welcomed by feedlot operators, a word of caution follows current projections for fed cattle scheduled to be marketed in the coming year. As shown in table 1, net returns are expected to turn much lower and actually negative in 2015 — if current futures market prices prove to be a true prediction. This sharp reversal reflects the notable increase in feeder cattle prices and the corresponding lack of further increases in expected fed cattle prices. This table also includes the projected and breakeven values for cattle prices and cost of gain which provide insight into both input and output price risk and the corresponding relationships.

Table 1. Historical and Projected Values of Finishing Yearling Steers in Iowa

Closeout Mo-Yr	Net Return*	FCOG**	Fed Price	Feeder Price	Breakeven FCOG**	Breakeven Fed Price	Breakeven Feeder Price
Sep-14	218.05	83.02	157.33	182.75	122.66	140.56	211.83
Oct-14	321.24	80.06	167.69	189.12	138.47	142.98	231.95
Nov-14	205.89	76.55	165.38	203.06	113.99	149.54	230.51
Dec-14	67.97	75.15	165.54	222.77	87.51	160.31	231.83
Jan-15	33.17	74.71	164.72	226.31	80.74	162.17	230.74
Feb-15	-20.85	74.96	163.92	231.95	71.17	165.53	229.17
Mar-15	-102.09	75.24	164.53	243.62	56.68	172.38	230.01
Apr-15	-12.16	75.56	166.98	235.64	73.35	167.92	234.02
May-15	-55.56	75.67	159.36	228.15	65.57	163.64	220.74
Jun-15	-72.91	76.08	158.17	228.09	62.83	163.78	218.37
Jul-15	-130.17	76.51	152.00	224.71	52.84	162.01	207.36
Aug-15	-143.61	77.05	152.09	226.27	50.94	163.14	207.12
Sep-15	-157.61	78.09	151.78	226.83	49.43	163.90	205.82
Oct-15	-160.26	78.58	152.44	227.97	49.44	164.77	206.60
Nov-15	-131.24	78.95	154.03	226.58	55.09	164.12	209.08
Dec-15	-135.98	79.25	154.19	227.28	54.53	164.65	209.15

Notes: * Net return is $/head and all other values are $/cwt. ** FCOG = Feeding cost of gain. Projections made October 31, 2014 using the Iowa State University Estimated Livestock Returns Series.

Iowa State University estimated wean to finish returns for September exceeded $32/head and this sector of the industry could continue to realize strong profits in 2015. Even though current projections for wean to finish production suggest 2015 could be a profitable year, there are several risk factors including price volatility in both input and output markets and any impacts of Porcine Epidemic Diarrhea virus (PEDv) on weaned pig prices.

Producers are encouraged to carefully compare their own costs and prices with those reported here. The Iowa State University Estimated Livestock Returns Series assumes a "hand-to-mouth" cash based process of procuring inputs as well as selling livestock. That is, the calculations purposely assume no risk management, forward pricing, or other strategies are in-place for operations. While this approach is used to provide a barometer over time for profitability trends, it fails to capture notable variability in operation specific situations and managerial approaches.

Table 2. Historical and Projected Values of Wean to Finish Production in Iowa

Closeout Mo-Yr	Net Return*	FCOG**	Lean Hog Price	Wean Pig Price*	Breakeven FCOG**	Breakeven Lean Hog Price	Breakeven Wean Pig Price*
Sep-14	32.62	45.05	106.85	67.52	57.70	90.74	100.14
Oct-14	31.31	44.12	102.46	62.34	56.26	87.00	93.64
Nov-14	4.08	42.53	84.26	56.83	44.11	82.25	60.91
Dec-14	3.09	42.23	85.48	61.05	43.43	83.95	64.14
Jan-15	-4.46	41.69	82.07	63.08	39.96	84.27	58.62
Feb-15	12.18	41.61	86.28	55.20	46.33	80.27	67.38
Mar-15	14.16	41.10	85.01	51.93	46.59	78.01	66.09
Apr-15	23.97	41.07	85.90	44.03	50.36	74.06	68.00
May-15	26.81	41.26	87.82	44.58	51.65	74.58	71.39
Jun-15	34.66	41.46	91.95	44.58	54.90	74.84	79.23
Jul-15	31.46	41.32	90.51	45.20	53.52	74.97	76.66
Aug-15	24.38	41.23	87.90	47.25	50.68	75.86	71.63
Sep-15	5.03	40.90	77.51	46.41	42.85	75.03	51.44
Oct-15	4.26	40.98	76.53	45.00	42.63	74.43	49.26
Nov-15	-2.90	40.67	69.64	39.00	39.54	71.07	36.10
Dec-15	-1.30	41.00	70.85	39.00	40.49	71.49	37.70

Notes: * Net return and wean pig price is $/head and all other values are $/carcass cwt. ** FCOG = Feeding cost of gain. Projections made October 31, 2014 using the Iowa State University Estimated Livestock Returns Series.

Lee Schulz

The Bounce in Futures Prices

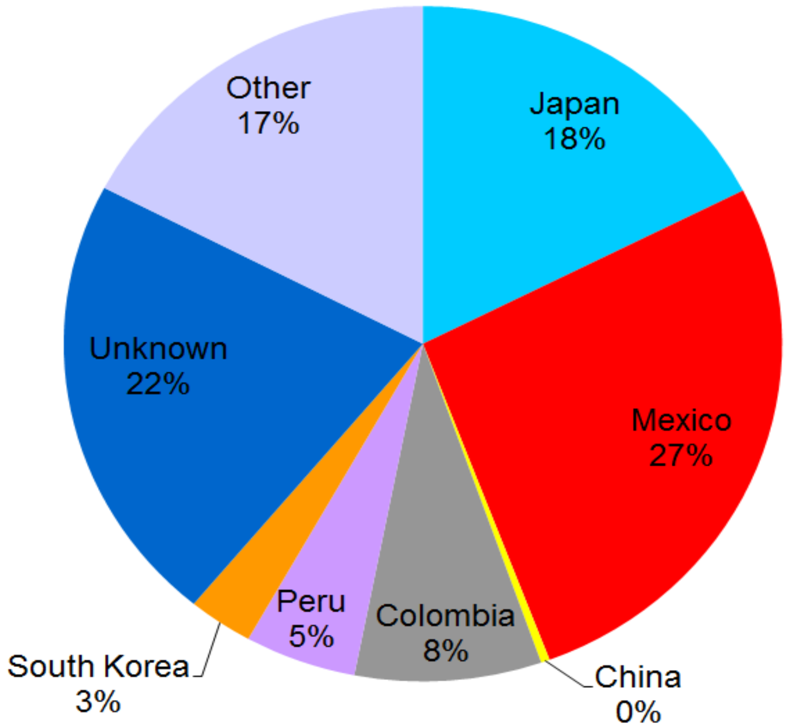
The month of October provided a bounce back for the 2014 crop outlook. While supplies are still more than ample, the trade has shifted its focus to demand. And that shift has put prices on an upward march. The price recovery has come just as the bulk of the Iowa crop production exits the field.

The slow pace of harvest has assisted the price recovery. Both the corn and soybean harvests are running behind schedule. As of October 26, 36% of the Iowa corn crop and 46% of the national corn crop had been harvested. Typically, 65% of the Iowa and the national corn crop by then. So the massive 14.5 billion bushel crop is slowly making its way into the marketing chain. The soybean harvest is closer to typical, but still behind. The 5-year average harvest pace by this time is 85% of the Iowa crop and 76% of the national crop. Instead, we’re at 81% of the Iowa soybean crop and 70% of the national crop. With harvest running behind, the pressure at local elevators and delivery points has been slightly less than expected.

At the same time, demand for corn and soybean is about as strong as it has ever been. USDA’s current demand projections show sizable growth in feed and residual usage for corn, near record usage for ethanol production, and a small increase in food and seed demand. For soybeans, domestic crush is approaching 1.8 billion bushels, based on expansions of the pork and poultry industries. But a key to any continuation of the price rebound will be international demand.

Figure 1 shows the active international buyers of U.S. corn so far this marketing year. Corn export pace is roughly the same as last year. But there has been a definite change in the markets U.S. corn is entering. Last year, China was a significant buyer of corn, representing roughly 10 percent of the international market. This year, China has retreated from the corn market as a dispute over genetically modified corn continues. But those lost sales have been replaced in other markets. The development of trade agreements with South American countries has been boosting prospects for increased sales. Colombia and Peru have stepped forward as major markets for the 2014 corn crop. Sales to Japan are also on the rise. Overall, USDA projects corn exports to dip slightly during the current marketing year. However, given the still relatively low prices and the emerging markets for corn, the potential is there for corn export demand to fall in line with the other demand lines and grow as we move into 2015.

Figure 1. Corn export sales. Source: USDA-FAS.



For soybeans, the export demand picture continues to rely on China. As Figure 2 shows, China continues to be the majority buyer for U.S. soybeans. But the growth in soybean exports is more broadly based than that. The European Union, Mexico, Indonesia, and Taiwan have also increased their purchases of soybeans. Overall, soybean export sales are running approximately 5% ahead of last year's pace. And that would put soybean exports are record pace once again. The soybean market has enjoyed strong international demand for the past several years and that pattern pushes through to today.

Over the course of the month, the trade has internalized the record crop supplies and has refocused on the record usage projected for the crops. Both the corn and soybean markets found their bottom near the 1st of October. And as we celebrated Halloween, crop prices had risen to levels we hadn't seen since late August. Soybean futures have returned to double digits. Some corn futures have returned to the $4 range. The futures markets are providing some incentive to store both crops in the hopes of capturing higher prices this coming spring.

Figure 3 displays the change in projected crop margins, given futures prices and Iowa State University Extension production cost estimates. The price rebound has added roughly $50 per acre back to soybeans and $75 per acre for corn. Both crops are still showing negative returns, but at least the gap is shrinking. And given that a sizable portion of the crop is marketed right at harvest, this rebound couldn't have come at a better time. USDA data from the last three years shows that nearly 14% of the corn crop and 25% of the soybean crop is marketed during October.

Figure 2. Soybean export sales. Source: USDA-FAS.

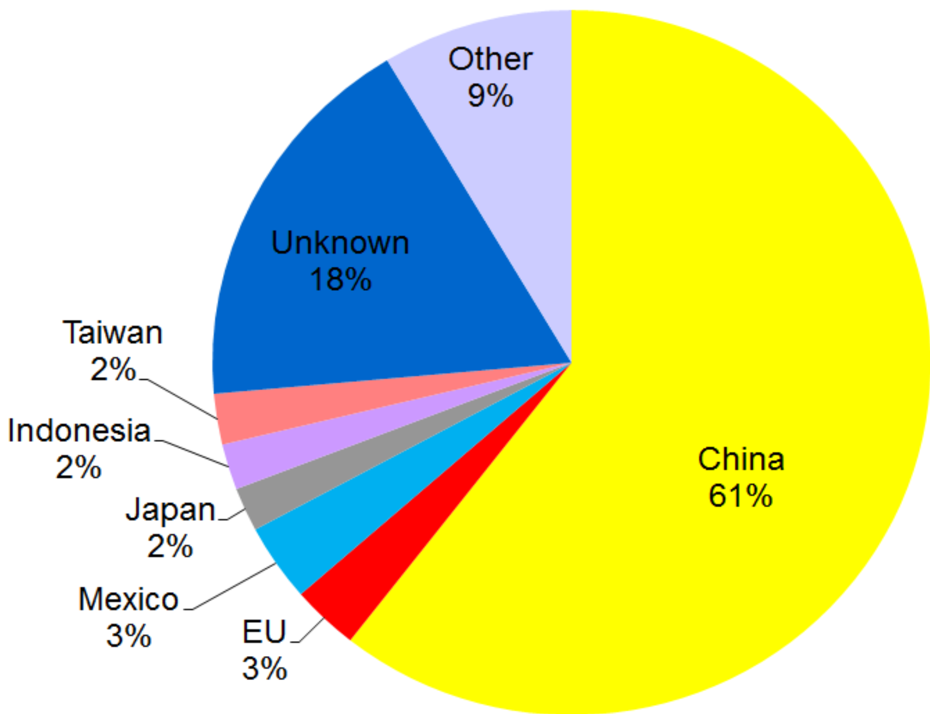
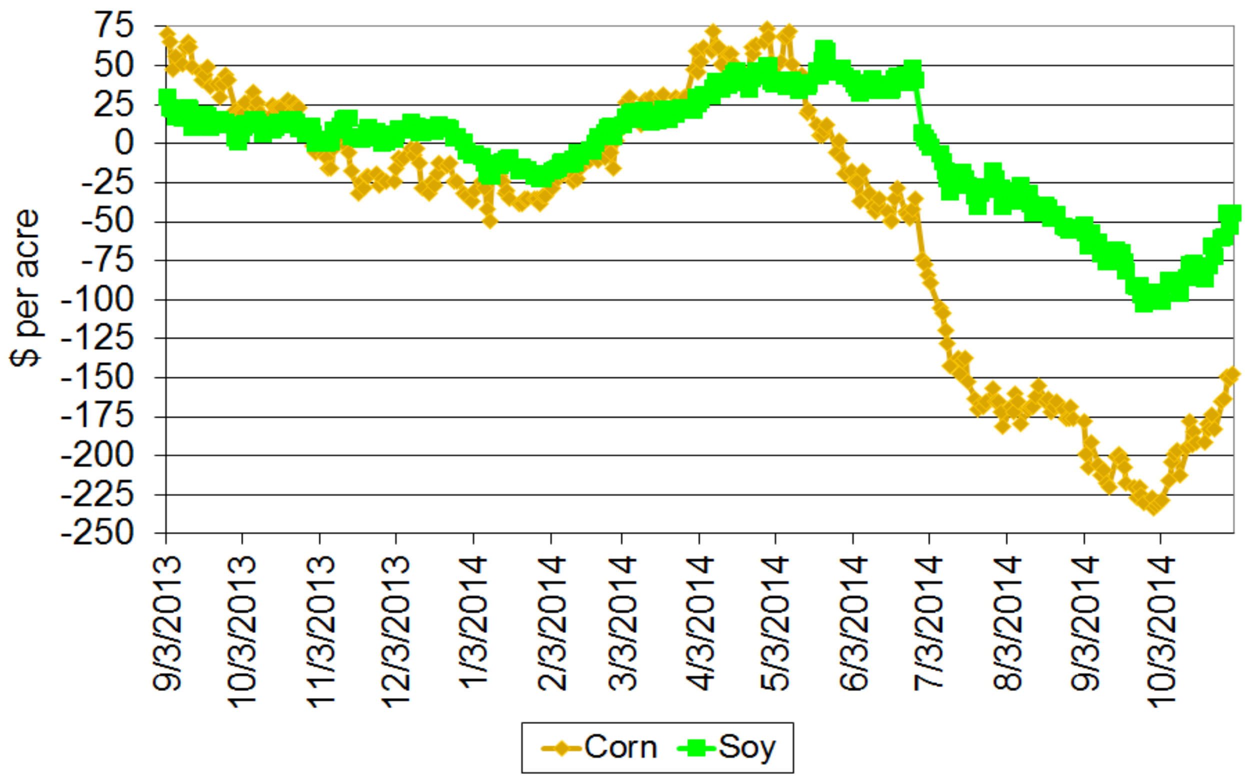
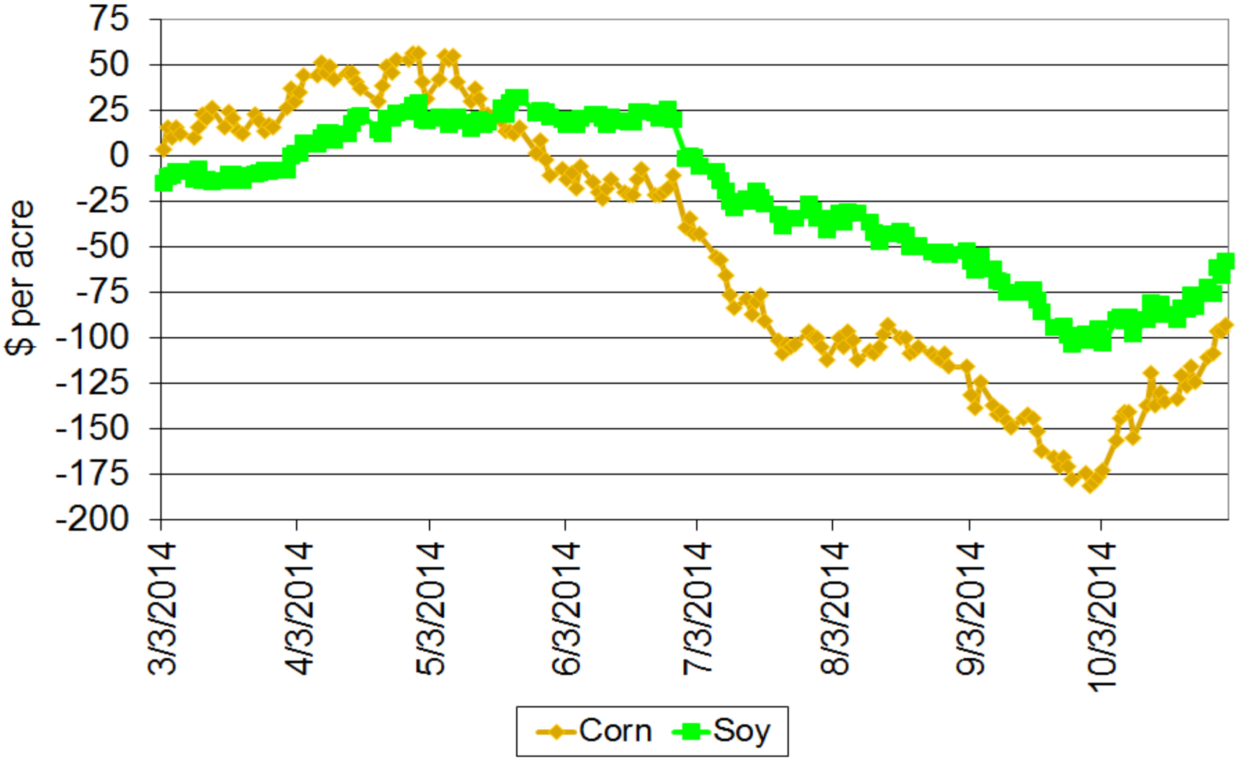


Figure 3. 2014/15 projected crop margins.



The prospects for the 2015 crops are also improving with the price recovery. And again, while the numbers aren't showing profitability, the hole is not nearly as deep as it was a month ago. Given the futures price structure at the end of October, projected margins were in the -$50 per acre for soybeans and -$100 per acre for corn. The losses have been cut by nearly half. Continued price improvement and some possible cost reduction for the coming crop year could extend that trend.

Figure 4. 2015/16 projected crop margins.



While futures prices have risen, cash prices have improved more modestly. Basis levels have been widening as the crops are rolling in. In eastern Iowa, basis on the nearby corn futures contract (December) has moved from 8 cents under at the beginning of the month to 25 cents under at the end. For western Iowa, the decline has been a little larger, shifting from 5 cents under to 34 cents under. The statewide average soybean basis has floated in the 30-40 cents under range through October, but some markets are starting to push the soybean basis to the 50-60 cents under range. Given the large crops, this is not surprising. The question over the next month is whether the futures markets can continue to rise enough to offset the weakening basis.

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