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Agricultural Outlook Forum Presented: February 17, 2006

A NEW LOOK FOR THE CANADIAN PORK AND BEEF SECTORS

Kevin Grier
Senior Market Analyst
George Morris Centre

GEORGE MORRIS CENTRE

A New Look for the Canadian Pork and Beef Sectors

2006 USDA Agricultural Outlook Forum

Kevin Grier

February 17, 2006

Purpose

- Provide a Canadian perspective of:
  - the characteristics of the North American pork and beef industry
  - the Canadian competitive forces facing the US industry

Presentation Outline

- Domestic Market Characteristics
- Price Determination and Discovery
- Trade Challenges
- Competitiveness
  - Status and prospects

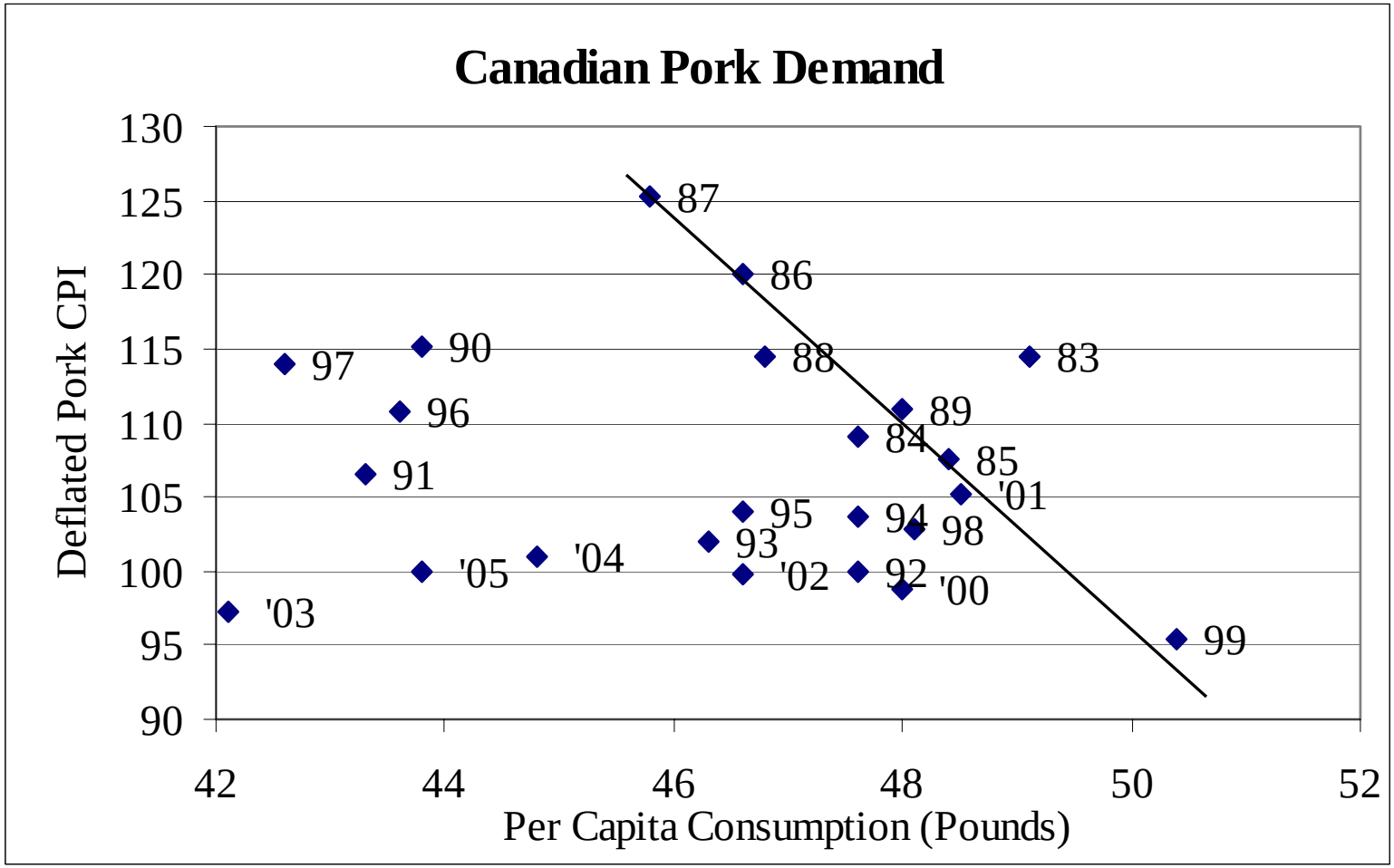
George Morris Centre

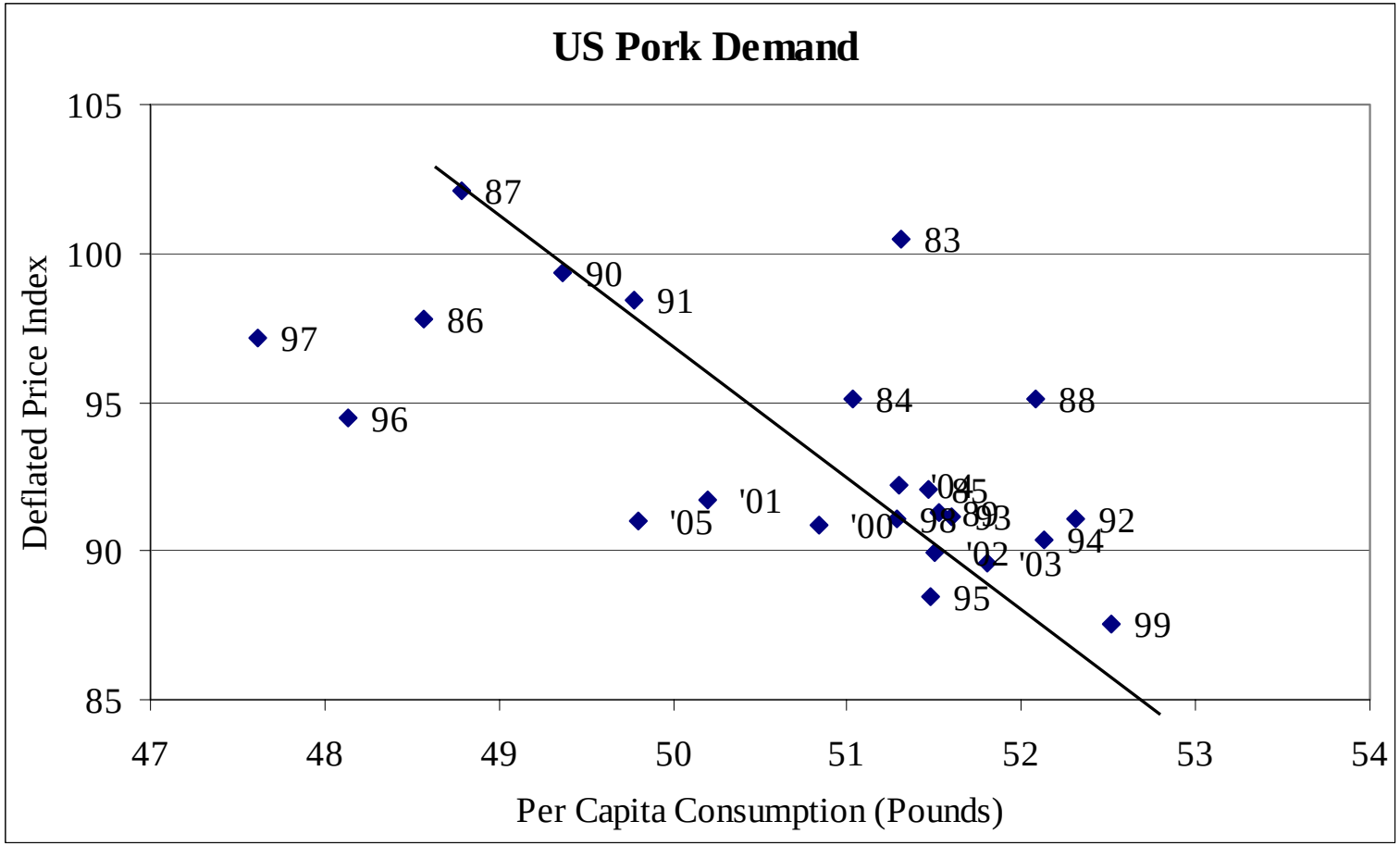
- Economic Research into the Canadian Agriculture and Food Industry
- Independent
  - Financially
  - Structurally
  - Research Perspective

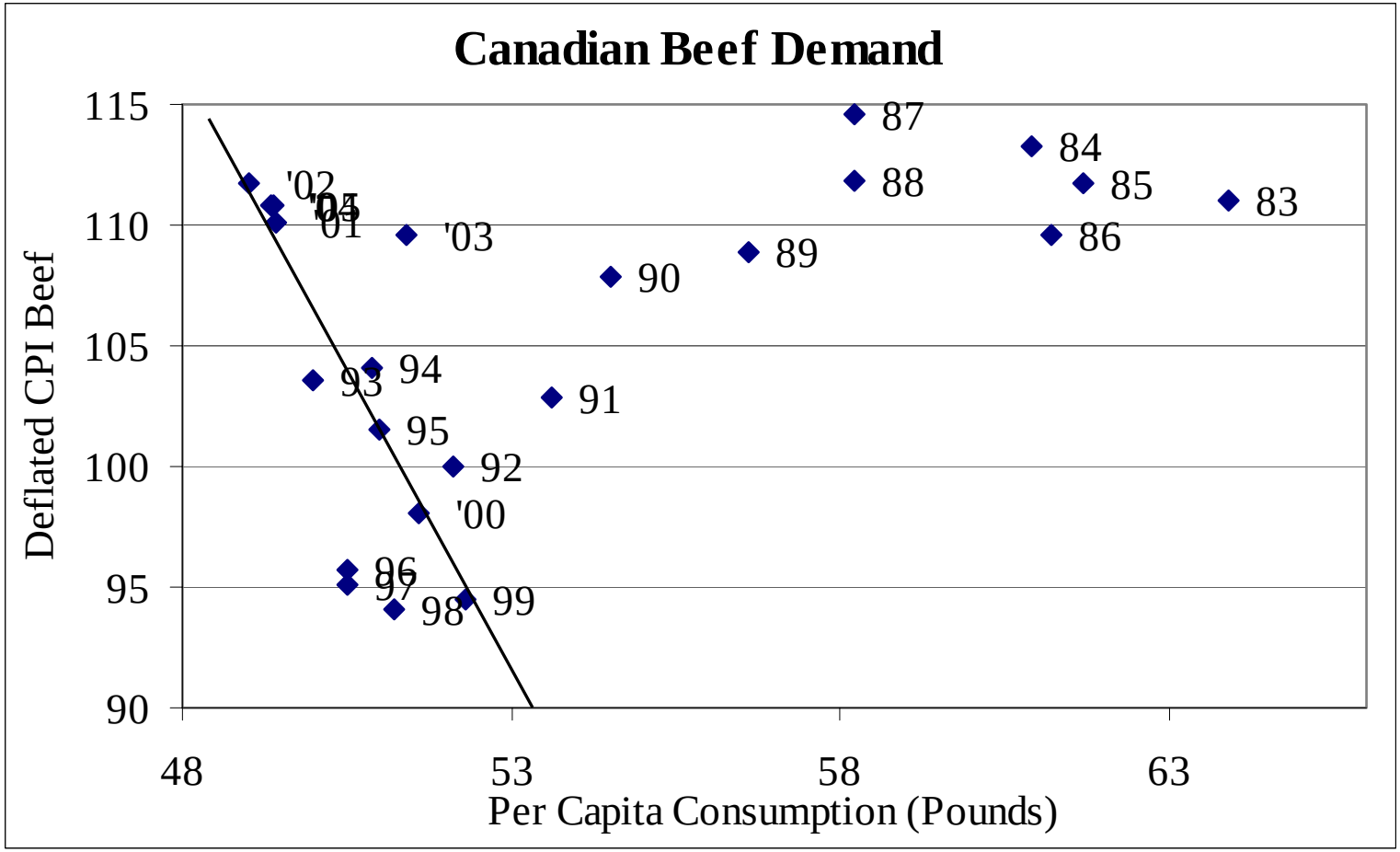
GMC Areas of Activity

- Contract Research
  - Clients: eg. Private Companies, Producer Associations, Government
  - 2005 Research examples: BSE, Hog Marketing, Environment
- Market Analysis
  - Beef, Chicken, Pork and Grocery Reports
  - Price Forecasting
- Education
  - Executive Development
  - Risk Management

Characteristics and Status of the North American Industry


Canadian Pork Demand
Deflated Pork CPI
130
125
120
115
110
105
100
95
90
42
44
46
48
50
52
Per Capita Consumption (Pounds)
87
86
90
97
88
83
96
89
84
85
91
'01
95
94
98
93
'04
'05
'02
92
'00
'03
99


US Pork Demand
Deflated Price Index
105
100
95
90
85
47
48
49
50
51
52
53
54
Per Capita Consumption (Pounds)
87
83
90
91
86
97
84
88
96
'04
85
'01
'05
'00
98
89
93
92
94
'02
'03
95
99


Canadian Beef Demand
Deflated CPI Beef
Per Capita Consumption (Pounds)
115
110
105
100
95
90
48
53
58
63
87
84
88
85
83
86
89
90
'03
'02
'04
'05
'01
94
93
91
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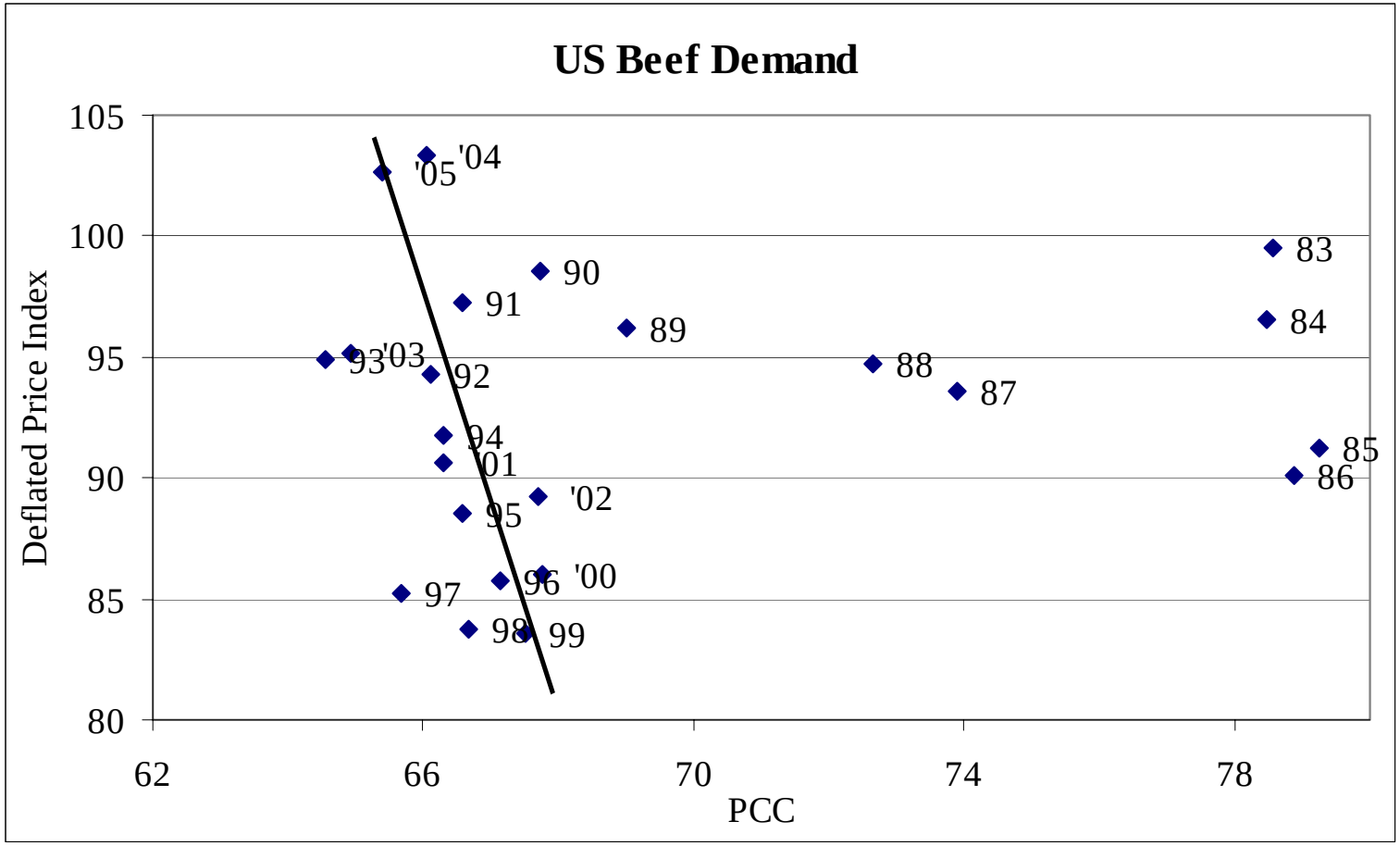
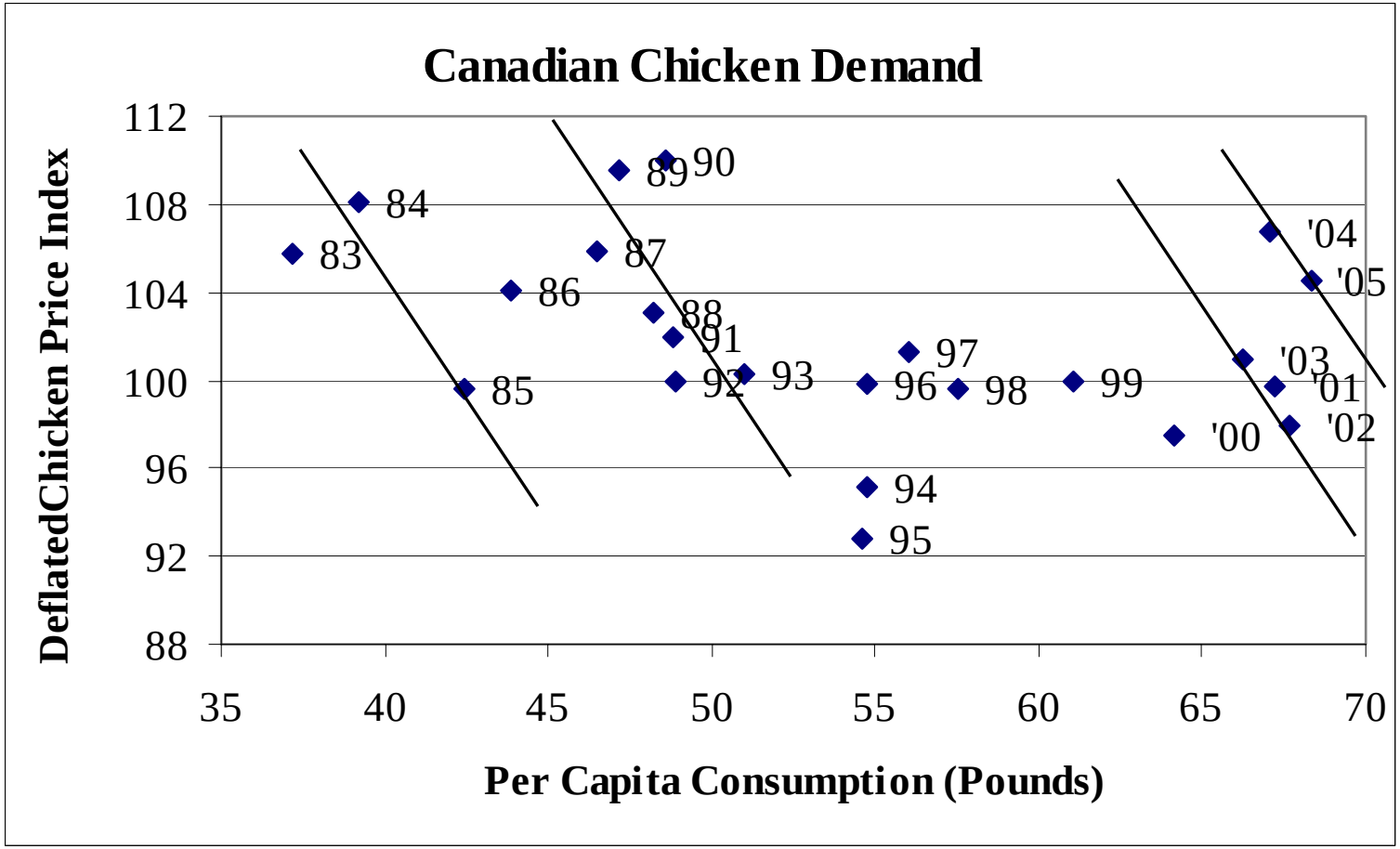
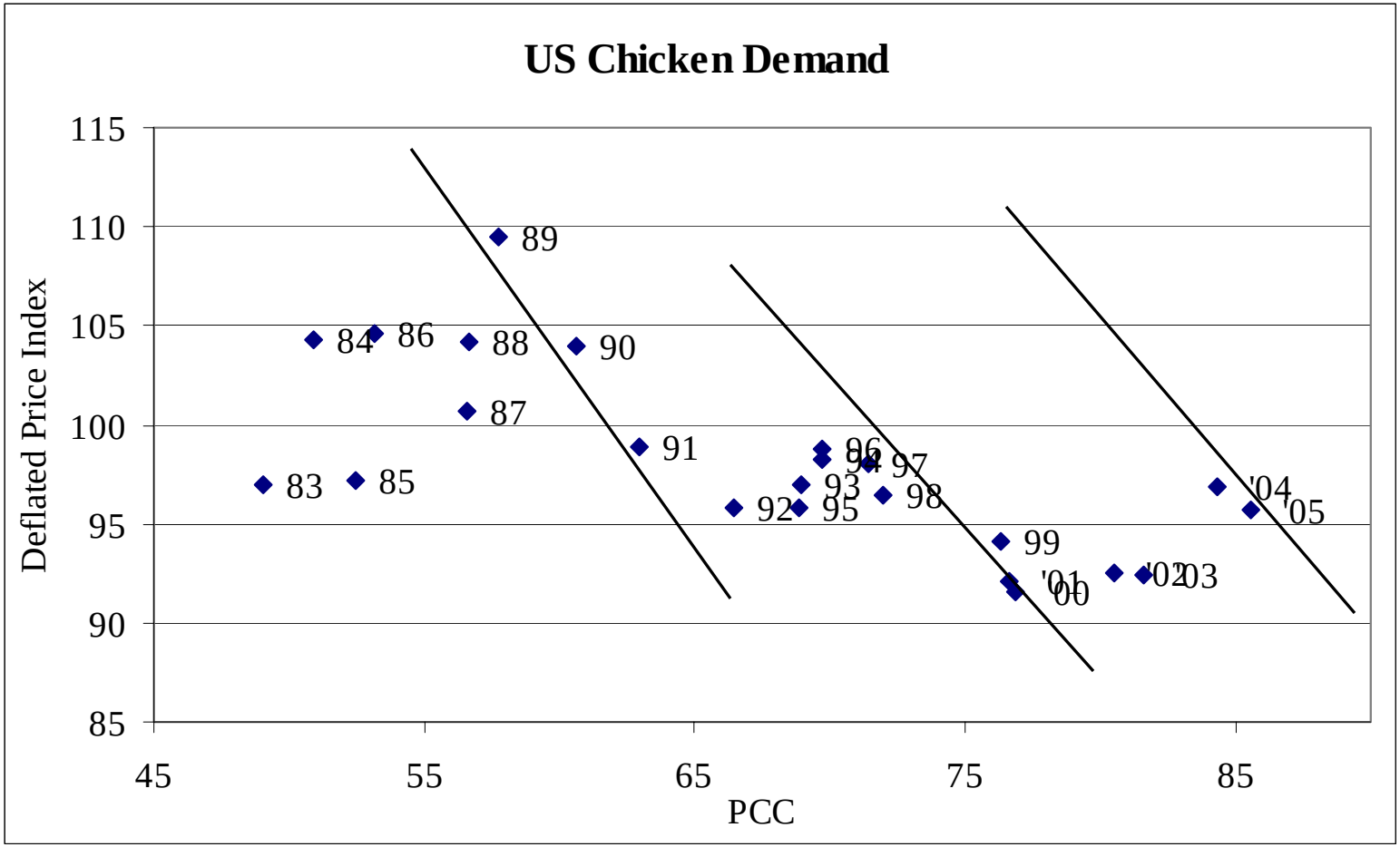
'00
96
97
98
99


US Beef Demand
Deflated Price Index
PCC
105
100
95
90
85
80
62
66
70
74
78
'05
'04
90
91
89
93
'03
92
94
'01
95
'02
96
'00
97
98
99
83
84
88
87
85
86


Canadian Chicken Demand
DeflatedChicken Price Index
112
108
104
100
96
92
88
35
40
45
50
55
60
65
70
Per Capita Consumption (Pounds)
83
84
85
86
87
88
89
90
91
92
93
94
95
96
97
98
99
'00
'01
'02
'03
'04
'05


US Chicken Demand
Deflated Price Index
PCC
115
110
105
100
95
90
85
45
55
65
75
85
83
84
85
86
87
88
89
90
91
92
93
94
95
96
97
98
99
'00
'01
'02
'03
'04
'05

Beef Production Characteristics

Canada and the US

- Cow-calf production based on western pasture
- Feeding in large scale feedlots close to grain
- Grain based feeding
- Packing in large scale plants close to feedlots
- Cargill and Tyson

The Beef Sectors are Identical

Pork Production Characteristics

Canada and the US

- Three site production systems
- Farrowing driven by advanced husbandry
- Increasing integration in various forms
- Packing close to finishing
- Overseas export driven

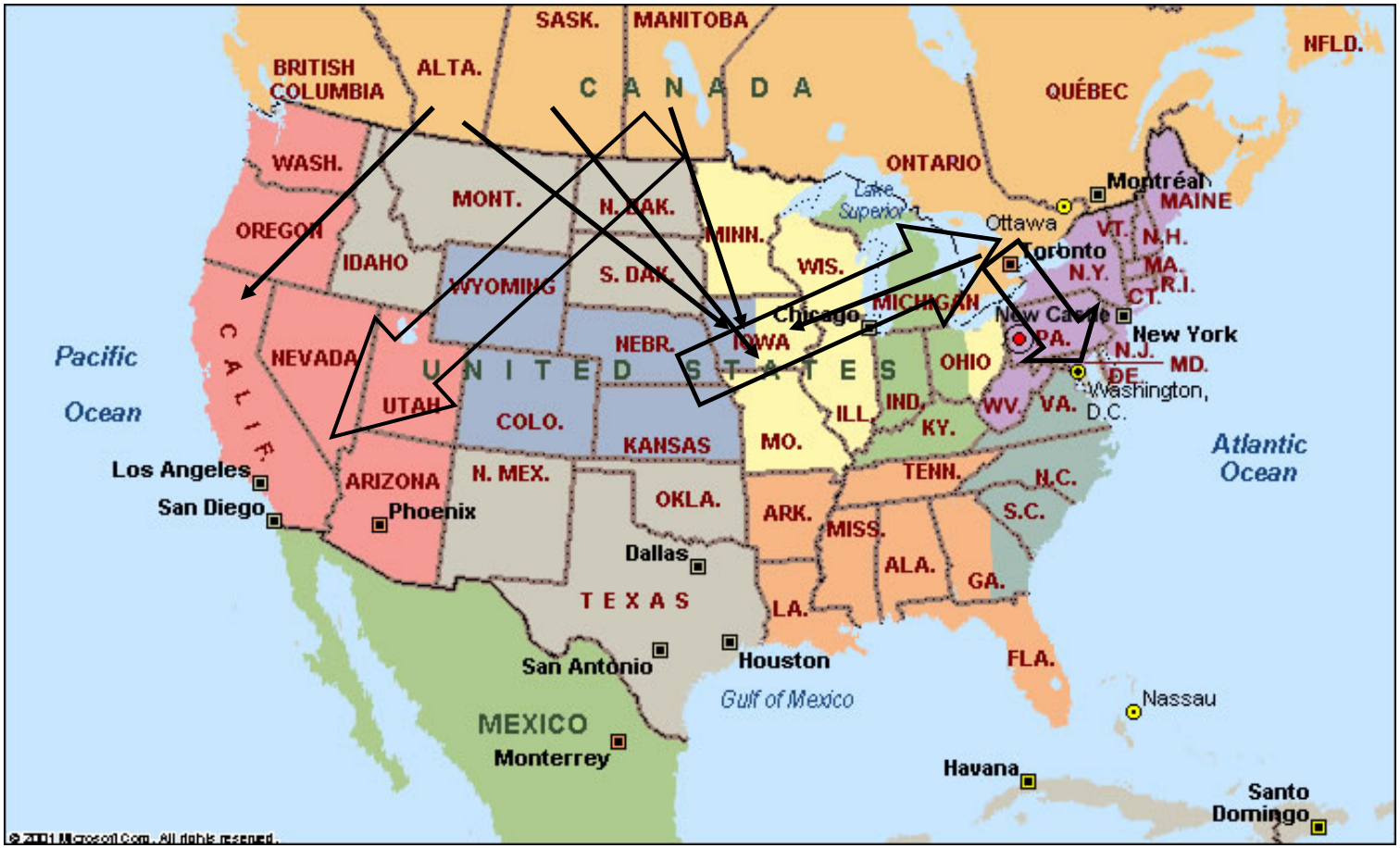
The Hog and Pork Sectors are Identical

Cattle and Beef Sales

Cattle →

Beef

Hog and Pork Sales



Hogs →

Pork ↓

Rationale for Hog and Pork Sales

- GMC Research; Informa Research; USDA ERS Research:
  - Sales occur for rational, economic reasons
  - Comparative advantage; structural change; industry evolution

Assertion

- Ontario weaner sales to Iowa occur for the same reasons that pull/push Oklahoma weaners sales to Iowa.
- Manitoba slaughter hog sales to Sioux Falls occur for the same reasons that pull/push Minnesota hog sales to Sioux Falls

Rationale for Cattle and Beef Sales Patterns

- GMC Research:
  - Western Canada is the most competitive region in NA for cow calf production
  - Western Canada is competitive with the High Plains for feeding
  - Tyson and Cargill plants in Alberta are among the most competitive in NA.

Assertion

- Alberta beef to California occurs for the same reasons that Nebraska beef goes to Ontario.

Cdn Livestock and Meat Pricing

- Pricing: US/Exch – Spread
- US benchmark
  - nearest alternative
- Exchange
  - price impact
- Spread
  - S&D, Freight
- Pricing is formula

Key Points

- There is no border for the livestock and meat market.
- Cda has small population and significant production resources…like Nebraska and the TPH

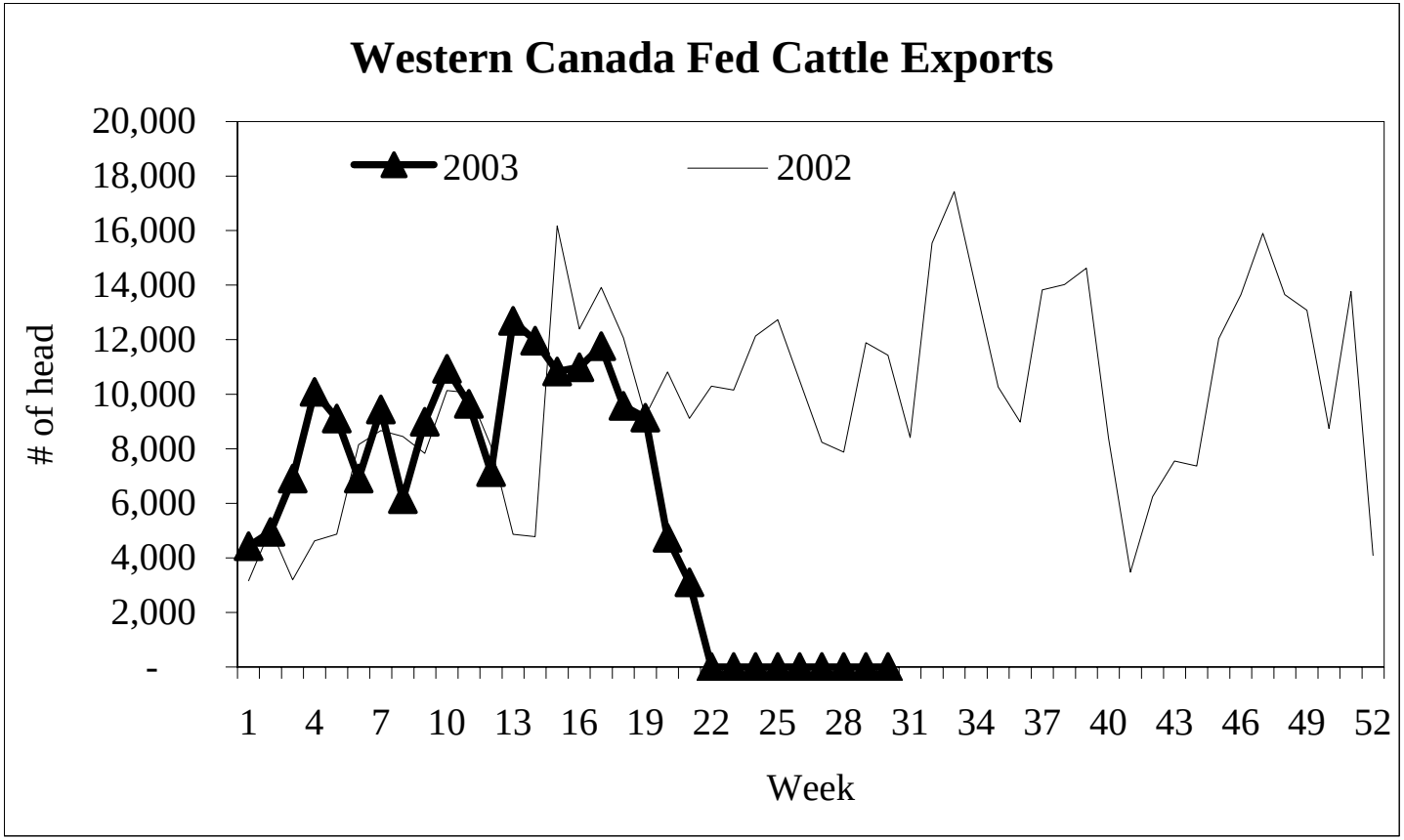
Recent Trade Issues

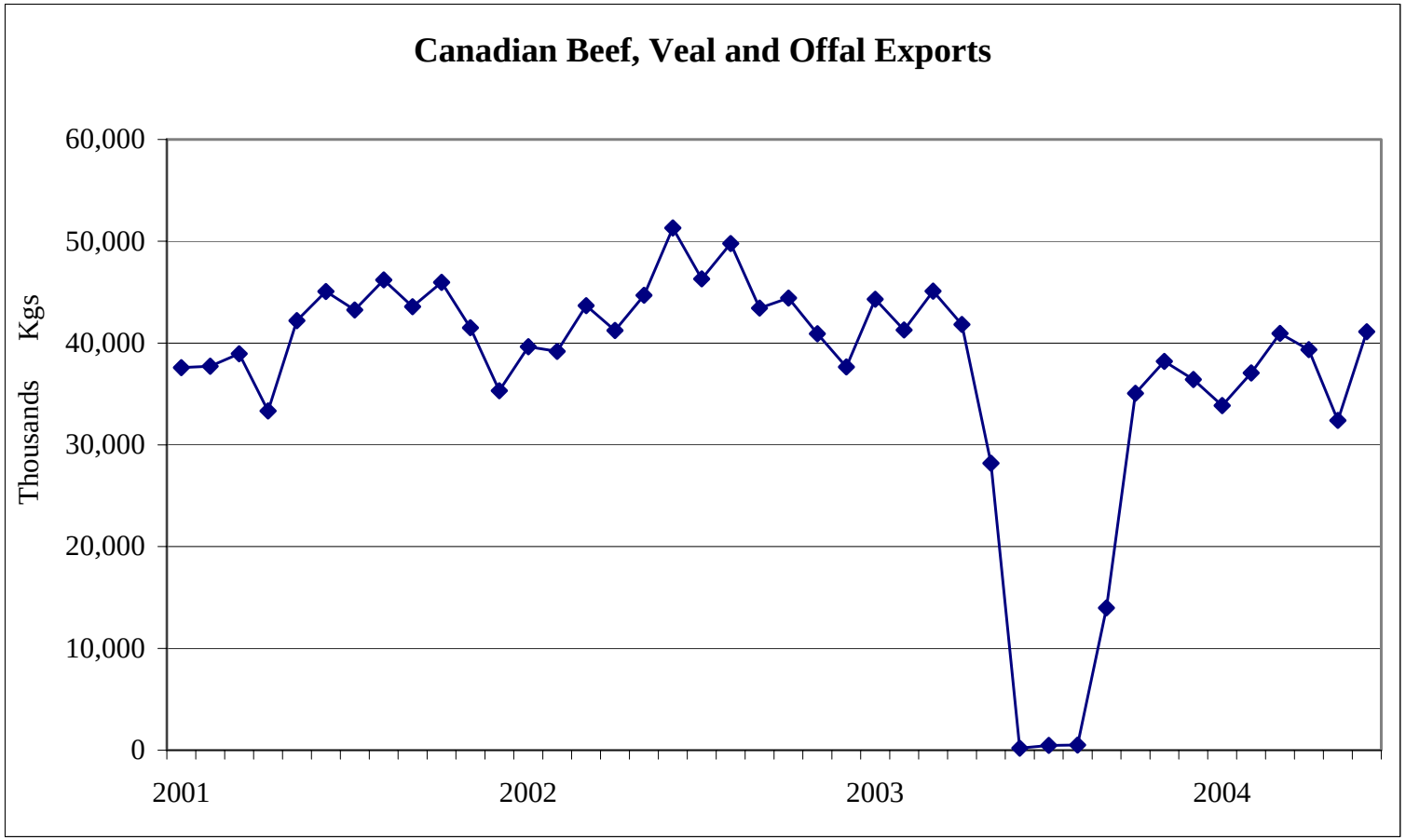
- Pork Countervail and Anti-dumping
- BSE

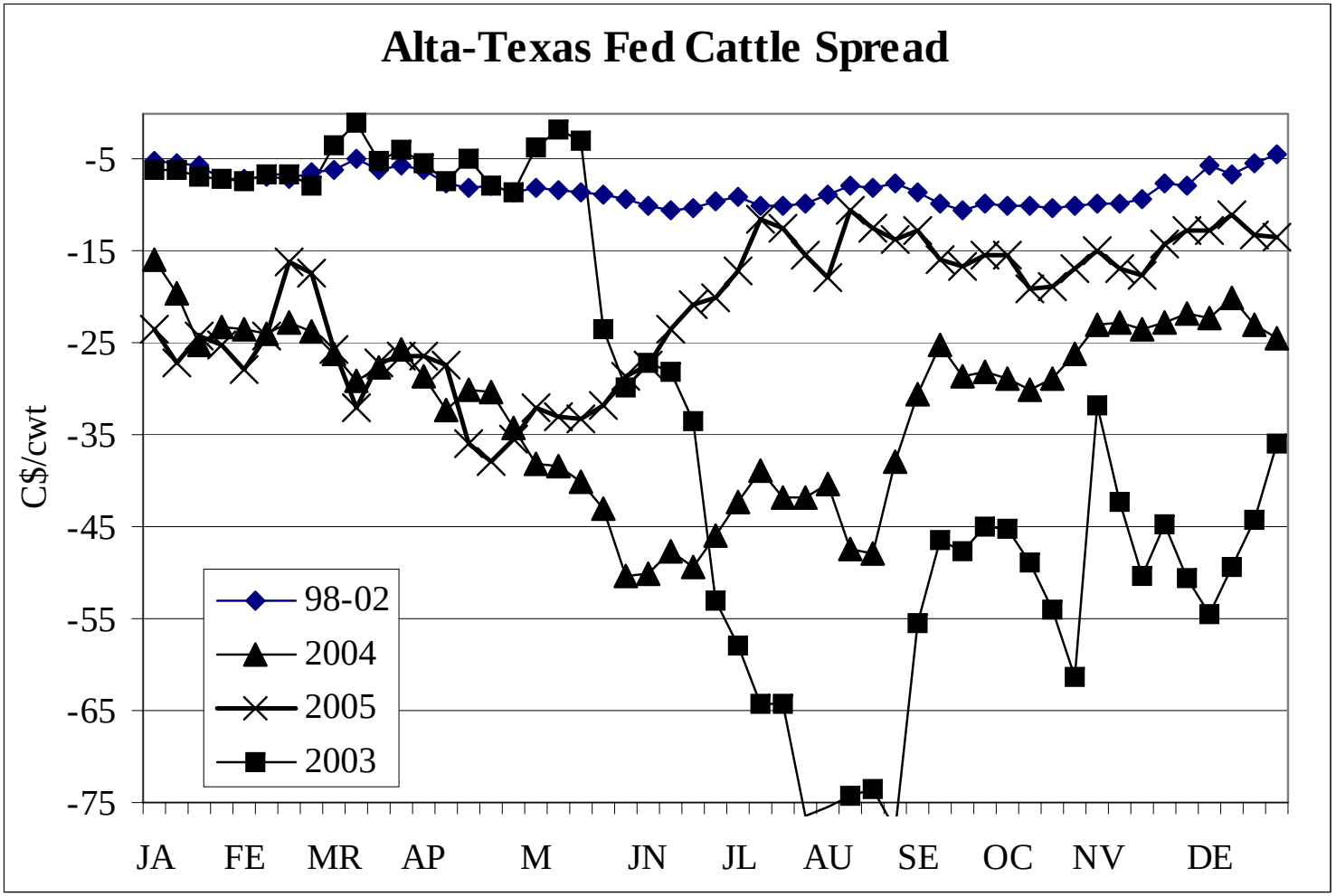
Pork Countervail

- US Commerce Department
  - Most expertise on Cdn programs
- Dumping
  - Major challenge for both countries
- Injury
  - Value added
  - Independent producers
  - Environmental
  - Structural Reorganization

BSE

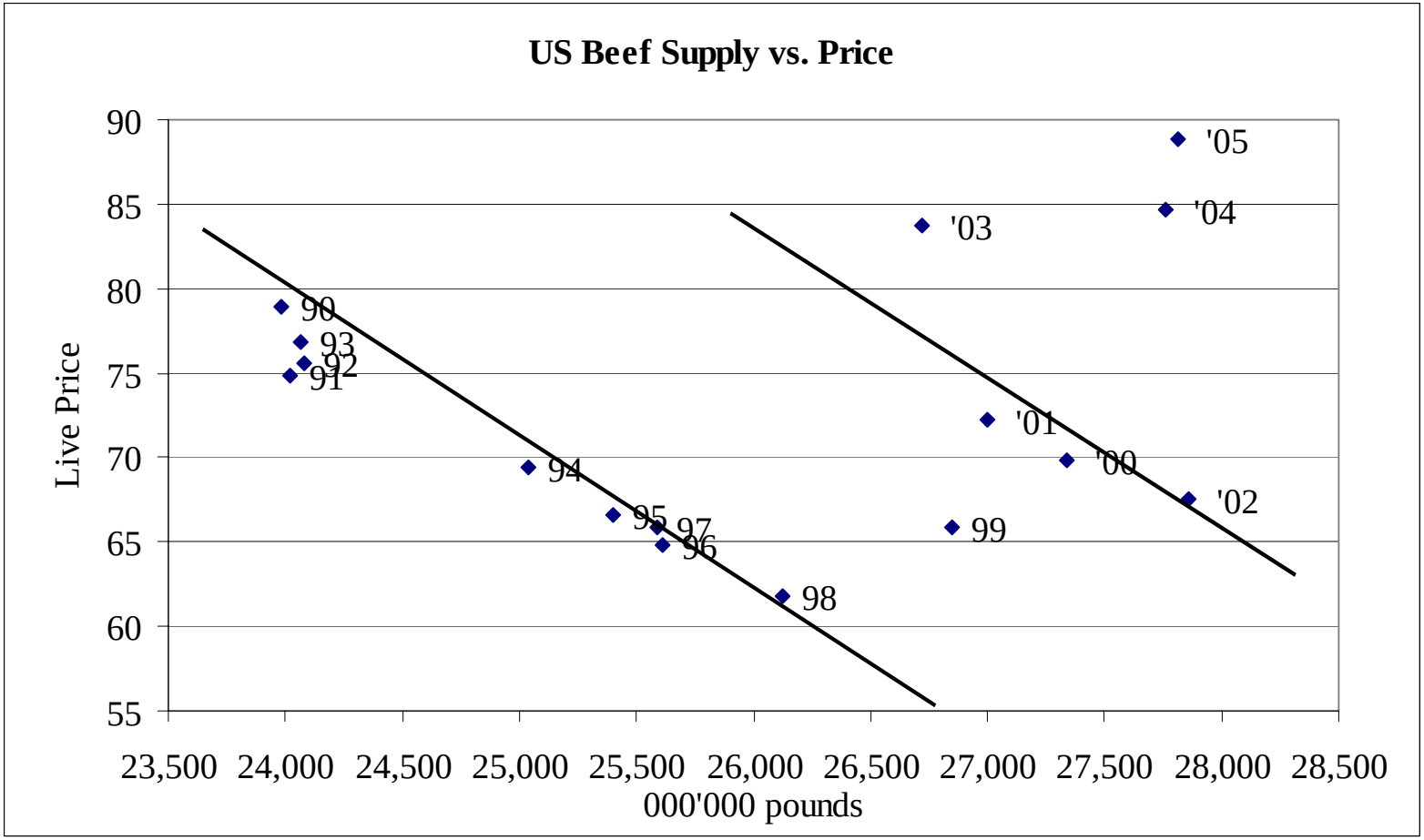

Western Canada Fed Cattle Exports
20,000
18,000
16,000
14,000
12,000
10,000
8,000
6,000
4,000
2,000
-
# of head
2003
2002
1
4
7
10
13
16
19
22
25
28
31
34
37
40
43
46
49
52
Week


Canadian Beef, Veal and Offal Exports
Thousands Kgs
60,000
50,000
40,000
30,000
20,000
10,000
0
2001
2002
2003
2004


Alta-Texas Fed Cattle Spread
C$/cwt
-5
-15
-25
-35
-45
-55
-65
-75
JA
FE
MR
AP
M
JN
JL
AU
SE
OC
NV
DE
98-02
2004
2005
2003

BSE

- USDA acted in good faith
- Minimal price impact in the US
- Cost the US
  - 4,450 head per day; 7 plants closed
- Painful lessons learned


US Beef Supply vs. Price
Live Price
90
85
80
75
70
65
60
55
23,500
24,000
24,500
25,000
25,500
26,000
26,500
27,000
27,500
28,000
28,500
000'000 pounds
'05
'04
'03
90
93
92
91
'01
'00
'02
94
95
97
96
99
98

Trade Disputes

- Negative Impacts
- Iowa Pork resolution…hog lanes

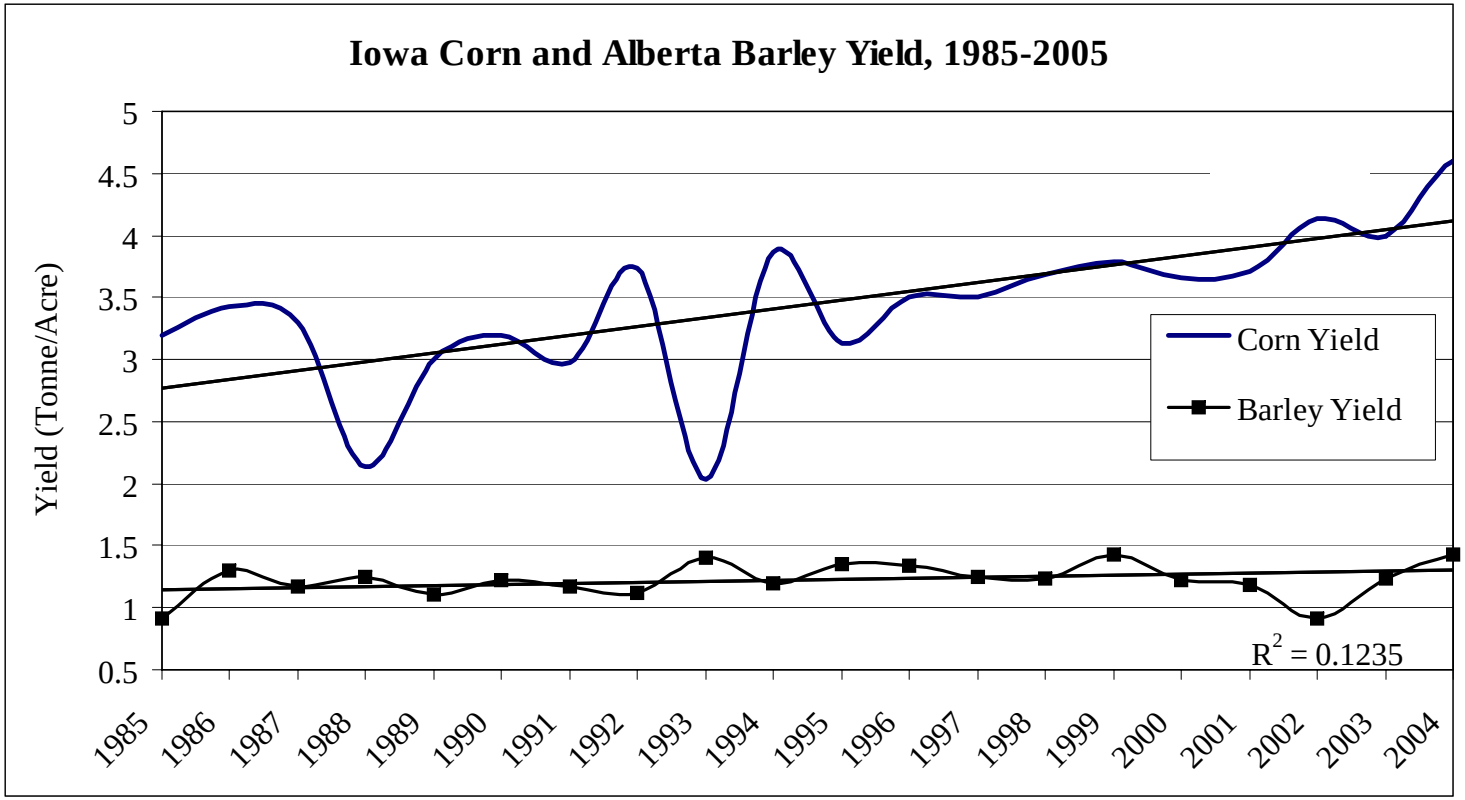
Canadian Competitive Forces

Competitive Assessment

- GMC H&P research:
  - Farrowing…advantage Cda
  - Finishing…advantage US
    - Ont and Prairies are cost competitive
    - Revenue issue
  - Packing…advantage US
- GMC C&B
  - Canada is competitive through the chain

Production Assertion

- Cost and productivity; Cdn prod'n is competitive, with one caveat:

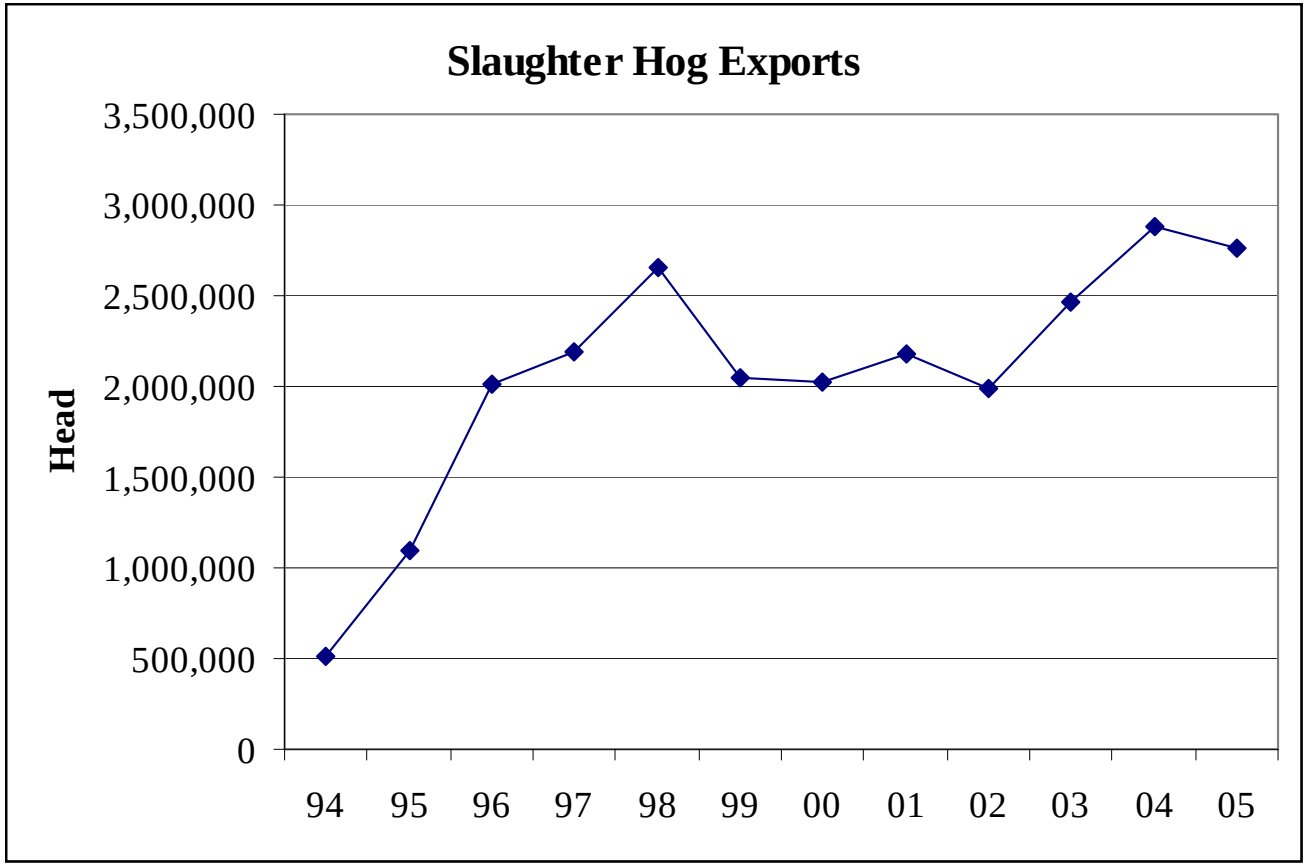


Production Competitiveness Challenges

- Environmental regulation
- Feed grain costs
- Veterinary drug licensing
- Pricing…

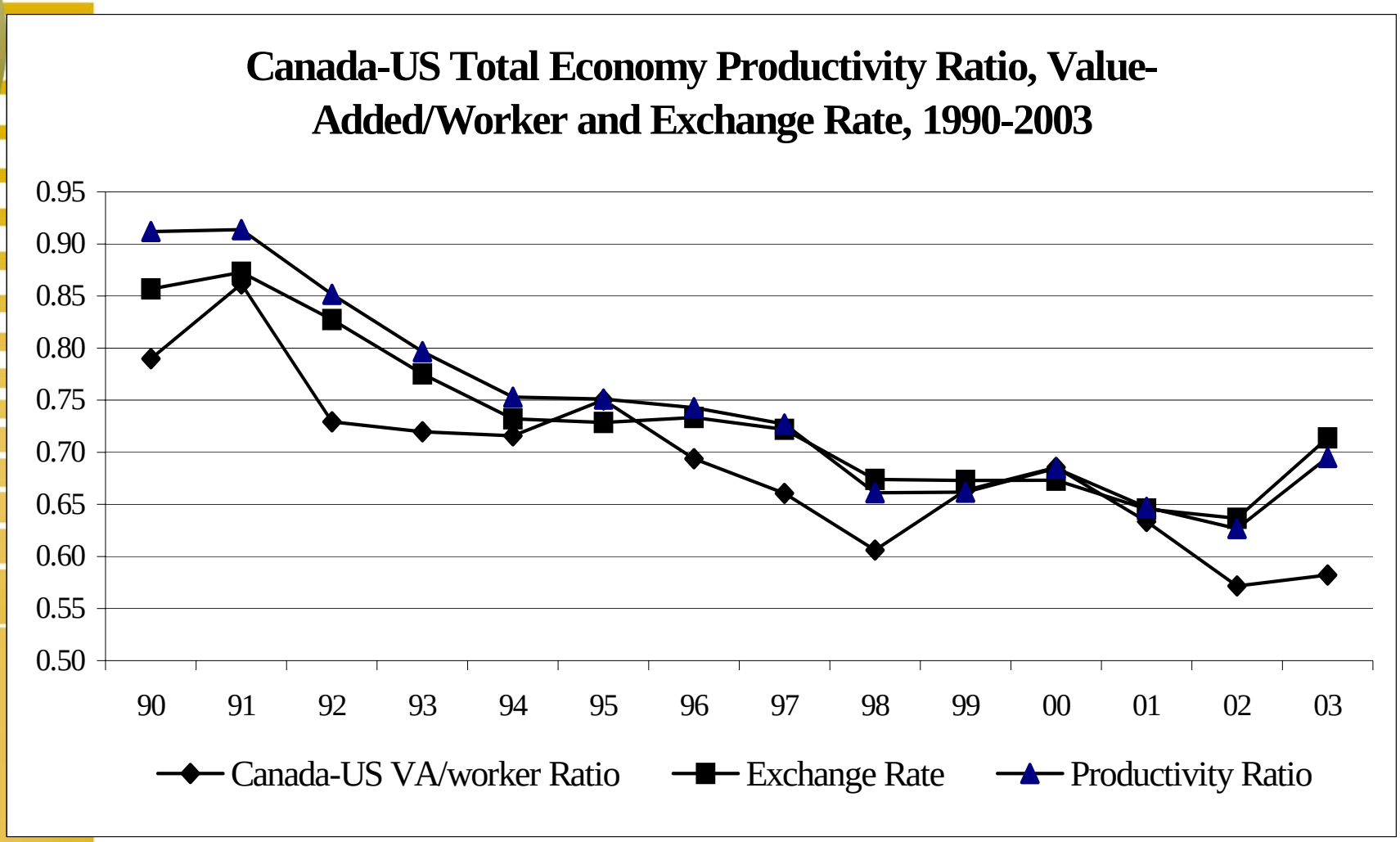
Packing: The Competitive Focus

- Pork Export trends suggest the industry is competitive…world leader
- But the slaughter shipment south suggest…?



Packing Sector Competitiveness

General Cdn Competitiveness



Packing Assertion

- The productivity challenge faced by the Cdn economy is applicable to the red meat sector and it’s a pork, not a beef problem.

Cdn Beef-Pork

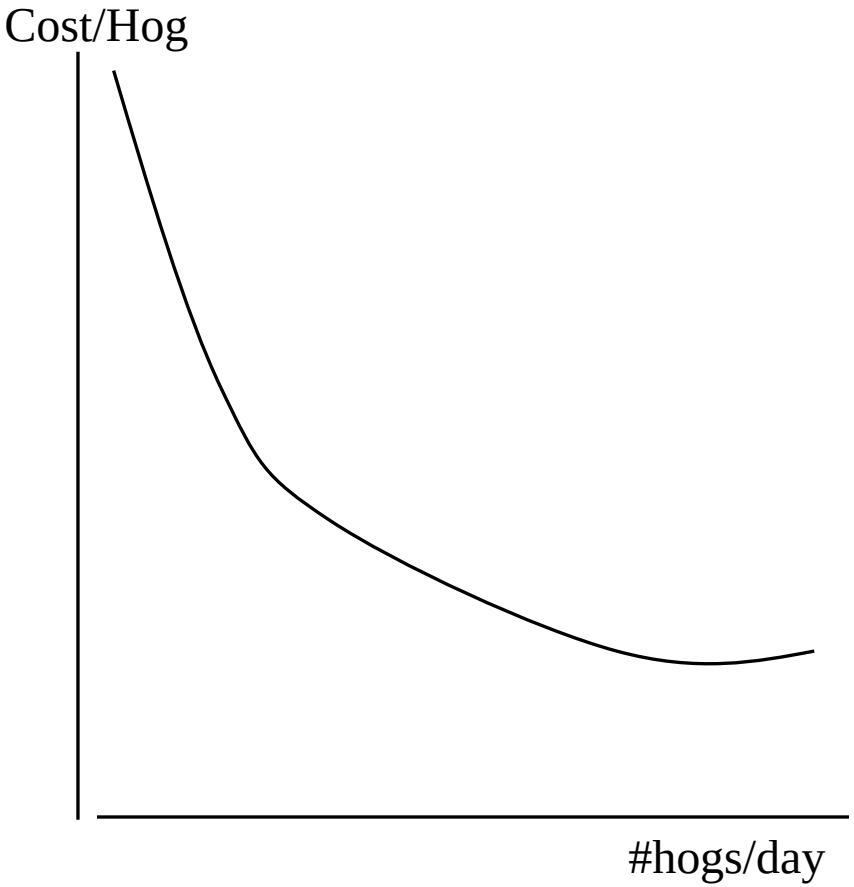
- Cargill and Lakeside are double shifted
- Cargill and Lakeside go on Saturday
- These plants rate high with the others in the Tyson & Cargill complex

US-Canada Comparison

- Canada
  - Cda average daily capacity: 3,200 head
  - 5 largest Cdn plants: 8,400 per day.
  - 3 of top 29 are >40,000 per week
- US
  - average daily capacity: 13,000 head.
    - nearly 4 times greater than in Canada.
  - 5 largest US plants: 21,000 head
    - 2.5 times greater than the top five in Canada.
  - 20 of top 29 are > 40,000 per week

Size Matters

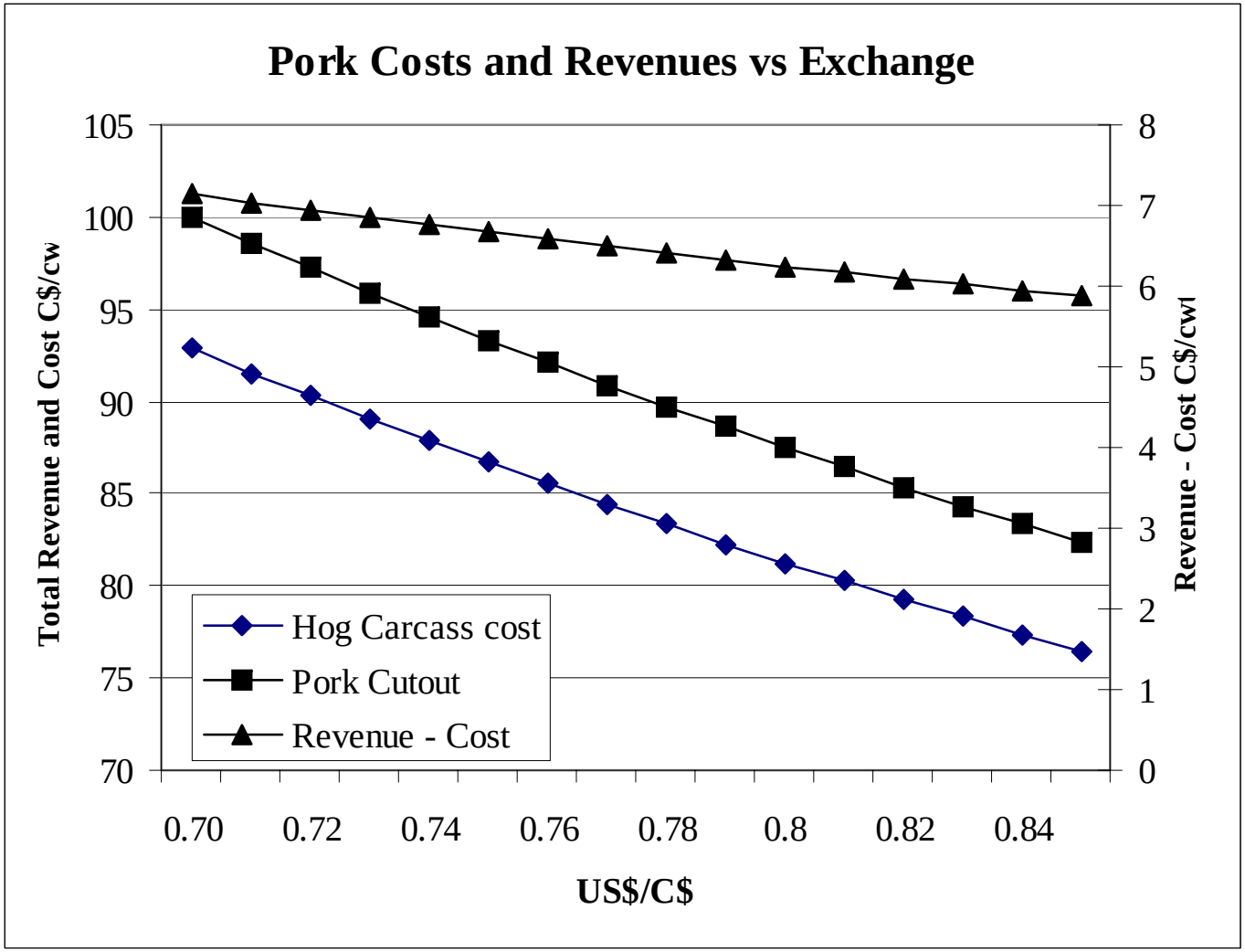
- Larger plants have lower costs/head than smaller plants.
- USDA research: $2-8/head lower



Double Shifting

- All major US plants double shift
- Until Olywest RD…not a factor in Cda
- GMC research: Double shifting a large, 45,000 head plant would reduce costs by around $5/head

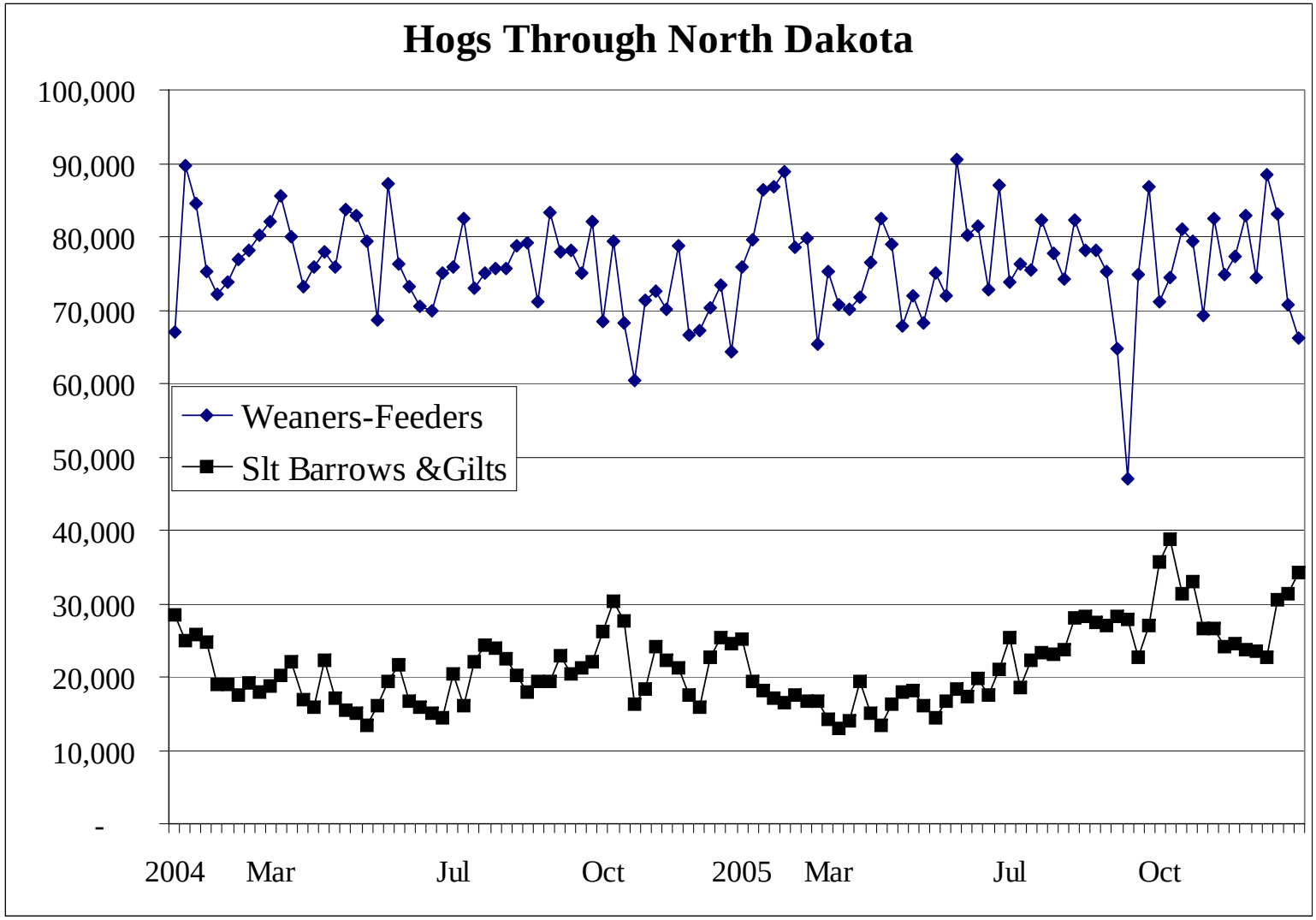
Exchange Rate Impact: Packer Level

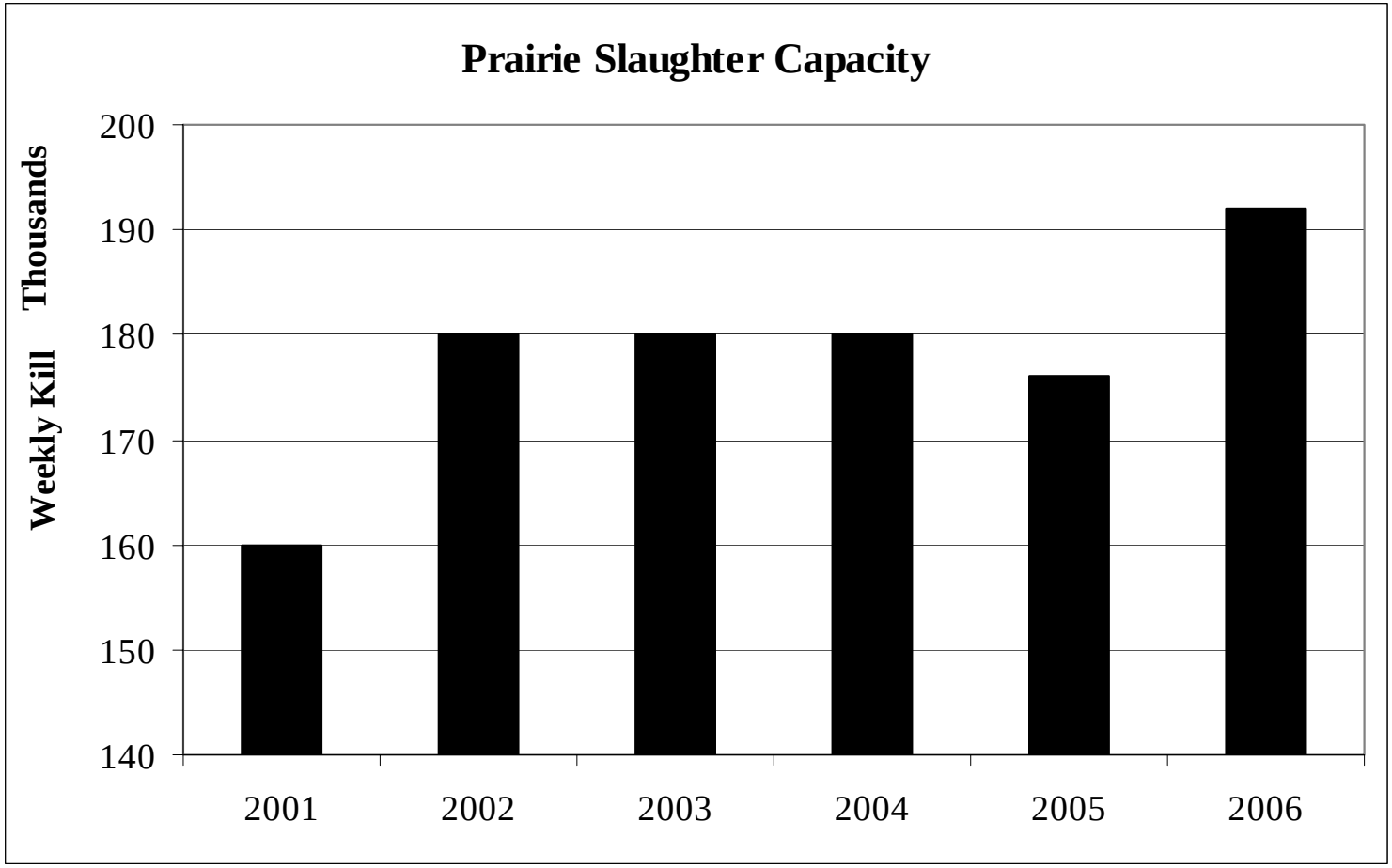


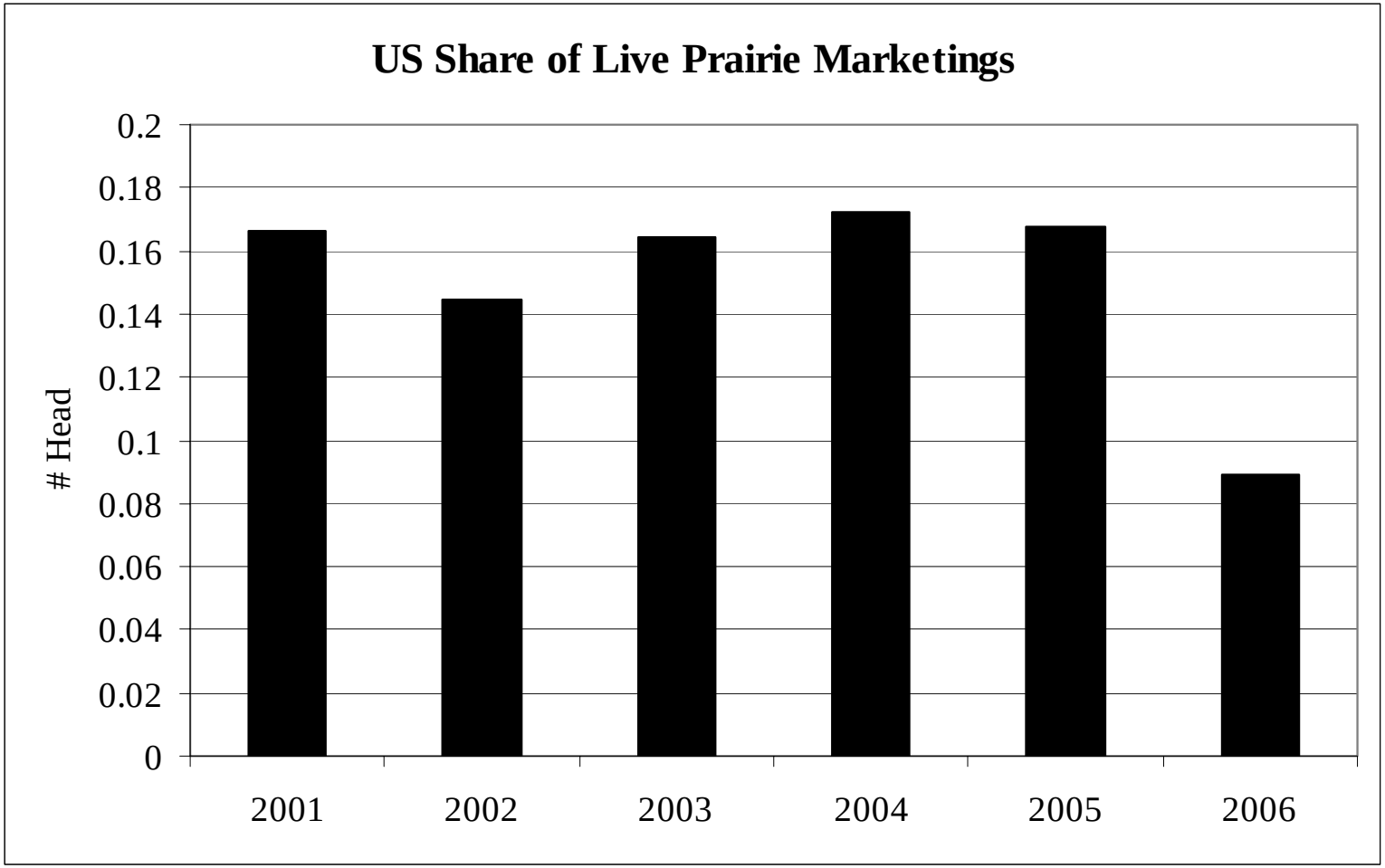
Exchange Rate Impact

- Operating Costs of $35/head
- Half = Labor
- @C$.63 = US$11/head
- @C$.85 = US$15/head

- Squeeze on the gross mgn and operating cost disadvantage


Hogs Through North Dakota
100,000
90,000
80,000
70,000
60,000
50,000
40,000
30,000
20,000
10,000
-
Weaners-Feeders
Slt Barrows &Gilts
2004
Mar
Jul
Oct
2005
Mar
Jul
Oct


Prairie Slaughter Capacity
Weekly Kill Thousands
200
190
180
170
160
150
140
2001
2002
2003
2004
2005
2006



Not counting weaners/feeders

Cattle Feeding Competitiveness

- Wider spread post BSE
- Large volumes of feeders going south
  - Usually north

Beef Packing Capacity

- 2002: 72-75,000/week
- 2005: 95,000
- > fewer cattle heading south…

Summary

- Canada and the US are one market.
- Sales between countries occurs due to comparative advantage.
- Trade disputes hurt both countries.
- Canada has competitive challenges ahead.
- Live animal sales will decrease with capacity increases.

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