



Economic Sustainability & Canadian Feedlots

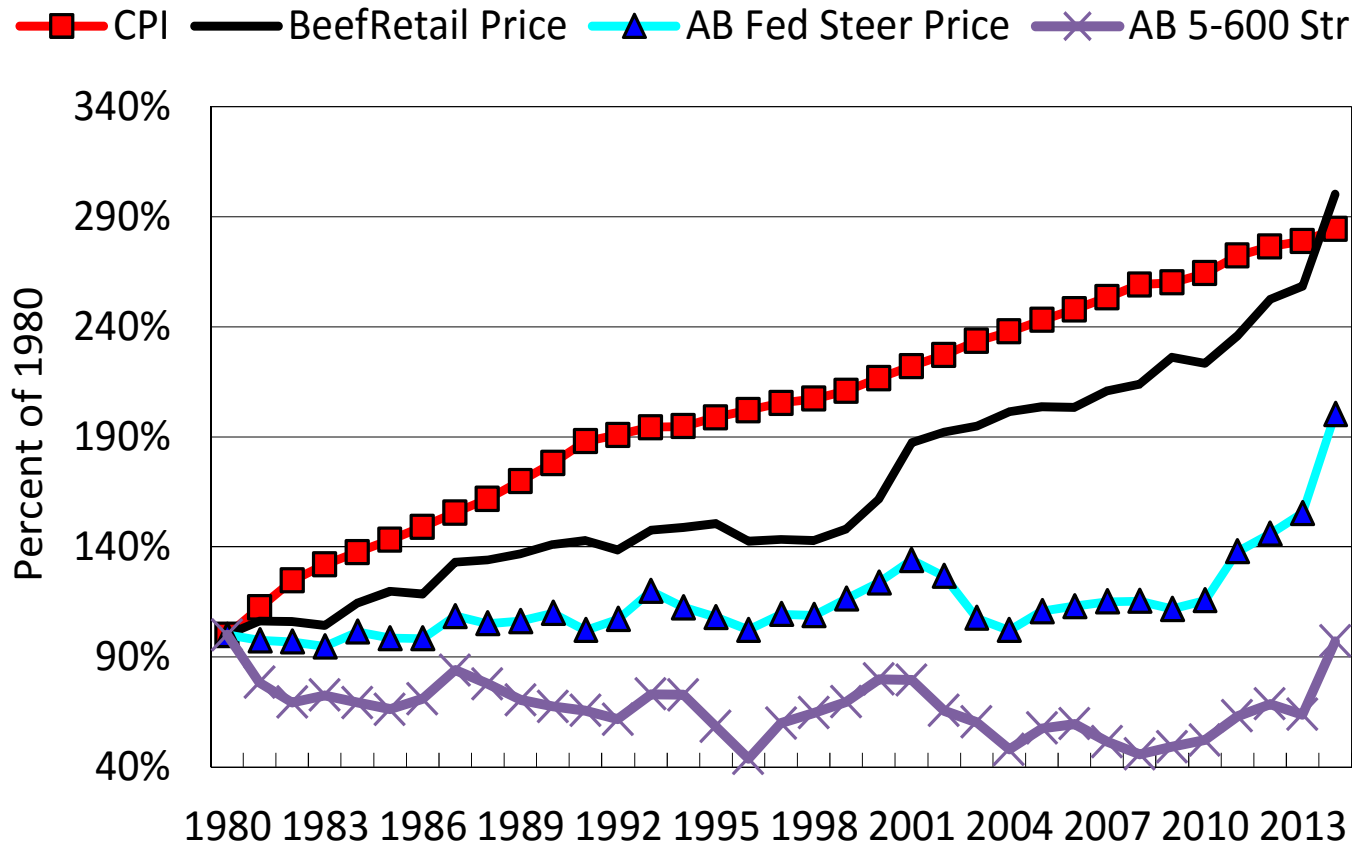
agri benchmark Global Forum
June 2016
Canfax Research Services





Declining Terms of Trade

Retail and fed steer price as % of 1980





Framework for Economic Sustainability

- Producer Viability
 - LT Profitability
 - LT COP
- Consumer Resilience
 - Domestic Demand
 - International Demand





Economic sustainability is defined as the ability of a system to maintain productivity in the face of a major disturbance, as well as slow shifts in consumer preferences.



Producer Viability





Producer Viability



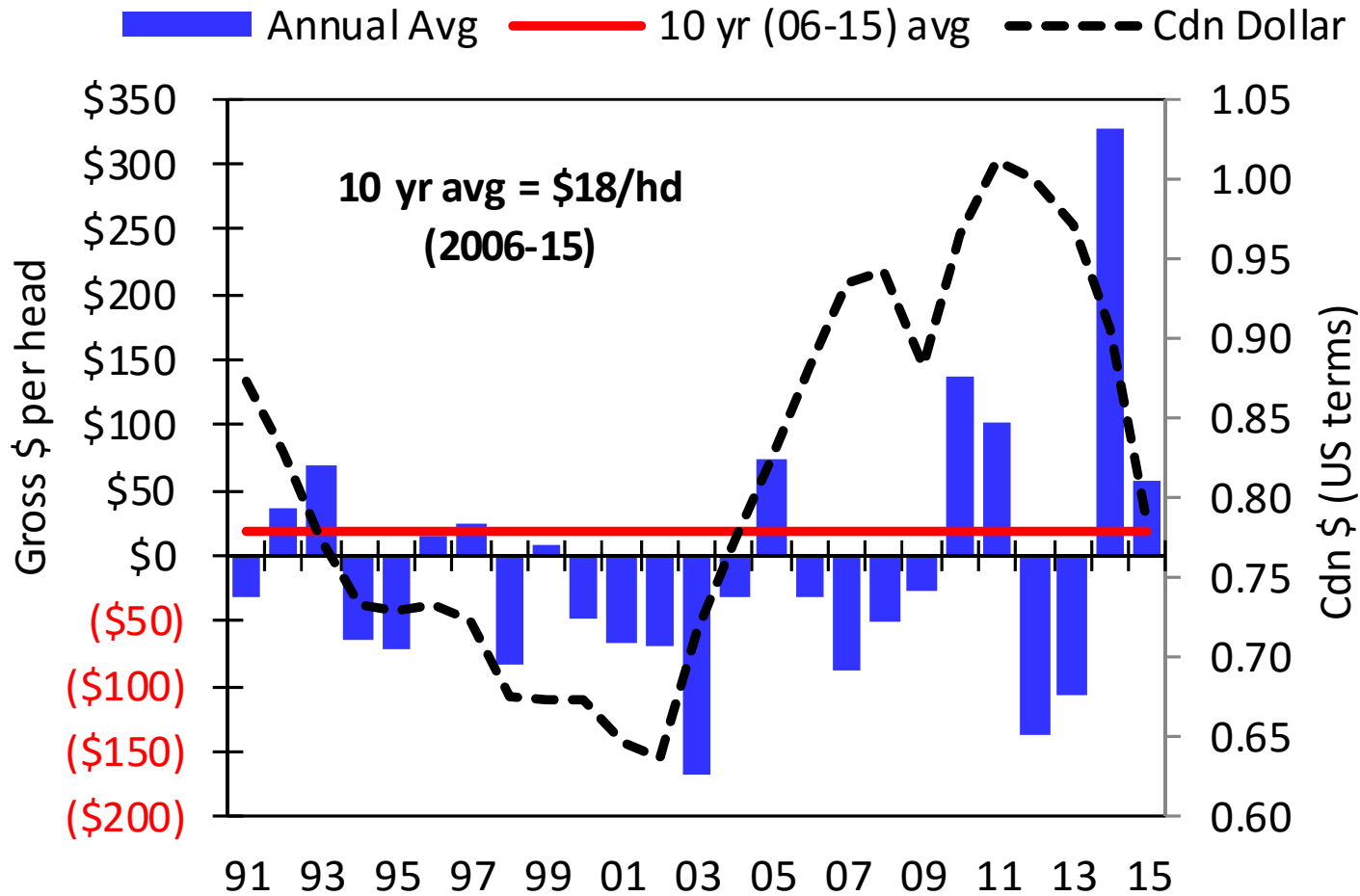
- Financial Profits vs. Economic Profits
 - ST (cash), MT (depreciation), LT (opportunity costs)
 - Zero economic profits does not mean zero financial profits
 - Characterized by small margins at all sectors
- The Cattle Cycle
 - Long-term average vs. annual
 - Supply Chain dynamics (one's output is another's input)
- Multiple data sources
 - agri-benchmark (2006-2015 annual)
 - Canfax TRENDS model (monthly)
- Risk Management
 - Price Insurance
 - Alternative Marketing Arrangements





Canadian feedlot margins small & volatile

Annual Feedlot Profit/Loss



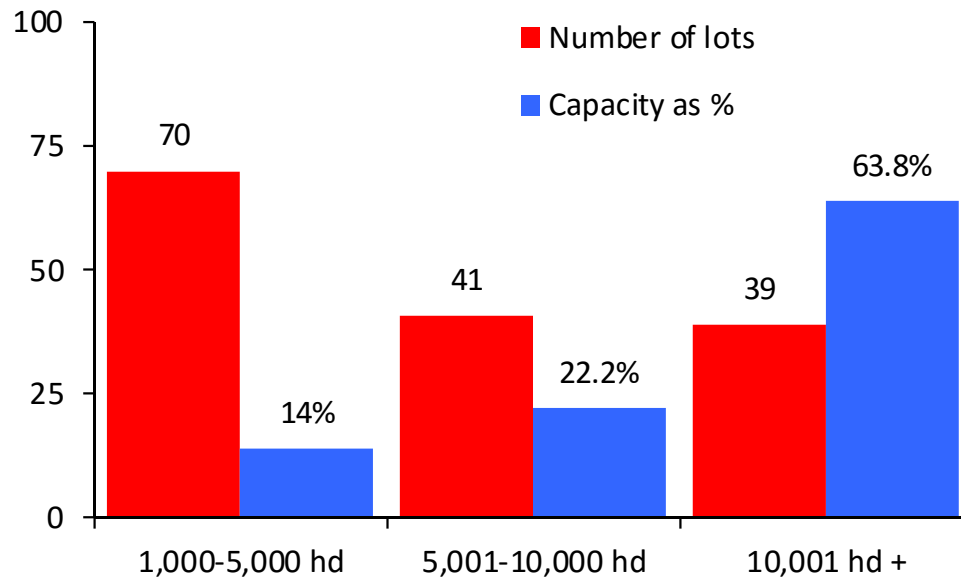
Source: Canfax Trends, Bank of Canada



Sustainable Farm Size

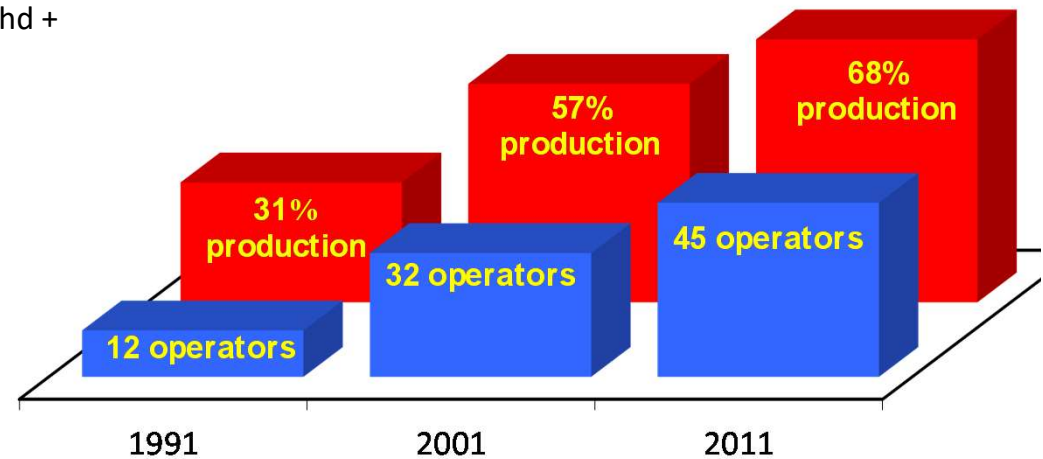
Consolidation of feedlots – larger lots but less of them!

Alberta/Sask Bunk Capacity - Jan 2016



Source: CanFax, AAFC

Concentration of Cattle Feeding in Alberta 10,000+ head feedlots





Demographics: infrastructure makes “feedlot alley” work

- Alberta finishes 70% of youthful cattle
- 36% of Alberta’s feedlot capacity is in Zone 3 “Feedlot Alley”
- Infrastructure in Lethbridge area includes:
 - Irrigation
 - Feed mills
 - Ag Suppliers
- Locally available feedstuffs
 - Potato's
 - Sugar beets

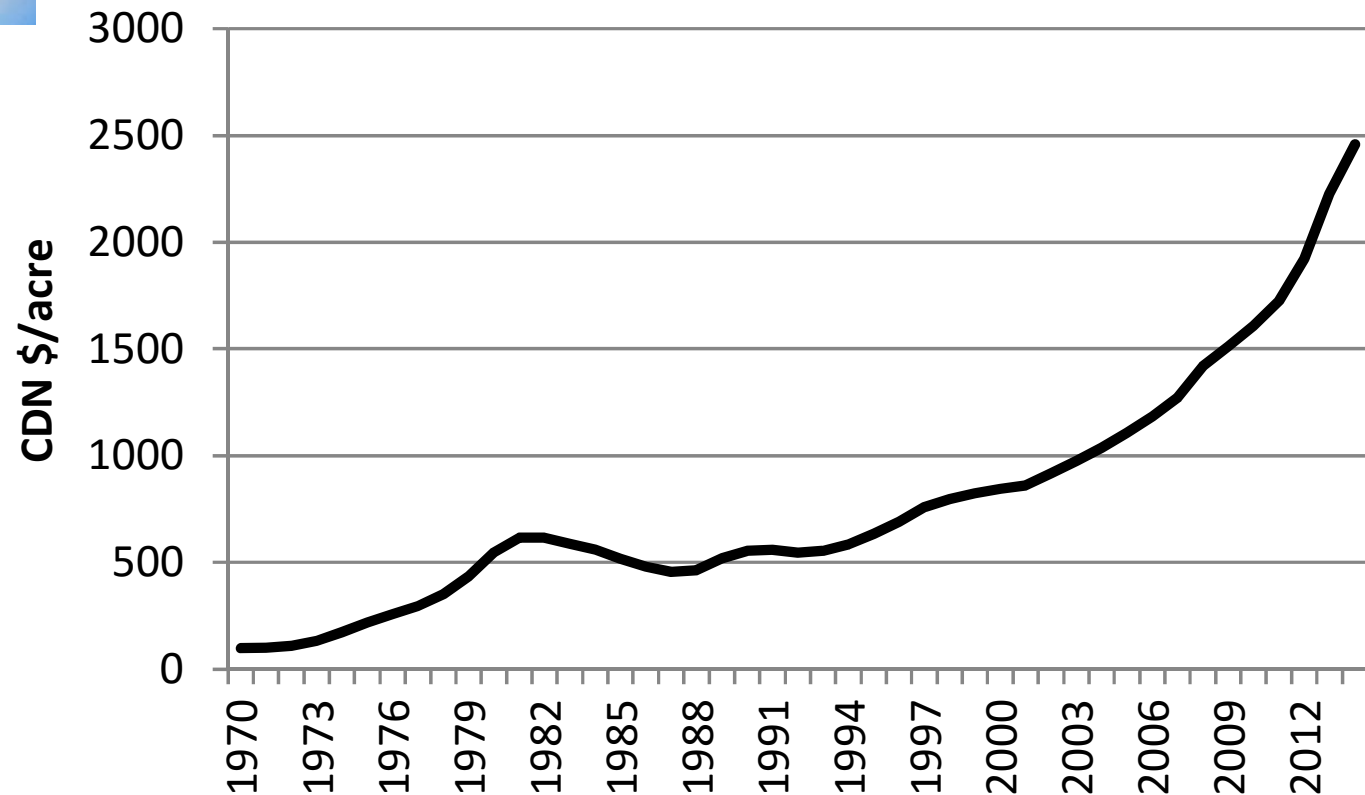




Protecting Equity – what is your retirement plan?



Value of Canadian Farmland

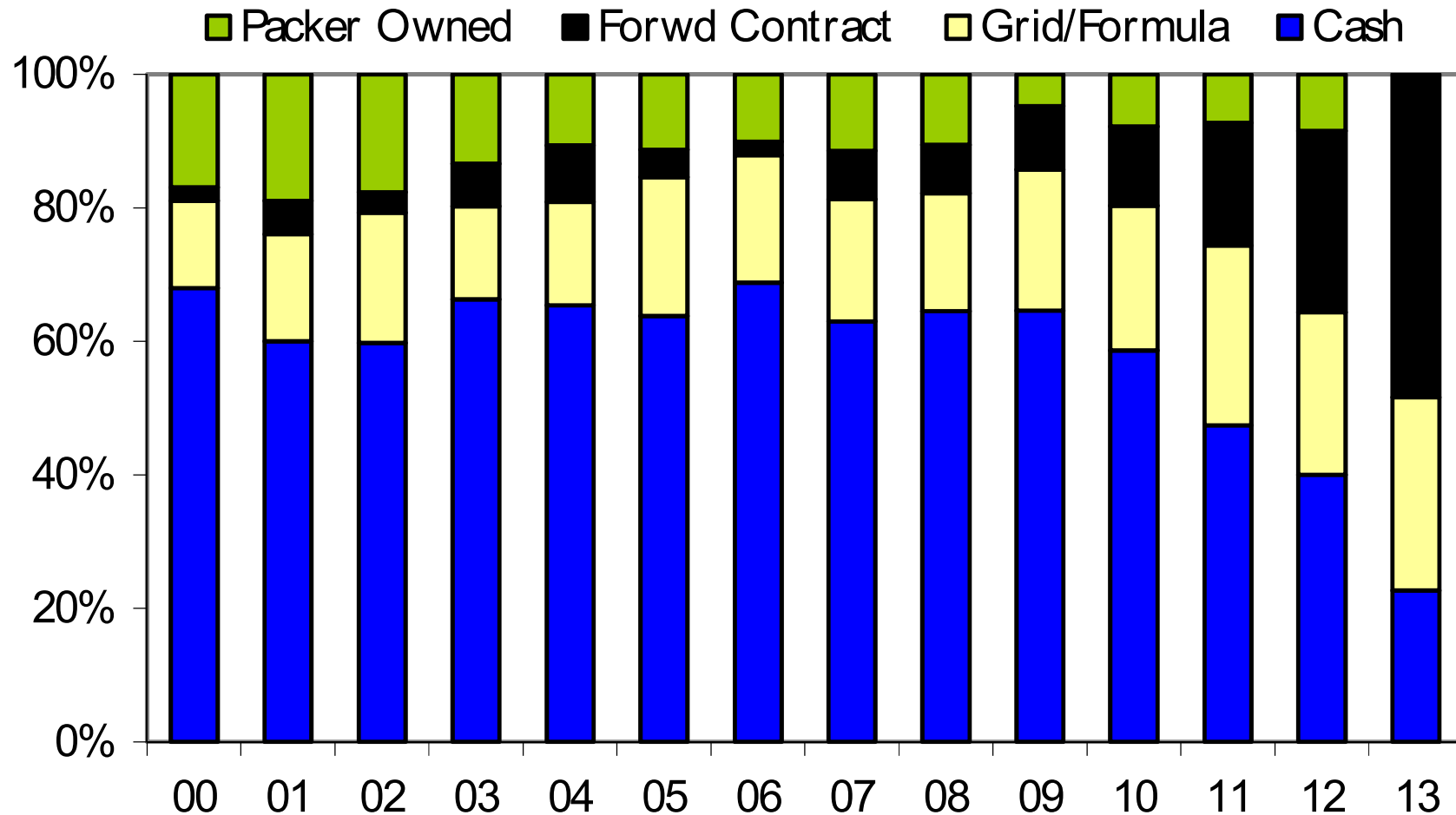


Source: Statistics Canada



Risk Management – ↑ use of Alternative Marketing Arrangements (AMAs)

Alberta Fed Cattle Procurement Mix

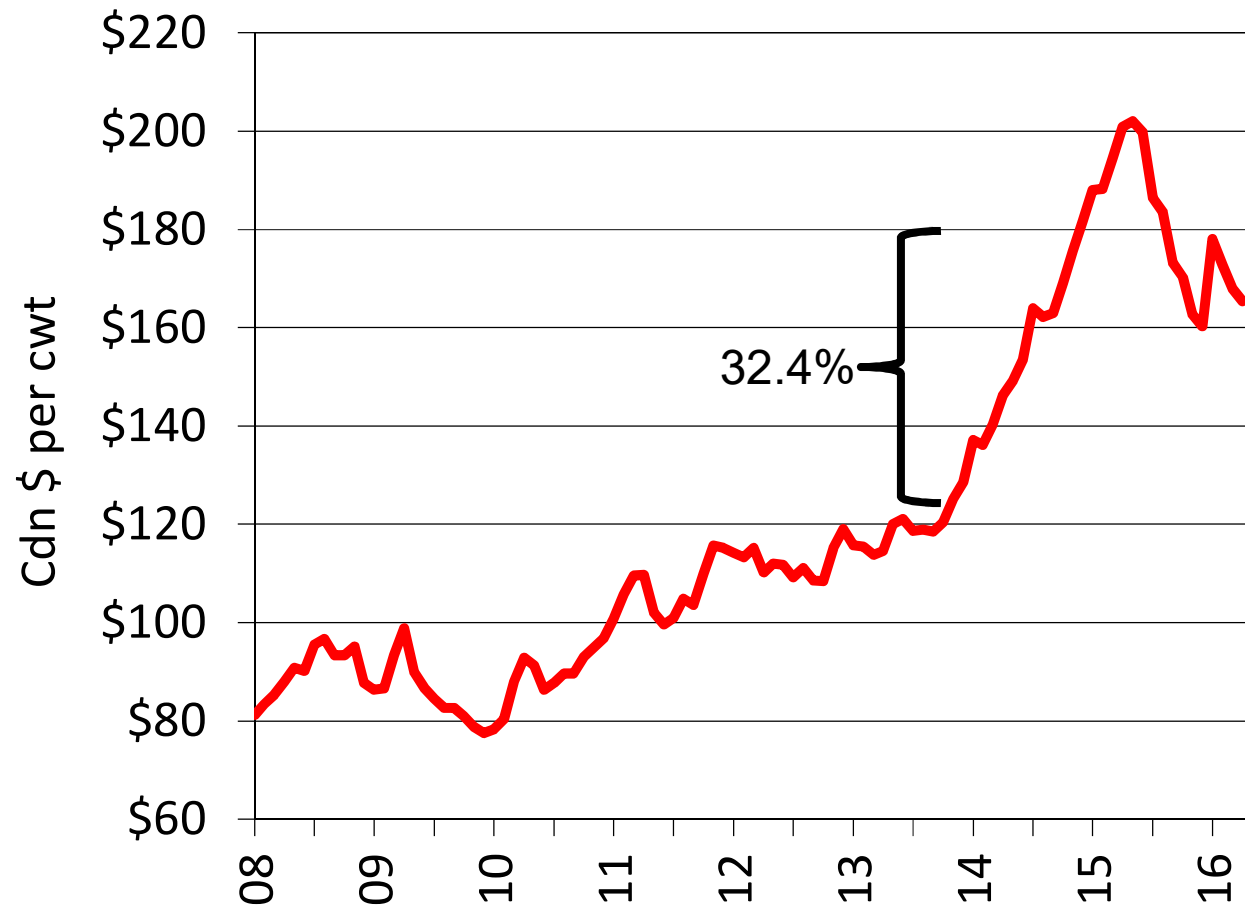


Source: Canfax



2014 – the incredible price rally

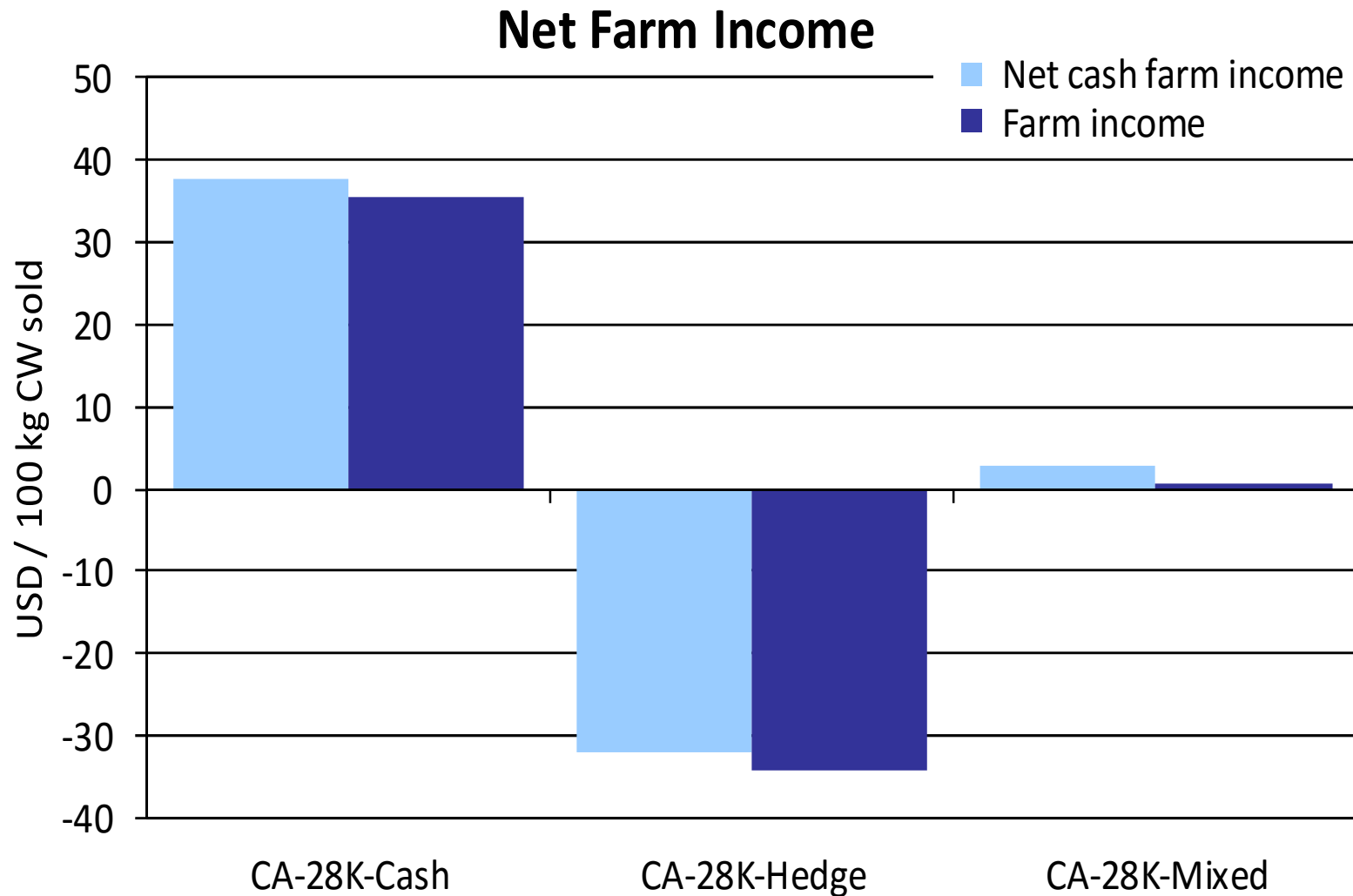
Alberta Fed Steer Prices



Source: CanFax



2014 – largest profits were on the cash cattle





2015 – the market turned

Alberta Fed Steer Prices

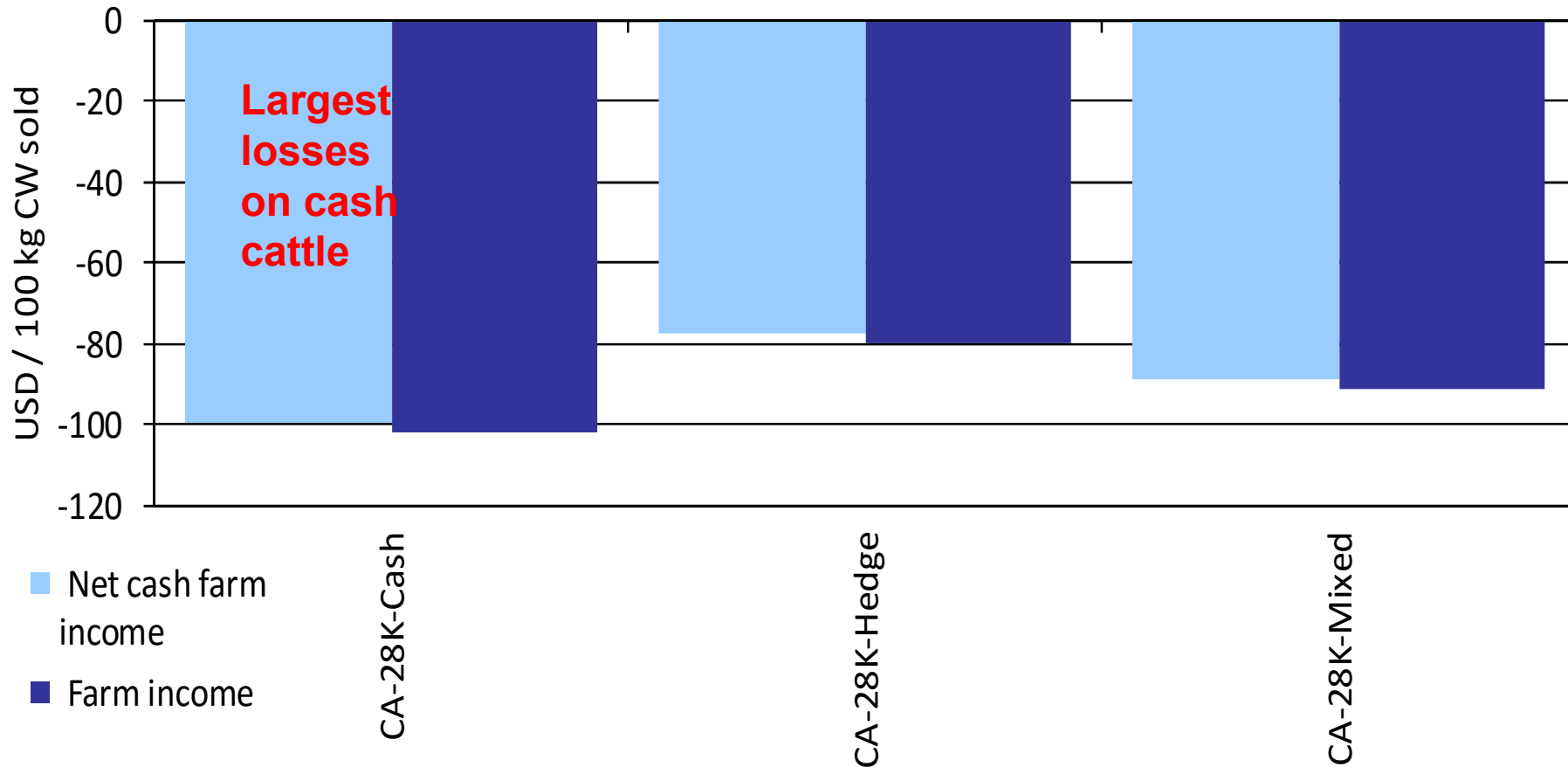


Source: CanFax



2015 – average losses ranged between \$80-100/head

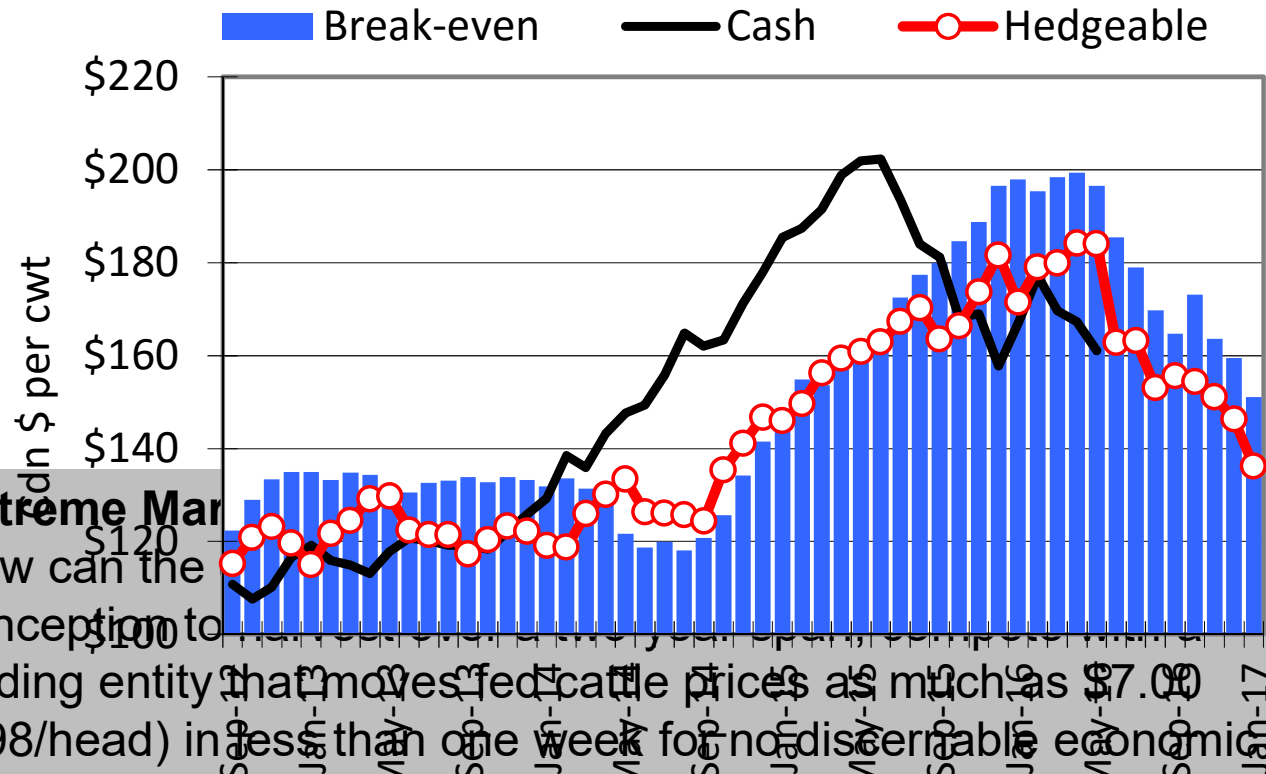
Net cash farm income and farm income per 100 kg CW sold





2016 - the losses continue... with extreme market volatility

Break-even vs Market Price STEER CALF



Extreme Market Volatility
How can the trading entity that moves fed cattle prices as much as \$7.00 (\$98/head) in less than one week for no discernable economic reason? They can't. **Cattle that might have been profitable on Tuesday could easily \$50 in the red on Thursday as a result of the extreme volatility.** ~ Hales April 29, 2016

Source: Canfax Trends West



Labour – big challenge

LABOUR AND SKILLS SHORTAGES IN CANADA: **led Labour Shortage Canada**
ADDRESSING CURRENT AND FUTURE CHALLENGES : 1

Report of the Standing
Human Resources, Skills and
and the Status of Persons

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Ag labour shortage getting worse

Posted Mar. 18th, 2016 by [Robert Amason](#)

Help wanted: The job crisis in Canadian agriculture

Jobs, But Lacks People

| Canada Business

e, Skills Shortage Canada, Skilled Labour
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, In Demand Jobs Canada,



r Shortage?



Labour is costing the beef industry

- Unfilled vacancies (6%) are costing the beef industry **\$141 million** in sales (farm gate cash receipts) in 2014 (CAHRC, CBC).
- Current gap estimated at 2,700 workers projected to quadruple to 12,500 workers in 10 years.
- Retirement of beef cattle producers is the driving factor behind reduced labour; CAHRC & CBC estimate that **one-third** of the current workforce will retire over the next decade. Producers over 65 years old, make up 15% of the current labour force with a portion of the 45-65 year olds also retiring.

Succession:

- Transfer of wealth
- Where is the next generation coming from?
- An unprofitable operation will not be passed on.



Risk Management

- Diversification vs. Specialization
- Cash vs. AMA (e.g. contracts, formulas, grids)
- Economies of Scale
 - Where do the economies come from?
 - Logistics/leverage: Multiple locations, single owner
- Tools
 - CME, hedging, basis & exchange risk, margin calls
 - Price Insurance: regional variability in programs

Diversification is a defense against ignorance, it makes little sense if you know what you are doing. - *Warren Buffet*

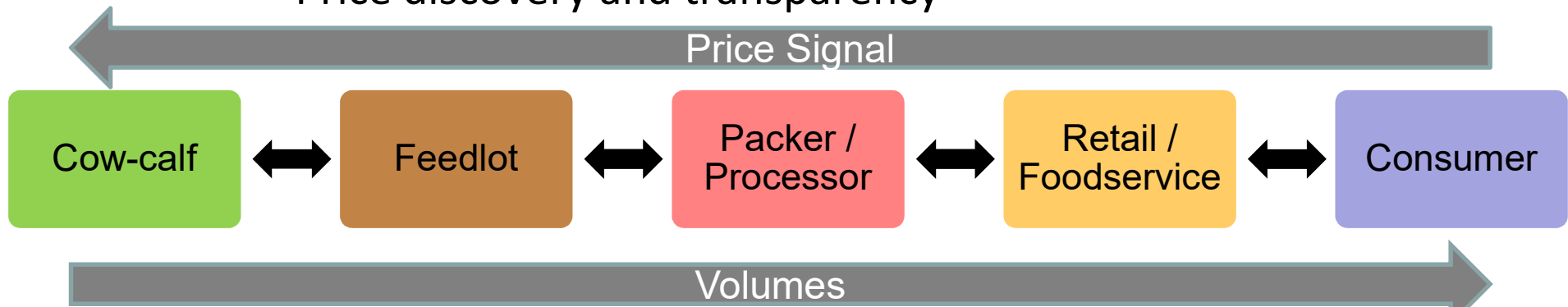
Specialization is the way of the future. If you have risk management specialization can foster greater productivity and efficiency.



Profitable but uncompetitive?



- Domestically vs. other commodities
 - Loss of land and labour resources
- International
 - Feeder exports: US feedlot will bid feeder cattle away
 - Priced out of the market, loss of market share and shrinking industry for finished beef cattle
- **Price signals** through the supply chain
 - Responding to changing demand for attributes
 - Price discovery and transparency





International Competitiveness

If packers are uncompetitive – fed cattle get exported to the U.S.

If feedlots are uncompetitive – feeder cattle get exported to the U.S.

If cow/calf operations are uncompetitive – industry shrinks!

Competitiveness is more than per unit COP:

1. **Transaction costs** influence the efficiency with which price and quality information flow along a supply chain, the incentives for investing in specific assets, and the nature of vertical linkages between producers, processors and distributors.
2. The closer **the vertical linkages** the more the industry is able to respond to the quality needs of different markets, enhancing **pricing efficiency** and operational efficiency.
 - Quality assurance & food safety
 - Traceability
 - Market specific contracts
 - Individual animal management

Consumer Resilience





Domestic Consumer Resilience

Quality & Consistency

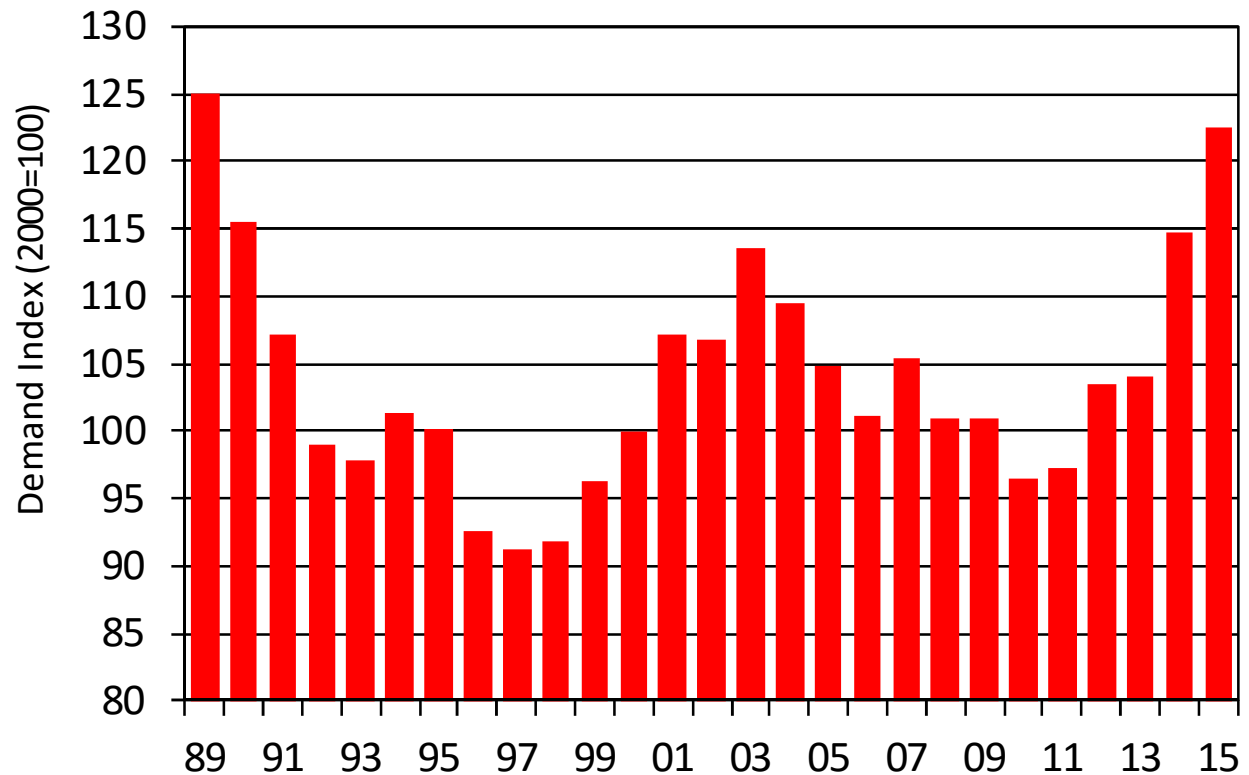
Health Perceptions

Food Safety

Consumer Preferences
(convenience, specific attributes)

Relative Price of Alternative Proteins & cuts

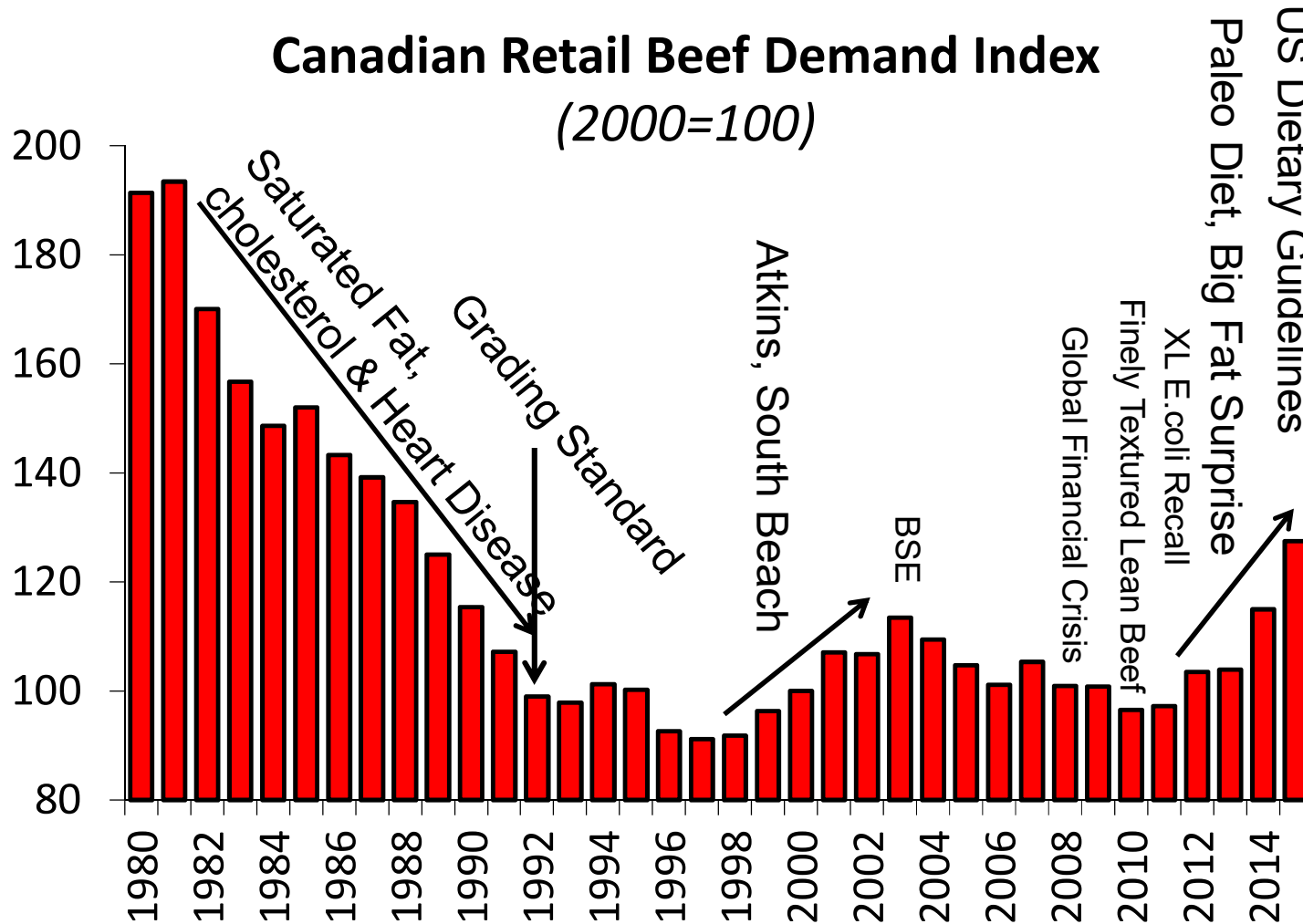
Canadian Retail Beef Demand Index
Index 2000=100



Source: Statistics Canada, CanFax, US Beef Demand Study Group



Health perceptions & product quality – can we reverse the 1980s?

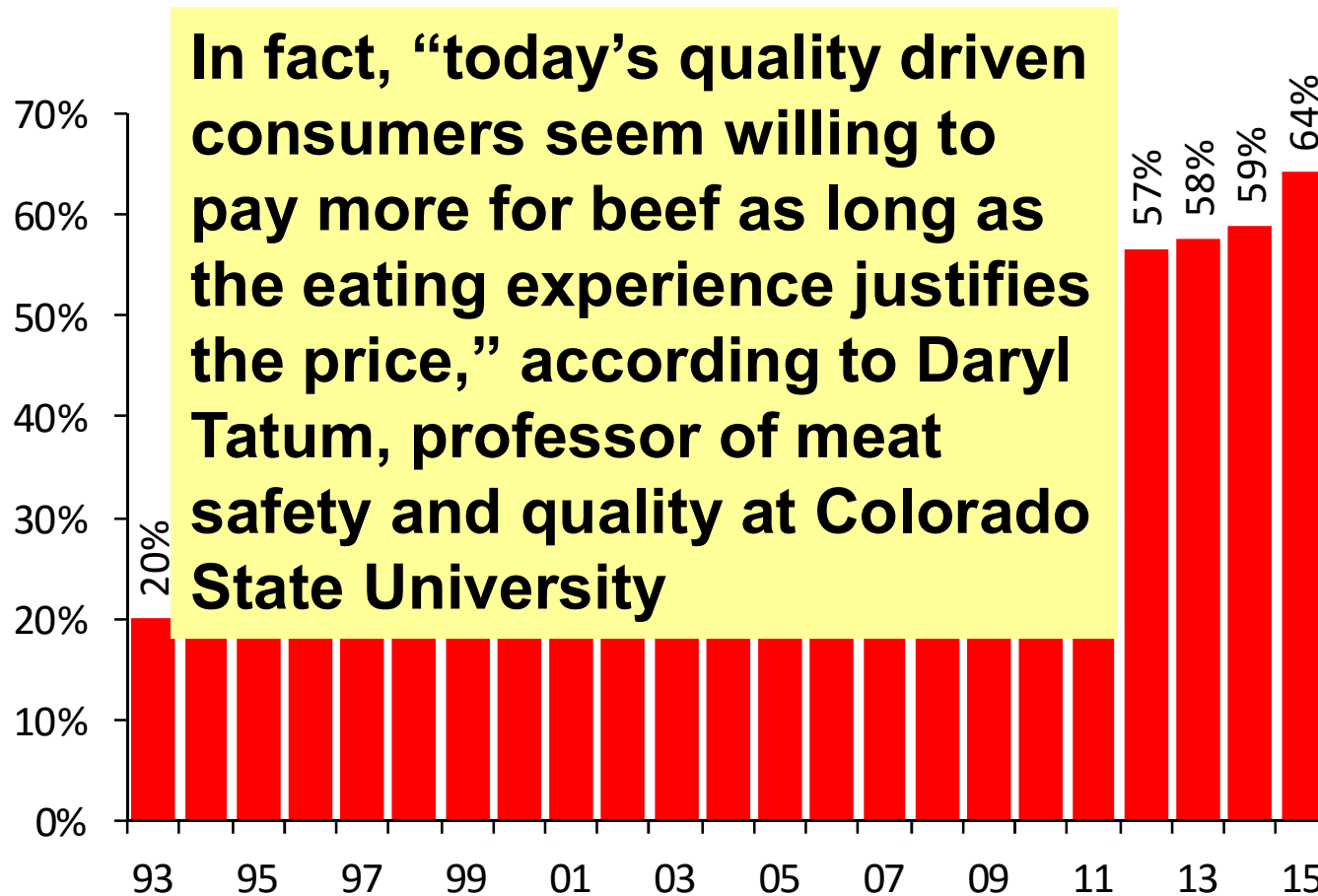


Source: CanFax Research



Producers contribution to supporting beef demand

Canadian AAA + Prime as a % of all A Grades





International Demand driven by Population & Income growth

Food Safety

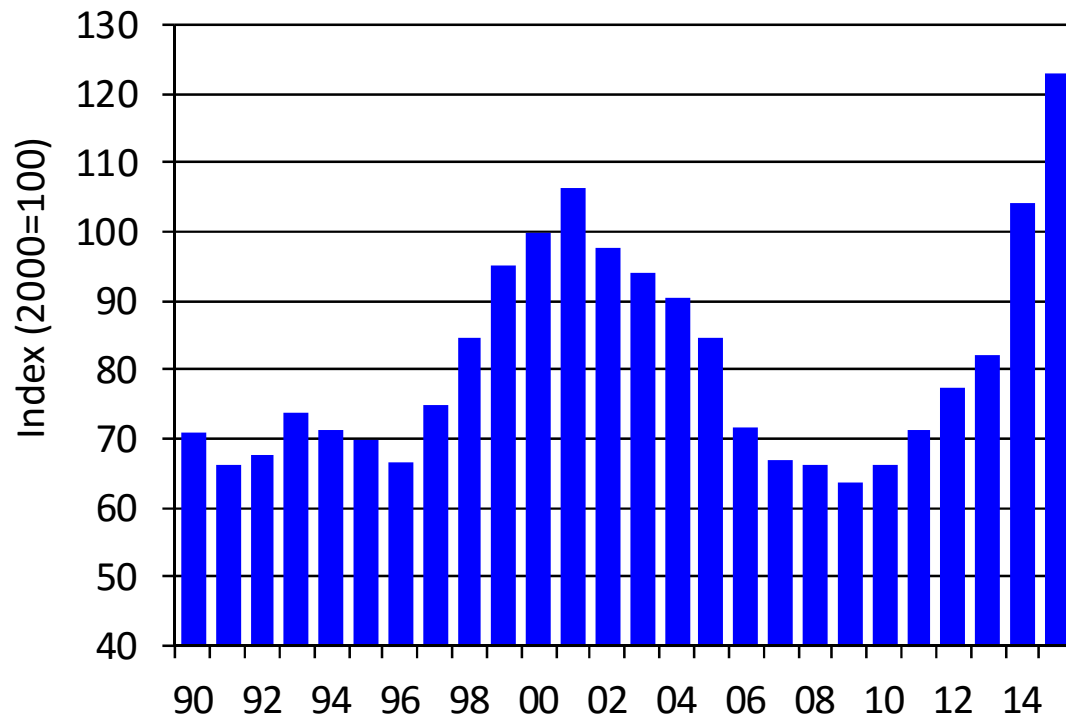
9 billion by 2050

An additional 3 billion middle class by 2050

Urban population to increase from 50% to 70%

FAO projects a 60% increase in consumption of meat, milk and eggs

International Beef Demand Index





Commercially Viable Market Access

- Strong international demand represents an opportunity for the Canadian beef industry in the global market.
- In order to take advantage of this Canada must have **reliable market access** and the **ability to compete** with other grain-fed beef producers.
- **Commercially Viable:**
 - Limited access (e.g. UTM/OTM, bone-in/boneless, fresh/frozen)
 - Packer approvals
 - Competitive tariff levels
 - Regulatory barriers (e.g. Non-Tariff Trade Barriers, SPS)

A photograph of a herd of cattle in a green field at sunset. The sky is filled with golden and orange clouds, and the sun is low on the horizon. The cattle are of various colors, including brown and black, and some have red ear tags. The overall scene is peaceful and scenic.

Continuous Improvement

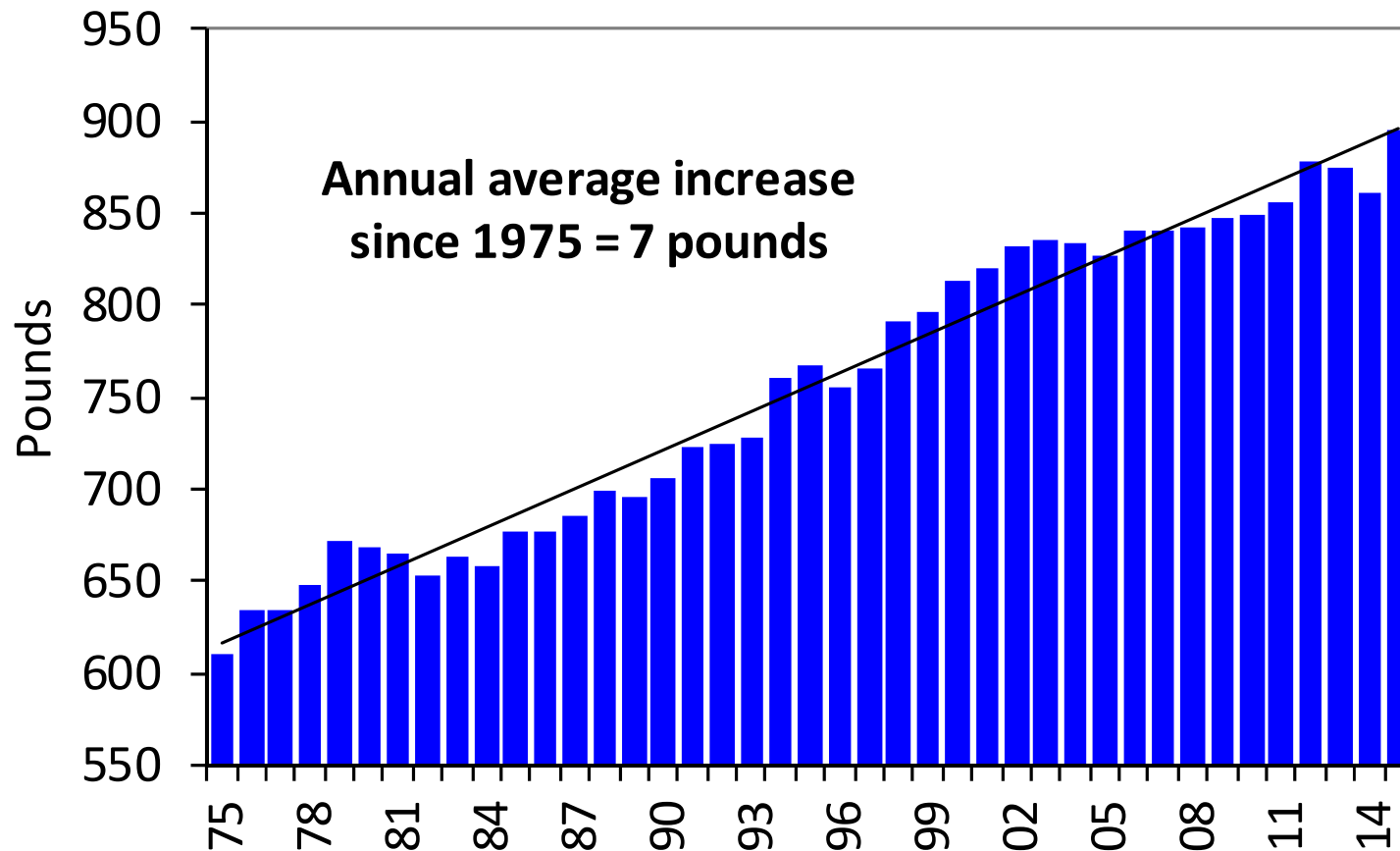
Do not expect profitability to continuously improve. But we do need to see producers and marketers adapting to changing market environment and consumer preferences.

Sherri Grant



Fewer cows needed today to produce more pounds of beef: *Carcass weights up 7 lbs/year*

Canadian Annual Steer Carcass Weight





Feed efficiency is good for both the environment and economic sustainability

1950's feed efficiency was 10:1



TODAY IT'S 6:1



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Productivity & Profitability

Diversity in geographic, climate, operations and structures.

- The physical environment will influence if you are high or low cash costs.
- High cash costs, high productivity – low per unit COP
- Low cash costs, low productivity – low per unit COP

While productivity support both economic and environmental sustainability...

Productivity is not enough