



## **CANFAX RESEARCH SERVICES 2010 ANNUAL OUTLOOK**

---



A PUBLICATION OF THE CANADIAN CATTLEMEN'S ASSOCIATION

## Foreword

The Canadian beef industry has faced a number of challenges over the last seven years including significant market turmoil, fluctuating exchange rates, the incidence of animal disease and food safety outbreaks, continued market access limitations, drought and new regulations. Over the last year global economic and financial uncertainty has changed access to credit for producers and consumers. In addition, increased unemployment and more conscientious consumers have changed their preferences at the meat counter.

Despite the economic struggles over the last year, long term global meat trade is expected to continue to expand. The outlook for GDP growth in developed countries is expected to be positive in 2010 and in fact beef exports increased in the last part of 2009 to certain countries. Canada is strongly positioned to take advantage of these opportunities in the global market place. However, success continues to be dependent upon regaining and expanding market access in key markets.

Volatility in the commodity markets and squeezed margins throughout the various sectors of the beef industry has made planning increasingly difficult - yet vitally important for producers as they look to managing risk in both input costs and market prices. Canfax Research Services is pleased to offer this second annual publication which is meant to assist industry. We trust that this publication is a valuable resource and will be a useful tool in managing your operations. We welcome your feedback on this publication. Recommendations or comments can be sent to [crs@canfax.ca](mailto:crs@canfax.ca). We wish you all the best in the coming year.

Brenna Grant  
Research Analyst

### **CANFAX RESEARCH SERVICES**

Email: [crs@canfax.ca](mailto:crs@canfax.ca)

Phone: 403.275.8558

Fax: 403.275.6943

Website: [www.canfax.ca](http://www.canfax.ca)

## **Table of Contents**

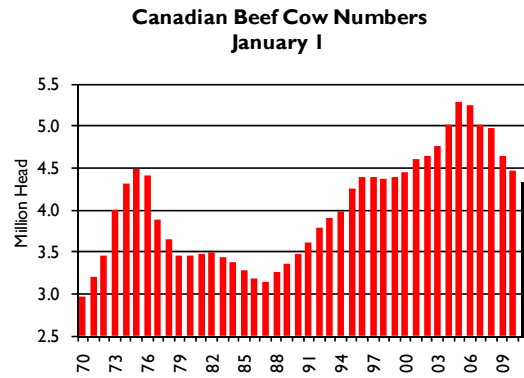
### **2009 Market Context**

Cattle Inventories	1
Prices	2
Fed Cattle	
Feeder Cattle	
Cow Prices	
Live Cattle Exports	5
Domestic Slaughter	5
Slaughter Capacity & Utilization	
Beef Production	6
Fed Production	
Non-Fed Production	
Boxed Beef Cutout Values	8
Competing Meats	9
Consumption	10
Trade	11
Canadian Beef and Cattle Exports	
Total Volume and Value of Beef Exports	
Beef Imports	
Trade Market Access Situation & Outlook	14
<b>Canadian 2010 Cattle &amp; Beef Supply Outlook</b>	<b>15</b>

## 2009 Market Context

### Cattle Inventories

January 1, 2010 total cattle inventories were down 1.3 per cent to 13.0 million head, while beef cow numbers were down 3.8 per cent to 4.47 million head. This is the smallest beef cow inventory since 2000. The smaller decrease in total inventories, as compared to beef cow numbers, was due to reduced fed and feeder exports that resulted in increased beef heifers for slaughter and steer inventories. Beef heifers for slaughter were up 9.1 per cent to 899,800 head. Steer numbers were up 7.9 per cent year over year to 1.14 million head.



Inventory reductions were expected given poor profitability in the Canadian cattle industry over the last several years. In addition to continued market access limitations associated with BSE trade restrictions that have limited exports of Canadian beef and cattle, the Canadian beef industry has been impacted by significant market uncertainty, volatile energy and feed costs, and a strong Canadian dollar. Increased costs for the Canadian industry are associated with the enhanced feed ban and the implementation of U.S. mandatory Country of Origin Labelling (COOL). Both market dynamics and regulatory costs have reduced returns across all sectors of the industry and provided clear signals for the reduction of the Canadian cow herd. In 2009 reductions were further accelerated, when drought in many major production regions and the associated feed uncertainty encouraged larger volumes of cows to move to market.

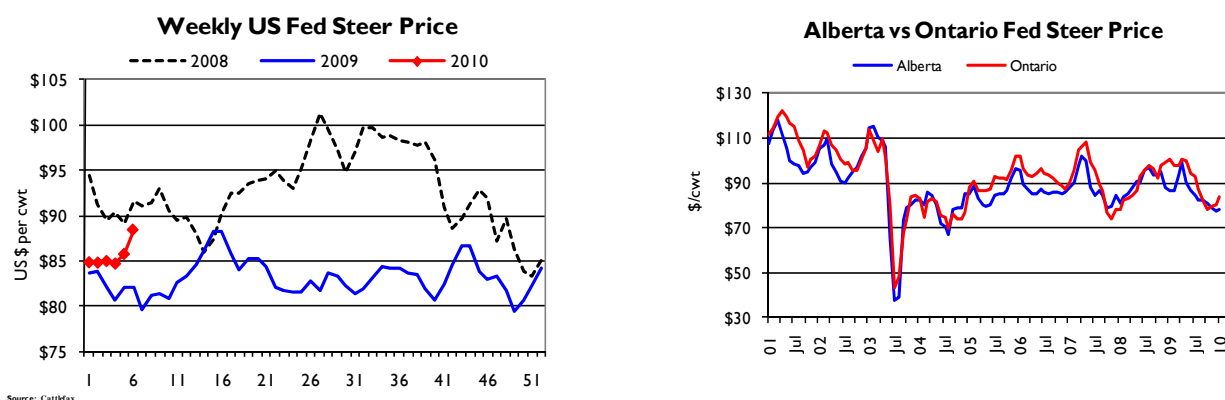
Canadian Cattle Inventory – January 1 (1,000 head)			
	2009	2010	% change
Bulls	243.9	230.1	-5.7%
Beef Cows	4,649.5	4,471.0	-3.8%
Dairy Cows	977.9	981.0	0.3%
Dairy Hfrs	455.6	458.7	0.7%
Beef Hfrs (brdng)	537.0	516.4	-3.8%
Beef Hfrs (sltr)	824.5	899.8	9.1%
Steers (> 1yr)	1,057.6	1,140.7	7.9%
Calves (< 1yr)	4,434.0	4,317.3	-2.6%
Total	13,180.0	13,015.0	-1.3%

Provincially the largest declines in beef cow inventories were seen in the west with British Columbia down 7.1 per cent, Manitoba down 3 per cent and Alberta down 6.5 per cent. This was followed by a reduction of 3.5 per cent in Quebec, 1.8 per cent in Ontario and 0.7 per cent in Saskatchewan. The smaller cow herd over the last four years will reduce beef calf numbers, which will result in tighter fed supplies moving forward. Further reductions in the beef cow herd are expected in 2010. With beef heifers for slaughter up 9.1 per cent and beef replacement heifers down 3.8 per cent, producers have not provided any indication of expanding the national herd within the next year.

## Prices

### Fed Cattle

U.S. fed prices averaged US\$83/cwt in 2009 down US\$10/cwt from 2008. Throughout 2009 U.S. fed prices traded in a very narrow range, between US\$80 and US\$88, as poor consumer demand prevented prices from moving upward despite tighter supplies. In 2009 Canadian fed cattle prices faced significant downward pressure due to the appreciating Canadian dollar and competition from increased pork supplies on the domestic market. Only a short seasonal rally was observed in spring 2009 when a period of extremely tight supplies existed between yearlings and calves being ready for market. In 2009, Alberta and Ontario fed cattle prices averaged \$86/cwt and \$91/cwt, down \$3/cwt and up \$1/cwt from 2008 respectively.



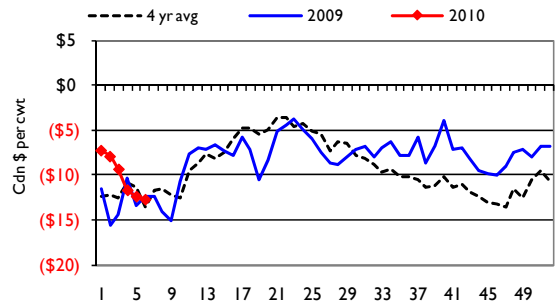
Source: CattleFax

In addition to recessionary pressures and large pork supplies providing limited upside opportunities for cutout values and consequently fed cattle prices, a large part of the fed cattle story in 2009 was about carcass weights. U.S. carcass weights in 2009 averaged 847 lbs up 22 lbs from 2008 levels in the first quarter and 9 lbs in the second. Not until the end of October did U.S. carcass weights drop below 2008 levels, as larger animals were cleaned up and animals were pulled forward. While large carcass weights pressured U.S. fed cattle prices in the first part of the year, larger carcass weights were seen in Canada in the second half of the year. With optimal production conditions and packers comfortably bought and not picking up cattle for several weeks, Canadian steer carcass weights in the third and fourth quarter of 2009 averaged 858 and 878, up 13 lbs and 38 lbs from the same time periods in 2008. These heavy carcass weights have pressured prices downwards. With such long delays before domestic packers are picking up cattle there has been renewed interest in selling cattle south. It should be noted that all of the increase in the Canadian carcass weights came from Alberta, with Ontario carcass weights trending similar to last year's levels which when coinciding with reduced supplies has provided some level of price support in Eastern Canada.

Moving into 2010 significantly larger fed marketings are expected for the first quarter in the U.S., which is anticipated to pull Canadian prices down unless the basis narrows even more. The Alberta to Nebraska cash to cash basis averaged \$8.40/cwt in 2009, steady with 2008. After being wider in the first two quarters at \$12/cwt and \$6.50/cwt compared to \$7/cwt and \$4/cwt in 2008, due to uncertainty around COOL, the basis in third quarter 2009 was steady

with the prior year at \$7.50/cwt. The 2009 fourth quarter has seen the basis narrow to \$8/cwt compared to \$15/cwt in 2008. Preliminary research that has focused on isolating the impact of COOL on the fed cattle basis from other market factors, estimates that the impact of COOL in Alberta has been around \$2.15/cwt while in Ontario the impact has been larger at \$3.58/cwt.

**Alberta Fed Steer Basis  
Alberta/Nebraska in Cdn \$ (Cash to Cash)**

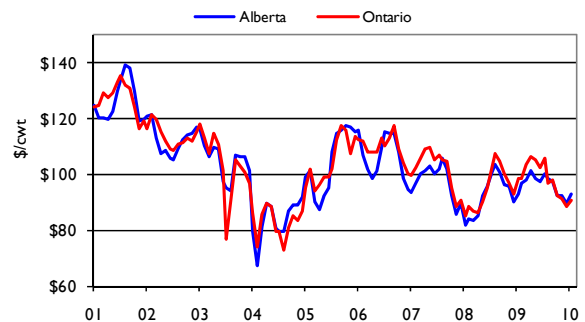


Source: CanFax

### Feeder Cattle

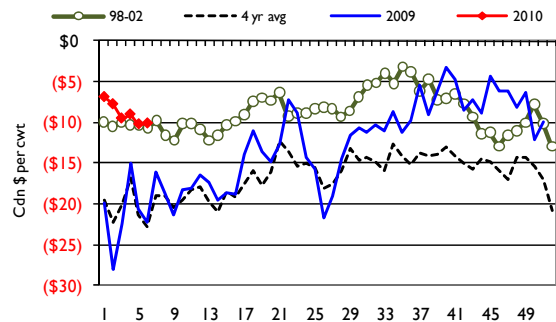
Alberta and Ontario 8-900 lb feeder steer prices averaged \$97/cwt and \$99/cwt in 2009, up \$4/cwt from 2008. Feeder prices in the spring of 2009 were supported by strong demand for grass cattle. Drought brought these cattle back to market early and saw large yearling supplies, in combination with limited upside for fat cattle prices, depress market prices in the summer. Feeder prices were expected to be pressured down in the fall 2009 with the stronger dollar and lower live cattle futures. However prices were supported by a smaller calf crop and strong demand by domestic feedlots to keep cattle in Canada, as seen by the narrowing feeder basis.

**Alberta vs Ontario 850 Feeder Steer Price**



The 2009 feeder basis narrowed significantly after July and is now at pre-BSE levels for the first time since 2003. In the fourth quarter 2009 the basis has been significantly narrower at \$6/cwt compared to \$20/cwt year ago. The basis has averaged \$13/cwt in 2009 compared to \$17.50/cwt in 2008. A narrower basis indicates stronger demand/smaller supply in Canada compared to the U.S. Despite the fact that a number of smaller feedlots are sitting empty, the large reduction in supplies and relatively strong Canadian feedlot demand due to a reduced cost of gain when compared to the previous two years has encouraged domestic placements of Canadian feeders. It is important to note that cost of gain has been by no means cheap, with it still well above historical levels.

**Alberta 850 lb Feeder Steer Basis**



Source: CanFax

A lower cost of gain has emerged primarily as a result of reduced feed grain prices. Despite a substantial decline in domestic barley production in 2009, barley prices have fallen with strong global production and decreased export demand. U.S. corn prices have also declined from previous highs due to reduced demand for corn for ethanol production with lower energy

prices and larger than expected global supplies. The U.S. corn crop came in at 13.1 billion bushels - a record high and 1 per cent higher than the previous high seen in 2007, placing global corn supplies in a relatively positive position.

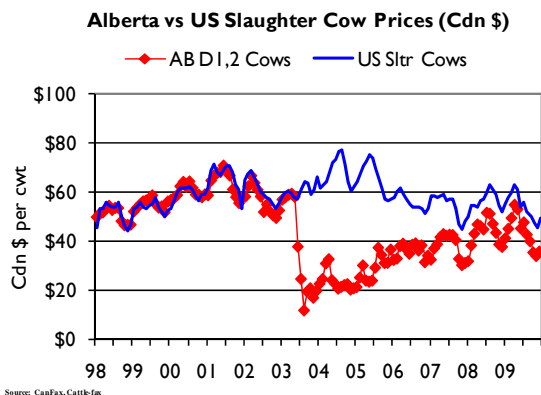
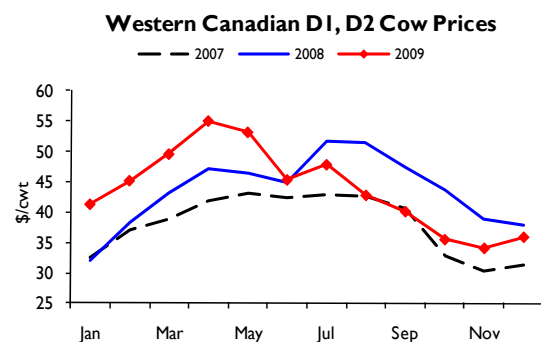
Feeder exports in 2009 were down 55 per cent, due to a narrower basis caused by reduced supplies and strong domestic demand for feeders, as well as COOL which has reduced U.S. feedlot demand for Canadian feeders. Total feeder exports finished the year at 283,000 head, which is still above the 98-02 annual average of 229,000 head. Moving into 2010 feeder exports are expected to continue to remain at lower levels, due to COOL continuing to create uncertain demand by U.S. packers for 'B' label cattle (Canadian feeders fed in the U.S.) and a more comparable cost of gain between the two countries.

### Cow Prices

Alberta cow prices averaged \$44/cwt in 2009, while Ontario cow prices averaged \$48/cwt. This reflects a \$0.50 increase in Alberta and a \$2 decrease in Ontario cow prices when compared to 2008. Cow prices have been pressured by large dairy and beef cow supplies for slaughter in North America, in combination with increased non-NAFTA imports to fulfill demands for lean trim. In

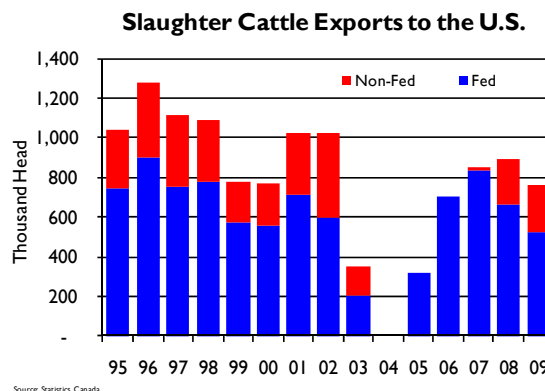
2009 the U.S. saw three dairy retirement programs that increased dairy cow slaughter by 9 per cent and pressured North American prices at various times throughout the year. Imports of beef from non-NAFTA countries are up 43 per cent. Eighty-five per cent lean trim prices have been moving steadily down since peaking in April 2009. In November 2009 lean trim prices averaged \$112/cwt, down \$51 from the spring peak of \$163/cwt and down \$54 from a year ago. Non-NAFTA lean trim imports are expected to continue to increase, in light of decreasing cow slaughter and strong consumer demand for ground beef in the current economic environment. Moving into 2010, cow prices should see support as supplies continue to tighten in North America with smaller inventories. This is barring any further dairy retirement programs in the U.S. or major droughts that encourage large numbers of animals to move to market in a relatively short period of time.

Canadian cow prices have trended \$10/cwt under the U.S. prices throughout 2009, due to the longer specified risk material (SRM) list for Canadian packers for over-thirty month animals when compared to U.S. packers. This provides the U.S. packer with the ability to pay more for cows. Despite this extra ability to pay more for cows in the U.S., age verification requirements under Rule II have kept Canadian cow exports relatively steady at 199,000 head for the year.



## Live Cattle Exports

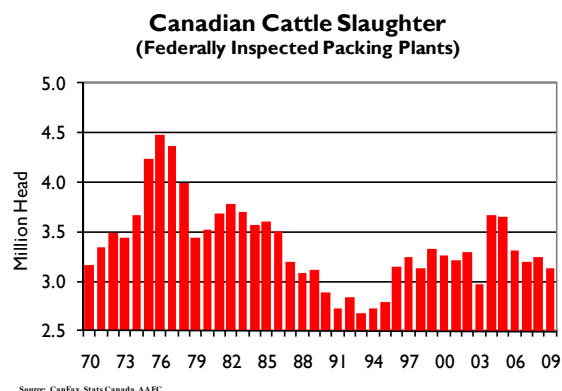
Similar to the trend seen with feeder cattle exports, fed cattle exports are down 21 per cent in 2009 at 523,000 head. Reduced fed cattle exports can be attributed to several factors including smaller inventories combined with steady domestic packer demand and COOL reducing U.S. packer demand. In the first 10 months of 2009 monthly volumes averaged 23 per cent lower than 2008. But in November and December volumes were down 4 per cent and 3 per cent. This provides some indication of a stable trend since COOL started and also is an indication of the current backlog of animals moving to domestic packers, encouraging Canadian feeders to more aggressively market cattle south of the border to avoid additional days on feed and quality discounts associated with heavy cattle.



Slaughter cow and bull (non-fed) exports have not been as negatively impacted by COOL, since these animals are primarily directed to processors in the U.S. that are producing large volumes of ground beef. While ground beef is not exempt from COOL regulations, the labelling requirements are more flexible to account for multiple country sources. In 2009 slaughter cow exports to the U.S. were up 7 per cent from 2008, while bull exports were down 16 per cent. Cow and bull exports totalled 239,500 head in 2009.

## Domestic Slaughter

Canadian slaughter (federally and provincially inspected) was down 4 per cent in 2009 at 3.39 million head. Decreased slaughter numbers were expected, with tighter fed cattle and cow supplies. Total fed cattle slaughter was steady at 2.69 million head. With fed cattle marketings down 3.6 per cent in 2009, all of the reduction was seen in reduced fed cattle exports while domestic fed cattle slaughter remained steady. Lower total slaughter was a result of a 19 per cent reduction in cow slaughter, which declined from 807,000 head in 2008 to 653,000 head in 2009. Bull slaughter was up 12 per cent in 2009 to 42,000 head.



The composition of total slaughter shifted in 2009, with fed cattle accounting for a higher proportion of slaughter at 80 per cent compared to 76 per cent in 2008. In 2009, 48 per cent of

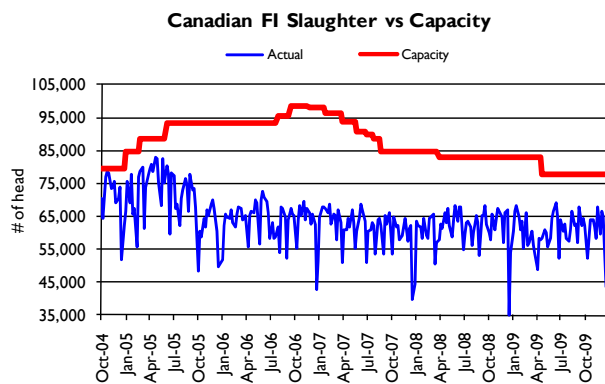
total slaughter was made up of steers, 31.5 per cent heifers, 19 per cent cows and 1.2 per cent bulls. Shifts in regional slaughter observed in 2008 also continued. Larger decreases are apparent in eastern Canadian slaughter levels, which were down 5 per cent compared to

Western Canada where slaughter was down 3 per cent. Eastern Canada has seen a larger reduction in heifer slaughter, which is down 7 per cent as compared to western Canada where heifer slaughter was up 3 percent. This implies that Eastern Canadian producers may be starting to retain heifers.

% Change in FI/PI Canadian Cattle Slaughter (2009/2008)			
	% Δ Western Slaughter	% Δ Eastern Slaughter	% Δ Total Slaughter
Steer	+2%	n/c	+1%
Heifer	+3%	-7%	n/c
Cow	-19%	-18%	-19%
Bull	-14%	+40%	+12%
Total	-3%	-5%	-4%

### Slaughter Capacity and Utilization

The relationship between total marketings and domestic slaughter was steady in 2007 and 2008 at 74 per cent. In 2009 slaughter as a proportion of total marketings increased to 76 per cent, as both marketings and slaughter declined with tighter supplies. As inventories decrease excess capacity has become increasingly apparent. Plants continue to close; most notably XL Moose Jaw closed their cow plant for the 2009 summer and failed to reopen in September. Labour issues were quoted as the major reason for the closure of this plant, but reduced supplies is also expected to have played a role.

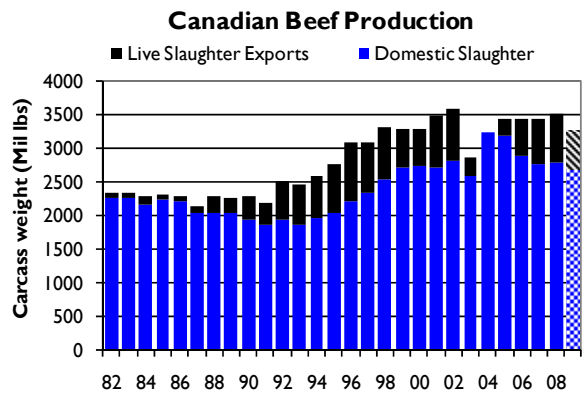


Utilization levels continue to struggle despite improved labour availability and COOL; primarily due to smaller marketings being available for purchase. Plant utilization averaged 77 per cent in 2009, compared to 76 per cent in 2008, with reduced domestic slaughter being offset by reductions in capacity in 2009 to support utilization. Plant utilization levels will need to be maintained in 2010 in order to compete with U.S. counterparts, but this will become increasingly difficult with smaller fed and non-fed cattle supplies and the potential for increased competition from U.S. packers for Canadian cattle as U.S. supplies tighten. In addition Canadian packer profitability continues to be challenged, as compared to the U.S., due to increased costs associated with the enhanced Canadian feed ban and specified risk material requirements.

### Beef Production

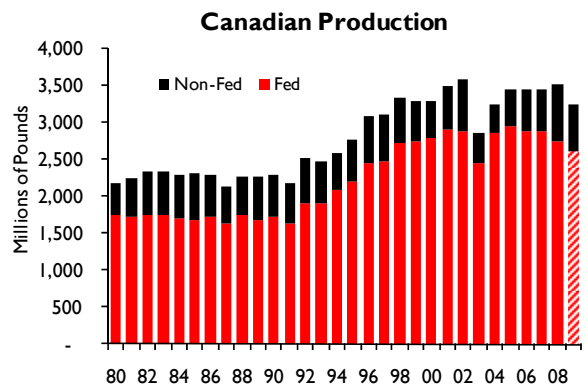
Total cattle marketings declined 6 per cent to 4.1 million head in 2009. With domestic slaughter down 4 per cent, the majority of the decline came from reduced slaughter cattle exports which were down 15 per cent from 896,000 head to 763,000 head in 2009.

Total Canadian beef production, which includes production derived from both domestic slaughter and slaughter cattle exports, was down 6 per cent to 1.54 million tonnes. This is the first decline in beef production since 2003, with production relatively steady at 1.6 million tonnes since 2005. The decline in beef production was seen in both domestic beef production, which was down 3 per cent to 1.22 million tonnes, and live slaughter exports which were down 16 per cent to 272,600 tonnes. The proportion of beef production derived from domestic slaughter increased to 82 per cent after being steady at 80 per cent for two years. Further declines in production are expected in coming years as both cow slaughter and fed cattle supplies continue to decrease. Overall smaller beef supplies, with smaller cow slaughter and fed cattle marketings, are expected to provide support to cattle prices if improvements in beef demand can be achieved as the economy recovers.



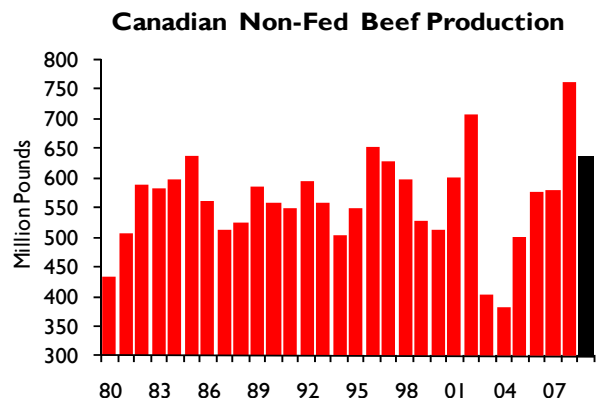
### Fed Production

A smaller calf crop and record large feeder cattle exports in 2008 resulted in a 3.6 per cent decline in fed cattle marketings in 2009 to 3.22 million head. With fed cattle exports to the U.S. down 21 per cent to 523,000 head, domestic slaughter did not see similar declines. Domestic slaughter was steady at 2.69 million head and steer carcass weights were up slightly to 846 pounds due to record high carcass weights in the second half of the year as domestic packers delayed pick up dates. Overall fed beef production decreased 3.5 per cent to 1.2 million tonnes, while domestic fed beef production remained steady at one million tonnes.



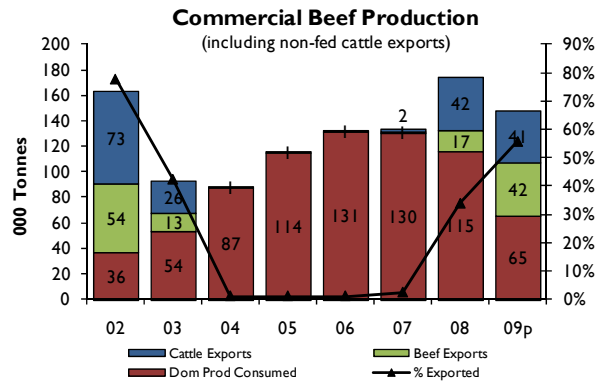
### Non-Fed Production

Non-fed beef production (derived from cows and bulls) was down 14 per cent from the record 345,000 tonnes in 2008 to 296,000 tonnes in 2009. With non-fed exports only down slightly, the majority of the reduction was seen in non-fed domestic beef supplies, which were down 20 per cent from 266,000 tonnes in 2008 to 218,000 tonnes. Cow



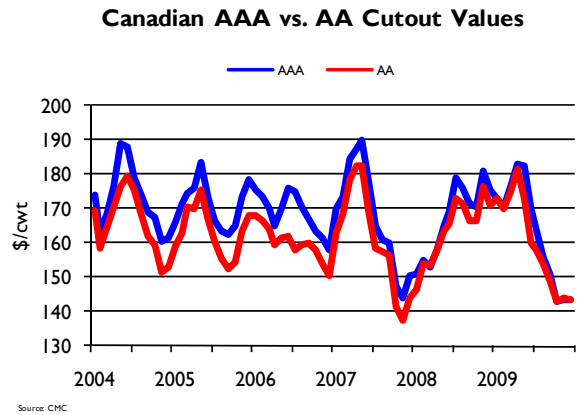
marketings were down 14 per cent with domestic slaughter down 19 per cent and exports up 7 per cent. Bull marketings were down 4 per cent, with slaughter up 12 per cent and exports down 16 per cent.

Of non-fed beef produced in Canada in 2009, it is estimated that 39 percent or 42,500 tonnes (boneless) was exported. This is up significantly from 2008 when an estimated 13 per cent of domestic non-fed beef production was exported. Strong exports were due to demand from a number of destinations that do not regularly look to Canada for trim/ground beef. When cattle exports are included a total of 83,000 tonnes or 56 per cent of non-fed beef production was exported in 2009.

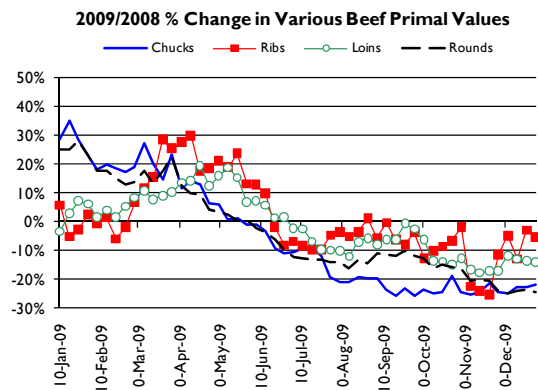


### Boxed Beef Cutout Values

The AAA cutout averaged \$163/cwt in 2009, down \$4 from 2008. The AA cutout averaged \$160/cwt, down \$3.50 from 2008. After seeing prices above 2008 levels for the first five months of year, cutout values have been moving steadily lower and are now close to the lows seen in late 2007. The cutout values have been pressured by larger protein supplies, weak consumer demand and an appreciating dollar throughout the year. The AAA cutout has been steadily declining since peaking in April at \$183/cwt and averaged \$143/cwt in November, down \$36/cwt or 20 per cent from the same period in 2008. The AA cutout averaged \$144/cwt in November, down \$32 or 18 per cent from 2008.



There is a strong correlation between carcass weights and the proportion of carcasses that grade AAA or higher. Large carcass weights have kept AAA as a % of all A grades high and with domestic fed slaughter steady, supplies of AAA beef have increased significantly. At the same time demand for AA continues to be comparatively stronger, as consumers look for cheaper protein options. The AAA/AA spread has averaged \$2.66/cwt in 2009 compared to \$3.17/cwt in 2008 and \$9.93/cwt in 2007. The trend towards a narrower spread is a combination of larger AAA supplies pressuring the AAA price



down and good consumer demand for AA product of which there are smaller supplies. This has resulted in AA prices falling to a lesser extent when compared to AAA.

Cutout values have been weak in 2009 due to struggling middle meats, which represent 50 per cent of the total value of the carcass. Middle meats have been pressured by the recession and reduced foodservice demand as consumers eat more at home and look to cut costs. In 2009, rib and loin primal prices were up 5 per cent and down 1 per cent below 2008 levels at \$2.54/lb and \$2.86/lb. Demand for chucks and rounds, which was particularly strong the fall of 2008, has also lost its shine. Chuck and round primal prices in 2009 were both up 5 per cent from 2008 at \$1.14/lb and \$1.34/lb respectively. Despite strong prices in the spring 2009, chucks and rounds only contribute 38 per cent to the cutout value, making it difficult to increase the overall cutout value with these items alone. In addition, consumers have also had their choice of a large supply of competing proteins at relatively cheap prices throughout the year, providing strong competition for beef at the retail counter where there has been renewed interest by consumers. Declines in cutout values have limited packer returns and ultimately prices that can be paid for fed and feeder cattle.

## Competing Meats

---

The Canadian hog industry has significantly reduced the sow herd due to poor profitability in the sector. This has been further exacerbated by severe reductions in live animal exports to the U.S. due to COOL and the impacts of H1N1 related trade restrictions. Large inventory reductions will reduce domestic pork supplies moving into 2010, after being higher in 2009 when export markets were closed due to H1N1 and larger numbers of animals were produced in Canada due to reduced weaning pig exports to the U.S. In 2009, live hog exports were down 49 per cent, while feeder pig exports down 26 per cent. This has increased domestic slaughter and production 1.4 per cent, with most of the increases offset by a smaller domestic herd. Pork exports are down 4 per cent in 2009, with market access continuing to limit volumes. Overall domestic pork supplies are estimated to be 4 per cent higher in 2009.

Due to the export dependency of the Canadian hog sector and heavy reliance on the U.S., the Canadian hog industry continues to be influenced by the U.S. market; albeit with a thicker border since COOL. The U.S. market has also been faced with profitability issues associated with high feed and input costs, trade restrictions associated with H1N1, and large supplies. However inventory reductions in the U.S. have been more modest than what has been seen in Canada, meaning continued reductions are going to be necessary in order to see any significant supply response that provides support to North American prices. Large North American pork supplies were evident in 2009 and unless exports pick up and more substantial reductions are seen in U.S. hog inventories, large pork supplies will continue to be a problem for the beef industry.

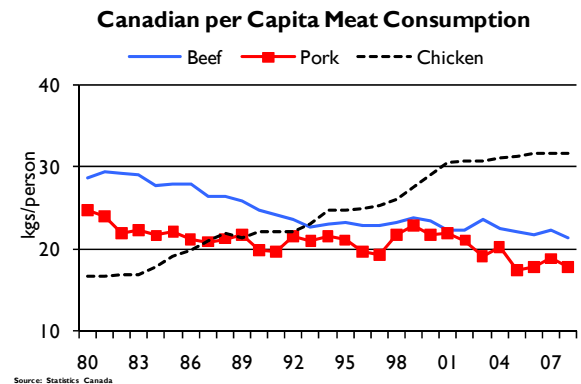
Any rally in the pork market in 2010 will be highly dependent on growth in exports. If the U.S. cannot get pork exports to move in the first half of the year large volumes will continue to weigh on the entire North American meat complex. In addition, forecasts of positive margins

by the third quarter may result in producers not liquidating the numbers needed to reach that forecast and further delay industry recovery.

Canadian poultry production was down 1 per cent in 2009, with imports up 1 per cent and exports down 8 per cent pushing domestic disappearance up 0.5 per cent. Retail poultry prices have averaged 5.6 per cent higher in 2009 pointing towards stronger demand. Reductions in U.S. poultry production were also seen, which supported U.S. retail prices. As prices have recovered production is expected to stabilize after seeing reduced egg sets throughout most of 2009. The U.S. experienced its first decline in poultry production in 30 years (-4%) after losses in 2008 occurred due to high feed costs and a market share battle. Although recovery is forecast for 2010 the year will start off with negative margins for processors who will need to be very careful as over production is a distinct possibility again.

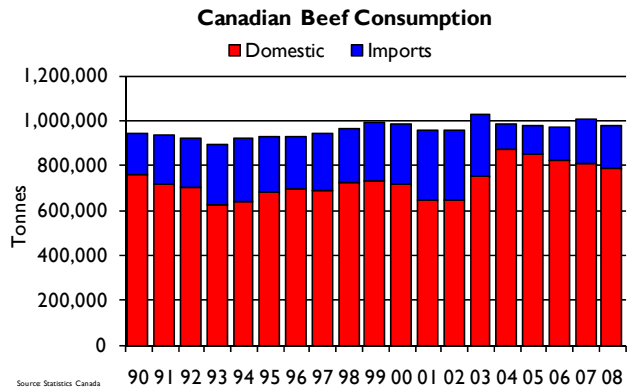
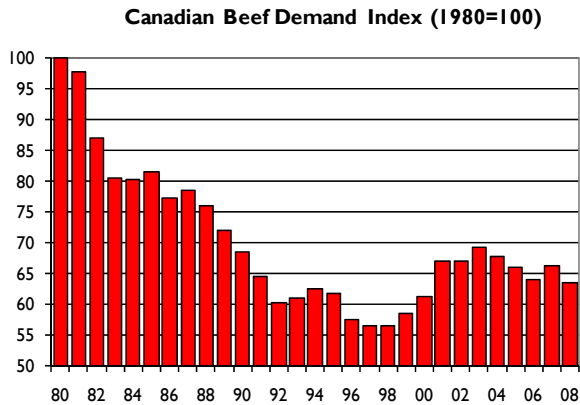
## Consumption

Canadian beef consumption in 2008 was down 4.5 per cent or 1 kg to 21.4 kilograms per person. This is similar to 2004 and 2005 levels. U.S. per capita consumption similarly fell 4 per cent to 28.5 kilograms. The first part of 2008 saw large supplies of pork providing stiff competition for beef at the meat counter. This was followed by a short grilling season, which was delayed due to cool weather until late June, early July. Further pressure was added, with large meat recalls in August due to *Listeria*. Then in the fourth quarter financial and economic concerns resulted in consumers tightening their purse strings domestically and globally, placing downward pressure on protein values. Consumer concerns about the economy had them trading down within proteins (steak to hamburger) and between proteins (beef and pork to poultry). Pork consumption declined 5 per cent or 1 kg to 17.9 kilograms per person and poultry increased 1.1 per cent or 0.4 kilograms to 38.1 kilograms per person in 2008. Total protein consumption declined 2.1 per cent to 78.4 kilograms from 80.1 kilograms in 2007, which is just above the historic average of 77.2 kilograms.



Total beef consumption in Canada in 2008 reached 977,266 tonnes (carcass weight) down 3 per cent from the previous year. Disappearance of Canadian beef accounted for 785,065 tonnes or 80 per cent while imports accounted for 20 per cent of Canadian consumption.

Lower consumption and lower deflated retail prices (which fell 1 per cent from \$9.04/kg in 2007 to \$8.96/kg in 2008) meant beef demand fell 4.1 per cent in Canada. The situation was similar south of the border with demand falling 3.7 per cent in the U.S. Demand is an indicator of consumer's willingness to pay. In 2008 consumers decreased demand for beef and pork, while poultry demand was strong with larger consumption at higher prices.



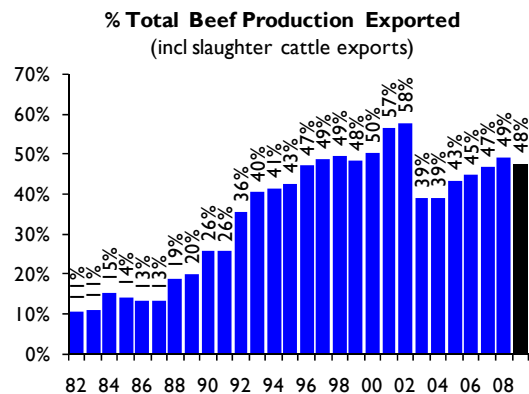
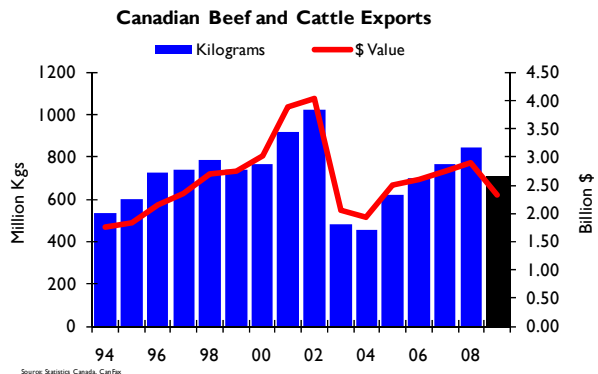
In 2009 H1N1 reduced markets available for pork exports. In addition COOL reduced live hog exports to the US resulting in large supplies available on the domestic market at relatively low prices. Strong consumer demand has supported poultry prices at retail which ending the year 5.6 per cent higher than 2008 levels. Beef disappearance data is incomplete at time of writing but deflated retail beef prices in 2009 were up 5% at \$9.44/kg. In 2010, protein consumption is expected to see small growth with slow economic recovery.

## Cattle and Beef Trade

### Canadian Beef and Cattle Exports

Canadian exports of beef and live cattle were down 16 per cent in volume to 710,000 tonnes and 20 per cent in value to \$2.32 billion in 2009. This is a substantial decline from 2008 exports of 846,500 tonnes valued at \$2.91 billion. Exports of Canadian beef are down 5 per cent in volume and value in 2009 with the majority of decline in total exports a result of reduced live cattle exports to the U.S., with slaughter cattle exports down 15 per cent and feeder exports down 55 per cent. The impact of the gradual appreciation of the Canadian dollar throughout 2009 has also impacted trade values, with prices for Canadian beef and cattle pressured downwards to remain competitive in light of the stronger dollar.

In 2009 exports accounted for 48 per cent of total beef production when slaughter cattle exports are included. This is a one per cent

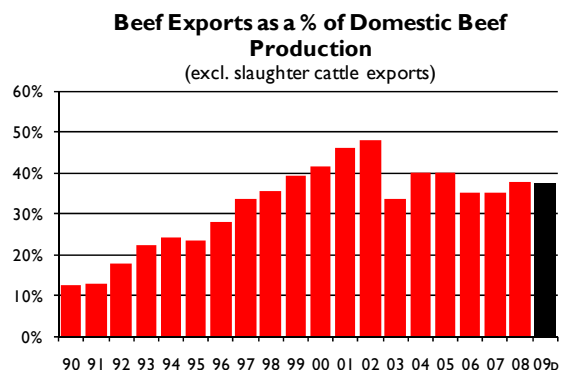


decrease from 2008 when 49 per cent of total beef production was exported.

### Total Volume and Value of Beef Exports

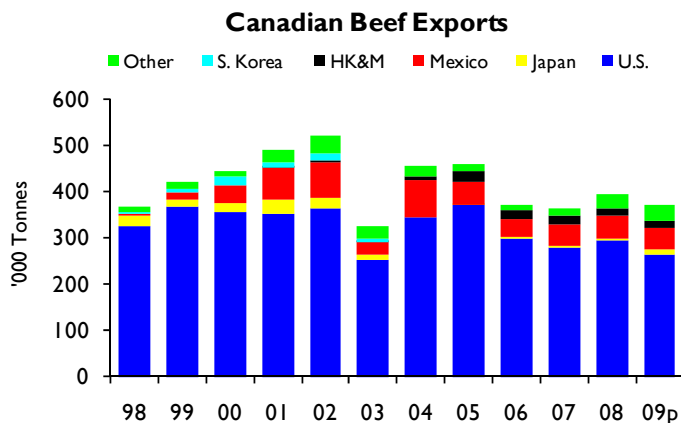
Beef exports in 2009 are projected to total 373,000 tonnes (product weight) valued at \$1.28 billion. The economic crisis has hit many countries, with one result being softening global beef demand in late 2008 and throughout 2009. Some importers saw credit limitations become an issue and others dramatically reduced import volumes due to reduced demand as many consumers changed consumption patterns with the recession. While slow recovery was seen during the latter part of 2009, trade volumes and values for many countries are still off from 2008 levels. A strong dollar during the second half of 2009 also severely affected the competitiveness of Canadian beef and resulted in depressed values, after being below year ago levels for the first 9 months of the year.

Beef exports as a percentage of domestic beef production (excluding slaughter cattle) is steady at 38 per cent, with production down 3 per cent. While beef exports are expected to rebound in 2010, they are expected to continue to remain well below the historical average of 42 per cent.



Beef exports to the **United States** from January to October are down 6 per cent in volume and 4.5 per cent in value in 2009, projected to total 277,000 tonnes valued at \$955 million. Like Canada, the U.S. has seen smaller exports and increased domestic supplies in the midst of reduced beef demand, which has reduced their demand for imports. The share of Canadian beef exports that is shipped to the U.S. has continued to decrease from a high of 80 per cent in 2006 to 74 per cent in 2009. This is a reflection of both reduced exports to the U.S., as well as increased market access and resumption of exports to other countries.

Exports to **Mexico** from January to October are down 6 per cent in volume and 7 per cent in value in 2009, projected to total 44,000 tonnes valued at \$166 million. Both domestic consumers and Mexico's tourist



industry were hit hard by both the recession and with further reductions in tourism evident as a result of H1N1 concerns. In addition changes in major purchasing contracts between Canadian suppliers and major Mexican end-users also caused significant disruption in Canadian beef export volumes. While Canadian beef exports to Mexico have rebounded in late 2009, this has not offset the large drops seen in the first part of 2009.

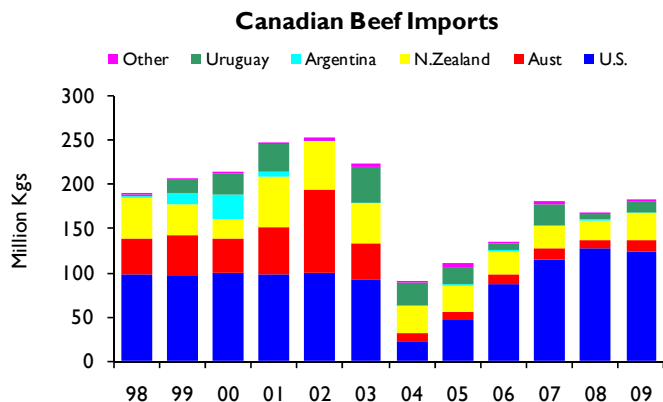
**Hong Kong and Macau** represents 4.5 per cent of total Canadian beef exports. Exports to Hong Kong and Macau are down 10 per cent in volume and 17 per cent in value, to total 16,000 tonnes valued at \$60 million in 2009. Exports to **Russia** have doubled in volume and are up 39 per cent in value in 2009, representing 3.4 per cent of total beef exports, totaling 12,000 tonnes valued at \$13 million.

Exports to **Japan** are up 50 per cent in volume and 52 per cent in value, with Japan's share of total exports increasing to 2 per cent of total export volumes. Exports to Japan are expected to reach 8,000 tonnes in 2009 valued at \$47.5 million. Exports to Japan continue to remain below pre-BSE average volumes of 22,000 tonnes, but continued growth and recovery has been apparent over the last several years despite current age and product restrictions. Exports to **Taiwan** are up 82 per cent in volume and 36.5 per cent in value, totaling 5,200 tonnes valued at \$18 million in 2009 and representing 1.5 per cent of Canadian beef exports. It is important to note that similar to Japan, exports to Taiwan have seen large increases - with exports the third highest on record after 2001 and 2002 despite continued age and product restrictions.

### **Beef Imports**

Beef imports into the Canadian market are up 9 per cent in 2009 to total 183,000 tonnes. Increased imports are a result of a 43 per cent increase in non-NAFTA imports. Strong consumer demand for trim product in North America during the recession and reduced Canadian cow slaughter saw elevated trim prices in the North American market. This, in combination with a strong Canadian dollar, made North America a very attractive market for Non-NAFTA countries.

Especially in light of the fact that demand for exports from these countries in many other major markets experienced declines with the softening global economy. Imports from Uruguay were up 146 per cent, from New Zealand up 37 per cent and from Australia up 28 per cent. In contrast imports from the U.S. were down 2 per cent, with reduced demand in Eastern Canada and a lower dollar in the first part of 2009. After reaching a record high in 2008 when imports from the U.S. totalled 128,000 tonnes, U.S. imports of 125,000 tonnes in 2009 still remain well above historical levels.



## Trade Market Access Situation and Outlook

---

Canada continues to recover market access for beef and live cattle exports, but the reopening of markets has been slow and in many cases only partial access in many important markets has been achieved. Age restrictions, product restrictions, and limitations on live cattle exports for breeding continue to place a significant limit on the ability of Canadian beef and genetic exporters to achieve meaningful gains. However steps taken toward greater normalization of trade are critical to the long-term sustainability and success of the Canadian beef industry.

Hong Kong announced a phased in program to market access in early 2009, which has resulted in full access for Canadian beef as of December 2009. Notable access was established for Canadian pork into mainland China in December 2009 after being closed since April 2009 due to H1N1, which should help improve the domestic market situation for all proteins. At the same time mainland China continues to remain closed for all Canadian beef. Taiwan continues to stay closed to bone-in access for North America and negotiations with the U.S. do not look promising for 2010 with consumers providing resistance to government.

Colombia restored full access for Canadian beef from cattle of all ages on September 18, 2009. This followed the May 2009 decision to partially re-open the border to Canadian beef. The Colombian market is estimated to be worth approximately \$6 million for Canadian beef products, plus \$1 million for Canadian livestock and genetics exports.

Russia announced on October 13, 2009 plans to expand access for Canadian beef to include all beef from cattle under-thirty-months (UTM) and boneless beef from cattle over-thirty-months (OTM) of age. Russia also agreed to continue a process aimed at achieving access for beef offal products by the end of 2009. In 2006 Russia restored access for Canadian boneless UTM beef, but a series of technical hurdles and difficulty obtaining export facility approvals kept exports to a minimum. Significant export volumes have only been seen since the end of 2007 and have been steadily increasing. The Canada Beef Export Federation estimates that Canada could export \$32 million per year of beef to Russia and a further \$10 million for beef offals. This is a significant jump from the 9,500 tonnes valued at \$8.7 million that Canada exported to Russia in 2002. Expectations for sales to Russia compared to historic levels demonstrate how this market has evolved over the past seven years.

The Canadian government has launched trade challenges through the World Trade Organization with both South Korea, for continuing to remain closed to all Canadian beef products, and the U.S. for the implementation of mandatory Country of Origin Labelling measures that contravene established definitions of country of origin labelling for products that are produced, slaughtered or processed in the U.S. While industry is pleased that these challenges are proceeding, trade challenges are long and time consuming processes that typically take several years prior to any changes being seen if rulings are favourable to Canada.

## Canadian 2010 Cattle and Beef Supply Outlook

---

The Canadian beef industry has faced a number of challenges over the last seven years. In addition to significant market turmoil and financial losses in the wake of border closures after BSE, continued market access limitations, a volatile currency and input costs, labour shortages, drought, and regulatory burden have all had a substantial impact on industry competitiveness and profitability. The last few years have seen substantial changes in regulations affecting the beef industry including the implementation of the enhanced feed ban in Canada that has placed Canadian packers at a competitive disadvantage to U.S. packers and resulted in substantial costs being incurred by all sectors. The Canadian industry has also now had to grapple with the implementation of mandatory Country of Origin Labelling in the U.S., which has not only resulted in decreased demand for Canadian fed and feeder cattle, but also resulted in increased transportation costs, reduced access to premium programs, and increased transaction costs associated with managing scheduling and labelling logistics. In 2009 profitability has been further challenged by both the global recession and trade restrictions associated with H1N1, which have negatively impacted beef demand and limited upside price movement for beef and cattle despite reductions in beef supplies. Furthermore the industry has been once again challenged by an appreciating dollar, which has negatively impacted beef and cattle prices.

In light of reduced demand for beef due to trade restrictions and more recently depressed global beef demand due to recession, reductions in beef supplies are a necessity to provide both price support and to see any potential price improvement. At the same time the Canadian beef industry has been challenged by large protein supplies. Beef production and supplies have been large over the last several years (05-08), as the industry has grappled with larger inventories for a period and then large cow slaughter over the last several years as producers began to downsize. The first actual reduction in beef production was not seen until 2009 and its impact was diminished due to large carcass weights and large competing protein supplies, namely pork. Pork supplies have increased as a result of both productivity gains and more product moving into the domestic and North American market, with both COOL and H1N1 related trade restrictions reducing live hog and pork exports.

In essence, declines in beef production have struggled to offset declines in beef demand and the result has been prices for beef and cattle trending steady to lower instead of seeing price increases, which is typically the response seen when supplies are reduced. The latter part of 2009 saw reductions in trade restrictions associated with H1N1, which should encourage greater pork exports and alleviate some of the pressure on the North American protein market. At the same time further reductions in both Canadian and U.S. hog inventories are expected and a necessity in order to see any substantial declines in pork supplies over the next several years that will provide meaningful price support to both the hog sector and also competing proteins such as beef.

Further reductions in Canadian cattle inventories are also a necessity to seeing price support for the Canadian beef industry. Cattle inventories were down 165,000 head or 1.3% on January 1, 2010 with further declines expected for 2011, depending on feeder cattle prices and Canadian

feed supplies and prices. While total cow marketings were down in 2009 the industry is still in liquidation mode, with beef cow culling rates at 12 per cent, which remains well above the long term average of 10 per cent and indicates the herd is still contracting. Heifer retention also continues to be low, with heifer marketings down only 6 per cent. The continued reduction can be attributed to calf prices remaining low and severe drought in many regions that limited feed availability and saw feed prices increase substantially.

Improved calf prices will translate into cow/calf producer's seeing positive returns and the Canadian beef cow herd stabilizing in size (as long as costs remain steady). As this occurs, not only will smaller fed cattle supplies become evident due to smaller calf crops, but cow and heifer slaughter will also decline revealing sharper declines in beef production due to both reductions in fed and non-fed beef supplies. Cow slaughter is expected to decline in 2010, as supplies continue to tighten, while cow exports are expected to stay steady as U.S. packers continue to have an advantage with a shorter SRM list. This will mean most of the decline in cow marketings and non-fed beef production in 2010 will come out of domestic slaughter.

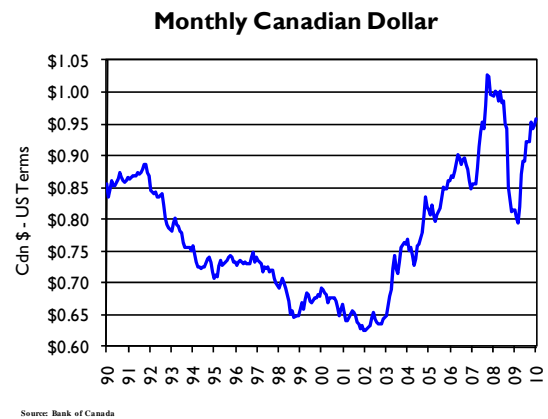
While beef production is expected to continue to decline, the question remains how quickly will beef demand recover and what will global economic recovery bring along with it from a cost standpoint? The latter part of 2009 saw green shoots of economic recovery. This is a positive indicator of resumed consumer expenditures and increased demand for beef from both North American and global consumers moving forward, as unemployment levels subside, foodservice demand increases, and tourism sectors recover in many major markets - all essential components for improving Canadian cutout and cattle values. At the same time consumer losses have been substantial and the speed of economic recovery is still highly uncertain.

There are two theories for economic recovery. The first is that we will see a long but steady climb back, with GDP growth small but positive at 2-3 per cent in 2010. This would provide support to stabilize consumer demand, but it would remain weak in 2010 prior to seeing more meaningful recovery. The second theory considers the fact that most recoveries after a recession are strong at 4-6 per cent GDP growth. Some argue that the current small, positive signs point toward the fact that this is not a true recovery and a second dip could occur sometime in 2010. Consequences of a second dip would include continued weak consumer demand for beef over the short term, but potentially a stronger recovery over the longer term. Either way it is clear that quick recovery of beef demand is unlikely, with the next couple of years more likely involving slow and continuous recovery of global beef demand along with continued reductions in global beef supplies.

Economic recovery is necessary for the industry to see improvements in beef demand, but with the Canadian economy's heavy reliance on oil and other commodities it also means higher energy prices and an appreciation of the Canadian dollar. The Canadian dollar has slowly been appreciating throughout 2009, after falling to 80 cents in the fourth quarter of 2008. This appreciation was expected. With renewed global demand for oil and energy and reduced supplies, given slowdowns in production start-ups and production cutbacks, energy prices have begun to increase and pulled the Canadian dollar up along with them. Furthermore the weak

U.S. dollar, resulting from substantial government stimulus spending, an outflow of investments to other global markets as economies stabilize, the U.S.'s burgeoning deficit, and expectations of increased taxes has resulted in many other currencies appreciating in value relative to the U.S. dollar.

A strong Canadian dollar is expected to prevail throughout 2010 and moving into 2011 given continued growth in global demand for oil is expected and the U.S. economic situation is not expected to turnaround quickly. If a second recessionary dip occurs, as outlined above, decreased oil prices could push the Canadian dollar down temporarily (potentially to around \$0.85) as security is sought in the U.S. market. But realistically this would only bring short-term relief to the beef industry and other Canadian export industries that are subjected to depressed prices as a result of a strong dollar.



The extent and speed with which the Canadian dollar appreciates will be highly dependent on global oil demand and supplies, as well as U.S. economic recovery and monetary policy. It is clear that as the economy adjusts to changes in monetary policy and new supply/demand dynamics, the dollar could see some short term volatility that affects industry prices and profitability. However, it is widely held that the global economy cannot support oil prices above \$80/barrel, which has placed a cursory ceiling on prices. This is important as it should provide some stability to the Canadian dollar. While the dollar will remain high, reduced volatility should assist industries in managing margins due to reduced risk of fluctuations in both input costs and prices received.

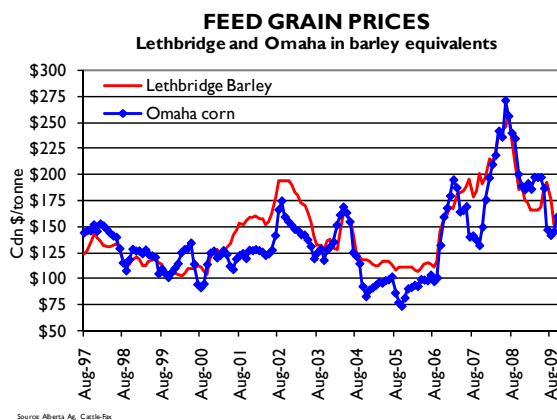
Increasing oil prices with economic recovery also will have an impact on the feed cost side of the equation, which needs to be watched closely. As global demand for oil declined due to recessionary pressures, the demand for corn for ethanol production also declined due to reduced profitability in this sector and reduced production that essentially levelled off to maintain production at levels that just fulfilled inclusion mandates. Reduced demand for corn for ethanol production in the U.S., in combination with ample supplies, softened prices across all feed grain markets globally. While feed grain prices remained above historical levels, significant relief was felt by many sectors that struggled to adjust to record high feed grain prices.

As oil prices continue to climb, it is expected that there will be increased incentive for ethanol producers to expand production as more operations become viable, beyond meeting minimum mandate requirements, and excess capacity comes into use. This of course will increase demand for corn and likely see an elevation of global feed grain prices - the question is to what extent and how quickly this occurs. Similar to predictions with oil prices, any increases in ethanol demand and feed grain prices are expected to be more gradual and modest than what

has previously been seen. While elevated feed grain prices are not positive for the beef industry, a more modest and less volatile appreciation allows for increased opportunities to manage risk and margins within livestock sectors. The biggest risk factors that could result in accelerated increases in feed grain prices are supply conditions and changes in government mandates. With the U.S. government deferring any decision on increasing ethanol mandates until mid-2010, feed grain supplies are the biggest variable in the near-term to monitor. With 2009/10 seeing the largest U.S. corn crop in U.S. history ample supplies are currently in the cards. While the competition for acres this spring will be intense, dramatic shifts that reduce corn production substantially are not expected.

Despite large reductions in Canadian barley production in 2009, decreased exports and large domestic feed grain supplies (due to delayed harvest and reduced wheat and barley crop quality) has kept barley prices stable. This trend is expected to continue, as long as corn prices do not adjust higher and pull barley with them. Delays in finishing the U.S. corn harvest have put barley at a cost of gain advantage. This is expected to change if the entire U.S. corn crop is put in the bin.

Relative cost of gain between Canada and the U.S. will be an important factor moving forward in determining if feeder cattle exports continue to trend lower, as occurred in 2009, or increase due to a cost of gain advantage in the U.S. With smaller calf crops expected over the next several years that reduce feeder cattle supplies North American wide, increased competition is likely to result from both Canadian and U.S. feeders given there are already indications of excess capacity.



While there is some expectation that some capacity will be removed from the equation due to poor profitability, whether this occurs north or south of the border remains to be seen. Current expectations for 2010 are that feeder cattle exports from Canada will continue to trend lower, with Canada being able to maintain a relatively favourable cost of gain advantage and COOL also reducing U.S. feedlot demand due to increased complexities of marketing Canadian born fat cattle. If reductions in feeder cattle exports continue this will somewhat offset reduced Canadian fed cattle supplies expected as a result of smaller overall inventories. At the same time tighter North American fed cattle supplies will be increasingly evident moving in 2010 and 2011.

Whether Canadian fat cattle become part of the domestic beef supply equation or are exported for slaughter will be largely dependent upon how domestic packers respond to smaller non-fed supplies, how determined they are to maintain Canadian operations at current utilization levels, and how willing U.S. packers are to increase procurement of Canadian cattle in light of tighter fed cattle supplies. With COOL currently reducing U.S. packer demand and domestic packer demand expected to remain relatively strong, fed cattle exports are expected to continue to

trend lower with proportionately more fed cattle kept in Canada for slaughter. This is expected to keep 2010 fed cattle slaughter steady with 2009 levels.

It is important to note that U.S. demand for feeder and fed cattle is anticipated to be more fickle and less predictable under the new COOL regime. When North American fed cattle supplies are tight, as seen in the fourth quarter of 2009, U.S. packers appear to be more willing to purchase and slaughter Canadian cattle – reducing the price discounts applied to them. In contrast, in periods of ample supplies, U.S. packers have been and are expected moving forward to be less willing to accept Canadian cattle and consequently apply larger discounts to these animals. This will create additional volatility in the basis and Canadian cattle prices.

U.S. fed cattle supplies are expected to be large in the first quarter of 2010 before tightening throughout the rest of the year, with a smaller calf crop and significantly smaller feeder imports from Canada in 2009. As such export volumes are expected to be lower in the first half of the year before increasing in the second half when supplies tighten. Overall exports are expected to be steady with 2009. Heavy placement weights in the second half of 2009 in the U.S. are expected to keep carcass weights large in 2010, supporting production levels.

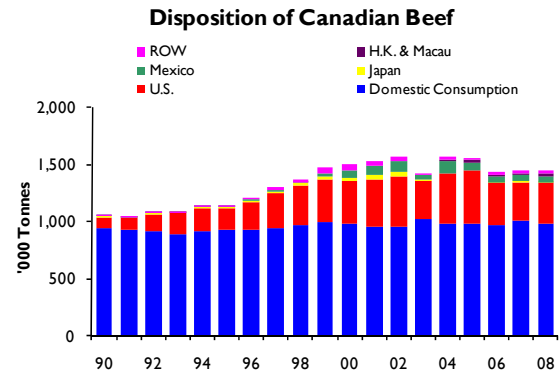
### **Canadian Beef Disposition and Trade**

Statistics out of the U.S. indicate an increased trend of consumers from 18-34 years eating more meals at home, resulting in a 13 per cent decline in foodservice consumption over the last four years. Casual dining restaurants have lost 20-25 per cent of their customers over the last four years, with fast food restaurants not far behind. The concern over decreased foodservice spending and increases at retail is that less than half the dollars that would be spent at foodservice are spent at retail. This has put pressure on cutout values, as retail is moving product mostly with features and lower valued cuts as opposed to high-end middle meats that drive overall cutout values. For every 4 percentage points of restaurant pain, there is a 1 per cent increase in retail sales. In addition the growth at retail has been disappointing for the beef industry, as most of the increase in sales is in pantry staples like pasta, sauces, soups and cereals. These trends can also be found in Canada.

Improvements in North American consumer demand for beef is expected to be limited moving into 2010, especially with U.S. unemployment over 10 per cent and Canadian unemployment at 8.5 per cent. Unemployment numbers are expected to stay at these levels throughout the first half of the year. It won't be until 3-6 months after consumers are back in stable jobs, have paid off some debt and increased savings before they will be looking to increase spending again. This puts us well into 2011 before seeing any significant upswing in North American beef demand.

The disposition of Canadian beef moving into 2010 will be highly dependent upon market access and where the highest values can be attained for specific cuts and productions. Despite expectations of reduced beef supplies, if improvements in global beef demand are achieved at a more accelerated rate than in North America and gains in market access can be achieved that provide access to higher value markets for specific products, beef exports will continue to

increase in both volume and value. The strong Canadian dollar will place some pressure on this growth, but as demand recovers and market access is achieved in important markets for specific products potential improvements are feasible. Opportunities will come from countries with a stable consumer base that has relatively small debt loads and has not been as severely impacted by unemployment and declining incomes over the last year. Whereas slower growth will occur in major Canadian export markets like the U.S., which will continue to see softer beef demand in light of consumers being hard hit and relatively large supplies of cheap competing proteins.



The recovery of Canada’s beef export volumes has been slower than anticipated due to a number of challenges in establishing full market access in many markets and gaining any access in markets that are fully closed. Significant gains were made in 2009 with further gains expected for 2010. However, legal and political circumstances make it difficult to predict when increased access will be achieved. Full market access is necessary in order to increase carcass values and improve returns to the Canadian beef industry.

*The predictions outlined in this outlook are a result of utilizing the best information available regarding numerous market facts that impact both the supply and demand situations for Canadian beef. A change in the global economy, Canadian dollar, feed grain situation, prices and relative cost of gain, packer or feedlot capacity, regulations, or margins could have a significant impact on the market in the coming year and needs to be monitored moving forward.*