



Gaining Production Efficiencies Value-Added Beef Production

For
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Major Grain and Beef
Industry trends over the
next 5 – 7 years





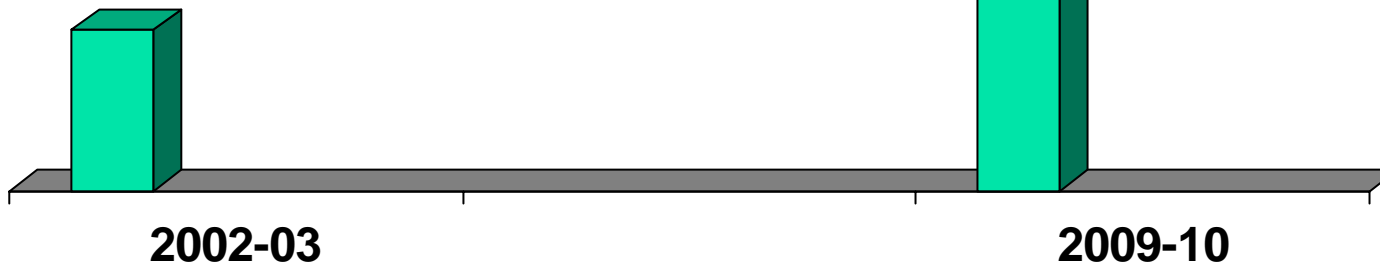
Corn Demand and Prices

- With normal crop growing conditions, average annual cash prices ranging between **\$3.00 and \$4.00** per bushel, compared to the **\$2.00** per bushel over the past ten years at the farm level.
- The substantial price increase for corn is **Demand Driven**. The hub of agriculture is **corn**.
- The train has “left the station” regarding ethanol production.
- Distillers grains will become much more plentiful and will very likely decline farther in price.
- Corn used for Ethanol production will increase substantially over the next several years (see bar chart on next slide).

Ethanol Use of Corn (Billions of Bushels)

**Represents 4.5
billion bushels or
35% of the total
annual corn crop**

**Represents 1 billion
bushels or 11% of
the total annual corn
crop**





Beef Cattle Inventory Numbers and Beef Supplies

- The Cattle cycle has changed. The trend is for flat to declining beef cattle inventory numbers.
- Primary reasons are (1) dry weather, (2) sharply higher corn prices, (3) average age of cow-calf operators and (4) the significantly higher costs of producing a calf.
- The demand for pasture and grass by ranchers and stocker cattle operators will increase significantly as a result of putting on more weight **before** steers and heifers are placed on feed. This is because of significantly higher corn prices.
- Total annual beef supplies will be relatively flat and tight.



Excess Feedlot and Beef Packing Plant Capacity

- Capacity utilization at the **feedlot** level will be in the **65 to 75%** range at best.
- Capacity utilization at the beef packing level will be in the **70 to 80%** range at best.
- Competition for fed cattle supplies among beef packers will increase significantly. Beef packers will have to pay more to get the fed cattle they need.
- Beef packers will have increased incentives to (1) “line up” fed cattle supplies and (2) find ways to add value to the fed beef they sell to retail food stores, the HR&I trade and to their beef export customers.



The Excess Feedlot and Beef Packing Capacity will Result in Accelerated Consolidation

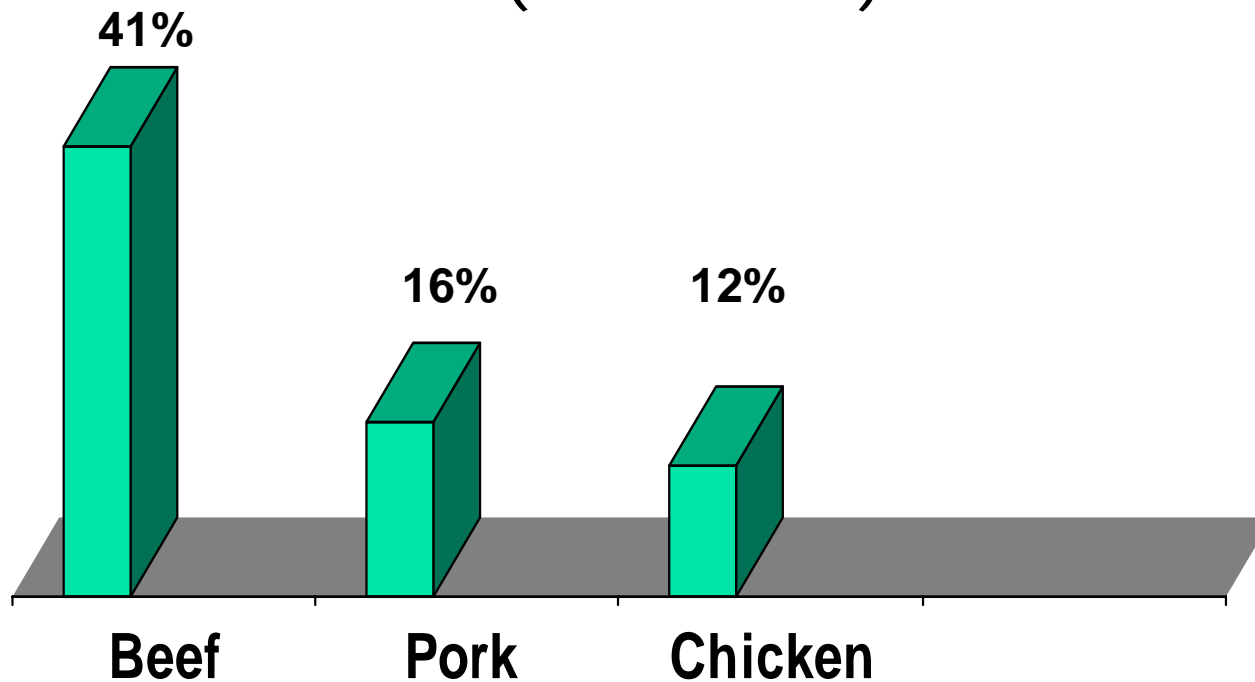
- Over the next **10** years, **1%** of U.S. feedlots will account for at least **75% to 80%** of all fed cattle marketed.
- Depending on their location, many of the **5,000 to 25,000** head feedyards will not be able to compete. **Many of these feedlots will become “dinosaurs”**.
- Most smaller farmer feeders in the corn belt will be able to compete.
- Over the next **10** years, the five largest U.S. beef packers will account for at least **90%** of all fed steer and heifer slaughter.
- Supply, pricing grid, value-added and branded beef agreements, “partnerships” and “vertical alliances” will accelerate between relatively large cattle feeding and beef packing companies.



U. S. Consumer and Export
Demand for Beef will remain
Strong and Increase Further

Over the past **8** years, U.S. consumer dollar expenditures for beef, pork and chicken have increased

Eight Year Percentage Increase
(1999-2006)

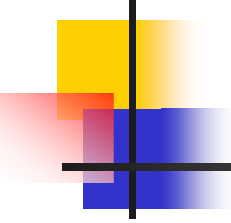


Why Consumer Demand and Expenditures have increased as much as they have over the past eight years

- The demand curve has shifted to the right.
- Consumer demand for beef has become significantly more inelastic.



Why has consumer demand for beef increased over the past 8 years?



- Growing economy and increasing consumer incomes.
- Improved beef product quality and consistency.
- People are living longer.
- Increased Hispanic (Mexican) population. They like beef.
- The beef check off program.
- Increasing beef export sales.

Why there is substantial excess feedyard and beef packing plant capacity



- The Beef Cattle Inventory is not increasing. Beef cattle numbers may decline. Feedyards will be feeding more yearling cattle and fewer calves.
- Since 1990, total U.S. feed pen space capacity has increased by at least **25%**.
- Since 1990, total U.S. Beef packing plant capacity has increased by at least **20%**.

Why there is substantial excess feedyard and beef packing plant capacity



- Many cattle feeding customers have stopped feeding cattle. Therefore, the feedyard owner(s) have to feed substantially more cattle. This will be even more true in the years ahead.
- This trend increases the market risks associated with cattle on feed ownership. It also substantially increases the amount of working capital and bank financing required by the feedyard owner(s).

Guiding Principles for successful large scale cattle feeding operations moving forward



- Owning and operating feedyards that have **35,000 to 100,000** head capacities in the right locations.
- Being a true low cost producer and taking advantages of major economies of scale for the feedyards operating as “hotels”.
- The feedyards operating at **85% to 95%** of capacity where **80% to 100%** of the cattle are owned by those who own and operate these feedyards.
- These feedyards using and taking advantage of wet or dry distillers grain and feeding primarily yearling cattle.



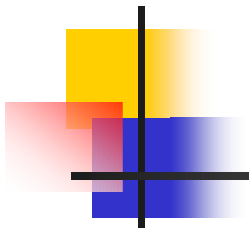
Guiding Principles Continued

- These feedyards buying and contracting more yearling feeder cattle from smaller “back grounding” and “grow” feedyards.
- These feedyards entering into various fed cattle supply, marketing and pricing grid agreements with one or more of the major beef packing companies.
- These feedyards will require more good data and information on their cattle relative to (1) source verification, (2) genetic makeup, (3) animal health history, (4) cattle feeding performance and (5) carcass quality characteristics.
- These feedyards and their beef packer “partners” being committed to achieving improved production efficiency and increased value-added beef production.



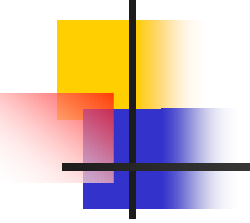
Guiding Principles Continued

- These feedyards doing more “partnering” with selected cow-calf and stocker cattle producers to jointly add-value and consistently produce what their customer (the beef packer) wants each week.
- These feedyards being committed to various branded beef “partnerships” or “alliances” that are win-win arrangements for all parties that result in increased value-added beef production and improved production efficiencies.
- These feedyards being committed to moving away from a commodity orientation system to a value-added and branded beef system.



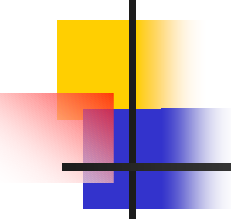
Commodity value vs. Added-value for beef producers, cattle feeders and beef packers

- **Beef Commodity Values** – Very little , if any, price differentiation for fed cattle. The same price is paid essentially for all fed cattle sold in a given week.
- **Beef Added Values** – Customers paying **more money** for fed beef that is perceived by customers as being of higher quality relative to such things as (1) tenderness, (2) taste and eating satisfaction, (3) consistency, (4) the use or non-use of growth hormones, (5) the use or non-use of antibiotics, (6) U. S. vs. foreign origin, (7) grain fed vs. grass fed beef, (8) carcass fat content, (9) breed and genetic makeup, etc.



Commodity beef vs. Value – added beef production and merchandising

- **Commodity Beef Production** – This is the traditional and historical **supply push approach** where **price** is a major factor impacting consumer buying decisions.
- **Value-Added and Branded Beef Merchandising**– This is where price is somewhat less important to consumers. This is the **demand pull and brand loyalty approach where customers and consumers perceive they are buying safe, dependable and consistently high quality beef products at a higher price.**



Key Information needed by cattle producers, cattle feeders, beef packers and their customers relative to Value-added and Branded beef production and merchandising

1. Tenderness and taste.
2. USDA quality and yield grades.
3. Consistency of quality and supply.
4. Age of beef and feed ration.
5. Genetic makeup.
6. Eye appeal and color.
7. Weight and portion size.
8. Fresh vs. Frozen.
9. Fat content.
10. Use or non-use of growth hormones.



Key information continued

11. Use or non-use of antibiotics.
12. Grain fed vs. Grass fed.
13. Food safety.
14. U.S. vs. Foreign origin.
15. Preparation time and convenience.
16. Package design and specifications.
17. Nutrition information.
18. New product development.
19. Cooked vs. non-cooked.
20. Price.

Conclusions



1. In order to better increase beef cattle production efficiencies and to increase value-added and branded beef production and merchandising opportunities, larger scale feedlot owners and operators must have more beef cattle ID data for each animal from the time they purchase the feeder cattle through at least the beef packing and carcass quality level.

Conclusions



2. By having this data, many of the increased production efficiencies and the value-added beef production opportunities are realistically achievable for beef cattle producers, for cattle feeders and for beef packers who take the value-added approach as opposed to the commodity approach.

Conclusions



3. Bottom line, the commodity approach does not require a lot of cattle ID data. The value-added and branded beef approach, however does require much more cattle ID data. For those beef producers, cattle feeders and beef packers who take the cattle ID road can expect to be well rewarded financially for doing so. **Value-added beef production is where the beef industry is going. This is where the real future is for the beef industry moving forward.**