

The Worst is Behind Us, but Caution Ahead

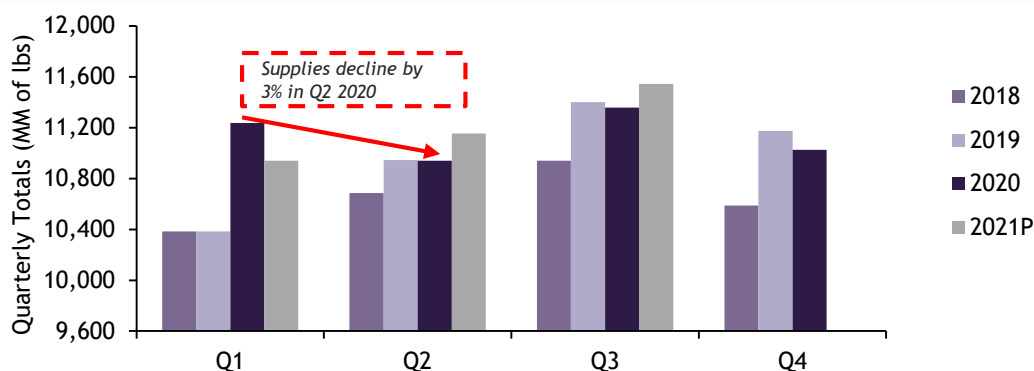
Price divergence occurred at the peak of COVID-19 as processing capabilities were taken offline, which in turn caused a bottleneck that resulted in temporary supply shortages in various retail channels. These challenges were exacerbated by record demand surges due to stockpiling; intense cost pressure due to COVID-related protocols and labor challenges; and severe disruptions in many export markets, which traditionally serve to balance an approximate 18% of domestic supplies. Quite simply, the U.S. protein complex is not sufficiently nimble to accommodate the near immediate imbalance in meal consumption that occurred as a result of the continuing pandemic.

Despite the chicken market showing some stability over the latter months of 2020, it remains difficult to draw forward-looking conclusions given that this is a period of seasonal weakness for the industry. Foodservice demand still lags historical averages, and supplies remain high as labor and production resume to traditional levels. The general trade environment for much of the agricultural sector remains muted due to softness in demand from international markets as a result of currency issues and logistical challenges; potential third-wave shutdowns have also resulted in lower commodity prices for a variety of goods. Shockingly enough, despite shelter-in-place orders, sport and live entertainment closures and minimal foodservice availability, the wing market has eluded all obstacles and left buyers paying premium prices for any product obtainable. With COVID-19 cases on the rise, monitoring restaurant traffic and frankly keeping these foodservice channels open will be crucial for any sense of sustained normalcy in the coming months.

Production: It is rare to see a sequential production decline in the second quarter of any year due to the fact that integrators are typically ramping production ahead of the strong summer season. In 2020, this is precisely what occurred as April plant closures and labor shortages resulted in a virtual reduction in capacity for several weeks. However, production challenges for most integrators were not as severe as for other protein sectors, and the backlog of heavier birds were accommodated by the temporary downturn in egg sets. Generally speaking, the broiler complex has been operating nearer normal levels since late August (Figure 1).

The industry is continuing to battle a resurgence in supply of heavy birds due to the challenges in demand from foodservice channels, including the notable shuttering of live entertainment venues, schools and universities, and restaurants. As mentioned previously, the wing market has not been materially affected because it is far less price sensitive (wings are sold to the consumer by count, not weight); however, the breast market has been generally weak due to excess meat. Conversely, the relative performance of the fast food sector, which has been resilient in the latter stages of the pandemic, has driven a shortage in smaller birds, which are scarce due to capacity constraints unrelated to COVID-19. The volatility of the market will continue in 2021 but with the added benefit that export markets appear to be improving with each month. This will help the domestic market clear excess supplies over the first half of 2021 and prepare for more predictable markets as the strain of the pandemic eases later in the year.

Figure 1: U.S. Broiler Production



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Highlights:

- Despite production disruptions emanating from COVID-19, broiler production has achieved some sense of relative normalcy and 2020 volumes (44.6 billion lbs) are forecast to be 2% greater than 2019 production (Figure 1).
- Broiler pricing has experienced turbulence throughout the year due to the conflicting effects of foodservice closures in one major channel but record retail demand among grocers (Figure 2).
- Export markets have begun to reopen and stabilize to pre-COVID-19 levels as U.S. processors seek destinations for record 2020 production; total export volumes forecast to 7.3 billion lbs, up 2% YoY.

Price: As has been widely publicized, food retailers witnessed record traffic in 2020, and many reported strong increases in margins and profitability. With consumers focused on availability, retailers enjoyed significant pricing power, which is evidenced by the material rise in retail pricing across most protein sectors. As shown in Figure 2, the aggregate rise in chicken prices was around 10%, though more popular cuts generally rose by higher amounts. As retailers remain on the offensive in an attempt to take market share, pricing decisions will remain important, but consumers should expect an inflationary price environment for food over the coming years. The “long tail” analysis of COVID-19 includes the likelihood of lasting impacts on the food industry, such as enhanced food safety protocols and employee safeguards, all of which come at a price.

In wholesale markets, it will be important to monitor commodity prices as we move towards the spring season, at which time we would traditionally expect pricing to improve ahead of summer inventory decisions. The timing of any improvement will depend on a number of factors, but importantly, recent broiler hatchery data (Figure 3) does not currently reflect any outsized changes in supplies. If the export markets continue to gain momentum, thus allowing excess dark meat and leg quarters to clear, it should create a sufficient landing spot for heavier birds such that commodity markets will rebound in the summer.

Trade: Export markets began to show signs of life in the latter half of 2020, bringing some much needed relief to both the broiler and pork sectors. Mexico, traditionally a large volume buyer of U.S. chicken, experienced major disruptions in 2020 due to the pandemic but should come back online this year. More encouraging have been the resumption of shipments to Eastern Asia, including China, which perhaps signals better trade relations can be achieved under the new Administration. Certainly there is more work to be done, but monthly shipment data is encouraging.

Figure 2: Retail Broiler Prices

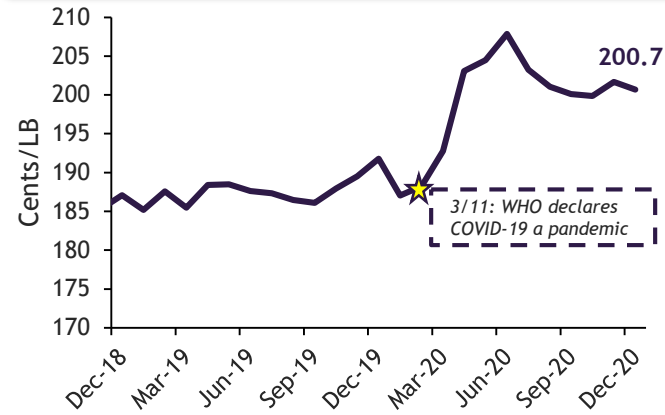


Figure 3: Rolling 12 Wk Eggs Set vs Chicks Placed

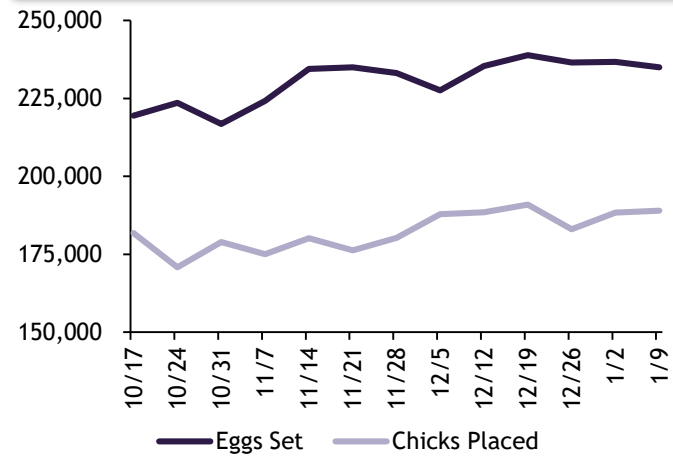
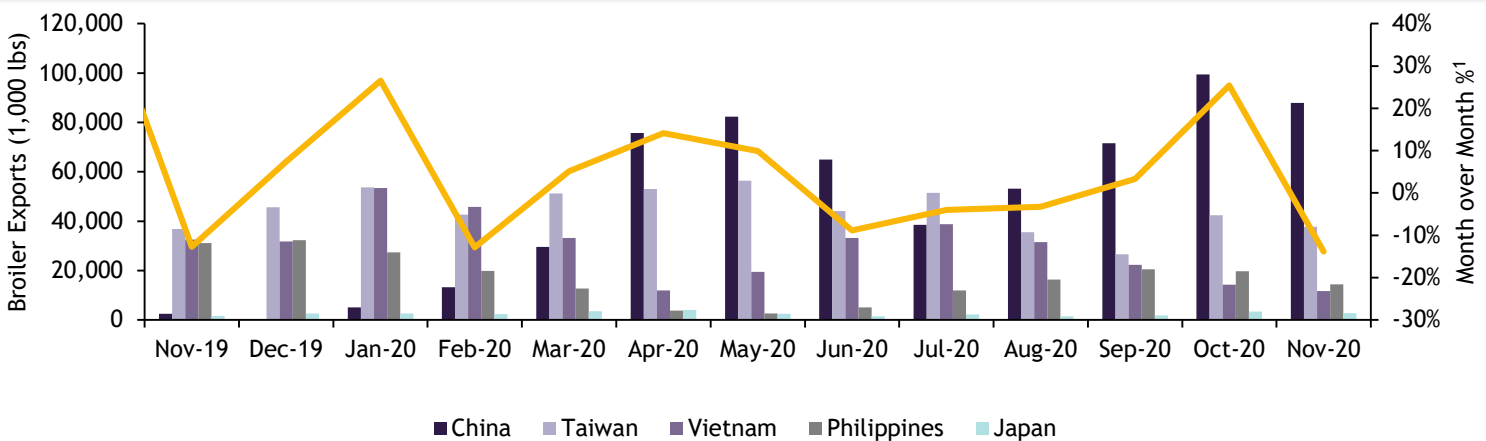


Figure 4: U.S. Monthly Exports to Eastern Countries



Sources: Livestock, Dairy, and Poultry Outlook October 2020, LDP-M-305, U.S. Department of Agriculture, Economic Research Service, November 16, 2020. UrnerBarry, USDA, Wall Street Journal
 1) Month over Month % is a subtotal of the five listed countries: China, Taiwan, Vietnam, Philippines, Japan