Fragmentation is both the blessing and curse of the U.S. beef cattle industry.

The equity required for production – land, feed, cattle, etc. – is so steep per head that the odds of any single entity ever owning a significant percentage of the industry, as is the case in pork and poultry, is remote at best.

In other words, while different segments enjoy comparative advantages at different points of the supply cycle – such as cow-calf producers currently – no single sector and no single player within a sector can drive the market.

Plus, there are 765,000 operations with beef cattle, according to the 2007 USDA Agriculture Census (the most recent available), across the U.S., which also spreads production risk.

With that said, calf production is concentrated in fewer, larger herds. According to USDA’s Economic Research Service (ERS), only 9% of beef cattle operations have herds of 100 cows or more, representing 51% of the total U.S. beef cow inventory.

“Most of these were small, part-time operations. About a third of farms that raise beef animals had a beef cow inventory of less than 10 cows, more than half had fewer than 20 cows, and nearly 80% had

As of Jan. 1, 2012, there were 29.9 million beef cows in the U.S., 3% fewer than the year before and the fewest since 1962. The total cowherd (dairy and beef) on Jan. 1 was 90.8 million head, 2% less than the prior year and the smallest total cowherd since 1952.

Fragmentation clouds direction

On the other side of the ledger, fragmentation makes it difficult for the industry to choose a direction (cattle size, carcass quality, etc.), let alone achieve it. And, in addition to the number of cattle operations, a veritable maze of potential pathways exist beyond the ranch gate.

For instance, although most market calves will end up in a feedlot sometime after weaning, some may stop off at a backgrounding yard first, spend time in someone’s stocker pasture, or both. Or they can take other routes, under the same or different ownership.

There were approximately 17,000 U.S. feedlots with a capacity of 1,000 head or more as of Jan. 1 of this year, according to USDA’s National Agricultural Statistics Service. Only 275 of those feedlots have a capacity of 16,000 head or more. Feedlots with a capacity of 1,000 head or more represent less than 5% of all feedlots but market 80-90% of the fed cattle each year, according to ERS.

From the feedlot, cattle flow to beef packers. The four largest beef packing organizations accounted for 85% of the steers and heifers slaughtered in 2010, according to the 2011 annual report from USDA’s Packers and Stockyards Program.

All told, 33.5 million head of cattle were slaughtered under USDA inspection last year, according to statistics compiled for the National Cattlemen’s Beef Association (NCBA) by CattleFax. Those cattle churned out a total of 26 billion lbs. of beef. Of that, 2.35 billion lbs. were exported.

According to the latest Census of Agriculture, cattle and calf sales generated about $61.2 billion in 2007. That accounted for about 20% of the total market value of agricultural products sold in the U.S. That ranks beef first in sales among agricultural commodities.

More than half of the value of cattle and calf sales come from five states, according to the 2007 Ag Census: Texas, Kansas, Nebraska, Iowa and Colorado. In terms of beef cow numbers, the top five states are: Texas (4.37 million), Nebraska (1.88 million), Missouri (1.86 million), Oklahoma (1.73 million), and South Dakota (1.61 million).

From the packer, beef moves to further-processors, some owned by beef packers, then into retail or food service channels, often by way of a massive, though concentrated, food distribution system.

There were 36,569 supermarkets in 2011 with annual sales of $2 million or more, according to the Food Marketing Institute. There were 580,852 U.S. restaurant units in the fall of 2011, according to The NPD.
Now, throw in other areas of food service that procure beef, be it schools, the military, hospitals, etc.

Ultimately, the beef that’s not exported winds up on the dinner plates of a current U.S. population numbering 313.9 million people. In round numbers, per-capita beef supply last year was about 57 lbs.

The end result is that domestic consumers can buy beef at retailers and through food service every day of the year, in about any form and volume they want.

To say that the overwhelming complexities necessary to achieve this reality are miraculous would be an understatement. No one could sit down with a roomful of the brightest minds and concoct such a scheme that works largely because of a marketplace that leads the way.

The cold reality is that supply and demand fundamentals seem to matter less to markets today, at least minute-to-minute and day-to-day. There is just too much money, from folks with no physical position to protect, shoving prices around. The amount of information fueling emotion and micro-logic is too fast and vast.

Over time, though, supply and demand fundamentals still drive the market, which drives each sector of the industry.

Along with murky directional ability, another glaring pitfall to this fragmented system is communication. When consumers want something different, or have a poor eating experience, their message begins a long way from the folks buying the bulls to breed to the cows that produce the carcass for future eating experiences.

Not to mention the distance in time. Figure a beef cow gestation length of 283 days. Figure a steer is 15 months old when he saunters beneath the golden arches. That’s right at two years from gate to plate.

**Understanding each other**

The truth is that industry sectors understand too little about one another. That’s what alliances and vertical cooperation between segments is supposed to help solve.

The good news is that, for all practical purposes, the carcass target for the greatest consumer value has remained virtually the same for at least 25 years.

But, understanding follows the bounty, or dearth, of communication. Both understanding and communication continue to elude beef industry sectors when it comes to one another.

Consider the recent consumer backlash surrounding lean finely textured beef (LFTB) this spring, which ultimately decimated more than one company, as well as a proven technology. There were as many beef producers unaware of LFTB as there were consumers.

When BEEF magazine recently asked leaders across the industry spectrum how the magazine could help producers the most—what topics it could cover that it wasn’t already—the common response was: “help them understand the workings of the different industry segments and their interdependence.”

All the respondents said fostering such an understanding is an industry necessity going forward. Thus, during the next year, we will profile each industry segment, offer a sense of its size, challenges and opportunities. Along with that, we’ll highlight important technologies that have helped deliver higher-quality beef animals and end products in a more efficient and cost-effective way.
Part 2: Seedstock Sector - Seedstock Sector Represents Both Beginning & End Of Beef Production

At its simplest, the seedstock sector represents both the beginning and the end of beef production. It provides the genetics utilized by commercial cattle producers to build market calves for harvest, as well as replacement females to replenish the commercial cow factory. Seedstock producers also provide the genetics they and their peers will use to build the next generation of seedstock.

Ideally, seedstock production also represents the final link in the production chain, as producers survey successes and failures based on economic signals received by them and their commercial customers, and adjust the genetic potential.

That’s where it gets complicated.

Even when economic signals are clear – and some would argue they never are – mating decisions for seedstock today cannot result in commercial use for at least two years; and market results can’t be known for at least three years.

What goes into mating decisions represents an attempt to find balance amid a chaotic array of data. There are weights, measures, EPDs, indices, various DNA profiles, pedigrees, inbreeding coefficients, etc.

Learning and sorting through this complexity is all the more remarkable when you remember that, in relative terms, modern seedstock production – modern beef production for that matter – is still in its infancy.

“Distinct breeds did not emerge until the second half of the 18th century when the industrial revolution in Europe created a need for more productive animals,” writes Harlan Ritchie, Michigan State University distinguished professor of animal science, in his book, “Breeds of Beef and Multi-Purpose Cattle.”

“More than any other single factor, the need to feed workers of the newly created mills and factories was responsible for the advent of modern breeds and breeding practices...It is probably not an exaggeration to state that the industrial revolution spawned the cattle revolution...,” Ritchie writes.

Consider that Hereford and Angus cattle came to the U.S. in the late 1800s. Research aimed at beef cattle didn’t start until the early 1900s. And the modern U.S. beef industry, built upon cheap corn and energy, didn’t start taking shape until after World War II. Technology to successfully freeze and thaw semen didn’t debut until the 1950s, and the Continental breeds didn’t show up in the U.S. until the 1960s.

If you ever wonder how successful seedstock producers have been in harnessing evolving technology, check out the genetic trends; some breeds have literally transformed themselves in less than two decades.

Successful seedstock producers

Charged with both anticipating and reacting to market signals and customer demands, it’s easy to understand why the most successful seedstock producers are those who understand the cattle business end to end. They know what drives customer profitability, as well as the marketability of their customer’s calves, whether sold at weaning, retained through the stocker pasture or retained clear through finishing.

“The challenge for commercial cow-calf producers is finding genetics that will complement their cowherds in their unique environments, while maintaining or reducing costs, and adding value to the
calf crop at the same time,” says Bob Prosser of Bar T Bar Ranch, based at Winslow, AZ. “Simple as that sounds, making it happen depends on forging a relationship with a seedstock producer who is committed to helping his customers reduce costs, add value to their product, and increase marketing opportunities while producing a quality product for the end consumer.”

The Prossers serve as an example of seedstock producers based in commercial production. In addition to their seedstock herd, they maintain a commercial one. They run stockers, feed cattle, and are involved in value-added branded beef programs.

**Demanding customers**

The only customer a commercial producer must face is the sale barn or order buyer. If seedstock producers are going to stay in business, they must face a lot of customers and prospective customers, all with different personalities, goals, resources, wants and needs.

Bull buyers can be a fickle lot, too. They’ve been known to cuss breeders for selling them bulls that melt in the pasture when turned out the first time because they were over-conditioned. Then they’ll go buy fat bulls again next year because they are more appealing to the eye than harder, pasture-ready ones.

_Industry Resource Page: Bull Management_

Of course, seedstock producers can be a fickle bunch, too. Some have been known to single-trait select for the purposes of marketing at the expense of balanced production.

“The seedstock sector is at a crossroads where more than superior pedigrees and outstanding EPDs will be required,” Ritchie said in his 2000 paper, “Where is the Beef Seedstock Industry Headed?”

“Commercial customers are continually expecting more from their genetic providers. In order for mainstream seedstock breeders to ensure their sustainability well into the future, it will be necessary that they strive to become full-service genetic providers,” Ritchie says.

_**My View From The Country Blog: Where's The Seedstock Sector Headed?**_

Troy Marshall, 9/2/11

I really admire breed associations and believe strongly in what they’ve done for our industry in genetic improvement. Breed associations employ some of the brightest, most passionate people in our industry and they’ve prospered over time because they’ve been very successful in creating value.

With bull prices at historically high levels and the value of superior genetics growing exponentially the last half-dozen years or so, many would argue that this is a great time to be in the seedstock business. But, as is often the case, good times invite new competition and innovation, and there are those looking to challenge the current structure of our business. Much like Blockbuster Video, which failed to recognize and adapt to changing marketplace realities, breed associations are finding they have to re-create themselves in order to survive.

The pork industry is a great case study in how breed associations and the traditional seedstock business model were rendered largely irrelevant by creeping change. We’re seeing similar changes occurring on the beef side, as various entities begin to challenge the traditional model by not utilizing the existing genetic evaluations or by looking at new ways of sourcing seedstock.

Of course, genomic-assisted selection has the potential to radically alter how we evaluate genetic merit. Then there’s the advent of sophisticated supply-chain systems that allow the assimilation of lots of real-world data merged with real-world economic factors, coupled with the capability to conduct herd genetic evaluations.

Throw in the fact that the industry is now making a shift from grid marketing to more program cattle, and the egalitarian view of access to information becomes more questionable. Every seedstock producer in
the country, from largest to smallest, has enjoyed equal access to the results of national genetic evaluations and the industry’s elite genetics. That, however, is looking increasingly less likely as we move forward.

It’s similar to the realignment occurring among major college football conferences, where some folks predict that television revenue distribution deals will lead eventually to four super conferences. Similarly, the need to be part of a bigger group will be crucial for survival in the beef industry. The questions then become those of what those groups will look like, and what role will the breed associations play in supporting them?

I’m not opposed to change; in fact, I believe change is usually either good or necessary. But I still hold dear the concept of individual producers controlling their own destiny, with seedstock purchases being based on genetic merit and personal relationships. From a personal standpoint, I don’t believe the pork industry model is in the best interest of the beef industry, and certainly not in the best interest of beef producers. So how do we ensure that we don’t end up going the same route?

Many would argue that there are two major factors that preclude the cattle industry becoming like the pork industry:

- The first is that the cattle industry is too capital-intensive, and too extensive in its nature. The argument is that there are far too many production schemes, environments and marketing programs inherent in the U.S. beef business to allow the definition or propagation of absolutely superior genetics.
- Second, it can be argued that the work of breeders and breed associations makes it extremely difficult for some entity to come in and develop genetics that are vastly superior to what’s already being produced.

There are other factors at play as well, things like generation interval and the like, but the bottom line is that we are looking at a highly competitive and ever-changing structure for the industry.

Personally, I’m betting individual producers and breed associations will adapt, remain relevant, and strengthen their relationships and genetic-selection capabilities. Admittedly, there are some betting that they can replace the existing models with something better. But, the new shape of the seedstock industry will be determined by how much genetic improvement and selection pressure the various models can apply, and how well those systems help their customers capture and leverage the value of the superior genetics and management that producers are putting into their cattle.

I certainly lean to the collective expertise that breed associations and seedstock producers currently have, but believe that both will dramatically rethink the way they conduct their businesses. It’s true that the pork and poultry industries went down the paths they went because someone employed better models; and many of those economic drivers exist in the cattle industry as well. The question is whether we can create systems to take advantage of those drivers without sacrificing the independence of individual producers.

I believe we can and will avoid those pitfalls. Leading breeders have produced genetics that add value to their customers and have backed those genetics with excellent customer service. Breed associations have provided their breeders with the tools to make rapid genetic improvement and to help their customers succeed. More, however, will be required and just how those attributes are defined is being rewritten.

Breeders are human and the tendency is to stay with what has worked, even after times have called for change. Similarly, breed associations have tended to develop a silo mentality, with the mistaken belief that they can defy economic drivers through policy. Those tactics may work for awhile, but long-term success will be gained by those who adapt the most quickly to the realities of the marketplace.

Though seedstock producers of all sizes are successful, selection dynamics, production and marketing costs, and customer service favor larger seedstock herds. That doesn’t mean the same herd, necessarily; alliances between individual herds offer similar advantages.
Richie explains, “A number of seedstock producers have already positioned themselves as full-service providers. The services they offer are similar to those provided by the genetic companies and mainstream independent breeders in the swine industry.”

**Seedstock opportunity**

Adding to the challenge of seedstock production is the simple fact that demand is always limited by the size of the commercial cowherd.

In 2006, there were 33.25 million beef cows that calved, according to the National Agriculture Statistics Service (that year is chosen for context with the breed numbers that follow). If you figure a bull for every 25 cows – excluding those bred artificially – there was a need for about 1.33 million bulls. If you figure a fourth of that requirement needs to be replaced each year, about 332,500 bulls needed to be marketed that year.

In round numbers, 17 of the most populous beef breeds registered 765,038 bulls and females in 2007, according to the National Pedigreed Livestock Council. (That’s the most recent year in which all of the seven most-used breeds reported registration numbers. The movement of some breed associations to whole-herd reporting has made year-to-year comparisons more tenuous.)

Of those registrations, 86% came from seven breeds, which speaks to the ongoing breed consolidation that began at least 15 years ago.

Ritchie proved prescient more than a decade ago when he predicted: “Very few of the 50-plus beef cattle breeds in the U.S. will disappear, but they will likely sort into three groups:

- 10 breeds, or perhaps less, that will provide the genetic make-up of the bulk of the commercial cattle population;
- a few breeds having unique attributes that will be involved in niche markets;
- recreational breeds that will provide pleasure and entertainment to hobby breeders via shows, field days, etc.”

Keep in mind, these numbers cannot account for unregistered seedstock. That includes commercial producers who find a cracking good calf to sell to the neighbors, as well as large entities currently crafting a model of seedstock production and marketing that mirrors that of the swine industry.

“Seedstock producers must produce genetics specific to commercial cattlemen’s needs, while meeting the specific requirements of the feeder, packer and retailer,” Prosser says. “This is not to be construed that every seedstock producer must produce cattle that will fix each and every commercial cattlemen’s problem. Rather, it means that responsible seedstock producers must forge relationships with commercial customers to identify opportunities and assist in finding solutions.”
Part 3: Cow-Calf Sector - Cow-Calf Production Is Largely A Part-Time Business

America’s beef **cow-calf business** seems straightforward enough – wean the highest percentage of calves possible per cow exposed, **wean the most pounds possible** per cow exposed, and do so for the least cost possible. Exploiting value-added opportunities is part of the formula as well, but the above has been the basic business model for at least five decades.

It’s the business reference in the model where reality becomes less straightforward.

Depending on the size of your abacus and whether you’re using your toes, beef cows, which are the lifeblood of the cattle and beef industries, fuel an annual economic impact of at least $1 trillion.

Cattle and calf sales were worth about $61.2 billion in 2007, according to the most recent USDA Census of Agriculture. Those receipts represented about 20% of the total market value of agricultural products in the U.S. that year, making it the leading commodity.

According to the American Meat Institute ([AMI](#)), meat and poultry industry sales in 2009 were $154.8 billion. “In all, companies involved in meat production, along with their suppliers, distributors, retailers and ancillary industries, employ 6.2 million people in the U.S. with jobs that total $200 billion in wages,” according to AMI’s **“U.S. Meat Industry at a Glance”** report.

“Through direct taxes paid, these companies and their employees provide $81.2 billion in revenues to federal, state and local governments. The consumption of meat and poultry generates $2.4 billion in state sales taxes. The meat and poultry industry’s economic ripple effect generates $864.2 billion annually to the U.S. economy, or roughly 6% of the entire GDP,” the report says.

Okay, so lumping it together is cowboy math, but the point is beef cows are responsible for a pile of money and make a huge annual national economic impact, no matter how you figure.

**Few full-time producers**

Yet, the cow-calf business is, on average, largely a **part-time endeavor**.

“Operators of more than a third of beef cow-calf farms worked off-farm in 2008, and half of beef cow-calf farms are classified as rural residence farms,” say William D. McBride and Kenneth Mathews, Jr., in **“The Diverse Structure and Organization of U.S. Beef Cow-Calf Farms,”** which was published by USDA’s Economic Research Service ([ERS](#)) last year. “These farms are **small operations** that specialize in beef cow-calf production but report off-farm earnings as the primary source of household income.

Commercial farms with beef cow-calf enterprises are mostly diversified farm operations on which cattle are a secondary enterprise that accounts for about a fourth of farm product value.”

The ERS study summarized information from a 2008 Agricultural Resource Management Survey ([ARMS](#)) and also utilized state data from the USDA Ag Census for 1997, 2002 and 2007.

The lion’s share of beef cow operations (80%) had 50 head or fewer, representing 27.7% of the cow inventory in 2011. Operations with 100-499 cows represent 8.7% of the operations and 38.2% of the cow inventory (Table 1).

Noted agricultural economist James McGrann puts it this way: “In reality, fewer than 4% of beef cow-calf operations make their sole living from the cow-calf enterprise. This means that the industry can produce at least 50% of the feeder cattle and not be profitable to owners. These calves support the feedyard and packing industry and lower consumer cost of beef.” McGrann is a Texas A&M University professor emeritus and owns Ranch Management Economist, a ranch business consulting firm.
There are plenty of reasons why those who specialize in beef production tend to be among the smallest producers, and why the largest herds tend to be part of a diversified agricultural operation. Economics tops the list.

“No one can start a ranch business with ranch earnings and expect to earn $60,000 before self-employed and income taxes. With a 2% return on investment (ROI) in ranching, it would require $3 million in equity. Assets earning 2% can service only limited debt,” McGrann explains. “The cow-calf sector is an investment business and ROI is what attracts capital for growth.”

Beef cow-calf production continues to be driven as a byproduct of land ownership, with land becoming more difficult to acquire.

“Increase in land values does make landowners wealthy, but makes it prohibitive for young ranchers to enter the sector without equity contribution from parents or off-ranch income,” McGrann says. “The high cost of estate transfer means it’s difficult to hold ranches together between generations.”

Off-farm income is the rule

“The amount of off-farm income earned by beef cow-calf producers in 2008 dwarfed farm income,” say McBride and Mathews. “Average off-farm income was about $72,000 among all beef cow-calf farms, nearly three times higher than net cash farm income, and $20,000 more than gross cattle sales.” They explain average gross cash income in 2008 was $600,000 for commercial farms, $77,000 for intermediate farms, and $34,000 for those classified as a rural residence (RR).

ERS analysts divided ARMS participants based on what they term “farm typology.” RR farms are defined by less than $250,000 in gross annual sales and operators who consider the agricultural operation to be a secondary activity. Intermediate farms report farming as their primary occupations and have annual gross sales of less than $250,000. Commercial farms are large family farms or non-family enterprises with annual gross sales of more than $250,000.

“Net cash and net farm incomes in 2008 were about $174,000 and $136,000, respectively, on commercial farms,” McBride and Mathews say. “In contrast, intermediate farms earned about $11,000 and $7,000 in net cash and net farm income.”

For RR farms, net cash and farm incomes in 2008 were negative.

“Operators of RR farms often have goals other than profitability, as most work off-farm or are retired, and farming may be regarded as a lifestyle choice,” say McBride and Mathews. Off-farm earnings on RR farms averaged nearly $90,000/farm in 2008.

With profit a secondary motivation for so many, it’s little wonder the knowledge gap is growing between participant groups, or that there is so little progress in cow productivity on average (based on Standardized Performance Analysis data). It also helps explain the lack of what some would consider essential management in some parts of the sector.

For instance, according to the National Animal Health Monitoring System’s (NAHMS) “Beef 2007-2008 Reference of Beef Cow-Calf Management Practices in the U.S.” report, 46.1% of cow-calf operations calve year-round, 31% didn’t vaccinate any calves or cows within the previous 12 months of the survey, and 60% didn’t vaccinate for bovine respiratory disease from the time calves were born to the time they were sold, etc.

Industry Resource: Tools & Programs Exist To Help New Ranchers

Then there’s the age thing. The average age of RR farm operators in the ARMS survey was 60 years old, and 25% of those said they planned to exit the business within five years. Meanwhile, the average age of
intermediate farm operators was 62, and 24% of those planned to exit. And the average age for commercial farm operators was 55, with 14% of them indicating they planned to exit within five years. These realities help explain why, more than drought, the commodity bubble or the Great Recession is behind the ongoing reluctance of producers to expand the nation’s cowherd.

**Part 4: Stocker Sector – Beef Industry's Stocker Sector Is Vital But Fluid**

Defining the stocker cattle sector should be relatively straightforward. Producers add weight to calves removed from their mamas before those calves enter a feedlot. By and large, it’s a margin business that revolves around the value of gain – what the market is paying for additional weight – relative to the cost of adding that weight. Pay too much up front and margins are so narrow you’ll have a hard time ever catching up.

**A Closer Look: Managing The Margin Is Critical In Today’s Environment**

“Managing for a margin is much more important today than at anytime in the past,” says John Rakestraw, CEO of Colorado-based Agra Holdings, which feeds cattle, provides feedlot consulting, and manufactures feedlot nutritional supplements, among other feedlot-based activities. Between 1984 and 2003, Rakestraw worked for ContiBeef LLC – he was CEO and president from 1995 to 2003. ContiBeef – sold to JBS and operating currently as Five Rivers Cattle Feeding – was and is the largest cattle feeding organization in the world.

Rakestraw shared his perspective with stocker operators at the recent Mid South Stocker Conference in Tennessee (2012).

“You need about double the money to operate today than a few years ago,” Rakestraw says. “Your return on assets deployed has decreased and will continue to decrease unless net profits per unit of production also double.”

At the same time, Rakestraw explains, “There is no fundamental basis to determine prices today. Now, commodity prices are impacted greatly by the macro-economic environment and local-weather effect on international crops,” Rakestraw says. “The effectiveness of forecasting future prices based on underlying fundamentals has greatly decreased.”

Likewise, Derrell Peel, Oklahoma State University Extension livestock marketing specialist, says, “Pretty much anything you have to sell today sells pretty well. Marketing has gotten easier. Quality management is now the primary concern.

“You need to spend more of your attention than ever before on managing production. Manage health, manage nutrition and manage cost to benefit from this market environment we’re in.”

Peel was speaking to stocker operators at the recent Backgrounding for Quality seminar at White Brothers Cattle Co., Chickasha, OK.

So, Rakestraw suggests focusing more intently on managing the margin, recognizing and controlling components of production and marketing that can be controlled, while managing risk on the uncontrollable.

Purchase prices of cattle and feedstuffs, hedging and incremental selling prices are all aspects of marketing that can be controlled, Rakestraw says. Meanwhile, performance, consistency of performance, as well as production and operating costs, are production components that can be controlled.

Consider an example from Rakestraw – a $230 ration and putting 300 lbs. on a 550-lb. steer – where apparently inconsequential gains yield staggering return. Decrease purchase price by 50¢ and increase the
sales price by 50¢ through old-fashioned bargaining. Reduce feed costs by 5%, be it through buying outside the spot market, bargaining harder or finding lower-cost ingredients. Reduce mortality by just 0.25%. Make 50¢/cwt. by hedging. These small changes add up to $16.86/head or an additional 2.56% annualized return on investment.

Looking more broadly, stocker cattle and those who run them serve as the lynchpin of the entire cattle and beef business.

For one thing, this sector acts as governor to the industry engine, receiving cattle from a national cowherd that churns out most of its calves in the spring of the year, then parceling them out so that feedlots, beef packers and consumers have a steady supply throughout the year. This warehousing function also enables the industry to absorb supply shocks within and across years, whether it’s drought forcing more cattle to market than usual, or cowherd attrition serving up fewer calves.

Even before the recent higher grain price paradigm, the forage-focused nature of most stocker enterprises offered a more valuable alternative use to forage. With higher grain prices, cheaper forage-based gains are one way the industry can be more price-competitive with other meat proteins.

The stocker sector also removes incalculable levels of variation from the industry. No one can turn the proverbial sow’s ear into a silk purse, of course, but stocker operators can gather, manage and market load-lots and pen-lots of similar cattle. This packaging offers more value to buyers because management can be more consistent. In turn, that offers more value to the industry.

Stockers - ubiquitous, invisible

Yet, the stocker sector remains so nebulous that no one has ever been able to wrap their arms completely and surely around it.

For one thing, it’s often difficult to distinguish stocker operators from their participation in other industry sectors. The 2008 BEEF National Stocker Survey (NSS) found only 17.2% of stocker producers were exclusively in that segment of the cattle business. Of those, 52.3% said stocker cattle accounted for 50% or more of their annual gross income.

Cow-calf producers who also stocker cattle comprise the largest segment of stocker operators (64.6%). Others running stocker cattle include producers involved from cow-calf through cattle feeding (10.6%) and feedlots (4.8%).

Definitions and terminology create confusion, too. One person’s backgrounding program is another’s stocker enterprise. One person sees a starter yard where someone else perceives a preconditioning program. It’s that kind of thing.

Who’s Who in The Stocker Business: Bob Price, Gracie Creek Ranch Named 2012 Stocker

Part of the murkiness has to do with animal classification. One of the surest opportunities over time has been buying cull cows at their typical seasonal price ebb in the fall of the year, adding weight to them, and exploiting typically higher prices during the winter. Few would regard them as stocker cattle, though.

“The stocker industry can’t be distinguished by a particular age, size or class of cattle, or by a particular production system,” explains Derrell Peel, Oklahoma State University Extension livestock marketing specialist.

Even when you confine the stocker classification to calves, there’s no way to calculate how many there are at any given time. But you can estimate the potential supply of stocker cattle with the annual Jan. 1 USDA Cattle Inventory report.
For instance, there were 25.7 million head of stockers last January, 28.3% of all cattle and calves. Specifically, that number is derived from inventory classifications of calves weighing less than 500 lbs., as well as non-replacement heifers and steers outside feedlots weighing more than 500 lbs. But it can’t account for suckling calves at the time, nor does it consider what percentage of the inventory’s 500-lb.-and-heavier bulls will end up as steers.

Incidentally, while an imperfect measure, Peel explains this potential stocker calf pool can also be used to measure the relative supply snugness that feedlots face. The number of cattle on feed relative to the pool of calves outside of the feedlot used to run about 4:1. In other words, for every animal on feed, there were four more out in the country that could replace it. This ratio is now about 2:1.

Moreover, there’s no way of telling how much of that potential supply will go through some sort of stocker program. Common sense suggests most will, but any guesses are just that. And, there’s no telling how many different stocker programs an individual calf ultimately traverses.

Consider a calf that’s purchased and commingled, held on grass for a while, shipped to a starter yard, put on winter wheat pasture, and then sent to summer grass. When considering potential supply, this single head represented multiple opportunities. So, the supply of available stocker cattle at any given point in time is larger in reality.

Stocker operators are also difficult to describe because of the variety of business models. Traditionally, those outside the sector often view stocker operators as those who buy holes in the market, procuring the mismanagement of others. That’s true on one end of the spectrum, but on the other end are operations that buy only preconditioned calves of strict genetic profiles in order to sell into value-added markets. A wide variety exists in between.

For perspective, according to the NSS, 23.9% of stocker-exclusive operators buy cattle below the average (straightening out someone else’s problems), while 65.3% say they buy at market average; 10.8% say they buy over the market. Stockers of all operation types and tenure in the NSS say buying high-quality cattle is a chief tool for managing market risk.

Finally, the stocker business is difficult to corral because there are few biological boundaries. Cows typically remain in the herd until they’re culled. Calves move to another production phase at weaning. And, for every head entering a feedlot, there’s a narrow marketing window for its exit. For stocker operators, though, they’ll buy and sell whenever the market offers opportunity.

**Part 5: Feedlot Sector - High Costs Challenge Cattle Feeding’s Rules Of Thumb**

Beef Magazine 11/26/12

Cattle feeding has always revolved around opportunity and need, usually both at the same time.

Sugar and cotton mills in California – commonly regarded as the root of modern commercial cattle feeding in the 1930s – offered the opportunity with cheap sources of feed. The need was to feed an influx of Dust Bowl immigrants.

For the record, history tells us the practice of feeding groups of cattle to slaughter weight is at least as old as the nation itself. The sprawling, business-first, intensively managed cattle feeding industry of today grew from those California roots to Arizona and finally the High Plains in the 1950s and 1960s. Farmer-feeders had already been going strong in the Corn Belt and as far west as places like Colorado for decades.
Arguably, it was the beef price freeze in 1973 that spawned the first round of consolidation that led to today’s scenario where five cattle feeding organizations control 20% of all cattle feeding capacity and churn out 80% of the annual fed cattle supply. At the time, survival demanded greater economic efficiency. One opportunity was acquiring the feedyards that had bankrupted others in the colossal economic wreck.

In other words, cattle feeding has never been for the weak of heart. There’s too much money, time and risk tied up in a pen of cattle that will be priced in a narrow marketing window.

Though it was never easy, nor guaranteed, modern-day cattle feeding used to pay well enough, often enough to recover from the losses in between, if you stayed in the market.

One of the reasons is that for all the uncertainty – until the commodity bubble a few years ago – the averages associated with cattle feeding were fairly predictable. These included cheap corn, how much different classes and weights of cattle consume and gain, price seasonality, basis, how various technologies impact performance and carcass quality, even the fundamental way the futures market seemed to ebb and flow.

Though predictability remains for live-cattle performance, commodity markets have become so divorced from fundamentals, and competition for feed resources so fierce, that price volatility and increased financial risk reign as never before.

Another Perspective: Ethanol Policy Is Busted

Citing the “Historical and Projected Kansas Feedlot Returns” report from Kansas State University (KSU) as an example, from January 2002 to September of this year, estimated monthly net returns for steers fed in Kansas feedlots were negative 61% of the time. Only two months in the past 18 (up to September) showed positive returns. This past summer was historically ugly. Steers in August were estimated to have lost $253/head, according to the KSU data.

Keep in mind, these estimated returns are projected on a cash basis; there is no way to account for the risk management of different feedlots on each pen of cattle or premiums received beyond the average price.

As important, keep in mind, the estimated net returns are based on owning, feeding and selling cattle. Feedlots are a different business entity altogether. In the case of commercial ones, revenue is generated from services and feed sold. The line between feedlots and cattle feeding gets obviously blurry because many commercial yards own a substantial number of the cattle being fed there.

Economics demand downsizing

The need has emerged once again in recent years. It points to a need for the cattle-feeding sector to downsize because there are so few cattle relative to available feeding capacity. In part, it also has to do with the fact that cattle feeders have been able to produce as much beef in recent years with a cattle inventory of 90.8 million head or so, as there was produced in the mid 1970s with 135 million head.

“Not only are feedlots paying record prices for feed and essentially record prices for feeder cattle, it’s been recognized for quite a while now that the supply of feeder cattle will be increasingly inadequate to maintain feedlot inventories at any price,” says Nathan Anderson, Oklahoma State University (OSU) Extension director and agricultural educator for Payne County.

Breaking It Down: Feedlot Capacity And Long-Term Profitability
Anderson and Derrell Peel, OSU Extension livestock marketing specialist, explain that feedlots maintained inventories by feeding lighter and younger animals for longer periods of time when cattle numbers peaked in the 1970s and began to decline.

“Feedlot inventories (in the 1970s) represented slightly less than 11% of total cattle numbers and 31% of feeder supply,” Peel says. “This last figure means there were approximately three feeder cattle available to replace every animal already on feed at the beginning of the year.”

By the 1990s, Peel says feedlot inventory represented nearly 13% of total inventory and more than 40% of feeder supply. So, there were typically fewer than 2.5 replacement cattle available for every animal in the feedlot.

In the last decade, feedlot inventories represented almost 15% of total cattle inventories and 51.4% of feeder supplies.

In 2012, Peel explains the Jan. 1 feedlot inventory was 14.1 million head, a record 15.6% of total cattle inventories and 54.9% of feeder supplies. In other words, there are currently 1.8 feeder animals available for every animal in feedlots.

“Obviously, the only possibility for this level of feeder-cattle supplies to maintain feedlot inventories is with the very slow turnover rate that comes with feeding ever lighter and younger animals for longer periods of time,” Peel says. “Corn prices that average twice the historical level, and currently are 3.5 times historical levels, make this economically infeasible.”

If this year’s drought hadn’t occurred, Peel reckons corn prices might be closer to $5/bu. rather than the current $7 plus. “While these short-run factors would have changed the feedlot picture somewhat, they don’t change the fact that the role of the feedlot sector is changing and must change fundamentally in the future compared to how it has operated in the past,” he explains.

“It is likely that corn prices in the future will average at least twice the level under which the feedlot industry we know today evolved,” Anderson says. “The point is that even without the drought, feedlots face a significantly different business environment.”

Peel adds, “The already high pressure resulting from chronic excess feedlot capacity will increase sharply in 2013 and 2014.”

For perspective, there were 2,091 feedlots with 1,000-head or more capacity in 2000, according to the annual summary from the National Agricultural Statistics Service (NASS). In 2011, there were 2,140. In 2000, total bunk capacity of those yards was estimated at 16.5 million head. It was 17.0 million head in 2011. Tables 1 and 2 illustrate other feedlot trends.

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<th>Year</th>
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Source: Compiled from February Cattle on Feed reports from National Agricultural Statistics Service.

Ultimately, Peel and Anderson say that expanded beef cattle inventories will allow feedlots to respond appropriately to high corn prices by placing heavier cattle and reducing days on feed.

The need is there. It’s the opportunity side of the equation that cattle feeders are in the midst of conjuring.
Part 6: Packing Sector – Market Conditions Will Shrink U.S. Packing Sector

"It’s a complex business because there are so many moving parts, but it’s not really that complicated,” James Henderson says of the beef packing business. “You figure your cost on a per-head basis and your revenue by the pound. As long as that’s the case, the incentive is to make carcasses heavier.”

Henderson of the Bradley 3 Ranch in Memphis, TX, has a long history in the beef-packing business, including a stint as vice president of B3R Country Meats. He now consults in the packing business.

In simplistic terms, if you’ve invested in the capacity to harvest 6,000 head of cattle/day, the primary way to drive costs lower is by utilizing as much of that capacity as possible. But, as cattle numbers dwindle, that’s tougher to do.

In fact, it was declining cattle numbers and increased competition from poultry – the impact on cost and profit margins – that fueled the mass concentration and consolidation in the 1980s that had so many producers wringing their hands; some still worry their knuckle fuzz over it.

“When both are operated close to capacity, smaller plants are at an absolute cost disadvantage compared with larger plants,” according to the Livestock and Meat Marketing Study (LMMS) prepared for the Grain Inspection, Packers and Stockyard Administration in 2007. “When larger plants operate with smaller volumes, they have higher costs than smaller plants operating close to capacity and, thus, have an incentive to increase throughput. For all plants, large and small, average total cost increases sharply as volumes are reduced…”

Go back to the early 1900s and history says there were the Big Five packers – Armour, Cudahy, Morris, Swift and Wilson. Charges of packer collusion led to the Packer Consent Decree of 1920. Among other stipulations, the law forced them to divest ownership of public stockyards, stockyard railroads and market newspapers.

As the nation’s cattle population and beef demand grew, so did the number of independent beef packing companies. As late as 1980, what is termed the Four-Firm Concentration Ratio (Table 1) was 36%.

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Source: 2011 Packers and Stockyards Program (P&SP) Annual Report

Today, we have the Big Four – Cargill Meat Solutions, Tyson Foods, Inc., JBS Beef Co., and National Beef Packing LLC. They accounted for 85% of the nation’s steer and heifer slaughter in 2010, according to the 2011 Packers and Stockyards Program (P&SP) Annual Report.

There were about 140 cattle packing plants (not to be confused with packing companies) in 2010, according to the P&SP report. The Big Four owned 29 of them, according to Steve Kay at Cattle Buyers Weekly. The 258 firms subject to the Packers and Stockyards Act in 2011 were 28% fewer than in 2000.
Incidentally, packer ownership of cattle is far less pervasive than some perceive. According to the P&SP report, packer feeding represented a little more than 5% of cattle in 2010; and it doesn’t fluctuate much. P&SP defines packer-fed cattle as those obtained for slaughter from a subsidiary of the packer, the packer’s parent firm, or a subsidiary of the packer’s parent firm, owned in part, or in whole, for more than 14 days before the cattle are harvested.

**A Closer Look: What’s Ahead For The U.S. Meat Business?**

Forward contracting represented just over 12% of packer procurement in 2010. About 60% of fed cattle traded on a carcass basis in 2010 with the remainder purchased on a live basis. According to the P&SP report, around 40% of fed cattle traded in 2010 were procured by packers through negotiated trade; slightly more than 40% were formula-priced. The remainder was procured through forward-contracts or packer-feeding.

Though some folks carry on the packer witch hunt, the fact is that there is no grand conspiracy among packers to control the market. Instead, the sheer scope of this particular margin business demands strict adherence to economics. They’ve embraced tools like alternative marketing arrangements (AMAs) simply because that’s what the market says is in their best financial interests.

**Sorting cuts both ways**

“In the packing business, it’s never as much about the market as it is about plant utilization,” Henderson emphasizes. “Plant utilization drives packer profitability.”

Arguably both have been helped and hindered by the manifold increase in packer sorting that began with the latest round of beef branding in the 1980s.

“I can remember when there were three cooler sorts – Prime, Choice and everything else,” Henderson says. Today, he says the largest plants utilize more than 30 sorts, many of those occurring before cattle get to the cooler. Think here of such things as natural beef, different export requirements for beef that can go to Europe or Japan, the eligibility requirements for various breed brands, and all of the rest.

For each pre-cooler sort, Henderson explains the fabrication area must be cleaned, which costs thousands of dollars each time. Then packers must keep track of around 200 products from each of those sorts. Where packers might have produced and marketed 600 products 25 years ago, they might have more than 6,000 products today.

According to Henderson, this exponential increase in sorting, along with heavier carcass weights, has enabled packers to dilute the impact of dwindling cattle numbers to some degree. At some point, though, he suspects some packing capacity must exit the business.

Paradoxically, taking some of the sorting out of packer hands could grow the economic pie, both for packers and producers.

“As an industry, we decided to let the packers sort the cattle rather than sort them ourselves, and that’s not something they’re necessarily good at,” Henderson says.

Instead, imagine producers further employing technologies like ultrasound and genomics to sort cattle before they ever head to the packing plant. Currently, Henderson reckons all the packer sorting mentioned previously equates to a cost of around $15/head. That cost could be reduced significantly with more pre-harvest sorting.

**Working closer to the source**

In the meantime, the shifting consumer demand that led to product branding and required the additional sorting has fostered closer cooperation between packers and other industry segments.
That congressionally mandated LMMS report cited earlier explored the market effects of AMAs. According to the study, the term includes a variety of arrangements that establish an ongoing relationship for trading multiple lots of cattle to the packer, rather than negotiating the sale of single lots of cattle. In these arrangements, the seller agrees to deliver cattle to the packer at a future date, with the price generally being determined by some type of formula pricing mechanism.

Among the LMMS conclusions:

- “The beef producers and packers interviewed believed that some types of AMAs helped them manage their operations more efficiently, reduced risk, and improved beef quality. Feedlots identified cost savings of $1-$17/head from improved capacity utilization, more standardized feeding programs, and reduced financial commitments required to keep the feedlot at capacity. Packers identified cost savings of 40¢/head in reduced procurement cost. Both agreed that if packers could not own cattle, higher returns would be needed to attract other investors, and that beef quality would suffer in an all-commodity market place.

- “The producers surveyed that used AMAs identified the ability to buy/sell higher-quality cattle, improve supply management, and obtain better prices as the leading reasons for using AMAs.

- “The packers surveyed that used AMAs said that their top three reasons for using AMAs were to improve week-to-week supply management, secure higher-quality cattle, and allow for product branding in retail stores.

- “Regression analysis of the relationship between cash market (auction barns, dealers and brokers, and direct trade) transaction prices for fed cattle and use of marketing arrangements suggests that if capacity utilization within a plant increases through the use of AMAs, firms pay slightly less per pound for cattle purchased in the cash market.”

The bottom line, according to the independent study: “The cost savings and quality improvements associated with the use of AMAs outweigh the effect of potential oligopsony market power that AMAs may provide packers.”

Henderson points out: “These plants have operated at probably 80-85% of capacity for the past several years. My big concern over the next 18-24 months is who survives. If you lose some of these regional plants out of the heart of cattle country, what will that do to the rest of the industry?”

**Part 7: Distribution Sector - The “Middlemen” -- Retailers, Food Service Parcel & Peddle Beef**

Imagine a sea parceled out to hundreds of millions of consumers, who have instant access to the quantity they need and want, every day of the year at any time of day.

That’s basically what happens with beef every year, some 26 billion lbs. in 2011, according to USDA’s Economic Research Service (ERS). Beef production in 2011 was worth about $79 billion.

Every ounce of beef produced reaches domestic consumers through either retailers or food service operators. In turn, every ounce that leaves the packer and reaches retailers and foodservice providers must travel via a simple-appearing, yet extremely complex network of wholesalers, distributors and further processors.
Generally speaking, retailers and food service providers either buy directly from packers, from wholesalers/distributors who buy from packers, or from further processors. A further processor example is a company that buys trim to make and sell as ground beef, or a company that buys and cooks hamburger to create taco meat mix.

“Year to year, there’s about a 50% split between beef going to retail and beef going to food service,” says Trevor Amen, director of market intelligence for the National Cattlemen’s Beef Association (NCBA), contractor for the beef checkoff program.

Of the half going to food service, Amen explains about 65% is ground beef with the remainder being whole-muscle cuts. Of the half going to retail, about 50% is ground beef; the other 50% is marketed as fresh beef cuts.

These clear-cut avenues get shadowy in a hurry, though, because some companies serve multiple functions.

For example, Jim Henger, NCBA senior executive director of business-to-business marketing, explains many packers also own further-processing facilities.

Likewise, some of today’s largest retailers, such as Walmart and Costco, have their own divisions that serve the wholesale function, buying and warehousing a sea of beef, then parceling out the quantity and kind needed by various stores.

**BEEF Chat: Inside Costco**

You can buy everything from an emerald-cut diamond to a truckload of toilet paper at a Costco Wholesale warehouse store. If you’re among the bourgeois of American beef consumers, Costco is, by consensus, the place where you can always find a package of great steaks for tonight’s backyard barbeque.

While quality and value are the standard marketing modus operandi, don’t mistake your local member-driven Costco Wholesale for a discount store — certainly when it comes to a place to buy your beef.

Charlie Winters, vice president of Costco Wholesale’s fresh meat operations, got his start in the meat business working in a small, family owned slaughter facility in Aztec, NM. Winters, 56, pioneered Costco’s fresh meat department in 1987 at the Southcenter warehouse in Tukwila, WA. What began as a small selection of deli items and fresh meats serving Costco members in that south Puget Sound community is now one of the nation’s largest fresh meat retail programs.

Today, Costco sells about 150 million lbs. of ground beef annually; a little more than that in muscle meats. With beef making up 18-19% of Costco’s fresh meat sales on a value basis, Winter’s group, which includes Jeff Lyons, Chris Ostrander, Doug Holbrook and Teri Free, is one of the largest buyers of beef in the U.S.

**BEEF Chat With Charlie Winters**

**BEEF:** What’s the overall philosophy of Costco’s fresh meat program, specifically beef?

**Winters:** Our focus has always been product consistency. It takes diligence and discipline to deliver a quality product with consistency. When I first came here and started this program, we agreed quality would be the driving force behind the fresh meat program. That was supported by all the other Costco philosophies of managing a retail warehouse business.

**BEEF:** Beyond ground beef, your business is primarily in USDA Choice middle meats — the loins and steak meats. What’s the strategy behind USDA Choice?

**Winters:** USDA Choice is the only grade we offer our members. It fits with the profile of our customer base — higher-end shoppers who have more disposable income and for whom cost isn’t necessarily the only factor in their buying decisions.
Kirkland Signature is our private label. It's a name we've built over time and is well recognized among our members as a quality label, for a lot of different products. We're very exact in how we cut the beef in our warehouses so that every member gets the best possible eating experience.

**BEEF:** The hot issue the past few years with regard to beef has been food safety. What are your food safety initiatives today?

**Winters:** Food safety is a big part of our business; it has become part of our culture. We've established sanitation standard operating procedures and hazard analysis and critical control point programs over the past five years in every building.

We have a mandatory training and food safety/food code certification program for all employees — and an even more intensive training program for food managers.

Costco also audits all its vendors — and we accept outside food safety audits of their facilities. We're relentless about our buyers being inside the plants on an on-going basis.

Our seamless tracking system allows us to follow every pound of beef produced in our system to the supplier. Our ground beef program produces a half-million pounds each day, and we can effectively collect and analyze data on the microbiological quality of every single grind.

**BEEF:** How do things look from a supply standpoint?

**Winters:** Supplies are probably going to be tighter in the short-term. We use all the major U.S. packers and processors, and as the business changes we move from one vendor to another. Obviously, we need a good source of continuous supply, but, in general, supply and demand works very well.

All the proteins have to compete on a value basis, so we're probably going to see our beef volumes slow a bit as prices continue to escalate to cover those live cattle costs. Therefore, consumers may make other choices when prices get to a threshold they're uncomfortable with. I don't think supply will be a huge issue though.

**BEEF:** Regarding the new laws on country-of-origin labeling (COOL), what are the ramifications for Costco?

**Winters:** We're just now getting some meaningful information regarding that issue. I'm not sure anyone can prove it serves a great purpose and, at retail, we're still unclear as to what the final outcome will be — and how to do it. We're looking at a tracking system, how to verify country of origin and how to house the information that will be required of us.

In the end, we'll have to figure it out and deal with it. At this point, we don't have enough information to know what's going to be acceptable at the retail level.

**BEEF:** Will your members be willing to pay a premium for beef or pork labeled as born, raised and processed in the U.S.?

**Winters:** I don't think country of origin represents any value to the consumer. Our members aren't saying this is something important in their buying decisions. They're more focused on food safety and value — especially in these tougher economic times. They're more concerned about the ultimate eating experience — quality, consistency and value.

**BEEF:** The beef industry has changed a lot in the 15+ years Costco has been in the business. Are you concerned that consolidation in meatpacking is going to come around to haunt the retail sector?

**Winters:** With consolidation in the packing sector there's always uncertainty about who will be in charge of the supply. We're always looking for long-term relationships with vendors — and it really comes down to the individual relationships with the people in those companies. We're more concerned about who's going to end up with the largest piece of the pie — and whether we can depend on those long-term relationships.

Like every good buyer, we're never satisfied that we got the best deal at the lowest price. A new competitor is always welcome because it makes everybody sharper. I would hate to see more consolidation — it would not be to anyone's advantage; the producer or the consumer.

**BEEF:** How do you view what's going on in the ranching and feeding sectors?
**Winters:** The items we manufacture and sell in volume depend on consistency of supply from the cattle that are out there. If anything, we need to narrow the genetics as has been done in the pork industry to get more consistency in the live animal.

More information needs to be shared between the grower, feeder and packer about all the things that combine for profitability. That, in the end, translates into the best possible eating quality for the end-user. That said, the beef industry has to drive out some costs all the way through the chain. There are several profit centers in it that the pork or poultry complexes don't have. The beef industry has to get more efficient to compete with the other proteins.

**BEEF:** Some retailers are exploring alliances with packers, feeders and even cow-calf producers. Is this a concept Costco might buy into any time soon?

**Winters:** It's not even on the radar screen for us. We can get more involved as buyers as far as how products come to us — the specs and those kinds of things. But, as long as we're buying a certain product, there will be someone out there willing to make it available to us.

The way Costco has grown, we've created quite a demand and we try to get across to the beef industry that we're trying to build the business and that we have a vested interest in the beef industry. Give us some recognition for providing the red meat complex with the kind of high-quality format where we “feature” your best product 52 weeks out of the year.

**The Costco Profile**

Costco began operations in 1983 in Seattle, WA. In October 1993, Costco merged with The Price Company, which in 1976, pioneered the membership warehouse concept.

A publicly traded company, Costco's philosophy is to sell high-quality nationally branded merchandise, as well as its own private label. The business is based on high volume and rapid inventory turnover — offering a limited assortment of merchandise in a wide variety of product categories.

Headquartered in Issaquah, WA, the firm includes 411 membership warehouses in 36 states, Puerto Rico, Canada, Mexico, United Kingdom, Japan, South Korea and Taiwan, serving 38 million customers a day.

Costco is the seventh-largest U.S. retailer with sales in 2002 of $37.98 billion, is the fifth-largest food retailer, and has 100,000+ employees.

For purposes here, wholesale is defined as purchasing a large volume of beef and then selling and/or distributing it in smaller quantities and/or different varieties.

In the case of beef, trucks carry about 40,000 lbs. in a load, whether that weight is in live cattle, swinging carcasses, boxed primal or boxes of specific cuts of specific portion sizes.

“Wholesalers can buy full truckloads, get a cheaper price and maintain a fresh inventory,” Henger says. Conversely, he explains smaller-sized retailers and food service operators may not have the capital to deal in truckload quantities or enough business to turn enough volume to keep such a sizable inventory fresh.

For smaller retailers, wholesalers, like Supervalu and Associated Grocers, perform that same function. In food service, the largest wholesalers include the likes of Sysco Foods and U.S. Foodservice.

“Typically, wholesale used to be the step between the packer and the retailer,” Henger says. It still is, but he explains the line has grown almost invisible in some cases as large retailers take on the role themselves.

Incidentally, another reason the lines become murky is the simple fact that most of the data involved in figuring out who sells to whom is proprietary.

As an example, the beef checkoff funds research of beef volume and dollar sales within the retail and food service channels. For retail sales information, Amen says they rely on Freshlook Marketing retail
scanner data. For food service, they employ volumetric data through Technomic. Neither is fully reflective of every beef purchase or sale within the channels.

**Wholesalers are bigger, fewer**

The same consolidation and concentration that economics has driven in retailing has occurred in wholesaling, Henger says.

In an overview of the wholesaling sector from the ERS, analysts explain: “As consolidation in food retailing increases, manufacturers and large retailers offering a broad assortment of items have found it advantageous to negotiate directly with each other, reducing the power and influence of traditional wholesalers. Self-distribution is the preferred method of vertical coordination for large grocery chain stores (those with 11 or more stores). In 2001, 82% of chain stores were self-distributing.”

Some of the largest wholesalers are taking a similar integrated approach.

“Given uncertainty about the ability of independent retailers to compete with the larger chains, some of the largest grocery wholesalers are placing greater emphasis on owning retail operations,” ERS analysts say. “This is illustrated by Supervalu’s purchase of Albertsons in 2006, or the second-largest grocery wholesaler purchasing the third-largest grocery retailer.”

According to ERS, sales by the 20 largest food retailers in 2009 tallied $404.2 billion. That was about 64.2% of U.S. grocery store sales, compared to 39.2% in 1992.

**A Closer Look: It’s Not Your Grandmother’s Grocery Store**

I get excited when I get to hear from ya’ll because together – with the feeder, packer and retailer – we make an industry.”

That’s how Scott Nettles, senior perishables director with United Supermarkets in Lubbock, TX, opened his remarks at the Southwest Beef Symposium recently. Addressing a room of ranchers from West Texas and
New Mexico, Nettles gave producers a behind-the-counter glimpse of the beef business from a meat man’s perspective.

That chain from rancher to retailer makes a significant industry indeed. United Supermarkets is a regional chain with 52 stores in 30 Texas cities ranging from the Panhandle to Dallas. Total sales are around $1.5 billion annually and the meat market accounts for about $230 million of that. Of the total meat market sales, beef is the leader, accounting for a third of all sales. That means, he says, beef alone accounts for $75-$80 million in sales.

“Ground beef makes up 40% of all beef sales,” he says, but it’s not the largest. “The largest segment of my business is our Select program. We call it Genuine Texas Beef.” The product comes from cattle that were fed and processed in Texas. “It was a way to brand our Select program,” he says. “It improved our Select sales about 8-9% when we first kicked it off and it’s been really successful.”

Chef-to-Chef: 13 Trends for 2013

But he sees some signs in the numbers that cause him concern. “Sales (based on dollars) are up 4.8%, but our tonnage is down, and that’s alarming. As you all know, cost of beef continues to rise and it’s harder and harder to push more pounds of beef through the register. Sales look good, but when that tonnage number is down, that means people have left the beef counter and are moving over to the pork and chicken counter. And that’s not good for any of us. Any time you start messing with the big gun, that throws a red flag up to me,” Nettles says.

So United has added a wide range of products to appeal to about any customer niche including Choice, Natural and Prime programs, all Certified Angus Beef. Even though ground beef and Select make up the vast majority of sales, he says the fastest growing segment of the beef case is Natural. “The growth rate is over 100%, and we’re charging an average of $14/lb.”

However, what’s taken the brunt of that growth is not ground beef and Select, but organic and grass-fed. “Organic has kind of run its course,” he says. “I think they (customers) see natural as a competitive alternative. And grass-fed is losing share as well.”

Another Perspective: The Stanford Organic Food Study

And it’s not cost that is causing the shift. “We partner with Certified Angus Beef for our Prime program. And it’s interesting to me that our Prime sales are up 50%, tonnage is up 46%, and the average retail on the product is $20.50/lb. So price is not a deterrent.”

Industry challenges

Given the interconnectedness of the beef industry, challenges in every segment have implications up and down the marketing chain. “Our consumer sees beef as unhealthful and we as an industry, between us, still have to get the word out that beef is healthy.” United does that with a team of four dietitians who produce information on the nutritional attributes of all the products sold in the store, and especially beef.

“And guys don’t know how to cook, either. That’s why ground beef is such a huge part of our sales.”

A Closer Look: What’s Ahead For The U.S. Meat Business?

So it’s up to the meat department, working with their dietitians, to develop more value-added items. “To add spices, add seasonings, add traits to the meat so that you can just pop it in the oven. So we still have to do more work on our end to help you guys sell more beef.”

However, the thing that he wakes up every morning worrying about is E. coli. “We do a lot at the store level to educate our team members. Everybody in my department can tell you about cross-contamination, they can tell you cooking temperature for beef, they can tell you the correct way to stack the counter so you don’t cross-contaminate.” And they take extra pains behind to counter to sanitize knives, cutting
blocks and rags. “It’s a much different process today because of that one word – *E. coli* – than it was 20 years ago.”

But perhaps the biggest challenge he faces is the same one ranchers and feeders face as well – **cost**. “Beef cost to me is up over 10% from last year and we’re up 6% in retail price. So we’re fighting the same battles you guys do. We just do it on a different scale and in a different arena,” Nettles says.

“The nation’s 210,000 traditional food stores sold $548 billion of retail food and nonfood products in 2009,” say **ERS analysts**. “Grocery stores, including supermarkets, accounted for the largest share of food store sales (89.6%), followed by convenience stores without gasoline (6.4%).”

**Non-traditional retail stores** continue to account for more food-at-home sales, too. Think here of the cold cuts sold at the local drugstore, as an example. In 1999, non-traditional store’s share of food-at-home sales was 18.6%. It was 27.8% in 2009, according to ERS.

“Some wholesalers get bigger, buying smaller regional wholesalers,” Henger says. “One reason smaller wholesalers don’t make it is that they can’t afford new technology or to update facilities to compete with larger players.”

If you’ve ever had a chance to stand amid the automated, high-speed chaos of a packer’s boxed-beef distribution facility, then you have some idea of the seven-figure-plus investments required of modern, competitive inventory tracking and control, distribution and all the rest. The technology employed in these areas is truly mind-boggling.

**Food service is consolidating**

Unsurprisingly, food service distributors have grown more consolidated and concentrated in tandem with the sector they serve, too.

According to Amen, the top 500 food service chains comprise 65% of total restaurant sales today.

“To illustrate the growth of restaurant chain sales: the top 100 restaurant chains comprised 51% of total restaurant sales in 2001; by 2011, they were 58%,” Amen says. “Distributors have gained significant market share over the years. In 2005, the top nine distributors had 35% of total food service sales. By 2010, the top distributors reflected 46% of total food service sales.”

For perspective, giant food distributor **Sysco** cites $42.4 billion of sales in its 2012 annual report; $1.1 billion in net earnings.

In general, there are three types of food service distributors, **ERS** says:

- **Broadline food service distributors.** These are companies that traditionally purchase a wide range of food products from manufacturers and stock these goods in one of their distribution centers. Most broadline distributors offer value-added services designed to meet the needs of single-store restaurants and small chains. For instance, food service operators without the staff to research new products and plan menus may rely on a distributor’s sales representative for assistance.

- **Specialty distributors.** These are entities that don’t stock a wide range of products, but operate in niche markets where it’s necessary to have specialized knowledge about the type of product being handled or type of operator being served. For example, there are product specialists for specialty-cut meats, produce, ice cream and coffee. Market specialists serve a wide range of niche operators, such as convenience stores, hotels/motels, and club warehouses.

- **System distributors.** These are food service wholesalers that serve a customer base consisting mostly of chain restaurants with centralized purchasing and menu development. Individual operators within chains may not require the value-added services provided by a broadline or
specialty distributor, such as obtaining information about new products or assistance in developing and preparing new menu items.

Doing it right

Once a calf leaves the ranch, or a fed steer loads out of the feedlot, producers have no control over how the beef will be handled. By knowing more about the process, though, Henger says you have keener awareness of how vital everyone’s role is at each stage.

“It’s just so important that each step in the supply chain is done right. It’s critical that each one does their job right so the next one in line can concentrate on what they do,” Henger says. “Everyone relies on everyone else before them and after them to do the right thing.”

Part 8: Food Service Sector - Consolidation Is Driving Retail Change in Beef Merchandising

Amid the cacophony of the retail marketplace – partly due to, and in spite of, beef’s high price compared to competing proteins – beef remains an essential centerpiece of the retail meat case.

For one thing, beef’s high relative price means that it rings the cash register longer and louder than other meats. In fact, according to the Cattlemen’s Beef Board, beef accounted for more than 52% of the dollars spent for meat at retail in 2008.

By way of comparison, chicken accounted for 22% of the dollars spent on meat at retail. In that same year, beef accounted for 39.3% of the pounds of meat purchased at retail.

For another, consumers love beef. Though consumers traded down during the Great Recession, increasing their demand for ground beef and value cuts rather than middle meats, they appeared to trade away from beef entirely only as a last resort. In the last couple of years, beef demand has actually grown.

Moreover, retailers continue to use fresh beef as a point of differentiation between themselves and competitors. This differentiation can be based on such things as unit cost, consistency and quality, or stocking brands the competitor doesn’t.

“Beef is the largest category in all of HEB,” explains Mike Jarzombek, vice president of meat operations for HEB. The San Antonio-based company has 305 stores in Texas and 42 in Mexico. “It (beef) towers above grocery, pharmacy…everything. It’s over $700 million in annual sales.”

HEB offer nine lines of beef, from a value program aimed at its lowest-income shoppers, to premium lines like Prime and Wagyu. For more of Jarzombek’s thoughts, see “A Retailer Speaks On Beef, Consumers & The Future:”

When your job is to keep a $700-million slice of business growing, the heartburn factor can be pretty high. Just ask Mike Jarzombek.

He is vice president of meat operations for HEB, a San Antonio, TX-based grocery store chain that boasts 305 stores in Texas and 42 in Mexico, making it the largest privately held company in Texas and the 12th largest such company nationally. And as VP of meat operations, he’s responsible for the care and nourishment of HEB’s largest single business category.

“Beef is the largest category in all of HEB,” he told cattle feeders at the recent convention of the Texas Cattle Feeders Association. It towers above grocery, pharmacy…everything. “It’s over $700 million in
annual sales.” The stores offer nine different lines of beef, from its value program aimed at its lowest income shoppers, to premium lines like Prime and Wagyu aimed at the other end of the spectrum.

So what keeps him awake at night? Lots of things – maybe some of the same things that keep your brain and stomach both churning into the wee hours. Here’s his list, which he says is not inclusive and not in any particular order:

**Pathogens** – “When is the next big one going to hit? Hopefully never,” he says. “But when they do hit, it’s all hands on deck and we’re scrambling for a response – what are we going to say, what are we going to do, how are we going to assure the public that our meat supply is safe and it’s never been safer?” That’s a big deal, he says. “I think we’ve got to do more with educating our customers that the U.S. meat supply has never been safer.”

**Emerging pathogens and new regulations** – He’s not sure what the next big food safety regulatory issue will be, “but there’s a lot in the media about STECs; there’s a lot we hear from USDA about bench trim.”

STECs are shiga toxin-producing *E. coli*, which have been in the food safety crosshairs for a while. The possible new regulations designed to control STECs will further impact the beef industry. And bench trim has been part of the regulatory discussion as well.

**A Closer Look: STEC Pathogens Are A Food Safety Challenge**

Bench trim is what’s left over after steaks and other cuts are trimmed and prepared for retail packaging. Regulatory officials are taking a hard look at whether or not bench trim should continue to be added into the grind to produce ground beef, or whether it should be discarded as a food safety effort. For Jarzombek, that’s an issue. “We’re one of the few retailers still cutting meat,” he says.

**Media and social media** – Jarzombek jokes that when things hit, he talks to everyone else more than he talks to his wife. Using the recent lean finely textured beef debacle as an example, he says not only was the media calling him within hours after it blew up, but so was the company’s e-mail, Twitter, and Facebook accounts, plus old-fashioned phone calls from customers were pouring in. “People were calling me left and right – what are we doing, what’s HEB’s stance? It was incredible.”

In that instance, both media and social media combined to bring down a previously viable business and put around 650 people out of work. “So you can see the impact media and social media can have on our business, good and bad. We’ve got to be prepared in an even bigger way than we ever have been,” he says, to respond positively and quickly.

**Animal welfare** – “I used to get lots of questions about the price of meat, tenderness, variety or selection. Today, it’s about pathogens, it’s about animal welfare.” And the questions are specific and pointed. He says animal welfare and food safety questions are media-driven, but they’re real and his customers want to know what’s being done in those areas.

And, he says, while most of the attention has been focused on pork and poultry production, cattlemen shouldn’t get complacent. “Eventually somebody is going to be targeted. Animal welfare is a big deal. I’m sure all of you keep that near and dear to your hearts, but we’ve got to be prepared.”

**COOL** – “From where I sit, COOL (country of origin labeling) doesn’t mean a whole lot to our customers,” he says. That’s because they find the COOL labels confusing. And as a retailer, Jarzombek spent the GNP of a small country developing a computerized-tracing system to ensure HEB stays in compliance with the labeling requirements.

“We had to build a system to be able to trace this stuff every day in our stores. And with over 300 stores, you can’t do that with a Big Chief tablet and a pencil,” he quips. “Those of you who know anything about computers, it’s seven figures anytime you tell them to build a system.”

**Supplier financial health and industry consolidation** – “Believe it or not, we talk about you guys daily. We talk about the cow-calf guys, we talk about the feeders, we talk about the packers – how you’re doing, how you’re faring. And I know it’s tough right now, particularly with the cost of corn. But we’re concerned about that.”

**Tight supply** – “This worries me,” he says. HEB produces an ad every week of the year, and beef is featured in every ad. “In terms of supply, hopefully we’re going to be able to find the supplies we need,”
he says. “When we feature something on an ad, it’s multiple truckloads. So that could affect our business, depending on what’s available. I’m concerned about where costs are going in 2013.”

High costs—His concern about the effect tight supply is having on retail prices has already come to fruition. “Some of our customers are shifting away from beef. So what are we doing about that?”

A number of things, he says. “We have to change how we fabricate. We’ve got to do more muscle harvesting.” For example, consider a bone-in chuck roast. “Three years ago, that roast was $8. Today, it’s double that.”

Many of HEB’s customers simply can’t afford to plunk that much money down on a single piece of beef. “So we’re going to harvest muscles off that. We’re going to remove the muscles off the top blade and put out smaller portions.”

Jarzombek grew up in a family not unlike many of the people who now shop in his meat department. “We didn’t have a lot of money and there were five people in the family. And Mom always had five pieces of meat on the plate. They weren’t big pieces of meat, but there were always five pieces of meat.”

So that means, in addition to changing how cuts are harvested, that changes are needed in how they’re packaged. “We’ve got to focus more on unit price, keeping it affordable. It’s about lowering the unit price and selling through, because we can’t sell monster chucks anymore.”

Value-added cuts—For other customers, time and ease of preparation are conveniences that have moved into the “needs” category. “There are more two-party working households, so we’ve got to do more with that,” he says. HEB recently launched beef cuts that come in a bag, complete with seasoning and gravy. “It’s raw and all you do is put it in the oven when you get home. We’ve got tons of items like that and we’re going to be doing much, much more to try to please the customer.”

Customer education—Drawing a circle back to his first point, Jarzombek says HEB has a service called Cooking Connection in stores. “These are large stations that are staffed by chefs. Basically what they do is train people how to cook.”

Beyond that, however, he says the stations can become a hub of food safety and nutrition education as well. “We’ve got to do more with education, not just how to cook, but the health values of eating beef,” he says. “We have a lot of customers switching to ground turkey because they think it’s leaner. I say buy the 96% ground beef. It’s just as healthy for you, if not healthier. So we have a lot of work to do as retailers to educate our customers.”

Retailing is a competitive, tough business. “We’ve got to use innovation and we’ve got to use technology, not just to create things, but to find ways to get cost out of our business,” he says. “We’ve got to eliminate those things that don’t matter to the customer.”

And then proactively address the things that do matter to the customer. “We’re all in this together,” he says. “I know you know that, but I want you to know that we realize that, too. And we’re going to do everything we can to keep this business very healthy and thriving going forward.”
Consolidation drives retail change

The retail landscape changed dramatically during the last few decades, with massive consolidation on one hand, and non-traditional retailers entering the fray on the other. Both have taken market share from traditional independent grocers. See “Who Sells Beef?” for definitions of different retailer types.

Consolidation in the grocery business took flight in earnest during the 1990s, spawned by mergers and acquisitions. Think here of Supervalu – then the nation’s eighth-largest retailer – acquiring 1,124 Albertson’s Supermarkets in 2006 and becoming the fourth-largest retailer by 2009.

A Closer Look: Who Sells Beef? We Explain

The Traditional Grocers

**Traditional supermarket** – Supermarkets offering a full line of groceries, meat and produce with at least $2 million in annual sales and up to 15% of their sales in general merchandise/health and beauty care (GM/HBC). These stores typically carry 15,000-60,000 SKU and may offer a service deli, a service bakery, and/or a pharmacy.

**Fresh format** – Fresh stores emphasize perishables and offer center-store assortments that differ from those of traditional retailers – especially in the areas of ethnic, natural and organic.

**Superstore** – A supermarket with at least 30,000 sq. ft. that generates $12 million or more/year and offers an expanded selection of non-food items. Specialty departments and extensive services also are offered.

**Warehouse store** – Grocery stores with limited service that eliminate frills and concentrate on price appeal; items may be displayed in their original shipping cartons rather than placed individually on shelves. Stores may also sell bulk food and large size items.

**Super warehouse** – A high-volume hybrid of a large traditional supermarket and a warehouse store. Super warehouse stores typically offer a full range of service departments, quality perishables and reduced prices.

**Limited-assortment store** – A low-priced grocery store that offers a limited assortment of center-store and perishable items (fewer than 2,000).

**Other** – The small corner grocery store that carries a limited selection of staples and other convenience goods. These stores generate approximately $1 million in business annually.

Non-traditional Grocers

**Wholesale club** – Membership retail/wholesale hybrids with varied selection and limited variety of products presented in a warehouse-type environment. These 120,000-sq.-ft. stores have 60%-70%...
GM/HBC and a grocery line dedicated to large sizes and bulk sales. Memberships include both business accounts and consumer groups.

**Supercenters** – A hybrid of a large traditional supermarket and a mass merchandiser, supercenters offer a wide variety of food, as well as non-food merchandise. These stores average more than 170,000 sq. ft. and typically devote as much as 40% of the space to grocery items.

**Dollar store** – A small-store format that traditionally sold staples and knickknacks. Now, sales of food and consumable items at aggressive price points account for at least 20%, and up to 66%, of their volume.

**Drug store** – A prescription-based drug store that generates 20% or more of its total sales from consumables, general merchandise, and seasonal items.

**Mass merchandiser** – A large store selling primarily hard lines, clothing, electronics and sporting goods, but also carrying grocery and non-edible grocery items.

**Military commissary** – A format that looks like a conventional grocery store carrying groceries and consumables, but is restricted to use by active or retired military personnel.

*Source: Food Marketing Institute, Supermarket Facts, Store Format Definitions*

Emergence of non-traditional grocers – primarily warehouse clubs and giant general merchandise stores, such as Costco, Super Target and Walmart Supercenters – was the other catalyst.

“Sales by the 20 largest food retailers totaled $404.2 billion in 2009, amounting to 64.2% of U.S. grocery store sales, an increase from 39.2% in 1992,” say analysts from USDA’s Economic Research Service (ERS) in their Retail Trends report. “Although shares held by the largest four, eight, and 20 supermarket and supercenter retailers decreased slightly from 2008 to 2009, the longer-term trend shows an increasing concentration of sales among the nation’s largest grocery retailers.”

One contributing factor to such increases over the past decade has been the rapid growth of Walmart Supercenters. Its food and non-food grocery sales amounted to an estimated $103.7 billion in 2009, making it the largest U.S. retailer of grocery products. In comparison, second-place Kroger, the largest traditional grocery retailer, had sales of $65.6 billion in 2009.

For perspective, according to the Food Marketing Institute, there were 36,569 supermarkets in 2011 with annual sales of $2 million or more. Total supermarket sales that year were $584.369 billion.

More specifically, the folks at ERS say there were 210,000 traditional food stores in 2009 that sold $548 billion worth of food and non-food products. They point out that traditional grocery retailers experienced negative inflation-adjusted growth through the Great Recession.

“During the past decade, there were many years in which grocery store sales growth (in current dollars) exceeded the rate of inflation. Inflation-adjusted sales growth was small, averaging 0.07%,” ERS analysts say. “The slow and negative inflation-adjusted growth in annual sales at traditional grocery stores was likely due in part to increased competition from nontraditional food retailers – such as warehouse clubs, supercenters, drugstores, and other retailers, as more consumers economized on food spending.”

According to ERS, you can chalk up most food sales growth between 1999 and 2009 to supercenters and warehouse club stores; their sales more than doubled in that time span.

“Since the late 1990s, nontraditional retailers have steadily increased their relative share of food-at-home sales, compared with traditional retailers,” ERS analysts explain. “Nontraditional stores’ share of food-at-home sales increased from 18.6% in 1999, to 27.8% in 2009.

“In response to the sales inroads made by nontraditional retailers, traditional grocers are expanding the number and types of product offerings, designing new store formats, and using innovative in-store technologies,” say the ERS folks.
Now, increased consumer interest in knowing more about their fresh foods is driving more interest in locally grown foods.

“Supermarkets have responded by emphasizing local offerings such as fresh fruits and vegetables, baked goods, meat, poultry and dairy products, depending on the location and time of year,” ERS analysts say. “Safeway, Kroger, Food Lion, and HEB Grocery Company are some of the largest supermarket chains that promote a variety of locally grown or produced foods. Other sources of local food include farm-direct and farmers’ markets. While many local foods are promoted as organic or natural, retailers often claim that local foods support local agriculture and are more environmentally friendly.”

Part 9: Restaurant Sector – Time & Money Drive the Retailing of Beef Products

Beef Magazine 5/6/13

Some of us of a certain vintage can remember when going to the new McDonald’s franchise a couple of towns away was a big deal; it was a destination treat when a celebration or extra cash was on hand.

These days, of course, whipping through the drive-through of a fast-food restaurant is typically as special as deciding between toast and cereal for breakfast.

By 2011, according to the USDA’s Economic Research Service (ERS) Retail Trends, consumer food-away-from-home spending accounted for 48.7% of all food spending, up from 47.1% in 2000 and 43% in 1990 (Table 1).

Of that spending, full-service restaurants (FSR) and limited-service restaurants (LSR, such as fast food) account for upward of 75% of all food-away-from-home spending (Table 2). Other food service players included institutional food service operators in schools, hotels, nursing homes, recreational facilities and the like.

As for beef specifically, according to the Cattlemen’s Beef Board, beef remains the number-one protein served in restaurants. LSRs accounted for more than 43% of all beef served in commercial restaurants in 2008.

Changing U.S. households

Prior to the Great Recession, ERS analysts say, “…the share of household expenditures for prepared foods and meals had risen due to changes in household composition – such as more single-person households and more households with two working adults – as well as increased household incomes and changes in consumer preferences for convenience foods.”

For perspective, ERS analysts note in Let’s Eat Out: Americans Weigh Taste, Convenience, and Nutrition, that: “Traditional families, defined as a married couple with children, accounted for 30% of all households in 1980 ... they totaled only 24% of all households in 2000 and may further decrease in share to about 17% by 2020. By contrast, single-person households increased from 23% of all households in 1980 to 26% in 2000, and may reach 29% in 2020.”

Even a decade ago, ERS analysts noted in The Demand for Food Away from Home: Full Service or Fast Food? that: “U.S. households are becoming, on average, richer, older, smaller, more ethnically diverse,
and more likely to contain single people or multiple adults without live-at-home children. These changes each have foreseeable impacts on the demand for food away from home, the subsequent offerings of food service establishments, and ultimately the diet and health of all those going out to eat.”

Whatever the reasons, ERS analysts note, “Whether eating out or buying carry-out, Americans are consuming more and more of their calories from full-service and fast-food restaurants. The share of daily caloric intake from food eaten away from home increased from 18% to 32% between the late 1970s and the middle 1990s, according to USDA’s food-intake surveys (1977-78 and 1994-96) …”

Consumers seek increased value

LSRs enjoyed greater growth than FSRs for decades as they established more locations, often closer and more convenient to consumers; and, at times, in non-traditional food retail locations.

But, FSRs appear to be gaining more traction as consumers look for more value amid the menu of convenience, quality, price entertainment and overall dining experience.

In response, ERS analysts say, “… some fast-food restaurants are now offering more of the variety of items and heightened amenities typically associated with full-service establishments …” But, they add, “Both FSRs and LSRs are increasing the variety of foods and services available to their customers.”

Aside from a cacophony of new menu items, think about everything from electronic self-order kiosks to table-top television, and the equipment in the kiddie playground.

“Although many factors could be contributing to the evolution of the food service industry, a sustained shift in consumer demand appears to be the primary force,” ERS analysts say. “A change in demand can alter the competitive dynamics of a market. If consumer demand is shifting in favor of the foods and services traditionally offered by FSRs, then FSR companies will be encouraged to operate more outlets offering more variety and dining amenities. Fast-food restaurants (LSRs) might also introduce many of these same foods and services themselves …”

Fulfilling consumer demand has grown more costly and precarious as the nation’s unemployment rate increased and consumer incomes decreased through the Great Recession and the nascent recovery.

On the one hand, the National Restaurant Association (NRA) expects wholesale food costs to continue on an upward trajectory through 2013, putting significant pressure on restaurants’ bottom lines as about one-third of sales in a restaurant goes to food and beverage purchases.
On the other, folks at the NRA point out that there’s a strong correlation between restaurant sales and consumer disposable income.

Then there’s health care and the threat of higher costs with reform.

According to NRA, one-third of a typical restaurant’s sales go toward labor costs, so significant increases in those costs will result in additional cost management measures to preserve the slim pretax profit margins of 3-5% on which most restaurants operate.

“Despite a continued challenging operating environment, the restaurant industry remains a strong driver in the nation’s economy,” says Dawn Sweeney, NRA president and CEO.

According to NRA’s 2013 Restaurant Industry Forecast, total restaurant industry sales are expected to exceed $660 billion in 2013 – that is a 3.8% increase over 2012. It would be the fourth consecutive year of real sales growth for the industry.

“The fact that the restaurant industry will continue to grow in an operating environment that presents substantial challenges is a testament to the essential role that restaurants play in our daily lives,” says Hudson Riehle, NRA senior vice president of research and knowledge. “Restaurants are offering products and services that consumers actively seek out and enjoy.” He adds that even with cash constraints, consumers seek to eat out because doing so has become an important component of their lifestyle.

**Restaurant trends**

Local sourcing and nutrition are among the strongest consumer trends for 2013.

According to survey research from the National Restaurant Association (NRA), more than seven of 10 consumers say they’re more likely to visit a restaurant that offers locally produced menu items, and more than six out of 10 said locally sourced menus are a key attribute for choosing a restaurant.

Currently, a majority of table-service restaurants offer locally sourced produce, meat or seafood. Such availability is highest in the fine dining segment.

As for nutrition, more than seven out of 10 consumers in the NRA research say they are trying to eat healthier at restaurants now than two years ago – and women more so than men (75% vs. 66%). About three-quarters of consumers say healthy menu options are an important factor when choosing a restaurant (80% of women vs. 71% of men).

And restaurants appear to be responding to this increasing demand for nutritious options. In fact, 86% of consumers say restaurants are offering a wider variety now than two years ago.
There Are More Consumers Today, And They're More Diverse

Buckle up. The road of consumer change is fixing to get winding and the grade, steep.

“The next half-century marks key points in continuing trends,” says Thomas L. Mesenbourg, acting director of the U.S. Census Bureau (USCB). “The U.S. will become a plurality nation, where the non-Hispanic white population remains the largest single group, but no group is in the majority.”

The U.S. is projected to become a majority-minority nation for the first time in 2043. Minorities represent 37% of the U.S. population currently, but are projected to comprise 57% of the population in 2060.

In December 2012, USCB estimated the U.S. population at 314 million; it pegs the population in 2050 at 399.8 million. Though significantly less than the agency’s previous quadrennial projections, it still represents an increase of 27.3% in fewer than four decades.

According to USCB, the population is projected to grow more slowly over the next several decades than previously estimated, due to lower projected levels of births and net international migration.

Incidentally, the U.S. population represents approximately 4.5% of the world’s population today.

Melting pot continues to thicken

The non-Hispanic white population in the U.S. is projected to peak at 199.6 million in 2024, up from 197.8 million in 2012. Unlike other race or ethnic groups, however, it is projected to slowly decrease, falling by nearly 20.6 million from 2024 to 2060.

Meanwhile, the aforementioned Hispanic population is projected to more than double, from 53.3 million in 2012 to 128.8 million in 2060. If this is correct, by 2060, nearly one in three U.S. residents would be Hispanic, up from one in six today.

The black population is expected to increase from 41.2 million to 61.8 million over the same period. Its share of the total population would rise slightly, from 13.1% in 2012 to 14.7% in 2060.

Meanwhile, the Asian population is projected to more than double, from 15.9 million in 2012 to 34.4 million in 2060, growing from 5.1% of the U.S. population today to 8.2% by 2060.

Moreover, the ethnic and racial lines are getting blurred.

“Once a mainly biracial society with a large white majority and relatively small black minority — and an impenetrable color line dividing these groups — the U.S. is now a society composed of multiple racial and ethnic groups,” say authors of the 2011 Congressional Research Service report, The Changing Demographic Profile of the United States. “Along with increased immigration are rises in the rates of racial/ethnic intermarriage, which in turn have led to a sizable and growing multiracial population. These trends are projected to continue for the next decades.”

Millennials poised to drive

The U.S. population is growing older as it becomes more ethnically blended.

Baby boomers (born between 1946 and 1964) have long been the leading market target. They numbered 76.4 million in 2012 — about 25% of the total population.
The population aged 65 and older is expected to more than double between 2012 and 2060, from 43.1 million to 92.0 million. According to USCB, the older population would represent just over one in five U.S. residents by the end of the period, up from one in seven today.

According to beef checkoff-funded research, the marketplace is fractured into three major generational cohorts: baby boomers, generation X (which followed the boomers) and millennials (born 1980-2000). At 80 million, millennials outnumber boomers and are set to carry the mightiest market stick.

That’s why millennials are a research priority for the beef industry.

Checkoff-funded studies in late 2011 and 2012 revealed that, although this generation enjoys beef, some issues hinder their consumption of it.

For one, Wendy Neuman, director of market research at the National Cattlemen’s Beef Association (NCBA), a contractor to the beef checkoff, says millennials have little experience with shopping for beef, or preparing it once they get it back home. They recognize beef’s nutritional benefits, but don’t necessarily know the appropriate number of servings, or understand how beef fits in a healthy diet and active lifestyle.

Millennials view food as a route to diverse cultural and social experiences. But, 54% of them say it’s hard to know which cuts to choose in the meat case. In part, because of their lack of experience preparing beef, 56% reported disappointment in the results when cooking hamburgers (compared to 31% of boomers); and 55% are disappointed when they cook steak (compared to 40% of boomers). Flavor drives the disappointment for burgers. Tenderness is the reason for steak disappointment.

The good news is that millennials are knowledge seekers. In the research, 75% said they wanted information about steaks, and how to prepare and cook them; 55% wanted information on preparing and serving beef to their children.

Millennials tend to buy the same cuts rather than diversify their choices, too. However, 50% said they would buy more beef if they knew more about the different cuts.

One startling find in the 2011 research was that millennial parents are limiting their children’s consumption of beef. Besides being the key consumer group of the future, these millennials will influence the following generation.

The checkoff-funded “Millennial Parent” study last year asked why millennials limit beef in their children’s diets. One reason is they perceive chicken as being easier to prepare. Plus, kids prefer the taste of chicken (including strips and nuggets), and it can be served in a wide variety of ways.

Millennial parents also perceive other meats as more heart-healthy than red meat.

Strategies need to evolve

Rick McCarty, NCBA vice president of issue analysis and strategy, and John Lundeen, NCBA senior executive director of market research, summarized some megatrends that will affect the beef industry in coming years.

• **New, sometimes smaller packaging**: “Households composed of 1 to 2 persons now represent 62% of total households. In addition, some families are now eating more à la carte meals,” the duo says. “Retailers are going to need several merchandising options as they reach out to these consumers.”

  Checkoff-funded research indicates strong consumer interest in packages of small, 4-5-oz., expertly trimmed steaks in the meat case, as well as on the restaurant menu.
Market research also indicates that beef’s subpar performance in the microwave is a limiter to beef consumption.

- **Ethnic shifts change the landscape:** “Not only will tastes shift, but the beef industry must be able to satisfy increasingly diverse consumer palates,” McCarty and Lundeen say. “This will create an explosion of taste options to enjoy, particularly for millennials, who embrace ethnic flavors to a much greater degree than older segments of the population.”

- **Technology aids decision-making:** According to McCarty and Lundeen, research indicates millennials are much more likely than other consumers to use a “shopping app” at the supermarket — an app that tells them, for example, what’s on sale and where to find certain foods in the store, and provides recipes and suggest ingredients.

- **More product, consumer targeting:** “The beef industry has come up with several new beef cuts [Denver Cut, Flat Iron Steak, etc.] that have helped make steak-eating more affordable, and increased the value of the carcass to the beef industry,” Lundeen and McCarty say. “Today, half of U.S. households are low- to moderate-income households, and these consumers are typically higher-frequency beef eaters. Innovation is needed to find affordable beef options for all income levels...”

- **More convenient beef products:** “Nearly one-third of consumers believe that 40 minutes is too long to wait for their meals, from start to table, and 70% say an hour is too long. Add to that the fact that 70% of women now are working — it’s easy to see that convenience is critical,” McCarty and Lundeen explain. “While ground beef has been the fallback product for the time-conscious, more convenient whole-muscle cuts, including microwaveable roasts, could boost demand. So, too, could easy beef options that quickly assemble into one-pot meals, an increasingly popular choice,” they add.

- **“Trust me” is more than a slogan:** “Wall Street scandals, political scandals, product recalls, pyramid schemes, economic meltdowns, corporate layoffs ... it’s no wonder consumers today have become cynical,” McCarty and Lundeen say. “How does the industry develop a trusting dialogue with those who are pessimistic but love our product? Connecting with consumers involves creating trust in how beef is produced, and assurance that beef is a safe, wholesome, and sustainable food. Consumers, indeed all stakeholders, are demanding more transparency regarding how food is produced.”