

April 29, 2020

COVID-19 Retail and Feature Activity Report

The dynamic of the food commodities' industry has changed dramatically over the last 8 weeks and will continue to change in the near, medium, and possibly long term. With the foodservice sector significantly shrunk, demand has naturally shifted from restaurants to grocery stores, causing price volatility during and after the first few weeks of the "Great Lockdown." Such situations have been true with all market shocks over the years, but none of them have experienced such a persistent strong demand (and inelastic demand, to a degree) in the retail sector combined with an overnight shutdown of the foodservice sector. Therefore, we believe that price volatility will persist in the wholesale trading sector due to numerous factors, later to be discussed, where retailers will not only play a significant role in channeling this shifted consumer demand from foodservice to retail, but also in absorbing price shocks at the wholesale level—all of this while still offering consumers affordable protein products, particularly in times of hardship for many Americans.

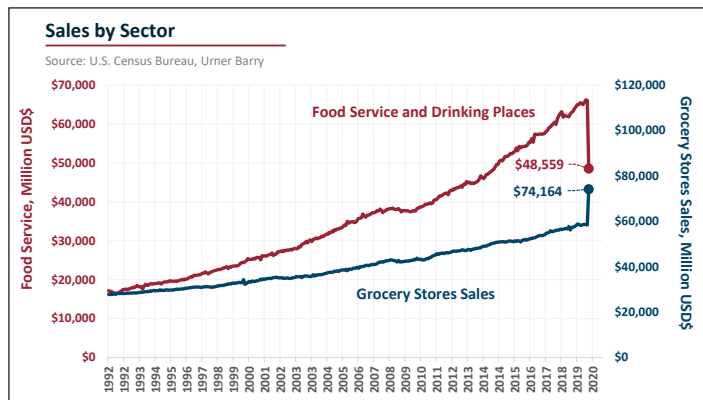


Figure 1. Advance Retail Sales by Sector, U.S. Census Bureau.

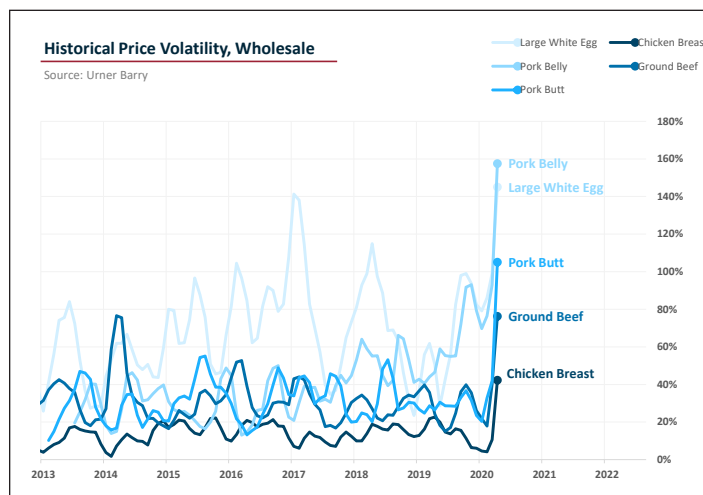


Figure 2. Historical weekly price volatility, monthly average, wholesale; Urner Barry.

To achieve this, items traditionally sold to the foodservice sector could possibly become more commonly offered at grocery stores. Stringent product specifications at the retail level will have to

become less strict for these products to be sold and offered to the consumer. For instance, 30-egg trays of small or loose graded eggs, which traditionally trade in the foodservice sector, are now making their way to the retail case. Some reasonable regulations will also have to be relaxed, such as providing temporary flexibility to nutrition labeling for certain packaged foods, among others. But more importantly, this means that retailers will be forced to get creative with their retail features to promote items purchased at the wholesale level at vastly different prices. During the initial weeks of the demand rush at grocery stores following stay-at-home directives, consumers purchased lower-priced items like eggs, chicken, and ground beef. As a result, retailers were replacing these products at rising prices week-to-week despite near-record high meat and egg production. However, it would be complicated to offer all the different cuts and parts of a 900-pound beef carcass at the retail case. For example, while a number of skirt steaks and beef tenderloins are offered at retail, these cuts are predominantly sold to the foodservice sector. During the first weeks of the lockdown, prices of these items declined steeply while lower-priced items like ground beef sky-rocketed.

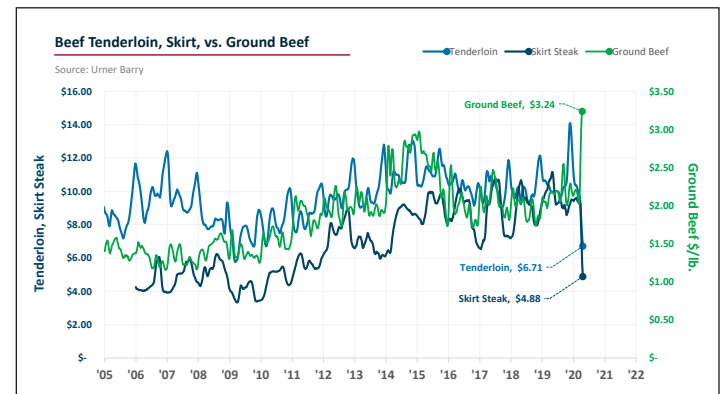


Figure 3. Four-week moving average of wholesale prices for 189A 4 Loin, Tenderloin, PSMO, CH; 121C Outside Skirt, Peeled Choice & Select; and 136 Coarse Ground Beef 81%, Urner Barry.

Prices across a wide variety of animal protein commodities have experienced record-high levels, as well as multi-decade lows in about a 6-8-week time period. While there was a time during the initial weeks of the Great Lockdown where traders were worried about mounting inventories of lean beef trimmings and pork bellies, those concerns essentially vanished a few weeks later. Processing plant closures and reduced slaughter schedules as a result of COVID-19 cases among plant workers are now a reality to contend with and will continue to reduce processing capacity across the country—impacting meat supplies at least in the near term. If incomes decrease, will consumers eat less meat as they trade down? Will unemployment and stimulus checks change protein consumption habits even if incomes are similar to those prior to the Great Lockdown?

We will try to answer some of the questions that have arisen during these unusual times through the lens of retail feature ads and wholesale prices.

EGGS

Eggs are in a world of their own. Since there are few substitutes, if any, demand for this item is relatively inelastic. Pricing for eggs has experienced multiple market shocks over the years, some supply driven like in 2015 with avian influenza, and others demand driven, like during snowstorms when buyers rush to the stores for eggs, milk and bread. Though the situation during the Great Lockdown is, in essence, no different from the latter, the data available is quite revealing.

Prior to the Great Lockdown, wholesale prices for Large White Eggs (Midwest) were relatively low amidst near-record production levels. Since Urner Barry began reporting retail features in 2012, we found a moderate negative correlation between wholesale prices (UB price) and the amount of retail features. In other words, if prices at the wholesale level of Large White Eggs increased over a certain threshold, the number of features would decrease. Sometimes the lag would vary between 3 to 6 weeks; in the case of the Great Lockdown, the reaction took only 2 weeks. Here, we saw a record low number of feature ads, a record-high price at the wholesale level, and the 2nd highest feature ad price.

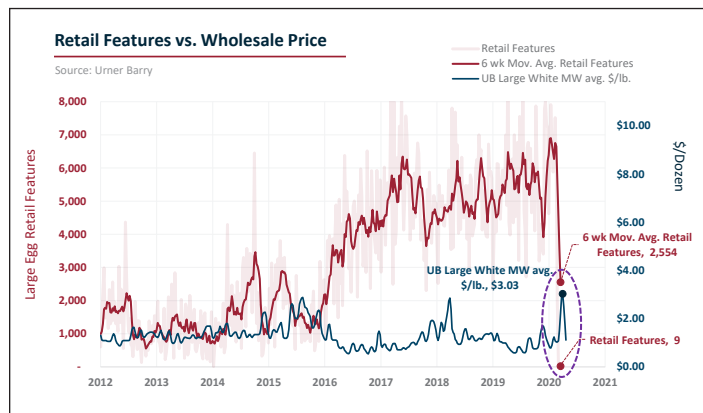


Figure 4. Left axis: Retail feature ads for large eggs, national level—current data, and 6 week moving average through April 22nd, 2020. Right axis, Urner Barry's large white Mid-West quote.

What is interesting to note is that while prices at the wholesale level have since come down to pre-Great Lockdown levels, as have retail feature ad prices, retail feature volume still remains low. The chart below shows that the drop in retail features is not a seasonal occurrence, features fell two weeks prior to Easter and have remained hovering at record-lows for three straight weeks.

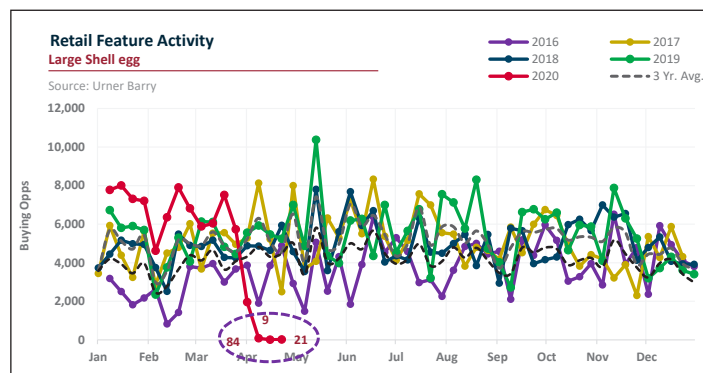


Figure 5. Retail Feature Ads for Large Eggs displayed cyclically. Urner Barry's Retail Features.

Finally, the number of cases of shell eggs broken for further processing (which is one indicator that we have found to be much more closely correlated to wholesale prices than any other) also fell to multi-year lows. These eggs go into production of liquid eggs first, largely destined for the foodservice sector. Therefore, it is crucial to mention that the decrease in this case, this indicator's behavior is now influenced by a combination of not only a high demand at the retail sector, but also a dramatic decrease in demand for liquid eggs in the foodservice sector.

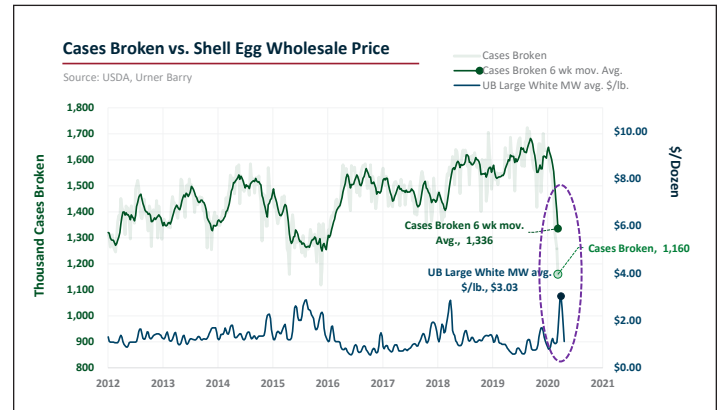


Figure 6. Wholesale prices using UB large mid-west quote vs. USDA volume of cases broken.

Our initial thoughts are that there is no real need to promote Large White Eggs when there is constant and consistent traffic/demand at retail stores all over the country—yet, retail ads for items traditionally sold at the foodservice sector could increase. This means that the egg retail case will now be shared between small, medium, loose grade, eggs with the traditionally showcased white, X-large, and brown shell eggs. In the meantime, regular prices—not featured prices—for eggs have moved up considerably in tandem with the wholesale prices.

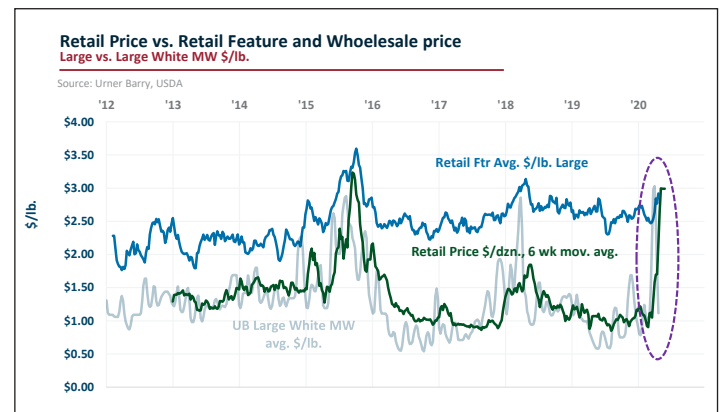


Figure 7. USDA Retail Price, 6 wk. moving average, Urner Barry's retail feature average price, and Urner Barry's Large Midwest quote.

BEEF

Beef's turmoil has been somewhat contained in terms of prices. As the largest animal with hundreds of different cuts, the beef carcass cutout—an integration of values relative to the weight of each—has not seen as much volatility as eggs have. However, the volatility of individual cuts relative to each other has been unprecedented. As shown in figure 3, the main item in very high demand has been ground beef. Similar to eggs, ground beef is perceived as a value item by the consumer. With a retail feature price oscillating around \$4.00 per pound, ground beef is an affordable staple across animal proteins. At the wholesale level, regular 81% lean coarse ground beef, which is mainly destined for retail, has skyrocketed in price to a record level, while feature ads for ground beef have plummeted to the lowest level since we began collecting this series in January 2012.

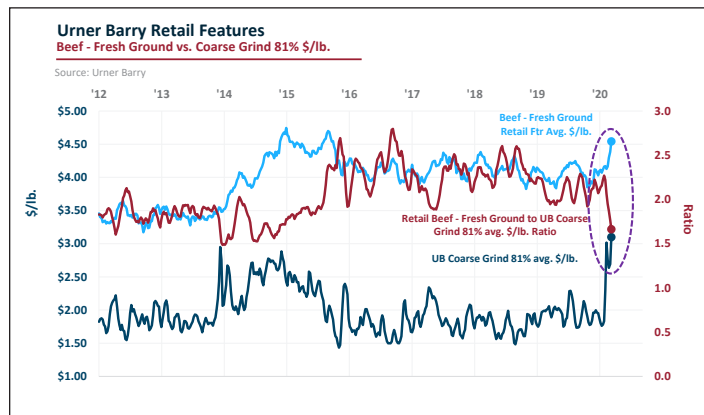


Figure 8. Urner Barry's Retail avg. price for ground beef, and Urner Barry's 81% coarse ground beef wholesale quote; the red line depicts the ratio between the two over time.

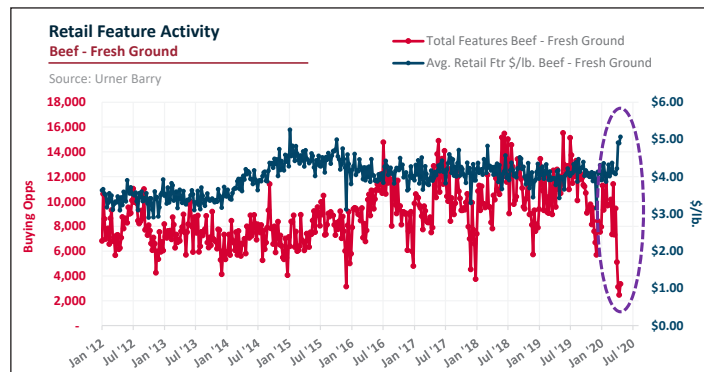


Figure 9. Retail Feature Activity vs. Retail Feature Avg. Price for all fresh ground beef. Urner Barry.

It is important to also consider that beef trimmings represent a significant amount of the beef cutout; in other words, trimmings represent a large portion of the yield of the carcass. So, in theory, a large upward swing in prices could offset steep losses seen in smaller portions of the carcass that are deemed “more valuable.” As such, despite massive losses for tenderloins, skirts, and ribeyes in late March and early April, cutout values reached record highs in mid and late April. In addition, demand at QSR (fast food) establishments strengthened as drive-thru windows remain open. This means that ground beef still has a large alternative channel to move product into aside from grocery

stores. And even though the foodservice sector has shrunk considerably it does not mean that beef consumption would go down by the same proportion. Beef consumption—and for that matter meat consumption—was sitting at a record high prior to the Great Lockdown.

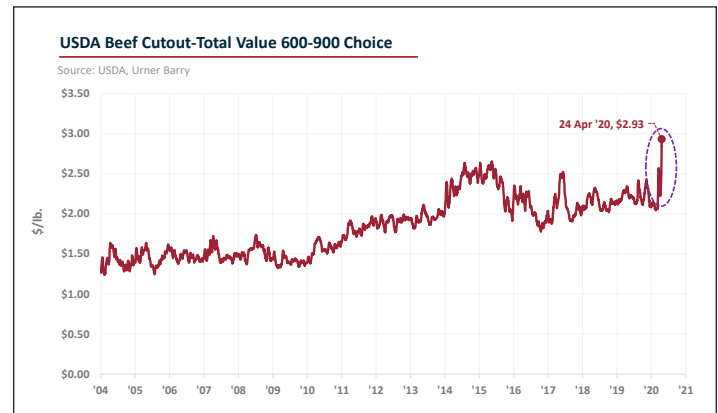


Figure 10. Choice 600-900 Carcass Cutout, USDA, Urner Barry.

This situation has also spurred demand for lean end cuts like chucks and rounds to grinders in order to process more ground beef. This has largely contributed to the strength of the cutout and has been passed on to the retail case. The roast feature category, comprised mainly of rounds, chucks and shoulders/clods, have seen significant declines in feature activity and increases in average feature price.

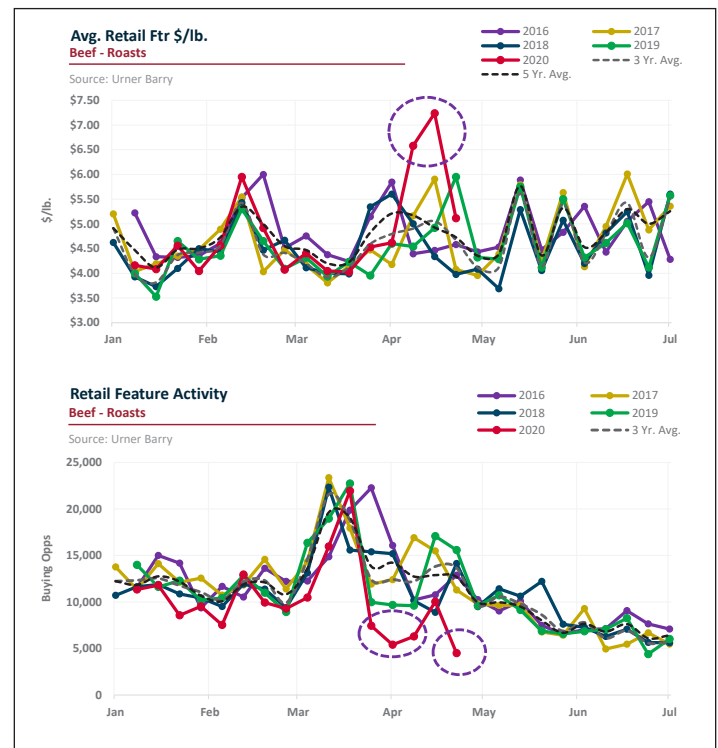


Figure 11. Retail Feature Activity for Roasts, largely comprised of large end cuts, Chucks, Shoulder Clods, Bottom Round, Top Round.

Furthermore, recent plant closures and reduced slaughter schedules due to workers testing positive for COVID-19 have reduced slaughter capacity and the overall meat supply over the last couple of weeks. This situation could have severe immediate effects on the market, as well as long-term impacts on the entire production supply chain, from cattle producers, feeders, packers and processors.

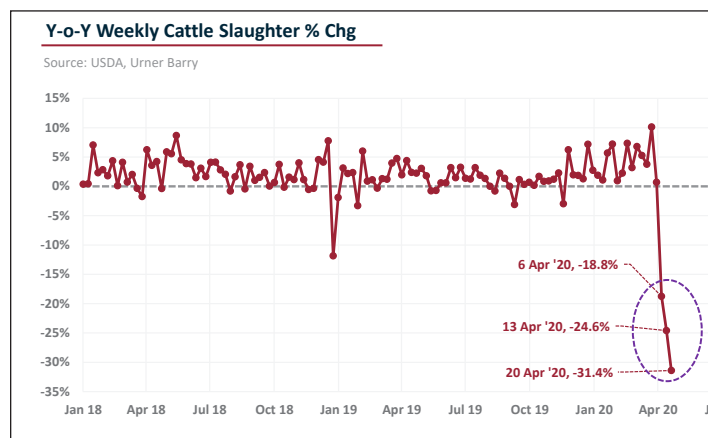


Figure 12. Federally Inspected Weekly Cattle Slaughter, USDA and Urner Barry adjustments.

The situation is likely to persist. Though plant closures may increase, some may come back in line and offset processing capacity loss. In addition, the reopening of the economy in several states will certainly help demand to some extent. But we believe demand for ground beef is here to stay for the foreseeable future, which will help support prices for ground beef—at the wholesale and processing level—as well as for end cuts traditionally used for grinding. Therefore, beef prices could continue to see support despite a significantly shrunken foodservice sector.

PORK

The situation with pork has also been quite volatile. Unlike ground beef, there is only so much bacon that can be moved through the retail sector. At about 20% of the carcass yield, bellies have experienced significant volatility since the beginning of the Great Lockdown, mainly downward. While the initial rush of demand supported prices for bellies destined for retail bacon production—soon after, prices on all types of bellies collapsed. Also different from ground beef, we cannot assume that the bacon not eaten at foodservice will naturally be shifted to the retail sector. There is a significant demand void in the pork market when the foodservice channel is limited.

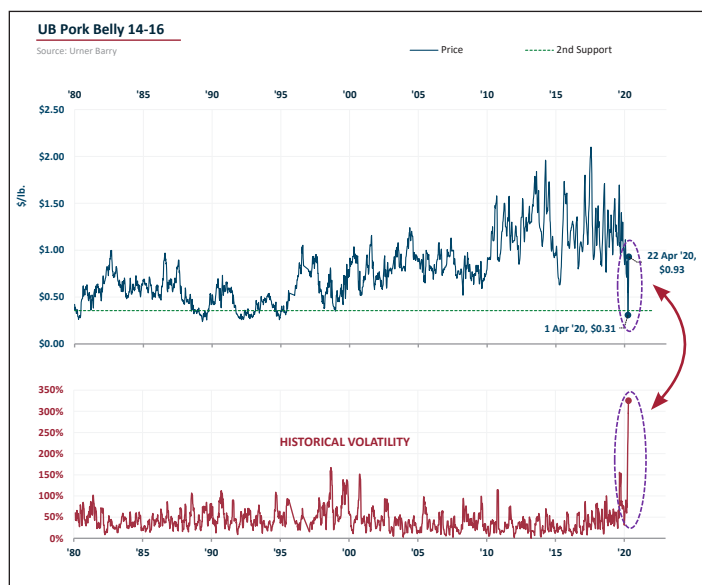


Figure 13. Urner Barry's quote for 14-16 bellies, and historical weekly volatility.

Surprisingly, we have seen features decline, not increase, despite these historic low prices. We believe this is because within weeks, prices for bellies returned to where they were prior to the Great Lockdown. The main driver has been plant closures across the country, which have reduced meat supplies, as opposed to a stronger demand.

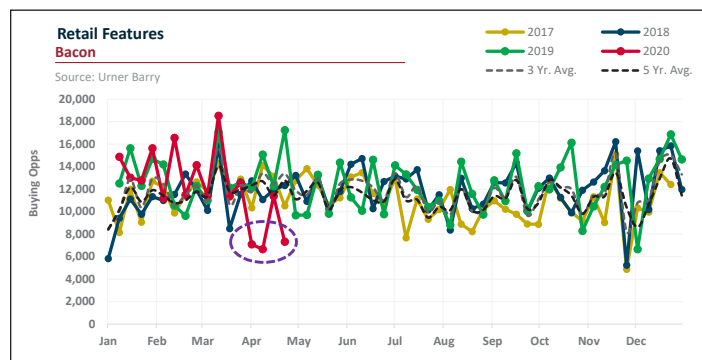


Figure 14. Retail Features for Bacon, Urner Barry.

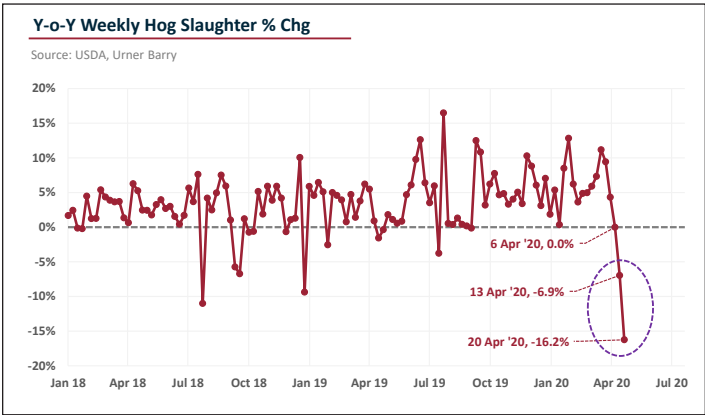


Figure 15. Federally Inspected Weekly Hog Slaughter, USDA and Urner Barry adjustments.

However, one item that has remained strong throughout the Great Lockdown have been loins both at the wholesale and retail level. While prices at wholesale have been adjusting lower over the years, prices for boneless loins since early March have only moved up, largely due to a strong retail demand. As a result, retail feature volume decreased, and retail feature price moved up.

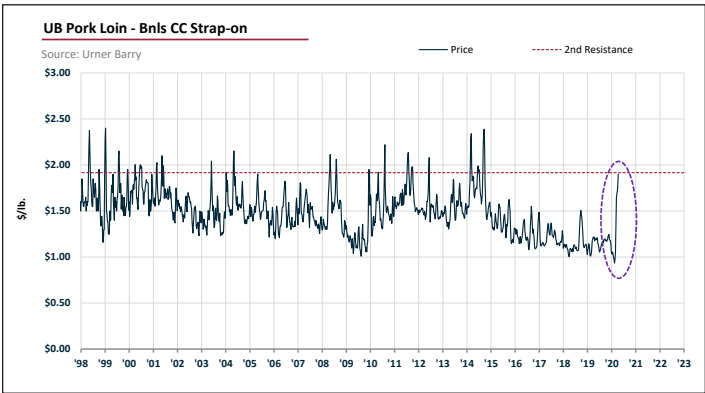


Figure 16. Urner Barry's Pork Loin, Wholesale Bnls CC Strap-on Quote.

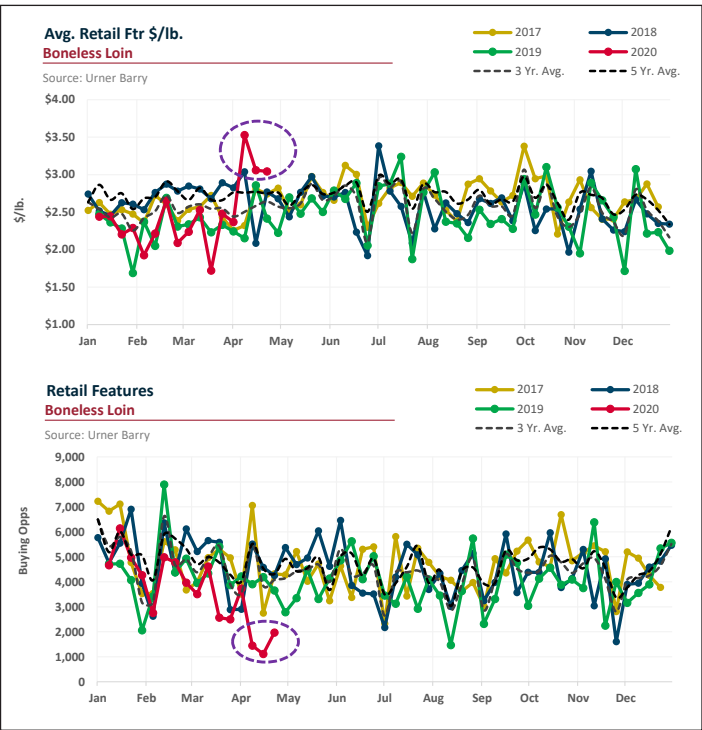


Figure 17. Retail Feature Activity and Avg. Price for Boneless Pork Loins, Urner Barry.

The pork market is largely supported at the moment mainly due to a significantly reduced slaughter. Limited labor continues to exacerbate the availability of certain cuts, particularly those that need de-boning, like hams. We expect further price volatility for pork due to variable meat supplies led by plant closures and re-openings, rather than demand at retail and the already diminished foodservice sector changing much.

CHICKEN

The most consumed meat in the country has also been quite volatile. Though some behavior follows the same patterns as beef, pork and, to an extent, eggs—chicken prices at both the wholesale and retail level remain relatively low. For example, during the first weeks of the Great Lockdown, consumers rushed to buy chicken, causing high volatility for many items at the wholesale level. At the same time, retail feature activity dropped dramatically along with ad prices. While lower ad prices left us scratching our heads, it appears that the incentive to promote an item that is already being consistently purchased at relatively affordable prices diminishes in the mind of the retailer.

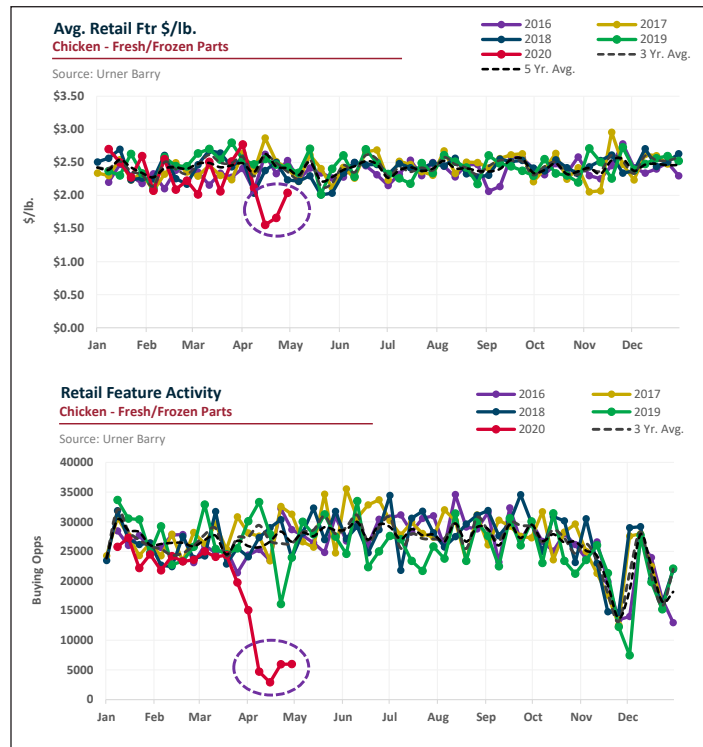


Figure 18. Retail Feature Activity and Avg. Price for Chicken Fresh/Frozen Parts .

Let us take a few steps back. Retail feature activity and average retail feature prices for chicken had remained steady from 2015 through 2019, amid falling wholesale prices. From 2018 to now, overall chicken prices had remained historically and comparatively low. We can clearly notice that chicken prices follow a clear seasonal pattern and, in 2020, we were bound for a seasonal price increase—all else equal—as we approached March. However, initial retail feature activity in 2020 was lower than in the previous five years. One assumption we can make here is that retailers and sellers had less of an incentive to promote an item that is already priced low and has a consistent and strong demand.

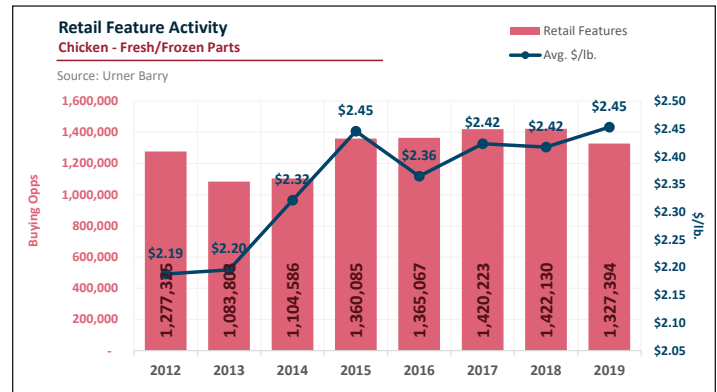


Figure 19. January-December cumulative feature ads and retail feature price per pound for fresh/frozen chicken parts. Urner Barry.

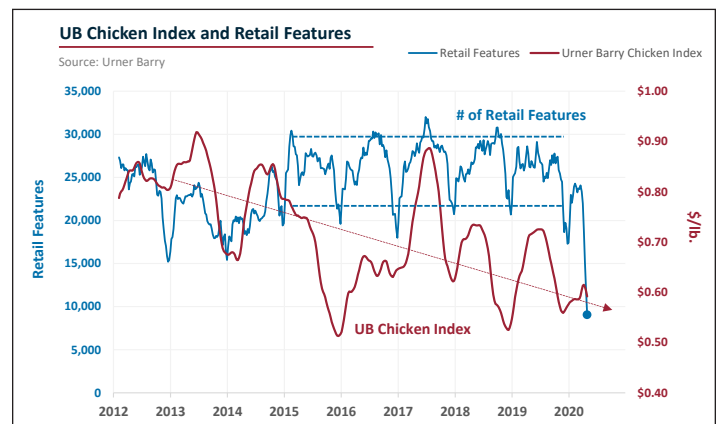


Figure 20. Urner Barry's Chicken Price Index, and Urner Barry's Retail Features for fresh/frozen chicken parts.

However, this seasonal increase in prices occurs regularly in chicken wings and tenders mainly due to college basketball, aka March Madness.

Looking at wings, we can clearly see that, not only did we not experience the seasonal uptick in price, but we even saw prices for both wholesale and retail fall dramatically as a direct result of the lockdown.

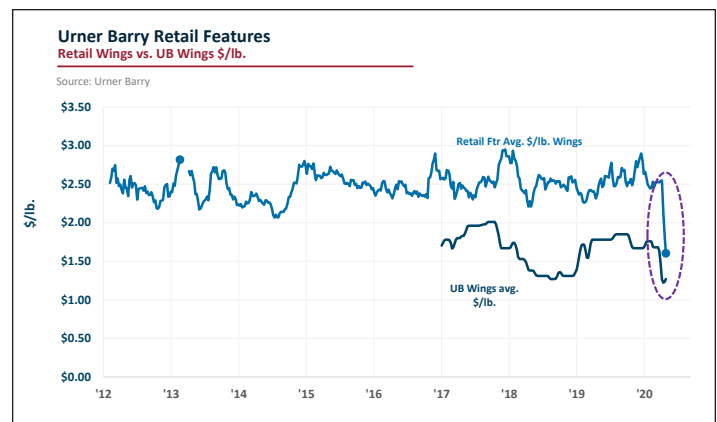


Figure 21. Urner Barry's Wings Quotation, Urner Barry's Retail Feature Ad average price per pound.

Boneless skinless chicken breasts, a popular retail item, experienced an initial opposite reaction. Wholesale prices rose at the fastest rate seen in a 3-week period only to see prices fall dramatically immediately after. The interesting thing here is that despite retail feature prices to the consumer remaining steady for the last few years, lower ad prices have been passed to the consumer in 2020. We can see this by looking at the ratio of retail feature price to wholesale prices. Yet, as mentioned at the beginning of this section, retail features continue to decrease amid declining prices at the wholesale level and steady prices at the retail level.

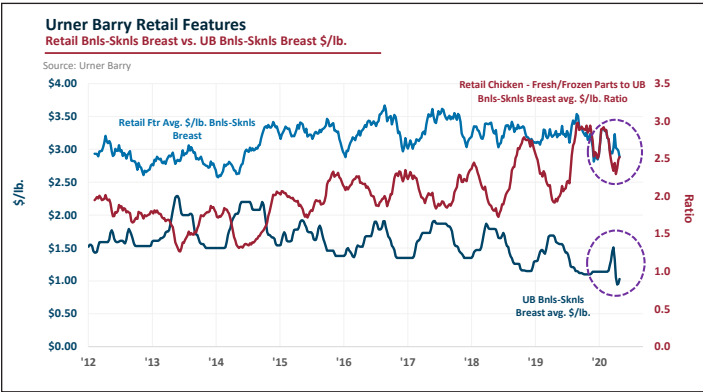


Figure 22. Urner Barry's Skinless/Boneless, Chicken Breast Wholesale Quote vs. Skinless/Boneless, Chicken Breast Retail Feature Ad avg. price per pound.

Chicken also faces disruptions at the plant level with workers at several plants testing positive for COVID-19. As a result, slaughter has also decreased considerably in the past two weeks, with supplies of RTC (ready to cook) chicken experiencing a steep decline. As a result, chicken prices at the wholesale level are gaining support despite a significantly decreased demand from a paralyzed foodservice sector. Our view is that prices will continue to remain volatile at the wholesale level but since chicken is perceived as a lower-priced protein, in addition to wholesale prices sitting at comparatively low historical levels, retailers have more room to play with and still offer this item at an affordable price.

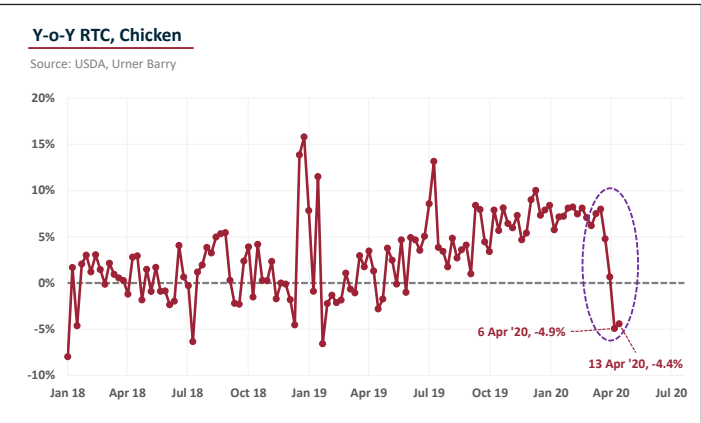


Figure 23. USDA RTC (ready to Cook) chicken.

CONCLUSION

We believe that price volatility will persist as the industry juggles creativity through limited outlet channels as foodservice remains largely paralyzed. In addition, plant closures and delayed schedules will cause meat supplies to vary widely, increasing uncertainty on trading positions.

Food expenditures at home will overtake those away from home once again and will very likely remain that way for a few years. While food expenditures growth away from home have outpaced those for food at home, it is not unreasonable to expect this reversal to be dramatic. In terms of the recovery, the coin is still in the air. There are many questions surrounding what all of this will look like on the other side, starting with what the potential space and occupancy restrictions will be for the foodservice sector at both the state and national level. This will hinder—or not—much of the recovery seen in previous recessions. The share of these expenditures between these two categories will very likely take us back to at least 2011 levels, where food at home covered around 54% of the share. Thereafter, the growth rate for expenditures of food away from home is not likely to be close to what it was in years' past. We will elaborate more on this in a later report.

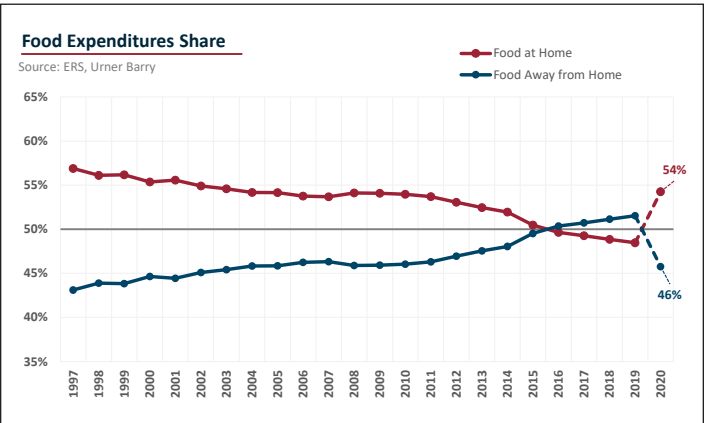


Figure 24. ERS, Food Expenditures Series, Urner Barry.