

foot and mouth facts

For Livestock Producers

How does the foot and mouth disease outbreak in Europe affect price volatility in the futures and option markets, and the degree of uncertainty in current short- and long-term price forecasts?

The European outbreak of foot and mouth disease is believed to be positively effecting U.S. pork prices. Pork production in Europe is more than double that of the United States and Canada combined.

Most of the pork produced in Europe is consumed in Europe. However, about 3 billion pounds of pork are exported, primarily to Japan, Hong Kong and the United States. The United States and Canada export only 3.2 billion pounds combined, so if Europe was unable to export pork, the loss to the world supply would about equal United States and Canada's combined exports. Denmark is the largest European exporter. An outbreak of foot and mouth disease there could increase hog prices in the United States. It is not clear whether that possibility is already expected and reflected in the market.

The value of beef by-products, such as hides, are increasing because of the disease in Europe and raising U.S. live cattle prices. Other than by-product values, there is little impact expected from foot and mouth disease on domestic cattle prices, assuming that the disease does not reach North America.

Beef producers and consumers benefit from recent trade barrier reductions over the years and net exports have grown rapidly. Any arbitrary restrictions on trade imposed by the United States would cause retaliation from our trade partners and damage the United States' ability to increase its share of an expanding world beef trade. The risk of importing foot and mouth disease through cattle and beef products is extremely low. Three countries — Australia, Canada and New Zealand — provide the bulk of U.S. beef imports (87 percent) and two countries, Canada and Mexico, provide 100 percent of our live cattle imports. None of these countries has foot and mouth disease as of mid-April, 2001, and all have safeguards in place to help prevent a foot and mouth disease outbreak.

Some believe that the current outbreak in the UK could boost United States wheat exports as long as the disease does not spread to the United States. For example, reports of an outbreak of foot and mouth in Argentina led to rumors that Brazil could ban the import of wheat from Argentina. Brazil is the largest importer of wheat, and Argentina is its principal supplier. While Brazilian authorities did provide clearance for the import of several varieties of U.S. soft wheats, only time will tell whether the United States can penetrate that market. For now, barring major production problems in Argentina, such a scenario seems unlikely.

In the meantime, news about foot and mouth disease will influence the wheat market, but most likely through spillover reactions from the feed grain and oilseed markets. These markets are most likely

to react negatively toward news of increased foot and mouth outbreaks because less feed will be needed as livestock becomes sick or dies from foot and mouth and its control measures around the world. The United States exports very little corn to the United Kingdom, but the decline in feedgrain demand in the United Kingdom may eventually affect grain movement in the global market.

Fundamentally speaking, the wheat market's reaction to news about foot and mouth disease is, at best, difficult to explain. Very little wheat is currently fed to livestock because current prices make wheat an expensive feed relative to corn. That means that reactions in the wheat market seem to be irrational. One explanation is that the uncertainty surrounding the foot and mouth disease situation creates a cost to holders or buyers of the commodity, which causes buyers to bid lower. Economists refer to this "cost" as a risk premium. It is unclear when the markets will recover or whether they already have.

What market and risk management strategies should Colorado producers consider now? How should production and marketing plans change?

The market risk from foot and mouth disease for livestock producers stems from consumer perceptions towards eating meat. Currently, U.S. consumer habits are remaining unaffected by foot and mouth disease. Consumers may start making different choices, however, based on the information they get from the media and each other even though there is no human health risk from foot and mouth disease.

Assuming that foot and mouth disease is contained in Europe soon and it does not spread to North America or Denmark, the net impact of foot and mouth disease on U.S. livestock prices should be positive because of potential pork exports and increasing value for beef by-products. Currently, underlying supply and demand conditions are very supportive to prices, but a negative consumer reaction could impact prices later in the year. Thus, now is a good time for cattle and hog producers to consider forward pricing expected spring and summer sales through futures, options or forward cash contracts.

Grain and oilseed producers concerned about additional unfavorable news about foot and mouth disease should consider stepping up forward sales of 2001 production, even though a considerable risk premium may already be built into current price levels.

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For more information, contact your local Colorado State University Cooperative Extension office, usually listed in the county government section of your local phone book, or visit www.footandmouth.colostate.edu.