

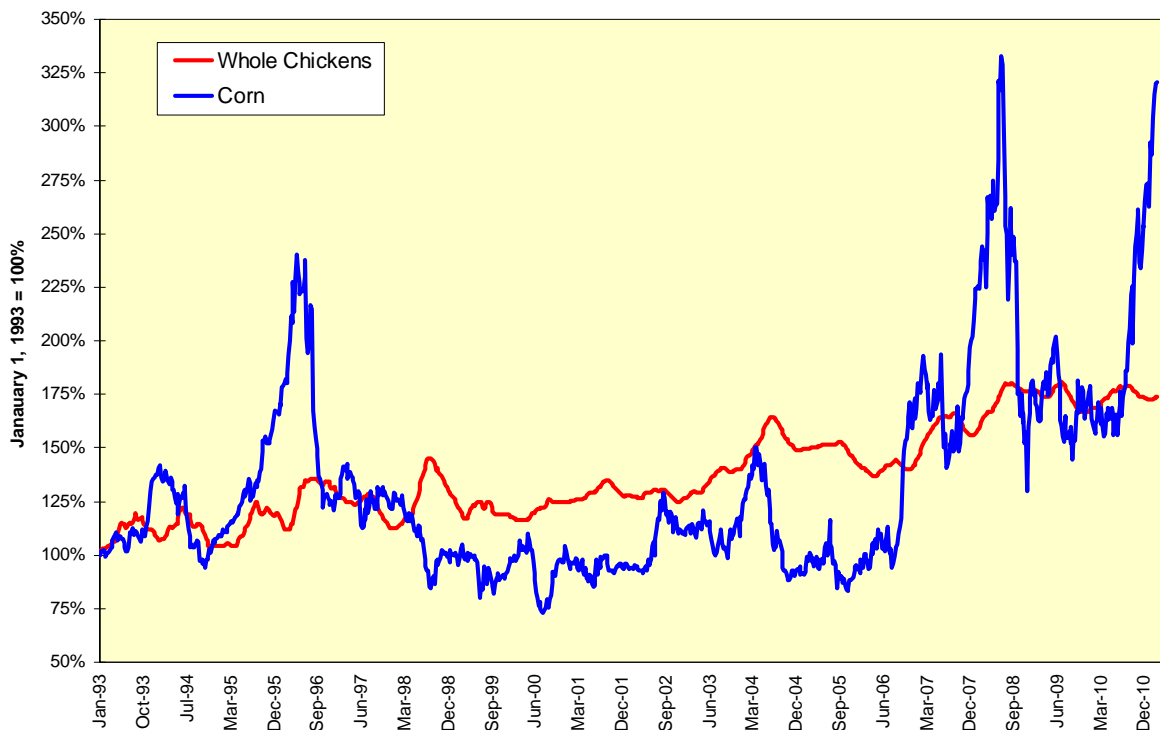
Corn Is Chicken Feed

Commodities are not pretty, and my sincere apologies in advance for more sensitive readers. The livestock and poultry businesses always viewed their herds and flocks as conversion devices for turning low-value corn into high-value meat; one poultry feeder I know used 9 million tons of corn a month. That is equivalent to a 1,300-car train; think about that the next time you are stopped at a railway junction.

If would stand to reason, therefore, the collective decision to divert almost 40% of our corn crop to ethanol distillation and away from livestock and poultry feeding before distillers' dried grains are added back to the feed mix should have a dampening effect on the profits of the poultry industry.

The actual answer is more complex. Poultry feeders can adjust the size of their flocks fairly rapidly and liquidate excess inventory as feed prices rise, and vice-versa as they fall. The net effect is a surprisingly steady price path for whole chickens relative to corn processors' 15-30 day bids for corn.

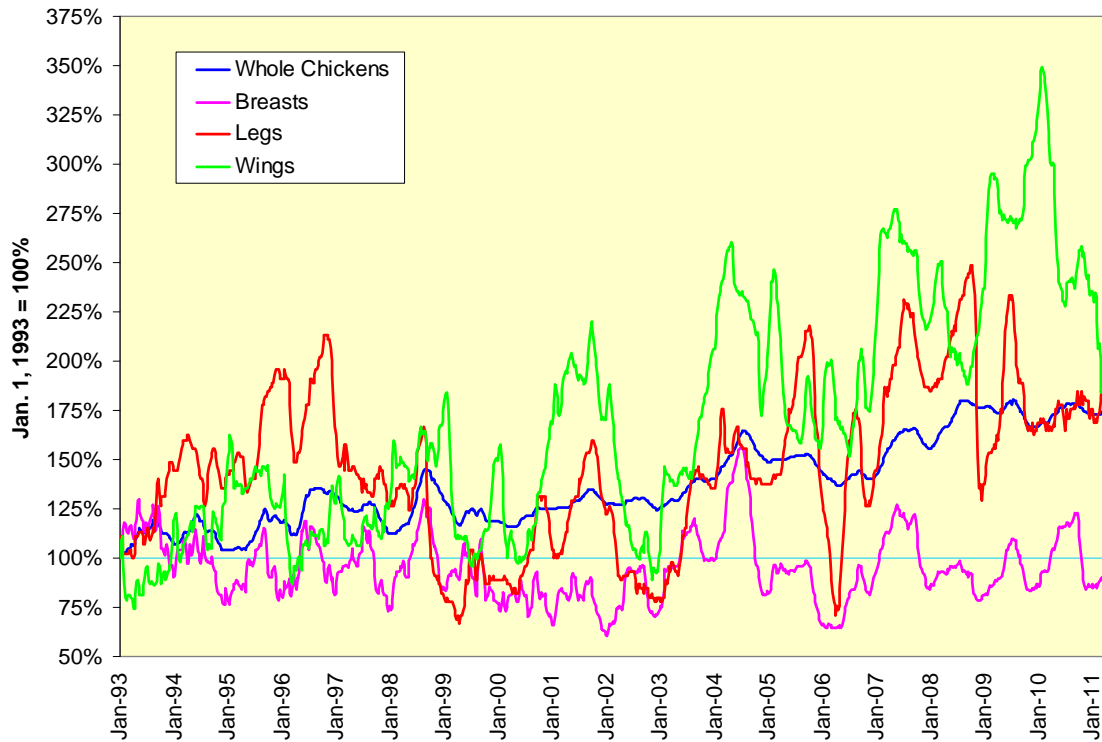
Corn And Chickens



Party Of The First Part

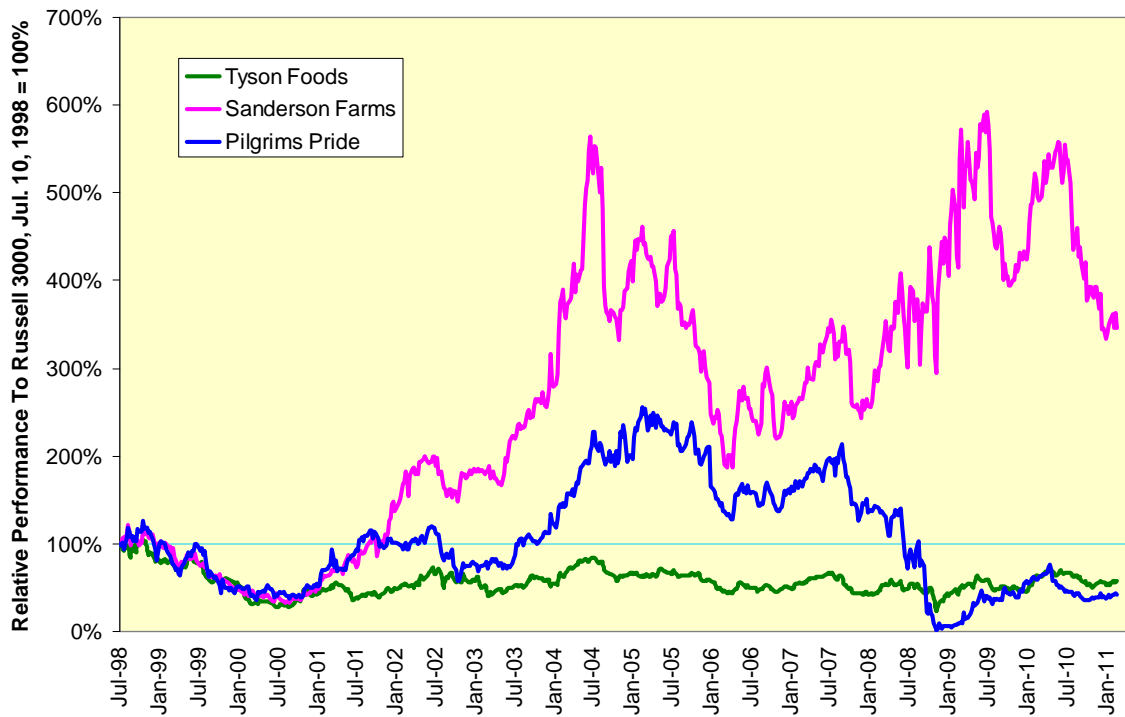
Chicken processors also add value to their output by selling parts instead of whole birds and by branding their output as much as possible. The cash market for chicken parts – all data below represent Georgia-dock, packed-in-ice prices – is active and reflect final markets. Note how volatile the wings market is; this is because wings tend to wind up in restaurant chains such as Buffalo Wild Wings while breasts face competition in supermarkets.

The Flap Over Wings



Not all poultry processors are alike. Let's map the total returns for three firms, Tyson Foods, Sanderson Farms and Pilgrims Pride relative to the Russell 3000. In the absence of prior knowledge, you would be hard-pressed to know these firms are operating in the same industry. Tyson has been a flat-line relative performer for the past decade, while Pilgrims Pride has had minor ups and downs en route to winding up near Tyson. Sanderson Farms, however, is in a world of its own; it is the high-beta tech stock of the industry.

Sanderson Farms: A Flock Of One



The last two corn price spikes, the one in 2007-2008 and the one from July 2010 through today, have led to a downturn in Sanderson's relative performance. Should corn prices remain high, and there is little reason to believe the yet-to-be-planted Northern Hemisphere crop will be a difference-maker, we should expect downward pressure on Sanderson Farms and indeed on the whole livestock and poultry industry to continue.