

Snow Crab Markets for 2005

A Customer Revolt

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2005 Will be Difficult Year

- U.S. Customers refused to buy crab at last years prices.
- Large inventory overhang as new season begins
- Inventories exist in U.S. and Japan
- Pattern very similar to 2001 when prices decreased by \$.75 to \$1.00

2004: producers did well but our customers lost money

- Customers have high inventory at high cost
- Brokers and Wholesalers lost money on crab in many cases.
- Quality took a nasty downturn
- Japanese importers face markets below their wholesale cost.
- U.S. customers are angry about their experience with Crab last year.

Today's Discussion

- Review of 2004 Season
- Price and demand trends in the U.S. and Japan
- Other Market factors: quality, inventory, substitute products and currency
- Outlook for 2005:
 - Gulf, Nova Scotia & Newfoundland production
 - U.S. Market
 - Japanese purchases

What Happened in 2004

- Japanese burned in 2003
 - Came late to market
 - Surprised by U.S. Demand
 - In 2004, they were determined not to repeat mistake.
- 2004 – Japan set the market price too high
 - Newfoundland negotiated very well.
 - Some companies were out of product to process in China
 - Result: First contracts were at \$4.40 FOB plant. This was about 25 cents higher than the Japanese expected

Second year with crab prices over \$4.00

- The U.S. market cuts back when snow crab is priced over \$4.00.
- 2003 had high prices at end of season due to Japanese demand; most U.S. buyers not affected.
- 2004 U.S. buyers reacted to high prices by significantly cutting back on orders.

Snow Crab Products & Markets: Japan

- Japan:
 - Whole Crab
 - Sections
 - Tourism trade (hurt in 2004 by earthquake in Niigata, a major snow crab market)
 - Retail (poor end of year buying season)
 - Meat
 - Sushi (produced in China)

Competition from Russian crab

- Live crab landings
 - Heavy live crab landings from Russia, fed by black market, provide lots of supplies to domestic Hokkaido producers.
- Black market sales made at lower prices for cash.
- Slow selling at end of year has left some inventory in Japan

Japan Market Factors 2005

- Japanese said in Boston that they will likely buy same amounts of crab as in 2004.
- Determined to get lower price.
- Current prices in Japan are down by ¥300 to ¥400 below importer cost for gas frozen crab.
- Japanese feel it is a buyer's market

U.S. Products

- Sections
 - Asian Buffets
 - Casino's
 - Seafood Buffets (Southeast U.S.)
 - Retail promotion
 - Darden & Foodservice
- Crabmeat: Canadian snow crab practically non-existent.

2004 Market Factors: U.S.

- Hurricanes in Florida hurt tourism and cut into crab sales in prime market in August and September.
- High prices meant most retailers cut back purchases by 80% to 90%. Little movement of 2 pounders.
- Increase in quality complaints.
- Biggest factor was switch to alternative crab products.

The Customer Revolt

- Buffets bought Angulatus and Dungeness
 - Priced \$0.50 to \$0.70 below snow crab
- Retail refused to promote, stopped buying
- Darden refused to promote and advertise “endless crab”
 - Darden promotion of crab lifts entire industry
- Result: high inventories of unsold product

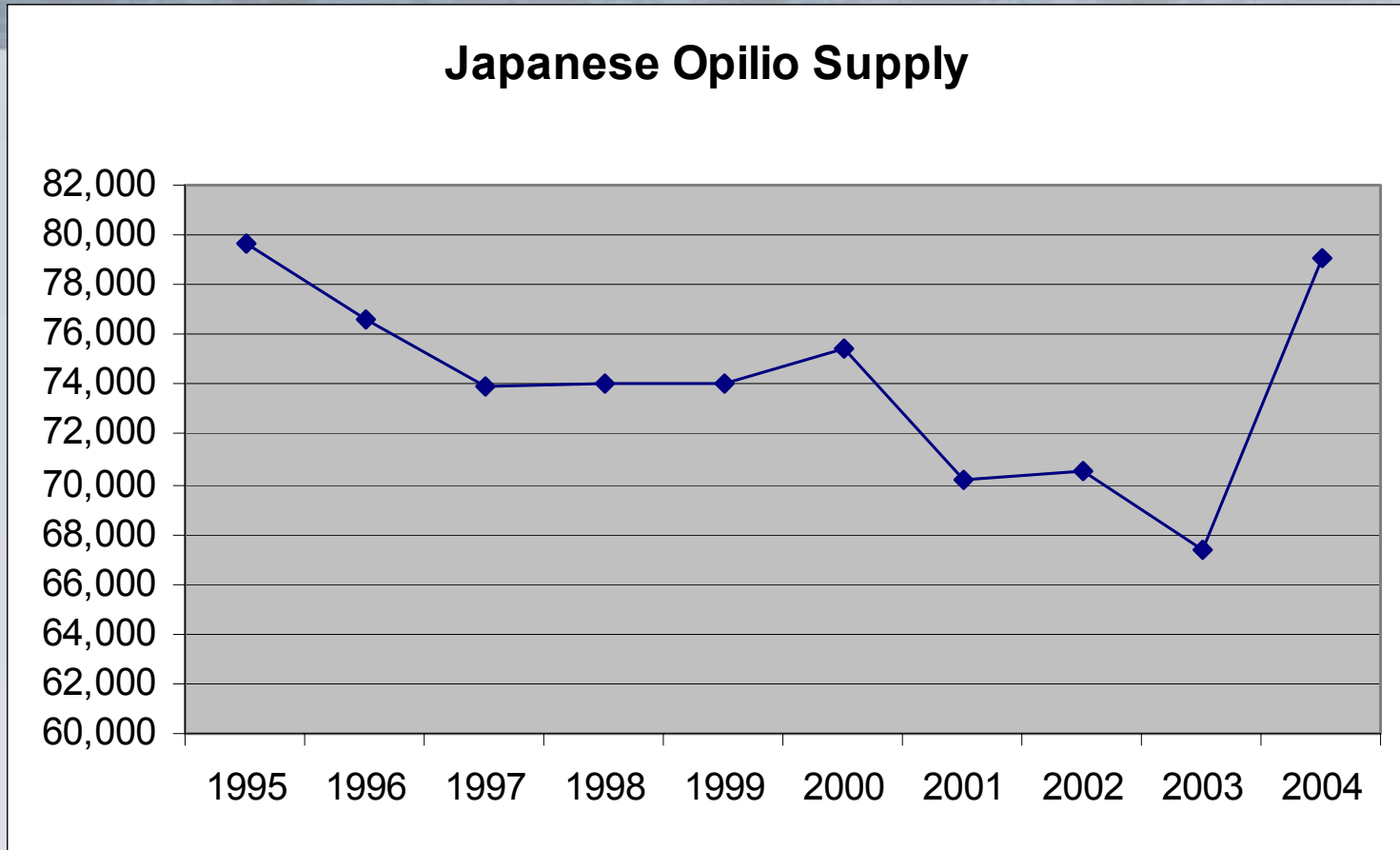
Size of U.S. Market

- Increased imports of substitutes
 - What is size of U.S. crab market
 - Imports 72,000 tons in-shell product
 - Imports of 35,000 tons crabmeat
 - Landings of 10,000 tons snow crab in Alaska
 - Landings of 30,000 tons Dungeness
 - Landings of 80,000 tons blue crab
 - Total Market is about 190,000 tons in shell crab products, and 35,000 tons crabmeat.

Snow Crab

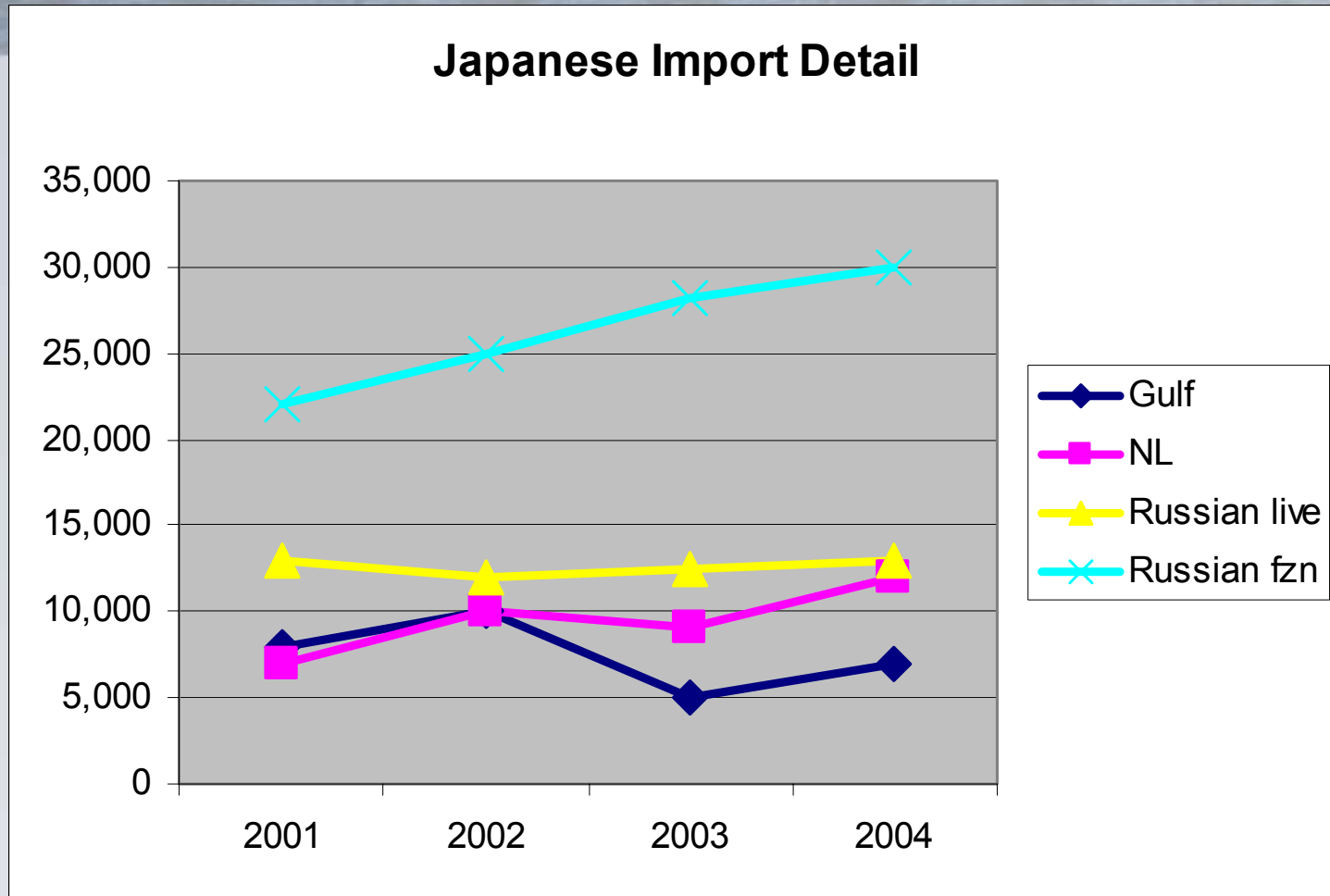
- 2003 Imports 51,134 tons
 - Canada 42,700 tons
- 2004 Imports: 49,138 tons
 - Canada 40,642 tons
- Other (angulatus etc) around 10,000 tons
- Even though more Canadian snow crab shipped to Japan, U.S. market was supplied with large volumes in 2004.

Size of Japan Market



Source: Bill Atkinson News Report

Details on Japan Snow Crab Market



Reasons for Increase in Supply to Japan

- Russian Imports up 2400 tons
- Canadian imports up 5000 tons
- US Imports up 1800 tons

Perceived shortage of crab in 2003 caused market to over react in 2004

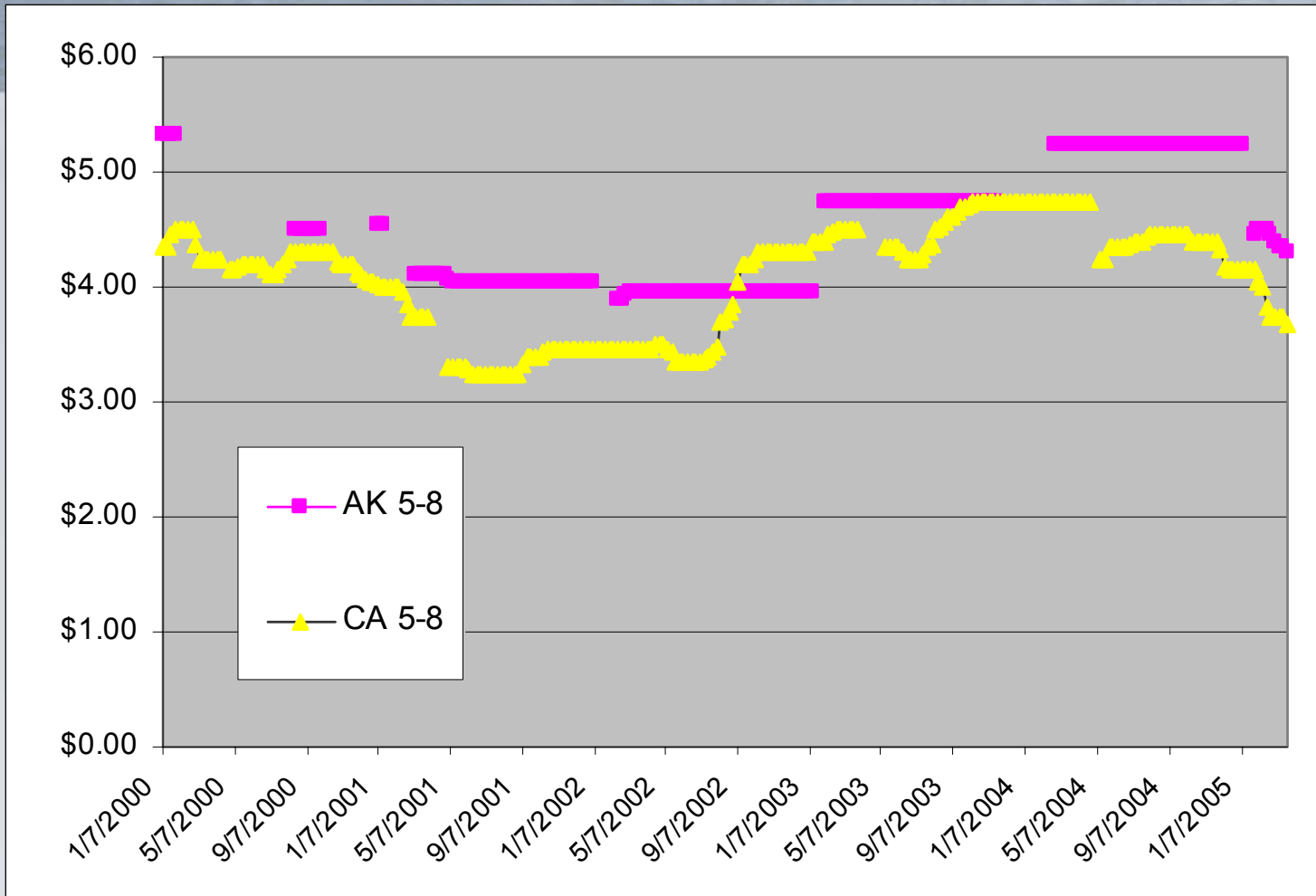
Situation in Alaska

- 2005 Production 7000 tons processed crab
- Reports of huge Catch per Pot rates
- Industry thinks 2006 may be big year.
- Darden major buyer
- Japan did not buy as much this year due to price.

Summary of Price and Demand trends

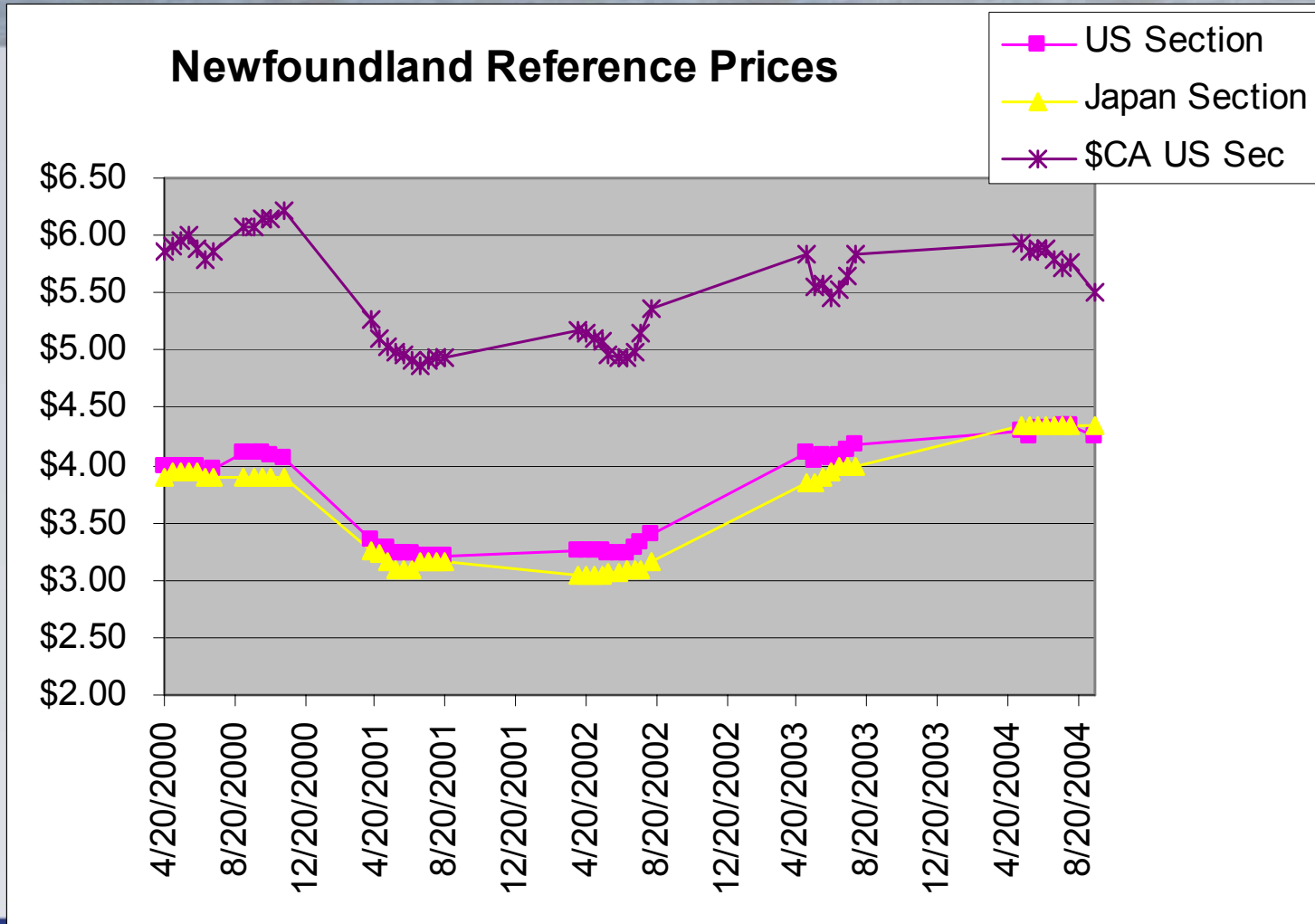
- Reaction to perceived shortage in Japan led to Japanese over buying in 2004.
- U.S. market faced with higher price for crab than they could absorb.
- Japan sales in 2004 weaker than expected.
- U.S. sales in 2004 very poor.
- Net Result: unsold crab in both markets.

Price History for U.S.



Source: Urner Barry

Reference Price History in Newfoundland



Major Factors impacting market in 2005

- Inventories
- Quality factors
- Substitute Products
- Currency

Inventories

- Best estimates are that between 17 and 24 million pounds of crab remain unsold.
 - Taylor: 10 million pounds (mostly in Newfoundland)
 - Others: Customer's have large inventory
 - Issues:
 - Mark down creates huge financial problem
 - Sales of old season product hurt sales of new season product.

Quality Factors

- High Prices led to a “anything goes” mentality. Newfoundland’s 15% processed rule mostly ignored
- Buyers rejected product for both quality and market reasons.
- Need to develop a second tier market for lesser quality crab. In 2004, hurt the market.

Substitute Products

- Dungeness: record landings in U.S. in 2004 & 2005. Retail began to special Dungeness instead of snow crab. \$0.50 cost saving.
- Angulatus: looks great, lower meat fill than snow crab. Priced mid \$3.00 range.
- Japonicus: smaller and cheaper
- Jonah and Rock Crab: used in some alternative applications

Currency Trends very unfavorable: example of NL formula

- \$3.55 crab returns \$1.57 today
- \$3.55 crab would return \$1.72 last Sept.
- \$3.55 crab would return \$1.88 last May
- \$3.55 crab would return \$1.97 May 2003

- \$4.00 crab would return \$2.33 in May 03
- \$4.00 crab would return \$2.24 in May 04
- \$4.00 crab would return \$1.86 today

Production Outlook for 2005

- Canadian Production: slight increase in Gulf Quota; decrease in 2J and 3K, likely net 15% - 20% drop in NL quotas.
- Possible Tie Up in Newfoundland
 - Real possibility that harvesters will strike.
 - Could delay start of season one month or longer.
- Net result: lower production will not be sufficient to maintain last years pricing

U.S. market will continue to take most volume

- Disagreement over pricing:
 - Boston Seafood Show
 - \$3.25 foodservice buyers
 - \$3.50-\$3.75 packers
 - Japanese will not set price this year.
 - Need to make crab a promotion item again.
 - Customers all have existing inventory.
 - Traders offering big discounts

Foodservice Users have cut back

- Crab comes off menus when it is over \$4.00 for a sustained period.
- Retail cannot promote at that price.
- Delayed impact: two years. This year will be the impact.

Strategy for getting back into U.S. Market

- Make crab a positive item for retail promotion.
- Retail works on 30-35% margin.
- \$4.99 crab must be bought at \$3.25 to \$3.50 maintain retail margins.
- This price may be too low—but hard to get retailers interested at higher than \$3.50.

Foodservice needs to work off inventory

- Tend to cost items at last purchase price, don't cost average.
- Have to buy way back into market
- Sysco content to not buy crab until current inventories run out.
- Some distributors still have 2003 crab(!).

Underlying value for snow crab

- Snow crab value levels
 - Moderate production: \$3.50 to \$4.00
 - Shortages: \$4.00 to \$4.50
 - Heavy production: \$3.00 to \$3.50
- This year's normal expectation would be pricing in the \$3.50 + range. But psychology may not be normal.
- Buyers may have to be convinced to come back to snow crab.

Strategy for Japanese Market

- Sell at best price for Japan – could be higher than U.S. price if it wasn't for buyers market.
- Japanese have different pricing considerations than U.S., due to different types of crab markets.
- Japanese can afford to pay more than U.S. again this year, but may not do so.

Overall Outlook for 2005

- To restore crab market to health, inventories will have to be cleaned up. This means pricing crab at a market clearing level.
- Disruptions in the market that keep prices higher will simply postpone the problem, and will keep the market smaller than it needs to be.
- A small market will not absorb Canadian and Alaskan and Russian production should there be any increase.

Harvesters and Packers have to find a way to remain profitable at lower price levels.

- Need to pay true value for lower quality, smaller crab.
- Plants must run efficiently. Glut landings hurt quality.
- Cost control is necessary due to currency constraints. Your product is worth 15% less, without you lifting a finger.

Alaskans are talking about better crab production over the next 2 years

- Boat captains report huge concentrations of young crab. Will recruit to fishery next year if they survive.
- Alaskans believe in an 8-10 year cycle— next few years should see upswing, like late 1990's.
- Major volumes of new production would transform market, and would return to under \$3.00 pricing

Prosperity in the crab fishery in the U.S. market over the past few years came from the market expansion of the late 1990's

- Lower prices for crab are likely here to stay for several years. We must learn to adjust.