



THE MONTHLY RED MEAT OUTLOOK: HOGS & PORK

AUGUST 2020

The hog and pork complex in the US has regained a sense of normalcy and packing plants are now operating at about 95% capacity after the big reductions in slaughter this spring as a result of COVID-19 infections in plants. The pork cutout has been trading in the \$60s for the past two months and could very well stay there for another month or two. Cash hog prices have improved modestly, with the Western Corn Belt negotiated price moving from the high \$20s in early July to the low \$40s currently (see **Figure 1**). With the rise in cash hog prices, packer margins

Cash hog prices have moved higher in recent weeks suggesting improving fundamentals in the production sector

have been compressed somewhat, but still remain above \$25/hd, which is a very large margin for this time of year. Thus, packers have a strong financial incentive to keep kill levels high and help work through the backlog of hogs that was created this spring when packing plants were forced to close due to COVID-19 infections. The industry has made some modest progress at reducing the backlog, but we estimate that at least 2 million hogs remain backed up in the pipeline. Producers have done a remarkable job of slowing down weight gains in hog barns by shifting to lower-energy rations. That has helped, but it is clear to us that more animals will need to be euthanized because the packing industry will just not be capable of clearing all of those backlogged hogs within a reasonable time frame. In fact, recent carcass weight data suggests that hog producers are more current than imagined and thus there probably has been some unseen clearing of the backlog through sacrifice of animals via euthanasia.

SUPPLY PICTURE

Daily slaughter levels at or above 470,000 head are now the norm. Packers even managed a 480,000 head kill one day last week. However, the Saturday kills have recently pulled back to under 200,000 head and that has kept weekly kills below 2.6 million head. By our estimate, from mid-August onward, slaughter would need to be above 2.6 million head per week just to clear the animals that were targeted for slaughter late in summer. That means that there will be no additional room for clearing out backlogged hogs and the need for bigger kills grows even more after Labor Day. As a result, the industry will be forced to clear the remainder of the backlog through euthanasia and we suspect that producers have already accomplished a portion of that.

The reason we think that there has been ongoing euthanasia of backlogged hogs is because price levels in the negotiated markets have risen and carcass weights are trending seasonally lower. In contrast to the cattle markets where carcass weights have abandoned their seasonal tendency, hog carcass weights appear to be back on track (see **Figure 2**). The USDA *Hogs & Pigs* survey data would indicate a backlog of more than 2 million hogs, but the price and weight data suggest otherwise. Prices don't lie, but sometimes surveys do. Therefore, we tend to put more credence

According to USDA, the backlog of hogs stands at about 2 million head, but there are reasons to believe it is much smaller than that

in what we are seeing from carcass weights and prices than from the numbers reported in the *Hogs & Pigs* report. Thus it is our belief that there has been more euthanasia of hogs than many believe and there are far less hogs backlogged than imagined.

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One theory that hasn't been discussed much is the potential for a hole in the hog supply this fall. If producers euthanized primarily weanling pigs and other light weight animals back in April and May, this could create a dip in the number of market-ready hogs later this fall. Kills would fall short of what is expected based on prior pig crops and the supply of pork would be tighter than expected. It is difficult to know for sure if this scenario will play out, but the possibility is there, and end users need to be thinking about the potential for a counter-seasonal rise in pork prices this fall as a result. Right now, the futures market is not seeing it that way as it is pricing October hogs below August, but we think there is a good chance that hogs in October will actually price above where August settles. That is way different from the normal seasonal price pattern which normally has October hogs valued \$10-15/cwt below August.

DEMAND SITUATION

Domestic pork demand continues to look weak, particularly for processing items such as bellies and hams. The drop in foodservice demand as COVID-19 infections surge is depressing demand for bacon and keeping the belly primal well below normal levels for this time of year. There is no reason to think that will change anytime soon. With hams, the problem seems to be in the processing sector where there have been COVID-19 infections in plants and operators are having difficulty finding enough labor to debone hams. As a result, boneless ham muscles are trading at a much higher than normal level relative to the bone-in product. That has caused some wild swings in the ham primal daily value recently. On days when boneless muscles make up a large percentage of the ham sold, the primal shoots higher and on days when the bone-in hams dominate, the primal crashes lower. Ham processors are entering the season of the year when they normally begin preparing product for the end-of-year holidays. But with the current tight-labor situation, we might expect that holiday processing to be delayed this year or even curtailed from normal levels. That would keep the ham primal on the defensive and since hams account for a large portion of the carcass, it might also very well keep the cutout on the defensive. The retail cuts (loins, butts, ribs) might be called upon to carry the cutout in August and

beyond. Fortunately, retail features are picking back up from the low levels seen during the spring and early summer. Pricing on those features is much better too and that could boost demand for the retail items in the weeks ahead. Our take has been that strength in the retail cuts will largely be offset by softness in the processing items and thus the cutout could stay mired in the mid-to-high \$60s for weeks or months.

Pork exports continue to be unimpressive. Based on the weekly data that USDA releases, pork exports following the plant closure problem have been about 23% below where they were earlier this year. They are still marginally above last year's level, but the fact that they have stayed rather depressed this summer when pork prices were low is concerning. China is taking a lot of US pork compared to historical norms, but the movement to China has stagnated and seems to be no longer increasing. That is bad news for a pork industry that will have growing quantities of pork to market as we move into the heavy production periods this fall and winter.

SUMMARY

Hog kills seem to have stabilized just below 2.6 million head per week but come fall the industry will need to do better than that to clear the production pipeline. Price and carcass weight data seem to suggest that producers have euthanized more aggressively than most think and that could provide some support for the market this fall. In fact, there is a chance that hog and pork supplies could dip lower this fall if producers euthanized mostly young pigs back in April and May. Pork demand is just so-so at present and isn't getting a lot of help from the export market. Problems with labor for ham boning operations this fall could keep hams cheaper than normal and that would weigh on the cutout. Our fundamental analysis suggests that the pork cutout will remain comfortable in the \$60-70 range right through September but could break to the upside come October. Retail cuts will likely need to lead the way. Buyers are advised to remain close bought through August and early September but might want to consider covering a portion of Q4 needs now while the futures market is depressed. **Table 1** provides our near-term price forecasts.

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Figure 1: WCB Negotiated Cash Hog Price

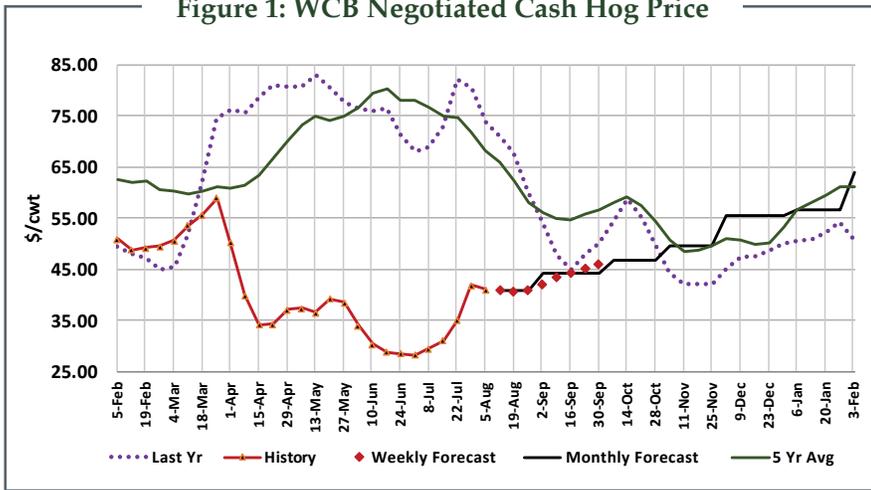


Figure 2: FI Dressed Wt., Barrow & Gilts

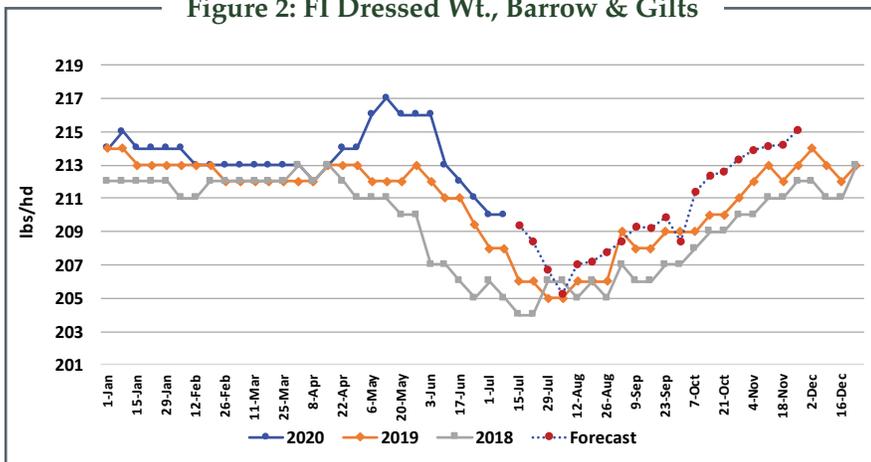


Table 1: JSF Hog and Pork Price Forecasts

	12-Aug	19-Aug	26-Aug	2-Sep	9-Sep	16-Sep
Pork Cutout	66.6	66.4	66.5	66.8	67.7	67.9
Loin Primal	64.8	63.3	61.4	63.1	63.5	63.9
Butt Primal	66.3	65.5	67.4	68.5	67.4	68.1
Picnic Primal	48.9	48.5	51.1	52.6	54.2	55.0
Rib Primal	118.3	118.0	117.1	115.1	113.2	113.0
Ham Primal	60.3	60.2	59.2	56.8	58.4	60.0
Belly Primal	90.2	92.2	94.7	96.0	98.6	95.2
Lean Hog Index	52.0	51.6	51.8	53.0	54.4	55.2



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