



THE MONTHLY RED MEAT OUTLOOK: HOGS & PORK

JULY 2020

A sense of near normalcy is beginning to return to the hog and pork complex. Daily slaughter is now running above what we estimate is necessary to kill all of the pigs that were targeted to finish in July and that means that the extra kill is helping to clear up some of the hogs that were backed up during the plant closures in April and May. It is a long way from being done, but at least it is a start. With the increased production has come lower pork pricing and buyers are responding by restocking at a good clip. Packer margins are still very wide—estimated to be about \$35/hd last week—and that is necessary to incentivize them to keep the kill high and further help clear out the backlogged hogs. We think that packers will be in a position

July pork production could average **8-10% over last year** as packers work through backlogged hogs

to keep their margin in the \$25-35/hd range through the balance of the summer (see **Figure 1**). That means that if the cutout slips lower, they will likely put pressure on cash hog prices in order to maintain their margin. By the same token, if the cutout should rally then there is a good chance that cash hog prices will improve. For now though, the Lean Hog Index that the futures settles to is stuck in the mid \$40s and isn't showing much sign of leaving that level in the near-term. Pork buyers, many of whom stood on the sidelines while the cutout was falling rapidly in June, have now come back into the market and the supply pipeline appears to be full once again. Going forward, ample supply seems assured as long as COVID-19 doesn't force any more plant closures and price levels will largely depend on consumer demand in the next few months.

SUPPLY PICTURE

Pork packers produced a couple of daily kills over 470,000 head recently and that is a huge improvement over the 260-270,000 head that they were able to slaughter when COVID-19 was rampant in their plants. We have also seen a couple of weeks where the kill was close to 2.6 million head. The Dec/Feb pig crop suggested that kills in June and July would need to run about 2.45 million head per week, so the recent kills are more than what is necessary and thus helping to clear out some of the backlogged hogs. However, that same pig crop also suggests that by the end of August weekly kills will need to be near 2.7 million head. Packers can probably manage that, but it won't leave much room for clearing out extra hogs. As we look further into the future, weekly kills in Nov/Dec will likely need to be at or above 2.8 million head per week so there is some risk that when we get to November the supply of hogs will outstrip the industry's ability to kill them. That wouldn't impact pork prices nearly as much as it would hog prices, but it is a concern for producers late in Q4.

Hog carcass weights are running about a half-percent over last year currently and that is pretty amazing given how many hogs are backed up in the system. Producers must have done a very good job of transitioning hogs to maintenance diets in order to keep the weight off. The de-trended and de-seasonalized weight data that we use to gauge producer currentness is falling rapidly and that is a good sign (see **Figure 2**). It is unclear just how many hogs were euthanized in recent months, but the recent *Hogs and Pigs* report suggested a larger number than what we would have guessed based on anecdotal reports from producers. In either case there should still be over 2 million hogs backed up in the system. But we caution the reader that quite possible that a lot of those hogs will never show up for slaughter. It is not easy to explain, but we have seen situations in the past where hogs that existed on paper seemed to disappear into thin air before they

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could make it to slaughter. Thus, don't be surprised if this fall people start asking, "What happened to all those extra hogs?"

The recent *Hogs and Pigs* report did confirm that producers are finally scaling back their herd, although not as aggressively as we think they should. The June 1 breeding herd inventory was reported down 1.3% from last year. That is the first YOY decline in the breeding herd since Q3 of 2014. We think that poor profitability over the next six to twelve months will induce further reductions in the breeding herd. That is a necessary step in order to restore profitability to the production sector. It also means that pork availability will begin to tighten as we head into 2021 and price levels will rise. The futures market does not yet seem to be factoring in these future supply reductions.

DEMAND SITUATION

Domestic pork demand appears to be pretty soft at present. Buyers are no longer panicking over tight supply and the cutout has been mired in the mid \$60s for a couple of weeks. COVID-19 infections have surged in a large number of states and many are beginning to put additional restrictions on restaurants and bars. That doesn't bode well for demand as we move through the hottest part of the summer when consumers are already a little less likely to exhibit strong demand for pork. Pork does still hold a price advantage to beef, so that could help somewhat as retail featuring rebounds in the weeks ahead. Bellies look particularly weak at present and we don't expect a lot of improvement in those price levels anytime soon. With the resurgence in COVID-19 infections, there will be fewer large gatherings and thus limiting the demand that would normally flow from those types of events. Since we know that packers will be incentivized by large margins to keep kills high in July and August, it will be crucial for demand not to sag too much or else we could easily see the cutout move into the \$50s before the end of summer.

Pork exports look good, but not great, at present. All eyes have been on China in hopes that they would begin to import even more US pork this summer, but so far those numbers have been trending lower. We did see a nice increase in new sales to China

last week after several weeks of small sales and so that might be an indicator that China is going to expand its purchasing as we move deeper into summer. Movement to the big markets of Japan and Mexico also looks pretty soft in the most recent data. USDA released their international trade data for May this week and it showed total pork exports up about 21% YOY. However, the YOY comparisons will get much tougher in the second half of the year because we will be comparing against some pretty big export numbers from last year. We have adjusted our export forecasts downward for the balance of 2020 and now expect that exports for the year as a whole will be up about 14%. That is a long way from the 40-50% YOY increases that many of the bullish traders were expecting as 2020 began.

2020 pork exports now expected
to be up only 14% YOY

SUMMARY

Normalcy seems to have returned to the hog and pork markets, although producers are still struggling to clear the backlog of hogs that developed this spring when plants were forced to close because of COVID-19 infections. The pork cutout has stabilized in the mid \$60s, but there is some risk that it will dip down into the \$50s later this summer if domestic pork demand doesn't improve. Cash hog prices are expected to remain weak and packer margins are expected to remain very large in order to incentivize the big kills that are needed to clear out backed-up hogs. Foodservice demand is on the decline again as restaurants are facing tighter restrictions as COVID-19 cases surge. The pork pricing environment over the next couple of months looks like it will be soft. However, producers are starting to take steps to scale back their herds and that will eventually lead to tighter supplies and higher prices, but that might not be noticeable until late 2020 or early 2021. Until then, it is likely to be a buyer's market and we are advising buyers to remain relatively close bought at least through August. **Table 1** provides our near-term price forecasts.

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Figure 1: Packer Margin

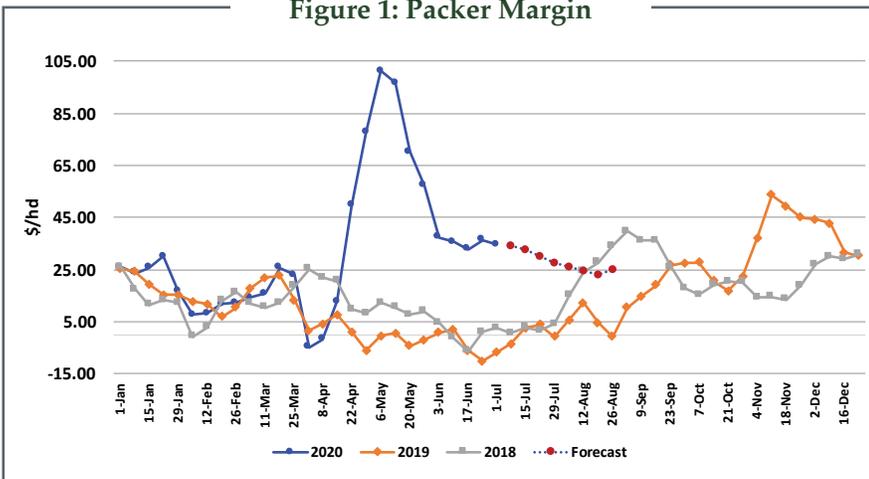


Figure 2: Detrended & Deseasonalized Barrow & Gilt Carcass Weights

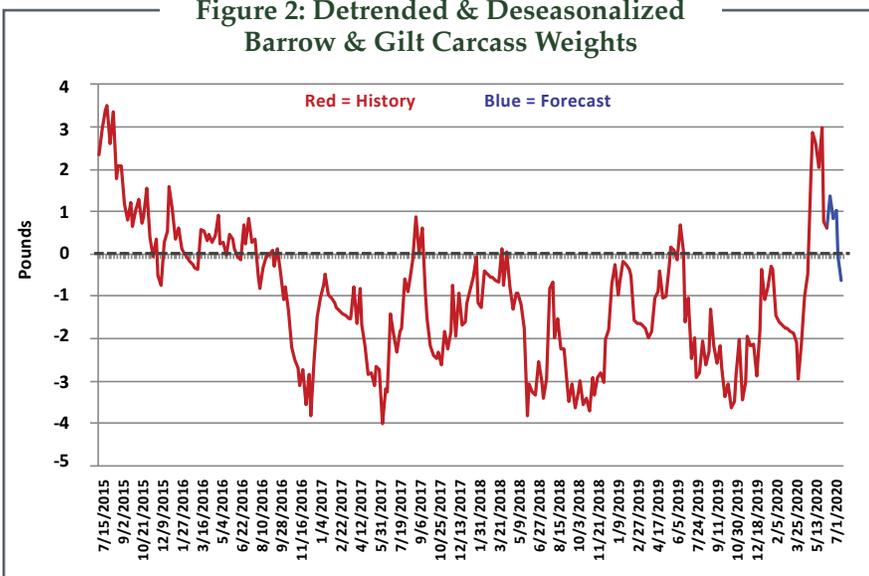


Table 1: JSF Hog and Pork Price Forecasts

	15-Jul	22-Jul	29-Jul	5-Aug	12-Aug	19-Aug
Pork Cutout	62.4	60.0	60.1	59.2	58.9	59.8
Loin Primal	63.1	60.9	60.1	58.4	58.0	61.3
Butt Primal	69.8	67.4	63.5	60.5	56.8	56.0
Picnic Primal	44.6	41.1	40.5	39.7	40.6	38.7
Rib Primal	122.3	119.0	116.0	114.5	113.8	116.0
Ham Primal	49.3	48.4	49.7	48.1	45.6	45.5
Belly Primal	83.6	78.8	82.3	85.4	89.9	92.2
Lean Hog Index	43.9	42.8	43.9	43.7	44.1	45.9



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