

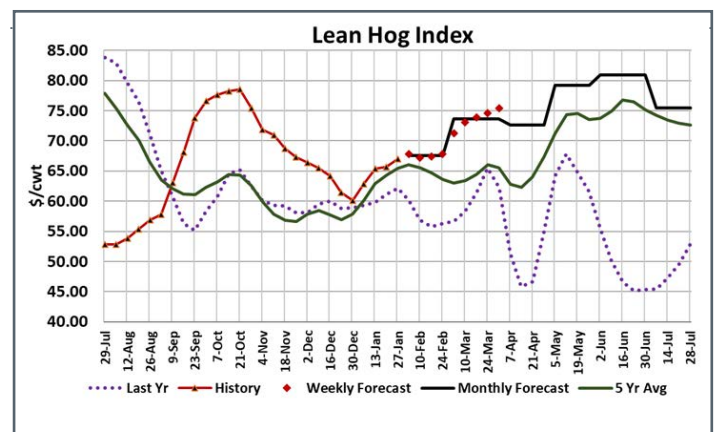
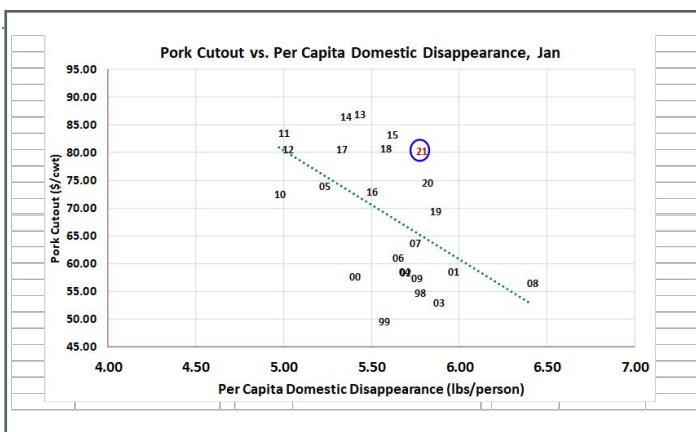
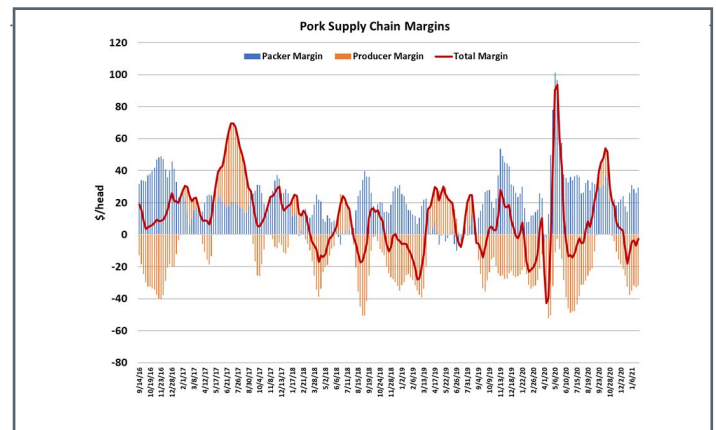
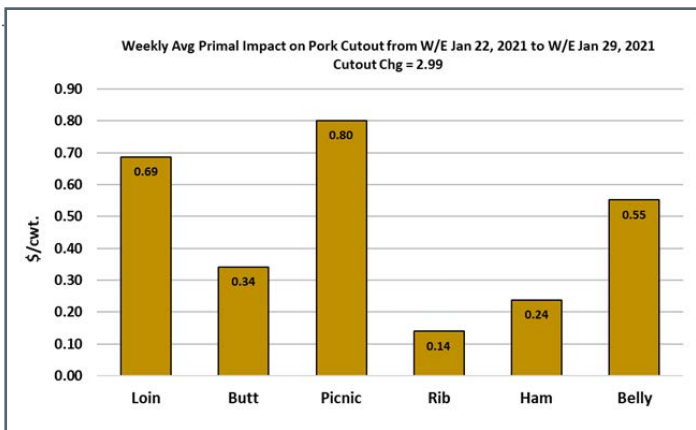
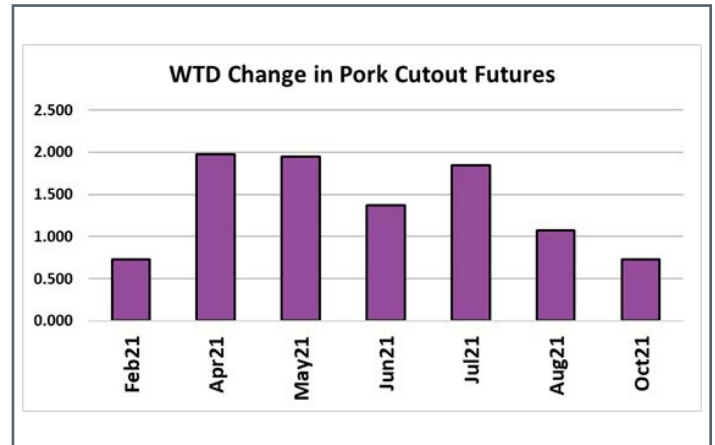
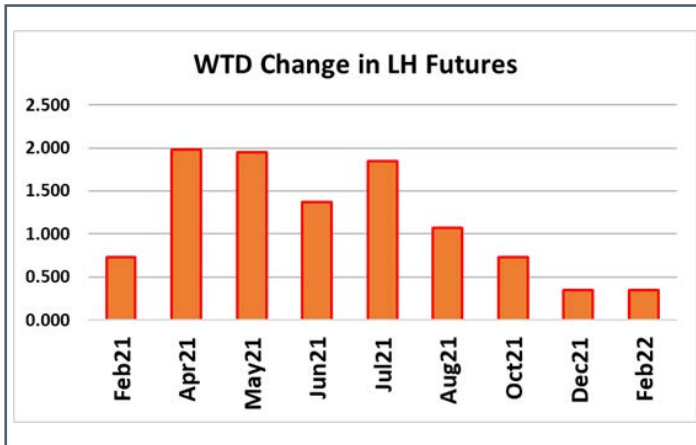


JANUARY 30, 2021

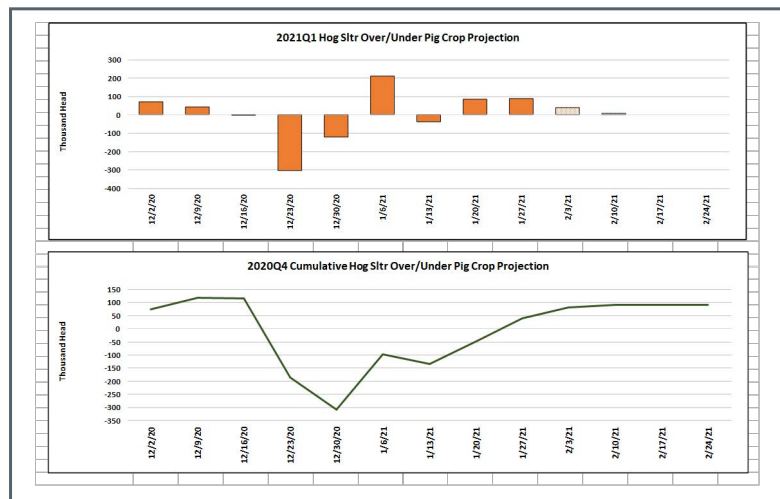
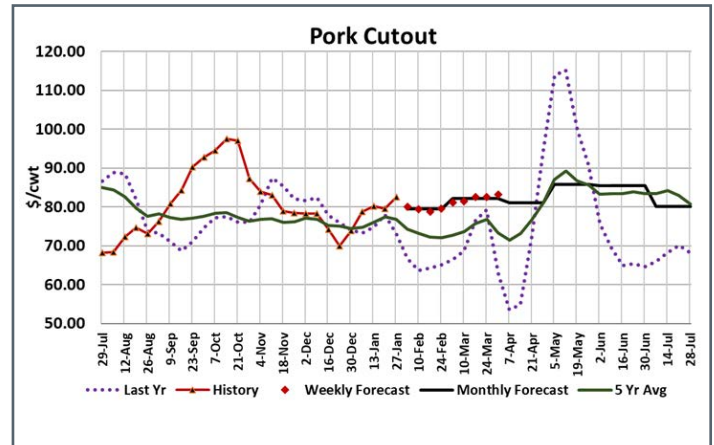
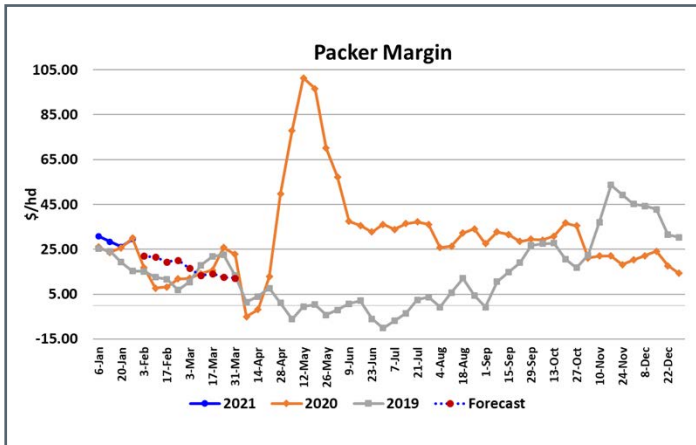
THE PORK WRAP

Last week I said that we should watch the pork cutout this week for signs that it would buckle under the weight of large production. It didn't. The cutout added almost \$3 this week (weekly average basis) and this happened on the heels of a 2.75 million head kill the week before. So, I think we can conclude that domestic pork demand is very strong at present. Further bolstering that thought is the fact that all of the primals were higher this week. This cutout isn't being held up by just a single primal. The strength is across the carcass and this week the retail cuts were the strength leaders (chart below). We also saw the combined margin tick higher, so the little down move that I pointed out last week appears to be a head fake. Now, having said all that good stuff about pork demand, it's clear that the pork cutout isn't roaring to quite the same degree that the beef cutouts are. Stronger cutouts led to cash hog prices rising, with the NDD up about \$1.30 on a weekly average basis. Packer margins moved higher to \$29.50/hd—almost identical to where margins were last year at this time. However, last year packer margins went from \$30/hd down to \$8/hd in a span of about 3 weeks during February as the cutout collapsed. Will it do that again? It certainly doesn't feel like it right now. I do have margins declining as we move into February, but only down to \$17/hd, which is still a pretty good margin. Pork supplies are ample. This week's kill registered 2.66 million head, but there was a weather-related slowdown on Tuesday. I'm looking for a slightly smaller kill next week and from there kills should slowly work lower towards a bottom in late June. Even with the weather-related issues this week, the kill was a bit above what the pig crop implied (chart below). However, with four weeks left to go in the quarter it looks like kills are on a trajectory to validate USDA's (revised) pig crop estimate. The official weekly carcass weight data still has carcass weights very high, but those are two weeks behind and the daily weights have been coming down at a good clip, so I'm confident that these big kills here in January are taking the excess weight off of hogs. That's important because the DTDS weights look really ominous right now. Anyway, strong demand can cover up a lot of sins on the supply side and that seems to be what is happening right now. For the past few weeks I've been having to raise my pork price forecasts because the market continues to outperform.

That was the case again this week. I'm looking for the cutout to hold in the lower \$80s, then work back into the upper \$70s as we get deeper into February, but I might already be behind on that because the cutout printed \$85 this afternoon. We saw a similar thing happen back in September and October where big production didn't seem to matter and the cutout just kept grinding higher, reaching \$100 briefly. Is that what is happening now? Possibly. We now know that that strong fall rally last year was driven by excellent domestic demand and that seems to be the case right now also (scatter below). Will it go to \$100? I doubt it, but it's not a zero probability. It would seem rather odd to have a \$100 cutout in February, but it seemed pretty odd back in October also, so I don't rule it out. Keep in mind that cold storage stocks are really low and so some buyers won't have the option of drawing on freezer stocks as the cutout rises. Low cold storage stocks were also a part of the scenario back in Sep/Oct. The futures market was higher again this week, but traders were a bit more cautious on Feb than they have been in prior weeks. Corn futures rebounded sharply this week and whenever that happens traders seem to want to buy the hog curve. I don't really think that this spate of high corn futures is going to materially impact pork production, so the inflation in the hog curve based on corn is probably misplaced and those contracts become really vulnerable should the corn market take another dive. As we move into next week, I'd like to see carcass weights come down because if demand does falter while weights are high it could be a problem.



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