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WEEK ENDING APRIL 09, 2021

THE PORK WRAP

This week the pork cutout added a little over $2 on a weekly average basis and the WCB negotiated market added a little under $2. So, the markets are still working higher–no change there. Packer margins increased a tad to $18.20/hd. All of the same supply/demand dynamics that have been in play for the last few weeks–tightening supply, strong demand–remained in place this week. This swine kill came in at 2.49 million head, with packers using a big Saturday kill to offset a very soft kill on the Monday following Easter. That kill was a little larger than what the pig crop suggested (chart below), but not by a lot. As of right now, the cumulative over/under kill for this quarter is very close to zero, so there is no reason to think that the USDA survey got the pig crop wrong. Barrow and gilt carcass weights remained flat at 215 (+2 pounds YOY) in this week's data, so no surprises there. The supply side of this market is behaving as expected.

It is the demand side that is causing all of the fireworks. Further, it is domestic demand that is driving prices higher, not surging international demand. This week USDA released trade data that showed pork exports in February were down 10.1% YOY. That was expected, since the weekly data has been running consistently below year ago since the beginning of 2021. So, if the price strength isn't being driven by a supply restriction and it isn't being driven by strong export demand, then there is only one possible culprit left: domestic demand. The combined margin chart below shows a pretty strong move higher this week after looking like it might be trying to peak last week. Recently, I've said that this market reminds me a lot of the Atkins Diet fad back in the early 2000s and the longer this demand strength goes on the more it resembles that market situation. If it is true that some shift in the public's dietary patterns has occurred and that shift causes them to demand more animal protein, then this demand strength could last for a long time. In that situation, what I think we would see on the combined margin chart is a long, relatively sideways pattern start to develop. You can see from the chart below that the combined margin has rarely plateaued. It is almost always going either up or down. It is worth keeping an eye out for that.

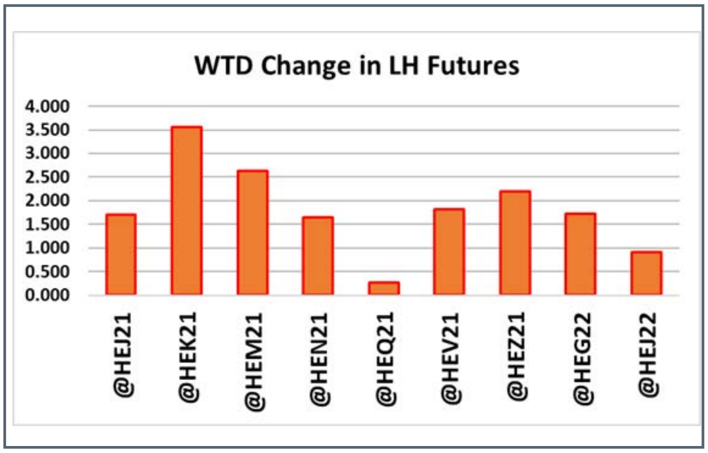
One thing that makes me think that this is something different from the many demand cycles we have seen in the past is that it seem to be affecting all of the animal proteins at the same time. A big part of what drives normal demand cycles in retailers switching from a relatively pricey protein to a more attractively priced one. So, it is not very common to have all of the protein demands in an strong upcycle at the same time. When they do all show strength at the same time, it makes me think there is something beyond the normal retailer-driven cycle going on.

Another thing that would impact the demand of all proteins in relatively the same way at the same time, is growth in consumer disposable income. Three rounds of stimulus checks have been sent to US consumers in the past year and so it is also possible that this demand surge is being driven by stimulus money. However, pork demand started strengthening way before the most recent (and largest) stimulus checks were issued. I have to think that the stimulus payments are helping this demand cycle along, even if they are not the primary cause of it. The other things that get mentioned but I don't really think are doing much to boost demand are:

1) *Increased vaccination rates causing an increase in consumer confidence and thus spending and,*
2) *Increased foodservice demand as the economy reopens.*

The latter seems to be the one that gets the most attention and I will grant that there could have been a modest demand pressure from foodservice operations rebuilding inventories in anticipation of reopening, but that rebuilding of inventories is a one-time event and once that is done then meat sales at foodservice takes away from sales at retail and any demand strength created shouldn't persist. Further, the demand index data indicates that red meat demand improved during the pandemic compared to where it was prior. If that was due to the shift in consumption from the foodservice channel to the retail channel, then movement back in the other direction should be negative for meat demand.

At this point I'm leaning strongly toward either a dietary shift or stimulus money, or both, driving this demand shift. Understanding the cause of a demand shift is important because it will help us to better gauge how long it will last. The futures market thinks it will last for quite a long time given the way it has priced the summer and fall contracts. My fundamental forecast is not as generous, but I'm assuming that this demand cycle will turn lower in a reasonable time frame like all the others before it. If something structural has changed (like dietary patterns) then the fundamental forecasts will likely prove too low. Next week, watch the daily demand scatters since those will give the first indication if demand were to soften, but remember that it takes several consecutive down days to confirm the trend has turned.


WTD Change in LH Futures
4.000
3.500
3.000
2.500
2.000
1.500
1.000
0.500
0.000
@HEJ21
@HEK21
@HEM21
@HEN21
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@HEG22
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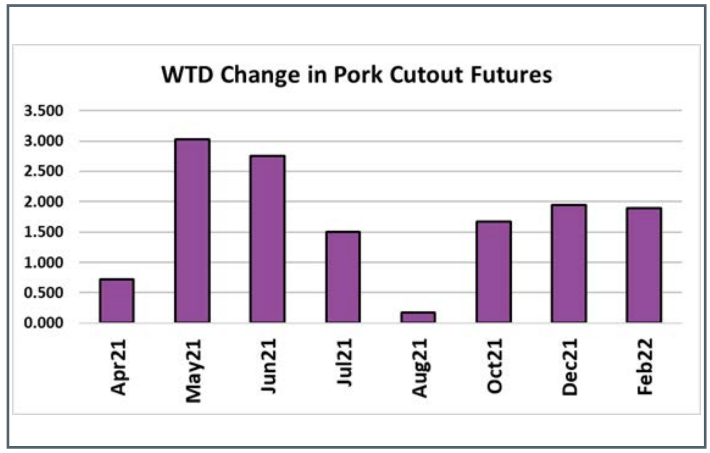
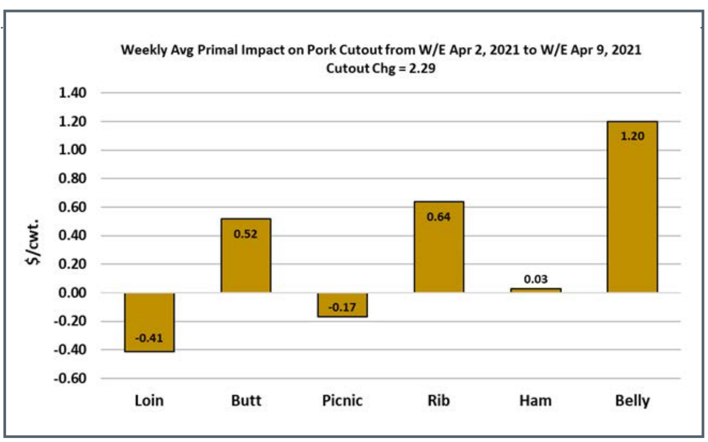
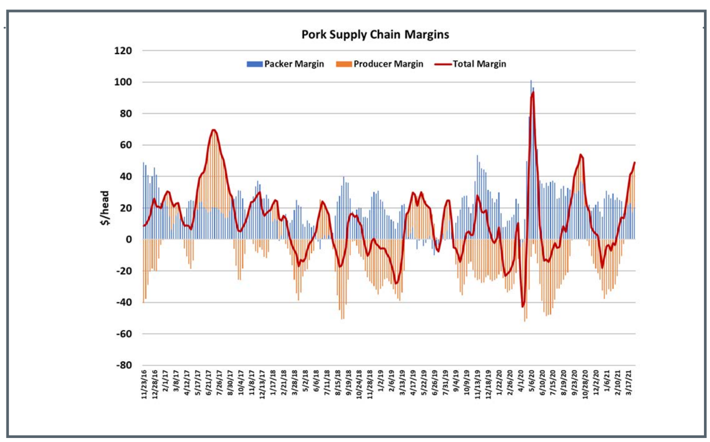
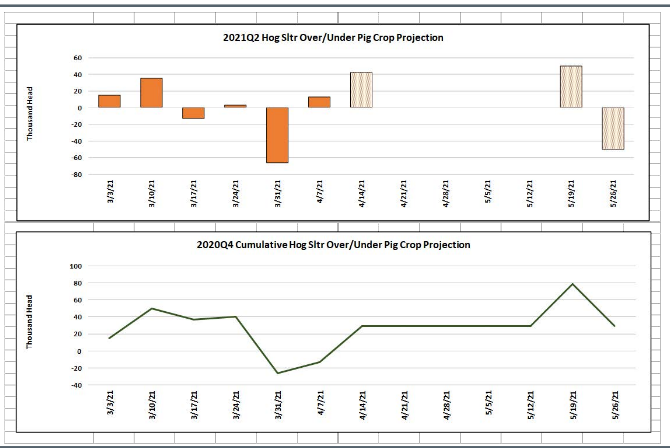
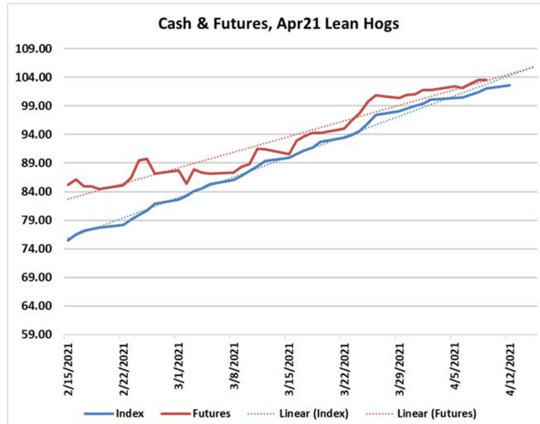
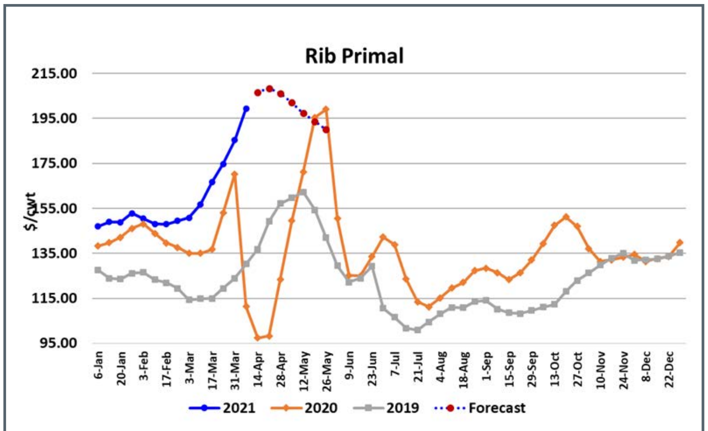

WTD Change in Pork Cutout Futures
3.500
3.000
2.500
2.000
1.500
1.000
0.500
0.000
Apr21
May21
Jun21
Jul21
Aug21
Oct21
Dec21
Feb22

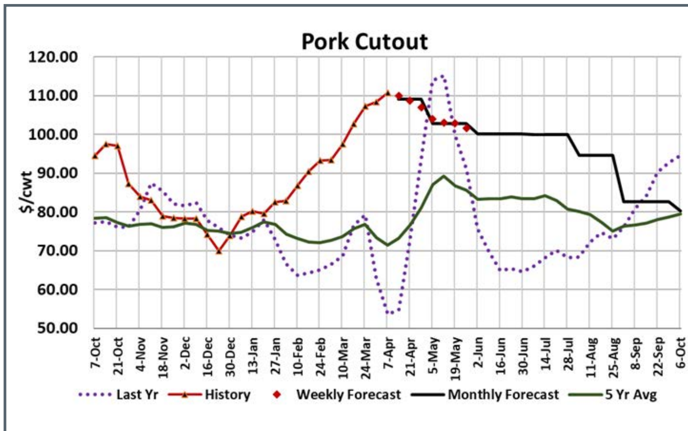

Weekly Avg Primal Impact on Pork Cutout from W/E Apr 2, 2021 to W/E Apr 9, 2021
Cutout Chg = 2.29
$/cwt.
1.40
1.20
1.00
0.80
0.60
0.40
0.20
0.00
-0.20
-0.40
-0.60
-0.41
0.52
-0.17
0.64
0.03
1.20
Loin
Butt
Picnic
Rib
Ham
Belly


Pork Supply Chain Margins
Packer Margin
Producer Margin
Total Margin
$/head
120
100
80
60
40
20
0
-20
-40
-60
-80









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Dr. Rob Murphy is an agricultural economist and business leader with over 29 years in the industry. He has a wealth of experience in the North American meat and livestock industries studying, analyzing and predicting market movements.