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THE MONTHLY

RED MEAT OUTLOOK: HOGS & PORK

MAY 2021

The US pork market continued its steady rise during April, with the cutout briefly reaching the $115 mark. Those gains appear to have stalled a bit here in early May, but the market has given no indication that is prepared to retrace substantially. Cash hog markets have followed the pork market higher and in some of the negotiated hog markets, prices for hogs are actually stronger than the cutout itself. That means packer margins are very narrow and may actually move into negative territory for the next few weeks. We calculate last week's packer margin at only about $1/head. The normal course of action for packers experiencing margin difficulties is to scale back the kill in order to raise pork prices and lower hog prices. However, that approach might not be viable in the current environment where available hog supplies are declining seasonally. If packers cut the kill now, their capacity utilization rate will fall to levels that will cause their per-unit costs to rise rapidly. So, packers might just be forced to endure very small or even negative margins in the near-term. With super-high hog pricing, hog producers are enjoying some of the best margins in almost two years. We estimate that producer margins during April were close to $19/head. It is even more amazing that producers were able to realize such strong profitability during a period where corn and soybean meal prices have been rising rapidly. The entire hog and pork complex is benefiting from the convergence of very strong domestic pork demand with seasonally-tightening hog supplies. That dynamic is expected to remain in place until mid-summer and perhaps even longer.

> **Negotiated hog prices have exceeded $115/cwt** lately — at times higher than the cutout

SUPPLY PICTURE

US hog slaughter last week totaled 2.45 million head, which is about 300,000 head less than the peak slaughter levels observed back in December and January. This reduction in the kill simply reflects the normal seasonal pattern at this time of year and slaughter numbers for the March/May timeframe have aligned very closely with USDA's estimate of the Sep/Nov pig crop. That pig crop was estimated to be down 1.5% from the year prior and thus it makes sense that hog supplies are a little snugger than what we had last spring. As we move past Memorial Day, the industry will begin working on the Dec/Feb pig crop, which was estimated to be down about 3% from the previous year. That portends even tighter hog supplies this summer than what we have seen here in the spring. But there is nothing dramatic in these numbers. By and large, the kill has been very well behaved this spring, following the normal seasonal patterns and matching up closely with the advertised pig crops.

Carcass weights also offer nothing out of the ordinary. Barrow and gilt weights have been stuck at 215 pounds for the last ten weeks, but should soon start to move lower in normal seasonal fashion. It is not unusual for carcass weights to plateau during the spring before starting their summer swoon. Weights are currently registering about three pounds, or 1.4%, heavier than last year at this time. That helps to offset some of the YOY decline in hog slaughter, such that overall pork production is holding pretty close to 2019 levels.

Hog producers are having to deal with very high feed ingredient costs, as corn and soybean meal prices have escalated rapidly in the last few weeks. Normally, we might expect such high feed prices to change producers' behavior, causing them to feed to lighter weights or even perhaps scale back their herds. However, producers haven't faced much financial pressure from high feed costs because the price they are getting for their hogs more than

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makes up for those higher costs. Producer margins are currently running positive by about $19/head and are likely to stay positive for at least another couple of months has the available hog supply continues to contract. If the high feed costs persist into fall, then producer margins will likely come under pressure and that might generate some reaction by producers. However, the corn futures curve is currently indicating fall corn pricing almost $2 below spot levels and so there is some hope that the feed cost situation will moderate by the time hog numbers start to expand this fall.

DEMAND SITUATION

Over the past couple of months, we have noted how strong domestic pork demand in the US has been. Nothing has really changed in that regard. The price-quantity scatter diagram for the month of April shows the 2021 data point far above any other except for 2014 when buyers were scrambling amid PEDv-reduced supplies (see **Figure 1**). That strong demand environment remains in place with one exception: the pork belly market hit a bit of an air pocket last week and that moved both belly prices and the pork cutout lower. It was the first week-on-week decline in the pork cutout since the middle of January (see **Figure 2**). We expect the belly market to remain a bit defensive for a few more weeks and that could reduce the potential for near-term gains in the cutout. However, demand for the other primals remains quite strong, particularly for items such as ribs and loins, so we aren't looking for a large collapse in the cutout by any means. Pork demand during May will also benefit from very high beef pricing and retailers will not have anywhere to turn in their efforts to escape high meat prices. We don't see the current demand strength in the pork market as simply a refilling of the foodservice pipeline. Sure, there may have been some moderate rebuilding of inventories by foodservice operations that are anticipating increased business as COVID-19 vaccinations increase and restrictions are lifted, but that would have been a brief event and not likely to be the primary factor causing the months-long strength in pork demand that we have witnessed. Instead, we think the demand strength is caused by a combination of a resurgence in high-protein diets among US consumers together with government stimulus money that has added to strong household savings during the pandemic and thus gives consumers the resources to upgrade their diets to include more animal protein. All of this means that this demand surge is not like the typical 2-3 month cycling of demand that we see in normal times. This demand surge is likely to last a lot longer than cycles in the past and should help keep pork price levels elevated above normal for at least a few more months.

Some have wondered if the recent strength in hog and pork prices has been caused by a surge in export demand. There have been a lot of rumors that China is ramping up its purchases of US pork due to a resurgence in its ASF case counts. Unfortunately, the export data that the government collects does not indicate any abnormal surge in export demand. The weekly export data has shown a mostly sideways pattern in pork exports over the past couple of months and the official monthly ERS export data points to Q1 pork exports being down about 7.5% from last year. Some observers have suggested that perhaps carcasses bound for China are escaping detection in the export numbers, but we think that is unlikely, especially in the monthly ERS totals. Movement to the Philippines has been very strong in recent months as ASF in that country has drastically reduced their domestic pork supply. Still, with the numbers that we see on regular basis, there is not much evidence to support the idea that pork exports are running abnormally high.

Seasonally-smaller **hog supplies will support pork prices into July**, and buyers should be prepared for the **cutout to remain over $100/cwt**

SUMMARY

The US hog and pork markets continue to exhibit very strong pricing as a result of extraordinary domestic demand and seasonal reductions in the hog supply. Both of those dynamics are expected to remain in place into July and that means that buyers will be dealing with stronger-than-normal pork pricing for at least that long, and perhaps much longer. A surge in corn futures has caused traders to bid up the deferred hog futures under the idea that high corn will eventually result in high hog prices. As a result, we see the fall and winter futures as being too rich and advise buyers not to extend forward pricing into the fall as a result. Taking coverage in May through July is encouraged, however. The supply side of the market is very well behaved at present, but both slaughter numbers and carcass weights are expected to decline of the next two months in a normal seasonal fashion. The main point of emphasis in this market continues to be extremely strong domestic demand. We see this demand strength as being different from the normal demand cycles that are typically observed in the pork market and it could last for several more months. **Table 1** provides our near-term price forecasts.

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Figure 1: Pork Cutout vs. Per Capita Domestic Disappearance, Apr

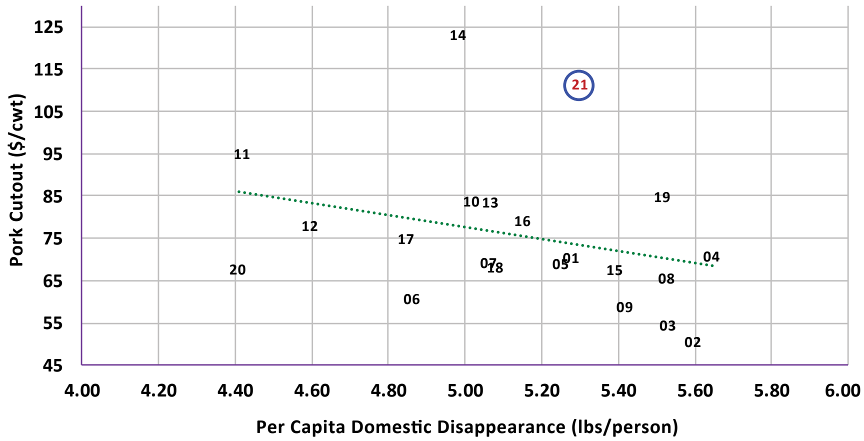

Figure 2: Pork Cutout

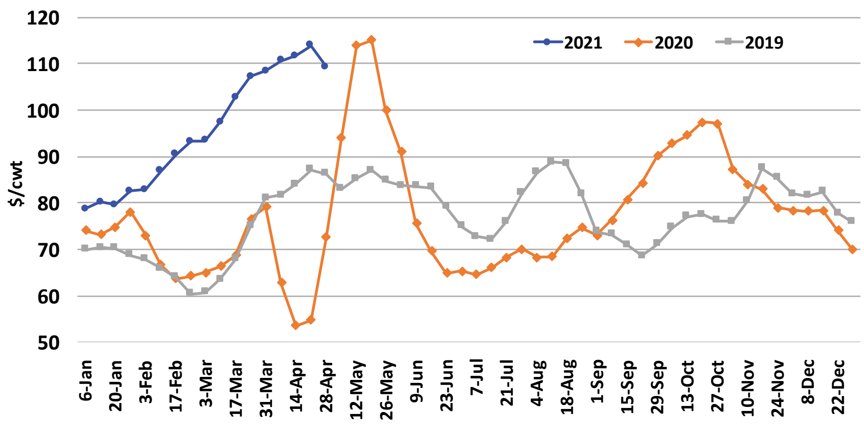

Table 1: JSF Hog and Pork Price Forecasts

	12-May	19-May	26-May	2-Jun	9-Jun	16-Jun
Pork Cutout	105.3	104.2	103.5	103.2	103.0	102.8
Loin Primal	94.2	94.0	93.1	92.2	92.7	92.2
Butt Primal	106.1	107.1	106.5	108.2	108.8	110.0
Picnic Primal	72.4	71.9	71.2	68.7	67.7	66.5
Rib Primal	243.8	245.0	242.2	237.5	232.1	226.0
Ham Primal	101.7	100.0	95.6	93.3	90.1	88.2
Belly Primal	145.0	140.3	146.0	151.1	155.6	160.0
Lean Hog Index	104.5	102.6	100.8	99.5	99.3	99.9

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