VOLUME 4, ISSUE 10
EN | FR | ES

J.S. FERRARO

THE MONTHLY

RED MEAT OUTLOOK: HOGS & PORK

OCTOBER 2021

The pork cutout trended lower through August and September after peaking in early August, but it now looks like that downtrend has run its course and the cutout may hold in a sideways-to-higher pattern for at least a few weeks. Stronger demand for hams and bellies are largely responsible for the turn around while the retail cuts seem to be content to tread water. Pork production is increasing in normal seasonal fashion and that will likely constrain the gains in the cutout as we move through October, but a smaller hog herd means that production will likely remain well below last year as we move through 2021 and into 2022. Packer capacity in the new tight-labor environment hasn't been tested yet, but very well could be in the next few weeks. If labor constraints prevent packers from killing all of the hogs as they become market-ready, then we could see packer margins swell in Q4 as negotiated hog prices drop while pork prices advance. So far, we don't see a lot of evidence in the weight data that hogs are being delayed in their date with destiny. USDA's recent *Hogs and Pigs* survey pointed to a much smaller hog herd than expected, with the summer pig crop down 6% from last year. If the government's numbers are correct, then hog supplies will continue to show big YOY declines at least through the first half of 2022. Those survey results energized futures traders, who have been busy revising their price expectations for 2022 upward. So far, we haven't seen a lot of panic on the part of pork buyers, but that is probably because they know we are currently in a market where hog supplies are expanding seasonally.

SUPPLY PICTURE

Hog slaughter is moving seasonally higher and should soon breach the 2.6 million head per week mark. Based on what was reported for the March/May pig crop, peak slaughter this fall is expected to be just a hair shy of 2.7 million head. However, slaughter in the Sep/Nov quarter has already failed to live up to the expectations set by the prior pig crop, so there is a pretty good chance that peak slaughter will fall short of expectations. That is important because we know that packers will be struggling to find enough labor to move the seasonally-large fall volumes through packing plants. Normally, the largest kill of the year comes either just before or just after the Thanksgiving holiday. This year, it is more likely to come before Thanksgiving because once December arrives, the industry will transition to the Jun/Aug pig crop which USDA just reported to be down 6% YOY.

> Peak kills this fall should be **just shy of 2.7 million head per week**

> USDA shocked observers by reporting the **Jun/Aug pig crop down 6%**

Dressed weights for barrows and gilts are now moving seasonally higher as hogs have access to freshly harvested corn and cooler weather, both of which promote weight gains. For the week of September 15, barrow and gilt weights averaged 208 pounds, which was dead on with 2019 and one pound under 2020. That implies that carcass weights are close to normal and are not indicative of hogs backing up in the pipeline. That could change quickly however, if packers struggle with the larger kills that need to be processed from mid-October onward. There are two things to watch for as indicators that the labor in plants is insufficient to slaughter all available hogs: carcass weights will rise rapidly and packer margins will grow at a much faster than normal rate. Currently, packer margins are near $35/head, which seems larger than they should be for this time of year and a hog supply of this size. It is possible that packers are already beginning to have problems getting all of the hogs slaughtered. That would be bullish for the price of pork but very bearish for the price of hogs. Industry participants would be wise to watch carcass weights and packer margins closely in the next few weeks.

While the information contained in this report has been obtained from sources believed to be reliable, J.S. Ferraro disclaims all warranties as to the accuracy, completeness or adequacy of such information. The information is not a recommendation to trade nor investment research. User assumes sole responsibility for the use it makes of this information to achieve his/her intended results. No part of this material may be copied, photocopied or duplicated in any form by any means or redistributed without the prior written consent of J.S. Ferraro.

© Copyright J.S. Ferraro. All Rights Reserved, 2021.

USDA released its latest issue of the *Hogs and Pigs* survey on September 24. Reported numbers in almost all categories were below the average of industry expectations, mine included. The breeding herd actually registered a small decline quarter-to-quarter when many were expecting to see an increase. The percentage of sows farrowing during the quarter was also reported to be unusually low, leading me to believe that perhaps problems with the PRRS virus were more widespread than initially thought. PRRS can cause sows to abort their litters, thus the low farrowing percentage. Whatever the cause, lower productivity gave us a Jun/Aug pig crop estimate that is down 6% from last year. Those are hogs that will be slaughtered in the Dec/Feb quarter, so buyers need to be prepared for additional supply tightness heading into the first half of 2022. The futures market reacted to the news by adding nearly $10 to the Dec and Feb futures in the days following the release of the report. It forced a significant downward revision in my supply estimates also and raised my price expectations through May 2022. Of course, supply is only half of the price equation. Demand will have some say in where prices go over the next few months.

DEMAND SITUATION

Domestic pork demand trended lower until about mid-September after peaking in early August. It now appears that demand has entered another upcycle and the combined packer+producer margin confirms this (**see figure 1**). So far, the boost in demand seems to be largely focused on the processing items — hams and bellies, although there have been some modest improvement in demand for the retail items. Even when demand was moving lower, it was still very strong by historical standards. That has been the case ever since the pandemic began and remains true today. I don't see any reason why that would change now. Industry participants need to get used to the idea that domestic pork demand is going to stay way stronger than in the pre-pandemic days for a long time to come. I do expect some demand fade if we can ever get the pandemic contained to the point where life in the US goes back to normal, but that seems a long way off in the current environment. Perhaps by next spring or summer normalization will be underway and that is when we might expect domestic pork demand to loose the luster that was applied by the pandemic. It is important to point out that this demand strength is not unique to pork. It seems to be present in every part of the economy, from shipping containers to real estate and everything in between, including pork and beef. Even when demand returns back to more traditional levels, buyers need to be prepared for pork prices to remain well above levels seen prior to the pandemic as packers and others in the supply chain will need to recoup their much higher labor costs. That will come in the form of higher prices for pork and lower prices for hogs. It is reasonable to expect the current upcycle in pork demand to last another six weeks or so, but that stronger demand will be met by seasonally increasing supplies, so the price impact will not be as large as it was this summer when supplies were declining.

International demand for US pork continues to weaken from the extremely strong levels we saw in 2020 and early 2021. High US pork prices have probably played a role, but a bigger factor is the recovery in the Chinese swine herd following the 2018 African Swine Fever outbreak. The Chinese have worked hard to contain the disease and rebuild their swine industry with less emphasis on backyard farms and more emphasis on commercial operations, which have better biosecurity. Chinese hog and pork prices are at very low levels presently and that limits their need to seek overseas pork. US producers are keenly aware of how important that Chinese business was and perhaps that is why they have been so reluctant to expand their herds here in 2021 even though profit margins have been outstanding. There could be a short-lived flurry of Chinese buying in October and November as buyers in that country anticipate the Chinese New Year and the Winter Olympics, which will be held in Beijing in early February. If that buying does happen, it will coincide with the upcycle in domestic demand and thus help support prices even further. Time will tell, but last week USDA did report a really big volume of new sales to China in their weekly export report (**see figure 2**).

SUMMARY

Pork buyers have grown accustomed to enjoying the lowest prices of the year in fall and early winter due to seasonally-large hog and pork supplies. That may be in jeopardy this year as supplies will increase less than normal due to exceptionally small pig crops earlier in the year and strengthening domestic demand as we move into Q4. Peak kills this year will be well under last year's level and cold storage stocks are already very low. That suggests the price-depressing effect of growing supplies will be muted this year compared to years past. Labor problems in packing plants raise the potential for packers to have difficulty slaughtering all of the available hogs this fall. So far, that hasn't been a problem but does bear close watching in the next couple of months. Rapidly increasing carcass weights and huge packer margins will be the first signs that plants can't manage the hog supply. Should that occur, it would strengthen pork prices and depress hog prices. Increases are expected for belly and ham prices through much of October, but the retail cuts probably don't hold as much upside risk. USDA recently reported the hog herd far smaller than expected and that has resulted in rather large upward adjustments to price expectations for Q4 and the first half of 2022. Export markets look a lot less rosy than they did last year at this time, but that won't be enough to offset the impact of strong domestic demand and pork supplies that are well below last year. **Table 1** provides our near-term price forecasts.

While the information contained in this report has been obtained from sources believed to be reliable, J.S. Ferraro disclaims all warranties as to the accuracy, completeness or adequacy of such information. The information is not a recommendation to trade nor investment research. User assumes sole responsibility for the use it makes of this information to achieve his/her intended results. No part of this material may be copied, photocopied or duplicated in any form by any means or redistributed without the prior written consent of J.S. Ferraro.

© Copyright J.S. Ferraro. All Rights Reserved, 2021.

Figure 1: Pork Supply Chain Margins

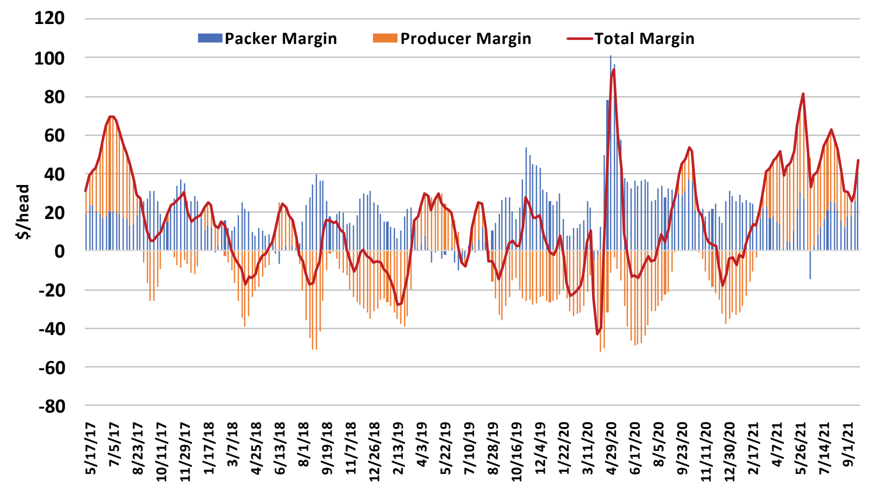

Figure 2: Net New Pork Sales to China

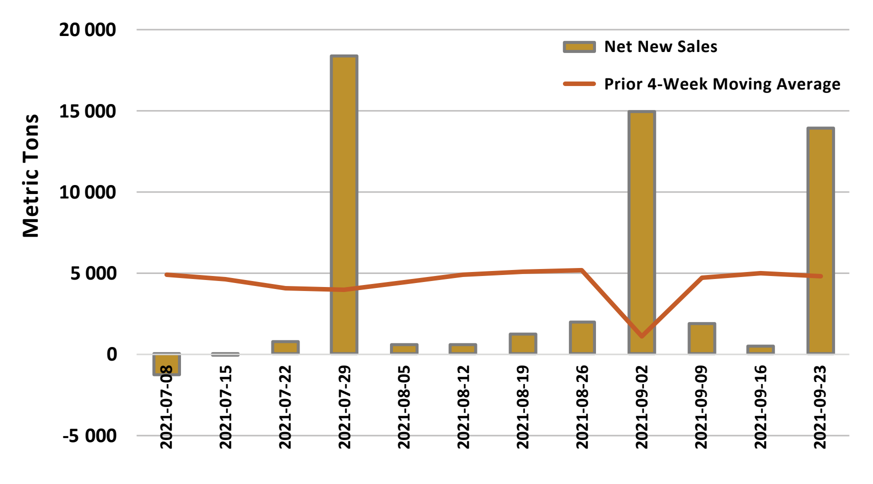

Table 1: JSF Hog and Pork Price Forecasts

	13-Oct	20-Oct	27-Oct	3-Nov	10-Nov	17-Nov
Pork Cutout	118.3	118.9	115.3	109.7	104.9	101.6
Loin Primal	111.2	109.2	106.0	101.2	96.1	92.2
Butt Primal	112.6	113.5	111.0	108.7	105.0	105.3
Picnic Primal	81.6	82.4	80.5	78.1	75.3	75.4
Rib Primal	137.1	134.6	134.5	135.4	136.8	134.6
Ham Primal	100.3	102.2	100.1	93.5	86.7	83.0
Belly Primal	216.6	220.4	209.0	195.2	188.0	179.3
Lean Hog Index	96.5	96.7	94.4	90.9	88.3	85.5

DR. ROB MURPHY BS, MS, PhD Agri Economics,
Executive Vice President, Research & Analysis,
J.S. Ferraro

E: Rob.Murphy@jsferraro.com

Dr. Rob Murphy is an agricultural economist and business leader with over 30 years in the industry. He has a wealth of experience in the North American meat and livestock industries studying, analyzing and predicting market movements.

SUBSCRIBE NOW to receive our monthly edition

While the information contained in this report has been obtained from sources believed to be reliable, J.S. Ferraro disclaims all warranties as to the accuracy, completeness or adequacy of such information. The information is not a recommendation to trade nor investment research. User assumes sole responsibility for the use it makes of this information to achieve his/her intended results. No part of this material may be copied, photocopied or duplicated in any form by any means or redistributed without the prior written consent of J.S. Ferraro.

© Copyright J.S. Ferraro. All Rights Reserved, 2021.