



J.S. FERRARO



THE MONTHLY RED MEAT OUTLOOK: HOGS & PORK

JANUARY 2022

The US hog and pork complex was stuck in a sideways pattern for much of December. Cash hog markets finished the month very close to where they began it and the pork cutout averaged \$85-86 for most of the month. USDA gave us another look at future hog supplies with the December edition of *Hogs and Pigs*. The supply picture going forward looks tighter than last year, but not tight enough to send prices spiraling back into triple digits. Demand is the biggest unknown going forward. Export demand from China continues to fade and that is creating worry among US hog producers. Domestic demand will be tested by surging COVID-19 infections as the omicron variant works its way through the population. However, this surge in infections may not create

Surging omicron infections could threaten plant throughput in early January

the same consumer response that we have seen in past waves because vaccines are now readily available and by all accounts the disease itself is less threatening than earlier versions. Very strong consumer demand for pork in 2021 rescued the industry from declining export prospects and gave hog producers their best margins since the PEDv crisis back in 2014. Pork packers also enjoyed a very profitable year. Extra strong demand often has the power to improve the fortunes of all segments in the supply chain and last year that definitely was true. It appears to us that the next move in the hog and pork complex will be up, but the strength of that move might disappoint those who witnessed the breath-taking rallies of 2021. After a year like we've just come through, a return to normalcy is likely to feel a little non-normal.

SUPPLY PICTURE

As the calendar rolled into December, the industry began harvesting the Jun/Aug pig crop, which USDA estimated to be down 6% from the year prior. So far, kills have been a little larger than what the pig crop implied, but not egregiously so. Now, after two holiday-shortened weeks, packers will resume a full schedule that should see total weekly kills in the 2.5 million head area. As the quarter progresses, kills are expected to fade back closer to 2.4 million head per week. Overall, barrow and gilt slaughter during the first quarter of 2022 is expected to be about 5.3% below last year, while carcass weights should run relatively close to last year. If we add in the impact from lower sow slaughter compared to last year, we could easily have total pork production down 7% in the first quarter of the year. The last time we had pork production post a 7% YOY decline was in Q3 and we all saw how high pricing got this summer.

Q1 pork production could be down as much as 7% YOY

Nearby corn futures are now trading above \$6/bushel and soymeal futures are in excess of \$400/ton. If those critical feed input markets remain elevated (and that looks likely), then hog producers could be looking at breakevens in the high \$80s and maybe even low \$90s for much of Q1. Given that the lean hog index is trading around \$72/cwt, this points to a pretty dismal quarter ahead for hog producers. Now of course, hog markets could advance during the quarter and the February futures contract is expecting about an \$9/cwt increase over the next six weeks. But even if that heroic feat is accomplished, it will still

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likely leave producer margins \$10-20/head underwater. That is not the type of environment that encourages producers to expand production. The market is sending signals to producers that caution is warranted in this period of stubbornly high feed costs.

USDA released its most recent survey results a couple of weeks ago and it showed the breeding herd nearly unchanged from last year and last quarter (see Figure 1). It is almost as if producers are in a holding pattern waiting to see if they have removed enough production potential in order to counter the loss of exports to China. The total number of swine in the US was reported down 4% YOY, but that is because USDA revised last year's totals upward. Without that revision, the total swine herd would have been down only 3.4% YOY. The most important number in the report from a supply perspective was the Sep/Nov pig crop, which was estimated to be down 3.6% YOY. Those are the hogs that will come to slaughter in the March/May quarter and thus we now say with some confidence that hog supplies will remain below last year during the first half of 2022.

DEMAND SITUATION

By now it should be clear to all observers that the pandemic, and the government stimulus that it spawned, has been a strong positive force for domestic pork demand. In the near-term, consumers are going to be faced with yet another surge in COVID-19 infections that could very well cause them to shift consumption away from foodservice and back toward the retail channel. If consumers adopt a stay-at-home mentality here in early 2022, it could result in another boost to domestic demand. However, this time around it is unlikely that the government will shower consumers with stimulus money. Instead, consumers will face high price inflation throughout the economy and very high retail pork prices in particular. That could make this next pandemic-driven boost in demand quite a bit weaker than what we saw in 2021. In addition, January always brings bills from holiday spending and it does look like US consumers were heavy spenders in late 2021. So, while we are optimistic for some rebound in domestic demand during January, we also recognize that there are some headwinds that might prove disappointing. Beyond the near-term surge in omicron infections, it is likely that pork demand will continue to erode as the government stimulus efforts fade further into the past. That longer-run effect is not unique to pork —

we should see a slow softening in demand for all meat proteins. As a result, even though pork availability is likely to be tighter than last year during the next six months, price levels could easily be well below last year due to a softer demand structure.

Not much has changed over the past month with respect to international demand for US pork. Movement to China continues to be way down from last year and the hole left by China's absence is too big for other countries to fill completely. USDA reported pork exports in October down 8.2% YOY and the weekly numbers make us think that the totals in Nov/Dec could be down 20% or more. At the same time, pork imports have risen considerably. Q3 saw a 36% increase in imports and the forecast looks for at least a 20% increase when the Q4 numbers become available (see Figure 2). So, both sides of the trade picture have been negative to prices, with exports down and imports strengthening. These are not trends that will likely turn on a dime, and so we see them continuing at least through Q1 and perhaps well into summer.

SUMMARY

Markets have been mostly sideways for a month or more, but we see the next move in prices as being higher. Hog supplies are well below last year, but not quite as tight as the summer pig crop suggested. So far, packers have been successful in keeping plants running smoothly, but the rapid spread of the omicron variant poses a risk to throughput over the next few weeks. USDA reported the Sep/Nov pig crop down 3.6% YOY and that solidifies the idea that hog supplies will remain tighter than last year at least into summer. Price improvement originating from the smaller hog supply should be at least partially offset by a softer demand structure in 2022 as consumers work through the savings that the pandemic has afforded them. In the near-term, omicron could cause some switching away from foodservice and back toward retail, but that might only last a few weeks. With vaccines and treatment therapies now widely available, consumers should be in a better position to weather this covid wave and thus we expect less economic dislocation that was seen with past waves. China's waning need for US pork has made it necessary to reduce the US swine herd and producers are now working through that process. Pork buyers can expect the cutout to average close to \$90 in Q1 as tight supplies provide support.

Table 1 provides our near-term price forecasts

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Figure 1: US Swine Breeding Herd, 2006-2021

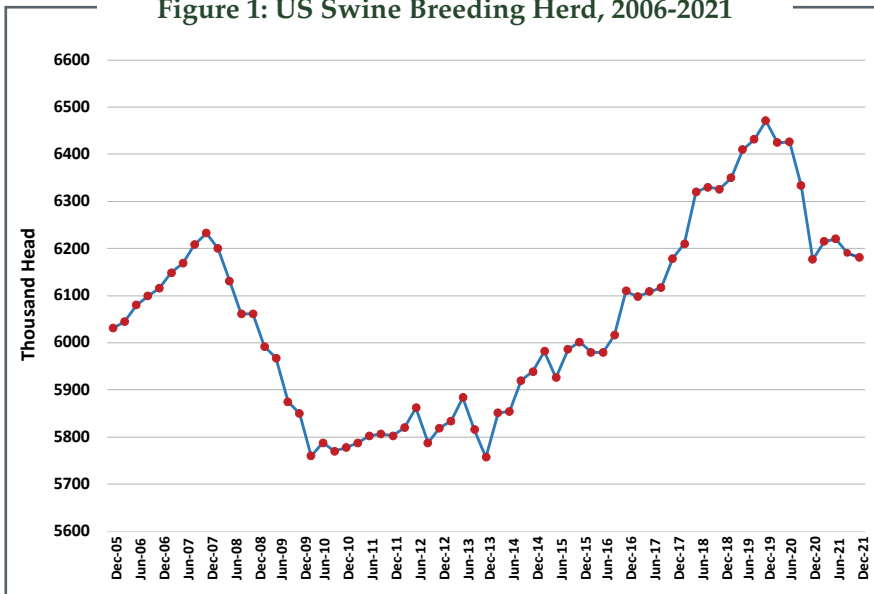


Figure 2: Total Pork Imports, Quarterly

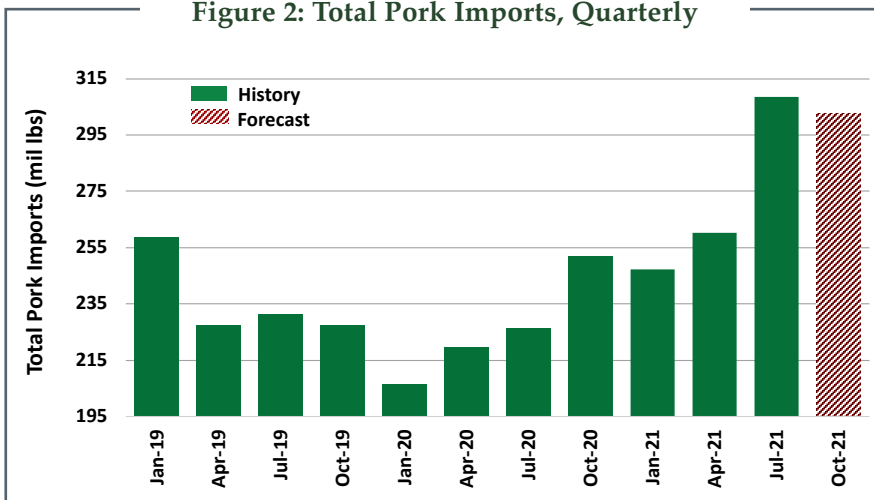


Table 1: JSF Hog and Pork Price Forecasts

	12-Jan	19-Jan	26-Jan	2-Feb	9-Feb	16-Feb
Pork Cutout	91.0	91.3	92.3	92.5	94.6	92.5
Loin Primal	85.6	84.8	86.6	87.5	86.6	86.0
Butt Primal	109.6	105.8	103.1	101.0	99.8	98.2
Picnic Primal	71.6	70.2	71.7	69.6	69.0	66.9
Rib Primal	151.2	150.2	148.8	150.1	147.8	147.5
Ham Primal	66.4	68.5	66.7	64.4	69.5	71.3
Belly Primal	144.3	148.2	155.7	162.1	170.7	158.5
Lean Hog Index	73.9	75.6	79.8	81.9	83.5	83.3



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