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WEEK ENDING MAY 13, 2022

THE PORK WRAP

After months of being stuck at roughly $105, the pork cutout finally moved lower this week, averaging $100.77. A downturn in ham prices combined with already soft belly prices to take $4.62 off of the cutout this week. While the cutout was moving lower, cash hog prices were moving higher. The WCB cash market added $2.42 this week and the National market added $4.06. That was a bad combination for packers and their margin dropped to -$2.70/head. That is the first negative margin since last June when bellies collapsed and pushed packer margins into the red for one week. Over the past three years, there have been very few weeks where packers were running with negative margins. My guess is that they will work quickly to try and correct this problem before it gets any worse. They did reduce the kill somewhat from last week's rather large level, but even so it still appears to be larger than what the pig crop implied. This week's kill was estimated at 2.38 million head, about 40k less than last week.

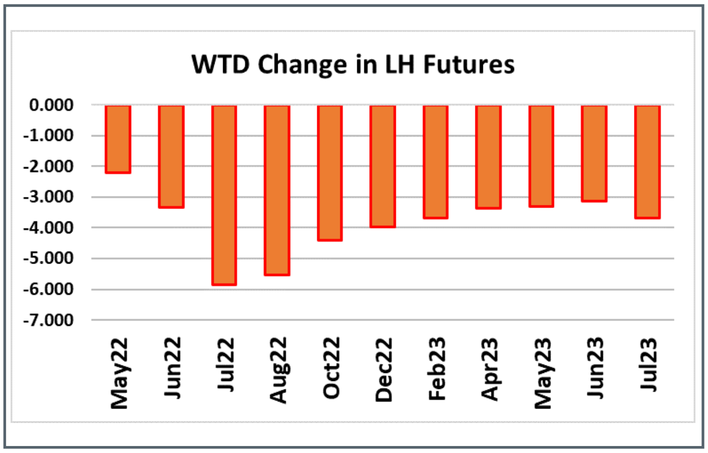
The attached chart indicates that was about 50k more than what was expected. There are two weeks left in the March/May quarter and it looks to me like the industry will over-kill the pig crop by about 200k. That's not a serious miss, but it could mean that kills during the upcoming Jun/Aug quarter will also run a little larger than expected. Barrow and gilt weights remain plateaued at 217 lbs and hopefully they will start to move lower soon. There have been some very warm temperatures in the Midwest recently and the forecast is calling for warmer-than-normal weather next week, so perhaps that will be enough to get weights started going lower. There will, of course, be a short kill in the first week of June to account for the Memorial Day holiday on May 30, but after that we should see weekly kills down below 2.3 million head until the end of July. Kills should rise seasonally in August and by the time the end of August arrives, we could have slaughter levels back up to 2.5 million head per week.

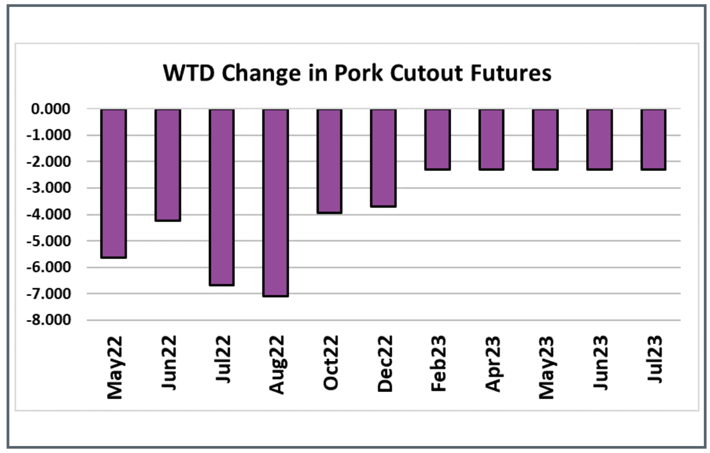
I mentioned that packer margins were negative this week, but it is important to note that producer margins were also negative by almost $3 per head. That means the combined margin pushed into negative territory this week for the first time since early in the year. The combined margin is pretty close to where it bottomed last time, so perhaps the demand softness has almost run its course for this cycle. The main concern demand-wise is still the bellies and hams. Hams clearly turned lower this week and the primal dropped almost $6/cwt. Bellies also posted some soft numbers this week, although there was an encouraging bounce in the primal on Friday. Hams I think will continue lower next week. Bellies, I'm not so sure, but it is too early to call them sharply higher. I want to see how they behave early next week. The loins, butts and pics all seem to be trading relatively steady and I'd guess that is likely to continue next week. The forecast has the cutout just a tad lower next week and then moving back up into the $105-110 range from Memorial Day onward.

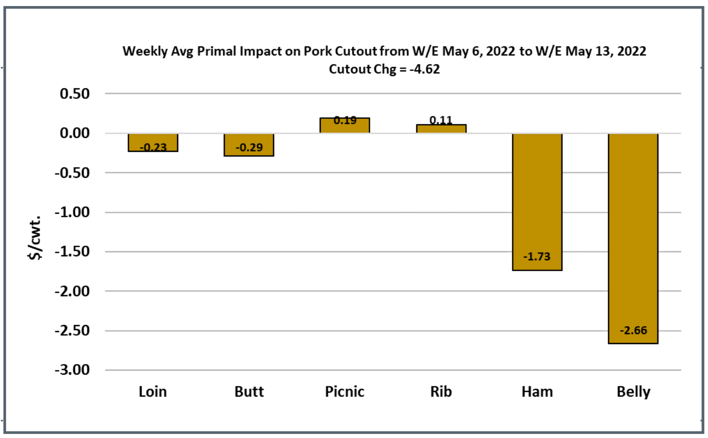
To get to that forecast, I'm assuming that the downcycle in pork demand is just about over and we will start to see seasonal reductions in pork production soon. Both of those should be good assumptions, but I'm more concerned about the demand side than what will happen to supply. It is possible that the hams will continue lower for longer than I imagine and thus keep the cutout depressed for longer. Even futures traders are starting to grow wary of the pork demand as they trimmed over $3 off of the Jun contract this week and $5-6 off of the July and August contracts. By now, it is clear that there is not a serious shortage of hogs that is going to cause price levels to skyrocket this summer. I'm projecting the cutout to average around $108-110 in June and July and the LHI getting back up to perhaps the $105-107 area.

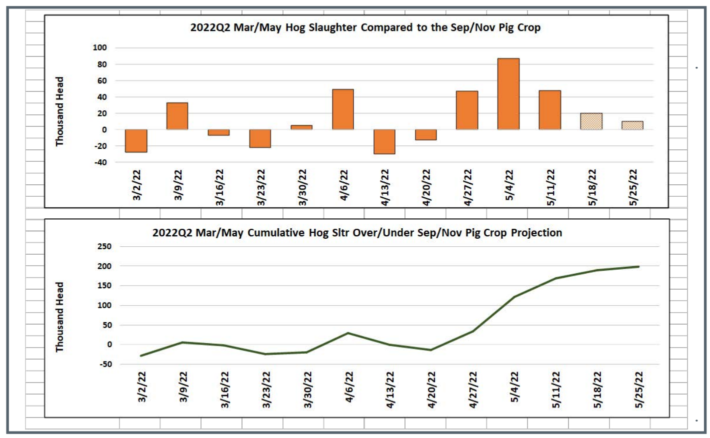
That's not a huge gain from today's levels and certainly well below what traders were thinking this spring when they ran the Jun hog futures up to $127. After running the futures up way too high and then getting burned as the cash failed to live up to expectations, I'd hope that futures traders will be more reserved this summer and resist the urge to become wild-eyed bullish just because the cutout moves up a few dollars. Further, there is the risk that packer's margin management efforts will be successful in pushing cash hog prices down enough to offset a lot of the benefit to the LHI from a stronger cutout. I think that the hog and pork complex will become more bearish toward the middle of July because demand typically sags after that and kills start to escalate. As a result, all of the contracts from Aug onward look too rich relative to my take on the fundamentals.

Export demand is still a lot softer than last year and with big imports also, it is likely that pork availability this summer will be around 2% larger than last year. If we throw in much softer demand than last year, then there is no reason to think that price levels will get anywhere near as high as they did last summer. Buyers would be wise not to extend coverage too far into the future as things get sorted out this summer. Corn prices remain very elevated and producers are dealing with strong price inflation in a lot of other inputs. That means breakevens will likely stay over $100/cwt for much of the summer. Producer profitability is likely to be much worse than what they have come to expect in the summer months and that could lead to further reductions in the breeding herd later this year. That is not necessarily bullish for price levels though, because demand is expected to be working lower through the balance of 2022 also. Next week, watch the bellies for signs that the bottom is in and also watch the hams because if the cutout moves lower, that will likely be the primal that is to blame.


WTD Change in LH Futures
0.000
-1.000
-2.000
-3.000
-4.000
-5.000
-6.000
-7.000
May22
Jun22
Jul22
Aug22
Oct22
Dec22
Feb23
Apr23
May23
Jun23
Jul23


WTD Change in Pork Cutout Futures
0.000
-1.000
-2.000
-3.000
-4.000
-5.000
-6.000
-7.000
-8.000
May22
Jun22
Jul22
Aug22
Oct22
Dec22
Feb23
Apr23
May23
Jun23
Jul23


Weekly Avg Primal Impact on Pork Cutout from W/E May 6, 2022 to W/E May 13, 2022
Cutout Chg = -4.62
$/cwt.
0.50
0.00
-0.50
-1.00
-1.50
-2.00
-2.50
-3.00
-0.23
-0.29
0.19
0.11
-1.73
-2.66
Loin
Butt
Picnic
Rib
Ham
Belly


2022Q2 Mar/May Hog Slaughter Compared to the Sep/Nov Pig Crop
Thousand Head
100
80
60
40
20
0
-20
-40
3/2/22
3/9/22
3/16/22
3/23/22
3/30/22
4/6/22
4/13/22
4/20/22
4/27/22
5/4/22
5/11/22
5/18/22
5/25/22
2022Q2 Mar/May Cumulative Hog Sltr Over/Under Sep/Nov Pig Crop Projection
Thousand Head
250
200
150
100
50
0
-50
3/2/22
3/9/22
3/16/22
3/23/22
3/30/22
4/6/22
4/13/22
4/20/22
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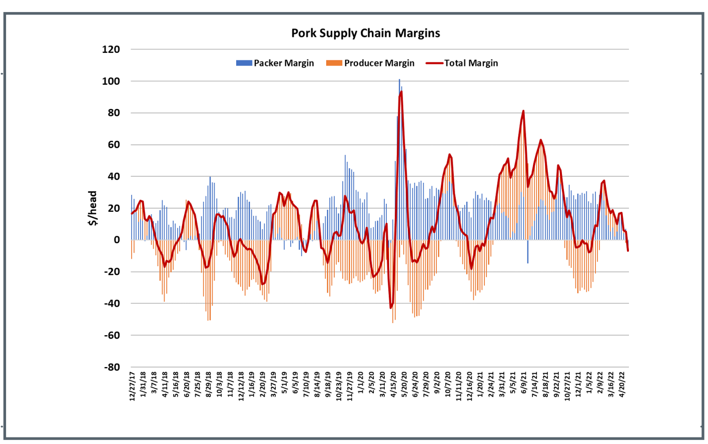
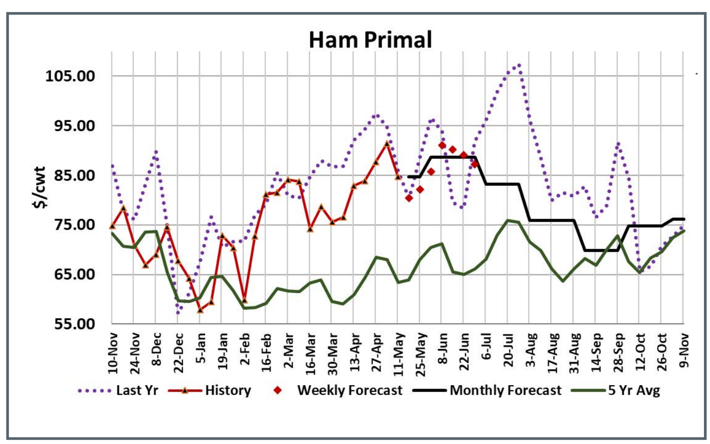
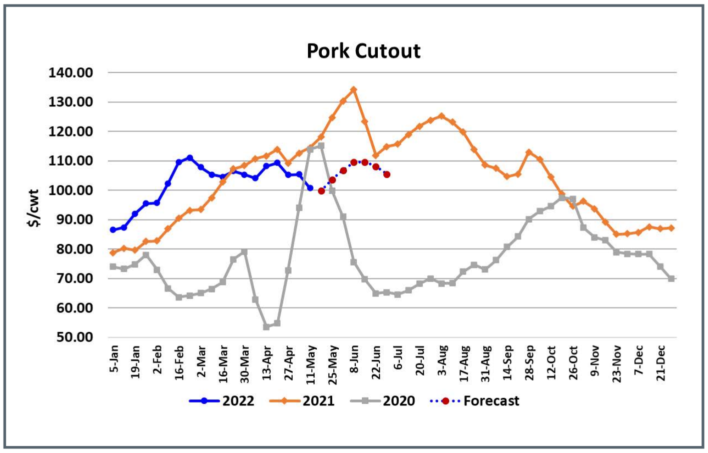
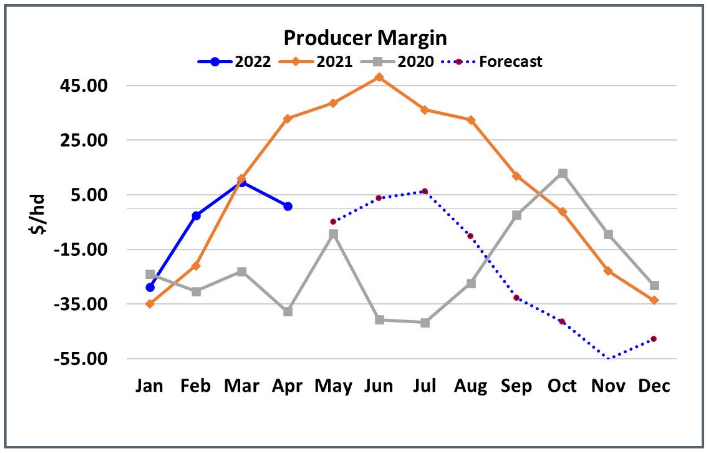
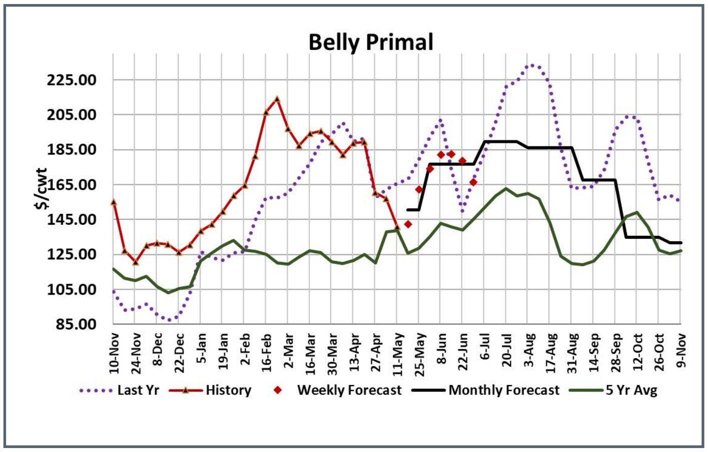
5/11/22
5/18/22
5/25/22


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


Ham Primal
$/cwt
105.00
95.00
85.00
75.00
65.00
55.00
10-Nov
24-Nov
8-Dec
22-Dec
5-Jan
19-Jan
2-Feb
16-Feb
2-Mar
16-Mar
30-Mar
13-Apr
27-Apr
11-May
25-May
8-Jun
22-Jun
6-Jul
20-Jul
3-Aug
17-Aug
31-Aug
14-Sep
28-Sep
12-Oct
26-Oct
9-Nov
Last Yr
History
Weekly Forecast
Monthly Forecast
5 Yr Avg







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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.