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THE MONTHLY

RED MEAT OUTLOOK: HOGS & PORK

JUNE 2022

With summer just around the corner, pricing in the US hog and pork complex is starting to firm up as is typically the case at this time of year. Reductions in the breeding herd over the past year or so have resulted in smaller pig crops and smaller pork production. Just a few years back, the industry added significant slaughter capacity with the aim of supplying overseas markets with cheaper US pork. That worked great when China was dealing with an African Swine Fever outbreak, but now that China has backed away from the US market and hog production costs have soared, packers are having to deal with a hog supply that is too small for the slaughter capacity that exists. They are forced to compete more aggressively for the hogs that are available and that is now starting to pinch their margins. Negotiated hog prices have been slowly rising since mid-April and are likely to continue on an upward trajectory through June. The cutout has also moved a little higher, but packers are faced with a much softer demand environment than they experienced last year, so the potential for sharply higher pork prices is limited. Currently, packer margins are running about $4/head, which is well below the $22/head margins seen last year at this time (see **Figure 1**).

Packer margins squeezed down to $4/head as packers chase hogs to utilize capacity

Corn prices have pulled back a little recently, but the US crop is not yet fully planted and there will be plenty of opportunities for weather cause concern over the next few weeks. Even though negotiated hog prices are relatively firm right now, hog producers are struggling to cover their input costs and we calculate producer breakevens to be near $103/cwt currently. That is almost the same level as the Lean Hog Index, which measures what packers pay for hogs and thus hog production margins are very near zero. That isn't likely to encourage expansion in the next few months.

Very high input costs have pushed hog production **breakevens over $100/cwt**

SUPPLY PICTURE

Hog slaughter is now trending lower in normal seasonal fashion and should reach a low point near the end of June or early July. Last week's swine kill registered 2.35 million head and was about 1.1% smaller than last year at this time. However, the kill has been declining a little slower than normal and in the past four weeks the kill has actually been higher than what the Sep/Nov pig crop implied. For the March/May quarter that just ended, when we compare actual slaughter with what the Sep/Nov pig crop suggested, we find that USDA probably under-estimated that pig crop by about 340,000 head when they did their survey back in December. That's not a huge miss, but it does suggest that perhaps the summer kill will also be a little larger than the 1% YOY decline that USDA's March survey indicated. We expect the smallest non-holiday kill of the year to be right around 2.25 million head in late June.

Barrow and gilt carcass weights have been a little slow to come down this year and are currently plateaued at 216 pounds. The weather in the Midwest production regions has moved back and forth between hot and cool and we haven't seen the prolonged periods of hot weather that normally cause pigs to eat less and thus gain less. Those conditions are more likely from mid-June to mid-August. At this point, there is nothing in the data that would suggest that the hog production pipeline is too full or too sparse and thus we feel pretty confident that the flow of hogs this summer will not create a lot of surprises. Even though the hog kill is expected to be down about 1.5% YOY during the summer, much softer export markets and strong imports make it likely that overall pork availability in the domestic market will be nearly the same or perhaps even slightly larger than what was experienced last summer (see **Figure 2**).

High corn and soymeal prices are likely to be with us for a long time given that the war in Ukraine has no end in sight and fertilizer shortages are reported in many parts of the world. In addition, extreme weather events seem to be much more common than they were just a few years back. Drought is a major risk for crop production in the US this summer. In addition to feed, labor and energy costs have skyrocketed for pork producers. In this high-cost environment, producers are finding it hard to turn a profit and thus there is very little reason for them to expand. USDA will release its next *Hogs and Pigs* survey on June 29 and we expect that it will show the breeding herd almost unchanged from March 1 and about 2% lower than last year. With some modest productivity increases, that suggests that the Jun/Aug pig crop could be down about half a percent. Those are the hogs that will come to market from December through February. In early fall (Sep/Nov), packers will be slaughtering the March/May pig crop which was reported to be down 1% YOY. Thus, it seems reasonable to expect hog slaughter to be down around 1% YOY for the balance of 2022. If we are wrong, it could be that the breeding herd on June 1 is down more than expected and thus production late in the year could also be smaller than expected.

DEMAND SITUATION

Domestic pork demand remains relatively good, but not nearly as good as it was last year at this time. As with beef, we believe that pork demand is on a longer-term downward trajectory as it retraces from very high levels during the two years of the pandemic. This will likely be a slow process and there will still be small cycles in demand every month or two, but by the end of the year we expect to see our demand indexes registering much lower than they are today. Retail pork prices are very high right now and that is an impediment to consumption. Further, retailers are unlikely to lower prices until production stops shrinking in July and starts to expand. That is a two-month roadblock that could cause retail movement to slow and wholesale pork prices to be lower than they might be otherwise. The one product that has the most potential for stronger demand this summer is bellies, which typically benefit when meals away from home are increased and it is our sense that Americans will be doing a lot of traveling this summer. Items that typically take many hours to smoke on a backyard grill such as butts and ribs are more likely to see softer demand simply because fewer people will be seeking fill time at home now that COVID-19 concerns have eased. The Federal Reserve will be actively raising interest rates throughout the balance of the year to combat price inflation and that may tip the economy into a recession at some point. Pork demand generally fares better than beef demand in recessions, but it wouldn't be completely unscathed. Finally, USDA reported last week that pork stocks in cold storage are increasing and may soon be back to pre-pandemic levels. Those larger stocks will be used to provide more buffer against high prices. Buyers will likely find pork pricing this summer to be much more to their liking that what they experienced last year.

Pork exports continue to track well below last year and the main culprit is China's lack of interest. China is struggling to contain COVID-19 outbreaks with lockdowns and that has a demand-depressing effect. It has also snarled traffic at China's ports, which makes Chinese buyers less enthusiastic about importing pork from abroad. Fortunately, Mexico has been an aggressive buyer of US pork this year, with shipments up 42% in Q1. That growth is encouraging, but it isn't nearly enough to make up for the lost business with China. The YOY comparison for exports will get much easier in July through December because that is when exports started to drop off last year. In fact, we are currently forecasting exports in the second half of 2022 to be up 6% YOY.

SUMMARY

Summer is typically the pork industry's strongest pricing season of the year. We think that will be the case again this summer, but don't expect pricing to be nearly as strong as last summer when the cutout averaged over $121/cwt in June through August. Our forecast is for the cutout to average about $106/cwt this summer, with the strongest pricing early and weaker pricing from mid-July through August. Pork production is likely to be down about 1%, based on prior pig crop surveys, but because exports are expected to be a lot softer this year and imports larger, actual pork availability per person might be up slightly this summer. Domestic demand faces a number of headwinds, not the least of which is retailers' reluctance to lower their selling prices while pork production is still declining. Price inflation across the economy is forcing consumers to make more difficult decisions about what they purchase, and pork will likely see softer demand as a result. The risk of a recession looms for later in the year as the Federal Reserve raises interest rates to help quell inflation. That too, would be a negative for pork demand. Hog producers are struggling with high input costs and may find it difficult to make meaningful profits this year. That would likely lead to further downsizing of the herd and higher pork prices down the road, but not until 2023. Hog and pork prices are expected to work moderately higher through June, but the rate of increase should be much less than last year. Buyers are encouraged not to extend coverage beyond mid-July because by then production should be increasing and demand softer than at the beginning of summer. **Table 1** provides our near-term price forecasts.

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Figure 1: Packer Margin

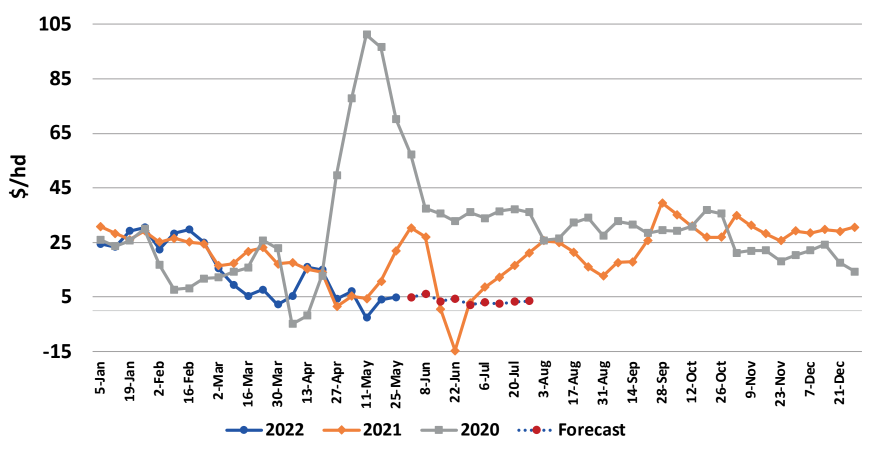

Figure 2: Per-Capita Pork Domestic Availability
(shaded is forecast)

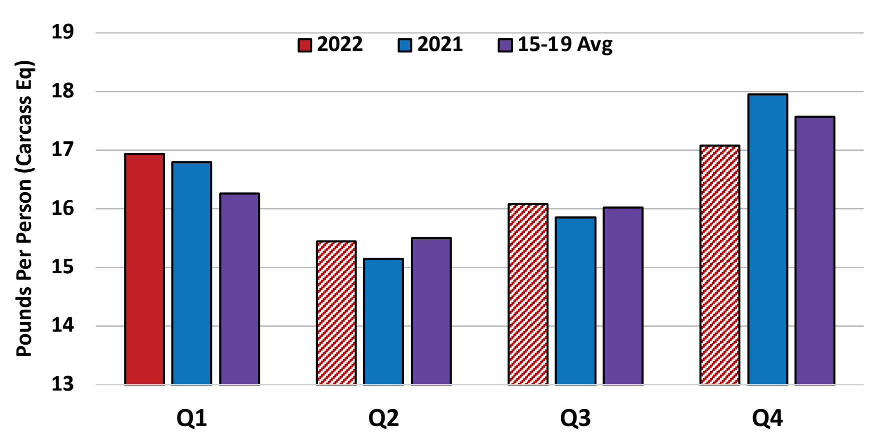

Table 1: JSF Hog and Pork Price Forecasts

	8-Jun	15-Jun	22-Jun	29-Jun	6-Jul	13-Jul
Pork Cutout	112.5	112.4	110.9	108.2	108.1	110.3
Loin Primal	104.3	104.4	103.3	103.5	102.4	101.6
Butt Primal	115.4	115.7	117.2	115.3	116.6	117.7
Picnic Primal	72.6	70.1	68.4	68.6	68.4	70.2
Rib Primal	190.7	182.1	180.6	175.9	169.3	166.6
Ham Primal	94.3	92.3	90.4	88.3	85.4	82.1
Belly Primal	192.3	198.9	194.8	182.8	189.3	208.3
Lean Hog Index	108.6	109.8	107.9	106.2	105.7	108.1

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