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RED MEAT OUTLOOK: HOGS & PORK

Pricing in the US pork complex has been mostly sideways for the last three months, with the cutout averaging in the $105-106/cwt range in February, March, and April. There have been brief trips above $110 and down to $100, but in general the cutout has been amazingly stable (see **Figure 1**). The Lean Hog Index, which measures the national average price paid for hogs, averaged $101/cwt in both March and April. The failure of the market to advance as the weather warmed in April has caused some to wonder if pork demand is losing its luster. It has also forced traders in the futures market to re-evaluate some of the very strong premiums that had been placed on the summer futures contracts earlier this year. The June futures, which had traded as high as $127/cwt during March, recently saw steep declines that now has the contract valued closer to $105/cwt. Hog supplies are slowly tightening in normal seasonal fashion and that will result in progressively smaller pork production from now until midsummer. Normally, that results in a very reliable upward trend in prices through May and June, but this year the softening of demand may make those seasonal price gains a lot smaller than in years past. The market continues to see daily volatility in negotiated hog prices as a result of disease problems earlier this year, but warmer spring and summer weather is expected to reduce disease spread and its impact should minimal going forward.

> **The pork cutout** has been range bound **near $105-110** for nearly three months now

> Traders have significantly scaled back expectations for summer prices, pushing the **Jun futures down below $105**

SUPPLY PICTURE

Weekly kills during the March/May quarter so far have tracked the prior pig crop very closely. That has alleviated some of our concerns that perhaps disease would severely limit hog supplies this spring and thus send prices soaring. Weekly average slaughter during April was close to 2.4 million head and is on track to average around 2.3 million head per week in May. June is likely to see kills average around 2.25 million head per week. In general, the slaughter pipeline appears to be operating as expected for this time of year. Hog supplies are a bit tighter than they were last year at this time, but they are not so tight as to cause significant availability issues. In fact, we estimate that because of sharply reduced exports this year, per capita availability during the May-July period will be close to 2% higher than last year.

Hog producers have seen no relief in input prices over the past few months. Nearby corn futures have traded over $8/bushel recently and that has pushed hog breakeven prices over the $100/cwt mark (see **Figure 2**). Given that the Lean Hog Index has recently held in the $101-102/cwt range, it is easy to see that producer profit margins are very near zero. Producers are caught between rising input prices on one side of their profit equation and falling pork demand that has tempered output prices on the other side of the equation. We don't really expect much relief from high input prices over the next few months and so if producer profitability is going to improve it will need to come from higher hog prices. Barrow and gilt carcass weights are currently plateaued near 216 pounds but should soon start trending seasonally lower toward a bottom in early July. There is nothing unusual in the weight data that would suggest supplies in the hog pipeline are either burdensome or tight.

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Longer-term, if grain markets remain elevated at these levels producers will struggle to remain profitable and that would likely lead to further reductions in herd size. Eventually, declining pork production would lift hog and pork prices to a level that allows for improved profits in the hog production sector. Over the past couple of years, producers have been trimming back the herd in response to declining export demand, but now it looks like high feed costs and inflation in other input prices could continue that trend for several more quarters. The hog supply is largely fixed for the next 6-9 months and so pork buyers can remain relatively confident that no big supply surprises lie on the horizon. Domestic production will be down from last year during the balance of 2022, but smaller volumes entering export channels will, at times, render domestic pork availability larger than it was last year.

DEMAND SITUATION

It is our belief that domestic pork demand has benefited in early 2022 from consumers trading down from beef as their budgets became stretched by high price inflation across a wide range of items that they purchase. However, signs are beginning to emerge that consumers are now trading down from pork to even lower-priced proteins. We look for that trend to continue, and possibly even accelerate as we move toward summer and beyond. Retail pork prices remain very high and that has had the effect of limiting consumption and thus allowing more product to flow into cold storage recently. During the pandemic, users kept cold storage stocks very low because potential covid restrictions created a lot of uncertainty that made stock holding a much riskier proposition. Now that the pandemic has faded, users are building stocks once again and that will provide a bigger buffer against high prices going forward. Last year at this time consumers were flush with cash due to direct payments from the government, but there are no such payments now and consumers have largely spent all of last year's windfall. Further, retail pork prices are about 15% higher than they were last year at this time. Perhaps the most important headwind for pork demand is that consumers are simply less interested in cooking at home now that all COVID-19 restrictions have been lifted, allowing them to focus more on other activities. This process of reducing pork demand back to more-typical levels following the pandemic is likely to take many months to play out, but it seems to be underway now. Slowly declining demand over the balance of 2022 will likely help to offset some of the upward pressure on prices that is expected from smaller YOY pork production as producers reduce the size of their herds.

Not much has changed with respect to international demand for US pork. The latest government figures for showed February exports down 18% and we look for even bigger declines when the March numbers are released later this week. In fact, our forecast has pork exports during the first six months of 2022 down almost 20% from last year. That is a huge loss for the industry, and it will force more product to clear through domestic channels this year. China remains the weakest link in the export picture, with YOY volume falling close to 70%. Mexico has picked up some of the slack, but it cannot fully make up for all of the movement lost in China. We don't see anything promising on the horizon that would suggest that pork exports should improve vastly as we move deeper into the year. In fact, there is concern that exports will slip further as recession starts to grip parts of the globe in response to the war in Europe. That war has started to alter pork trade flows, but it doesn't seem to be increasing overall demand for pork out of North America.

SUMMARY

Hog and pork prices in the US have been relatively steady over the past couple of months as smaller supply has been offset by modestly softer demand. Export demand is way down from last year and that may be the difference-maker that is keeping wholesale pork prices in check. Concern over possible disease issues in the herd is starting to ease and warmer weather makes it less likely that any existing disease problems will worsen. Our fundamental analysis suggests that price levels should work higher during May and June as kills decline seasonally, but the increases are not expected to be large and should be well below the levels of last summer. Inflation in the macroeconomy continues to be a headwind that could limit consumer spending on pork this summer. We look for consumers to continue to move back down the protein ladder in coming months and begin to substitute cheaper proteins for pork. The prospect of a recession later this year is growing. US equity markets have been in decline recently and the Federal Reserve is in the process of raising interest rates in an effort to tame inflation. Buyers are urged not to extend forward purchases too far into the future because the potential for some fallout from problems in the macroeconomy could reduce demand further, while the risk of substantially higher prices will be limited by larger cold storage stocks. In general, buyers should find this summer's pork market much more palatable than the one they experienced last year. **Table 1** provides our near-term price forecasts.

Figure 1: Pork Cutout

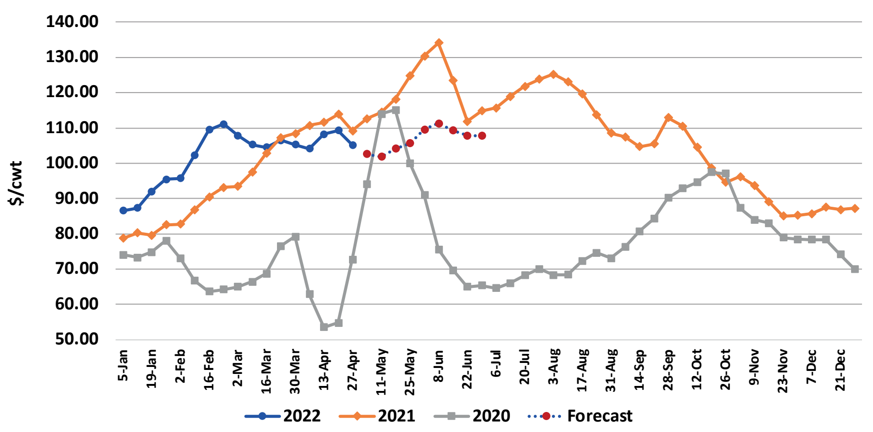

Figure 2: Hog Producer Breakeven Price

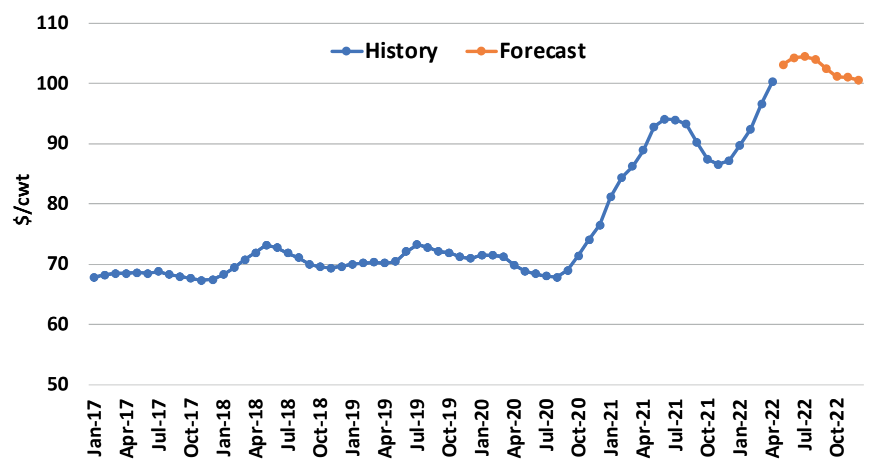

Table 1: JSF Hog and Pork Price Forecasts

	11-May	18-May	25-May	1-Jun	8-Jun	15-Jun
Pork Cutout	101.9	104.1	105.7	109.6	111.3	109.3
Loin Primal	97.7	100.3	101.1	102.8	105.2	105.7
Butt Primal	115.9	112.5	112.2	114.0	111.9	112.2
Picnic Primal	63.5	61.3	62.8	65.2	66.5	68.2
Rib Primal	195.2	193.6	191.2	192.5	186.3	182.2
Ham Primal	81.8	81.7	81.1	83.5	84.6	83.7
Belly Primal	161.3	176.2	185.1	200.3	207.3	194.3
Lean Hog Index	99.0	100.8	102.3	106.8	108.8	107.3

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