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WEEK ENDING JUNE 3, 2022

THE PORK WRAP

The hog and pork complex continued along its upward path this week, with the cutout adding $2.45/cwt on a weekly average basis and the NDD negotiated hog market gaining $3.15. Negotiated hog prices are rising because of the seasonal tightness in the hog supply that is causing packers to have to dig a little harder to fill their kill schedules. Although some packers are probably better off than others as far as having their kill needs met, we have seen some days where over 20k head have traded in the spot market. If packers had all of their formulas based on the negotiated market, then they would be in the red right now because that market is running about $4-5 over the cutout. As it is, a good chunk of formulas are based on the cutout and that is helping to keep the LHI just a few dollars under the cutout and keeping packer margins slightly in the black. I calculate this week's margin at $7.50/head, up about $3 from last week.

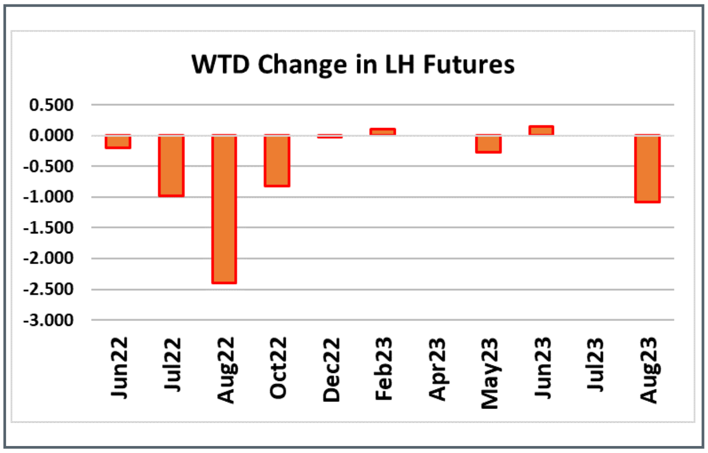
I wouldn't expect margins to get much better than that for the next several weeks and they very well could move lower. The stronger negotiated market and cutout from this week has yet to be fully reflected in the LHI, but if both stayed where they are as of Friday afternoon, the LHI would be worth about $107.50. The Jun futures settled today at $110.20, so clearly market participants are expecting further advances in the cutout and negotiated markets over the next seven trading sessions before the contract expires. I think the Jun futures are a little overdone at this point and see expiration coming in the $108-109 range. The Jul and Aug contracts have been careful not to get too far ahead of Jun so far. Pork demand remains in a small upcycle, as evidenced by the attached combined margin chart, but longer-run I think it is still in the process of reverting back to pre-pandemic norms. The gains in the cutout this week were generated mostly by the retail primals, with the exception of ribs, which show a strong seasonal tendency to peak near Memorial Day and then work lower.

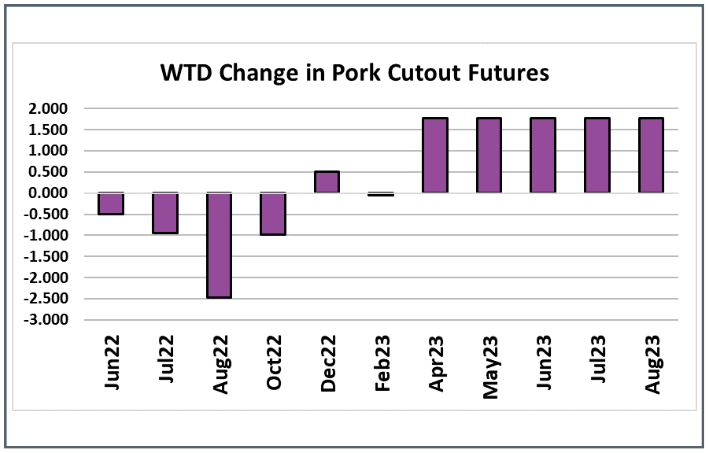
The belly primal did a lot of bouncing around this week, but in the end, it produced an average not far different from the previous week. Hams are the star players of the processing market right now and we are seeing bone-in heavy hams regularly trading over $90/cwt. The excess premium for boneless hams that was a market characteristic during the pandemic has largely dissipated now and that suggests that packers have their labor force back in good shape. As usual, the hams and bellies will likely drive any big moves in the cutout in coming weeks. I'm forecasting both higher, which means there should be some additional appreciation in the cutout. The strength in hams may only have another week or two to run, but the bellies could stay on an upward trajectory into the first part of July. Right now, the forecast has the cutout topping in the $113-114 range (weekly average) sometime around mid-June. That might also mark the top in the combined margin. From there, I think the cutout holds in a mostly sideways to slightly lower pattern until mid-July.

By then, we should be back into another downcycle for demand and hog supplies should be increasing slightly. That makes me think that pricing in the hog and pork complex will be much softer in August than in the June/July period. I look for the cutout to average around $103 in August, down from a $111 average in June. Interestingly, futures traders are currently valuing the Aug pork cutout futures about $1.50 over Jun. This week's kill came in at 2.04 million head, with packers killing 145k on Saturday to help make up for the missed production on Memorial Day. Going forward, we should expect very small Saturday kills outside of holiday weeks until the end of July. This week's kill was larger than the pig crop projected, but goofy things happen around holidays with the pig crop projected kill, especially when the holiday fall right at the end of one quarter and the beginning of another.

The problem stems from which week the holiday falls in, so I don't want to read too much into this week's apparent over-kill. Let's see what happens next week. Barrow and gilt carcass weights were reported another pound lower this week and they do appear to be trending lower now in normal seasonal fashion. The DTDS weight calculation isn't pointing to any problems in the hog production pipeline at the moment. Nearby corn futures have come down about $0.75/bushel since late April, but cash corn prices in Iowa have not fallen as fast as the futures. Back in April cash prices were solidly under the futures and now they are almost on par with them. Producer breakevens are still clocking in at around $103/cwt and since the LHI is now approaching $107, there is a small positive profit on the table for producers. However, the $4 margin they are making this year is a far cry from the $45 margin they collected in the first week of June last year. The difference can be traced to weaker demand and higher feed prices.

Producers are likely not in any mood to expand right now and I'd be surprised if the breeding herd is any larger than where it was back in March when USDA reports their survey results on Jun 29. Export markets for pork continue to track in a mostly sideways pattern and well below last year. Cold storage stocks are on the rise and that is likely a sign of users feeling more confident about holding larger stocks now that much of the pandemic uncertainty has been resolved. Those larger stocks should help provide a buffer against sharply higher prices this summer. Next week should be a good one for the cutout, with hams and bellies providing most of the support and the retail items cooling off a bit. Also, it is always important to keep an eye on the weather at this time of year because if a heat dome builds over the production regions in the Midwest it can cause hog weight gains to slow and thus tighten the hog supply further. Right now, the weather forecast doesn't seem to point to that type of an event, but weather forecast can often change faster than a pork belly price forecast, so stay alert.


WTD Change in LH Futures
0.500
0.000
-0.500
-1.000
-1.500
-2.000
-2.500
-3.000
Jun22
Jul22
Aug22
Oct22
Dec22
Feb23
Apr23
May23
Jun23
Jul23
Aug23


WTD Change in Pork Cutout Futures
2.000
1.500
1.000
0.500
0.000
-0.500
-1.000
-1.500
-2.000
-2.500
-3.000
Jun22
Jul22
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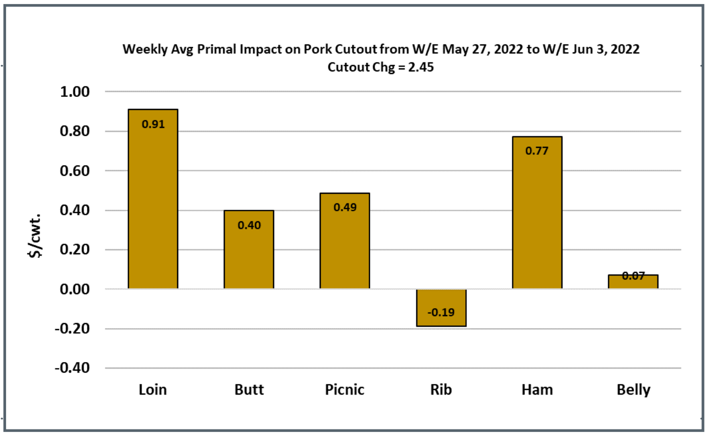
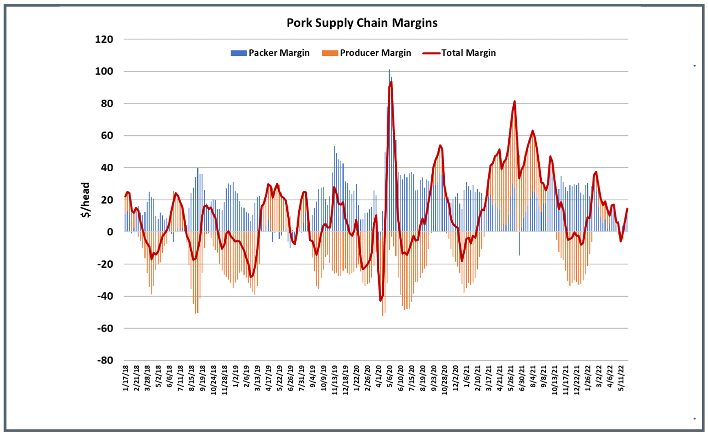
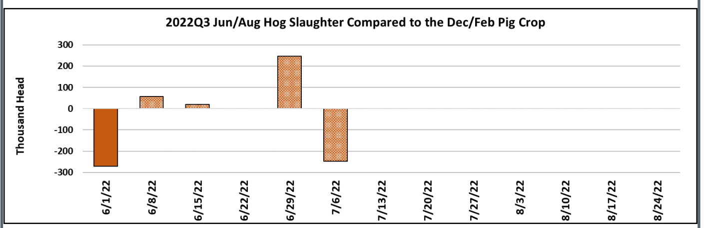
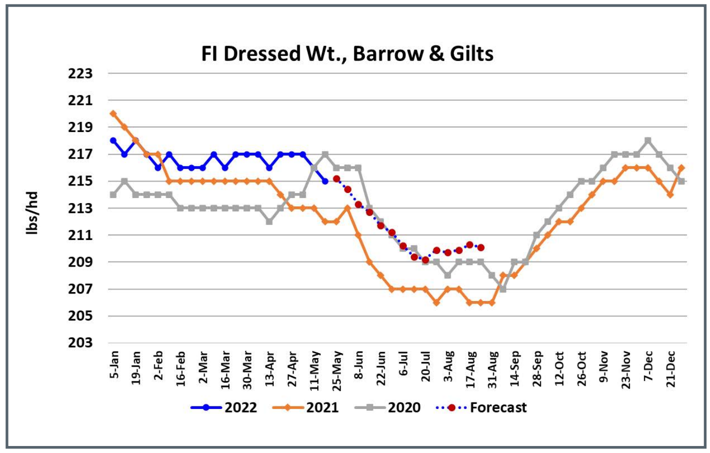
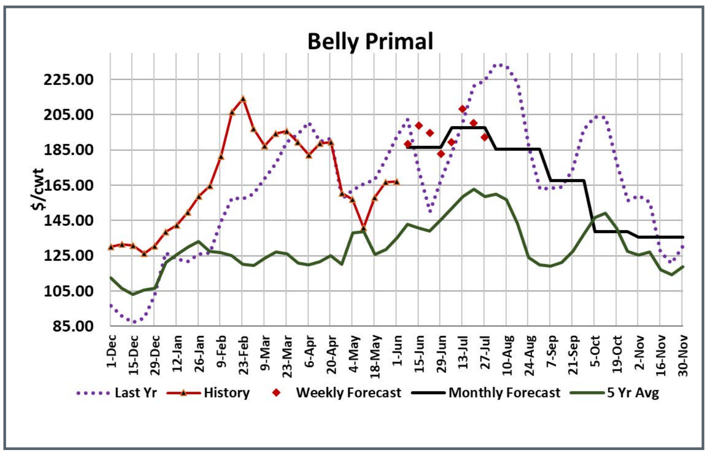
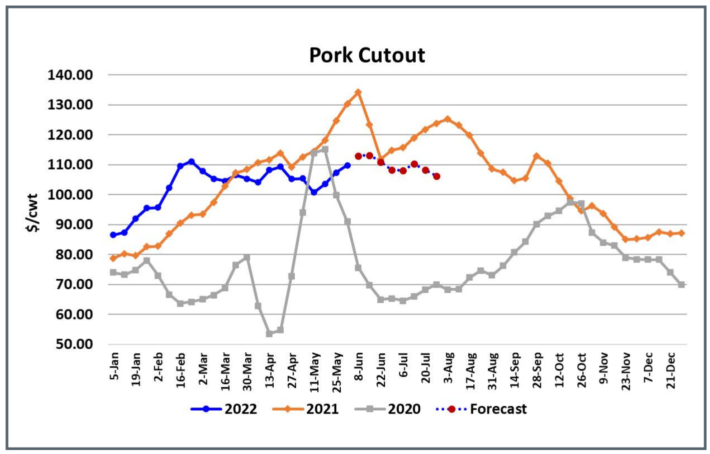

Weekly Avg Primal Impact on Pork Cutout from W/E May 27, 2022 to W/E Jun 3, 2022
Cutout Chg = 2.45
$/cwt.
1.00
0.80
0.60
0.40
0.20
0.00
-0.20
-0.40
0.91
0.40
0.49
-0.19
0.77
0.07
Loin
Butt
Picnic
Rib
Ham
Belly


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









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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.