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WEEK ENDING AUGUST 19, 2022

THE PORK WRAP

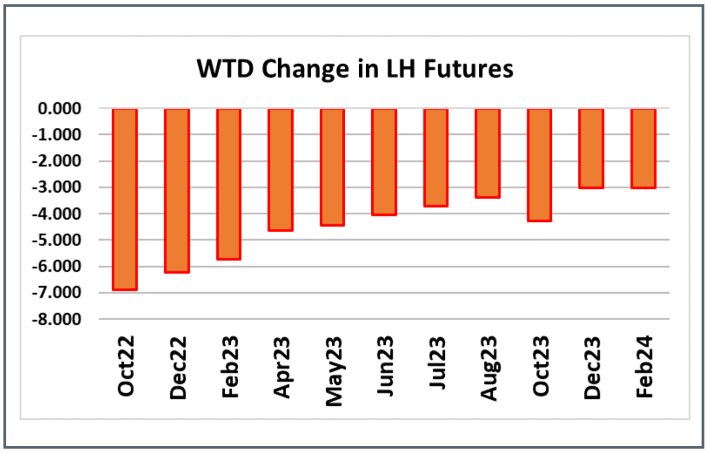
The hog and pork complex continued to ease lower this week as the cutout dropped $3.02/cwt and the WCB negotiated market was down $3.32/cwt. The losses in the cutout were largely driven by big declines in the belly primal. Hams also moved a little lower, but the downtrend there seems to be slowing. Perhaps the most surprising event this week was the collapse of the Oct futures, which lost close to $7. It is not unusual for the next nearby contract to make a big move around the time when the front month expires, but I had assumed that move would be upward this time because of the large gap between the LHI and the Oct contract when the Aug expired. Instead, traders sensed that a top had been made in the cash market and the fear of a rapid price decline created a lot of selling pressure in the futures. That futures selloff took the Oct contract down close to my forecast for the LHI at Oct expiration, so it is now very close to fair value.

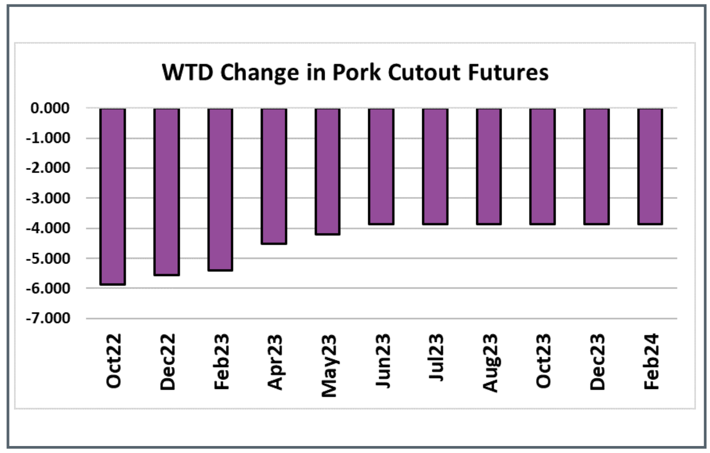
However, I think the risk to that forecast lies to the upside and could easily see the Oct contract expiring $5-10 over the $93 level where it traded today. The combined margin continued lower this week, helping to confirm that a new downcycle in demand is firmly in place. If you look closely at the combined margin chart, you will see that hog producers are the ones making all of the money in the current market and packers actually posted a small negative margin this week. That gives you an idea of who has the upper hand in this market: producers. The supply of uncommitted, market-ready hogs remains very tight and as a result, packers continue to pay a lot for the spot hogs they need to fill out their kill schedules. It is that tight supply of uncommitted hogs that makes me think prices in the hog and pork complex won't decline as fast as the futures wanted to imply this week.

Of course, hog supplies will grow a little every week as the seasonal expansion takes hold, so prices should slowly work lower, but they probably won't come crashing down as they have in some years. Skinny packer margins are a symptom of not enough hogs to meet slaughter capacity and it is pretty uncommon for packers to still have negative margins this deep into August. In fact, the last time that packer margins went negative in the third week of August was 15 years ago. Even in 2014 when PEDv slashed hog supplies, packers managed a small positive margin throughout August. So, the supply side is pretty tight. Barrow and gilt carcass weights were reported another pound lower this week and the DTDS weights also moved lower. That is another sign of tightness in the hog supply. This week's kill registered just a little shy of 2.4 million head, with a small Saturday kill. Once again, slaughter was below what the Dec/Feb pig crop projected. It now looks like USDA might have over-estimated that pig crop by as much as 700k head. Next week's kill should also be near 2.4 million head and then there will be two smaller kill weeks around the Labor Day holiday.Packers will likely give employees the Saturday before Labor Day off, which will reduce the kill in the week prior to Labor Day, and then there will be no kill on Monday of Labor Day week. The holiday will provide packers with a chance to rebalance the hog supply with capacity and perhaps get their margins back in the black. As we move into September, the industry will begin killing the Mar/May pig crop, which was reported by USDA to be down 1% from last year. Given that USDA clearly over-estimated the Dec/Feb pig crop, we shouldn't be surprised if they are a little too high on the Mar/May as well.

Domestic pork demand does seem to be slowing a little, but most of that seems to be concentrated in the processing items. Butts continued working lower this week and are nearly back to where they were this spring before the great summer rally began. Picnics seem to be following the same pattern as butts, only a month or so behind them. Picnics are currently topping and are forecast lower from here. The trim products remain firm and that could slow the decline in the picnics, which are often used in the same applications as trim. Loins should see good retail interest just after Labor Day and so I think they can hold current values for a few weeks longer. There is not much doubt that the majority of pork items will see lower pricing in the next couple of months as hog supplies expand and the demand downcycle continues.

There is less certainty around how fast the price declines will come. With spot hog supplies so tight, packers may have to keep the kill contained by necessity and thus the product markets could outperform my forecasts in the next few weeks. There isn't much new to report in the export markets. Weekly volumes seem to have stabilized at a level that is about 5-10% below last year and I don't see any reason for that to change in the next couple of months. Next week, look for the cutout and the negotiated hog markets to continue to ease as supplies slowly grow. Futures are likely to recover some of this week's huge selloff.


WTD Change in LH Futures
0.000
-1.000
-2.000
-3.000
-4.000
-5.000
-6.000
-7.000
-8.000
Oct22
Dec22
Feb23
Apr23
May23
Jun23
Jul23
Aug23
Oct23
Dec23
Feb24


WTD Change in Pork Cutout Futures
0.000
-1.000
-2.000
-3.000
-4.000
-5.000
-6.000
-7.000
Oct22
Dec22
Feb23
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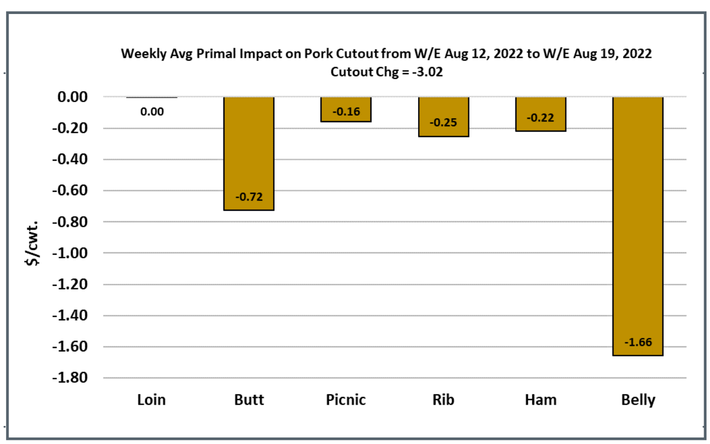
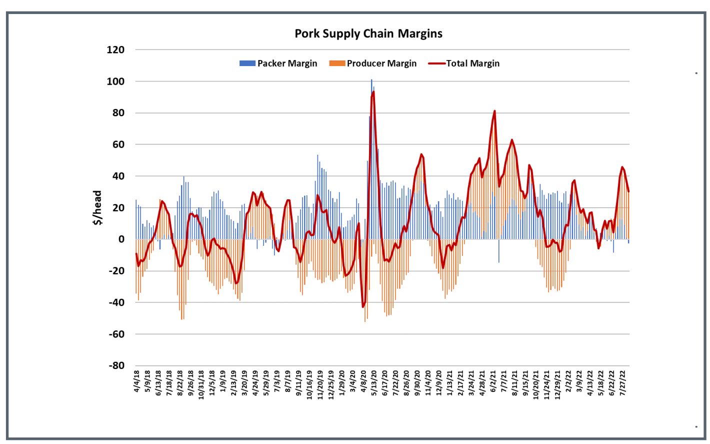
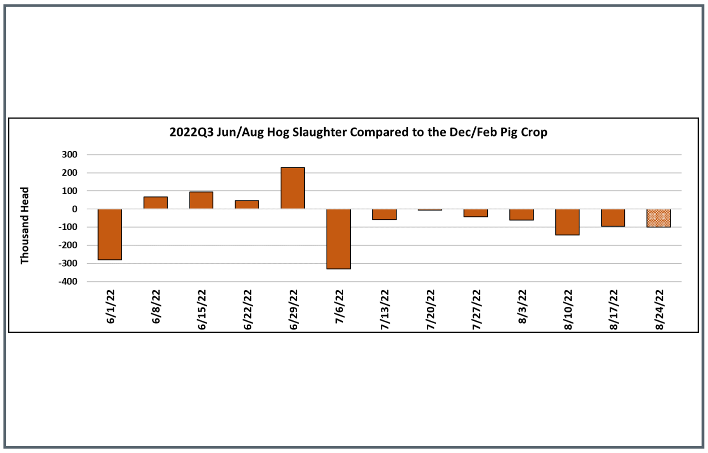
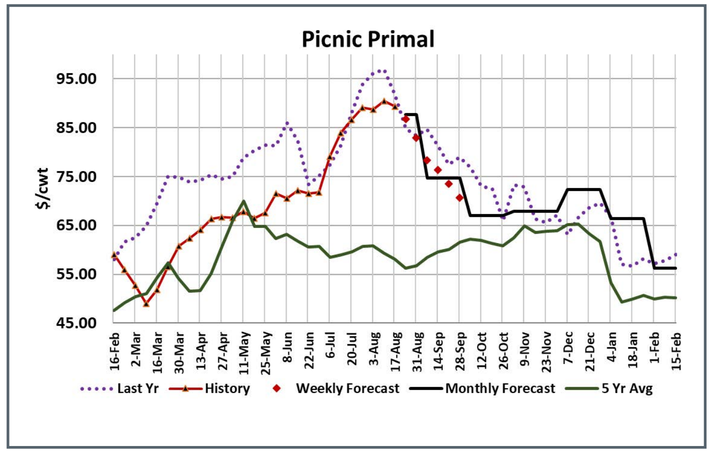
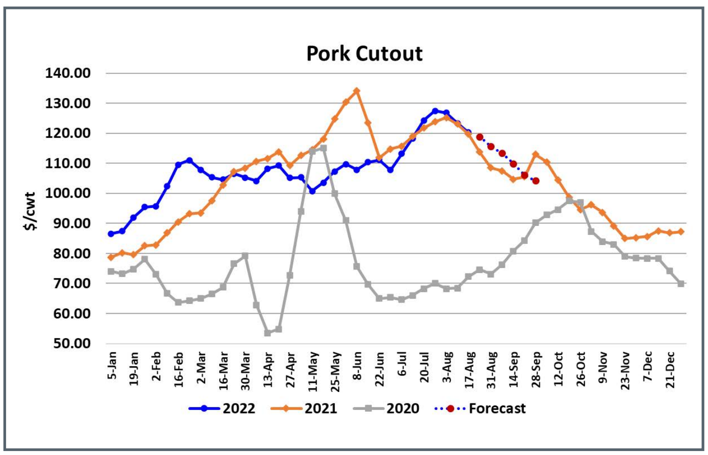

Weekly Avg Primal Impact on Pork Cutout from W/E Aug 12, 2022 to W/E Aug 19, 2022
Cutout Chg = -3.02
$/cwt.
0.00
-0.72
-0.16
-0.25
-0.22
-1.66
Loin
Butt
Picnic
Rib
Ham
Belly


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.