J.S. FERRARO
jsferraro.com | 416.306.8788
130 Adelaide Street West, Suite 3302 Toronto, Ontario M5H 3P5

WEEK ENDING OCTOBER 21, 2022

THE PORK WRAP

This week saw the pork cutout stall, averaging $102.46/cwt., down $0.23/cwt. from last week's average. A $102 cutout in late October is pretty impressive, but what is even more impressive is the renewed strength in cash hog prices. This week the WCB negotiated market averaged $97.38, up $6.75 from the week before. The NDD negotiated market was up $4.37. A flat cutout combined with rising hog prices spells trouble for packer profits. Packer margins declined about $2/head this week to $17, but all of the increase in the cash hog price has yet to be reflected in the LHI, so I'm looking for margins to drop another $4 or so next week. Over the past five years, packer margins near the end of October have averaged about $26/head, so it is very clear that margins are well below normal this year. Packers have only 2 choices if they want to fix their margin problem: raise pork prices or lower cash hog prices. It seems to me that they might not have much power to do either, so they may just have to live with below-normal margins for a while.

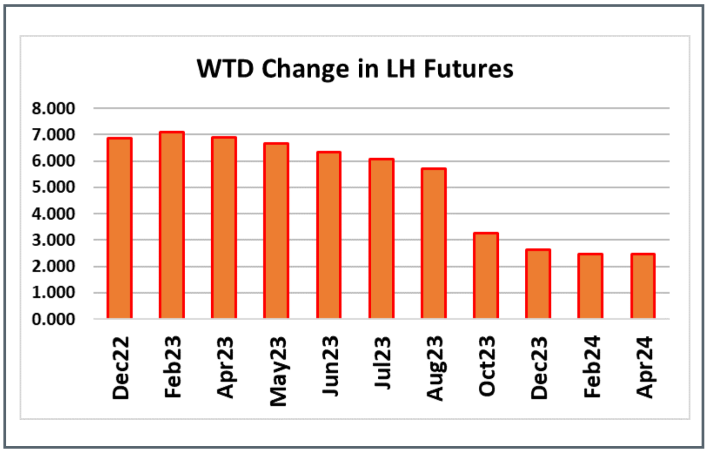
It is hard to see how they could add much to the cutout in the current environment where kills are close to annual highs. This week, loins and hams exerted the most downward pressure on the cutout, but that was mostly offset by strength in the picnic and belly primals. I'm expecting both the bellies and hams to ease a little next week, so that may be enough to move the cutout lower. I think we should still see another week or two of the cutout averaging over $100, but soon it will slide into the upper $90s, where it is likely to spend most of the remainder of 2022. The combined margin was a little higher this week and, while it seems that we should be in a demand upcycle, it is hard to see where the additional strength will originate from. Producers are likely to gain a little margin from packers due to the strong cash hog market, but that doesn't help the combined margin.

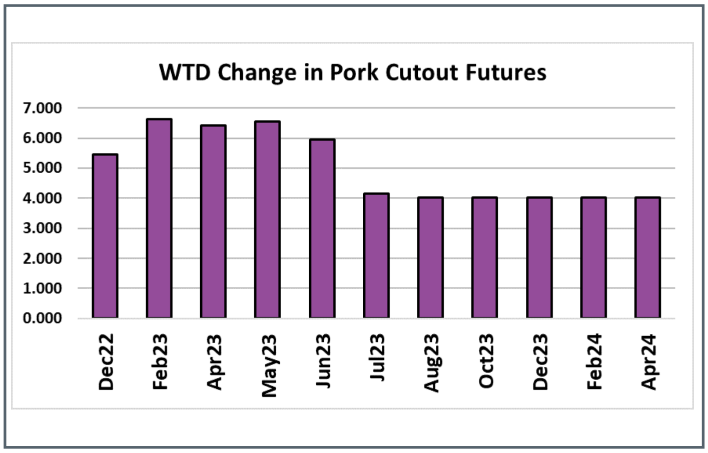
I could be wrong about the bellies and hams and we may see further strength there, I guess. I think packers will have a strong incentive to try and push pork prices higher early next week to try and compensate for the stronger hog market. Whether or not they are successful with that attempt remains to be seen. The fact that the WCB negotiate market is still being quoted near $100/cwt in late October tells me that the hog supply is pretty tight in that region. That fact alone should be pretty bullish for the hog and pork complex in the next few weeks. In the past when cash hog prices were stubbornly high, packers have seemed to find a way to raise pork prices. Maybe that will be the case again this time. It is pretty clear that packers are having to compete more aggressively to fill out their kill schedules than they have at they have at this time of year in the past.

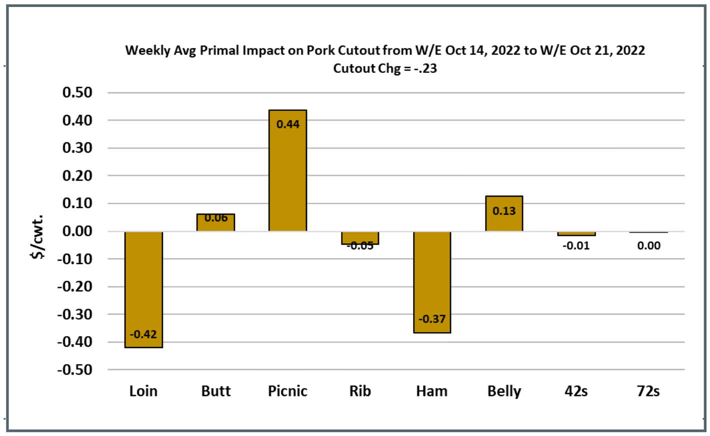
The same situation is occurring in beef, resulting in much smaller margins than what packers have become accustomed to. This surprising late-year strength in the hog market has really kept the futures market on the move. Today, the Dec contract traded very close to $90 for a period of time. A little over two weeks ago it was trading at $74. The rally in Dec over the past two weeks has been impressive and it wiped out everything that Dec lost when the market swooned in September. The back of the futures curve has taken notice too, and we saw the summer 2023 contracts gain close to $6 this week. Those issues still look a little under-priced relative to the fundamental forecast, but the fall 2023 contracts are now $8-10 above the fundamental forecast. USDA had some issues getting reports out in a timely fashion this week as one or more packers were late in submitting their daily data. That problem now appears to be corrected. This week's slaughter registered 2.57 million head, up 20k from the week before. This was a "big Saturday" week and that meant that packers over-killed the pig crop slightly.

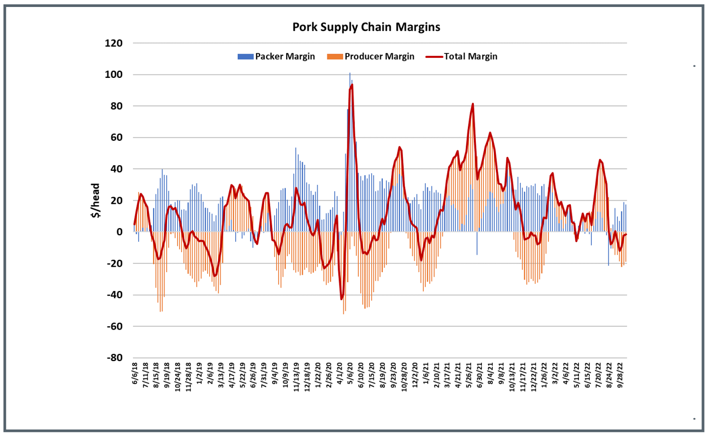
Still, for the Sep/Nov quarter as a whole, so far the kill has only fallen short of the pig crop by a little over 100k. Not a big miss, and not much to be concerned about. Next Saturday's kill should be smaller and we may see the total kill drop back to 2.55 million head. The Mar/May pig crop projects the maximum weekly kill this fall at 2.61 million head, so we are getting really close to a top in slaughter levels. Hog carcass weights were one pound higher this week, but that is typical for this time of year and the DTDS weights aren't indicating any problem with hogs backing up in the system. Low water in the Mississippi River system has hampered efforts to export corn and we are now seeing cash corn in the Midwest go discount to the futures for the first time since early June.

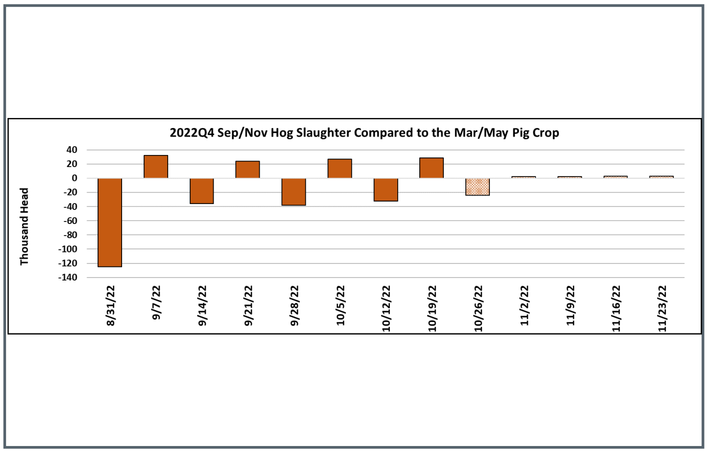
Even so, corn costs for hog producers are way higher than in recent years and are likely a big factor discouraging expansion in the hog production sector. Hog and pork prices in China have been steadily increasing and that has raised hopes that soon Chinese buyers will increase their orders for US pork. Some of the recent strength in the deferred futures is probably linked to trader hopes for stronger pork exports to China in 2023. It is possible that we could see improved interest from China over the next few weeks as the deadline for shipping pork to arrive in time for the Chinese New Year moves closer. Next week watch the early-week cutouts closely for signs that packers have been able to coax more money out of pork buyer to help cover their higher hog costs. Keep an eye on the negotiated hog markets also, because the longer they remain at these elevated levels, the more bullish the outlook becomes.

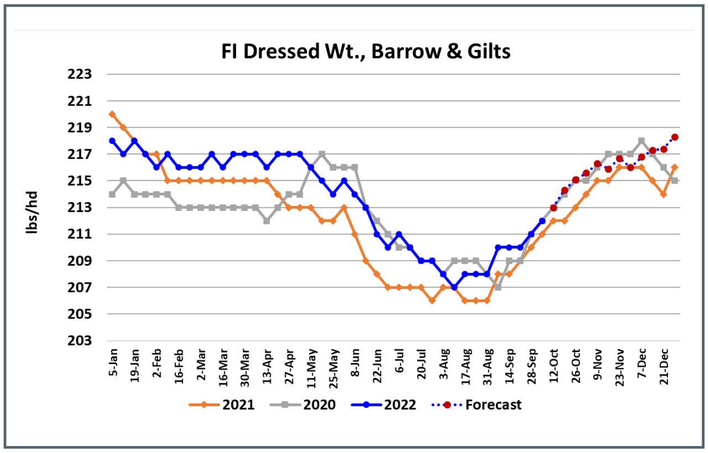

WTD Change in LH Futures
8.000
7.000
6.000
5.000
4.000
3.000
2.000
1.000
0.000
Dec22
Feb23
Apr23
May23
Jun23
Jul23
Aug23
Oct23
Dec23
Feb24
Apr24

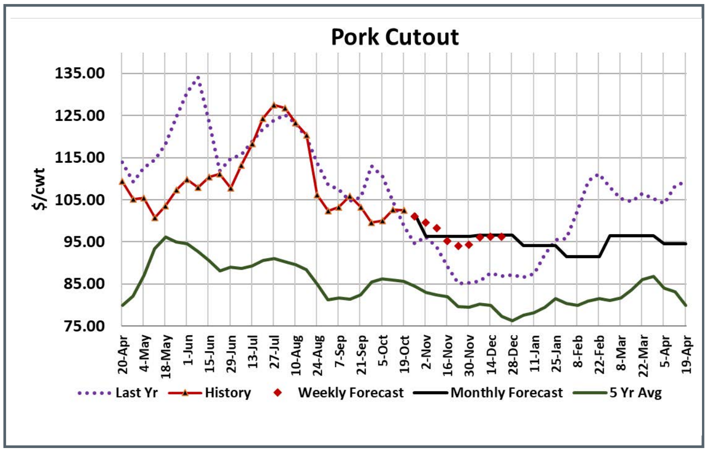

WTD Change in Pork Cutout Futures
7.000
6.000
5.000
4.000
3.000
2.000
1.000
0.000
Dec22
Feb23
Apr23
May23
Jun23
Jul23
Aug23
Oct23
Dec23
Feb24
Apr24

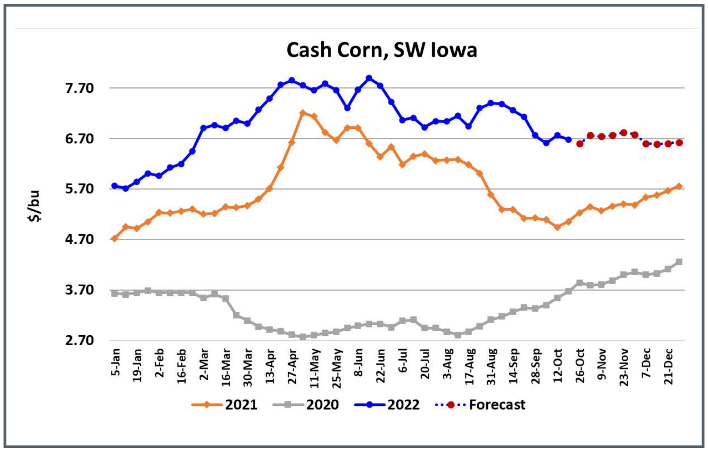

Weekly Avg Primal Impact on Pork Cutout from W/E Oct 14, 2022 to W/E Oct 21, 2022
Cutout Chg = -.23
$/cwt.
0.50
0.40
0.30
0.20
0.10
0.00
-0.10
-0.20
-0.30
-0.40
-0.50
-0.42
0.06
0.44
-0.05
-0.37
0.13
-0.01
0.00
Loin
Butt
Picnic
Rib
Ham
Belly
42s
72s


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









DR. ROB MURPHY BS, MS, PhD Agri Economics,
Executive Vice President, Research & Analysis,
J.S. Ferraro

E: Rob.Murphy@jsferraro.com

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.