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

WEEK ENDING OCTOBER 28, 2022

THE PORK WRAP

The main feature in this week's market was the cutout dipping below the $100 mark for several days and averaging $2.86/cwt. less than last week. There were some interesting dynamics within the carcass and within the week however, starting with the surprising bump higher in the belly market on Friday. Prior to Friday, the bellies had been trading softer, but someone managed to sell a good quantity of 13/17 lb. bellies at $205 on Friday morning and that caused the belly primal to jump. However, the bellies that traded Friday afternoon were much closer to the $160/cwt. level that had been common earlier in the week. So, while that might have been an anomaly, it did allow the cutout to finish the week back in triple digits. On a weekly average basis, the belly primal was down about $3.50 this week.

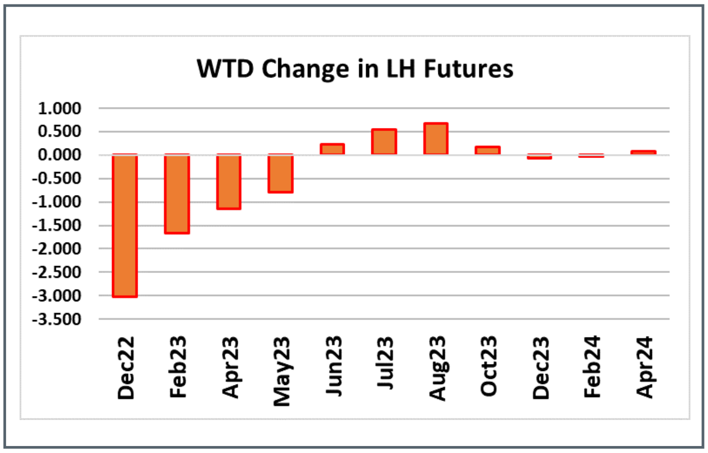
Another important feature in this week's market was the continued slide in the loin primal, making it the biggest drag on the cutout. That is probably a sign of some pork fatigue starting to set in at the retail level. Hams also lost ground this week and that is probably due to less demand from domestic processors who are now up against a tight timeline in order to get hams processed in time for the holidays. Trims were the bright spot, with both the fat and lean trim up around $3 on a weekly average basis, but trims make up a much smaller part of the cutout calculation than do the other primals. When it was all said and done, the cutout posted an average of $99.59 for the week. Last year at this time, the cutout was about $5 lower than where it is now. On the surface, that would seem to indicate that pork demand is still robust, but when we take inflation into account, the picture isn't so rosy.

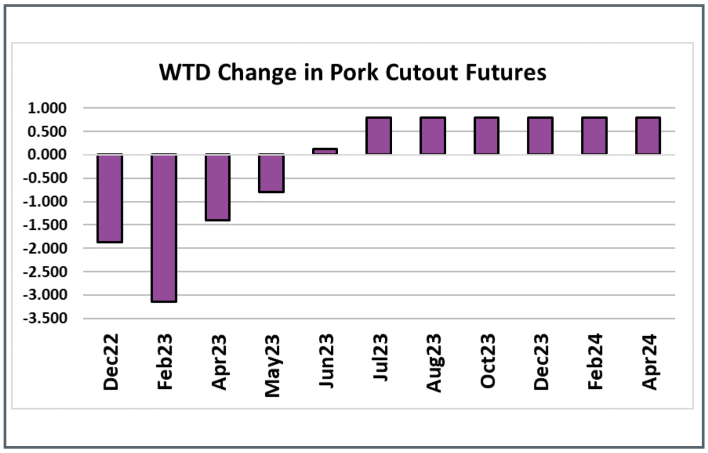
The attached scatter diagram gives the demand curve for October calculated using CPI-deflated price levels and we see clearly that demand was stronger in October 2021 than it was this year. In fact, demand looks really soft compared to recent years. That fits with the combined margin, which is also on the defensive and signaling weak demand. If we have a $99 cutout on weak demand, imagine where it will go when demand enters its next upcycle, which I would expect to begin in the second half of November. The forecast has the cutout easing lower through most of November and then strengthening modestly into December. One place where there is definitely not weak demand is the negotiated hog market. The WCB market averaged $97.22 this week and was nearly steady with the week before. I think the strength in the negotiated hog market is simply a sign of the hog supply being too small for the available processing capacity.

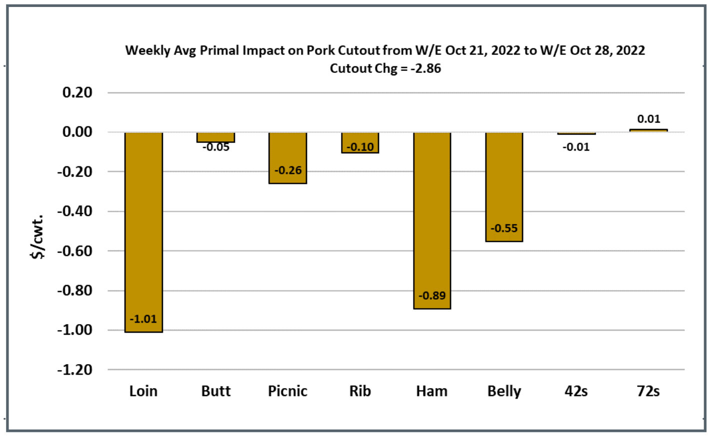
As a result, packer margins this fall are much narrower than in recent years. This week's margin is estimated at $9.86/head, well below the $27/head that packers were realizing last year at this time when labor constraints were reducing processing capacity. The Lean Hog Index averaged over $94 this week and the cutout is just shy of $100, so it is easy to see that margins are tight for this time of year. I think that is going to continue and may get worse as we go into 2023 because USDA's surveys have been telling us that the hog herd is going to stay on a downward trajectory at least for another six months. This week's kill was reported at 2.56 million head and this was a "small Saturday" week in the context of the oscillating weekend kills that are clearly visible on pig crop implied chart.

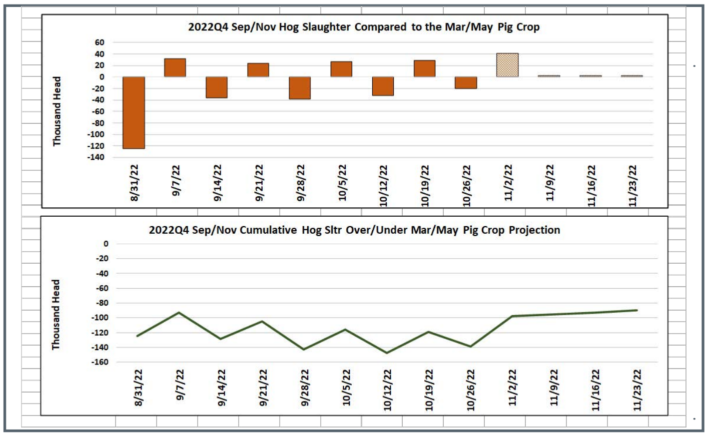
Next week will be a big Saturday and we could even get the weekly kill up to 2.61 million head, which should be the practical top this fall. Except for Thanksgiving week, we should look for kills to hover in the 2.55 to 2.62 million head range until early December. By January, the weekly kill should ease back into the 2.4-2.5 million head range. Hog weights were steady this week, but they still could add 3-4 more pounds before they hit their annual top. The DTDS weights continue to tell a story of relatively current market hog supplies and that fits with the strong pricing in the negotiated hog market. Producer margins are about $17/head in the red right now and may reach -$35 or -$40 later in December. Stubbornly high corn prices are gobbling up any benefit that producers might have seen from high hog values. However, producers are accustomed to losses of that magnitude near the end of the year when hog supplies are near their peak.

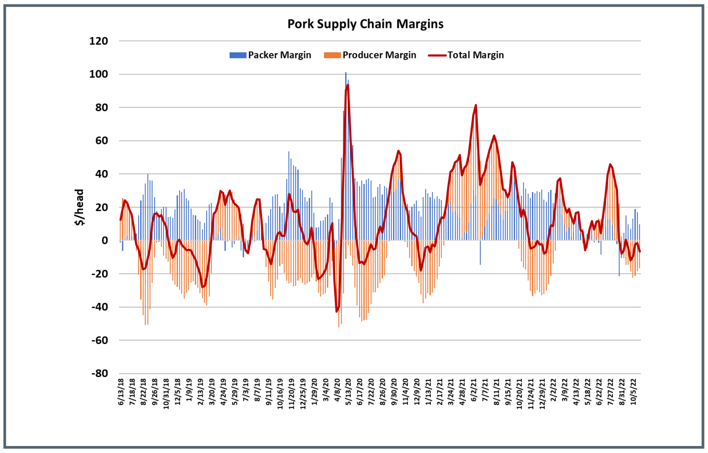
They know that they will likely make it back in the summer when hog supplies tighten and hog prices soar. This week the nearby futures made an abrupt turn lower on Thursday in response to the cutout softening. On the week, Dec lost close to $3 but keep in mind that Dec probably got a little overdone when it gained $7 the week before. As of Friday's close the Dec LH futures are sitting very close to what the fundamental forecast says is fair value. They are in a comfortable spot with little need to move much higher or much lower unless something dramatic happens to the cutout next week. Of course, if packers decided to slow the kill in order to improve margins, that could have a material impact on both the cutout and hog prices, but my sense is that they currently don't have an appetite for that. If anything, they would like to kill more, not less. Next week, watch the belly market to ascertain if Friday's bump has any staying power and keep an eye on the retail primals since they seem to be the weakest link in the complex right now.

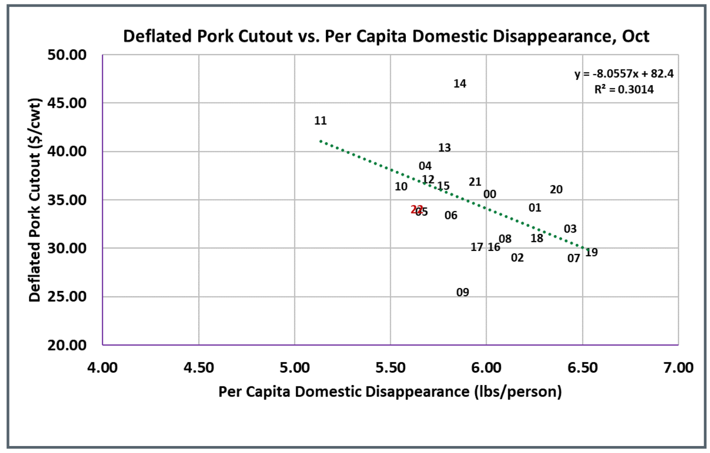

WTD Change in LH Futures
1.000
0.500
0.000
-0.500
-1.000
-1.500
-2.000
-2.500
-3.000
-3.500
Dec22
Feb23
Apr23
May23
Jun23
Jul23
Aug23
Oct23
Dec23
Feb24
Apr24

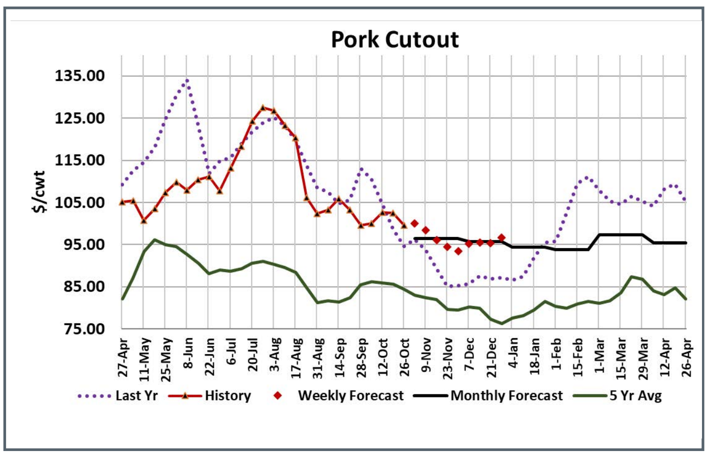

WTD Change in Pork Cutout Futures
1.000
0.500
0.000
-0.500
-1.000
-1.500
-2.000
-2.500
-3.000
-3.500
Dec22
Feb23
Apr23
May23
Jun23
Jul23
Aug23
Oct23
Dec23
Feb24
Apr24

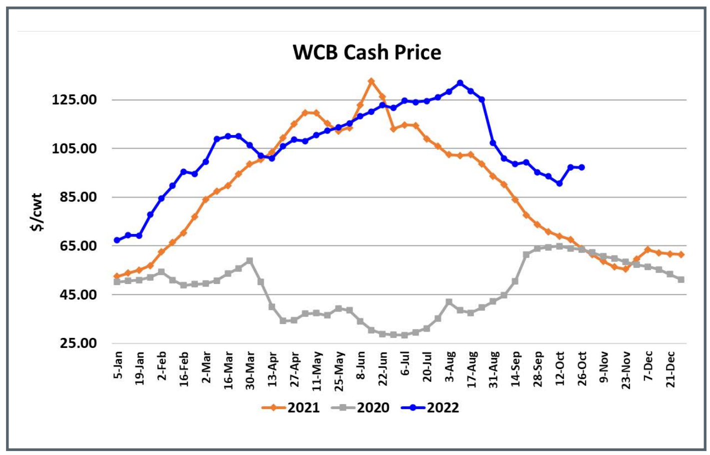

Weekly Avg Primal Impact on Pork Cutout from W/E Oct 21, 2022 to W/E Oct 28, 2022
Cutout Chg = -2.86
$/cwt.
0.20
0.00
-0.20
-0.40
-0.60
-0.80
-1.00
-1.20
-1.01
-0.05
-0.26
-0.10
-0.89
-0.55
-0.01
0.01
Loin
Butt
Picnic
Rib
Ham
Belly
42s
72s


2022Q4 Sep/Nov Hog Slaughter Compared to the Mar/May Pig Crop
Thousand Head
60
40
20
0
-20
-40
-60
-80
-100
-120
-140
8/31/22
9/7/22
9/14/22
9/21/22
9/28/22
10/5/22
10/12/22
10/19/22
10/26/22
11/2/22
11/9/22
11/16/22
11/23/22
2022Q4 Sep/Nov Cumulative Hog Sltr Over/Under Mar/May Pig Crop Projection
Thousand Head
0
-20
-40
-60
-80
-100
-120
-140
-160
8/31/22
9/7/22
9/14/22
9/21/22
9/28/22
10/5/22
10/12/22
10/19/22
10/26/22
11/2/22
11/9/22
11/16/22
11/23/22









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.