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J.S. FERRARO

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RED MEAT OUTLOOK: HOGS & PORK

The most important factor in the US hog and pork complex during December was further expansion of packer margins. The cutout eased only a tiny bit lower during the month but negotiated hog prices dropped nearly $10/cwt. over the same span. For the last week of the year, we calculate packer margins very close to $31/head (**Figure 1**). That is up from about $20-25/head at the end of November. When packer margins expand like that, it is almost always due to growing hog supplies relative to the amount of packing capacity available. The latest *Hogs and Pigs* report, released just before Christmas, confirmed what the slaughter data has been telling us for months: there are way more hogs out there than initially reported by USDA. As a result, packers needed to be incentivized to run bigger kill schedules and that was accomplished by producers accepting progressively lower hog prices and thus expanding packer margins. It doesn't seem like that process is complete, either. It looks like the post-holiday kills could still run over 2.6 million head per week for most of January and that likely will continue to keep pressure on cash hog prices. How the cutout performs is an open question because demand will have some say in that and there is always hope that demand will improve somewhat from the dismal state it has been in for the past couple of months. The current forecast only looks for only a little more downside risk to the cutout, with expectations that it will begin to improve near the end of the month and slowly build on that improvement as spring approaches.

SUPPLY PICTURE

Hog slaughter has been constrained over the past couple of weeks by the holidays, but prior to that we saw weekly kills that were at or near 2.7 million head. If USDA's estimate of the spring and summer pig crops had been correct, then the expected top in kills would have been closer to 2.6 million head. Those extra 100,000 head per week really helped to tip the leverage meter in favor of packers. It should be more of the same during January, with kills running about 50-100,000 head per week over USDA's initial estimate of the Jun/Aug pig crop. As a result, we now see January kills closer to 2.6 million head per week instead of 2.5 million and that is likely to limit gains in negotiated hog prices even though the cutout could improve marginally by the end of the month.

> Upward revisions to prior pig crops means **there are more hogs available this winter** than initially anticipated

To make matters worse, pork production is being boosted further by the seasonal increase in carcass weights. Barrow and gilt weights now stand at 214 pounds, just one pound under last year's level. The weather in the Upper Midwest region has been exceptionally mild over the past few weeks and that has kept hogs gaining well and may very well result in better conception rates than might otherwise be expected. All of this adds to the pork supply and helps to keep prices low. Pork production during Q4, looks like it will be up just a little over 2% YOY and there is a real risk that the YOY increases will carry over into Q1. As a result, buyers should find ample product availability and pricing to their liking during January. However, stocks of pork in cold storage are not as burdensome as they were last year and that creates a buffer against excessively low pork pricing since some users will find it advantageous to put product away for use later in 2024 when prices are higher.

The most recent *Hogs & Pigs* report indicated that producers cut the breeding herd as of Dec 1 to just under six million head, and that represented a 3.3% decline from the same period last year. However, as producers cull, they are getting rid of the least productive sows, helping to boost productivity in the herd that remains. USDA reported the number of pigs saved per litter during the Sep/Nov quarter to be up 3.9% YOY and that comes on the heels of a 4.3% increase in the Jun/Aug quarter. So, while producers are actively trimming down the breeding herd, we aren't seeing a meaningful reduction in the number of hogs born because

Producers have cut breeding stock, but strong productivity has kept piglet production from declining much

productivity is so strong. This means that deeper breeding herd cuts will be needed in future quarters to limit hog supplies enough so that they better align with consumer demand and thus bring better profitability to the hog production sector. Producers had one of their worst years ever in 2023, losing a little over $30/head (**Figure 2**). If they want 2024 to look any better, more drastic reductions in breeder animals is needed.

Hog production margins averaged **around $30/head in the red** during 2023

DEMAND SITUATION

Not much has changed with respect to domestic demand for pork. It still looks very soft compared to past years and there isn't much hope for improvement in the short run. Our estimated demand index for Q4 was down 4.8% from the previous year and the forecasted demand index for Q1 calls for a 3.5% YOY decline. As you might remember, Q2 of 2023 saw one of the softest demand indexes ever recorded in our dataset and there is concern that could be challenged again this spring. It isn't obvious what is driving weak consumer demand, especially since demand for beef is registering well above normal at present. Perhaps the easiest explanation is that consumer tastes and preferences have shifted away from pork and towards other forms of protein, such as beef. The weakness in demand is manifesting in all parts of the carcass, but the demand for bellies seems to be particularly soft. It is hard to imagine that consumers are shying away from something as tasty as bacon, but it could be that retailers just aren't featuring it as frequently or at attractive prices and thus less product is making its way into shopping carts. The retail-centric cuts, particularly loins and butts, should see better demand in January as they offer a lower cost per unit of protein than many competing items at a time when consumers are likely to be looking to cut expenses. California's Prop 12 regulation will be more rigorously enforced after Jan 1 and that might lead to a little less demand for the non-compliant pork products that make up the reported cutout value. We don't expect a large impact however, since most of the adjustment needed to comply with Prop 12 has likely already been accomplished. USDA is reporting that animals which meet the confinement specifications required by Prop 12 are trading at an average of $5/cwt. over non-compliant hogs. That premium has been stable for several months now, leading us to believe that the market has found the right balance with respect to Prop 12.

US pork exports have been strong recently, as you might expect given the low pricing in the pork markets and abundant production. USDA reported October exports up 6% YOY and it wouldn't be surprising to see the November and December numbers come in at that level or stronger. Since October, the weekly data released by FAS has indicated a huge surge in shipments to S. Korea that is probably being driven by a shift away from more-expensive European product. The swine herd in Europe is in decline and thus we expect US pork to continue to attract interest from importers that previously relied on sourcing from Europe. Movement into China continues to be soft however, as that country is dealing with macroeconomic problems and very large domestic pork supplies. Fortunately, it looks like there are plenty of other destinations that will pick up the slack left by China's waning interest in US pork.

SUMMARY

At present, the US hog and pork complex is plagued by over-production and soft demand. That has led to weak pricing and very poor margins for hog producers. Packers are faring much better as the large production is allowing them to run their plants at high rates of capacity utilization and reap very strong margins. Producers seem to recognize that they need to scale back the breeding herd in order to better align production with the new reality of soft demand, but efforts in that direction have been largely offset by strong productivity in recent quarters. The financial strain on producers continues to be intense and we estimate that, in the last week of 2023, they were losing close to $45/head on every animal marketed. Pork buyers will likely do well by remaining close bought during this period of ample availability and low prices. However, the summer months are likely to see the cutout solidly back into triple digits and thus buyers might be wise to consider using the current price weakness to extend coverage into the late spring and summer quarters. Domestic pork demand continues to run very soft and that suggests that perhaps there has been a structural shift in consumer preferences away from pork and towards other proteins. That type of change is often very difficult to reverse quickly and so we may be looking at a long period of below average demand in the pork complex. Near-term, we see a little more downside potential in the cutout during early January, but then some modest strengthening near the end of the month and into February as slaughter levels finally start to moderate. **Table 1** provides our near-term price forecasts.

Figure 1: Packer Margin

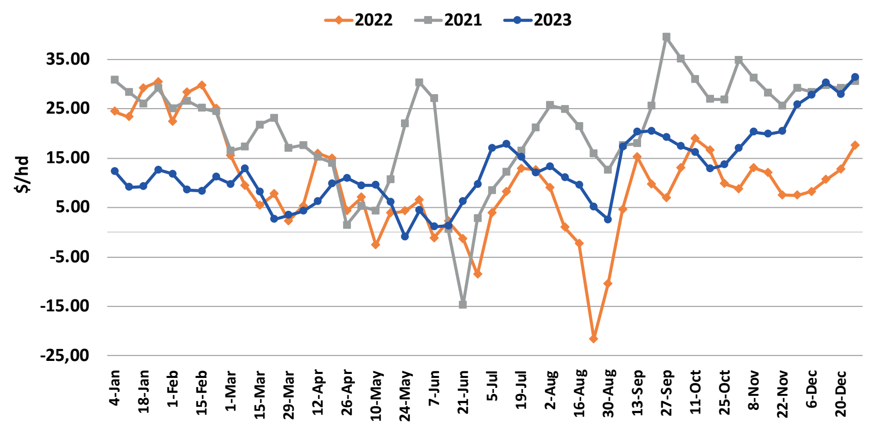

Figure 2: Average Annual Hog Production Margin

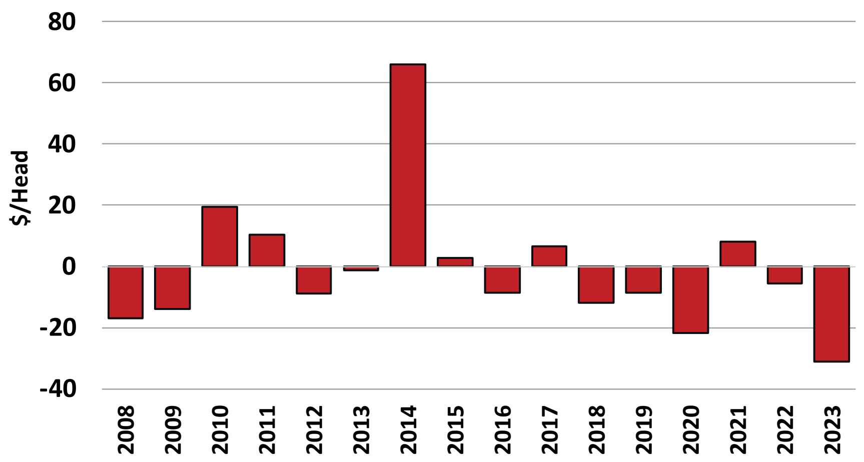

Table 1: JSF Hog and Pork Price Forecasts

	10-Jan	17-Jan	24-Jan	31-Jan	7-Feb	14-Feb
Pork Cutout	82.1	82.3	83.5	84.4	86.6	88.0
Loin Primal	85.2	84.3	86.2	86.0	87.2	88.9
Butt Primal	101.9	98.7	99.0	100.0	102.8	104.0
Picnic Primal	67.0	66.2	69.1	73.0	74.8	74.6
Rib Primal	114.6	115.3	117.2	116.5	118.2	120.3
Ham Primal	77.9	78.3	77.1	75.6	76.5	79.3
Belly Primal	93.2	97.0	100.4	105.3	112.0	111.6
Lean Hog Index	65.6	67.4	69.1	71.0	73.0	74.4

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 33 years in the industry. He has a wealth of experience in the North American meat and livestock industries studying, analyzing and predicting market movements.