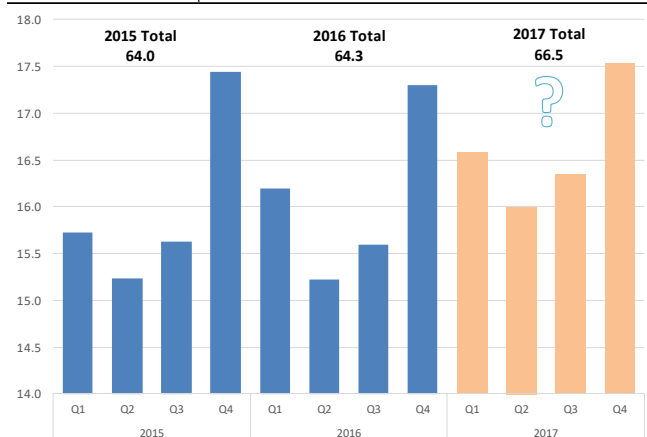


It is human nature to be drawn to tangible stories that bring both context and insight to our day to day issues. For those involved or following the pork market, the story of tight belly supplies and higher pork prices was immediately relatable, with images of beautiful crispy strips thrown in for good measure by news editors everywhere. But fun as it is to talk about bacon and how much some of us love it, there will be some 26 billion pounds of pork produced (cwe) in the US in 2017 and bacon is but 15% of all that supply. Making sense of that product flow and how much eventually will be available to the consumer can make for a very dry presentation. But we will proceed with the thankless task because **eventually our decisions should be anchored in reality rather than anecdote.**

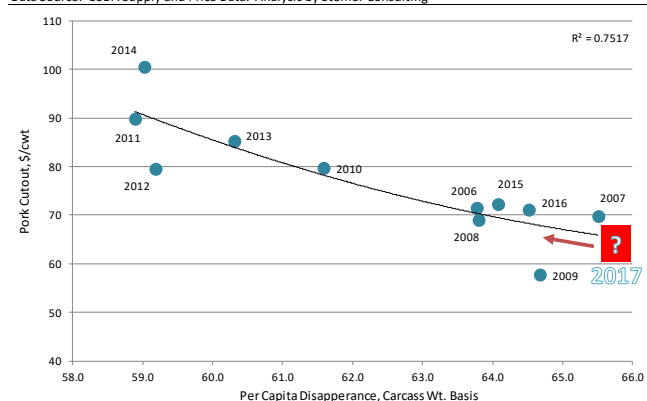
So what the heck are we trying to show in the attached charts. But **take a step back from all the production/slaughter discussion and recognize that eventually what matters for prices is how much of the supply ends up in front of the domestic consumer.** We have our own ideas and forecasts about production and available supply but for most producers and other market participants, USDA is the only/best publicly available information. And we will go with their numbers, raise a question or two and see where the discussion leads us. In the last WASDE report, USDA significantly raised its 2017 pork production estimate to the tune of 400 million pounds (+1.5%) from the December estimate. This followed a 'Hogs and Pigs' survey showing quite a bit more hogs were in the pipeline than previously thought. On a quarterly basis, USDA pegged Q1 pork production up 3.6%, Q2 at +6.8% and Q3 at +5.2% and Q4 at +4.9%. At this point **USDA analysts think that total production in 2017 will exceed last year's all time record by another 1.27 billion pounds (cwe).** It would seem to us that USDA is counting on a trend increase in hog weights, probably to the tune of +1% compared to a year ago. A couple of things may work against it this year. As producers work through a significantly larger supply of hogs, the tendency will be to push them through the door as soon as possible and, in the past, that has tended to keep weights below trend. In the first few weeks of this year weights are down about 1 pound or so from a year ago. Also **new feeding rules may also impact productivity in the short term.** But even with an adjustment on weights, the overall pork supply should easily exceed last year's levels. As mentioned earlier, what matters for prices is how much you are asking the domestic consumer to buy. You can sell everything at the right price but with larger supplies lower prices are required to make that product disappear. Will we ask the domestic consumer to eat 5% more pork than a year ago? Not really since we are counting on export markets to take some of that pork. Again going back to the USDA WASDE report, their analysts expect pork exports in 2017 to be around 231 million pounds (+4.4%) higher than in 2016. Is USDA being too conservative in this estimate? Maybe although there are some very significant risks for those that hold a more bullish view. Exports have started the year on a very

Quarterly Supply of Pork Available/Consumed in the Domestic Market

Data from USDA Actual and Expectations from WASDE.

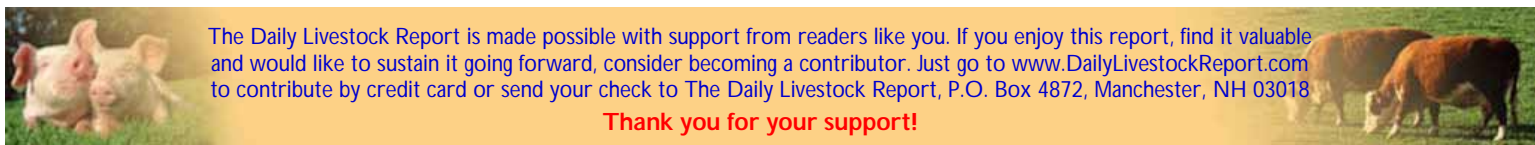


RELATIONSHIP OF THE PORK SUPPLY CONSUMED DOMESTICALLY (PER CAPITA) VS. PORK CUTOUT (PCE deflated)
Data Source: USDA Supply and Price Data. Analysis by Steiner Consulting



strong pace, we think January shipments are up around 15% from last year. China demand is showing some signs of improvement but remains to be seen if they will be as active in the spring as they were a year ago. Then there is all the uncertainty surrounding our trade with Mexico, which last year bought almost a third of all our pork.

The second chart shows the relationship of per capita domestic supply use (disappearance) relative to pork prices as represented by the cutout. Keep in mind we have deflated pork prices to remove price inflation effects. **If USDA is correct in their assessment and per capita supply use will exceed 66 pounds, then this would imply pork cutout prices under \$70/cwt for the year in 2017.** Hence the reluctance of hog futures to put more of a premium on spring as summer prices, despite very robust spot prices for both pork and hogs.



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