Daily Livestock Report

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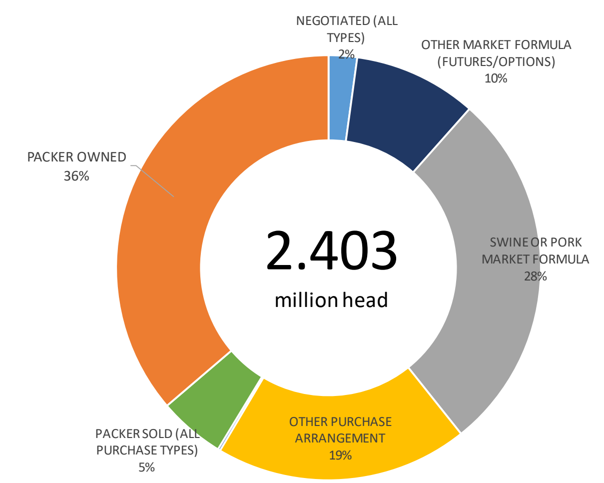
April hog futures are only a few days away from expiration and yet there continues to be a dramatic disconnect between cash prices and where the market is trading. As we write this, the April hog contract is locked limit up, maybe a realization that reality may be a bit different than what the board is currently trading. Money flows and uncertainty clearly have caused futures to trade quite wildly in the near term but ultimately fundamentals in the market will determine true product value. **On Monday the April lean hog contract settled at $41.125/cwt, 36% lower than where it was only a couple of weeks ago** (March 24). Is that representative of current cash prices? A better question: what are current cash prices? The reality is that there is no longer such a thing as one cash price. Over the last decade the hog market has been transformed into a kaleidoscope of price discovery, where individual hog values will greatly depend on who owns the product, the relationship between various agents to the processing plants, and the ability of individual producers to set up effective risk management programs and formulas.

When we first started writing this letter a couple of decades ago, we used to look at the IA/MN lean hog carcass base price as a pretty good indicator of cash prices. Some people still look at it today. On Monday that price was quoted at a weighted average of $40.31/cwt, $3.39 lower than the Friday close. The national base negotiated price was $41.77/cwt, $1.07 lower than the previous close. Those prices seem to match up with where futures are currently trading but the reality is that they represent only a minuscule number of hogs trading in the market. Looking at the USDA weekly average of hogs traded/priced last week, we see that **out of the 2.403 million hogs reported in the Mandatory Price Reporting system (MPR), only 32,896 hogs or 1.3% were traded on a negotiated carcass basis**. The average national price for negotiated carcass hogs last week was $49.07/cwt, 16% lower than the average price the previous week. While the decline was quite dramatic, it still was nowhere close to what futures did. **April lean hog futures last Friday closed 31% lower than the previous week**. Likely this was an over reaction based on the sharp decline in negotiated carcass hogs and the cutout. The average price of hogs based on formulas that are tied to futures/options contracts was $54.89/cwt last week, a 15% decline from the previous week but a 36% premium to where futures were on Friday. According to USDA, the hogs priced by these types of formulas represented 9.4% of the total. Hogs priced using formulas tied to the hog or pork market represented 28% of the total and the average price for this group of hogs last week was $57.56/cwt, 10% lower than the week before. A significant share of hogs in this group (we don't know how many but our guess is 40-50%) are priced off the cutout. The average pork cutout value last week was $62.88/cwt, 21% lower than the week before. Clearly the formulas used may have a bit of a lag or smoothing factor since we did not see a corresponding decline in this group of hogs. Another 20% of hogs priced last week used what are called "other purchasing arrangements," a catchall for formulas that are more complex and often include grain market pegs and premiums for delivering specific product attributes. The average price of these hogs, remember they were 20% of the total, was $62.64/cwt, 8% lower than the week before. And finally, the biggest group of hogs slaughtered but not sold in the market were owned by packers. According to USDA, packer owned hogs represented 36% of hogs reported in the MPR system.

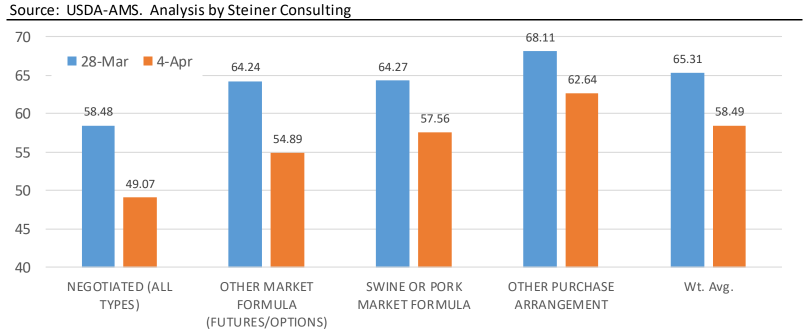
Hogs Slaughtered and Reported through USDA MPR System for wk ending 4/4

Data source: USDA-AMS. Analysis by Steiner Consulting



Prices Paid for Hogs Marketed through Various Pricing Mechanisms. $/cwt carcass

Source: USDA-AMS. Analysis by Steiner Consulting



Bottom line: While it may be convenient to look at one price as a gauge of cash market activity and use that directionally for pricing, it is important o recognize that the current dynamic in the hog market is far more complex than in the past. Negotiated hogs are just a sliver of the total at this time. If that volume falls further, futures will be even more dependent on the cutout for price discovery and, ultimately, index settlement.