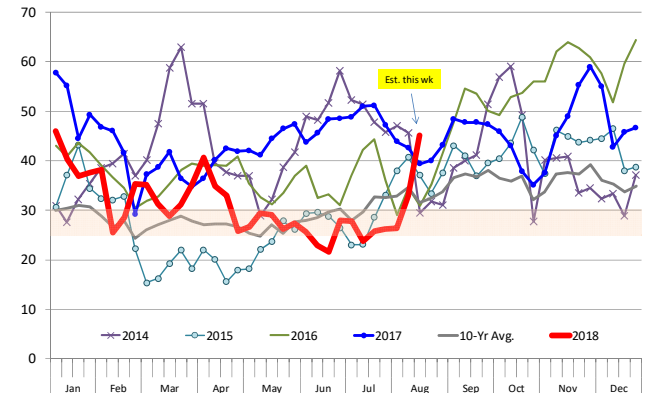


Pork packer margins were under pressure through much of the summer but they have expanded rapidly in recent days. The true extent of the improvement is a bit difficult to ascertain since we really do not know the impact that lower by-product values are having on margins. According to the latest calculations from the Livestock Marketing Information Center the by product value is around \$17.6/head, down about \$3 per head or 15% compared to a year ago. This estimate is much higher than what USDA is currently reporting and underscores **the difficulty of grasping the true value that packers derive from by-products.** While USDA quotes the price of specific items in a given weeks, be this hearts, stomachs, etc, we do not know what percentage of the weekly supply is sold at quoted levels, what percentage derives a higher value because it goes to export and what goes into pet food at a steep discount. **The main reason for the improvement in pork packer margins recently is due to the fact that hog values have declined at a much faster pace than the value of pork sold at wholesale.** The top chart to the right shows our estimates for gross packer margins this week and it includes some key assumptions. First, it assumes a derived by-product value of around \$17.5/hog, slightly lower than the last quoted value. It also assumes a national net hog price of \$56/cwt. The pork cutout for the week is estimated at around \$70.5/cwt. Cash hog prices have been pressured significantly in recent days. Last night the IA/MN lean hog base price was quoted at \$43.63/cwt, down 3.5% from the previous day, which implies a cash hog index around \$56/cwt. Since the end of July the IA/MN lean hog base value has declined by almost \$16/cwt. That's **a 27% decline in the base hog value in just 9 trading days.** There is little question that producers at this point are looking to return to a more normal flow of hogs to market, something that was disrupted first by the imposition of Mexico tariffs on US pork at the start of July and then the reduction in slaughter due to planned maintenance. **In the four weeks ending August 11 hog slaughter was 9.032 million head, just 0.8% higher than a year ago. This is well short of the 3.5% to 4% increase that was implied by the June hog inventory data.** On Monday hog slaughter returned to near full capacity at 467k head. Judging by the number of hogs scheduled for the next few days it appears packers will continue to run at above 460k head /day this week. Saturday slaughter will be critical. We expect it will be a little north of 140k head compared to 129k for the same week last year. **Improving margins may provide an incentive to run a bit harder on Saturday, something that the current hog markets desperately need.**

For now pork end users see little reason to put product away in the freezer. Hog slaughter is expected to increase in the next few weeks and retailers are focused on Labor Day features, which appear to us to be more heavily focused on beef rather than pork. However, **current low pork prices may set the stage for more robust pork features later in the fall. Pork demand also tends to improve in Q4.** Belly and ham prices are going to be key. Belly prices have subtracted a lot of value from the pork cutout since the middle of July. Last night the pork belly primal value was \$93.76/cwt, down almost \$80/cwt since July 19. The decline in the value of pork bellies has removed almost \$13/cwt from the value of the cutout. Since July 19 the overall pork cutout value is down \$12/cwt. Retail bacon prices are higher as retail features come to an end.

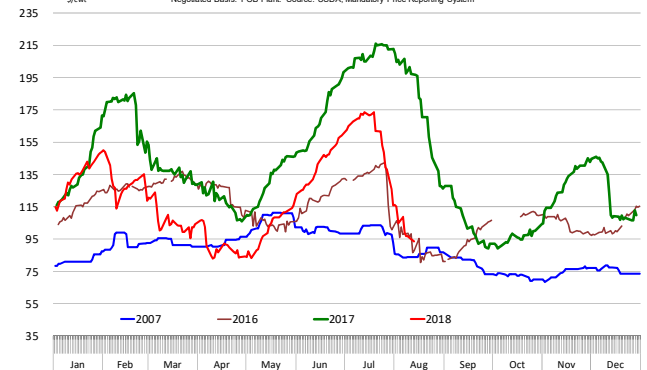
PORK PACKER CALCULATED GROSS MARGIN. \$/HEAD

Calculated Using the Weekly Pork Cutout Value, Number of Head Processed, and Drop Credit Value. Data Source: USDA, Steiner & LMIC Drop Credit



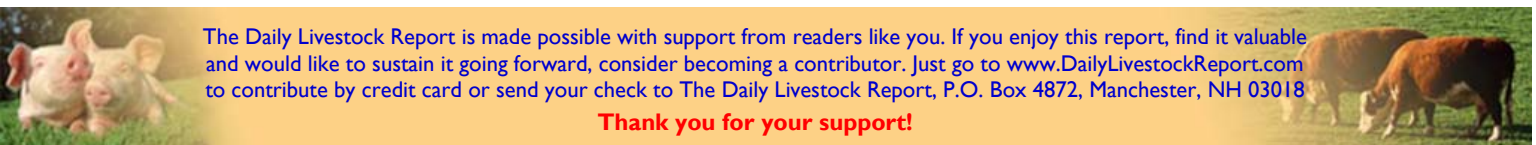
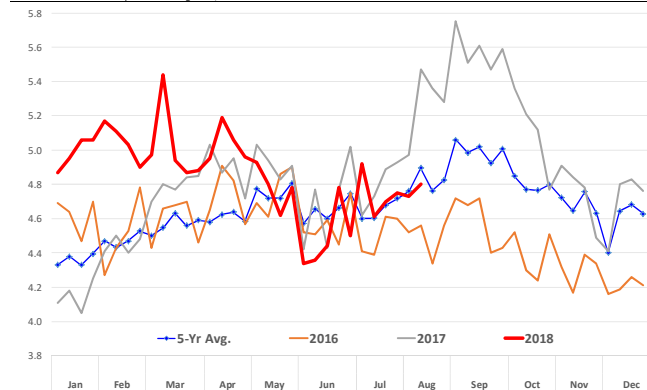
Pork Belly Primal Value

\$/cwt Negotiated Basis, FOB Plant. Source: USDA, Mandatory Price Reporting System



NATIONAL RETAIL PORK FEATURES REPORT: SLICED BACON, 1 LB PKG PRICE. USD/LB.

Source: USDA. Latest data point is for August 10, 2018



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