Daily Livestock Report

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<u>Clarification & Correction</u>: We have received feedback from a number of readers and industry participants regarding todays report. Rather than wait until tomorrow to address their points we thought it would be appropriate to send this out today. Our intention with this letter has always been to provide you with timely and accurate information to the best of our abilities.

The first issue that was identified had to do with the statement regarding the way in which formula hogs are priced. We probably should have phrased it more precisely. Our point was that pork prices now impact formula priced hogs much more than in the past. However, it was not our intention to suggest that all hogs priced on a formula basis are priced using pork prices. Some market sources indicate that 30-35% of the formula hogs today are priced using the cutout. We do not have any first hand information as to what that percentage is. It is certainly higher than even five years ago. As a larger percentage of hogs are priced using the price of pork, there may come a time when this category is separated into swine priced and pork priced.

The second point has to do with the "other purchase arrangement" category. Again we probably were not as precise in defining what goes into this category. We noted that "more producers (are) choosing to establish the value of their hogs using contracts incorporating production cost factors." But this does not mean this is the only way in which the formulas for pricing hogs in this category are established. This category incorporate all hogs that do not fit in the other three buckets. This includes cost of production hogs but it also includes hogs raised without ractopamine, hogs that receive premiums for non-carcass characteristics and premiums for raising hogs in other ways that market now values. As end users focus on specific claims that consumers find valuable, this information is now transmitted to producers via premiums and producers have responded. The increase in the number of hogs included in this category reflects that.

We appreciate all your comments and feedback.

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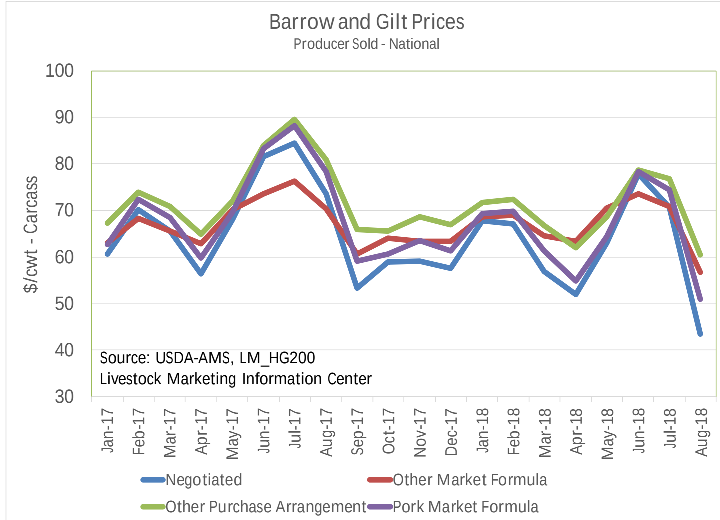
Negotiated barrow and gilt prices on a national basis, as reported by USDA-Agriculture Marketing Service (AMS) dropped below $40 per cwt. for the first time since 2016 on August 21. For the entire month, the national negotiated barrow and gilt price averaged $43.35 per cwt., which compares with $73.67 during August 2017.

USDA-AMS reports barrow and gilt prices sold by producers reflecting four types of marketing arrangements; negotiated in the spot market, pork product value driven price formula (e.g. the value of a carcass based on the composite value of pork products coming from the carcass), pricing formulas driven off of hog futures or options market values, and other purchasing arrangements (value relative to cost of inputs to produce the hog, mostly feed related).

Modern hog marketing practices have moved away from pricing hogs on the spot market negotiated basis to protect producers from swings in pork processor profit margins. The volume of barrows and gilts sold on a negotiated basis in the spot market so far this current quarter is only 3.6% of all barrows and gilts marketed. During the summer quarter of 2017, 4.4% of all barrows and gilts were marketed in this manner.



The majority of barrows and gilts are marketed with value based on prices for pork products sourced from these hogs, such as loins, hams, bacons and trimmings. So far this quarter, barrow and gilts priced under these arrangements accounted for 47% of all hogs sold by producers. The value of hogs sold by way of these formulas netted a price premium of $6.64 per cwt. compared to hog values established through spot market negotiations in August. Interestingly, in the summer of 2016 52% of all hogs sold by producers were valued based on pork product pricing formulas.

The decline in share of hogs marketed through pork product value formulas is a result of more producers choosing to establish the value of their hogs using contracts incorporating production cost factors. For the first two months of this quarter, 34% of all hogs sold by producers were valued irrespective of spot market prices, pork market value formulas or hog futures-options market inputs. During the summer of 2017, 27% of producer-sold hogs were marketed in this manner. In August, hogs priced with an orientation to cost of production garnered a $17 per cwt. premium to the spot market. A year earlier, this premium was only $7.