Daily Livestock Report

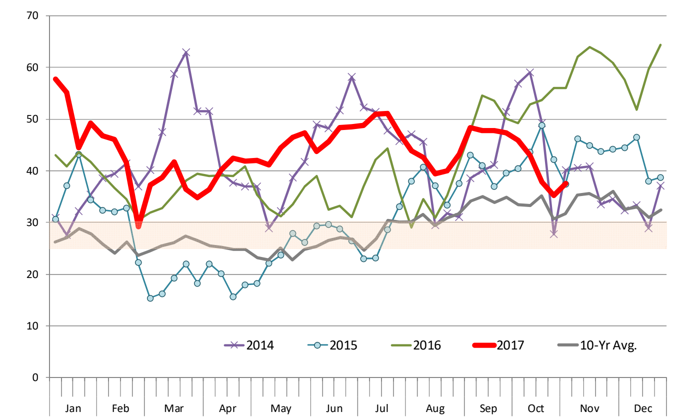
Vol. 15, No. 219 / November 7, 2017

Hog prices have rallied since late September on a combination of increased packer competition (two new plants ramping up) and robust pork domestic and export sales. Paying up for hogs while not getting much more for the pork they sell has meant tighter margins for pork packers. Not many expected packers to continue to see the kind of margins realized a year ago but the magnitude of the recent decline was also unexpected. There are a lot of pork processing margin calculations reflecting different assumptions about the cost of processing hogs, capacity issues and even the valuation of by-products. We have shown the attached chart before but it is worth pointing out what it does and does not show. We do not make an attempt to come up with estimated hog processing costs, every packer is different and costs will change depending on capacity utilization, etc. The shaded area in the chart shows we think the breakeven range is. The lines in the chart show weekly estimated GROSS margin calculation on a per head basis. The gross margin is nothing more than what's left over after you add up the monies made by selling pork and by-products minus what you paid for hogs. To calculate this we use the pork cutout from USDA (value of pork sold), which last week was $78.92/cwt. The by-product credit is a bit more tricky as we have seen many different ways of valuing/calculating this. USDA quotes by-product values regularly. Last week their quote was $3.85/cwt on a live basis. For a 280 pound hog this means a by-product credit of $10.78/head (3.85*2.8). However, over the years we have relied on the LMIC by-product calculations, which tend to have a higher (and we think more realistic) by-product valuation. For week ending November 3 LMIC calculates the hog by-product value at $18.85/head. The total gross margin for the week stood at $39.34/head compared to $55.98/head a year ago.

For a while packers were willing to maintain the slaughter pace despite eroding margins but that changed last week. Hog slaughter last Monday was estimated at 443,000 head, down from the +460,000 head that would normally be the case for this time of year. Tue-Fri slaughter then proceeded as normal but Saturday slaughter once again was light at 168,000 head, the lowest Saturday slaughter since the last week of August. For the week hog slaughter was estimated at 2.453 million head, 3.1% less than a year ago. **In the last four weeks, hog slaughter has averaged 2.490 million head, 2% higher than a year ago but well short of the +3.7% that was implied by the latest Hogs and Pigs report.** It appears that the slowdown in slaughter may be starting to affect producer currentness and, consequently, cash hog values. The average weight of producer owned barrows and gilts that have came to market last week was 211.8 pounds per carcass, 0.8% higher than a year ago. The trajectory in hog carcass weights appears to have shifted in the last two weeks and they are now closer to where they were in 2015. Cash hog prices have been slowly eroding as well and this has negatively impacted the December contract. **The IA/MN lean hog carcass base price closed last night at $61.22/cwt, 1% lower than the previous day and down 5.3% compared to a week ago**. The one day cash index continues to hover just under $69/cwt and has not lost as much ground as the base price. Robust cutout values and higher premiums have supported net hog prices. Ultimately demand going into the holidays will determine the appropriate price levels. **If packers have orders to fill it is unlikely they will pass on them for the sake of bolstering an arbitrary margin target**. Slowing export sales may be more of a concern for hog producers. Export sales from the Mandatory Price Reporting system for last week (this does not include NAFTA) showed weekly export sales down significantly from a year ago. The four week average of weekly sales is now down 18% from last year and it has been declining steadily since late September. Given expected large hog supplies through the end of the year, maintaining export sales pace remains critical.

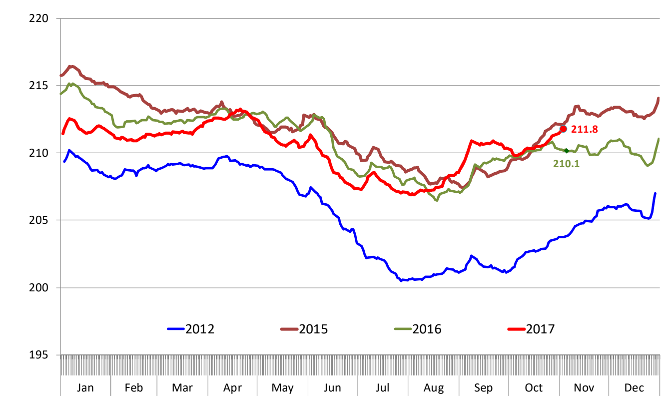
PORK PACKER CALCULATED GROSS MARGIN. $/HEAD

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



Barrow/Gilt Dressed Carcass Weights, 5-day Moving Avg. - Producer Hogs

Based on Daily MPR Report, LM_HG201. Data through Nov 3, 2017



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Weekly MPR Export Sales Volume, All Pork - 4-week Moving Avg.

Based on MPR. Does not include NAFTA. Data Source: USDA. Analysis by Steiner Consulting