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Weekly Outlook: Hog Prices Supported by Strong Demand

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January 2, 2018

***farmdoc daily* (8):1**

Recommended citation format: Hurt, C. "Weekly Outlook: Hog Prices Supported by Strong Demand." *farmdoc daily* (8):1, Department of Agricultural and Consumer Economics, University of Illinois at Urbana-Champaign, January 2, 2018.

Permalink http://farmdocdaily.illinois.edu/2018/01/hog-prices-supported-strong-demand.html

In USDA's December Hogs and Pigs report, pork producers indicated they continue to increase the breeding herd at a slow-sustainable pace. The breeding herd was up one percent and the market herd was up two percent. These were in alignment with pre-report market expectations.

The U.S. breeding herd has expanded by seven percent since the start of 2014. The major states that have the largest increases over this period are: Missouri +30%; Ohio, Oklahoma, and Nebraska each up 10%, and Illinois up 6%.

Pigs per litter reached another record in 2017 at 10.59, a .9 percent increase for the year and a remarkable 15 percent improvement over the past decade.

There was some indication that producers will expand more rapidly in 2018 than the one percent larger breeding herd. Farrowing intentions this winter were up three percent followed by a two percent increase in the spring quarter. If producers follow through, this will increase pork production more rapidly in the last-half of 2018.

Taking the numbers from the report's inventory count, pork production is expected to rise by three percent in the first-half of 2018 and by near four percent in the last-half of 2018.

The theme for the pork market in 2017 was higher production and higher prices when pork production rose by 2.5 percent and hog prices were up 10 percent. The reason was strong pork demand around the world. That was led by bacon demand in the U.S. where retail prices were up about seven percent and by pork exports expanding around seven percent.

For 2018, we once again ask if hog prices can be higher with a 3.5 percent increase in supply and with sizable increases in competitive meats as well. The lean hog futures market is currently saying, YES!

Why might the futures market be correct? The foundation of the argument lies with demand. In 2018, the U.S. economy will grow more rapidly. The unemployment rate will drop modestly and is already at the lowest level since 2000. With the economy growing and most people working, wage rates will rise more rapidly. In addition, the new federal income tax law is likely to increase the size of the average paycheck (but certainly not for every family).

In 2018, the world economy is expected to be the strongest since the 2008/09 recession. USDA analyst expect net pork trade (exports minus imports) to increase by nine percent. Finally, packer demand will continue to strengthen as newly opened processing plants continue to expand toward full capacity in 2018. Stronger packer demand can increase the percentage of the pork value that is received by producers.

Beef will be a big competitor with pork for those extra dollars in many consumer's paychecks in 2018. Beef supplies are expected to rise by near five percent with chicken production up two percent and turkey up fractionally. All meat supplies will rise by about three percent. The question remains, "Can hog prices be higher in 2018 with all that meat?

Live hog prices are expected to be higher in 2018 according to the current lean futures market prices. Live hog prices are expected to average around $53 in 2018 compared to about $51 in 2017. Prices are expected to be in the low-$50s in the first quarter and then move up seasonally to average in the higher $50s for the second quarter, then back to the mid-to-higher-$50s for the third quarter and finish the year in the mid-to-higher $40s.

Cost of production is expected to be slightly higher for 2018 due to somewhat higher corn prices in the fall of 2018. Total costs is estimated to be around $50 per live hundredweight. Estimated profits for 2017 were around $5 per head above all cost of production. For 2018, that estimate is slightly better at $5 to $10 per head of profit.

All of the animal industries have now increased their production in alignment with U.S. average corn prices at $3.50 per bushel or lower and high-protein soybean meal at $350 or lower. Strong demand has helped carry animal prices in 2017 and is expected in 2018. However, the pork and beef industries will not be able to continue expanding at the nearly four percent annual rates of increase since 2014 where pork production is up about 16 percent and beef is up 14 percent (the four years from 2014 to 2018).

Avoiding supply expansion to a point where prices are not profitable is the goal for the animal industries. Secondly, the 2017 crops are now the fourth consecutive year of great yields and low feed prices. History suggest that these forces will not continue forever. Finally, for those pork producers who believe hog prices cannot be higher again in 2018, the lean futures market is currently providing strong pricing opportunities.