Cooperative
Extension Service
University of Illinois
at Urbana-Champaign

WEEKLY OUTLOOK
Department of Agricultural Economics
College of Agriculture
University of Illinois at Urbana-Champaign

September 10, 1986

HOW FAST WILL HOG PRODUCERS EXPAND?

HOG PRICES HAVE REMAINED ABOVE $60 this summer and show no signs of dropping. Hog-corn ratios are at record highs. How fast will hog producers expand in response to these strong profits? The answer will determine how quickly prices fall next year. The next USDA Hog and Pig report, to be released on September 22, will show whether farrowings and producer intentions to farrow remain as low as in the June report.

Recent rallies in hog futures indicate that the market is expecting little or no expansion, as shown in the June report. Possible reasons for the lack of expansion are the unwillingness of bankers to lend money for expansion and the reluctance of producers to take risks because of poor profits in the 1980s. On the other hand, reasons to expect expansion include the availability of cheap corn and the fall in interest rates.

It is useful to examine past experience. The last hog price rally occurred in the summer of 1982, when hog prices averaged $61 per hundredweight. Pork production actually became profitable beginning in February 1982. As a result of expansion in response to positive profits, prices fell to $42 in the summer of 1983. Producers with more than 500 head were responsible for the expansion; smaller producing units actually cut production. It is likely that investment credits provided some incentive for larger producers to expand in order to reduce taxes on the windfall profits.

The Hog and Pig reports in 1982 did not predict the expansion very accurately. The June 1 report in 1982 showed farrowing intentions for June-August and September-November down 9.1 percent and 9.4 percent, respectively. The September 1, 1982, report showed that actual farrowings in June-August were down 9.5 percent, and intentions for September-November were revised down further to 10.8 percent. First intentions for December-February farrowings were down 6.1 percent. This report was unexpected and generated a rally in hog futures at that time. Actual farrowings, however, were not as low as indicated by intentions in the September report. September-November 1982 farrowings were down only 1.2 percent, and December-February 1982-83 farrowings actually increased 6.3 percent.

The September 1, 1986, report will probably be similar to the 1982 report and will show no expansion or even contraction in farrowings compared with the June report. Because the market already expects no expansion, a report showing no expansion should not generate much of a price rally. If an increase in farrowings over the June report appears in September, it may cause futures prices to decline.

If past experience is any guide, intentions in the September report may be misleading and actual farrowings may expand. In 1986, hog production became profitable in May, later in the year than in 1982. Normally, farrowings increase three quarters after profits are positive. High prices during June-August 1986 should lead to increased farrowings in March-May 1987 and a larger pork supply in the fall of 1987. Hog prices should decline somewhat before then because of growth in competing meat supplies and recovery of pork imports.

Current futures prices for 1987 hogs and corn offer very attractive profits. Even though cash prices remain strong, producers may wish to consider locking in profits soon. Selling hog futures would lock in the current futures price for next spring and summer production. Purchasing a put option to sell at the current futures price would provide a price floor equal to the futures price minus the option premium.

Laurian J. Unnevehr

Issued by *Laurian J. Unnevehr*, Extension Specialist, Prices and Outlook

Cooperative Extension Service
United States Department of Agriculture
University of Illinois
At Urbana-Champaign
Urbana, Illinois 61801