



Cooperative
Extension Service
University of Illinois
at Urbana-Champaign



WEEKLY OUTLOOK

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January 10, 1990

PROFITABLE HOG PERIOD: HOW LONG WILL IT LAST?

The latest *Hogs and Pigs* report shifted the 1990 hog outlook from basically a break-even year to one of anticipated profits. The USDA has already been criticized for not providing more accurate information about the size of the breeding herd last summer, and for its earlier 1989 reports that provided few clues to what appears to be declining production in 1990. The key for hog producers now is to attempt to sort through what is occurring with the breeding herd; to evaluate the current strength of hog prices and whether they will continue; and finally to examine management decisions.

In the September report, the USDA estimated the national breeding herd as down about 3 percent from the previous year. With higher weaning rates and heavier market weights, this meant that early 1990 hog supplies would be nearly unchanged. The December report, however, revised the September breeding herd downward an additional 2.3 percent, from 7.0 million head to 6.87 million. Fall farrowings were estimated at down 6 percent. The reports in June and September 1989 indicated an industry that was little changed, while the December report suggested the industry had likely been in liquidation since last summer. So, which story is to be believed?

There are several factors which suggest that the December report is correct. First, the December report is the most complete survey of the year. There are more producers surveyed in more states and the USDA places its greatest faith in this report. Secondly, fall slaughter rates were down about 4 percent. This implies that there was a greater decrease occurring in the spring and summer 1989 farrowings than earlier reports had indicated. Thirdly, after a period of major financial losses, we expect to see reductions in the breeding herd about nine months later. Large losses in the last half of 1988 should have caused some reductions in the herd by summer and fall of 1989. While the September report did not show this, the current revised numbers now seem to indicate that the herd reduction was in fact under way.

Once the breeding herd starts downward, history tells us it will not reverse itself quickly. In fact, there is a tendency to see the breeding herd even lower than the USDA initially indicates as the full impacts of liquidation become accurately known. The structure of the industry has changed, however, so caution is important.

How long will the herd stay in liquidation? The improved profitability in the fourth quarter of 1989 and now the improved 1990 outlook are likely to turn some producers' thoughts toward expansion. The nine-month-lag, however, means that it

will be into the late spring and summer of 1990 before the breeding herd begins to increase, and therefore spring of 1991 before slaughter supplies begin to rise.

While production is not expected to rise before mid-1991, some of the strong prices experienced in late 1989 were related to demand factors which may not continue into 1990 and beyond. For example, the hoped for Eastern European market is not likely to be a demand factor in the future; strong demand for McDonald's McRib may not continue; we do not expect to see pork pushed by retailers as strongly in the future as it was in late 1989; and pork exports are expected to drop a little in late 1990 as European production expands. These will be the price-moderating factors in 1990.

Terminal prices are expected to average in the high \$40 in the first quarter, before moving nearer to a \$50 average for the second quarter. Summer daily highs in the \$52 to \$54 range now appear likely. Summer quarter prices should average in the high \$40, before ending the year with near a \$45 average in the last quarter. At this point it appears that price levels will remain profitable through the first half of 1991.

If the breeding herd should drop more rapidly than USDA reports have indicated, there is a small possibility that cycle highs could be made this summer: In this event, producers would not want to be short futures, but rather use put options, to establish minimum prices.

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