UNIVERSITY OF ILLINOIS EXTENSION

WEEKLY OUTLOOK

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STRONG HOG PRICES WILL OUTPACE POTENTIAL GRAIN PRICE INCREASE

Hog producers can look forward to strengthening hog prices into the summer, and for a year of profitable prices. Even drought concerns are not likely to force grain and feed prices so high that losses would result. Perhaps the best news from the USDA's March *Hogs and Pigs* report is that the nation's breeding herd continues in contraction. Breeding herd numbers are down 5 percent compared to March of 1999, and down 10 percent compared to the same period in 1998.

The market herd was reported to be down 3 percent, with 3 percent fewer pigs in each of the weight categories. This means that the number of hogs available for slaughter will be down about 3 percent in the March to August time period. Pork production, however, will be down only 2 percent since weights will likely be about 1 percent higher than last year.

Sow farrowing intentions were down 4 percent for the spring and 2 percent lower for the summer of 2000. Given a 1 percent increase in the number of pigs per litter and 1 percent higher market weights, pork supplies will be down about 2 percent this fall, but about unchanged this winter.

There will be sharp differences in market supply by region. While national hog supplies this spring and summer will be down 3 percent, supplies in the eastern corn belt will be down 12 percent, and those in the western corn belt will only be down 1 percent. The large declines in the eastern corn belt are led by disproportionate reductions in breeding herds. In the east, breeding herd declines in the March report were: Wisconsin -24 percent, Ohio -18 percent, Indiana -17 percent, and Illinois -9 percent. In the western corn belt, breeding herd reductions were more moderate with Nebraska -7 percent, Missouri and Iowa -5 percent, and Minnesota -3 percent. In addition, the states of Oklahoma and Colorado increased their breeding herds by 7 percent and 11 percent, respectively. Some of these added supplies will find their way into finishing and processing in the western corn belt. Supplies will be very tight in the eastern corn belt, while western supplies will be nearly unchanged from last year.

There will be 2.5 to 3.0 million fewer hogs available for eastern corn belt plants this year. This means that hog price premiums will be stronger in the east, that some hogs will need to be transported from west to east, and that eventually some plants will have to slow their production lines in the east.

Hog prices are expected to rally in late-April and May from the lower $40s to the higher $40s. Peak summer prices could come in June, with extreme daily highs reaching the $50 level, or even low $50s. Summer prices are expected to average in the $46 to $49 range. Seasonal reductions in price are expected for the fall, but sharp decreases are not likely. Fall prices are expected to drop into the $42 to $45 range, with winter prices only a few dollars lower. Over the next year, these price estimates average about $44. Current production costs for farrow-to-finish operations are around $38.

One of the interesting questions is how much higher would corn and meal prices have to be this summer before hog producers would be thrown into losses? The answer is surprisingly high. To have corn and soybean meal prices drive costs from $38 per hundredweight to the expected average price of $44 for the next year would require $2.90 per bushel corn and $230 per ton meal, about 35 percent higher than current prices. Assuming hog prices this summer will average $47.50, corn and meal prices would have to increase to about $3.40 per bushel and $270 per ton, respectively, to move hog producers into losses. In conclusion, if hog prices do rally as expected this spring and summer, it is very unlikely that grain and meal prices can move high enough to initiate a hog liquidation. This is especially true with nearly 1 billion bushels of wheat in carryover from the 1999 crop which can serve as a hog feed reserve.

Hedging summer lean futures prices in the very high $60s and low $70s should be considered. However, the history of the hog cycle suggest that futures tend to underprice the eventual price of hogs during cycle price peaks. For this reason, those producers who can take some price risk should not forward price more than 50 to 70 percent of expected summer production. Cash price estimates for the fall and winter suggest that lean futures should be priced in the very high $50s or low $60s. To date, futures have not achieved these levels. Producers are advised to wait until this spring and summer to make forward pricing decisions on fall and winter production.

When forward pricing, producers will want to consider selling futures rather than forward contracting. Packers saw extremely weak basis levels in the last two years and are reflecting these low basis values in forward cash bids. When producers sell futures, they take the basis risk. Basis levels will likely be much better for producers this year than bids currently reflected from packers. Some packers offer the service of selling futures for their producers, otherwise producers will need to use a commodity broker.

While corn and soybean prices will not likely move high enough to erode all of the profit potential for hog producers, higher feed prices can cut into the profit potential. For this reason,some protection on feed needs seems to be prudent for the last-half of 2000 and early 2001. This may mean covering 25 to 35 percent of feeding needs with futures or call options.

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