UNIVERSITY OF ILLINOIS
EXTENSION

WEEKLY OUTLOOK

A joint publication of the Department of Agricultural Economics, College of Agriculture, Purdue University, West Lafayette, Indiana, and the Department of Agricultural and Consumer Economics, College of Agricultural, Consumer and Environmental Sciences, University of Illinois at Urbana-Champaign.

JANUARY 6, 2003

RETURN TO HOG PROFITABILITY DRAWS CLOSER

The new year brings renewed hope for a return to profitability for hog producers. Last year was another tough one, as hog slaughter reached 100.3 million, the second highest annual count after the 101.6 million of 1999. Pork production set a record at 19.7 billion pounds, surpassing 19.3 billion pounds in 1999.

Prices were of course depressed in 2002. The annual average price for 51 to 52 percent lean hogs on a live weight basis was $34.90 per hundredweight, $11 lower than in 2001. Another discouraging factor was an increase in estimated production costs by about $1.50 per live hundredweight, to an estimated $38.60. Losses for average costs farrow-to-finish producers taking spot prices were estimated at $3.70 per hundredweight. The largest estimated losses occurred in the last two quarters, when they averaged $6.10 and $8.20 per hundredweight, respectively.

For 2003, price and profit prospects brighten considerably because of both supply and demand factors. Slaughter is expected to drop to 97.9 million, a 2.4 percent reduction. Pork production is projected to be at 19.4 billion pounds, a 1.6 percent reduction.

Perhaps more important to hog prices will be a reduction in supply pressure from other meats and poultry. USDA is currently expecting beef production to drop by 5.5 percent, with chicken production up only 1.4 percent, and turkey unchanged. Added to the decline in pork production, total meat and poultry supplies are anticipated to drop by 1.6 percent. A decline in total U.S. production of meat and poultry is rare. The last time this occurred was in 1982. A drop of 1.6 percent in total meat and poultry production means about a 2.5 percent drop in per capita supplies.

The decline in pork production is a result of a declining breeding herd as the industry experienced financial losses starting last spring. In the last-half of 2002, sow slaughter averaged about 12 percent greater than during the same period one year earlier. As a result, USDA reported that the breeding herd had dropped 3.2 percent by December 1. The total number of animals in the herd stood at only 6.0 million, the lowest number since USDA began tracking the breeding herd in 1963. Farrowings in the fall of 2002 were down by 2.5 percent, and the number of pigs per litter was constant at 8.83 pigs per litter. Intentions are down 1 percent, for the winter quarter and down 3 percent for the spring quarter.

Prices for 51 to 52 percent lean hogs on a live basis are expected to increase to near $40 for the year. Price recovery in January and February into the mid-$30s may be a bit slower than anticipated prior to the report. However, much of the price recovery for the year could come in from March to June, perhaps reaching the mid-$40s by June. Third quarter prices are expected to average near $40, with prices in the fall of 2003 falling back into the mid-to-higher $30s.
When might we see the highest prices on the next cycle? The most recent loss period stretched from the second quarter of 2002 through the first quarter of 2003. Generally it takes about 4 to 6 quarters after the loss period to reduce farrowings and 6 to 8 quarters to increase prices. These cycle guidelines would result in the highest prices on the cycle in late 2003 and the first-half of 2004. If so, once the industry turns back to profits in the spring of 2003, we can expect a favorable return period through the summer of 2004.

Given the tight carryover situation for both corn and soybeans, some ownership protection, especially on corn, seems worthy of consideration at this time. Soybean meal prices will be sensitive to weather in South America through the winter and corn prices will be sensitive to the pace of exports and weather in the U.S. through next summer. A return to the depressed corn prices of the 1998 to 2001 crops is not expected. At this point, an average U.S. market price of about $2.25 per bushel is expected for the 2003 crop rather than the sub $2.00 of the abundant crop years. This means that hog production costs, while dropping, will not achieve the low levels experienced from 1998 to 2001.

In the past I have argued that producers should be cautious about using futures to hedge when price prospects are improving as they are now. This is because the ultimate cash market prices have tended to be higher than anticipated by futures. Following this logic, hedging with options tends to be preferred. Of course, everyone wonders just how much faith to put in historical facts in the “new” hog industry, and thus each individual will have to evaluate the opportunities to “lock in” profitable hog prices using futures or options over the next 14 months.

Issued by Chris Hurt
Extension Economist
Purdue University