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WILL HOGS RECLAIM "MORTGAGE LIFTER" STATUS?

Rural communities throughout the Midwest can long remember when hogs were regarded as the "mortgage lifters." A hog enterprise had the reputation of generating positive cash flows and adding much needed returns to family living expenses plus a little extra to help pay off land debt. That reputation was lost after the early 1990s as technology and size of operations changed leaving mostly negative margins for family farms that could not meet the new industry standards.

This year, margins are back in the black and 2005 looks very good as well. Profit margins this year will reach an estimated $22 per head. In contrast, in the years from 1992 to 2003, the average annual profit margin was less than $4 per head. The margins this year have even small producers thinking as follows: "at $22 per head and 20 pigs per sow per year, one sow will generate $440 of profit, and 100 sows will generate $44,000 of profit per year." WOW!

So are hogs back? The first item to explore is why hog margins are so good this year and will remain so into 2005. The answer is a combination of three major events from outside the pork production sector. The first is the enormous 2004 corn and soybean crops that lowered feed prices. The transition from high feed prices in the first-half of 2004 to the low feed prices in the last-half increased profit margins by nearly $18 per hog.

The second is the discovery of a BSE cow in the U.S. (December 23, 2003). Exports of U.S. beef were initially cut off, and major buyers are still staying away. So far this year, beef exports are down 85 percent from the same period a year earlier. One of the beneficiaries of limited beef exports has been pork producers, since pork exports have risen by 24 percent. A record 10 percent of our pork production is moving to export markets this year. This compares with barely 4 percent ten years ago.

A third factor outside of the pork production sector is the way retailers are featuring pork this year. With record high retail beef prices, it appears that retailers are pushing pork as a more moderate priced substitute. This has resulted in retail margins for beef being very high, but margins for pork being very low. The reduced marketing margins (both retail and at the packer level) are enabling about $13 more per head to be returned to producers compared to last year's margins.

Unfortunately, each of these three positive contributors to 2004/05 profit margins can not be expected to continue into the extended future. First, feed costs will not likely stay as low as today when crop yields return to normal in the future. Second, the current level of pork exports will likely retreat when U.S. beef exports are restored. Third, marketing margins will likely return to more normal levels in late 2005 and 2006. The one positive that remains is that domestic pork demand does appear to be very good this year, with retail prices up nearly 5 percent even with almost 3 percent higher pork production.

So, will hogs return as the "mortgage lifter?" The safest answer seems to be NO! The current period of very favorable profits is primarily a result of three factors that occurred this year, but were outside the production industry. First, the industry was downsizing in the spring of 2004 due to the anticipation of high feed prices, but in reality, low feed prices resulted with huge corn and soybean harvest. Second, BSE resulted in strong pork exports, and finally pork marketing margins have been very narrow.

There are positives, however. The growth in U.S. pork demand seems to suggest that meat demand has turned the corner in favor of animal sourced proteins in general. Secondly, while pork exports have been extra strong this year, the overall trend remains positive.

There will not be a broad return to hogs as the "mortgage lifter" across the Midwest for another reason. The structure of pork production is totally different today. Most families that elect to become part of the modern pork industry will do so as contract operations for larger hog corporations. In this way, they may become an important part of a highly technical and sophisticated production system that is cost efficient. While this may help lift mortgages on these specialized hog farms, the ownership, and therefore the profits, are much more concentrated into many fewer hands today. As an example, *Successful Farming* magazine reports that the 30 largest U.S. hog production companies now control 45 percent of all the nation's sows (October 2004 issue).

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