UNIVERSITY OF ILLINOIS EXTENSION

WEEKLY OUTLOOK

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HOG PROFIT PROSPECTS NARROW

Hog prices have lost their luster. After higher than expected prices in 2004 and 2005, prices so far this year have been disappointing given only small increases in supply. While supplies will only be up two percent in 2006, prices are expected to be down about 13 percent.

A comparison of prices in the first quarter this year with prices in the first quarter 2005 will make the point. Live hog prices for 51 to 52 percent lean carcasses were $52 per live hundredweight last year and $42 this year, 19 percent lower. In a similar fashion, wholesale loin prices were down 15 percent; bellies were down 10 percent; and wholesale ham prices were down 16 percent. Meanwhile, pork production was up less than 2 percent. These are large price declines for such small increases in supply. The 2 percent larger supply this year will result from a 1 percent increase in the sie of the breeding herd and the other 1 percent will come from increased number of pigs per litter and heavier marketing weights.

The number of sows increased by 84,000 in the past year according to USDA's March *Quarterly Hogs and Pigs* report. The largest increases were in Iowa (20,000); Indiana (20,000); and Missouri (15,000). Given the favorable level of profitability in 2004 and 2005, these were small increases.

Since pork supplies do little to help explain much lower prices compared to year-previous levels, analysts quickly look to demand components for possible answers. While pork supply increases have been moderate, beef supply increased by 5 percent in the first quarter of 2006 on 2 percent greater slaughter volumes and 3 percent higher weights. In addition, Avian Influenza in parts of Europe and Asia have reduced demand for chicken and resulted in reduced exports from the U.S. Broiler exports were about 9 percent lower in the first quarter than had been anticipated. As a result, there has been nearly 5 percent more chicken in the domestic market as well.

Retail pork prices have also been slow to drop as hog prices moved lower. Retail prices were down about 5 cents per retail pound for the first two months of this year. However, the farm level value is down 17 cents per retail pound while the marketing margin is up 12 cents. This means that producers are receiving about 27 percent of the retail dollar so far this year compared to 32 percent for the same period last year. Rather than say the farmers' share is too low this year, it is more likely that the farmers' share was unusually high the last two years (and thus the higher than expected hog prices).

Hog prices are expected to average about $43.50 per live hundredweight in 2006 compared to $50 in 2005 and $52.50 in 2004. Second quarter prices are expected to trade in the $44 to $47 range with the summer quarter averaging about $1 lower at $43 to $46. Prices are expected to average $40 to $43 in the final quarter of the year and then $38 to $42 in the winter. Given current anticipated corn and soybean meal prices over the next 12 months, hog prices could drop to costs of production at times this fall and winter when costs are estimated to be about $40 per live hundredweight.

Lean hog futures prices are now roughly equivalent to the prices forecast here, so forward pricing with futures does not appear to be particularly attractive at this time. Historically, there has been a strong tendency for futures prices to experience seasonal increases in late-April and the first-half of May. If futures are able to add a few dollars per hundredweight over the next month, hedging could be considered, especially for those who need to be assured of profitable prices.

The potential for higher corn prices has become a somewhat increased concern since USDA's *Prospective Plantings* report showed a large reduction in potential corn acres. However, since the release of that report on March 31, new-crop corn prices have rallied relative to soybeans such that the incentive to plant corn is now as strong as soybeans according to Purdue University estimates. This likely means that not as many acres will shift to soybeans as suggested in that report, and that 2006/07 ending stocks of corn may be estimated at around 1.5 billion bushels, a bit more comfortable level. In addition, recent rains have eased Midwestern dry weather concerns, although some planting delays especially in the northern tier of the Midwest may now be a factor.

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