



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.

SEPTEMBER 27, 2010

HOGS: SAVED BY THE CORN ALARM BELL

Hog producers were ready to expand this fall. That may have been appropriate when the expectation of 2010 corn prices was close to \$3.50 in early July, but that is no longer an acceptable conclusion with expectations closer to \$5.00. Higher corn prices will cut margins over the coming 12 months, but hog producers can now avoid an expansion which would plunge margins deep into the red in late 2011 and 2012.

The clear message for the industry is “don’t expand and margins will be OK.” The other important message is that “the next two years will not be a repeat of the large losses of 2008 and 2009.” Fortunately, the September USDA survey indicates there are no signs of expansion yet. Producers report they have two percent fewer animals in the breeding herd than a year-ago. The primary story is in North Carolina where breeding herd numbers were down 110,000 head over the past year. In fact, without North Carolina, the net effect of all other states was close to unchanged. So will expansion occur? One key to watch is large corporate producers with production in North Carolina. There is likely little appetite for expansion over the next 12 months that would throw the industry back into losses.

The number of market animals on September 1 was down three percent. This will lead to a reduction of three percent in slaughter numbers in the last quarter this year and one percent in the first quarter of next year. This fall’s farrowing intentions were down one percent and will result in unchanged to one percent higher slaughter numbers in the second quarter of 2011. This winter’s farrowing intentions move up modestly and would result in a one to two percent increase in slaughter numbers next summer. The final quarter of 2011 might see slaughter numbers up two to four percent.

Marketing weights dropped below year ago levels in late August as higher corn prices began to have an impact. Given the expectation for corn prices to remain high for the 2010 crop, it is likely that weights will continue to be down one half to one percent through next summer. This means pork supplies will be down three percent in the fourth quarter this year, down two percent in the first quarter of 2011, unchanged in the second quarter, up two percent in the third quarter, and up three to four percent in the final quarter of 2011.

The U.S. average corn price will be at record high for the 2010 crop and may approach \$5.00 per bushel. This is sharply higher than the \$4.20 average for the 2007 crop, so why won't the pork industry repeat the losses of 2008 and 2009? There are three critical reasons: 1) pork producers have adjusted their herds lower such that they can pay \$5.00 per bushel for corn and still maintain positive margins, 2) the U.S. and world economy will continue to recover, and 3) H1N1 will not deflate hog prices.

The high cost of pork production resulting from high priced corn has been passed to consumers. Consumers are now paying record high prices for pork. Retail prices averaged \$3.23 per pound for the most recent month compared with an average of \$2.93 in 2008 and 2009. It was a long and difficult adjustment for the industry to reduce production over the past three years, but that is behind. Now, national average hog prices will be high enough over the next 12 months to pay up to \$5.50 per bushel for corn and still cover all costs. This is a much different situation than in 2008 and 2009 when the breakeven corn price for hog producers was only \$2.70 per bushel.

Hog prices are expected to average about \$55 on a live weight basis for the final quarter of 2010 with a breakeven corn price of \$5.15. A \$56 average price is expected for the first quarter of 2011 with a breakeven corn price of \$5.30. Prices should rebound in the second and third quarter, averaging \$60 and \$57, with corn breakeven prices of \$6.10 and \$5.50 per bushel. If production is up as much as four percent in the final quarter of 2011, prices will drop back near \$50 and corn breakeven prices drop to \$4.10. This demonstrates how even a modest expansion can put margins at risk.

Plans for expansion need to be put on hold for another year, until the size of the 2011 corn and soybean crops are reasonably known. World corn inventories cannot be rebuilt on Southern Hemisphere production this winter. A large crop in the U.S. and Northern Hemisphere in 2011 will be required to begin to restore inventories.

Pork producers should not panic. This is not a repeat of 2008-2009 and producers can get through the coming 12 months. They should avoid expansion, increase feed efficiency, and reduce marketing weights and margins should remain positive. Fear about the 2011 crops is already building among hog producers wondering how high corn prices can go if that crop is not record large.

That is panic thinking. For now, don't expand; do what you can and leave 2011 adjustments to 2011.

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