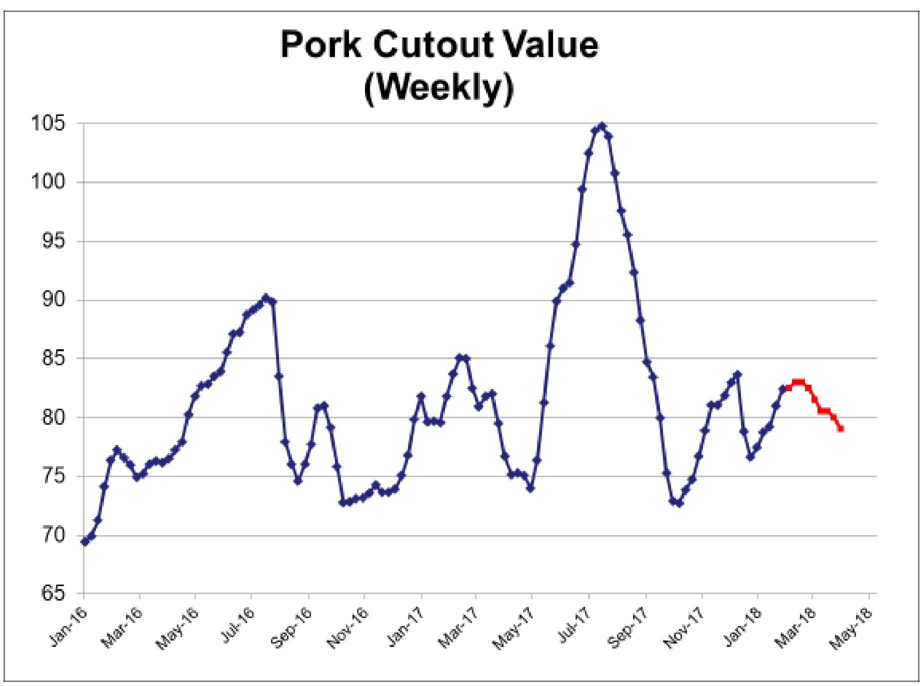
MEAT MARKETS
UNDER A MICROSCOPE

A perspective on the red meat markets by Kevin Bost...sometimes wrong, usually scientific, but always candid

January 28, 2018

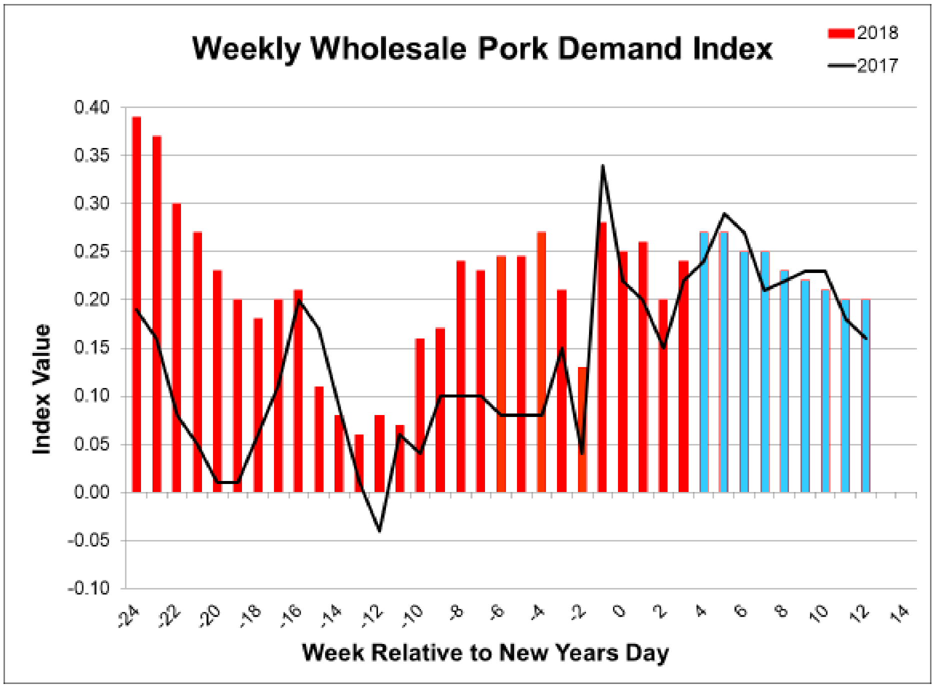
Hog slaughter is not quite keeping pace with the volume indicated by USDA's estimate of last summer's pig crop. It's not a huge discrepancy, but big enough to lower my sights for February—which I am now thinking will average 2,357,000 per week. I always make such "midstream" adjustments grudgingly, and yet in the interest of objectivity, I have to react whenever something appears to be "out of whack". In this case, the January kill is turning out to be unusually light relative to the initial projections for rest of the quarter…. this along with the fact that through the first three full-production weeks of 2018, hog slaughter is running just 0.9% above a year ago. A February average of 2,357,000 would be up 1.3%.

Anyway, it appears that kills over the next five weeks will hold essentially steady with this past week's output (2,370,000), which would accommodate a sideways trend in the pork cutout value during the same time frame. This should be followed by a mild downturn in March. My humble forecasts are represented by the red dots in the picture below:



The presumed weakness in March should result mainly from a slide in both ham and belly prices. I'll come back to these topics in a minute.

I am assuming that wholesale pork demand will follow a typical seasonal path—reflected by a relatively flat demand index—through mid-February…. and why not? But I am assuming that demand will slightly "underperform" afterward. My reasoning for the latter is sort of flimsy—it is mainly that the major peaks and troughs in the index value have been occurring at roughly the same times as they did last year. I don't know *why*, but they have. As long as it works, I'll cram anything into the Crystal Ball.



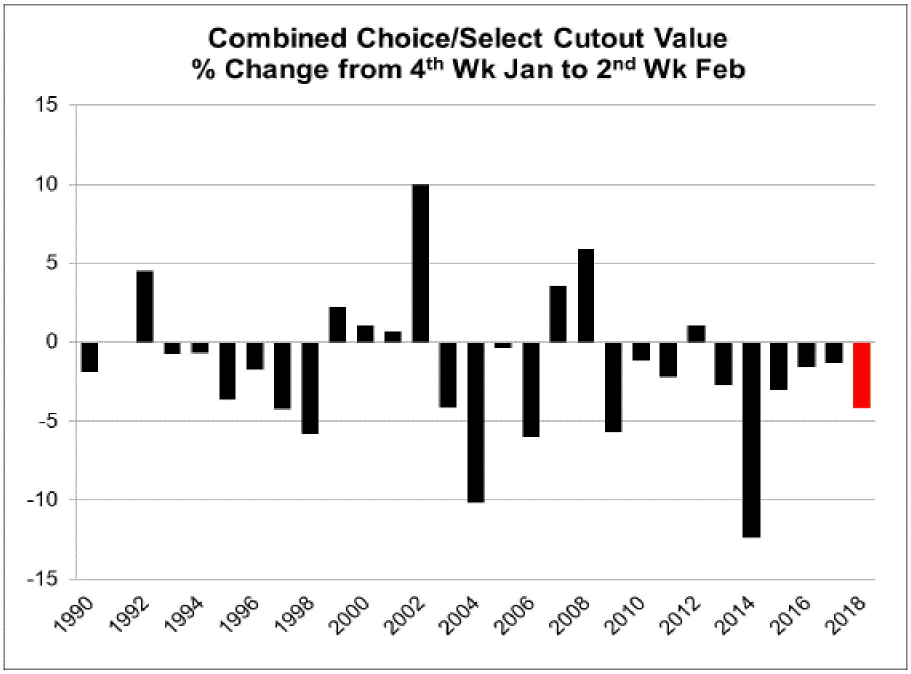
OK, then, what about the bellies and hams? As I expect only modest changes in loins (stronger), lean trimmings, (weaker), and boneless picnics, spareribs, and butts (steady) in the near term, hams and especially bellies will dictate the action in the cutout value.

I was only slightly less anxious about last week's *Cold Storage* report than I was by the revelation that Aaron Rodgers and Danica Patrick are now dating (*What*?). It is the buffer stock of frozen product that will distinguish the 2018 pork belly market from that of 2017. It turns out that there was an unusually small increase in belly stocks during December, but an increase nonetheless. I am also told by people who should know that there has been a small in-movement here in January—maybe a million pounds. If so, then the February 1 inventory will be 41 million pounds vs. 14 million a year ago. If nothing weird happens between now and then, then the May 1 peak will be close to 60 million vs 34 million. One would think that under these conditions, there would still be a sizeable, seasonal rally in store for the late spring and summer, but nothing near the July 2017 peak of $2.20 per pound.

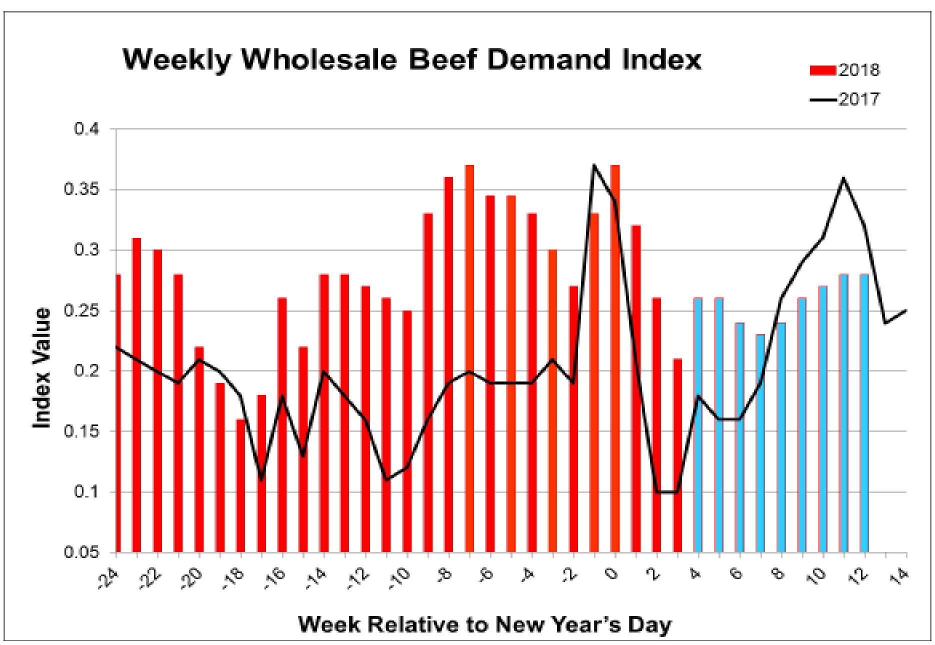
Closer-in, I have to believe that prices pushing $1.50 per pound are stifling demand for bacon from the supermarket sector, just as they did in late November/early December. If so, then this market will have to go through a correction in February/March in order to prevent a more serious downturn in demand this spring. Remember that as late as May 2, 2017, bellies were trading at $1.10. I'm not saying that prices will have to drop this low again, but there is no support on the chart between here and there….

As for hams, the fact that January 1 freezer stocks stood at an all-time high for that date—81 million pounds vs. 69 million a year earlier—makes one wonder if the pre-Easter peak might not be very close at hand, considering that hams are already trading about a nickel above their equivalent peak a year ago. A post-Easter slump down to $.55 per pound would shave roughly $3.50 per cwt off the cutout value by late March.

The unimpressive historical track record of the combined Choice/Select beef cutout value, along with relatively light forward bookings for February delivery dates, sustain my suspicion that the beef market is headed downward in the near term.

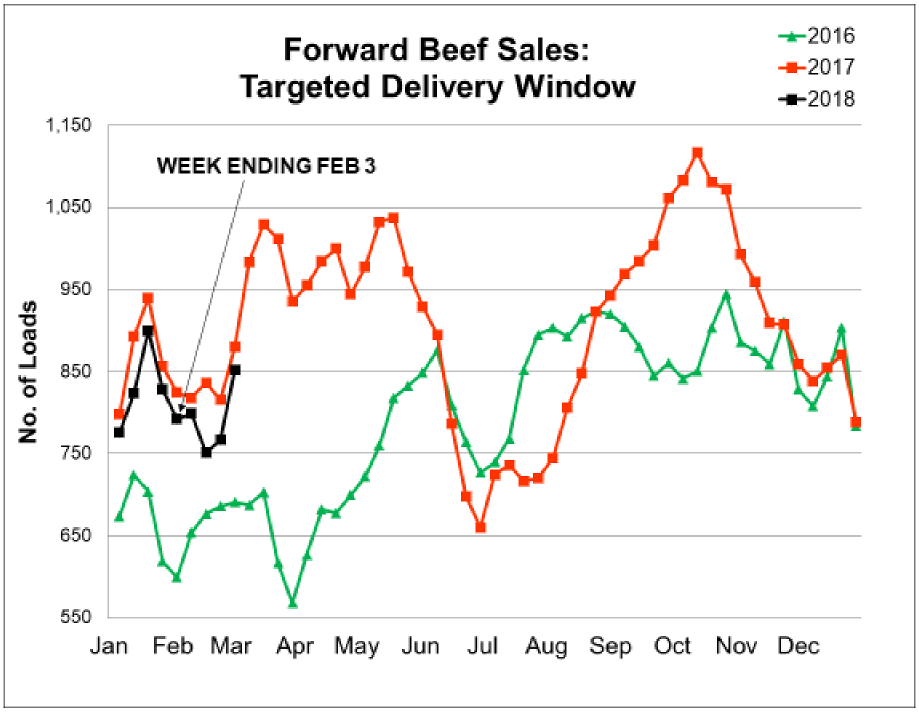


Identifying the seasonal tendency is of limited predictive value, but then again, what reason is there to think that there should be a departure from the norm this time around? I guess we could expect a stronger-than-usual market if production were to show an extraordinary drop into February, but that does not seem to be the case; fed beef production is on target for a 1.3% decline from January to February this year, only slightly greater than the 15-year average decline of 1.1%. Or, maybe an exceptionally firm beef market would result if wholesale demand were severely depressed and overdue for a cyclical rebound. Now, this condition *might* be applicable, judging by the weekly demand index. The index value has indeed slipped backward quite a bit over the last three weeks:



However, in order for the combined cutout value to match its current quote ($206 per cwt) in the middle of February, the demand index would have to jump to about .30, higher than my forecast of .24. It's not such a tall order, really, but how could that happen if retail features are to taper off as promptly as forward booking activity suggests?

The quantity of product pre-booked for February delivery is not dismal, but it has clearly been below a year ago…. not exactly indicative of a counter-seasonally strong beef market.



My guess is that the combined cutout value will retreat back toward its nearest conspicuous support level, which is $195.51. That would make for a $10 per cwt decline between now and the next cyclical bottom. I am counting on the chuck and round cuts (and chuck rolls in particular), briskets, 50% lean trim, and ground beef to be the sponsors.

Meat Markets Under a Microscope is published weekly by Procurement Strategies Inc., 99 Gromer Road, Elgin IL 60120. For subscription information, please contact Kevin Bost at (847) 212-7523, or visit our website at www.procurementstrategiesinc.com.