

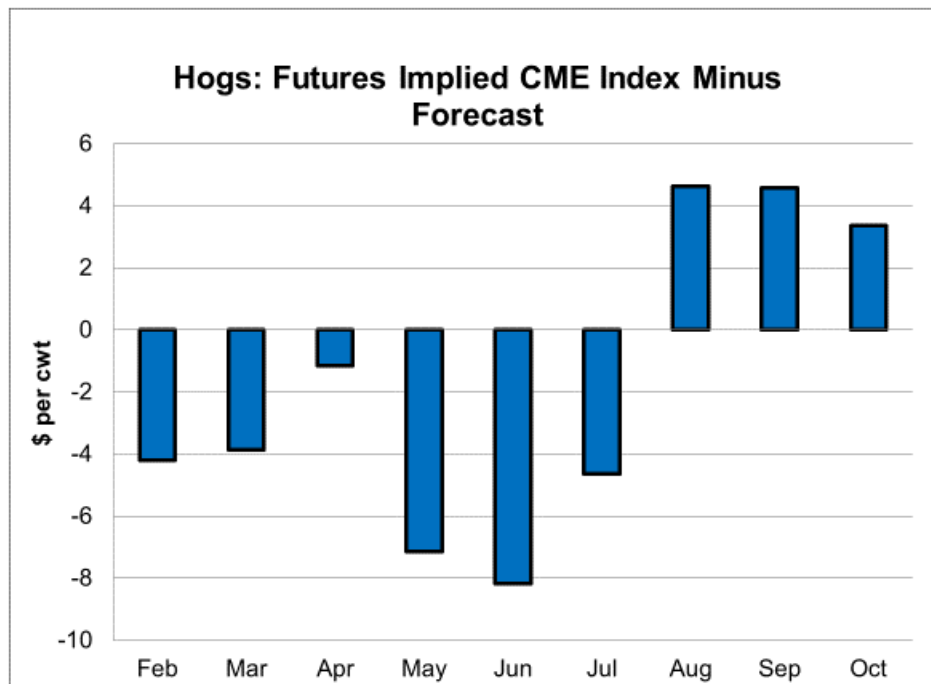
# Trading Hogs

## .... from a meat market perspective

A commentary by Kevin Bost

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January 14, 2019



I hold an aggressive long position in February hogs, such that I have no intention to add to it. To do so would turn this into an oversized bet and expose my capital to a greater amount of

risk than I had originally intended—a major violation of basic money management rules, which I have learned the hard way. I’m talking to myself here, as I always do in these letters.

The upside objective remains in the \$67-\$68 range. In order for the CME Lean Hog Index to reach \$57 before the February contract goes off the board would require that it gain an average of \$.42 per cwt per day. [I estimate that the single-day Index value for today’s kill stands at about \$57.75.] Over the last ten reporting days, the average daily gain has been \$.49. Thus, at the moment, the current \$4.90 premium in the February contract does not appear to be excessive.

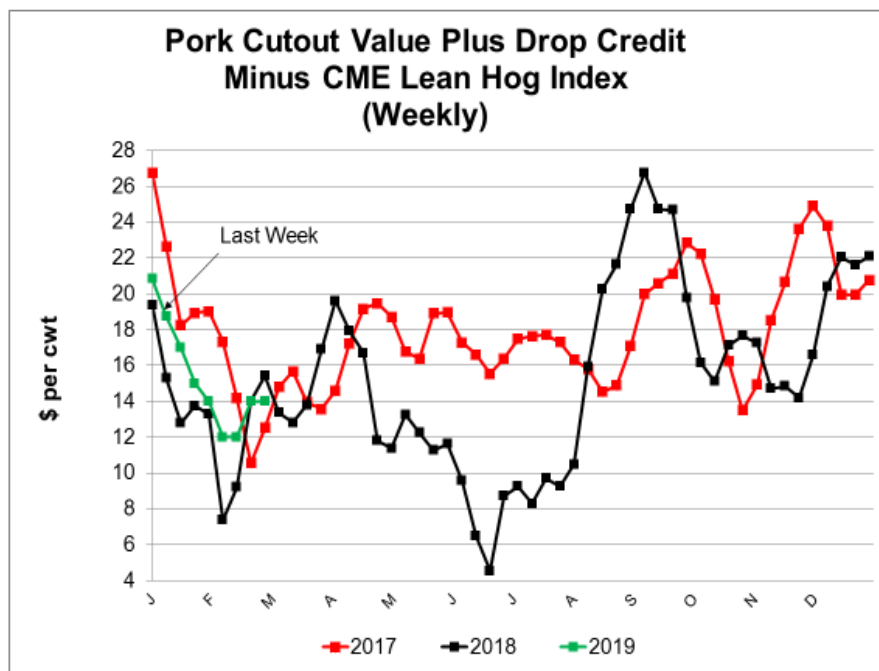
Let’s take a look at the potential “delinquents” in my forecast.

One is the ever-present possibility that hog supplies are bigger than we think they are, although I see no sign of that at this point. I am depending on a drop in

hog slaughter down to something near 2,500,000 this week, followed by another leg down to 2,450,000 in early February, to give the pork cutout value some fuel from the supply side. This is the pattern suggested by USDA's summer 2018 pig crop estimate. Between now and the second week of February, the 15-year average change in the cutout value has been +3.9% while the average change in hog slaughter has been -2.7%; This time around, I am anticipating a 4.3% decline in hog slaughter and a 7.7% increase in the cutout value. Obviously, I am also anticipating a somewhat stronger-than-seasonally-normal demand pattern to develop over the next month, a notion which is justified by the prospect of active retail pork featuring.

In regard to the cutout value, the bellies, presumably, are headed for \$1.50 per pound, which leaves about 8¢ of near-term upside potential. Loins and hams are beginning to show a bit of an upward "bent", but much more is required; I would be unpleasantly surprised if both of these items did *not* make significant headway this week.

The greatest risk factor in the equation is the packer margin. It is indeed drawing in, but at a slower pace than I had anticipated. As of Friday, the quoted gross margin stood at \$18 per cwt; I am counting on a decline to \$12 in the first half of February to push the CME Index up to \$67 at that time. In the first half of February 2018 the gross margin averaged \$8.29:



And so, just as I would be seriously disappointed by a flat market in pork loins this week, I would be even more disconcerted by an unchanged packer margin.

In any case, I am restricting

my bets in the hog market to the lead option. I have little confidence in my projections of *any* of the major fundamental factors this spring and beyond,

except perhaps hog slaughter—not packer margins, not pork exports, not wholesale pork demand—because the timing and quantity of China’s purchases of imported pork are but a guess at this point.

But in the February contract, the parameters are pretty well-defined. The critical support lies at \$60, and the \$64 area has become an important resistance level. The downtrend line, the 40-day moving average, and of course, last week’s high are all situated in that neighborhood. A close above \$64.25 would seem to clear the way for a move up to \$68, which would be the next resistance level of any consequence. Thus, I have decided against selling out of my long position if the gap on the daily chart at \$64.45 is filled, especially after Friday’s rather sharp correction.

#### Forecasts:

	Jan*	Feb	Mar	Apr	May*	Jun
Avg Weekly Hog Sltr	2,460,000	2,448,000	2,453,000	2,403,000	2,321,000	2,284,000
Year Ago	2,339,270	2,396,090	2,403,610	2,370,400	2,258,700	2,220,400
Avg Weekly Barrow & Gilt Sltr	2,393,000	2,380,000	2,385,000	2,335,000	2,255,000	2,215,000
Year Ago	2,273,500	2,330,170	2,338,350	2,304,900	2,195,200	2,154,700
Avg Weekly Sow Sltr	60,000	61,000	61,000	61,000	59,000	61,000
Year Ago	57,620	58,640	58,540	58,500	56,600	58,400
Cutout Value	\$72.75	\$75.00	\$76.00	\$78.50	\$86.00	\$92.50
Year Ago	\$80.74	\$78.04	\$72.71	\$68.08	\$73.59	\$83.18
CME Lean Hog Index	\$60.50	\$67.00	\$68.00	\$68.50	\$80.00	\$88.00
Year Ago	\$70.97	\$71.61	\$63.51	\$56.47	\$66.77	\$81.13

*\*Slaughter projections include holiday-shortened weeks*

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