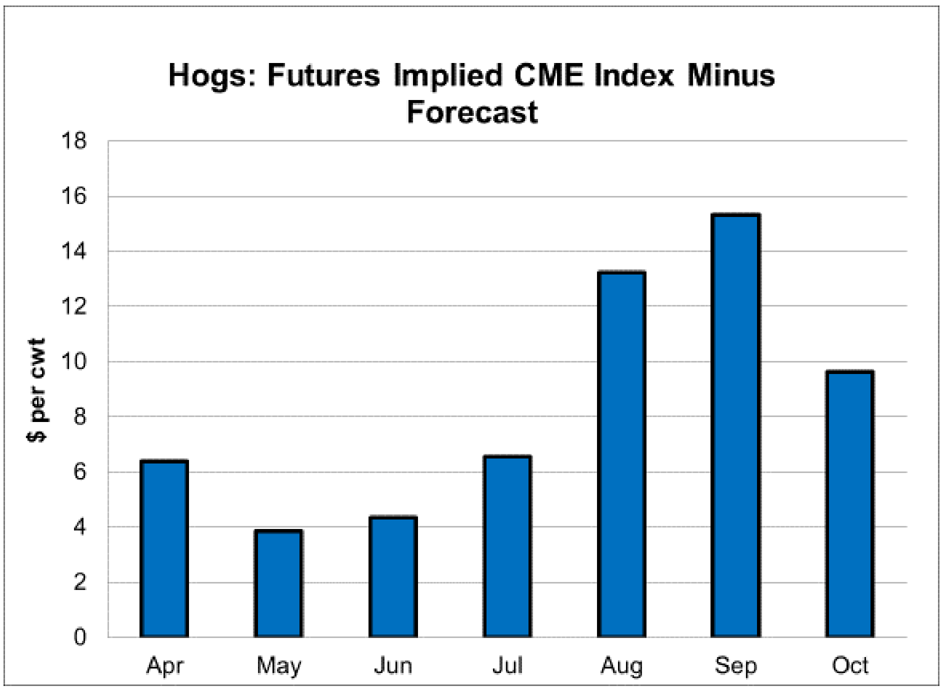
Trading Hogs
…. from a meat market perspective
A commentary by Kevin Bost

March 17, 2019

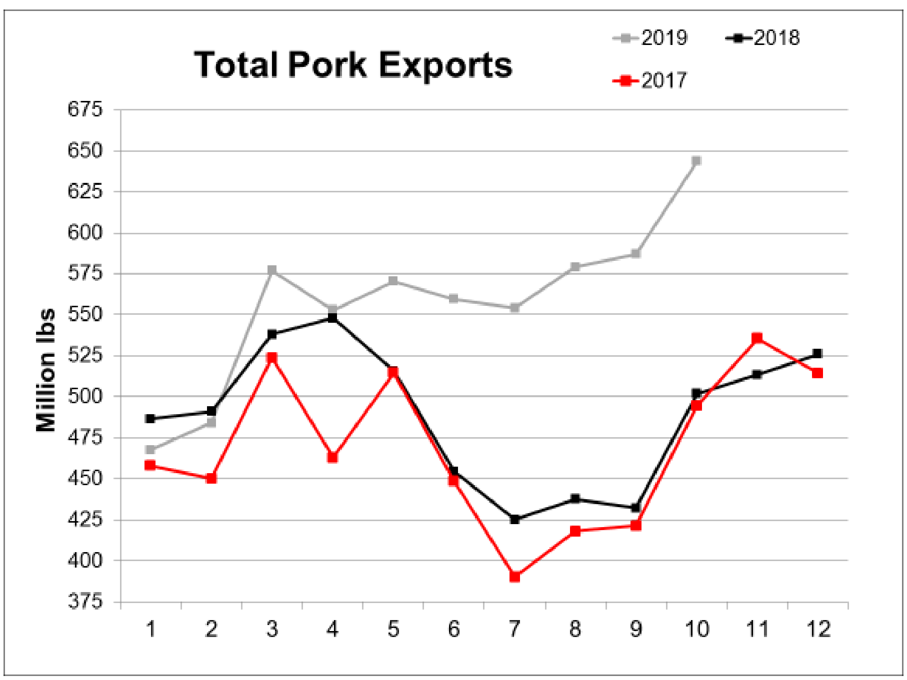


The central question in my mind at the moment is this: do I *really* need to be involved in the hog market right now? The picture to the left tells me that the market is probably too "rich" to bet on the long side; the futures charts tell me that if I'm going to play it from the short side, I'd better have a *damn* good reason--and a tight stop--before I lay my money on the table. Right now, I can think of no such reason. Finally, I have to constantly remind myself that under current conditions, my trading capital can suffer a massive drawdown in a very short period of time. Do I really want to take that risk?

Well, no. I do, however, hold a position in the long June/short August spread. I am risking this trade up to a new high close in the August-over-June premium (the existing high-water mark is $4.25). Comparing the prospective "fair values" of the two contracts, it appears to me that the June is worth considerably more than the August. Also, one would *think* that since the cash markets have turned emphatically upward, the front end would gain against the back. But the fact is, this spread has lost ground over the last four days, even as the June contract has rallied 650 points. The new longs in the hog market have gravitated toward the deferred contracts, presumably on the notion that the more time that goes by, the more pork the Chinese will buy, and the tighter domestic supplies will become. Without knowing how long this disparity of “money flow” can persist, I will let the market take me out if it proves that I have acted too early.

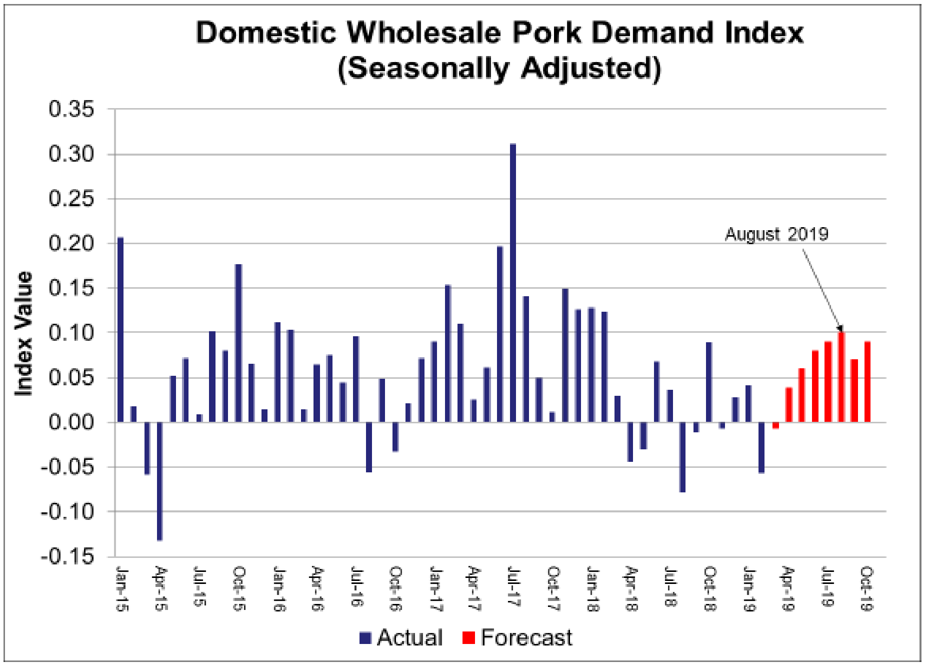
Since last week’s export sales report listed a Chinese purchase of 52.5 million pounds of U.S. pork, the clear indication is that this will be the first of many such buys. [And by the way, this also means that the futures market will now be hanging on to every detail of each Wednesday’s export sales report.] Let’s try to put this in some sort of perspective.

First of all, combined U.S. pork exports to China/Hong Kong/Taiwan averaged about 29 million pounds per month in the second half of 2018, and my guess--based on the weekly shipment data--is that they amounted to 40 million pounds in January and 50 million in February. So the new sales reported last week probably push the “Three-Region” pace up to about 60 million pounds. It’s a good start. And so I have ratcheted up my projections of U.S. pork exports--mainly in the second and third quarters, since the “time table” for Chinese purchases has been hustled up.



Without dragging you through more detail than you probably want to hear, I am factoring into my price forecasts an increase in monthly shipments to China /Hong Kong/ Taiwan from the current rate of 60 million pounds to 120 million by June; 150 million by August; and 160 million by October. My projections of total U.S. pork exports are shown above. Without having any idea of what I’m talking about, I think these are fairly generous assumptions. And factoring in these export quantities, I land on an average CME Lean Hog Index of $82 in June and $76-$77 in August. It’s almost laughable, isn’t it?

But the simple, statistical truth is that the August contract is discounting far greater export business than that. Assuming that pork production in August is up 1% from a year earlier, as suggested by the most recent estimate of winter farrowings; and assuming that domestic wholesale pork demand in August (after seasonal adjustment) is the strongest of any month in two years, as I show below; then it would require a rate of exports in August of more than 800 million pounds in August to drive the cutout value up to the $101-$102 mark that the board is pricing in today.



In somewhat calmer times and at some point down the road, the market will present an opportunity to sell August hogs that is justified by both technical and fundamental considerations. I can certainly afford to wait for that opportunity to come along.

Forecasts:

	Mar	Apr	May*	Jun	Jul*	Aug
Avg Weekly Hog Sltr	2,486,000	2,407,000	2,324,000	2,287,000	2,242,000	2,457,000
Year Ago	2,403,610	2,370,400	2,258,700	2,220,400	2,160,700	2,423,700
Avg Weekly Barrow & Gilt Sltr	2,419,000	2,340,000	2,260,000	2,220,000	2,180,000	2,390,000
Year Ago	2,338,350	2,304,900	2,195,200	2,154,700	2,099,000	2,358,200
Avg Weekly Sow Sltr	59,000	59,000	57,000	59,000	55,000	59,000
Year Ago	58,540	58,500	56,600	58,400	54,700	58,100
Cutout Value	$69.25	$74.50	$82.00	$88.00	$89.50	$88.50
Year Ago	$72.71	$68.08	$73.59	$83.18	$82.70	$69.05
CME Lean Hog Index	$57.50	$62.50	$74.00	$82.00	$83.00	$76.50
Year Ago	$63.51	$56.47	$66.77	$81.13	$78.73	$55.46

**Slaughter projections include holiday-shortened weeks*

Trading Hogs 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 Kevin_Bost@comcast.net; or visit our website at www.procurementstrategiesinc.com.