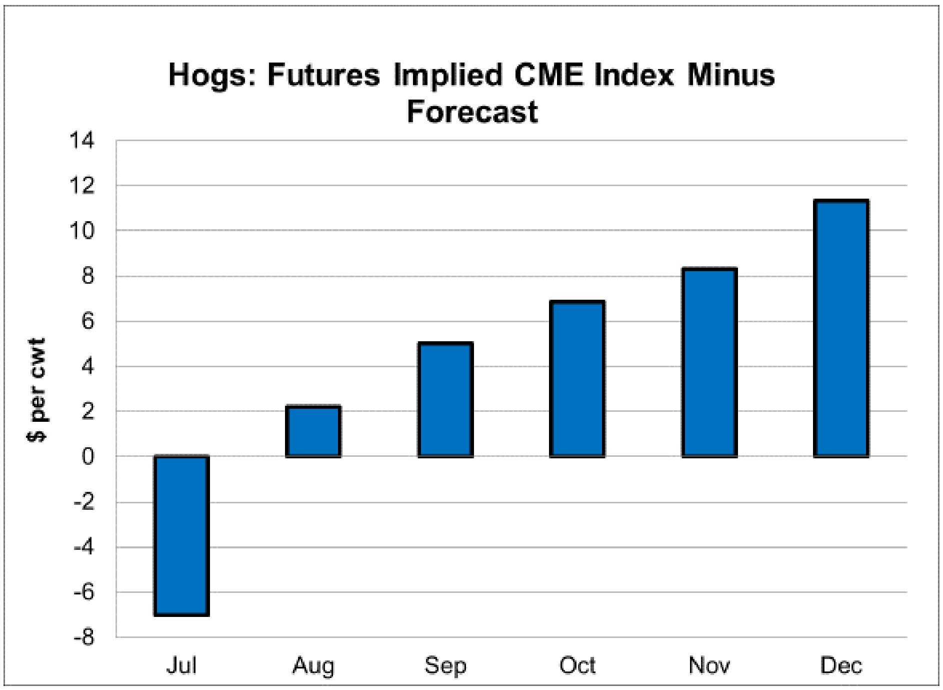
Trading Hogs

…. from a meat market perspective

A commentary by Kevin Bost

June 10, 2019



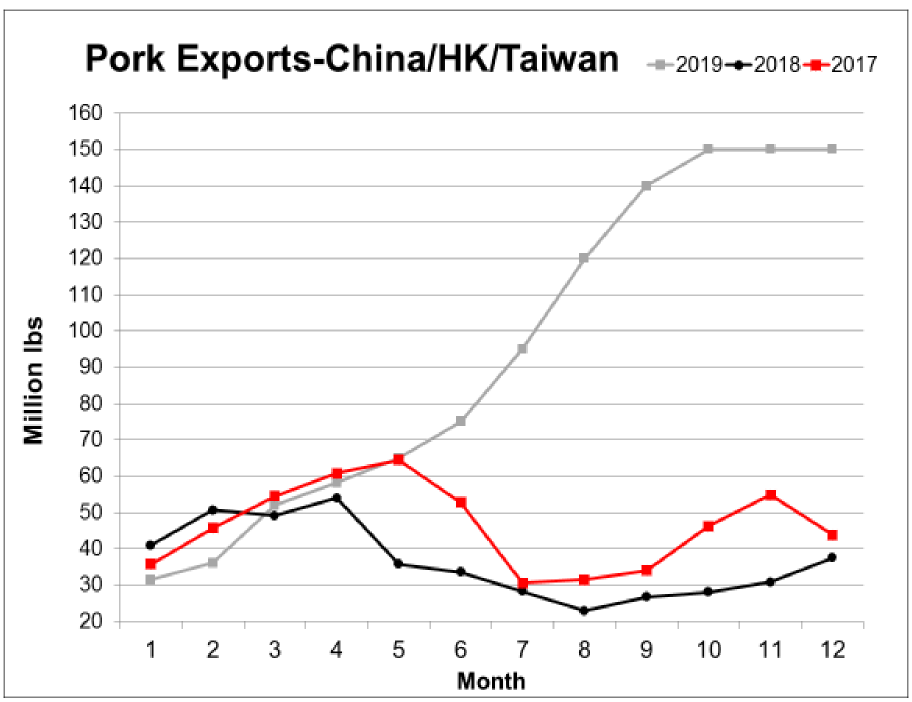
I was stopped out of my long position in the July contract on Friday, as the close below $83.55 was technically devastating and too weighty to ignore. It always stings to take a loss, but I guess I can take consolation in the fact that I adhered to the rules of good money management.

I am not finished with the long side of July hogs. As objectively as I can assess the upcoming supply and demand conditions in this market, the board is far too pessimistic about supplies, export prospects, or demand, or perhaps all of the above.

Let's address the supply side first. I acknowledge the possibility that hog supplies are much larger than suggested by USDA's winter pig crop estimate. But what evidence is there so far? The winter pig crop has just barely begun to be marketed. True, carcass weights are about three pounds heavier than a year ago. However, I'm not sure that this implies any sort of backlog. Temperatures have been considerably milder this time around; for example, the average daily high temperature in Des Moines during May 2019 was 69 degrees, compared with 82 degrees in May 2018.

If June-August slaughter aligns reasonably well with the winter pig crop estimate, and if kills in July fall within a typical range relative to the three-month total, then they will average somewhere in the neighborhood of 2,250,000 per week (in July, that is) including the shortened holiday schedule; that would be an increase of 4.2% from a year earlier. Applying a 3.3 pound year-over-year increase in carcass weights, that would bring about a 5.9% increase in pork production.

The supply of pork available to the domestic market will not be quite as large, due to increased exports. Of course, none of us knows exactly how that business will unfold. My guess is that U.S. exports to China/Hong Kong/Taiwan will rise from 58 million pounds in April (this is the most recent actual figure) to 95 million in July. It seems quite reasonable, especially since the Chinese government is allegedly preparing to grant exemptions from the 50% retaliatory tariff on U.S. pork to qualifying importers. I am projecting that total U.S. pork exports will decrease seasonally, from 525 million pounds in April to 514 million in July. Relative to a year earlier, though, they should be up 21%. And so the net domestic pork supply that I am inserting into the forecasting equation for July is up 2.1% from a year earlier.



In regard to demand at the wholesale level, my basic assumption is that it will moderately outperform the seasonal norm between now and July. I am assuming that as domestic supplies tighten in the weeks ahead, the seasonally adjusted demand index--which receded substantially in May--will return to the peak that it reached in April. I have to admit that this assumption is grounded as much in intuition as in fact.

But let’s say that the demand index does not improve at all from its May “pothole”. And let’s say that shipments of pork to China reach only 75 million pounds in July (up just 17 million pounds from April). And let’s say that gross packer margins average $10 per cwt at that time, $1.75 wider than last week’s average compared with last week’s average and $.88 wider than a year earlier. I think this describes a pretty pessimistic scenario--not fool-proof, but pessimistic. In that case, the cutout value would average about $87.50 per cwt and the CME Lean Hog Index would be between $82.50 and $83.00.

There is a channel line that passes just below $82.00 on the daily chart, and I am inclined to buy July hogs in modest quantity at that level if this downtrend continues. I will become more aggressive if the CME Index begins to print on the plus side, and/or if the cutout value pushes above $89, which is the upper boundary of its six-week trading range. I would also regard a close above $87.00 in the July contract a “green light”, as that would completely nullify Friday’s extremely bearish price action.

Forecasts:

	Jun	Jul*	Aug	Sep*	Oct	Nov*
Avg Weekly Hog Sltr	2,317,000	2,252,000	2,457,000	2,516,000	2,615,000	2,587,000
Year Ago	2,220,400	2,160,700	2,423,700	2,359,000	2,550,000	2,498,800
Avg Weekly Barrow & Gilt Sltr	2,252,000	2,190,000	2,390,000	2,450,000	2,545,000	2,520,000
Year Ago	2,154,700	2,099,000	2,358,200	2,294,600	2,480,900	2,433,500
Avg Weekly Sow Sltr	58,000	55,000	59,000	58,000	62,000	59,000
Year Ago	58,400	54,700	58,100	56,500	61,100	57,300
Cutout Value	$88.00	$94.50	$92.00	$86.00	$83.50	$81.00
Year Ago	$83.18	$82.70	$69.05	$74.33	$78.56	$69.41
CME Lean Hog Index	$84.50	$90.50	$80.50	$69.50	$70.50	$67.50
Year Ago	$81.13	$78.73	$55.46	$55.31	$66.89	$59.17

**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.