

Profit Prospects for Pork Producers – 2010 and Beyond

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Paragon Economics, Inc.



Profit outlook for 2010 and 2011...

GOOD!

FINALLY!!!!



Profits for the foreseeable future because:

- Lower – but NOT LOW – costs with even lower input prices possible
 - EXCELLENT planting season
 - Acres are good, condition is good at present
 - It's up to Mother Nature – and maybe the EU
- Hog price recovery – better than expected
 - Slightly lower supplies
 - Stronger wholesale and farm demand
 - Help from competitors – but will it last?



Short-term risks to consider:

- Weather – the crop is not made YET
- Economic turmoil in Europe and the impact on \$US and exports
- Domestic demand if the “recovery” remains soft
- Quick supply response to profits
- A host of potential goofy occurrences – remember H1N1?



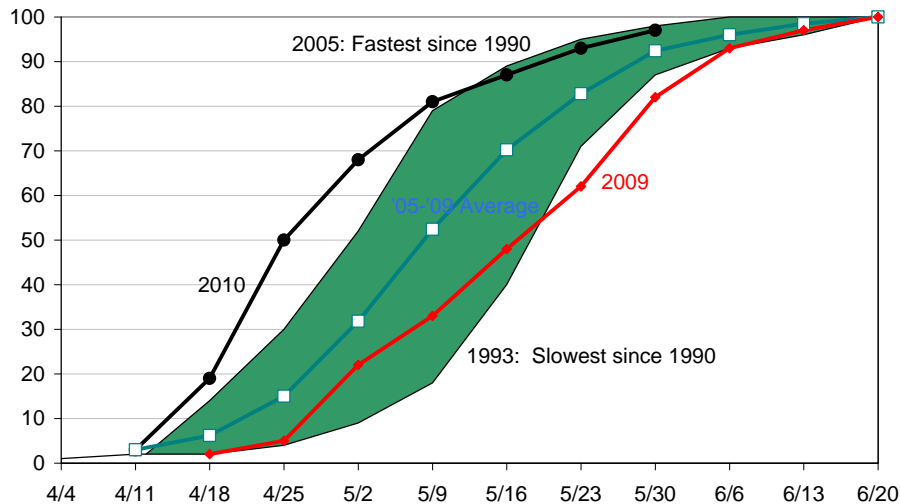
Grain and feed cost outlook – Issues:

- Record-early corn planting and very good crop condition
- Weak ethanol margins, “low” oil prices – will not be supportive of corn
- Modest increase in corn exports -- \$US???
- Expectations on E-15 decision
- El Nino – La Nina???
- Last week’s Crop Prod & WASDE – nothing big
- BIG REPORTS: June 30 Acreage & Stocks

Corn planting and condition

CORN CROP PROGRESS

Percent Planted, 18 States

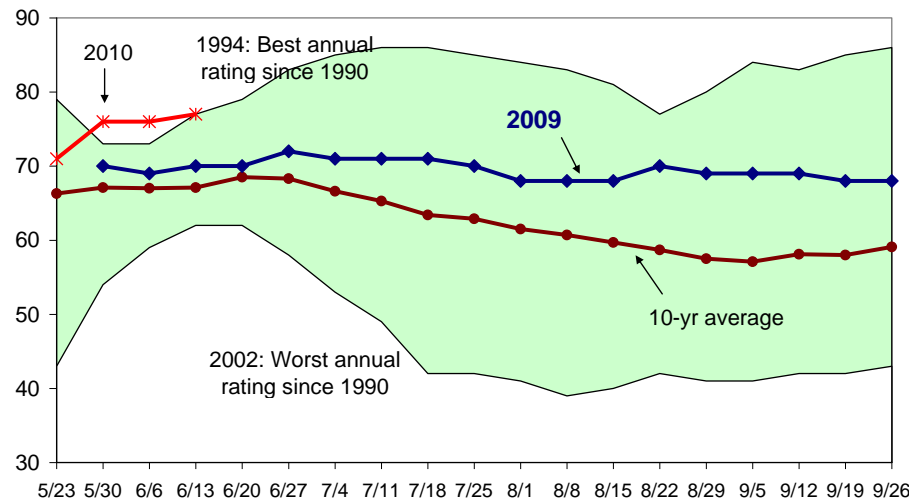


Corn planting is complete – but look when the bulk occurred!

Crop condition is the best ever for 1st week of June

CORN CROP CONDITION

Percent rated Good or Excellent



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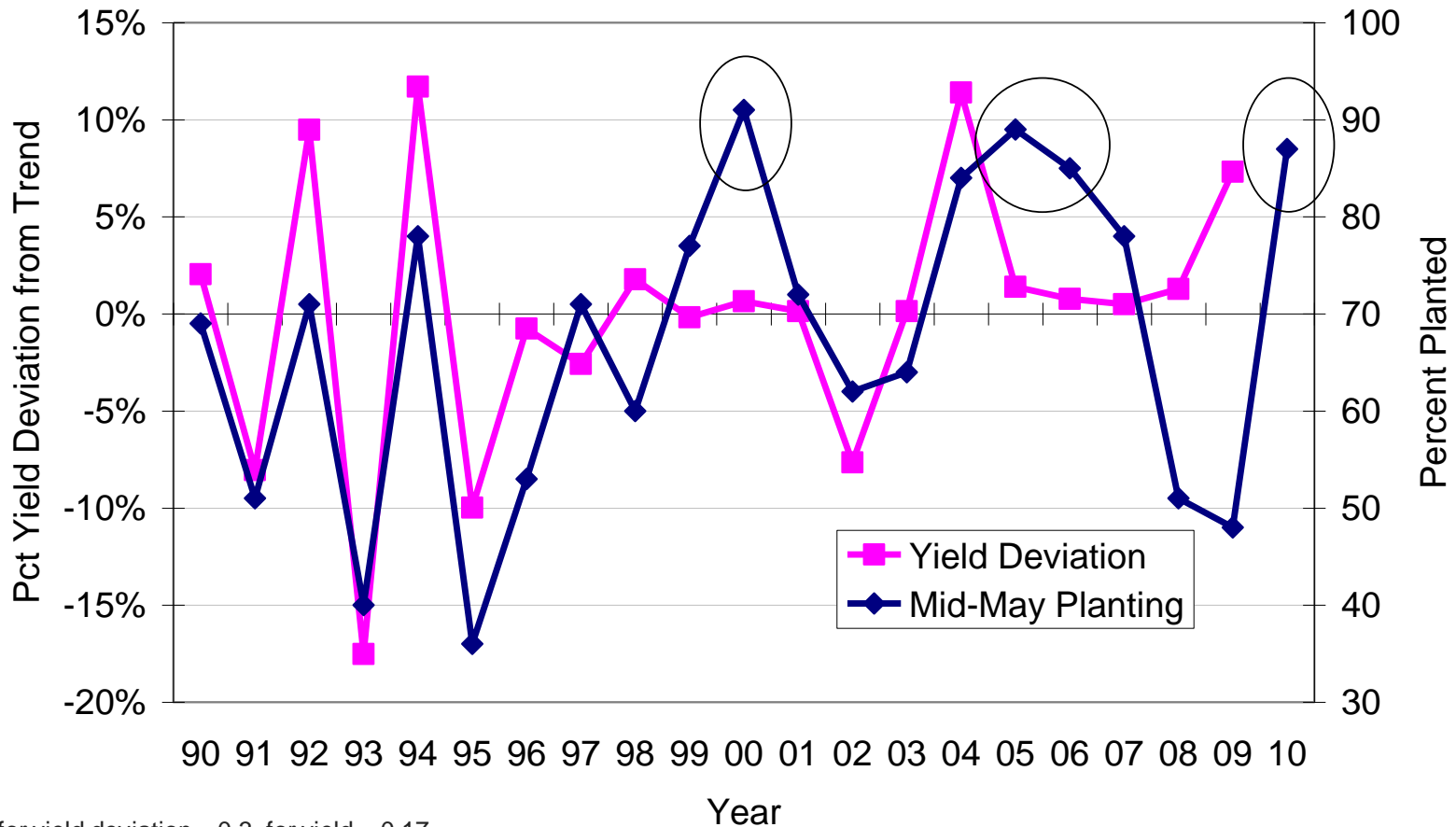
From information, knowledge



Planting progress, though ...

... Is NOT a good yield predictor

CORN -- YIELDS VS. MID-MAY PLANTINGS



R2 for yield deviation = 0.3, for yield = 0.17



June 2010 WASDE forecast by USDA

U.S. CORN SUPPLY AND UTILIZATION - JUNE

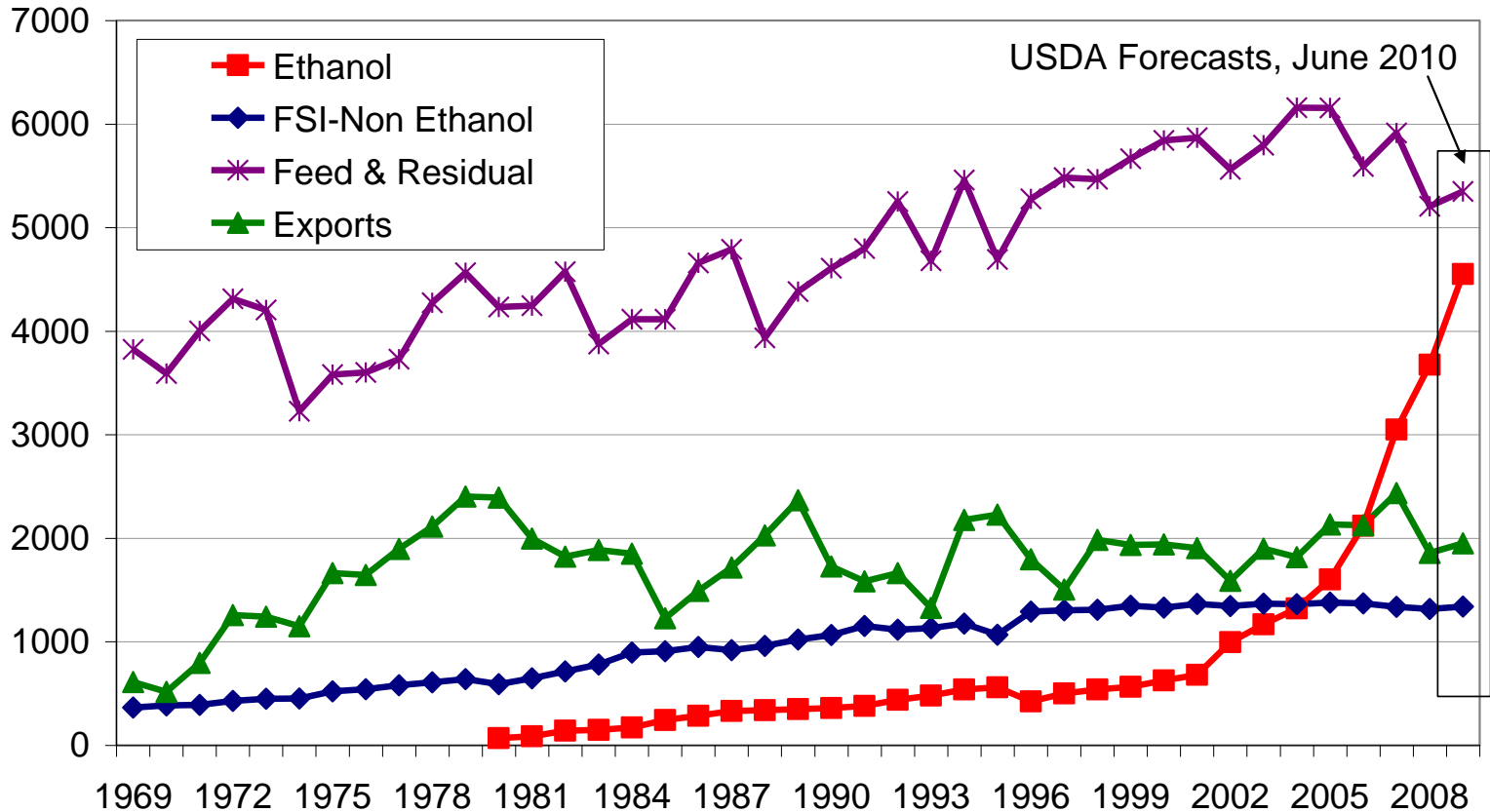
		2008/09	2009/10		2010/11	
			USDA, June	% Chng. vs '08-'09	USDA, June	%Chng vs. '09-'10
Acres Planted	Mil A	86.0	86.5	0.6%	88.8	2.7%
Acres Harvested	Mil A	78.6	79.6	1.3%	81.8	2.8%
Yield	Bu/A	153.9	164.7	7.0%	163.5	-0.7%
Beginning Stocks	Mil Bu.	1624	1673	3.0%	1603	-4.2%
Production	Mil Bu.	12092	13110	8.4%	13370	2.0%
Imports	Mil Bu.	14	10	-28.6%	10	0.0%
Total Supply	Mil Bu.	13729	14793	7.8%	14983	1.3%
Food, Seed & Ind	Mil Bu.	1316	1340	1.8%	1360	1.5%
Ethanol for fuel	Mil Bu.	3677	4550	23.7%	4700	3.3%
Feed & Resid	Mil Bu.	5205	5350	2.8%	5350	0.0%
Exports	Mil Bu.	1858	1950	5.0%	2000	2.6%
Total Usage	Mil Bu.	12056	13190	9.4%	13410	1.7%
Carryover	Mil Bu.	1673	1603	-4.2%	1573	-1.9%
Stocks/Use		13.9%	12.2%	-12.4%	11.7%	-3.5%
Nat. Wtd. Avg. Farm Price	\$/Bu.	4.06	3.45-3.65	-11.3%	3.30-3.90	-2.8%



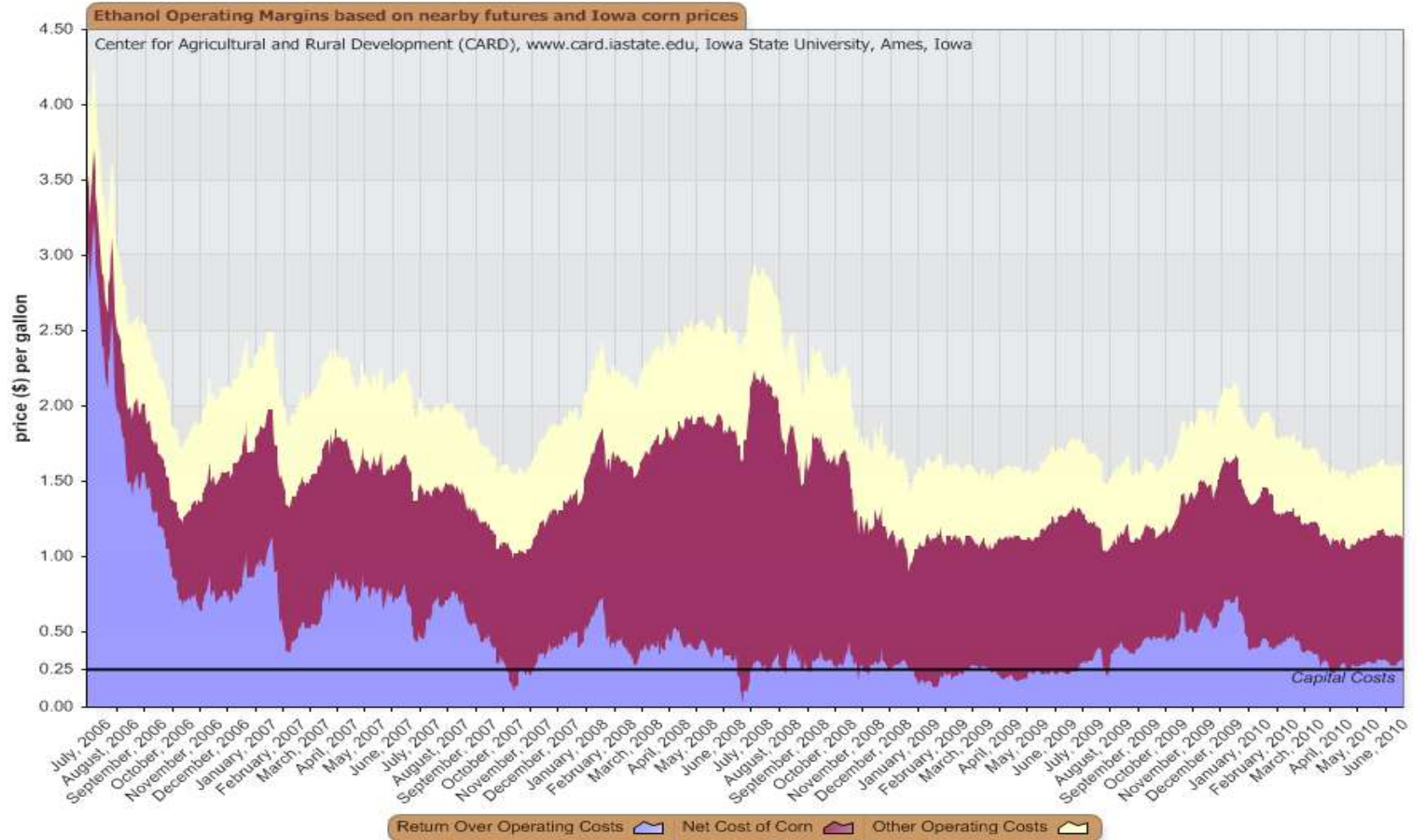
Usage - graphically

U.S. CORN USAGE BY CATEGORY

Million bu.

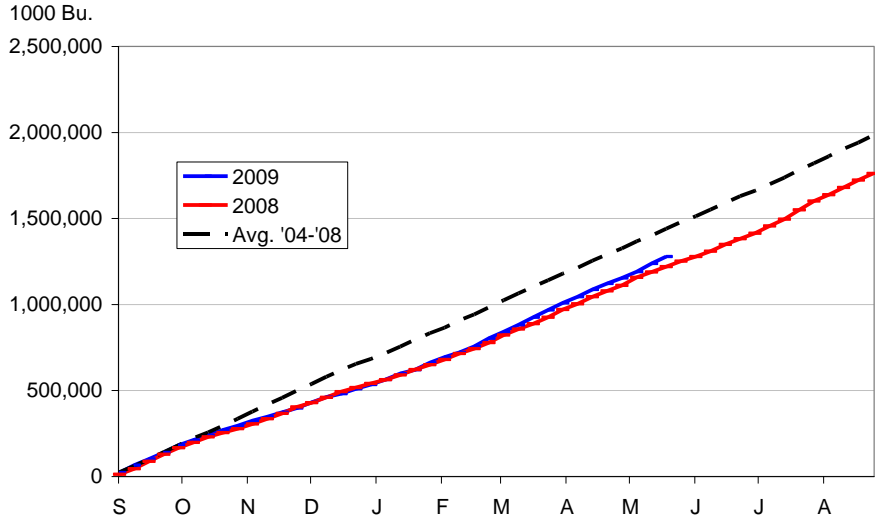


Ethanol margins have fallen -- again

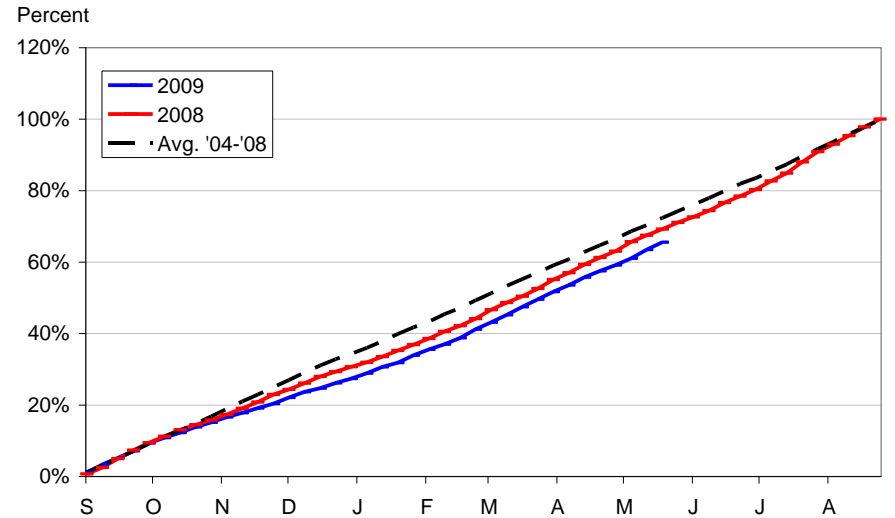


Corn export pace has been SLOW

U.S. CORN EXPORTS

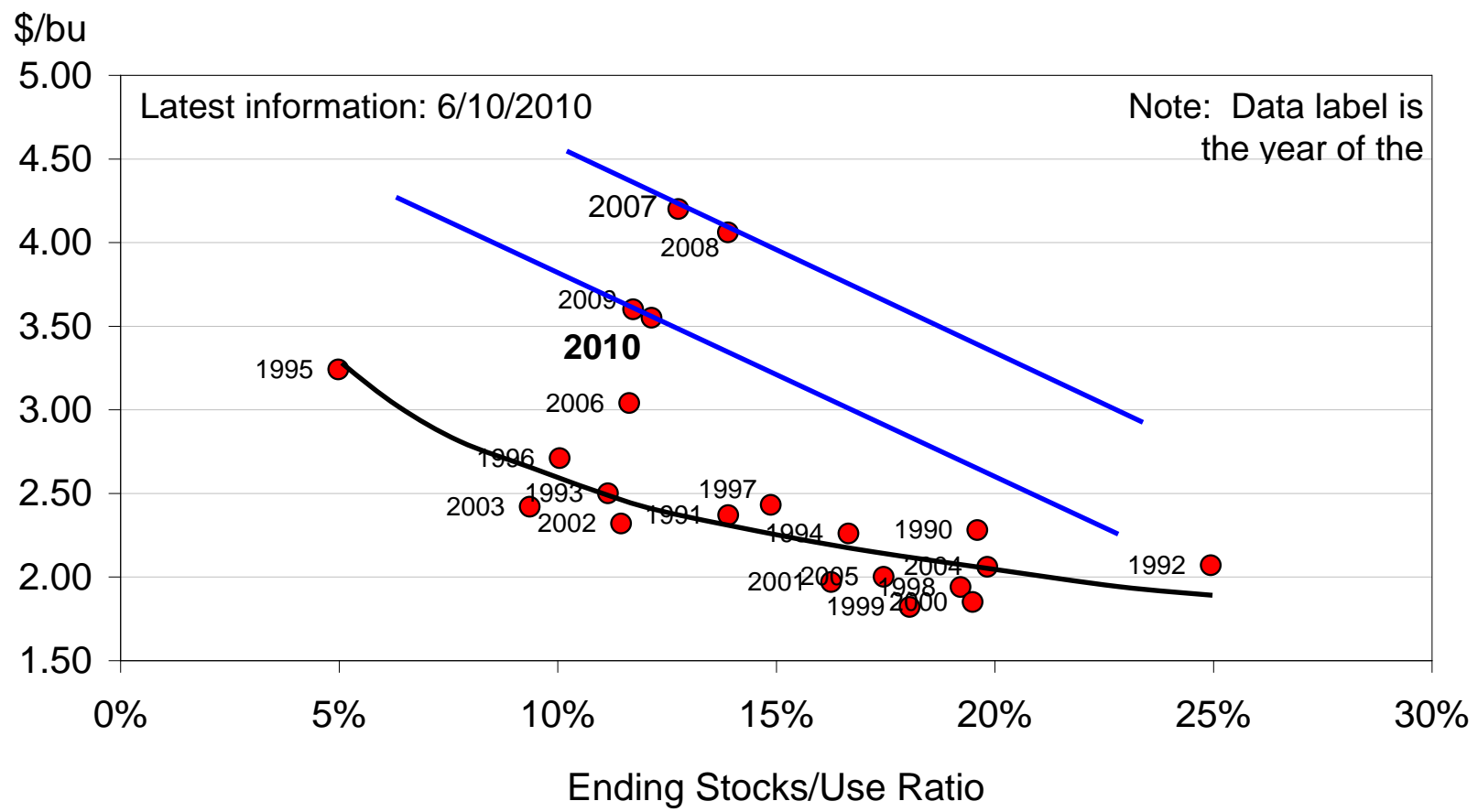


U.S. CORN EXPORTS, PCT. OF ANNUAL



2010 forecast is in line with '09 corn demand

U.S. CORN PRICE VS. S/U RATIO 1990-2010



Implications and risks

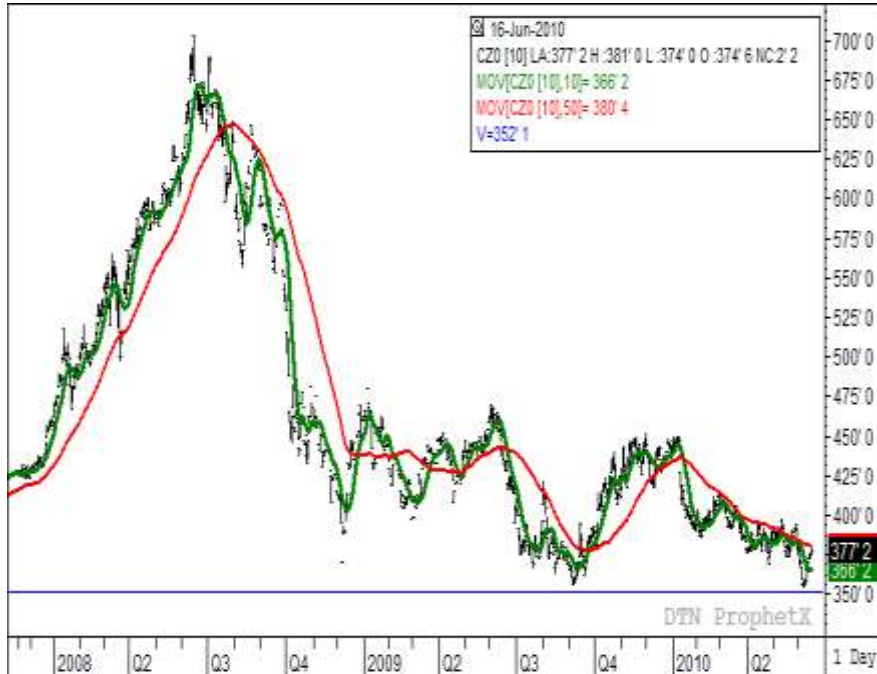
- Season-average price of \$3.60 implies an Iowa harvest price of \$3.10 to \$3.20/bu
- USDA yield of 163.5 bu./A is already 1.7 bu./A ABOVE the '96-'07 "biotech" trend
- Good crop conditions, lagging export pace may push corn lower through late summer



But new-crop futures found support ...

... At contract-life lows

Those “lows”, though, were at \$3.56 for Dec and \$3.88 for March!



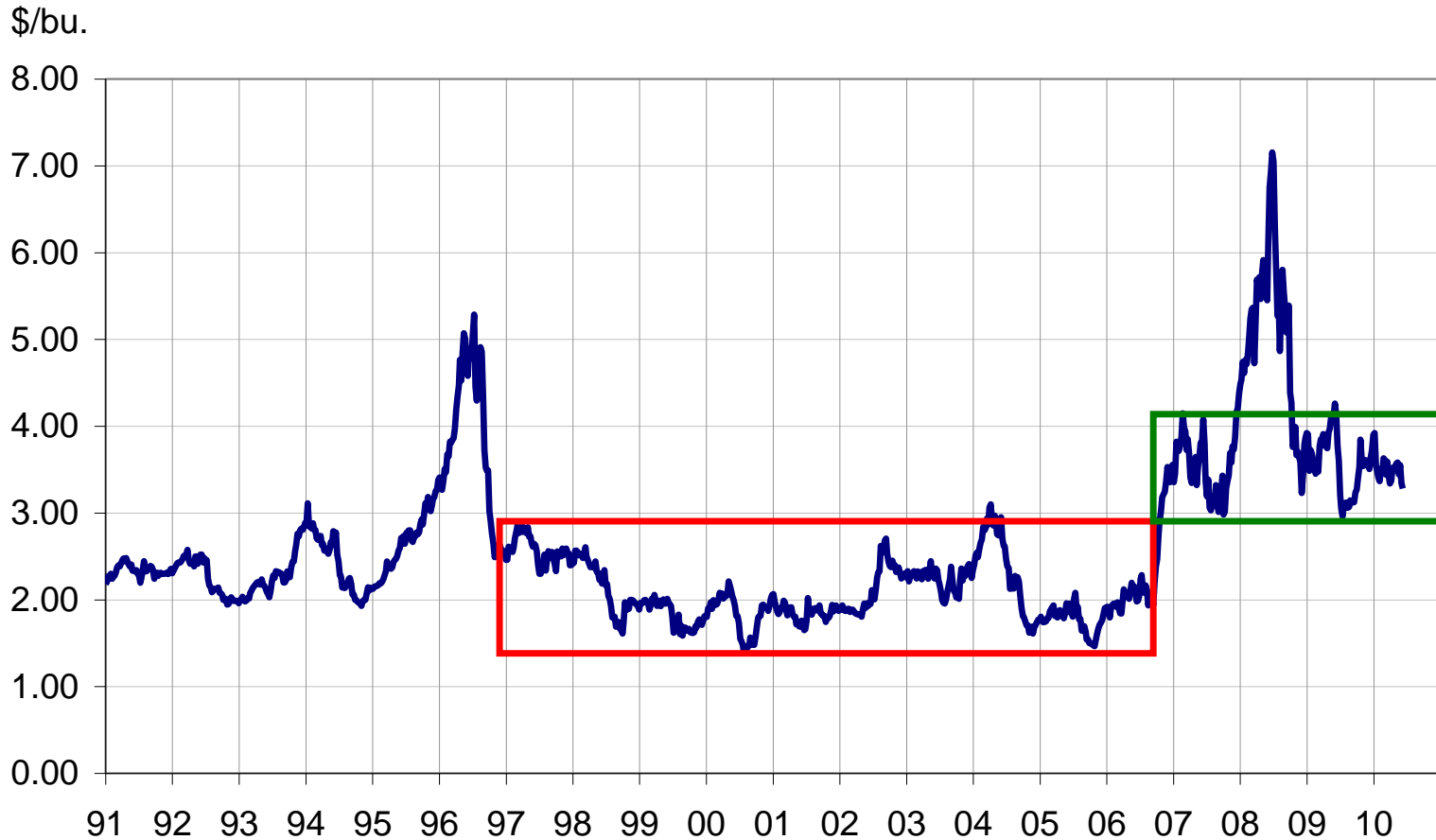
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How much bottom side is available?

CASH CORN PRICE, OMAHA, WEEKLY



Source: USDA, Agricultural Marketing Service

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Implications and risks

- Season-average price of \$3.50 implies an Iowa harvest price of \$3.00 to \$3.10/bu
- USDA yield of 163.5 bu/acre is 1.7 bu above the '96-'07 "biotech" trend
- Good crop conditions will push corn lower through late summer
- Remember -- Season lows were in Sept in '06, early Oct in '07 and July in '09

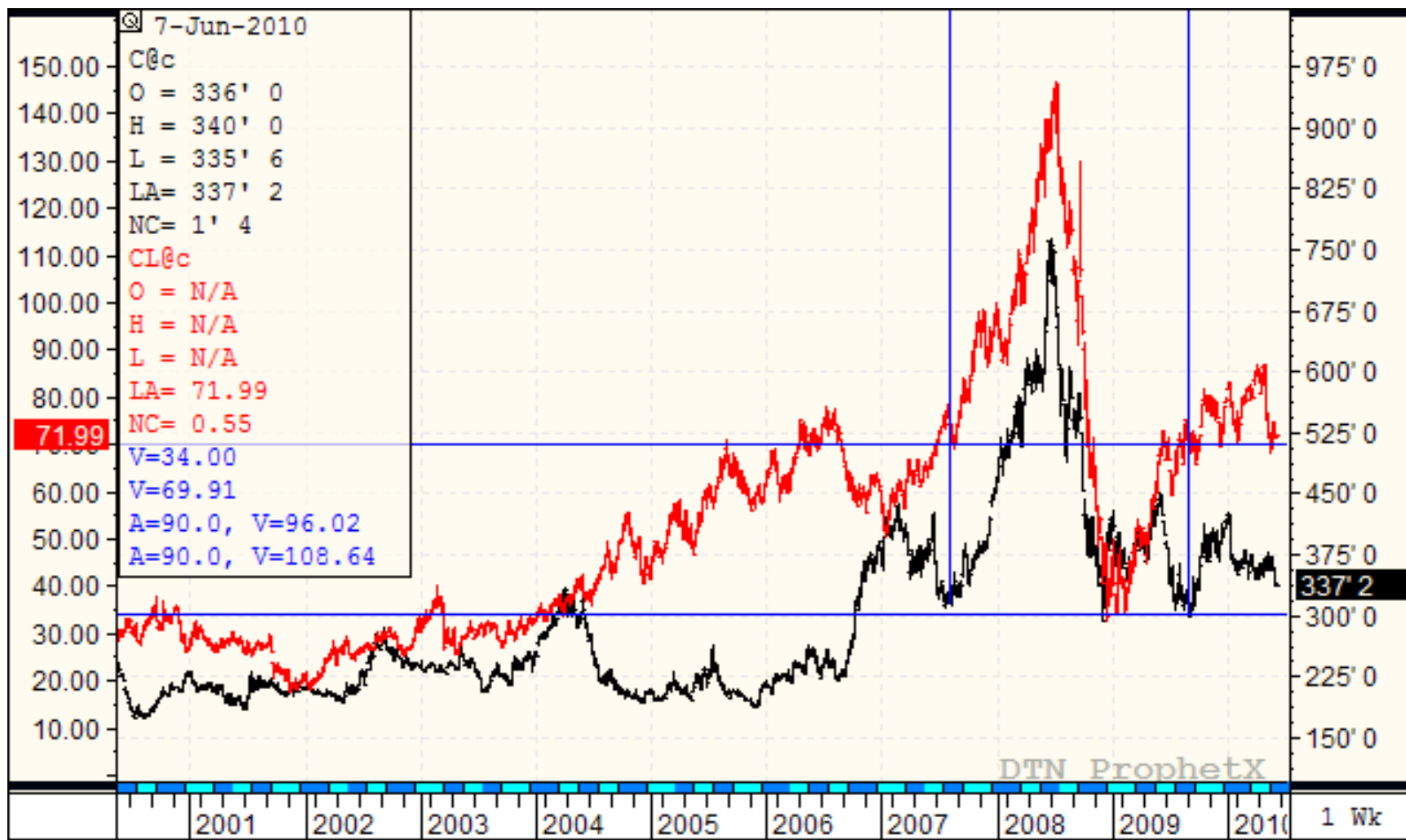


Implications and risks

- Season-average price of \$3.50 implies an Iowa harvest price of \$3.00 to \$3.10/bu
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- Good crop conditions will push corn lower through late summer
- Remember that season lows were in Sept in '06, early Oct in '07 and July in '09
- Strong \$US could keep oil prices – and ethanol prices -- in check



Oil is back near \$70 – less support for corn



Implications and risks

- Season-average price of \$3.50 implies an Iowa harvest price of \$3.00 to \$3.10/bu
- USDA yield of 163.5 bu/acre is 1.7 bu above the '96-'07 "biotech" trend
- Good crop conditions will push corn lower through late summer
- Remember that season lows were in Sept in '06, early Oct in '07 and July in '09
- Strong \$US could keep oil prices – and ethanol prices in check
- E-15 (or E-11 or E-12) decision



Corn strategies

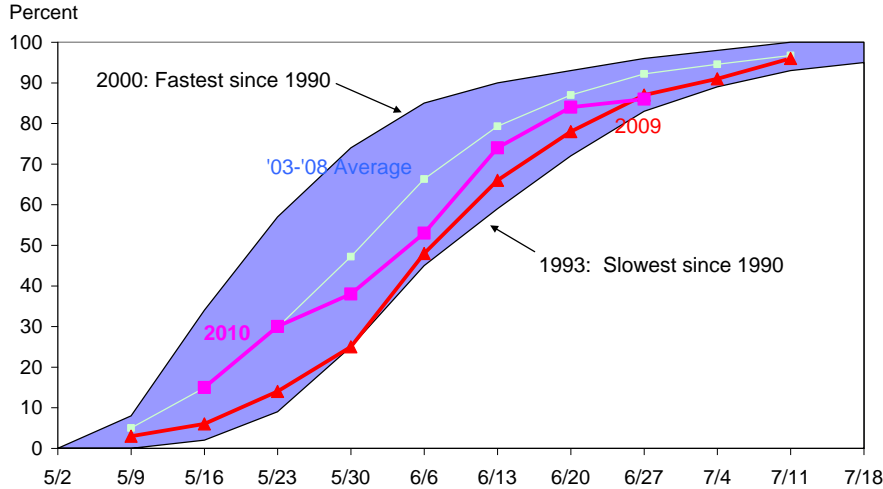
- Given the price outlook for hog --
 - “Higher” corn prices can be handled
 - Extreme corn prices, as always, cannot!
- Start filling storage EARLY in harvest
- Having physical corn in hand is normally advisable – perhaps not a big deal for 2010-11
- Buy “insurance” out-of-the-money calls if your balance sheet is still weak



Soybean planting and early condition

SOYBEAN CROP PROGRESS

Acres Planted, 18 States

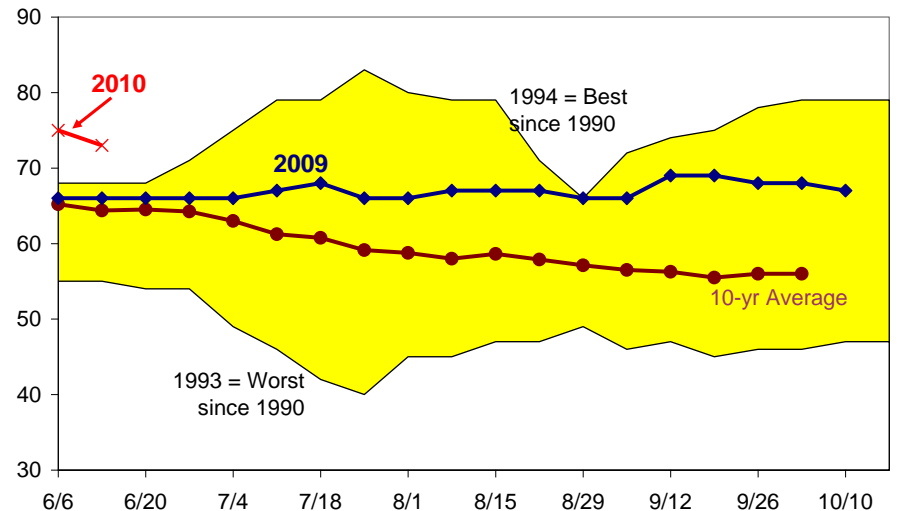


Soybean planting has been slowed by rain – now **EQUAL** to 2009

Crop rating this week is **RECORD HIGH** at **73% Good/Exc.**

SOYBEAN CROP CONDITION

Percent Rated Good or Excellent



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June USDA WASDE – 2X on S/U ratio for '11 ...

... But this summer could still be tight

U.S. SOYBEAN SUPPLY & UTILIZATION - JUNE

		2008/09	2009/10		2010/11	
		Est.	USDA, May	% Chng vs '08-'09	USDA, May	% Chng vs '09-'10
Acres Planted	Mil A	75.7	77.5	2.4%	78.1	0.8%
Acres Harvested	Mil A	74.7	76.6	2.5%	77.1	0.7%
Yield	Bu/A	39.7	44.0	10.8%	42.9	-2.5%
Beginning Stocks	Mil Bu.	205	138	-32.7%	185	34.1%
Production	Mil Bu.	2967	3359	13.2%	3310	-1.5%
Imports	Mil Bu.	15	15	0.0%	10	-33.3%
Total Supply	Mil Bu.	3187	3512	10.2%	3505	-0.2%
Crushings	Mil Bu.	1662	1740	4.7%	1640	-5.7%
Exports	Mil Bu.	1280	1435	12.1%	1350	-5.9%
Seed	Mil Bu.	95	91	-4.2%	88	-3.3%
Residual	Mil Bu.	11	42	281.8%	66	57.1%
Total Usage	Mil Bu.	3049	3323	9.0%	3144	-5.4%
Carryover	Mil Bu.	138	185	34.1%	360	94.6%
Stocks/Use		4.5%	5.6%	23.0%	11.5%	105.7%
Nat. Wtd. Avg. Farm Price	\$/Bu.	9.97	9.50	-8.2%	8.00-9.50	-7.9%
Soybean Oil Price	Cents/lb.	32.16	36.00	11.9%	34 - 38	0.0%
Soybean Meal Price	\$/ton	331.17	295.00	-10.9%	230-270	-15.3%

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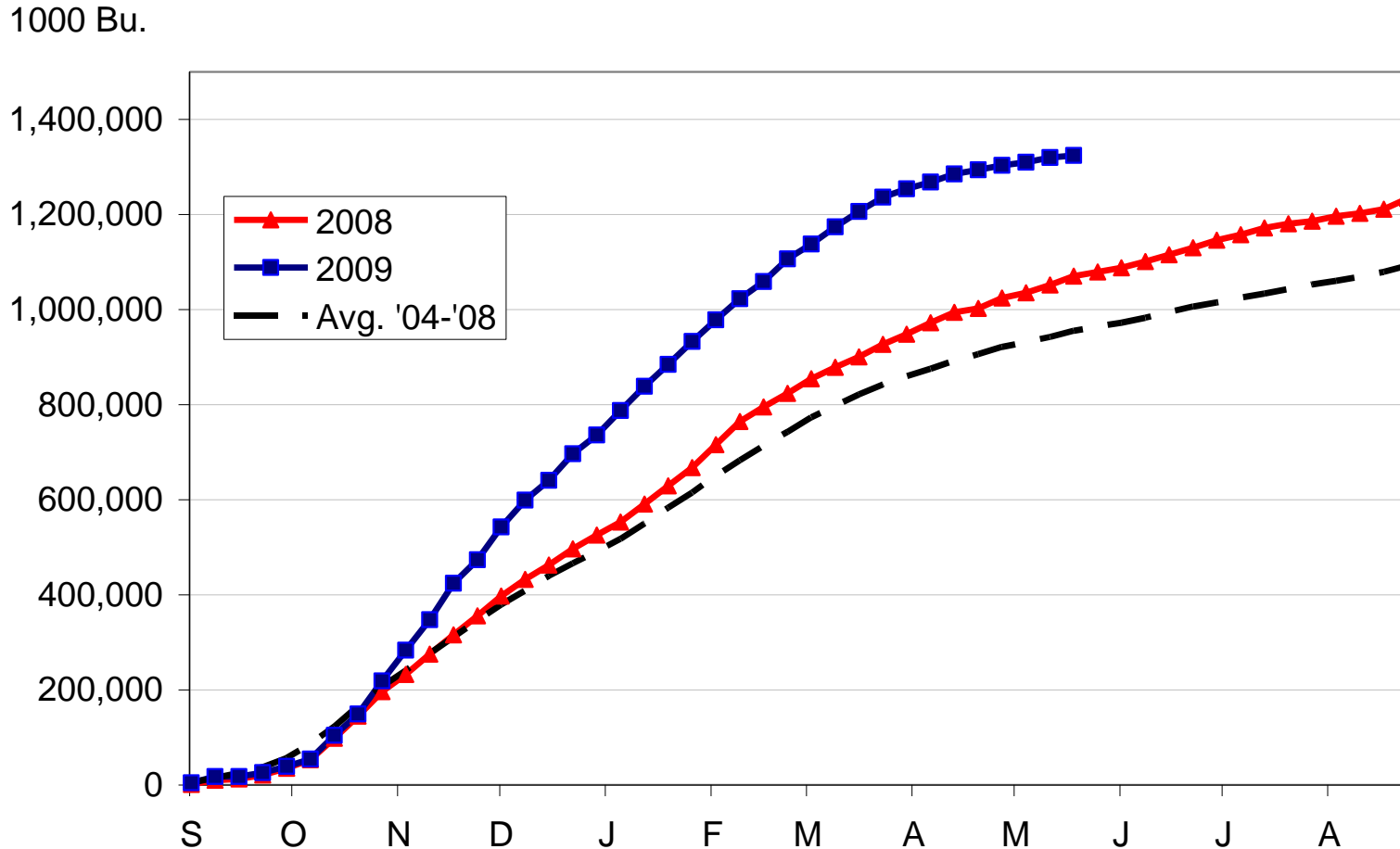
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Bean exports have been robust!!

... Could leave supplies tight in July-Aug

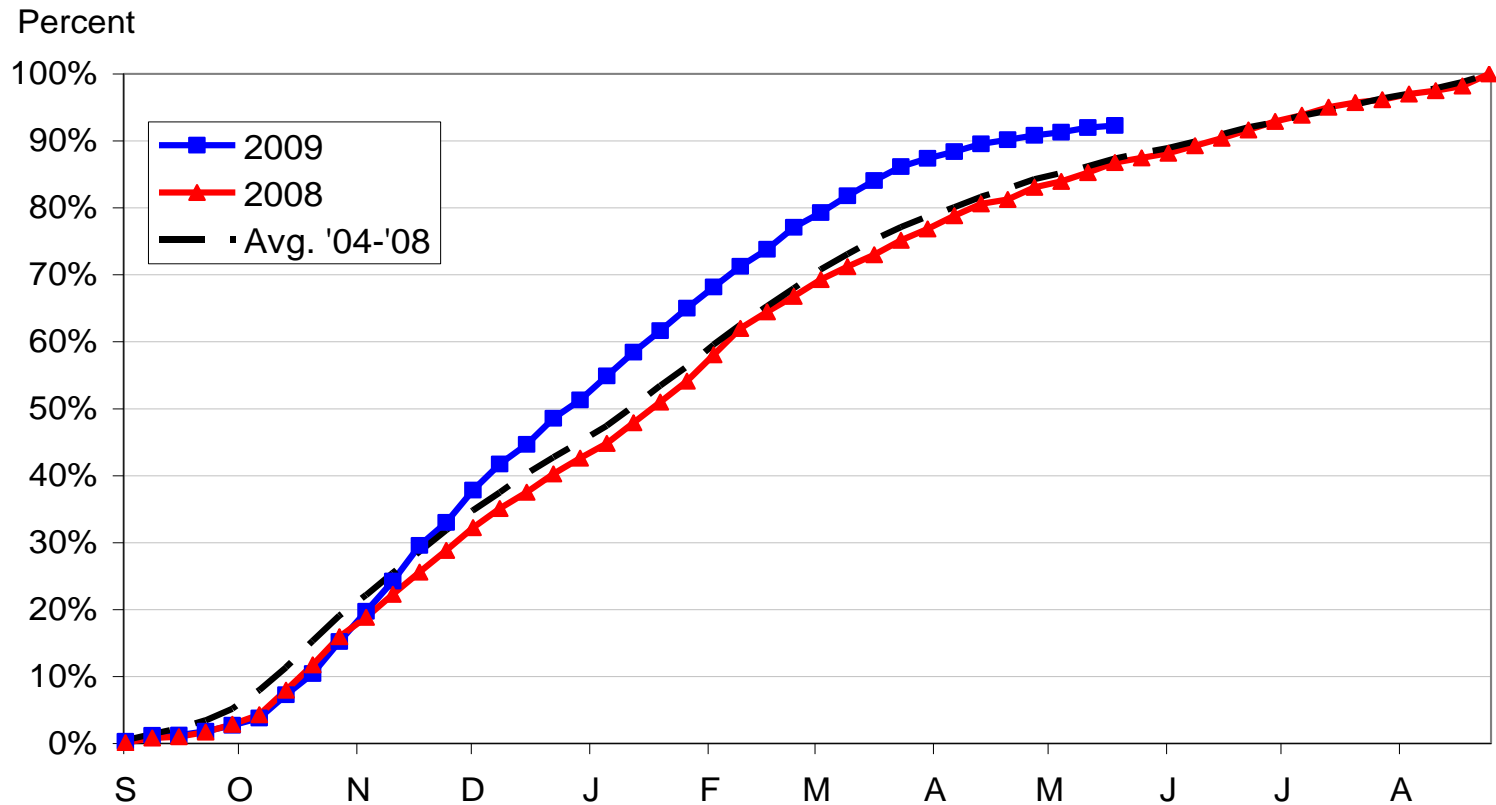
U.S. SOYBEAN EXPORTS



Pace relative to annual is slower ...

... will they exceed expected 1.435 bil. bu.?

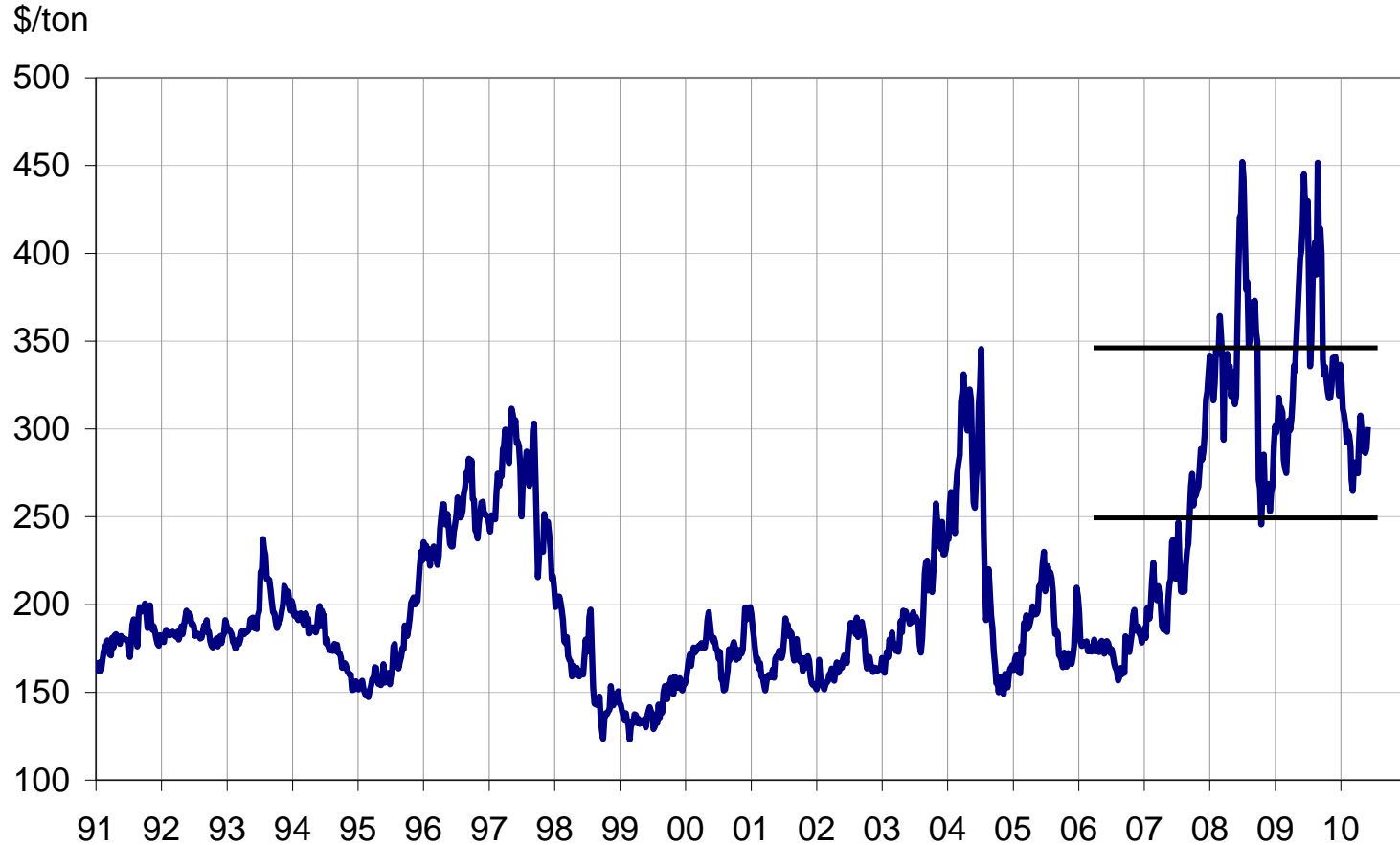
U.S. SOYBEAN EXPORTS, PCT. OF ANNUAL



Remember where cash SBM went ...

... The past two summers on tight supplies

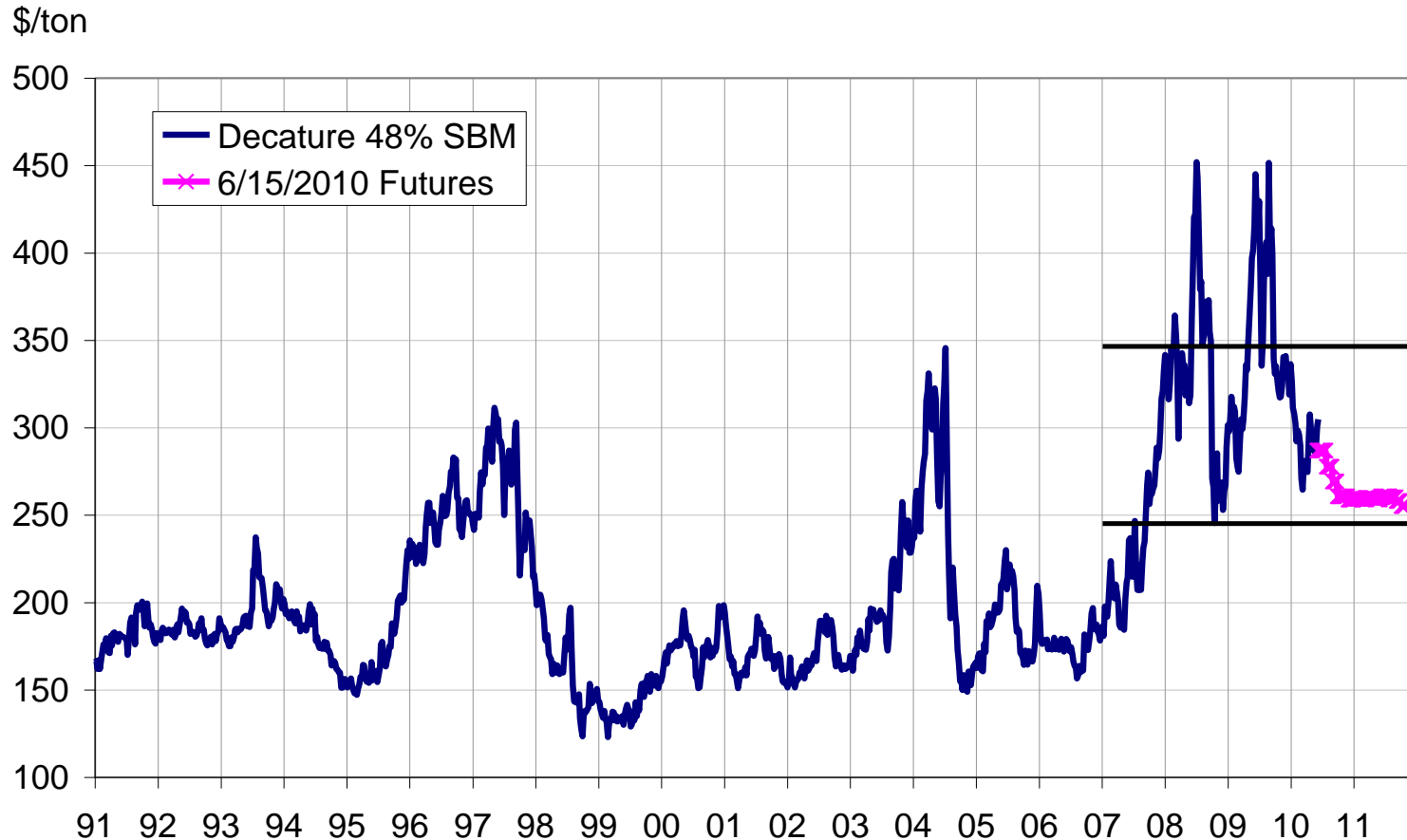
CASH SBM PRICE, DECATUR, WEEKLY



2011 futures are at the BOTTOM ...

... of the apparent "new normal" range

CASH SBM PRICE, DECATUR, WEEKLY



Factors to consider

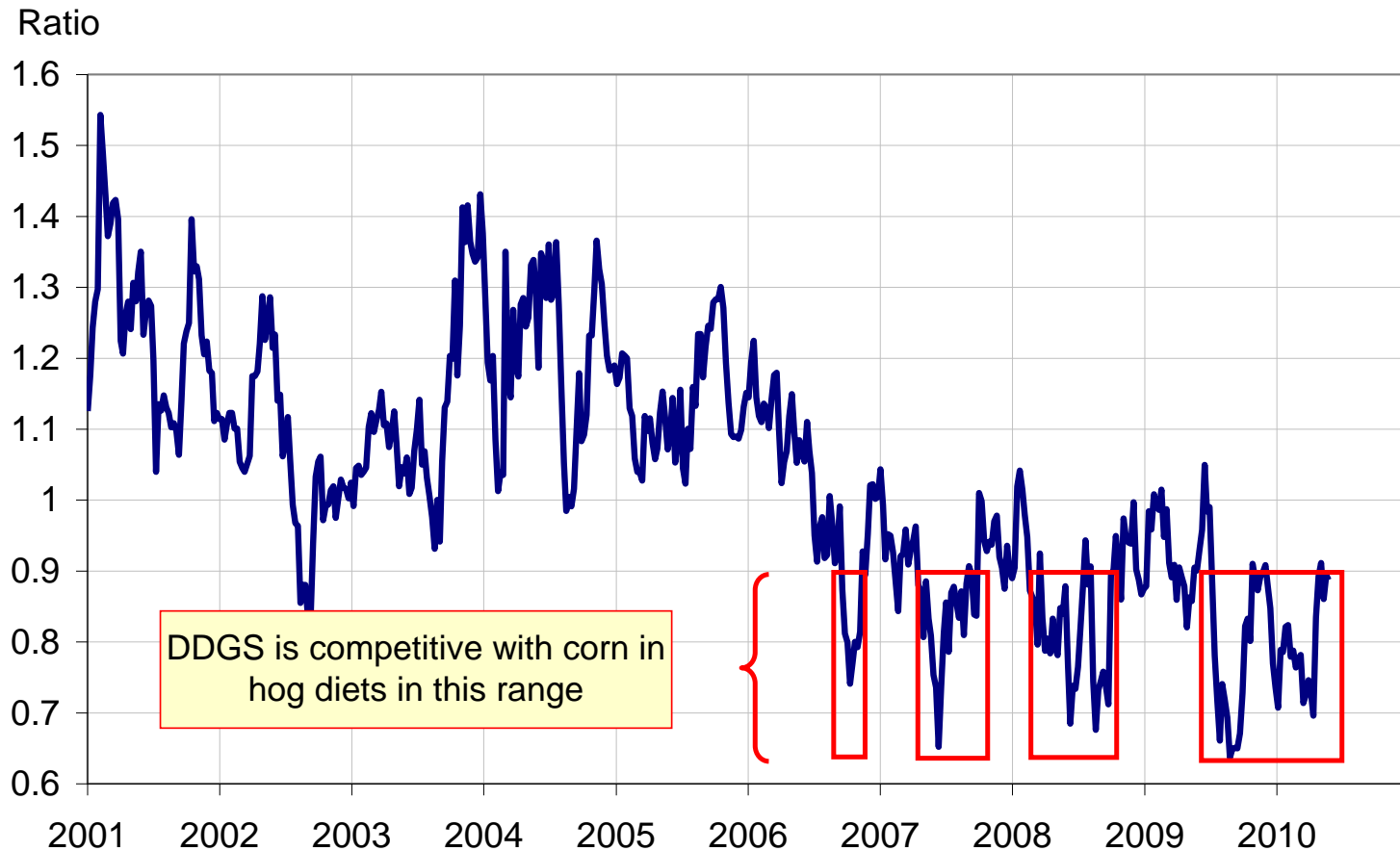
- As is the case for corn, good weather could push prices lower in late summer
- So could a slowdown in the torrid export pace
- 2011 prices: Will Brazil and Argentina raise another bumper crop?
- How wrong can you be with SBM hedged at \$250 or maybe even \$230?



A word about DDGS prices ...

... Larger supplies = Pricing "into" hog diets

DDGS \$ PER LB / CORN \$ PER LB



PORK AND HOG OUTLOOK

Summary

- Hog supplies have been CLOSE to levels expected from March H&P
- Prices have exceeded levels a) expected and b) consistent with supply changes and stable farm-level demand
- Conflicting signals:
 - Near-record cutout values and hog prices
STRONG packer margins
 - “Okay” exports – at least through March
 - But SOFT consumer-level demand



Summary (continued)

- Feed cost outlook is positive for profits – depending on weather
- Few signs of expansion yet
 - Sow slaughter is low but not exceptionally so as a percent of the BH
 - Gilt slaughter frequently above 49.5%
- But – anecdotal expansion evidence
 - Some repops in the works
 - 473k sows cut since Dec '07 – Estimate that 1/4th could be repopped – 2% growth

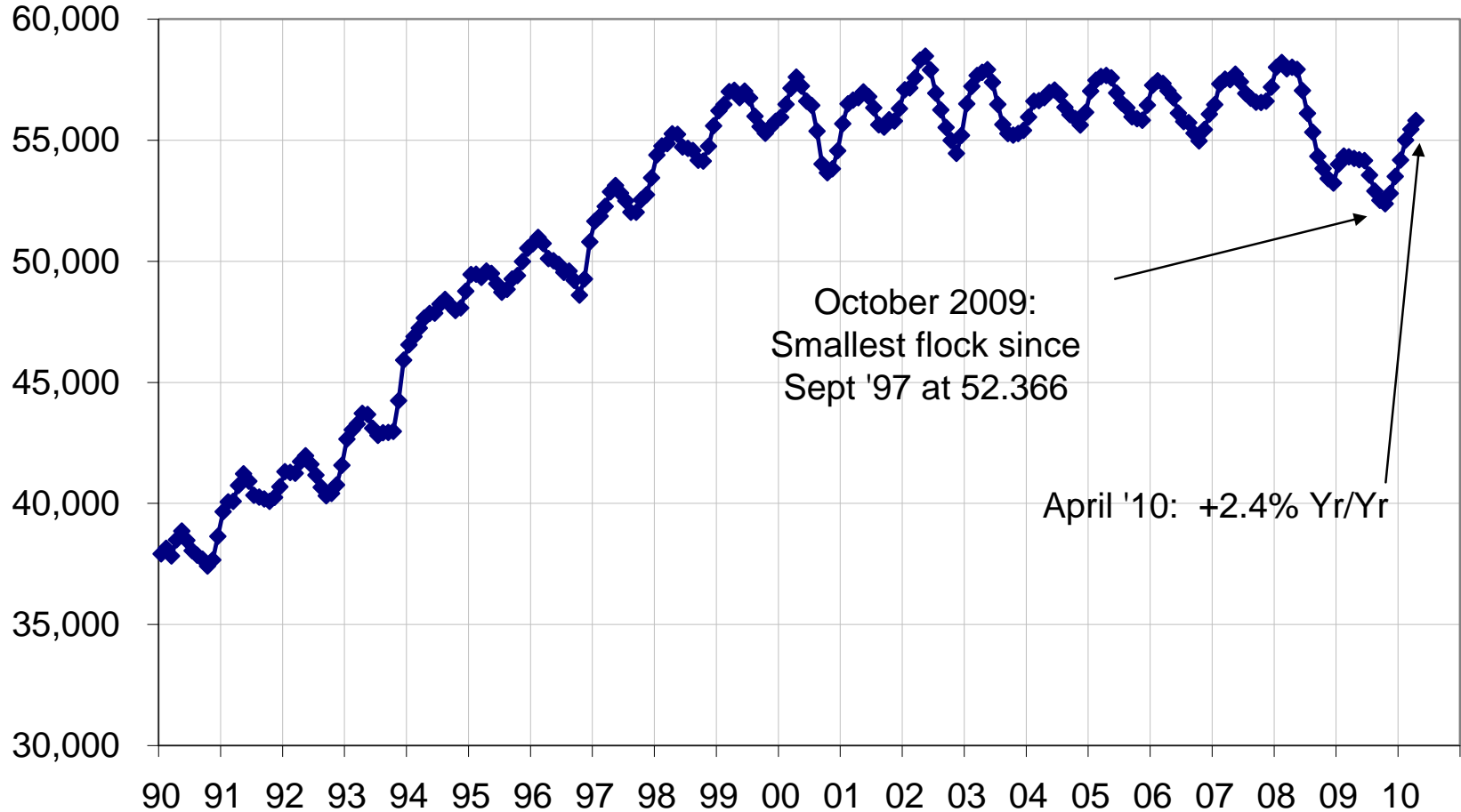


COMPETITORS

Chicken production capacity is growing ...

BROILER HATCHERY FLOCK

Thousand Hens



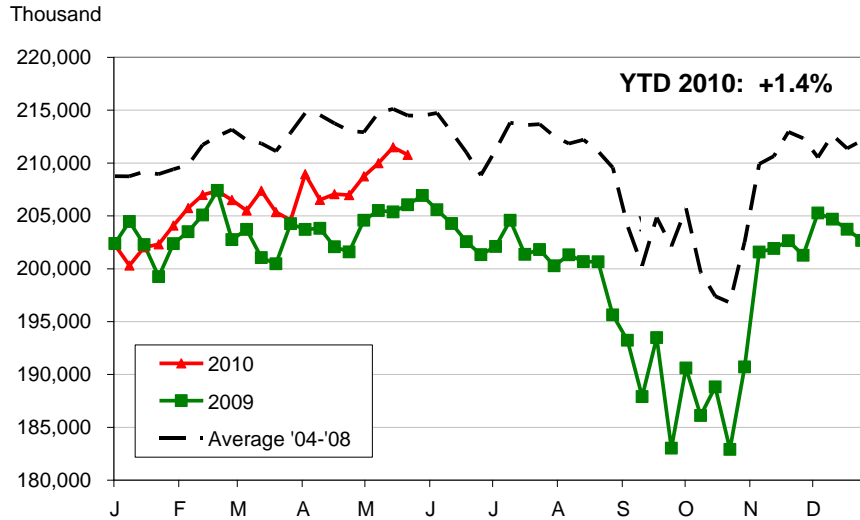
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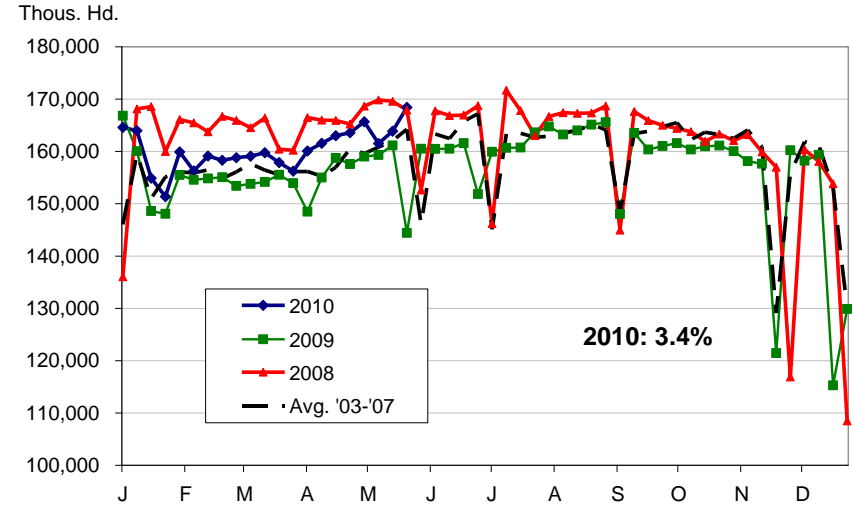


Current output measures are positive ...

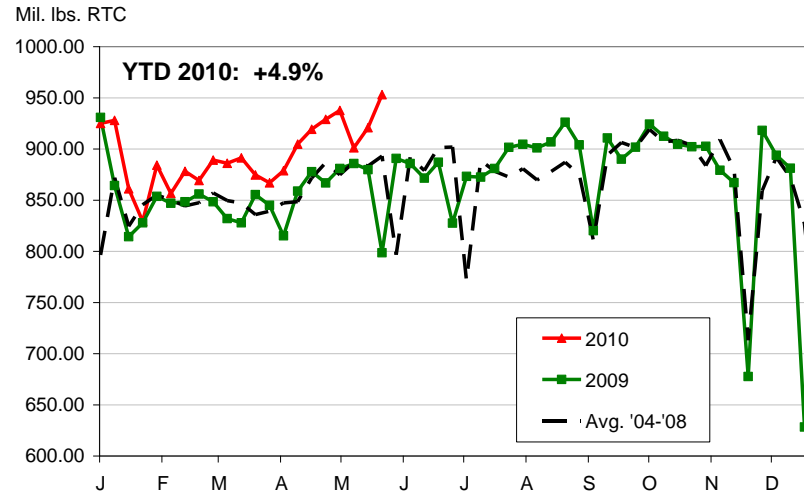
WEEKLY BROILER EGG SETS



U.S. FI BROILER SLAUGHTER, WEEKLY



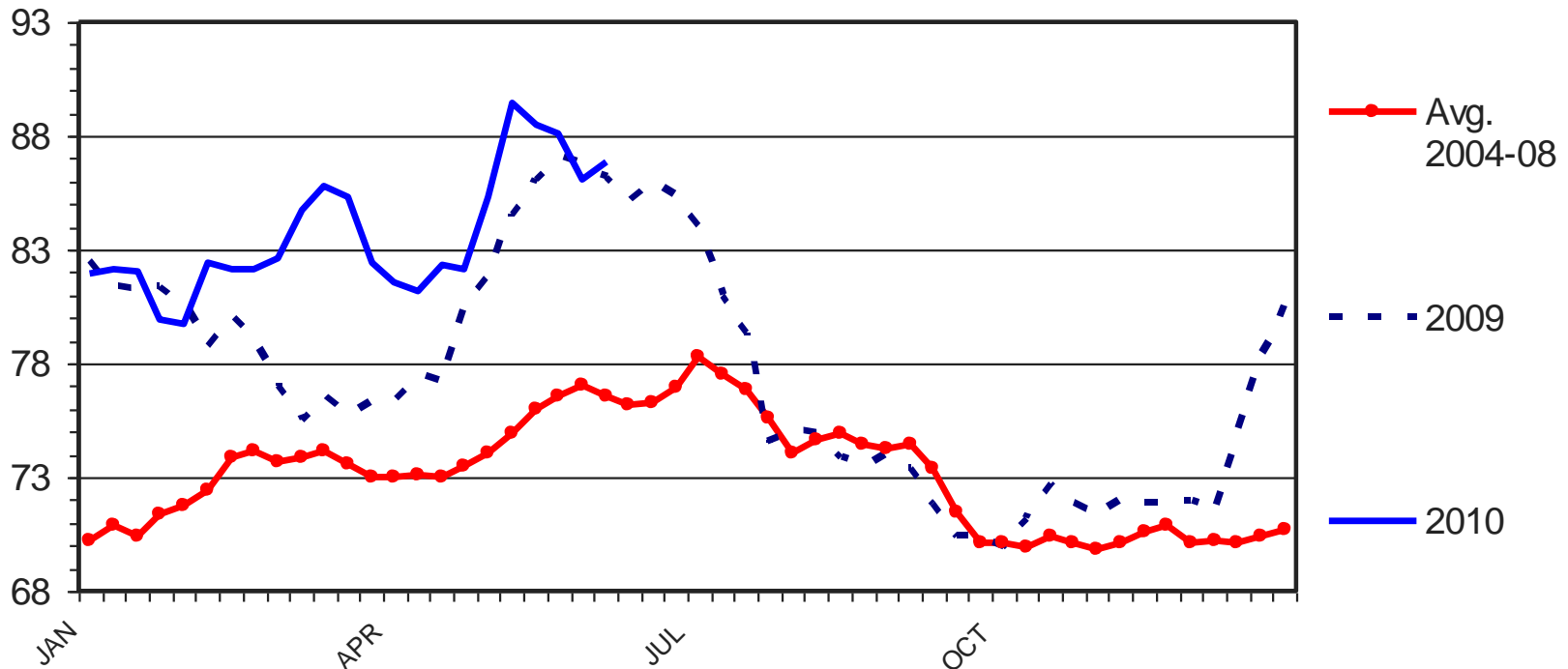
FI BROILER PRODUCTION, WEEKLY



But chicken prices are near-record high

BROILER PRICES 12-City Composite, Weekly

Cents Per Pound



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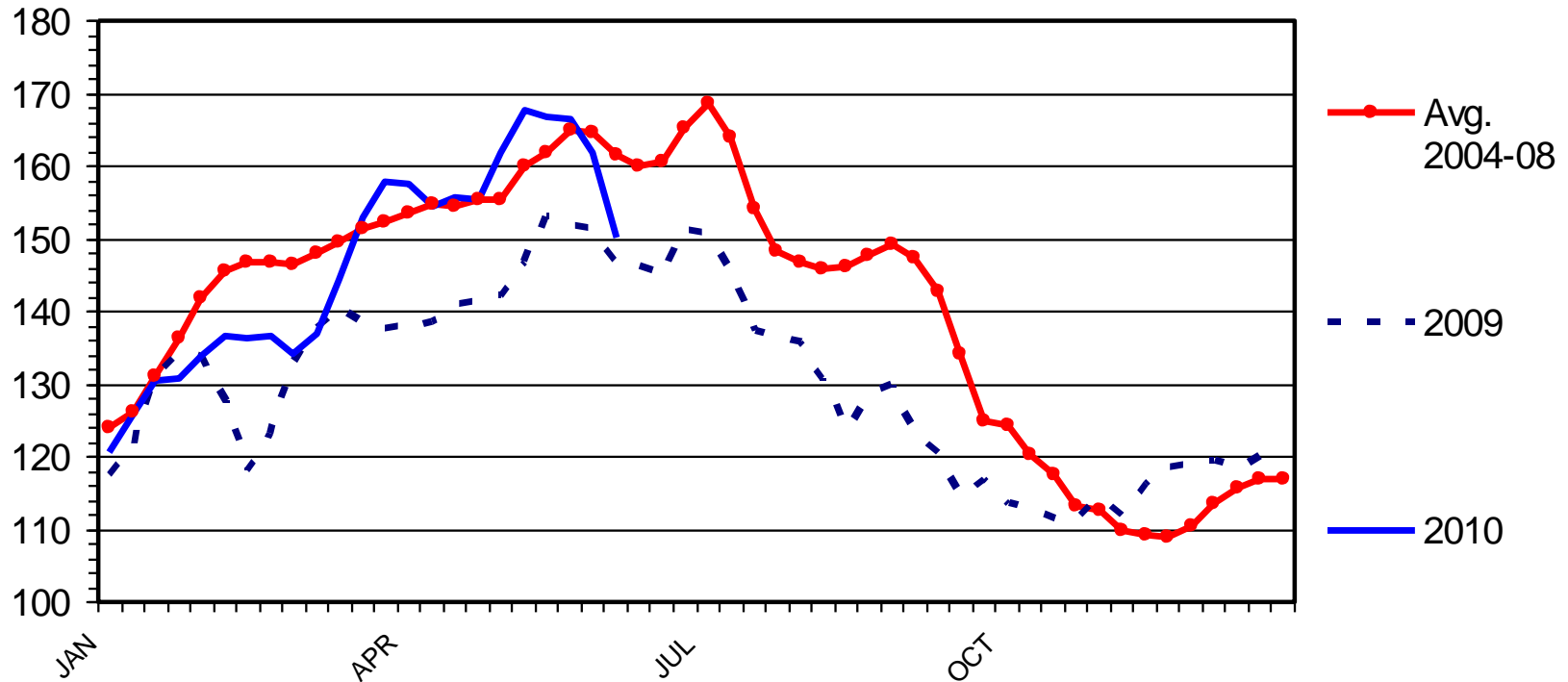
Driven by a resurgence in breast prices ...

... At least until last week!

WHOLESALE CHICKEN BREAST PRICES

Skinless/Boneless, Northeast, Truckload, Weekly

Cents Per Pound



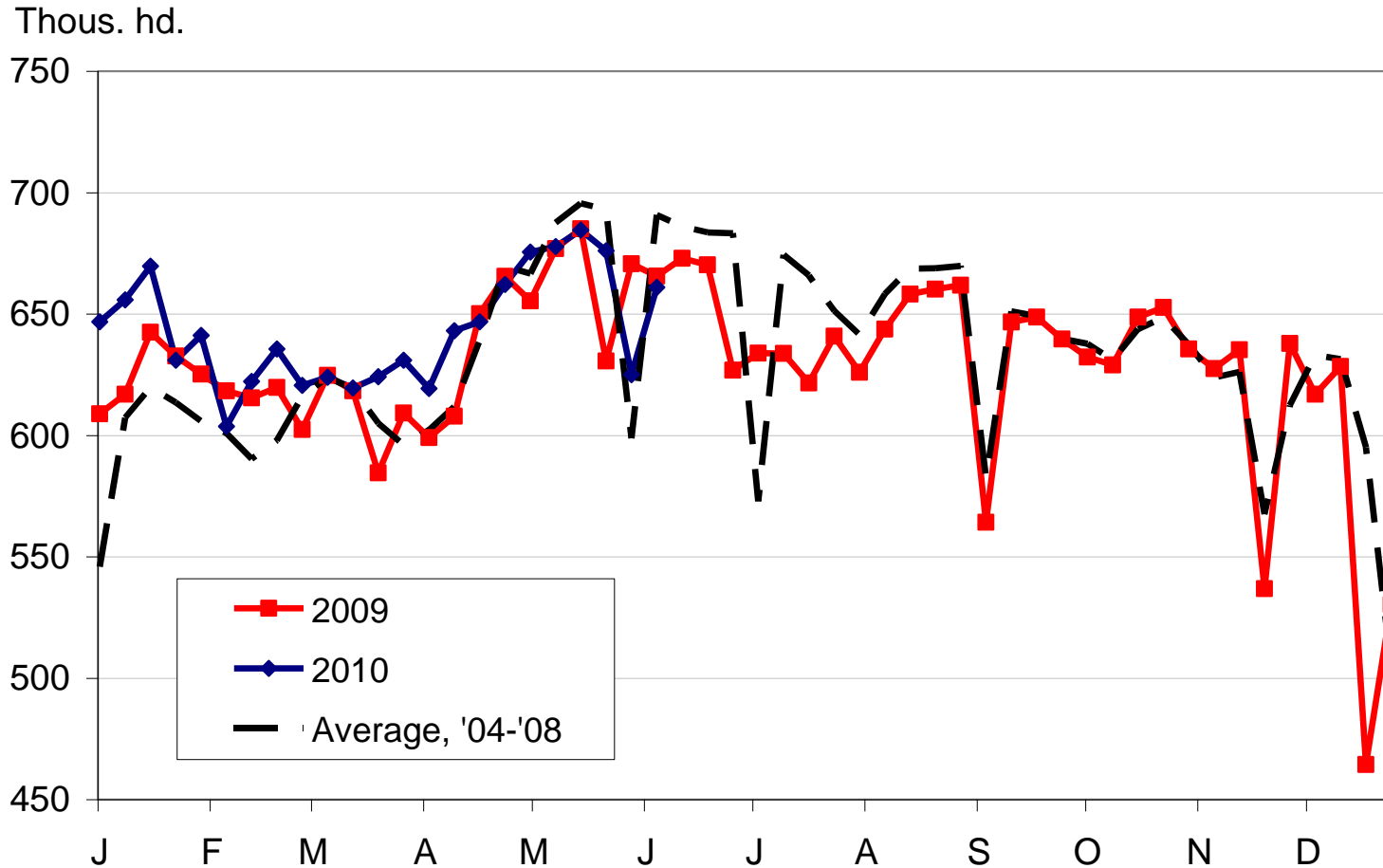
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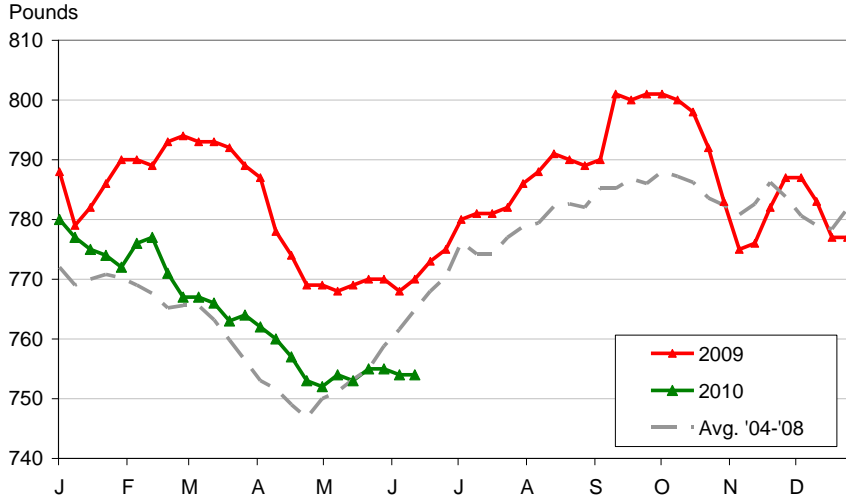
Cattle slaughter: Closer and closer to '09

U.S. FI CATTLE SLAUGHTER, WEEKLY

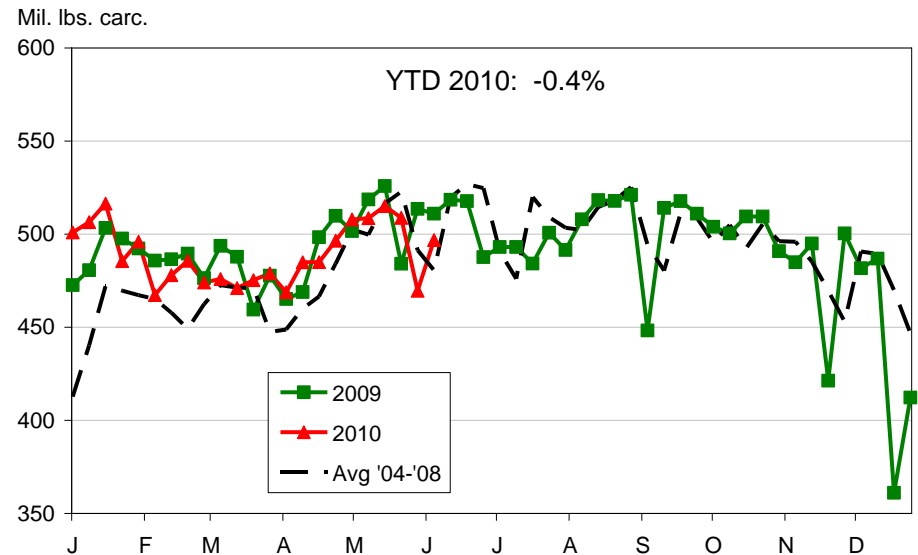


Sharply lower weights have limited output

FI CATTLE CARCASS WEIGHTS



FI BEEF PRODUCTION, WEEKLY

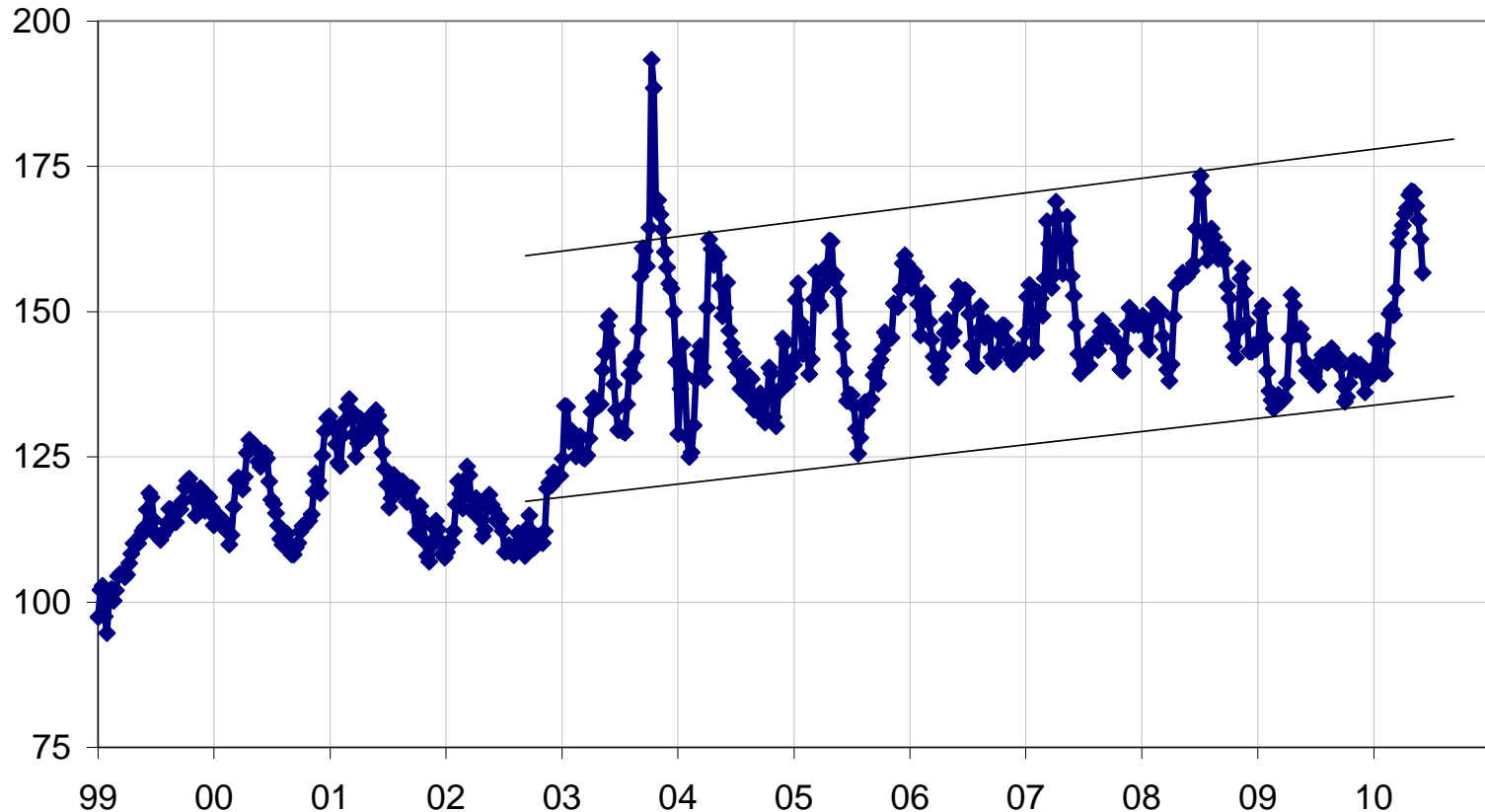


Cutout has been near record-high ...

... But has peaked for the year

600-900# CHOICE BEEF CUTOUT VALUE

\$/cwt carcass



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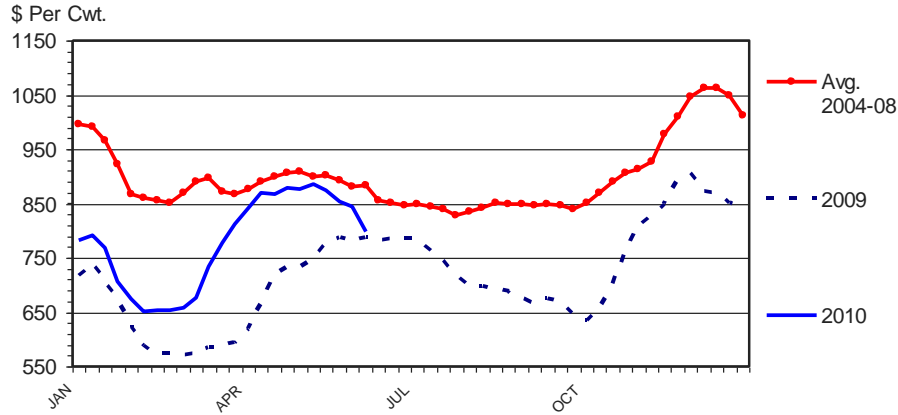
From information, knowledge



Beef F/S cuts have fallen, too

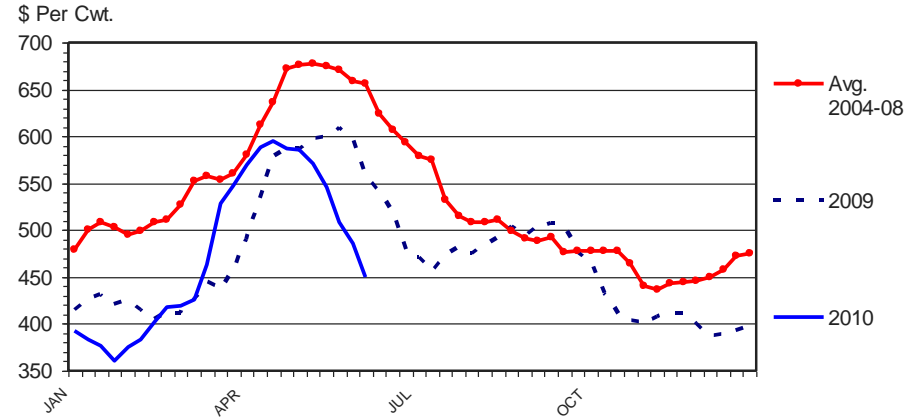
WHOLESALE BEEF FULL TENDER PRICES

Musl-On, 5 Pounds and Up, Weekly



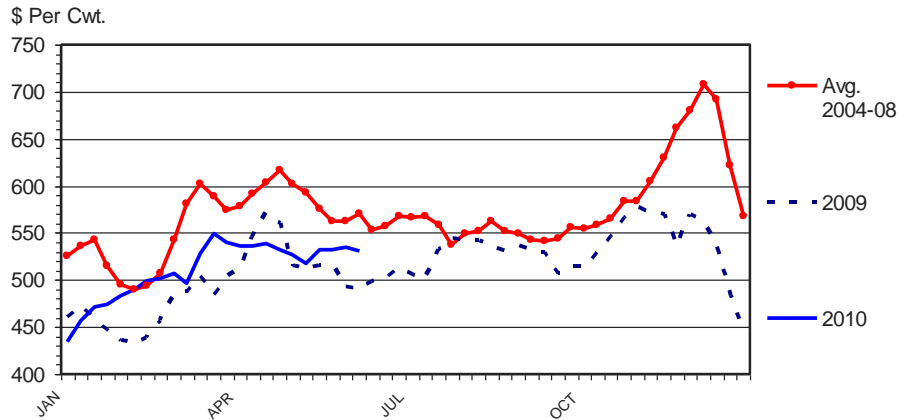
WHOLESALE BEEF LOIN STRIP PRICES

Boneless 0x1, Weekly



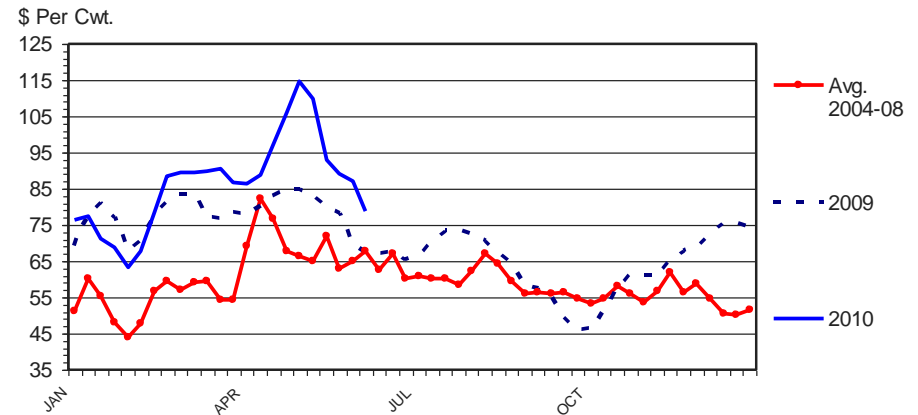
WHOLESALE BEEF RIBEYE PRICES

Boneless, Light, Weekly



WHOLESALE BONELESS BEEF PRICES

Fresh, 50% Lean, Weekly



Impact of competitors

- Positive so far! – chicken and beef prices have been very supportive so far in '10
- Will be less supportive in months to come
 - Beef is in a seasonal price decline but supplies will get tighter, higher fed prices in '11
 - Chicken may be at its peak – expansions by Pilgrim, Sanderson, others in '11 and '12
- Trade developments will help chicken – nothing has moved to Russia yet

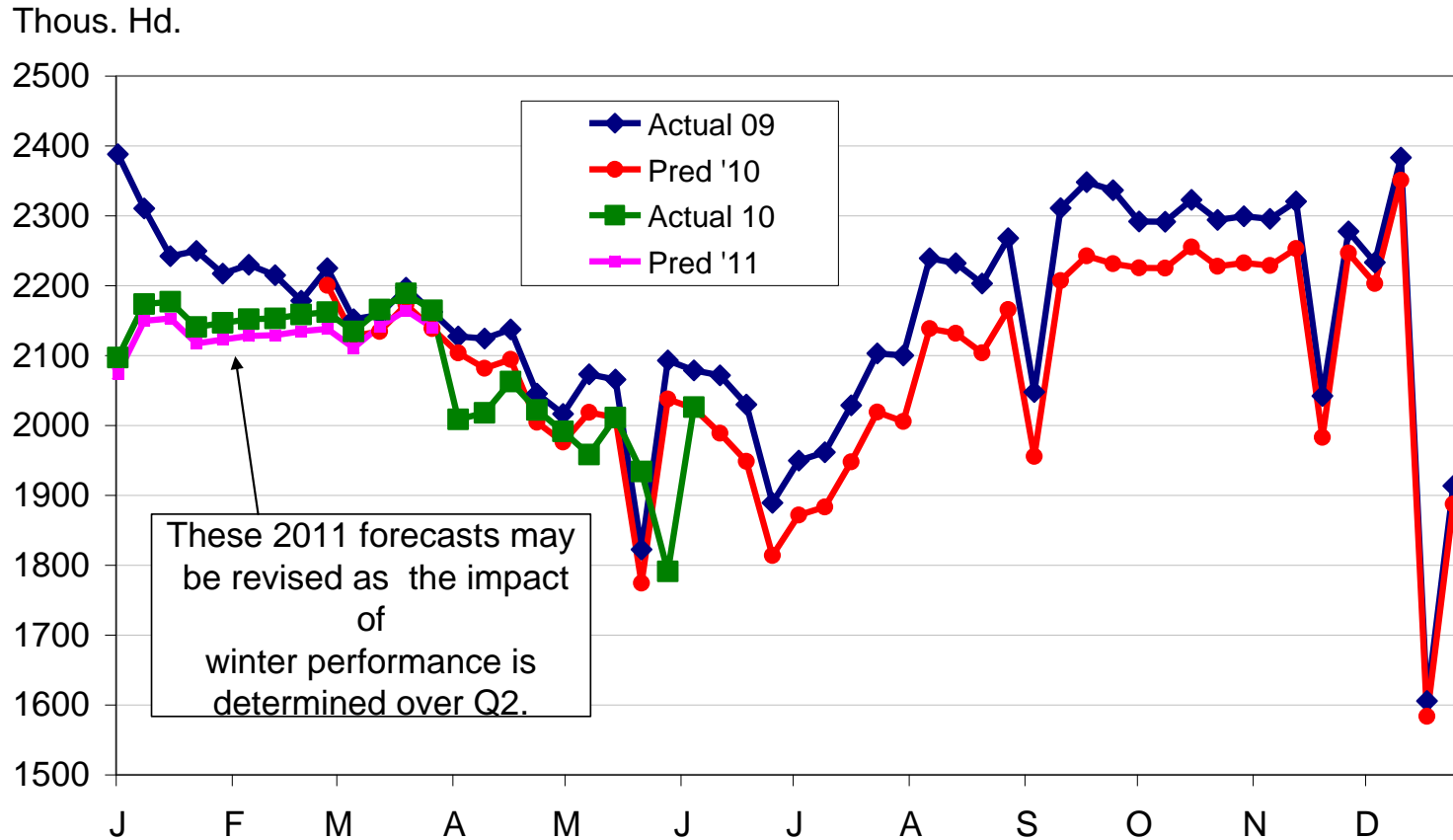


Actual slghtr has been -1% from March H&P

.. and -2.7% from '09 -- -4.5% yr/yr coming

FI HOG SLAUGHTER, WEEKLY

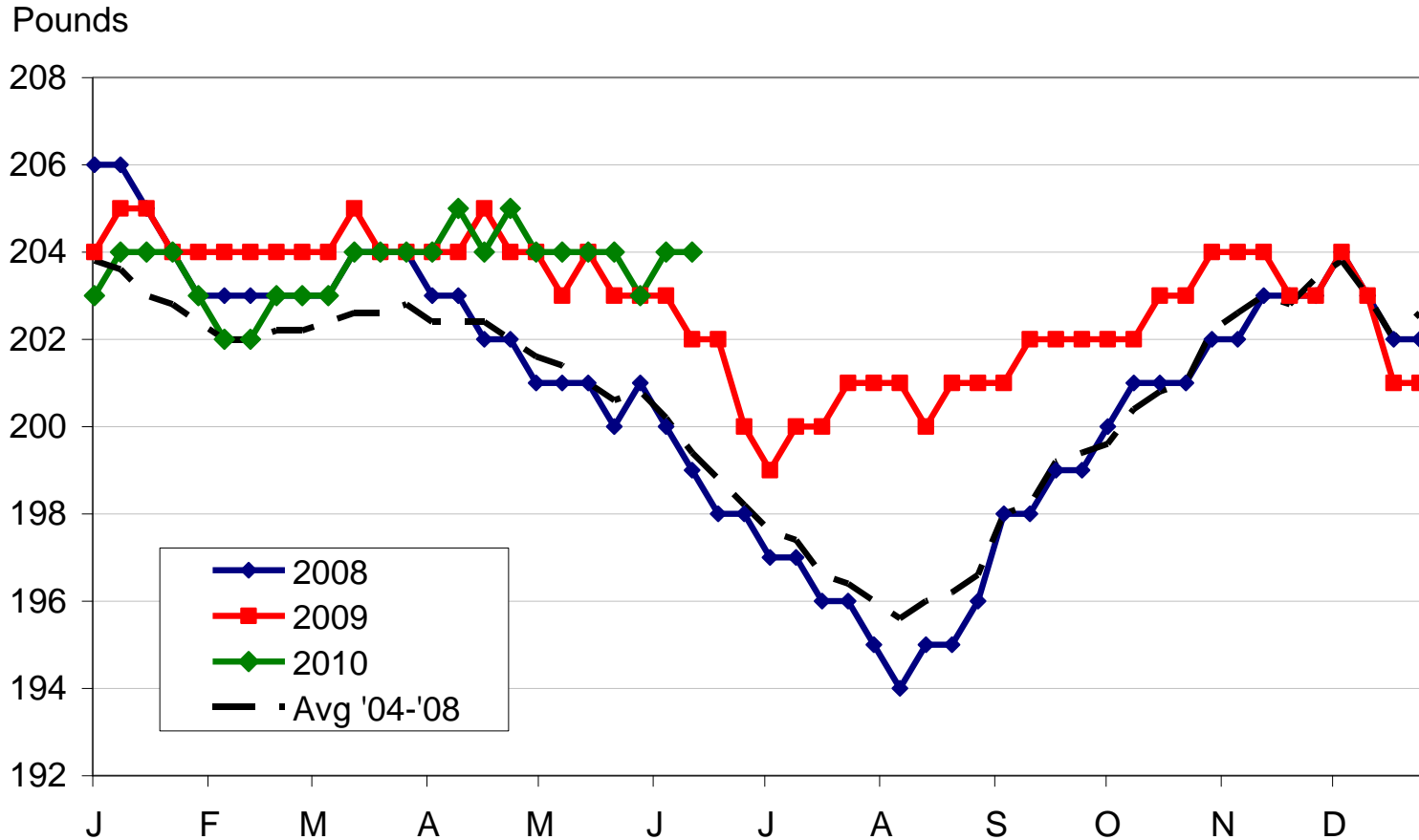
Based on USDA Hogs & Pigs Report, March '10



Weights: YTD equal to 2009, +1# recently ...

... larger hogs = more profit, slack space

FI CARCASS WEIGHTS, HOGS

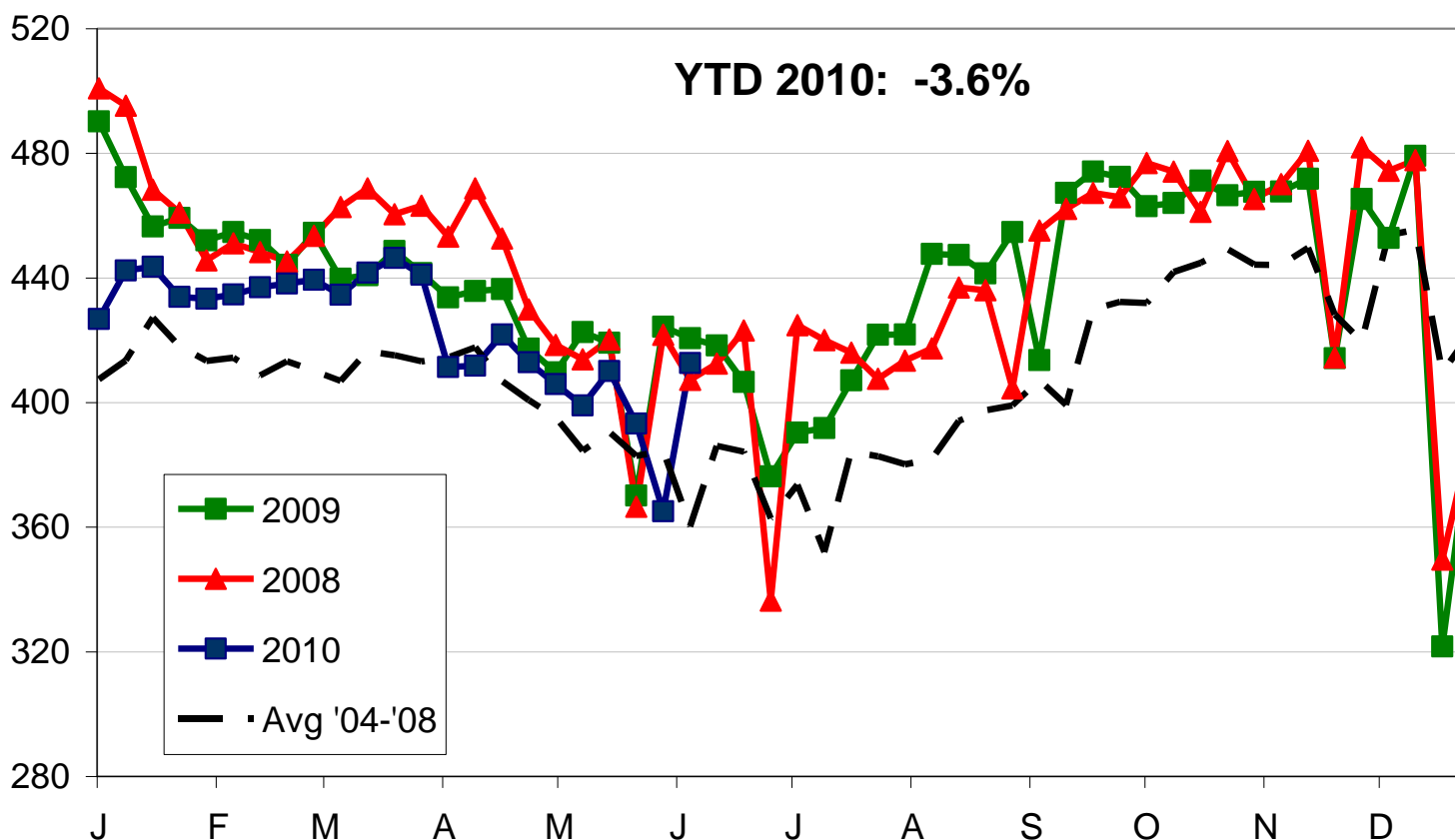


YTD output is still -3.6% from last year ...

... Says prices should be +8 to 12%

FI PORK PRODUCTION, WEEKLY

Mil. lbs. carc.



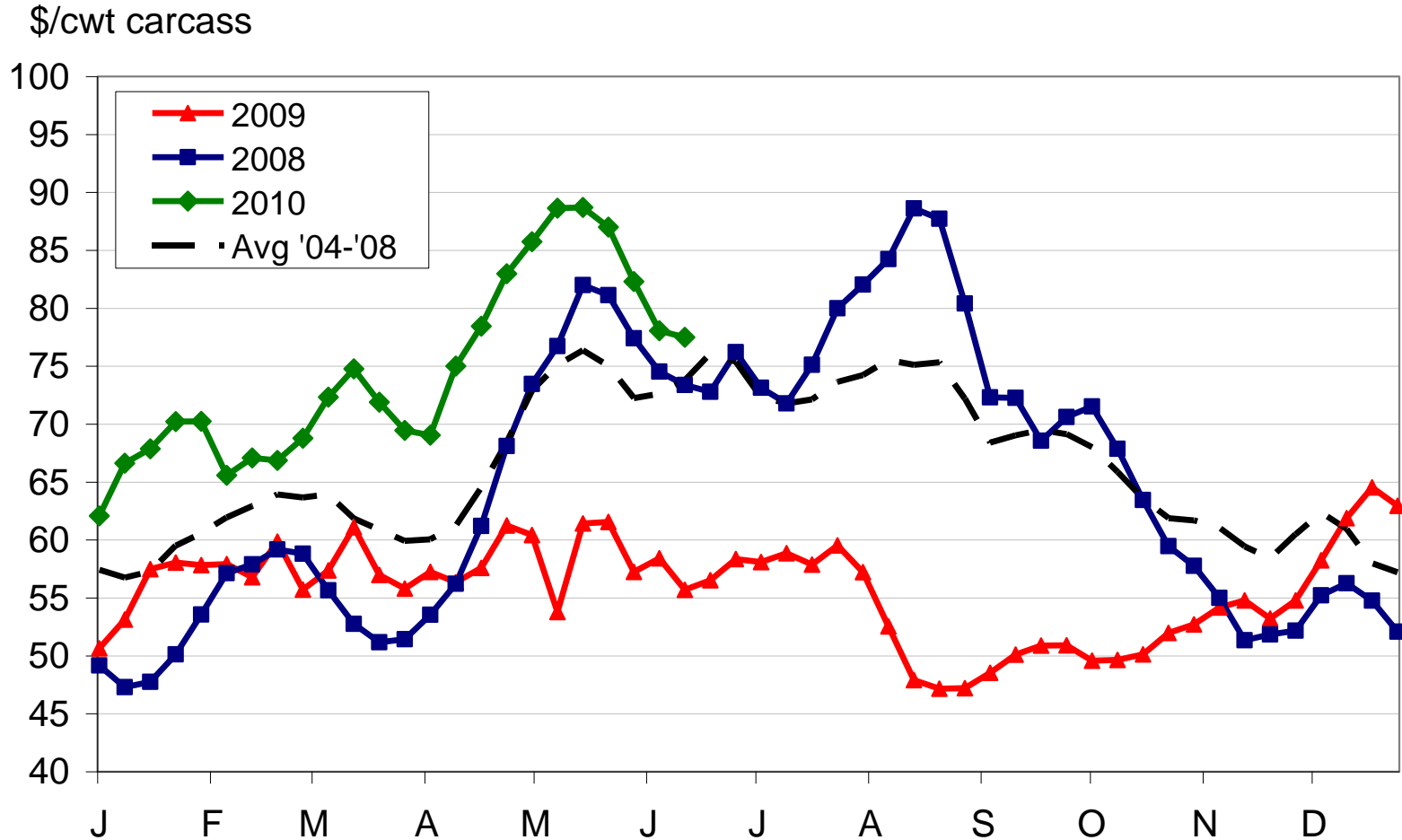
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Record-high hog prices -- +30% from '09

U.S. NEG'D NET PRICE, WTD. AVERAGE



Why the discrepancy in prices?

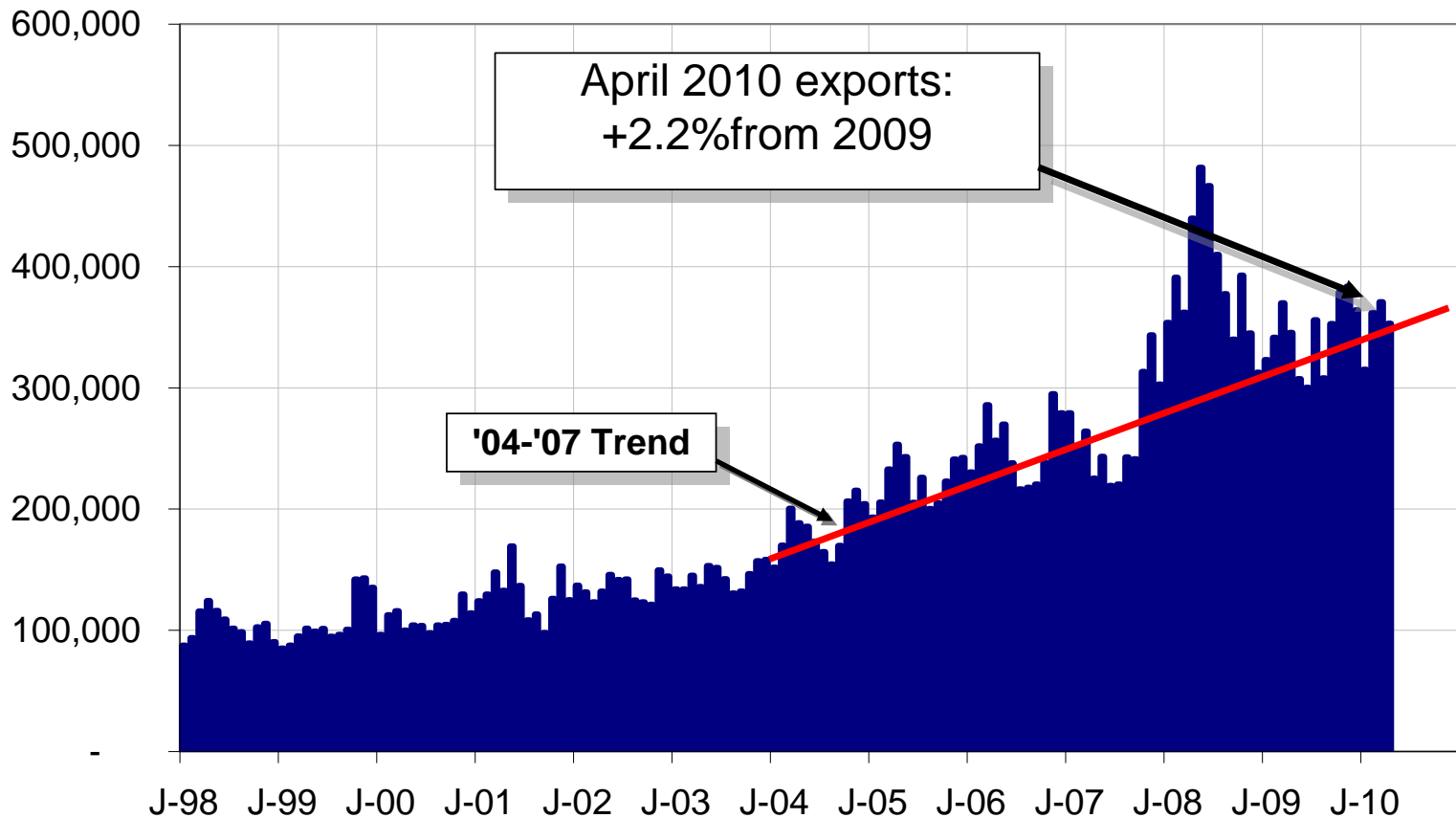
- '09 prices were artificially depressed
 - H1N1 aftermath
 - High weights driven by unusual weather
 - An “unrepresentative base” from which to compute prices
- Positive impact of other species
 - Using a price flexibility considers only own-quantity impacts
 - Cross-price elasticities are smaller but not zero!



Exports +2.2% in April, +1.5% YTD ...

MONTHLY U.S. PORK EXPORTS

Thous. lbs. carc.



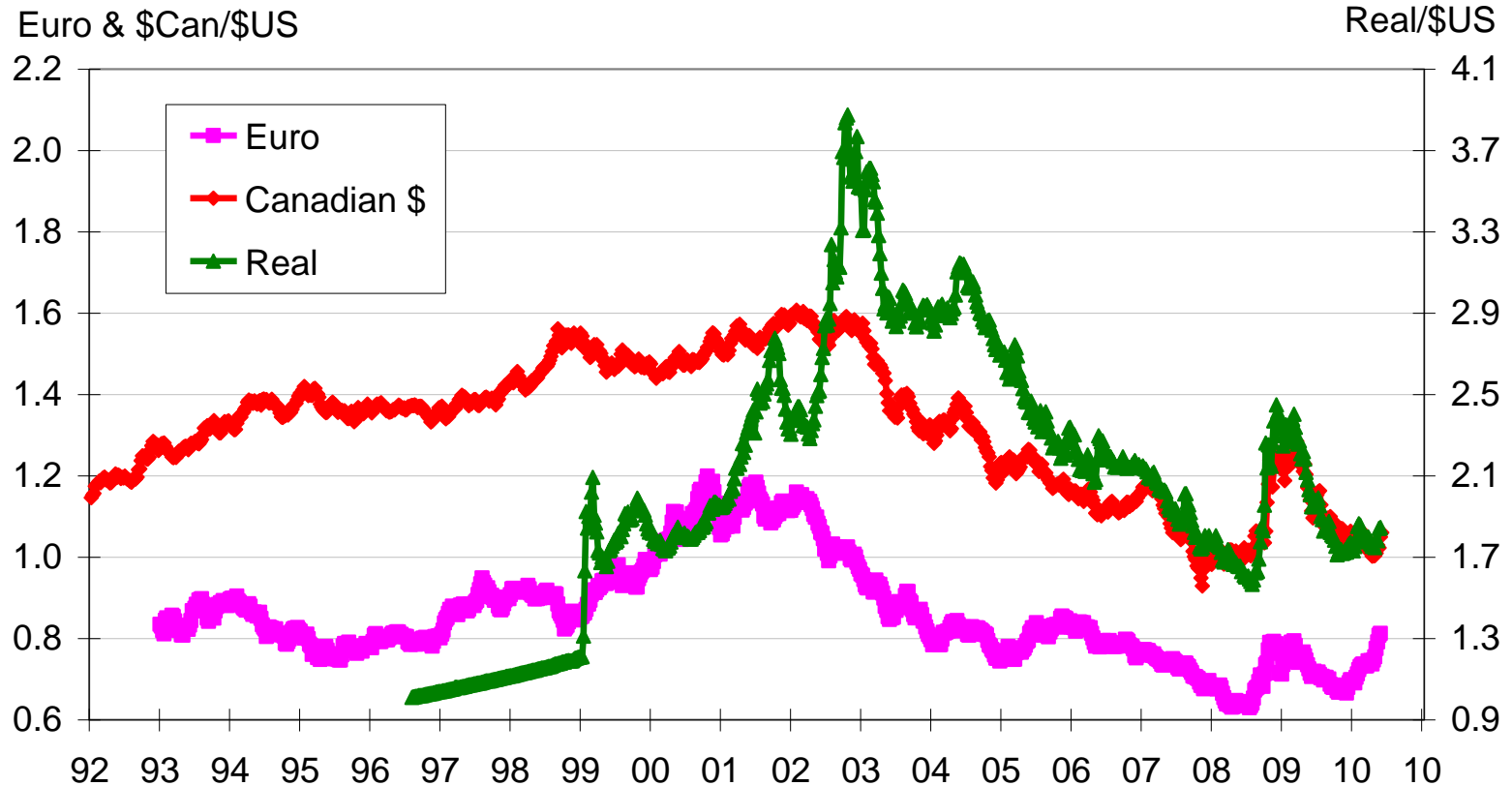
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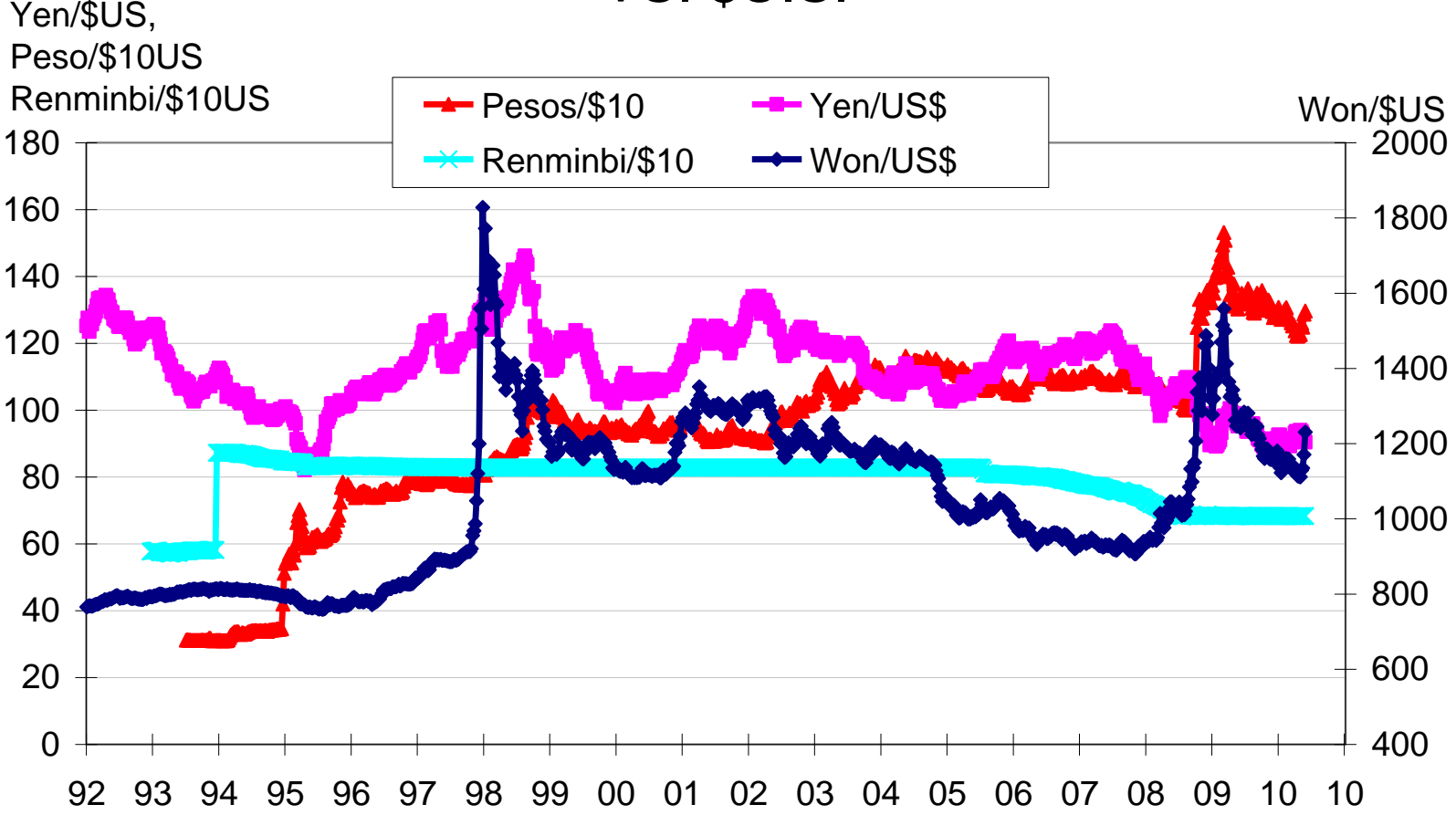
Competitors: EU has gained an advantage

U.S. EXPORT COMPETITORS' CURRENCIES VS. \$U.S.



Customers: Recent changes, Japan & Mexico

U.S. EXPORT CUSTOMERS' CURRENCIES VS. \$U.S.

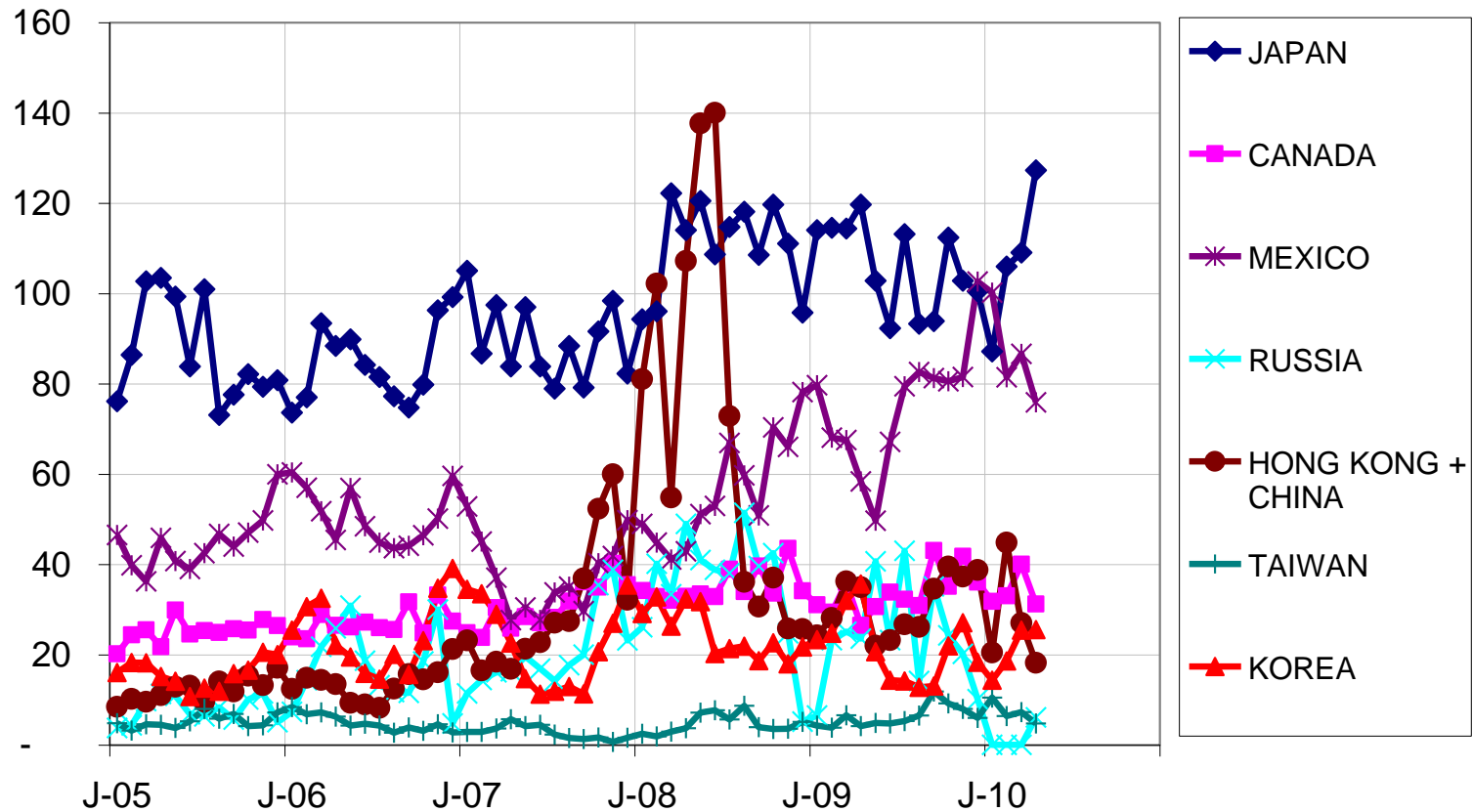


Big recovery for Japan in April ...

...Mexico is still strong, Russia's the problem

U.S. PORK EXPORTS BY DESTINATION

Million lbs. carc.



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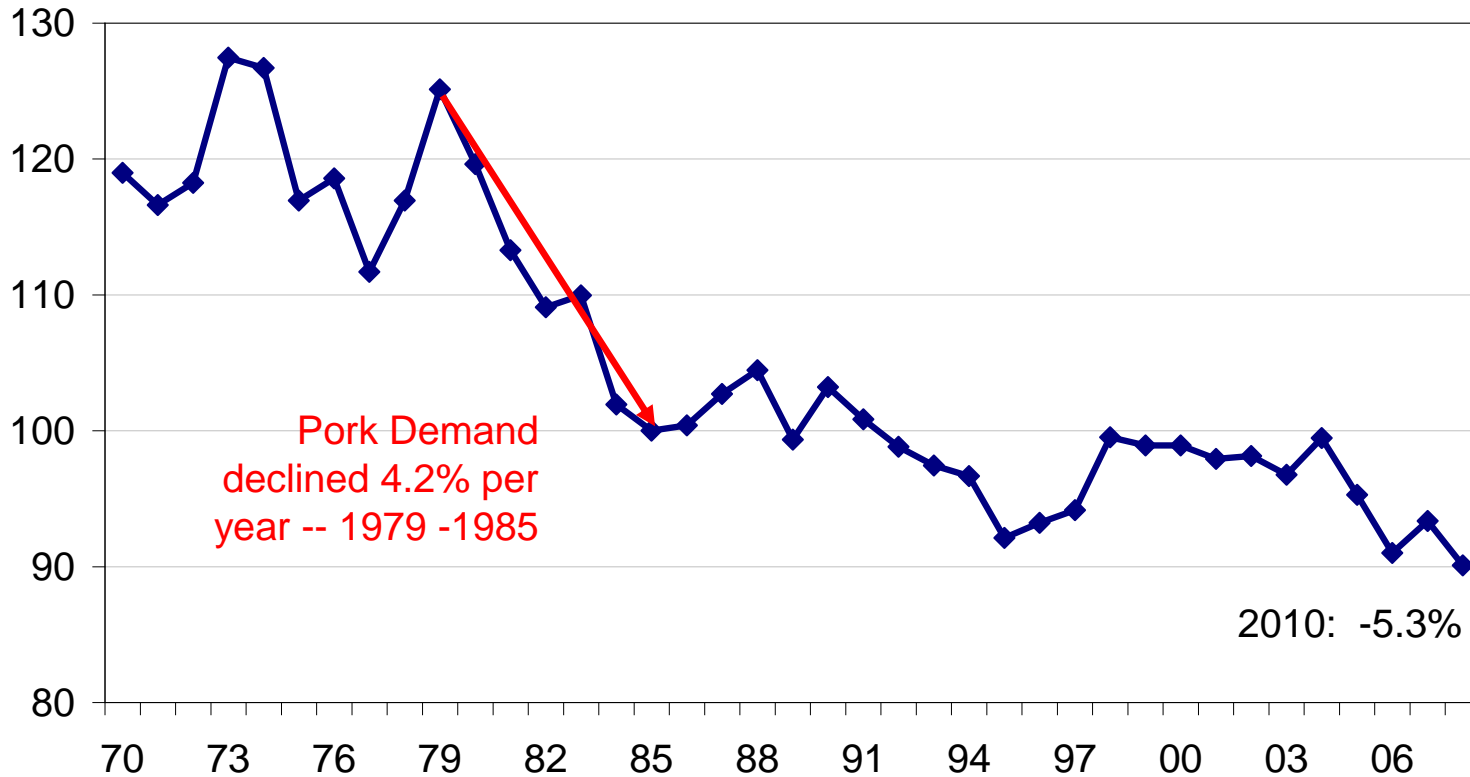


Pork demand: conflict with hogs & whisle ..

... I suspect the retail price data!

PORK DEMAND INDEX

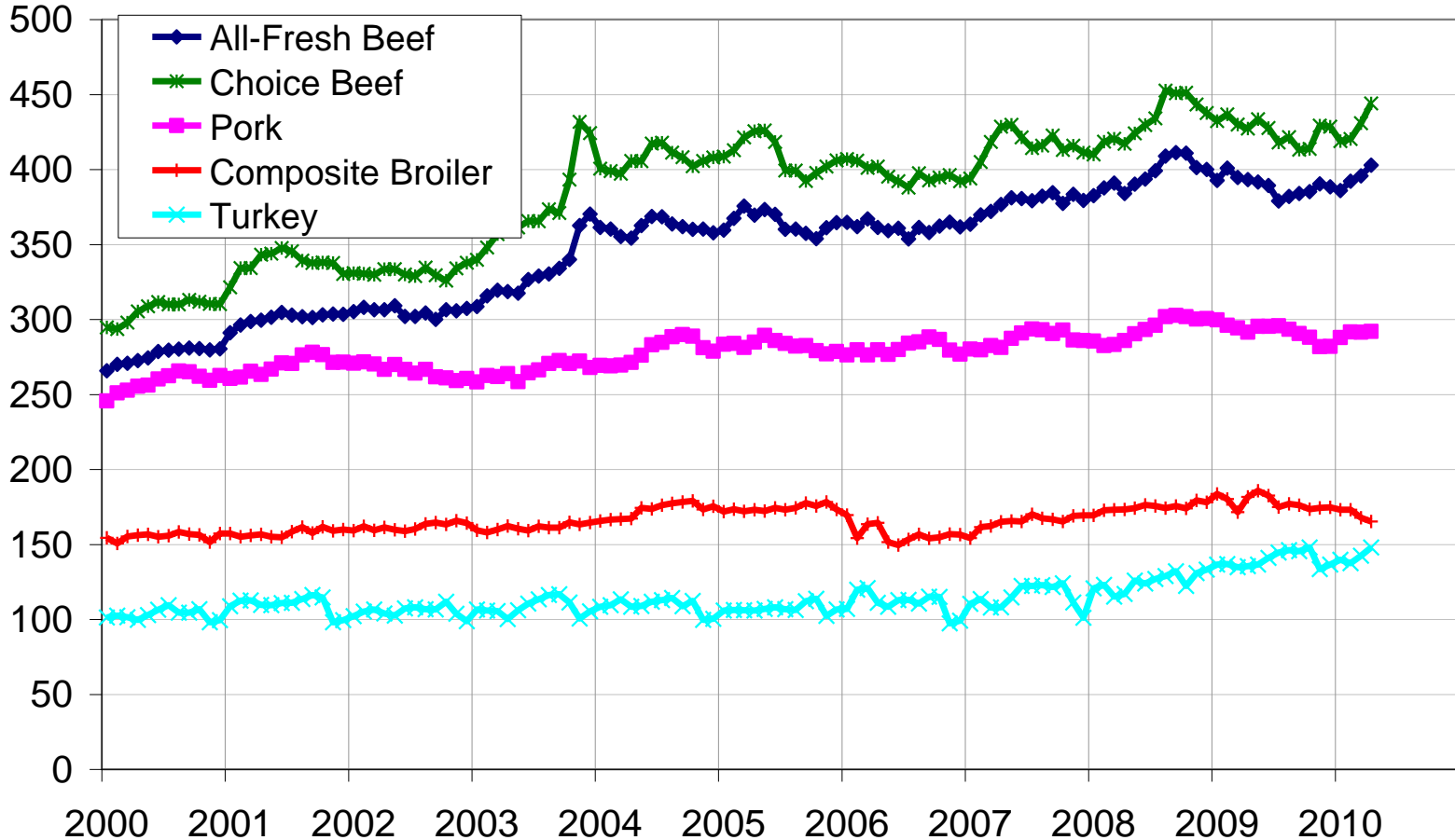
Index, '85=100



Pork and chicken prices don't make sense!

RETAIL MEAT PRICES, USDA

Cents/lb.



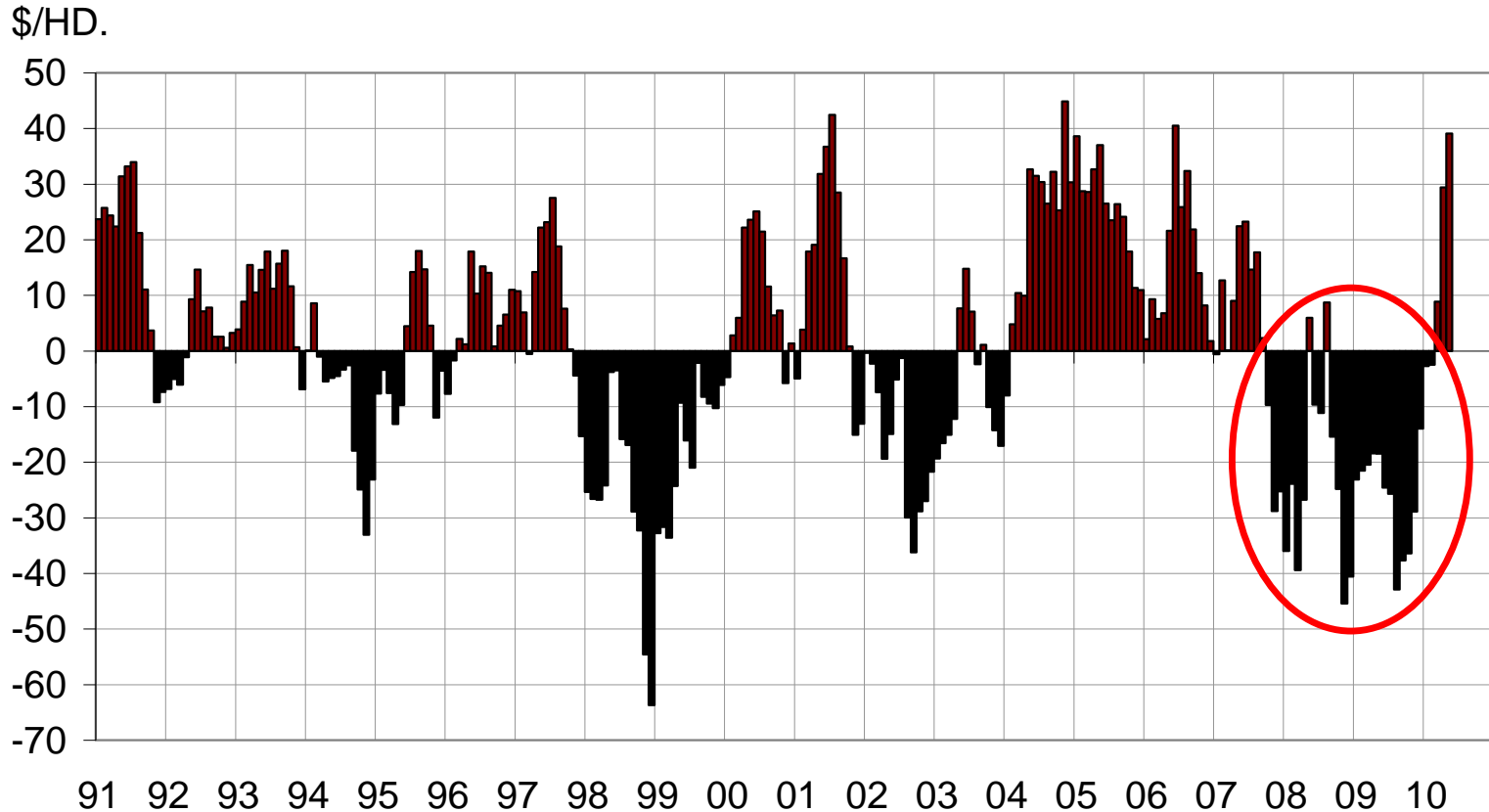
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Profits are back – in a BIG way!!!

PROFIT PER HEAD IOWA FARROW-TO-FINISH OPERATIONS



Source: Estimated Costs and Returns, Dr. John Lawrence, Department of Economics, Iowa State University

Paragon Economics, Inc.

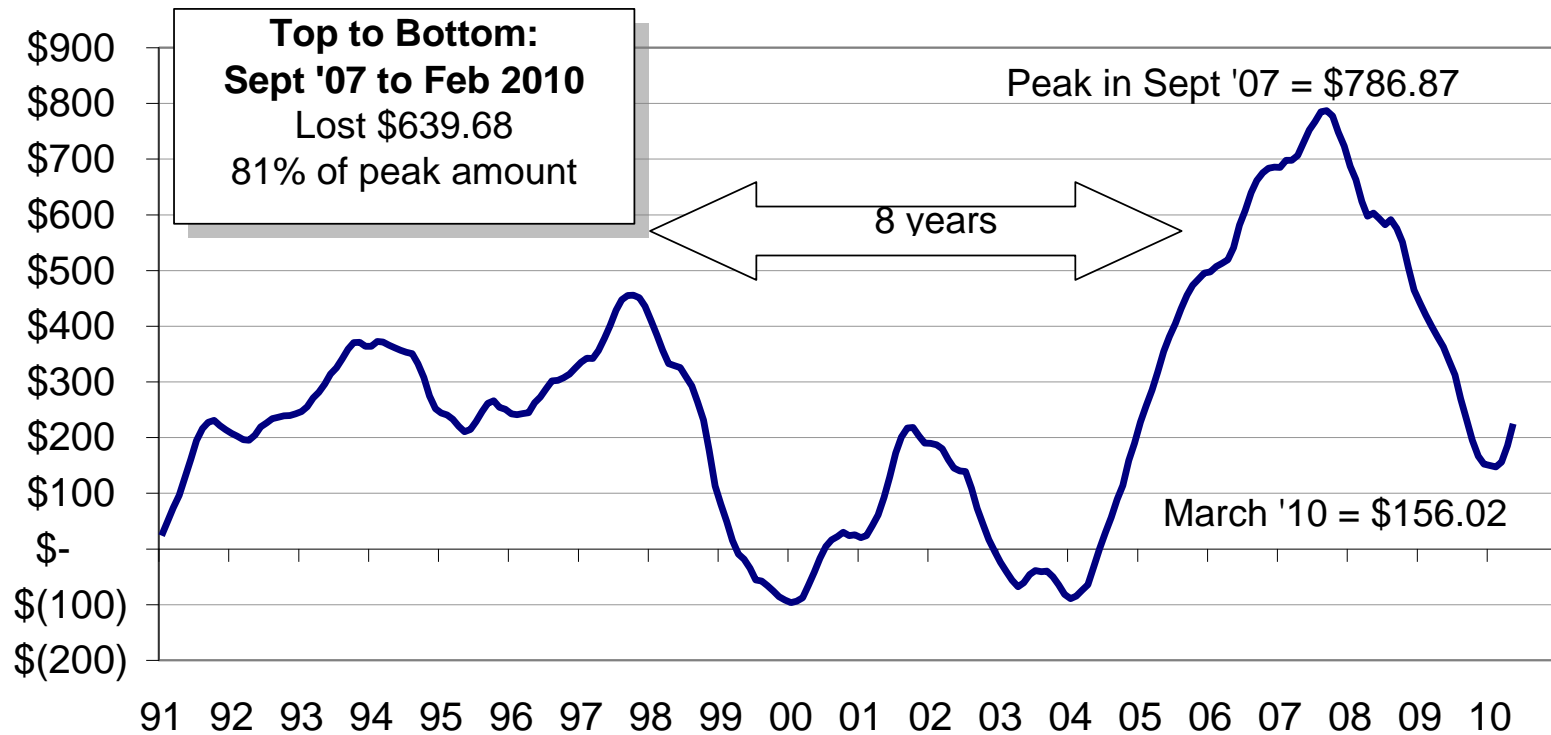
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But financial positions are generally weak

ACCUMULATED PROFITS IOWA FARROW-TO-FINISH OPERATIONS

(Sum of the profits from selling one pig per month since January 1991)



Source: Paragon Economics, Inc. using data from Estimated Costs and Returns, Dr. John Lawrence, Department of Economics, Iowa State University

Paragon Economics, Inc.

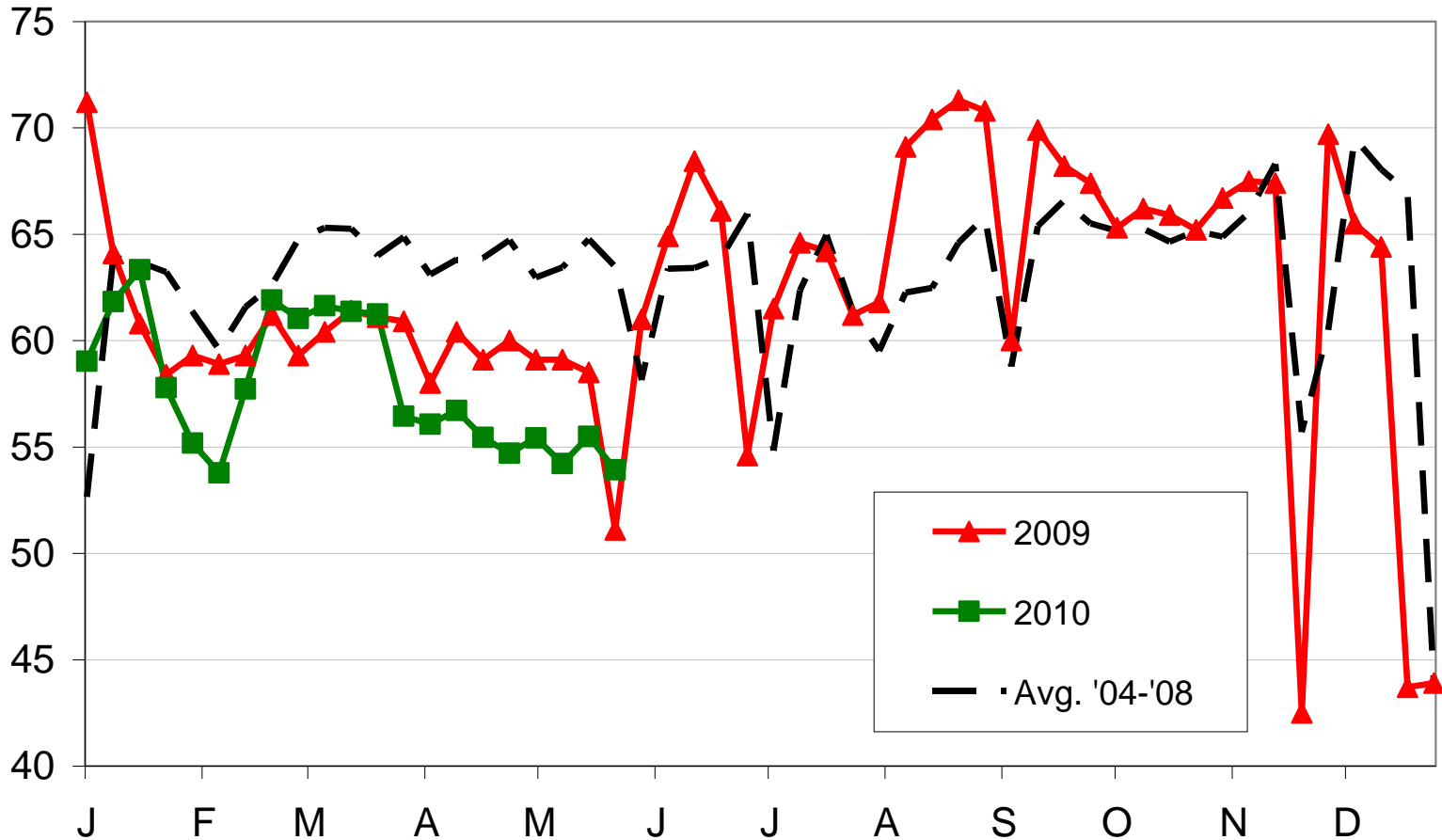
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Sow slaughter is lower – 3 to 4% since April

U.S. SOW SLAUGHTER

Thousand Hd.

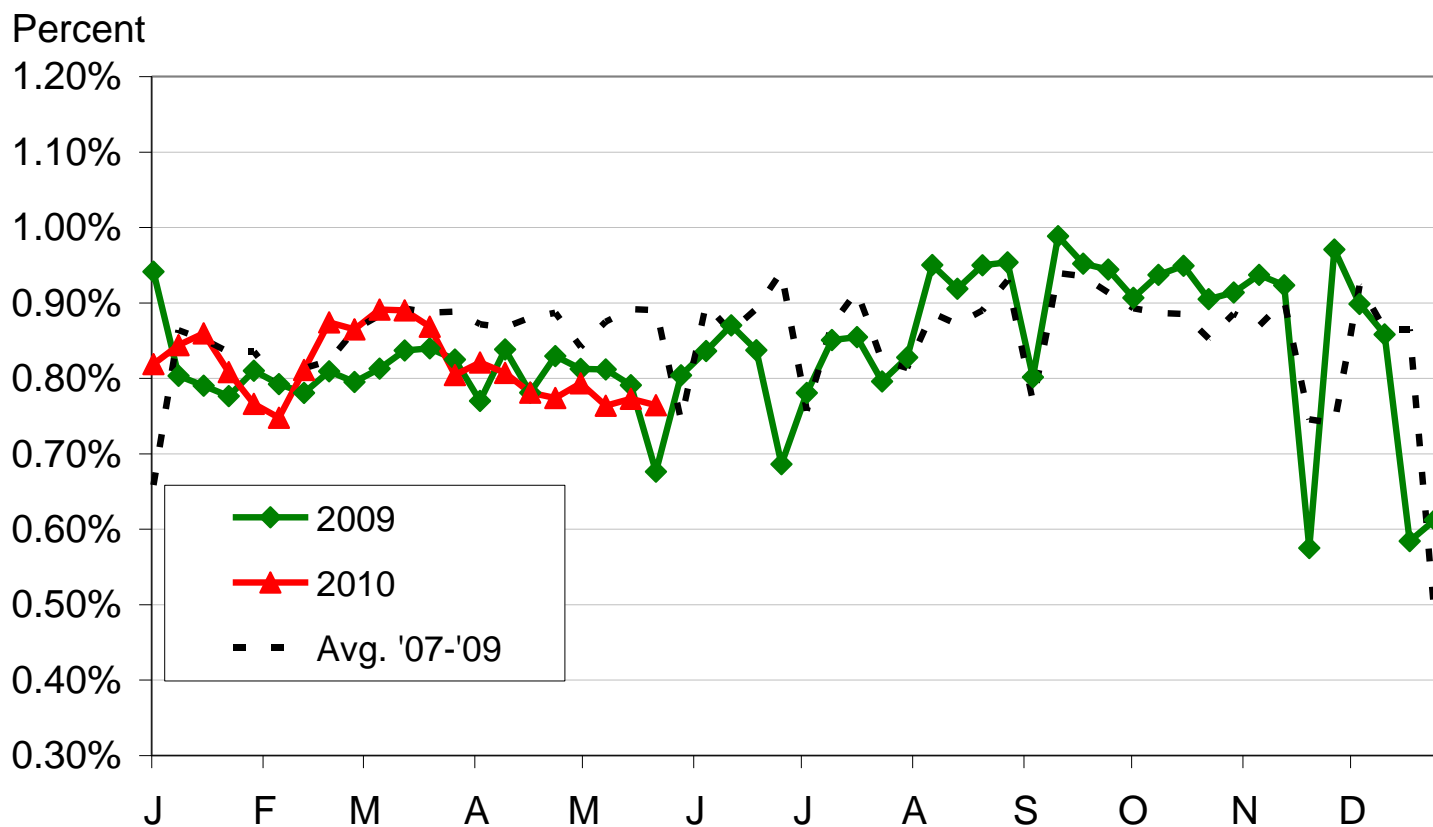


But slaughter of US sows is equal to '09 ...

... YTD '10 = 17.1% vs. 16.9% in '09

FI SLAUGHTER OF U.S. SOWS

As a Percent of Previous Quarter's Breeding Herd



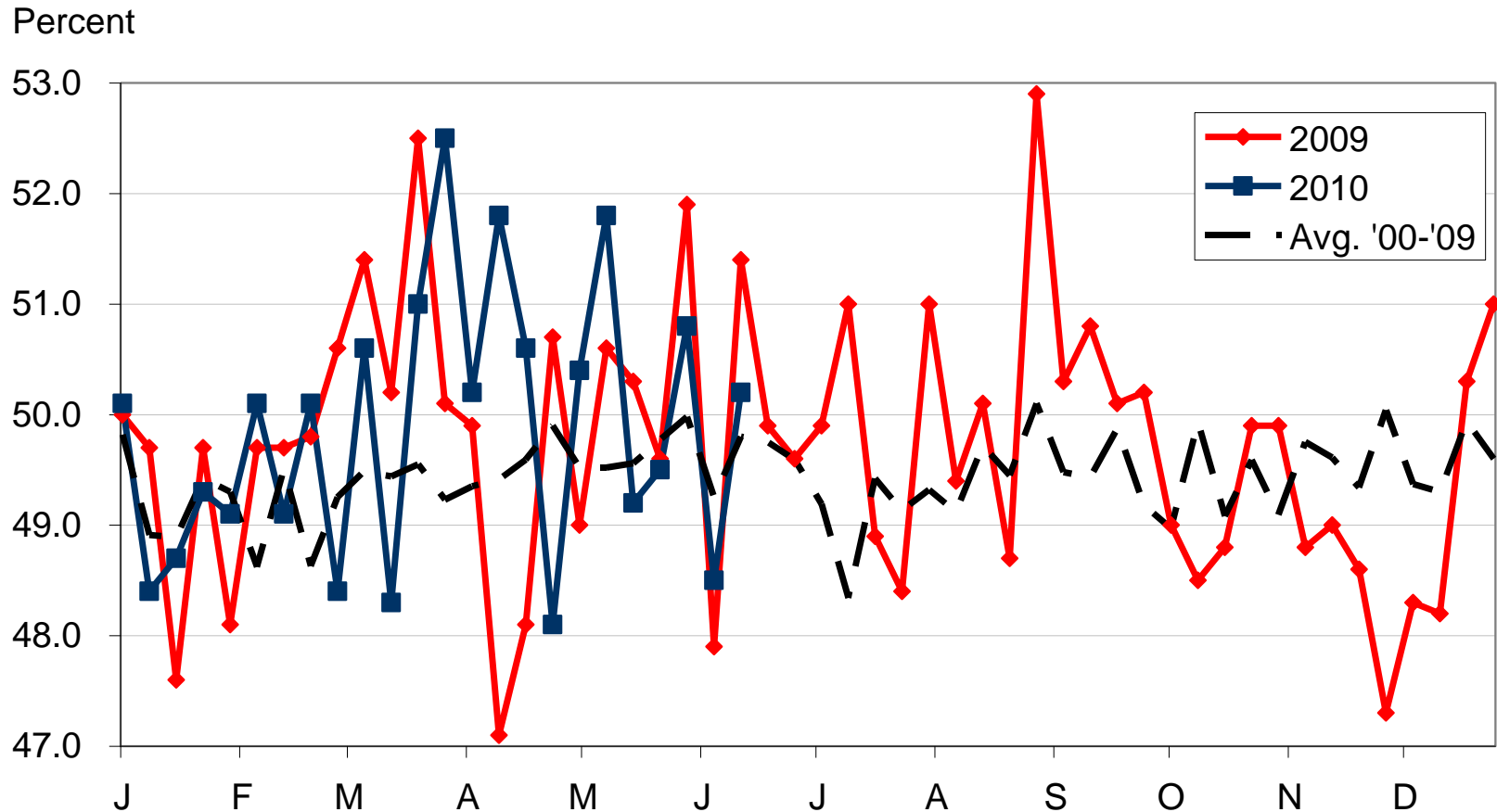
Paragon Economics, Inc.

From information, knowledge



YTD gilt slaughter: +0.1% vs. '09, -0.1 vs. '08

GILTS AS A PERCENT OF TOTAL BARROW/GILT SLAUGHTER



Paragon Economics, Inc.

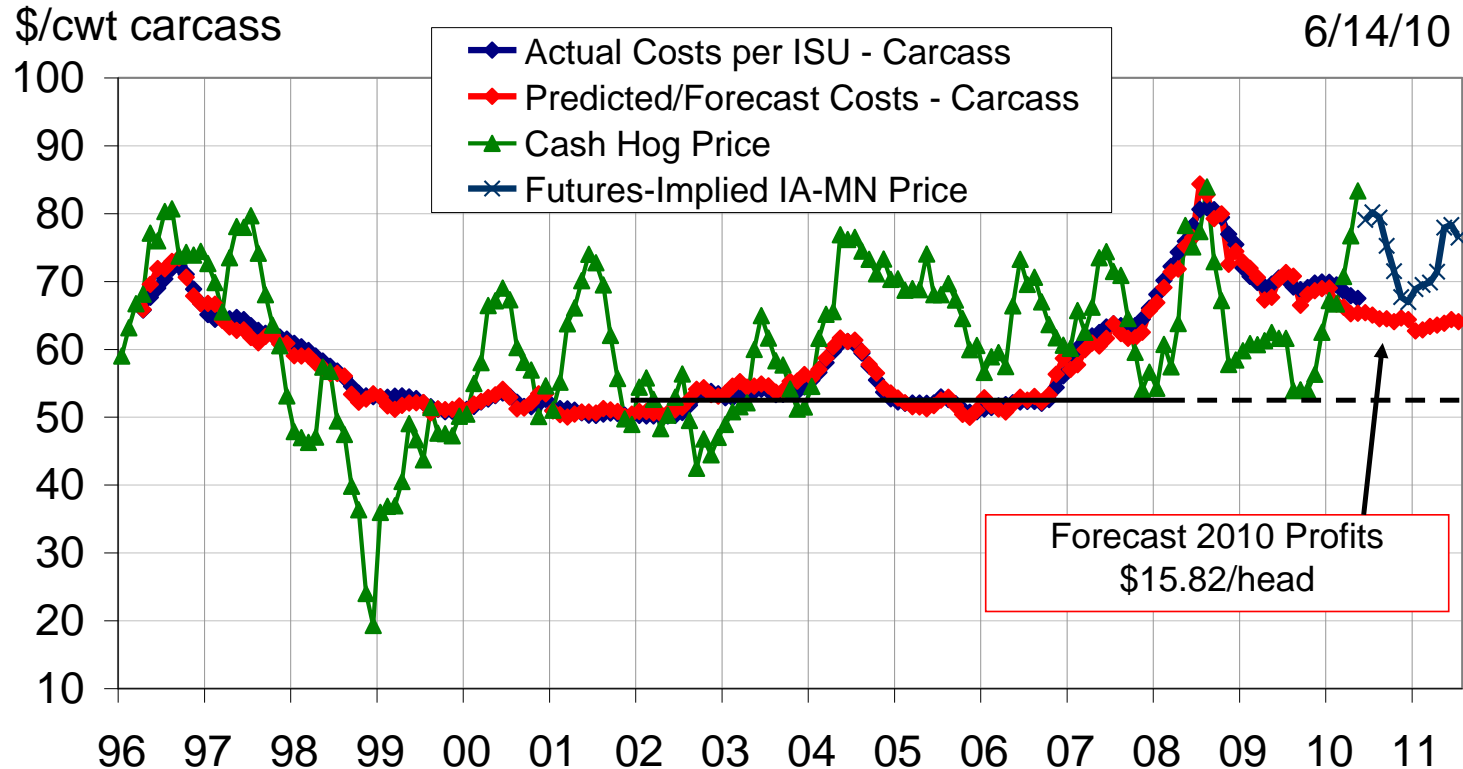
From information, knowledge



Futures: Profits of ~\$16/head for all of '10 ...

... and nearly \$20 for rest of '10, \$19 for '11

ACTUAL & PREDICTED HOG PRODUCTION COSTS* AND PRICES



*Based on relationship between ISU Estimated Costs & Returns data and historic Omaha corn and Decatur soybean meal prices

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Slaughter forecasts

March 2010 Commercial Slaughter Forecasts

		Mizzou		ISU		LMIC		Meyer	
		Mil. Hd	% Chnge	Mil. Hd	% Chnge	Mil. Hd	% Chnge	Mil. Hd	% Chnge
2009	Year	113.583	-2.7%						
2010	Q1	27.631	-3.1%	27.631	-3.1%	27.631	-3.1%	27.631	-3.1%
	Q2	26.575	-1.8%	26.395	-2.5%	26.198	-3.2%	26.139	-2.6%
	Q3	27.425	-3.5%	27.860	-2.0%	27.807	-2.2%	27.175	-4.4%
	Q4	28.775	-2.8%	28.726	-3.0%	28.973	-2.2%	28.184	-2.3%
	Year	110.406	-2.8%	110.612	-2.6%	110.609	-2.6%	109.129	-3.9%
2011	Q1			27.493	-0.5%	27.132	-1.8%	27.983	1.3%

Green figures are actual data from USDA.

3/2/10



Price forecasts

March 2010 Hogs & Pigs Price Forecasts

		Missouri	ISU	LMIC	Meyer	CME
		Producer-Sold Net Carcass	Ia-S. Mn. Live Price ¹	National Wtd Avg. Base Price	National Net Neg'd Price, Wtd. Avg.	CME Lean Hog Futures
						6/4/10
2009	Q1	60.43	56.48	58.11	57.22	\$58.14**
	Q2	61.76	58.39	59.45	58.19	\$59.03**
	Q3	56.68	52.60	54.01	52.39	\$54.18**
	Q4	57.64	55.92	55.57	55.81	\$56.60**
	Year	59.11	55.84	56.87	55.90	\$56.98**
2010	Q1	68.60*	70.41*	65.95*	68.75*	69.38**
	Q2	71 - 75	77 - 81	74-75	81.98*	80.70**
	Q3	73 - 77	72 - 75	70-74	76 - 78	77.51
	Q4	66 - 70	61 - 65	67-71	68 - 70	71.04
	Year	70 - 73	70 - 73	69-71	73 - 74	74.66
2011	Q1		63 - 67	70-75	66 - 70	70.13

¹Converted to carcass using a yield of 75% *Partial USDA data

**Average of CME Lean Hog Index



My expectations

- June Hogs and Pigs may show small BH growth from March but still down 2-3% from '09; 3-4% lower market supplies.
- Hog supplies will be supportive of prices in the upper \$70s to low \$80s for the rest of the summer
- Q4 prices in the upper \$60s
- Little or no expansion, 2011 numbers very close to 2010, prices depend on demand!



QUESTIONS & DISCUSSION?