Hog Liquidation Beginning

The USDA December Hogs and Pigs Report estimated that there were 62.2 million hogs on US farms December 1, with 55.5 million market hogs and 6.67 million breeding animals. These figures represent 2 percent more total hogs and market animals, and a 4 percent smaller breeding inventory. While this cycle has seemed longer than previous ones due to the extremely low prices, the breeding herd liquidation started approximately one year after producers began reporting losses. The estimated returns to farrow to finish operations reported losses beginning in November 1997.

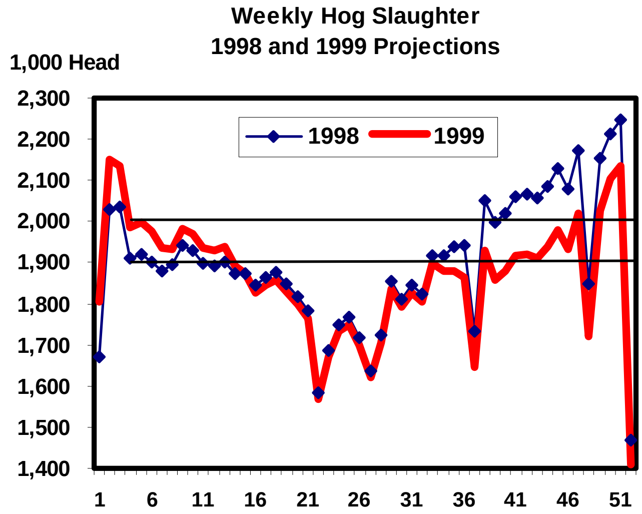
The key number to watch for signs of relief from the current low prices is weekly slaughter. Since Labor Day we have processed 2.0 million head a week or more. Statistical regression analysis indicates that prices have decreased $.09/cwt for each 1,000 head increase in weekly slaughter (100,000 head increase => $9/cwt lower prices). ***Prices should rebound in a similar manner as slaughter levels decline after the first of the year.*** The two holiday shorten work weeks will back-up some hogs into January, but based on this report we should begin to see weekly slaughter drop to the 2.0 million head level in February.

Below the 2.0 million head level, when supplies are below packer capacity, a 1,000 head a week change is slaughter results in only about a $.03/cwt price impact. Prices are expected to average in the teens in January before working there way to near $30 by the end of March. Second quarter prices are forecast to average in the mid $30s with the higher prices at the end of the quarter.

Table 1 USDA December Hogs and Pigs Summary

Category	**US 1,000 Hd**	**US % Chg**	**Iowa 1,000 Hd**	**Iowa % Chg**
All Hogs and Pigs	62,156	1.6%	15,300	4.8%
Kept for Breeding	6,672	-4.1%	1,260	-7.4%
Market	55,483	2.4%	14,040	6.0%
Under 60 Pounds	20,000	-1.2%	4,280	-2.1%
60-119 Pounds	13,641	2.4%	3,710	1.6%
120-179 Pounds	11,640	4.0%	3,180	14.4%
180 Pounds and Over	10,203	7.9%	2,870	17.6%
Pig Crop				
Jun-Aug	26,634	3.7%	4,638	-2.4%
Sep-Nov	25,878	1.5%	4,437	-0.8%
Farrowing Intentions				
Dec-Feb	2,893	-1.2%	490	-5.8%
Mar-May	2,884	-6.5%	490	-10.9%

First quarter slaughter will be largely determined by the Jun-Aug pig crop, estimated to be 3.7 percent above the year earlier. This will push weekly slaughter over the 2 million head range into February (Figure 1). Add to that figure increased sow and gilt slaughter, the backlog of hogs that currently exceed packer capacity, and continued imports from Canada and prices will be on the defensive.



Second quarter supplies will come from the Sep-Nov pig crop that was 1.5 percent above a year ago. *This will put weekly slaughter below the 1.9 million head range and near year earlier levels as we approach summer*. Additional sow slaughter during this period and pork product in cold storage from the previous two quarters of record production may limit prices below the 2nd quarter 1998 average of $38. In the September Hogs & Pigs report the Sep-Nov farrowing intention was +2.2 percent suggesting that producers have altered their plans since September.

Third and fourth quarter supplies will come from the Dec-Feb and Mar-May farrowing intentions which are both lower than the previous year and will result in lower pork supplies. The Dec-Feb intentions in the September report were +2.7 percent and it fell to -1.2 percent in this report as producers altered their plans over the last 3 months. ***This report is the first indication of the Mar-May intentions which are down a surprisingly large 7 percent***. Based on these estimates prices are forecast to average $37-40 in the third quarter and $33-36 in the fourth quarter.

The fourth quarter 1999 prices are forecast to be nearly $15 higher that prices averaged in the fourth quarter 1998. It assumes that weekly slaughter is below the 2.0 million head for the bulk of the quarter. It is possible that given this more optimistic price outlook producers that scaled back production without exiting the business may build back to full capacity or higher by breeding extra gilts to hit the fall 1999 market. While the recent large losses will limit expansion through construction, pushing throughput back to 105 percent of capacity in production facilities may occur.

Other factors…

Competing meats: Beef supplies are expected to be lower in 1999 than 1998. The biggest determinate will be slaughter weights that have been at record levels for over a year. Poultry supplies, particularly broilers will be 4-6 percent higher in 1999 than 1998. Much of the increase in poultry will be offset by the decline in beef.

Farm to retail: The farm to retail spread continues very wide for a much longer time than expected. Retail prices that have proven to be quite firm may begin to decline as cold storage stocks build. The increased attention to high retail prices by the national press and regulators will also pressure them and begin to aid pork movement. While lowering consumer prices to farm level prices will not help farm income, slightly lower retail prices to increase pork movement to pull product through the system will encourage packers to bid to keep plants running as full as possible.

Pork trade: Pork exports were 20 percent above the year earlier for January-October, but have slowed through the summer and fall. October exports were up only 2.2 percent over October 1997. While the lower hog prices will encourage exports, weak currencies relative to the US dollar will limit export growth. Further complicating the trade is the imports of pork. Through September imports were up 5.5 percent and they were higher in the summer months. The increases came from several countries, Canada, Denmark, Poland, Hungary, and Netherlands.

Canadian hogs: Year to date through the end of November live slaughter hog imports from Canada totaled 2.2 million head, 15 percent higher than the same period in 1997. In the month of November Canadian slaughter hog imports totaled 145,018 compared to 208,026 in November 1997, approximately 30% fewer. Canadian feeder pig imports totaled 1.145 million head January through November, a 25 percent increase over the same period in 1997.

The bottom line is that prices cannot increase significantly until slaughter levels decline back in line with packer capacity. When packers have to bid for enough hogs to fill a shift hog prices should rebound quickly. Once the slaughter capacity pressures are reduced, the industry must still move the product. Reduced retail prices, exports, and continued promotion will be necessary.

The structural change to fewer, larger, and more specialized hog operations and greater use of marketing contracts between producers and packers make it more difficult to say that history will repeat itself. The staggering losses and the loss of equity by large and small producers will undoubtedly limit the rapid expansion witnessed in 1996-97. The faltering Asian economies and slower growth of exports also added a dose of reality to the pork industry. In total, the flow of capital will likely slow in the years ahead.

Iowa Inventories…

Iowa's hog inventory is up 5 percent compared to December 1997 (Table 1). The breeding herd is 100,000 head or 7 percent lower while the market hog inventory is up sharply in the over 120 categories. The pig crops since June and farrowing intentions through May are also lower.

North Carolina, the second largest hog producing state farrowed more pigs in 1998 than did Iowa and breeding herd inventory that was unchanged from the previous year. *This is the first time that North Carolina's December breeding herd has not increased since 1989.*

Nebraska and Missouri were the only top ten states to report an inventory decline compared to a year ago. Minnesota and Ohio reported a stable inventory.

The number of farms with hogs did not decline as much as expected. The US total was 114,380 farms with hogs. *Nationally, the USDA estimates that 25,000 farms with at least 500 head hogs hold 89 percent of the inventory. In Iowa there are 8,300 of these farms with 90 percent of the state's hogs.*

Table 2. Pork Industry Structure, December 1998

Inventory	US Operations	US % Inv	Iowa Operations	Iowa % Inv
1-99	62,370	2.0	2,900	0.5
100-499	27,015	9.5	6,300	9.5
500-999	11,455	11.0	4,100	15.0
1000-1999	6,855	14.0	2,450	20.0
2000-4999	4,770	21.5	1,430	27.0
5000+	1,915	42.0	320	28.0
Total	114,380	100.0	17,500	100.0

Management Implications…

Producers and lenders are planning for 1999. The price forecast based on this report suggests that average producers will return to breakeven prices for a brief period in the summer after 18 or more months of losses. If this cycle behaves as previous ones the year 2000 should see higher, profitable prices. While the timing of liquidation is consistent with other cycles, the extent of the losses is unprecedented. A producer may be able to cut his or her losses by quitting the hog business, but the losses that have occurred must be regained.

Many operations that are committed to the pork industry will be able to restructure their short-term debt over a loner period of time and continue operating. Profits generated in 1996-97 reinvested in assets provide a base to borrow against. Realistic cash-flow projections made when the hog facility loans were originally financed should still be realistic today as the life-of-building earning power of the facilities should not be based on today's prices no more than it should have been based on the peak prices of 1997. However, restructuring the accumulated losses of 1998-99 over at 5-7 year horizon may add as much as 5-10 percent to the cost of production.

Each farming operation is unique and the individual farmer and lender will need to develop a plan that is best for the business. Some farmers will qualify for loan guarantees through existing Farm Service Agency programs. Other programs to assist producers that do not quality for FSA programs may be announced by either the federal of state government. Other, more innovative, programs are also being discussed and may also be available. Although it is difficult to make rational decisions in a crisis situation, that is what producers are facing. Efforts should be directed at financial management and planning and assistance is available to evaluate those plans. Farm Management Field Specialists and Farm Financial Planning Associates are available throughout the state to assist Iowa producers with financial and farm management decisions. Contact your Iowa State University Extension office for more information.