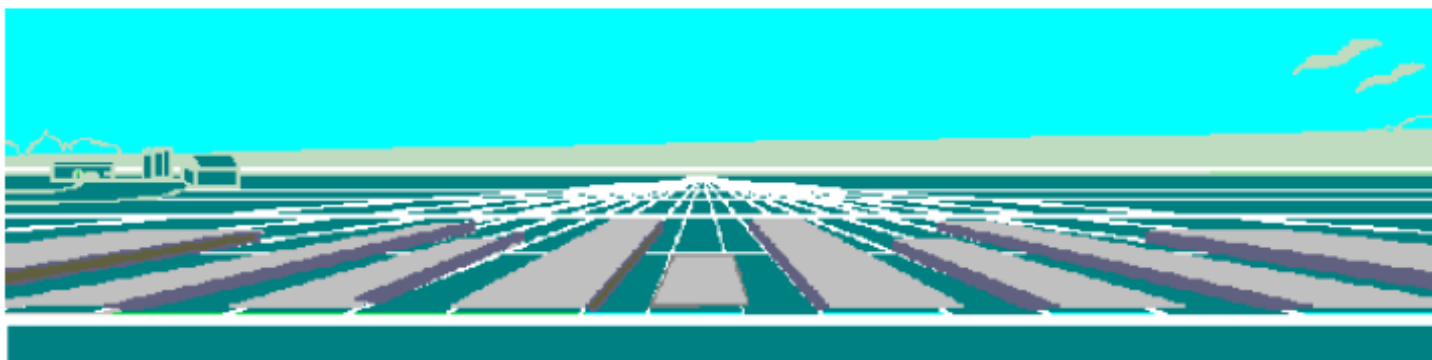


Iowa Farm Outlook



September 1, 2007

Ames, Iowa

Econ. Info. 1965

Pork Packer Capacity

Growing hog inventories, improved hog health, and increased imports from Canada will increase the supply of hogs this fall. At the same time, packing plants have closed, modestly reducing the US slaughter capacity. Larger pork supplies will pressure prices this fall. If we have multiple weeks of hog supplies at or above plant capacity, it will push prices lower yet.

Few pork producers will ever forget December 1998 when hog prices dipped below \$10/cwt and averaged below \$15/cwt for the month. One of the main reasons for the extremely low prices was the lack of packer capacity to slaughter and process the number of hogs on the market. The market hit a packer capacity constraint as most plants were operating double shifts, Saturdays, and in some cases Sunday. While no one is predicting a repeat of 1998, there are several factors and analysts pointing to potential problems this fall. We will first look at that expected packer capacity and hog supplies. Then we will look at risk factors that may cause capacity to be an issue.

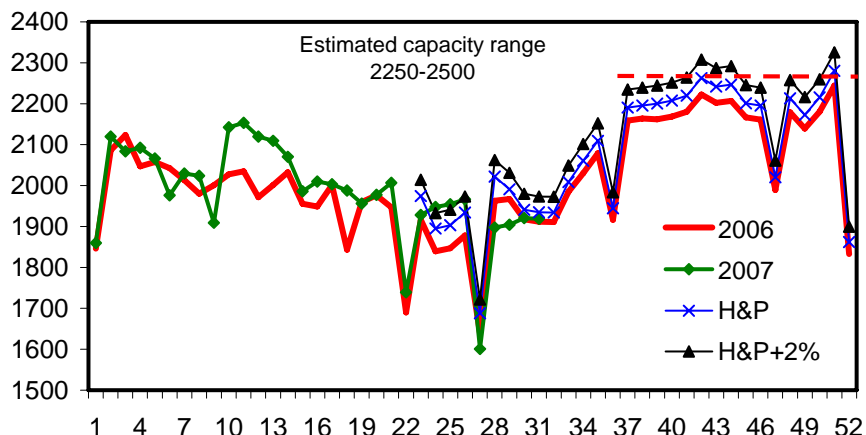
Expected Packer Capacity

In 2006 the largest daily slaughter was slightly over 428,000 head and the largest weekly slaughter was 2.24 million head. However, since that time a double shift plant in Mississippi closed, as did one shift of a plant in Sioux City, reducing daily capacity approximately 20,000 head. Other plants have added capacity and it is now estimated that daily capacity is nearly 425,000 head (estimated by Steve Meyer, Paragon Economics). That will put the five-day total at 2.125 million. Saturday operations will be an essential factor for slaughter capacity. While a “large” Saturday kill for fall is 120,000, the Saturday of Thanksgiving week in 2006 was nearly 400,000. Thus, a potential weekly kill may be near 2.5 million head, but a more typical week is closer to 2.25 million head.

Expected Hog Supplies

Based on the June Hogs & Pigs report there is expected to be approximately 1.2% more hogs for slaughter this fall. Using this increase there will be only three weeks near the 2.25 million weekly slaughter (Blue x-line in Figure 1).

Weekly Commercial Hog Slaughter



One of the justifications for hog slaughter in 2006 being lower than expected was Circovirus that caused higher than normal deathloss in finishing barns. There is now a widely used effective vaccine that reduces deathloss. As such, the change in hog supplies may increase more than indicated from the Hogs & Pigs report.

Year-to-day through early August slaughter hog imports from Canada were up 16% from the same period in 2006. On August 30, Maple Leaf Foods announced that it will close a hog slaughter plant in Winnipeg, Manitoba due in part to labor issues. This is the second Maple Leaf plant closed this year. Maple Leaf has announced plans to shift production to their Brandon, MB plant by 2009. However, for this fall and 2008, more hogs are expected to be exported to the US for slaughter.

Figure 1 has a line (Black triangles) that is 2% higher than the slaughter predicted by the Hogs & Pigs report, to reflect more hogs from the use of Circovirus vaccine and exports from Canada. If this scenario occurs, weekly slaughter could exceed 2.25 million head six or more weeks in the fourth quarter, but doesn't reach 2.4 million head. If there is a larger "vaccine" effect or hog imports are larger, there will be considerable pressure on prices.

Other Risk Factors

While packer capacity is an issue to watch, as it could significantly impact prices, there are other factors that could impact hog prices this fall.

Carcass weights, which had been lower than the year before through much of 2006 and the first half of 2007, have started to increase. While higher corn prices can explain lower weights in the fall and winter, they don't explain lower weights last summer. It is possible that the weight decrease was related to Circovirus that is now corrected by vaccine. Weights began posting year-over-year increases in July and are expected to continue higher through the remainder of 2007.

Pork exports have set new record levels in each of the last 15 years and in 2006 accounted for nearly 15% of US pork production. However, through the first six months of 2007 exports are lower than the year earlier. The decline is explained by decreases to Mexico, our second largest market, as other leading markets were steady to higher. There has been a lot of emphasis and bullishness on potential exports to China. Pork exports to Mainland China and Hong Kong were up 24% from the year before through June, but the expectations are for significantly larger exports to China later this year. It appears that these potential exports are already bid into the futures market. If the exports materialize, it is doubtful that there is much upside price potential. If the exports do occur, but are less than expected, then prices will be weaker.

Poultry supplies are increasing from the year before. In 2006, broiler producers were in significant red ink and began cutting chick placements in the fall of the year. As a result, supplies fell and broiler prices increased sharply to profitable levels. Broiler producers are now ramping up production. The higher poultry production will compete with pork at the retail meat counter.

Summary

Packer capacity will be tight this fall and pork supplies will be larger than last year. Weaker exports and cheaper competing meats will limit demand and more hogs at heavier weights will increase supply. In late August, December futures were trending higher at over \$69 (carcass weight basis). Even with a typical basis, the farm level prices would average in the upper \$60s and live hog prices over \$50/cwt live weight. These prices should offer breakeven price protection for most producers.

John Lawrence

Grain Markets Await September 12 USDA Crop Forecasts, Wheat and Soybean Market Strength: Implications for 2008 Acreage, Risk Sources for Corn

Corn and soybean prices will take direction from forecasts in the USDA September 12 crop production report and weather as the harvest season approaches. If production forecasts are near or slightly above last month, corn cash and futures prices would have modest down-side risk into the harvest season. Cash prices may have a bit more downward risk than futures because of shortages of storage space in some areas and pressure on elevator drying and receiving capacity. After harvest, a gradual upward trend in corn prices into spring appears likely as the corn, soybean, cotton, and wheat markets compete for cropland. World wheat stocks are at record low levels as a percent of annual use, and wheat prices are at a very large premium over corn. Some potential 2008 soybean acreage may be shifted to winter wheat this fall, thus causing the soybean market to attempt to draw some corn land back into bean production.

New-crop corn export sales so far are the largest for this date since 1995, when U.S. and foreign crop problems pushed Iowa cash corn prices over \$5 per bushel for nearly six months. Current strong export demand in part reflects high wheat prices that are reducing foreign wheat feeding. Risk factors that might temper or limit corn upward price potential into winter and spring include (1) a possible shortage of transportation and blending capacity for the large increase in ethanol production in the next several months, (2) a large increase in Brazilian and Argentine corn and soybean plantings this fall and favorable weather there, (3) a deterioration in global economic activity, or (4) an unexpected sharp decline in global oil prices.

Record Wheat Price Premium to Corn: Implications

Wheat prices on all three U.S. futures markets have been in a nearly steady uptrend since the April 2007 freeze. On the Chicago Board of Trade at this writing, December 2007 wheat futures are at an extremely high 230% of December 2007 corn futures. In dollars, the December 2007 wheat price is \$4.39 per bushel above this year's December corn futures. That compares with the old record of \$3.00-\$3.25 premium over nearby corn futures in the early 1970s, when the Soviet Union was just beginning to import wheat in large volumes. A chart on the wheat-corn price spread was shown this week on the Chicago Mercantile Exchange Daily Livestock Report. That is a free report available from www.dailylivestockreport.com/subscribe.asp

The high wheat prices have resulted from (1) record low global wheat stocks as a percent of use, (2) foreign weather problems, especially in Europe and last year in Australia, (3) a recent Canadian crop report indicating production there is well below last year, (4) an exceptionally wet harvest season in the southern U.S. Great Plains that prevented harvesting of a substantial amount of wheat, (5) recent nervousness about Australia's upcoming November-December harvest, (6) indications that India will be a large importer of wheat this marketing year, in contrast to its recent role as a wheat exporter, and (7) a large wheat market that has developed in Iraq. Normally, wheat is of minor interest to those in Iowa agriculture since very little wheat is grown here. However, the high wheat prices are supportive to corn price prospects this winter and next spring.

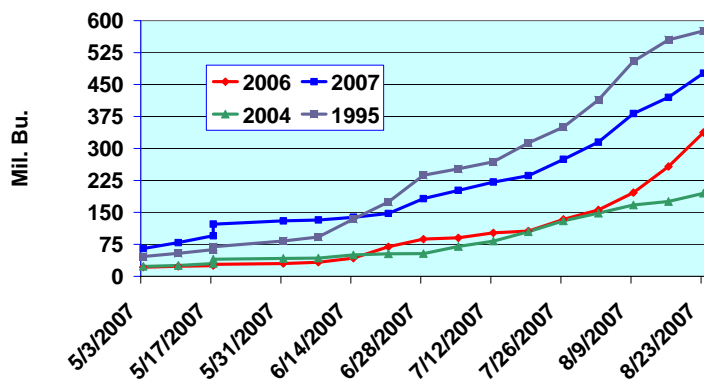
One connection between the record-high wheat prices and corn is through reduced wheat feeding here and abroad. Wheat feeding in the U.S. usually is relatively small and typically occurs mainly in the summer months. The September 30 USDA Grain Stocks Report will provide an updated indication of how much wheat was fed this summer, and how it affected domestic corn feeding during the summer quarter.

Another connection between wheat and corn prices will be in competition for cropland. Depending on the timing of the soybean harvest, farmers along the eastern edge of the Great Plains, as well as in the eastern Corn Belt and South will have a strong incentive to plant part of this year's soybean acreage to winter wheat. The temptation to do so is further strengthened by a strong soybean market that reflects tightening supplies that result from this year's 15% decline in U.S. soybean plantings. From the southern part of the eastern Corn Belt into the south central and southeastern U.S., high soybean prices offered for delivery in the fall of 2008 will make double cropping beans after wheat potentially more attractive than planting corn on those same acres. The eastern Corn Belt had an estimated 3.3 million planted wheat acres this year.

Wheat prices, global wheat feeding, and new-crop corn exports

At the global level, wheat feeding is much more important—typically being at least twice as large as U.S. corn exports. High priced wheat likely will reduce foreign wheat feeding. Since corn prices are so much lower than wheat, the higher wheat prices appear likely to strengthen export demand for U.S. corn. That and reduced feed grain production in the EU and parts of the former Soviet Union are factors behind the very strong U.S. new-crop corn export sales. New-crop export sales through August 23 were up 93% from a year earlier, and were the largest this early in the season since 1995. Strong export sales in 1995-96 and moderately reduced U.S. corn production led to \$5 per bushel cash corn prices for nearly six months in the spring and summer of 1996.

Figure 1. Outstanding New-Crop U.S. Corn Export Sales



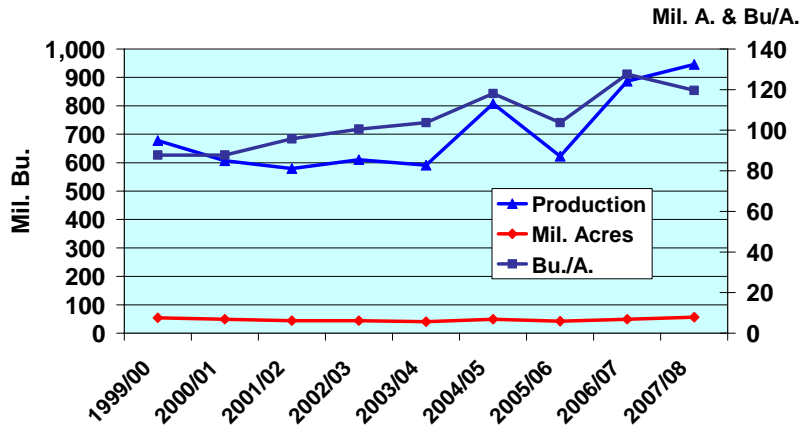
This year's corn export sales so far are up 41% from a year earlier. They are at the highest level for this time of the year since 1995, although they lag 17% behind the same date in 1995. The strong new-crop export sales suggest the USDA may be a bit low on their recent projection that 2007-08 U.S. corn exports will be up only 2.4% or 50 million bushels from the season just ending. Part of the recent large export sales also reflects foreign buyer desires to get supplies booked earlier than last season to avoid future price increases.

South American competition

Exports from May onward will reflect competition from South America's yet to be planted 2008 corn crop. Early reports from South America indicate a modest increase in corn planting is likely in Argentina. Our recent contacts with seed industry people from there suggest a moderate increase in its corn acreage is likely this fall. However, last spring's Argentine corn and soybean yields were exceptionally good, and somewhat lower yields are expected in 2008. Indications from Brazil suggest some increase in soybean acres is likely.

Projections we have seen range from increases of 5 to 6 percent to as much as 11 or 12 percent. Brazilian corn acreage may also increase some, but an exchange-rate disadvantage and high costs of getting the crop to the port in recently developed areas may limit the expansion. In northern parts of its Grain Belt, corn typically is planted after the soybean harvest. That's the dry season, and a time when rainfall is more variable. Timing of soybean planting and harvesting can affect corn yields if delayed soybean plantings delay corn planting, pushing it further into the dry season.

Figure 2. Argentine Corn Acreage, Yield and Production



While Argentina currently is the second-largest corn exporter in the world, its production is quite small by U.S. standards. Last spring, Argentina harvested an estimated 6.9 million acres of corn and produced about 887 million bushels of corn, with a national average yield of 127.6 bushels per acre. Argentina's total corn crop was equivalent to 8% of the U.S. crop. A 12 to 14 percent increase in Argentine corn area to be harvested next spring, with a 6 % decline in yield from last spring would produce about 43 to 59 million bushels more corn than last year. These potential numbers for the 2007-08 crop are consistent with those from a group of 32 Argentine seed company management people who recently visited ISU. USDA projects a 14% increase in Argentine plantings this fall, with a 6% increase in next spring's harvest. Last spring's Argentine corn yield was an estimated 18% above the three-year average.

Weather & U.S. production

The September 12 USDA crop report should provide insight on the net impact of recent heavy rains across parts of the northern Corn Belt and hot, dry weather from the southern 50-60 percent of Illinois into the Southeast.

Robert Wisner