HOG PRICES TAKE OFF, PROBABLY DUE TO PED-V

How large are the losses of baby pigs due to PED-V (Porcine Epidemic Diarrhea Virus) and how will the losses reduce slaughter supplies this spring and summer and for the rest of 2014? No one knows the correct answer, but lean hog futures market participants seem to have decided that the losses will be very large for slaughter supplies this spring and summer. In the past two weeks, April lean hog futures have risen by $10.68 and June futures have risen by $6.10 to record highs.

But, have market participants over-anticipated the magnitude of losses due to the PED virus? So far this year, the number of animals coming to market has been very close to the number indicated by the USDA December Hogs and Pigs report. When adjusted for the number of slaughter days compared to last year, the slaughter count so far is down about 0.5 percent. However, market weights have been higher by about 2.5 percent, resulting in total pork production being up about two percent. Year-to-date hog prices have been close to those in the same period in 2013.

The lean hog futures market has extremely high price expectations for the March through July period this year, apparently due to expectations of small slaughter supplies due to PED-V losses. Projected lean hog prices for that period using futures closes on February 28 suggest expected prices averaging near $105 per hundredweight, compared to $86 for the same period one year ago. If low supplies are thought to be the cause, then this is suggesting market participants believe that hog slaughter supplies could be down seven to ten percent during this time period. This also assumes that other factors, such as low beef supplies, are also factored in.

How does this potential seven to ten percent anticipated decline in slaughter numbers stack up against the USDA December inventory count? Second quarter 2014 supplies will come primarily from the under 50 pound pig count on December 1, which was down about 0.5 percent. Thus market participants may be anticipating that many of those very young pigs that were in inventory on December 1 ultimately died due to PED-V.

Third quarter 2014 supplies will be drawn heavily from winter farrowings and this is where numbers get very uncertain. Winter farrowing intentions were up 1.3 percent, but since PED-V kills baby pigs the number of pigs weaned per litter could be down sharply.
This is what no one knows for sure. One helpful reading from the USDA inventory survey was the number of pigs weaned per litter during the fall 2014 farrowing. That was about two percent lower than the trend weaning rate.

The impact of PED-V is thought to intensify in cold weather so the loss of baby pigs could be higher than two percent during the period of November 2013 to March 2014. Again no one knows the impact on a national basis, but lean hog futures participants may be expecting losses to be as high as seven to ten percent. If the actual impact is closer to three to four percent, then futures prices may ultimately have to adjust lower. Great uncertainty continues for the size of the spring pig crop. Farrowing intentions were also up somewhat over one percent, although the impact on death losses from PED-V are expected to moderate as weather warms. All great uncertainties eventually get resolved in the market place. For the hog market, this will occur as we see the actual number of slaughter hogs coming to market from March through July this year.

The bigger question is how PED-V will impact the economic returns for the entire pork industry in 2014. The initial answer may be somewhat surprising. PED-V will likely increase economic returns if those returns are measured across the entire U.S. industry. Why? The demand for pork is relatively inelastic and this means that when there are short supplies, consumers are slow to adjust consumption downward. As a result, prices will tend to increase by at least two percent for each one percent that the quantity of pork drops. This means that total revenue in the industry will likely increase due to PED-V and more than offset the losses from the disease.

However, the outcomes of individual producers will likely vary as higher revenues from increased hog prices are compared to the financial losses due to death loss. Those who have death losses from PED-V that are very severe (having PED-V losses that are greater than the national average) will probably have net financial losses. Those individual producers who have average death losses from PED-V will likely be better off as the revenue increase may be bigger than the PED-V financial losses. Of course those who have no or only small PED-V death losses will be better off as the increased revenue due to higher hog prices is more beneficial than the small PED-V financial losses.

At the farm level, current futures markets are suggesting a live price for 2014 at a record high of $73 per hundredweight compared to $64 last year. This will provide record high industry revenues and the highest profit per head since 2005.

Who is going to pay for these record high pork producer revenues? Unfortunately, the consumers of pork are expected to be large net losers from PED-V as they will have to pay record high retail pork prices and also have less pork availability.

Issued by Chris Hurt
Extension Economist
Purdue University