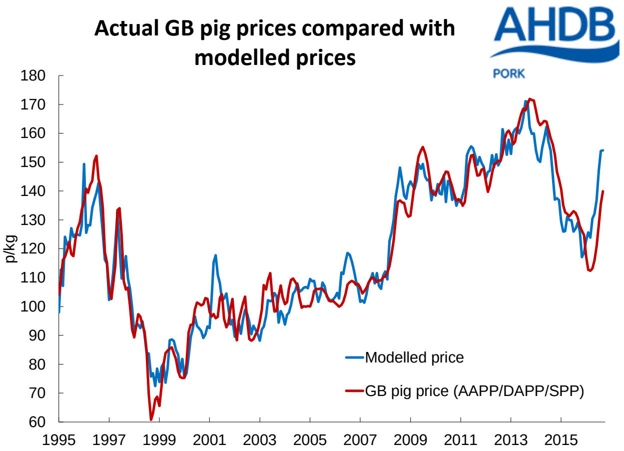
How high can the pig price go?

Back in April, we published the results of analysis of the factors affecting GB pig prices over the long-term. This showed that historical prices could be modelled fairly closely using factors such as exchange rates, production levels, imports and exports, global commodity prices, EU prices and the price of imported pork.

At that time, pig prices were at an eight-year low but the model showed that the direction of prices should have started to turn upwards. Sure enough, not long afterwards prices did, indeed, start to increase and have continued to do so. Since then, a lot has changed, with the Brexit vote meaning, in particular, that exchange rates are more volatile and likely to continue to be. So what does the same model tell us about the situation now?

The original model was based on data up to January 2016. We now have more data points available, so have updated the model. This confirms that prices might have been expected to start rising again at the start of this year and continued rising since. It also suggests that September prices might have been expected to be higher than they were.



Source: AHDB analysis based on data from various sources

However, one feature emerging recently is that the actual pig price appears to be lagging the modelled price by two or three months. In other words, the price level predicted by the model seems to be close to the actual level a little later. This seems to be true both when the market is falling and when it is rising. The reason for this is unclear but it may be because many contract prices now take account of a wider range of factors than just immediate market conditions.

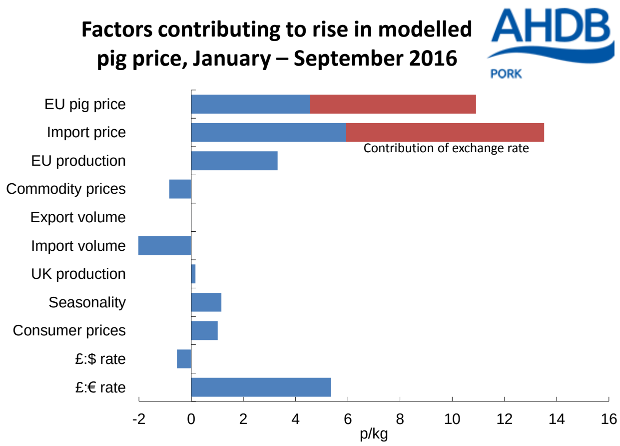
Whatever the reason for the time lag in the model, it does suggest that prices might have been expected to continue rising since September. So far, that has proved to be the case, with the GB SPP approaching 150p/kg in early November. If the time lag continues, the model suggests that prices may continue to rise in the short-term but could begin to level off towards the end of the year.

Of course, no model is perfect at predicting the future. A range of factors will affect pig prices and only some of them are included in the model. In any case, we don't know how the variables used in the model will develop in the future. History suggests short-term deviations from the model frequently happen, so there is still uncertainty about the future direction of the market.

Analysis of the modelled price can also tell us about the importance of different factors influencing the GB pig price. One thing which is immediately clear is the importance of the exchange rate between the pound and the euro.

The exchange rate itself is one of the variables included in the model and, this alone, accounts for around 5p of the rise in the modelled pig price between January and September. However, the value of the pound also influences both the EU pig price and the price of imported pork in sterling terms. Adding in these two contributions, the overall effect of the exchange rate may have been as high as 19p. That is more than half of the rise in the modelled price.

The weakening of the pound against the euro compounded the impact of higher continental prices and their effect on the value of imported pork. However, the tight supplies and higher prices on the EU market appear to be the other major drivers of the rise in UK pig prices over the last six months. This is partly offset by the unexpected increase in the amount of pork imported, based on official figures.



Source: AHDB analysis based on data from various sources

Based on the model, other factors to which some of the rise in prices have been attributed may have been less influential. These include exports and lower domestic production. However, these factors will be related to others in the model, so their true influence may have been stronger. Nevertheless, this analysis illustrates the key role which the exchange rate and the EU market still has on the UK pig price. In that context, the recent strengthening of the pound and drop in continental prices could sound a note of caution around prospects for pig prices into 2017, although the outlook still looks positive in other respects.