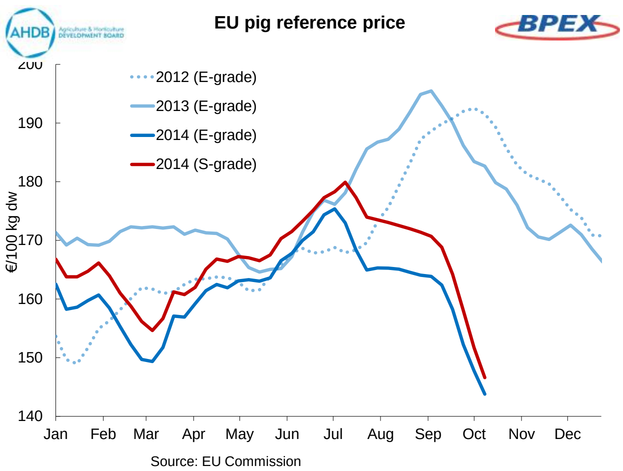
Challenging times for EU pig producers

This time last year, EU pig producers were expecting 2014 to be a positive year. Although pig prices had fallen back from last summer's near-record levels, they were still historically high. At the same time, feed prices had fallen and, with PEDv affecting production in many parts of the world, export markets looked favourable. All this meant that profitability looked set to be better, after several difficult years.

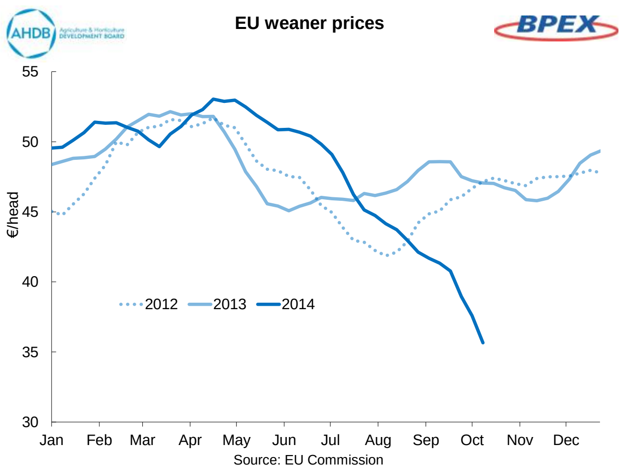
Then came confirmation of ASF in Poland and the Baltic States and the subsequent Russian ban on imports of pork products from the whole EU. While this had an immediate impact on EU pig prices, they quickly bounced back due to the strength of other export markets. Better weather conditions in northern Europe even stimulated some demand from consumers there. In fact, prices picked up so well that they were close to year earlier levels at the half way point of the year. At this stage, producers' expectations of a good year looked to be on track, with feed prices still falling.

However, unlike the previous two years, when prices continued rising throughout the summer due to tightening supplies, the onset of the holiday season led to falling quotes. Then, in early August, Russia announced its ban on a wide range of agricultural products from the EU and other western nations, in response to the situation in Ukraine. This meant that the prospect of being able to clear stocks from freezers and chillers within the next few months disappeared. At the same time, the global impact of PEDv was beginning to wane, leaving the market on a knife edge.



A modest increase in pig supplies in September was all it took to send prices tumbling. The EU average price lost over 20 cents per kg in five weeks, reaching its lowest level since early 2011, when the industry was affected by a dioxin scare in Germany. Despite feed prices also being at a 4-year low, this meant that most EU producers were back in the red.

The situation was particularly bleak for EU pig breeders. Since peaking in the spring at €53 per head, its highest level since EU expansion in 2004, the EU average weaner price has dropped by nearly a third. By mid-October it stood at little over €35 per head. Given the low level of feed prices at the moment, this indicates a particular lack of confidence about the future direction of pig prices.

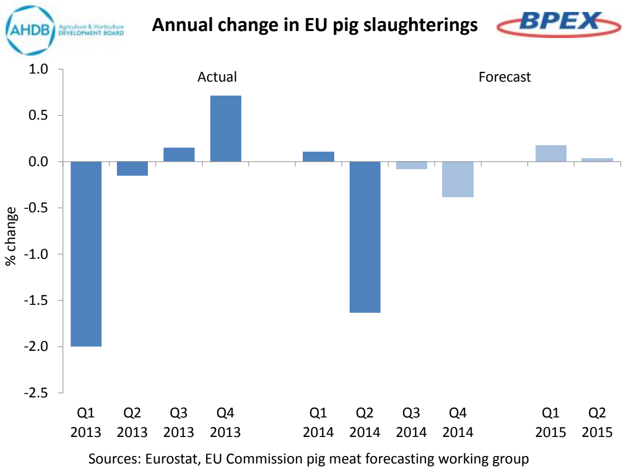


The subdued market this year has largely been demand driven. Pig supplies remain relatively tight, with EU slaughterings down by 1% on a year earlier in January to July 2014. Reports suggest there has been a modest increase in supplies this autumn but, even so, this is likely to be the third straight year of declining throughputs.

So what does the future hold? As reported last month, figures from the May/June agricultural surveys carried out in the major EU Member States show a 1% increase in the pig herd. More significant in a historical context was a rise in the EU breeding herd; the number of sows increased by nearly 1% compared with June 2013, the first rise since about 2005.

Despite these results, the tight supply situation is set to continue, according to members of the EU Commission's working group on pig meat forecasts. The group forecasts that pig slaughterings across the EU are set to remain close to year earlier levels through the rest of 2014 and the first half of 2015. The group's figures suggest a small year-on-year decline in slaughterings through the remainder of this year, with throughputs down about 0.5% for the year as a whole.

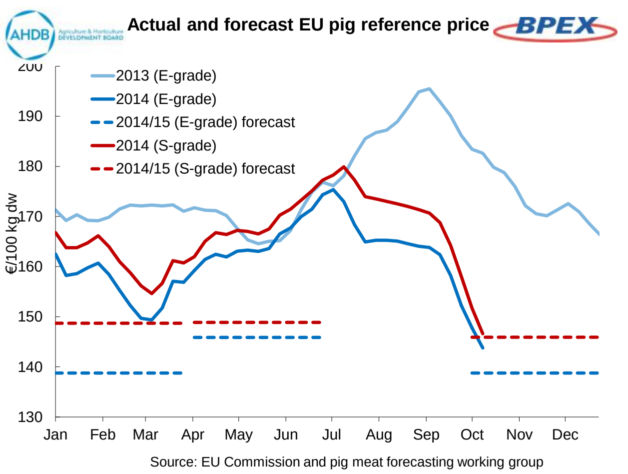
Furthermore, throughputs in the first half of 2015 are forecast to be only marginally up on this year. Most major producing Member States are forecasting little change in production. German output, for example, is forecast to track only slightly higher than a year earlier, while Danish slaughterings may fall, despite higher piglet production, as weaner exports continue to rise. Spanish forecasts also suggest little change in production from domestically born pigs, despite a bigger sow herd, although a rise in weaner imports will mean its kill increases. This may prove pessimistic, however, which may mean a slightly bigger than anticipated rise in EU slaughterings.



However, the relatively tight supply situation may not be sufficient to provide much support to prices. Having previously had only a modest effect on prices, the Russian ban on imports of EU pork is now beginning to bite. The autumn was previously the peak season for exports to Russia and, with freezers and cold stores reported to be full of supplies which might previously have been sent there, demand for slaughter pigs is lower than normal.

Although the market has shown signs of stabilising lately, further falls are still possible. The EU Commission's working group forecasts that the average price for E-grade pigs during the last quarter of this year and the first three months of next year will be below €140 per 100kg. This is around €5 below the level in mid-October. If realised, these would be the lowest quarterly averages since the final three months of 2010. Only a modest recovery is expected during the spring, with prices set to remain well below this year's levels.

Prices for S-grade pigs are expected to hold up slightly better, averaging around €145 per 100kg in the final quarter of this year, close to their current level. However, the gap between the grades is forecast to narrow in the spring. This is based on reasonable weather conditions stimulating demand, meaning that processors will be less choosy about the pigs they take.



Of course, these forecasts are based on the Russian market remaining closed to most EU pig meat products. It now seems certain that it will remain in place until August 2015, at least. Some estimates suggest that prices would have been 10% higher without the ban. However, one glimmer of hope relates to fats (e.g. lard), one of the main product groups which was previously exported to Russia. They are not included in the Ukraine-related ban (so the US and Canada can still send fats to Russia) but were covered by the earlier ASF one. With the EU its dominant supplier and others unable to fill the gap, Russia is short of fats. Although it doesn't seem likely at the moment, there is therefore a chance that Russia could be encouraged to reopen its market to some EU fat suppliers before next summer. This would add value to the EU market and give some support to prices.

With Russia still closed and little sign that domestic demand is going to increase dramatically, price prospects depend on developments on other export markets. Tight global supplies, because of PEDv in North America and Asia, have helped EU exporters to find alternative markets this year. Prices in other major exporters have been high, which means that EU pork has been more competitive than in previous years. This has prevented prices from dropping much more than they actually have done this year.

At this stage, it is unclear how global markets will develop. The key uncertainty is over PEDv. The number of cases has dropped away significantly over the summer but this is a winter disease. Much will depend on how cases build up again as the weather turns colder. Latest USDA forecasts suggest a strong rebound in US production next year but this is based on PEDv having much less impact than this year. If USDA is right, EU exporters will face more competition than they have this year. However, if not, US supplies could remain tight and, leaving EU exporters still in a good position.

Global demand will also depend on how PEDv develops in other markets, such as Mexico, Japan and Korea. It is likely there will be less import demand from these countries than this year but how much less is uncertain. However, this could be offset by increased Chinese imports, as production there is expected to be constrained following a reduction in the pig herd earlier this year. Recent announcements that several Chinese companies have been approved to export to Russia may add to its need to draw in additional imports.

Overall, it is quite likely that global export demand will be lower next year, while exportable supplies could be higher if PEDv has less impact. This could make the challenging conditions on the EU market even more difficult. All in all, any optimism which EU pig producers had a year ago is likely to have dissipated and it would be no surprise to see a resumption of the downward trend in the breeding herd.