

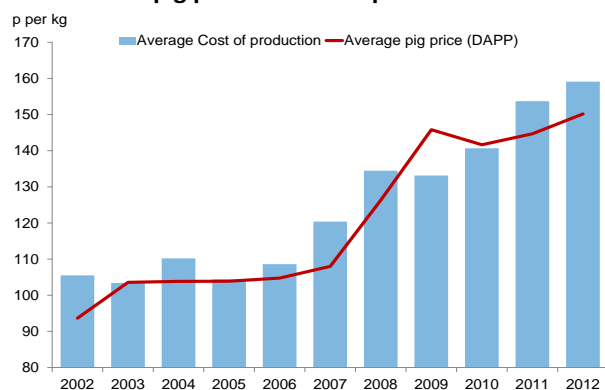
Pig Production Costs & Prices Report

October 2013

Pig producer margins

Each month AHDB/BPEX estimates the cost of pig production during that month, based on spot prices for feed and other input costs. This allows the net margin during the month to be calculated, comparing the cost of inputs utilised during the month with the income received from the pigs sold in that month. More detail on the calculation and how it should be interpreted, along with the latest data, can be found by [clicking here](#).

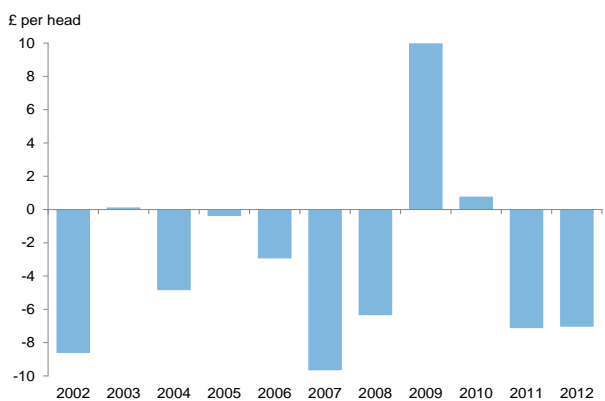
Total cost of pig production compared with the DAPP



Source: AHDB Market Intelligence

These calculations have been carried out annually using a consistent methodology since 2002. An explanation of the method can be found by [clicking here](#). Comparing production costs with the average price paid for pigs shows that producers have, on average, been losing money for eight out of the eleven years since then. Only in one year, 2009, did producers make a significant profit. Furthermore, even prior to 2002, producers had already been through a number of years of negative returns, which led to a sharp fall in the size of the UK pig herd. Not since the mid-1990s have producers been able to make money for a sustained period.

Average producer margin per pig sold

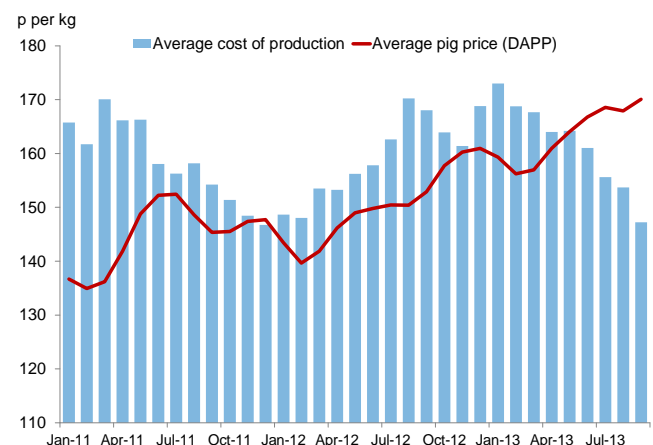


Source: AHDB Market Intelligence

Cumulative industry losses between 2002 and 2012 amounted to over £300 million. As a result, during the period the UK pig herd declined by 20 per cent, having already fallen significantly over the previous four years.

More recently, a number of feed price spikes have led to rises in production costs which have generally been larger than any corresponding rises in pig prices. Having been relatively low in 2009 and early 2010, feed prices increased rapidly in late 2010 and, while they have eased back at times, they have remained at a high level by historic standards ever since.

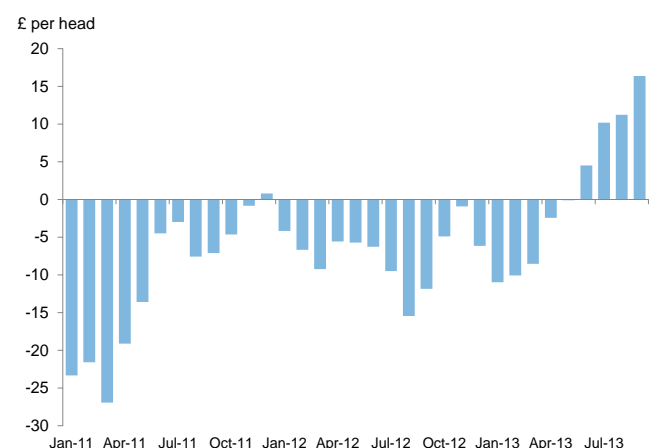
Total cost of pig production compared with the DAPP



Source: AHDB Market Intelligence

As a result, production costs moved back above pig prices in the final quarter of 2010 and by May 2013, producer margins had been negative for 31 out of the last 32 months. By May, producers' cumulative losses since late 2010 amounted to over £184 million, an average loss of over £8 for every pig sold during the period.

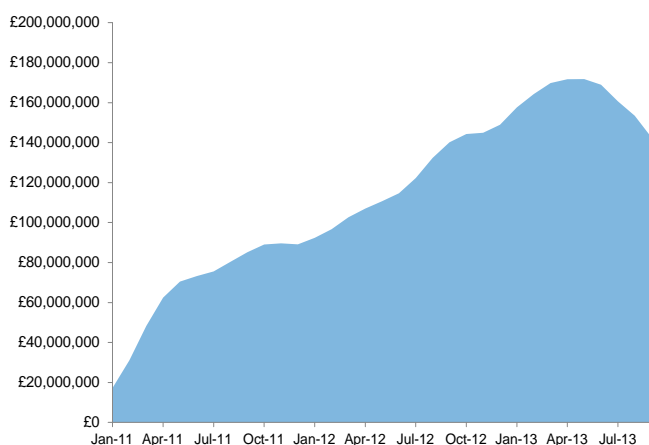
Average producer margin per pig sold



Source: AHDB Market Intelligence

Since June, producers have, on average, returned to a profitable situation. While this has allowed them to start recouping some of the losses made in the preceding three years, cumulative industry losses since the start of 2011 still amount to over £140 million.

Cumulative pig producer losses since start of 2011



Source: AHDB Market Intelligence

Lifetime production costs

Based on the production cost calculations presented above, producers returned to profit in June 2013 as feed prices eased in anticipation of a much improved Northern Hemisphere harvest this year. However, while this reflects the operating position of many producers during the month, it is not the whole story. In reality, it will be some time before producers return to a more comfortable position, never mind making significant progress towards recovering the losses experienced in recent years.

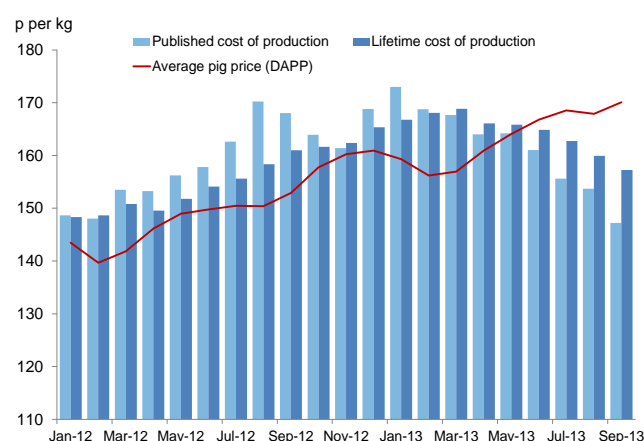
One of the main reasons for this is that the published cost of production estimates do not reflect the cost of producing the pigs which are sold in the month. Pigs sold in any given month will typically have been born around five to six months earlier. Their mother will have been served just under four months before that. Therefore, the cost of producing each pig will depend on feed prices during most of the preceding year, not just in the month when they were sold.

Precise estimates of the cost of producing pigs sold in a given month are not available. However, adjusting the feed component to take account of the variation in spot

prices during the life cycle of the pig gives the estimates in the table below for recent months.

On the basis of these revised calculations, producers are, on average, now getting a higher price for their pigs than they cost to produce. However, the margins are much smaller than indicated by the monthly cost of production estimate. Therefore, any significant fall in the pig price would mean that producers would again be selling pigs at a loss. It is worth remembering that until autumn 2012, the average finished pig price had never been above 156p per kg. A return to that level would mean that producers were still selling pigs at a loss.

Total cost of pig production compared with the DAPP



Source: AHDB Market Intelligence

Based on forward quotes for pig feed, lifetime production costs are not likely to reach the level of the current published cost of production until around March 2014. This assumes that feed prices remain close to the level they had reached recently. However, it is worth noting that in the last two weeks, global and UK wheat prices have started to increase, which could lead to production costs starting to rise again.

Relationship with pig prices

Although pig prices have generally been on an upward trend since the start of 2012, it would be incorrect to think that this was primarily due to the rise in production costs. Pig prices, like most market prices, are largely a function of supply and demand. To some extent, expectations about future levels of supply may

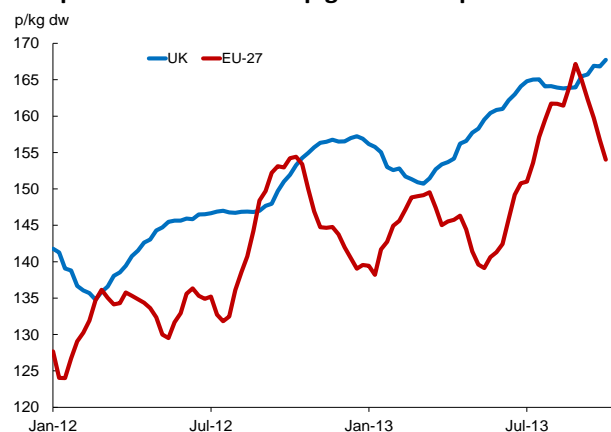
Month	Published cost of production (p/kg)	Published net margin (£/pig)	Lifecycle cost of production (p/kg)	Difference (p/kg)	Lifecycle net margin (£/pig)
May 2013	164.2	-0.11	165.9	+1.7	-1.41
June 2013	161.0	+4.53	164.8	+3.8	+1.54
July 2013	155.6	+10.19	162.7	+7.1	+4.59
August 2013	153.7	+11.23	159.9	+6.2	+6.32
September 2013	147.2	+16.40	157.3	+10.0	+8.49

Source: AHDB Market Intelligence

contribute to pricing levels but, given that pork is a perishable product, the effect of this on prices is likely to be limited.

UK finished pig supplies in 2012 were generally slightly more plentiful than in 2011. This suggests that higher prices were largely due to increased demand for British pigs. In turn, this can probably be mainly attributed to higher EU prices, reducing competition from lower-priced imported pork to some extent. This was particularly apparent in the second half of 2012, when UK pig prices bucked the usual seasonal trend by increasing steadily, following similar rises on the continent.

Comparison of UK and EU pig reference price



Source: AHDB Market Intelligence, EU Commission

EU prices have remained relatively firm throughout most of 2013 and have played a part in UK prices remaining high. Exchange rates have also contributed, with the pound weaker against the euro, increasing import prices in sterling terms. However, another significant factor in pricing has been an increased retailer preference for UK pig meat. This comes as they seek shorter and more transparent supply chains in the wake of the horse meat revelations earlier in the year.

During 2013, supplies have also been relatively tight, with finished pig numbers close to their level in 2012. In part, this is the result of the high production costs in 2012, which led to a reduction in the breeding herd as some producers chose to leave the industry. This demonstrates that production costs can have an indirect (and delayed) impact on pig prices. However, there is no reason why the fall in production costs in recent months will automatically lead to lower pig prices as the supply-demand balance has not changed. Prices may come down in the longer-term if the more favourable financial position leads to some expansion of pig production.

The increased demand for British pork is apparent from the latest results of BPEX's [Porkwatch](#) survey. These show notable increases in the British share of fresh pork facings in some supermarkets, with several now at or

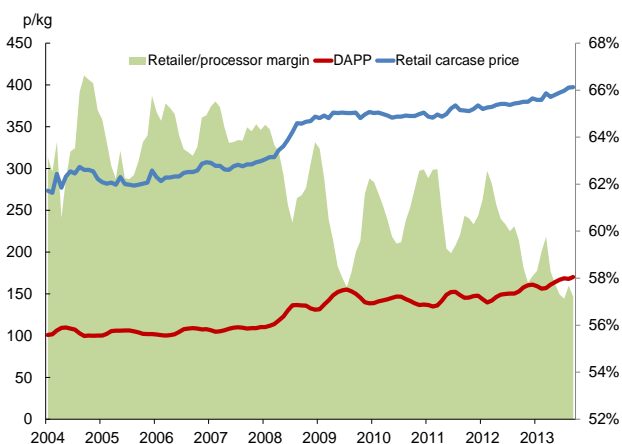
close to 100% British. The stable supply situation does mean that, as a result, some other retailers have been unable to source the same quantity of British pork, despite a stated desire to do so.

Supply chain margins

The volatility in both pig and feed prices in recent times presents challenges for all of the players in the supply chain. High raw material costs, for pigs or feed, are being met with consumer resistance to retail price increases as spending is still being impacted by the austere economic climate. In this climate, it has proved difficult to maintain sustainable margins for producers, processors and retailers.

Between September 2012 and September 2013, average pig prices increased by just under 20p per kg. Over the same period, retail pork prices increased by a similar amount (when averaged over the whole carcass). This means that producers are now receiving a higher proportion of the retail price; at around 43 per cent, their share is the highest since the mid-1990s. Despite this, pork producers' share remains well below that received by beef and lamb producers, who typically receive over half the retail price.

Comparison of pig and retail prices



Source: AHDB Market Intelligence

Over the longer-term, retail pork prices have increased as pig prices have risen. However, in recent years, retail inflation has been lower than for pig prices. As a result, margins in the supply chain have gradually been eroded. Over the last year, retailers and processors have received less than 60 per cent of the final retail price between them, down from around 65 per cent five years ago. Given that both processing and retailing involve significant additional costs, beyond the purchase of the pigs, this will have reduced profit margins even more significantly.