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China Plans to Purchase Pork for State Reserves

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Report Highlights:
On June 5, 2009, the National Development and Reform Commission announced the Government of China is preparing to purchase pork for frozen stocks under the National Swine Price Alert System. Significant pork purchases are considered likely in the near term to boost prices and returns for pork producers.

General Information:

NDRC Announces Preparations Underway for Pork Purchases

In response to a continued decline in pork prices, China's National Development and Reform Commission (NDRC) announced the government has launched preparations to purchase pork for frozen stocks to stabilize the market. Under the National Swine Price Alert System announced in January 2009 (see GAIN 9017), if the ratio of hog to grain prices falls below 6.0 for more than four weeks, the government will consider purchases for reserve stocks to reduce market supply and increase prices. On May 12, 2009, NDRC published a market alert announcing the live hog to grain price ratio had fallen below 6.0 and urged pork producers to reduce the marketing of hogs where possible, setting the stage for possible reserve purchases.

Chinese live hog prices in China have dropped for 20 straight weeks, as supply gains continue to outpace rising demand. NDRC reports on May 27, the nationwide average hog price in large and medium cities fell to 9.75 yuan per kilogram, down 3.75 percent from the previous month. Meanwhile, corn prices rose slightly during the same period to 1.66 yuan per kilogram. Pork producers are reportedly losing up to 100 yuan per head due to the continued price decline. With the continued slide in hog prices since the market alert announcement, significant purchases for government-held stocks are now considered likely in the near term to boost prices and returns for pork producers.

NRDC reports total live pig stocks at the end of April reached 454 million head, up 1.4 percent from the previous month. The number of sows stood at almost 50 million head, down 0.4 percent from March. According to NDRC, the proportion of sows to pigs in recent months has been the highest on record, suggesting further upward pressure on pork production.

Cold storage capacity for reserve stocks could be a significant limitation without government incentives to free up commercial space. An analyst with the Ministry of Agriculture confirmed the Government of China's warehouse space is likely insufficient, noting total frozen reserve capacity is roughly 600,000 MT. Therefore, commercial reserve space assisted with government subsidies will likely be key to ensuring sufficient capacity.

Overview of National Swine Price Alert System

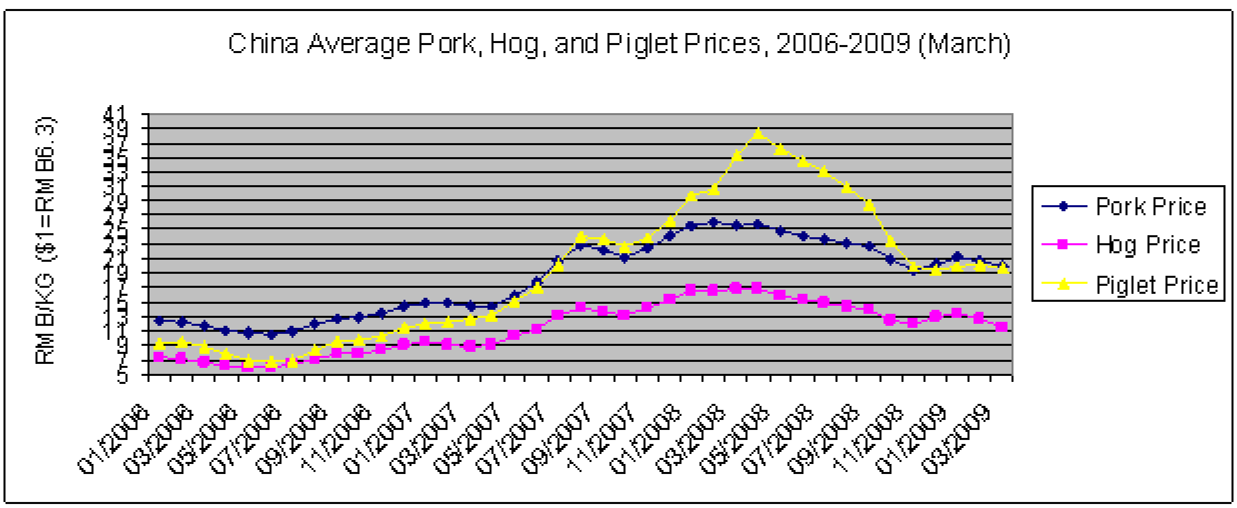
Under the National Swine Price Alert System, when the hog:grain price ratio falls below 6.0, the Chinese government shall announce a four-week market alert to encourage producers to reduce slaughter where possible. If the ratio remains below 6.0 for four consecutive weeks, the central and local governments shall increase frozen pork reserves. If the ratio drops further to below 5.5 for four weeks, the central government will further increase central reserves, and at the same time request main consumption areas in large-medium coastal cities to increase frozen reserves. When the hog:grain ratio drops below 5.0, the central government shall further increase purchases for reserves. If the hog:grain ratio remains below 5.0 following the increased purchases, the government directs producers to begin slaughtering significant numbers of sows until the sow inventory decreases considerably. For this stage, the Chinese government shall provide an additional one-time RMB100 ($14.6) for each productive sow for large swine producing counties that distribute hogs to other provinces, and also subsidize one-time RMB100 to each breeding boar at breeding farms identified by the Ministry of Agriculture (MOA). The government also shall encourage large-sized pork processing plants to increase commercial reserves with low-interest loans provided by the government, and increase production of processed products.

Although the four-week period following the market alert has not yet expired, some provinces have already started taking action. For example, in Sichuan Province, the largest swine producing province, the hog:grain ratio has reportedly been below 5:1 for more than four weeks. Sichuan authorities have requested large processing plants to help local government increase frozen reserves. Gaojin Foods Co., Ltd. reportedly purchased 22,000 MT in response to the request.

Subsidies for Productive Sows May Continue

A primary factor driving higher pork supplies is China's expanded subsidy regime for pork to encourage a recovery in production following a devastating outbreak of blue ear disease in 2006/07. The initial subsidy was 50 yuan ($7.30) per productive sow during the first yearly subsidy period which ended on June 30, 2008. The second yearly subsidy period is from July 1, 2008 to June 30, 2009. The second yearly subsidy is raised to 100 yuan ($14.60) per productive sow.

The subsidies have attracted large investment in swine raising. According to the China Animal Husbandry Association, swine raising investment in 2009 is double compared with that in 2007. Further adding to upward pressure on production is the return of millions of recently unemployed migrant workers who returned to rural China and began raising swine. This resulted in a quick increase in sow inventory and swine supplies, outpacing rising pork demand and resulting in higher supplies and lower hog prices. According to farmers, one fattened hog is losing RMB 100-200 ($14.6-29.2). However, the swine industry expects the productive sow subsidy program may continue from mid 2009 to mid 2010 to prevent a large slaughter of sows, short swine supplies and rising prices. A well-known swine farm contact told FAS Beijing (Post) that subsidy content may change to favor large-sized swine farms. Post believes that the productive sow insurance subsidy, which is RMB60 ($8.79) per productive sow with farmers only paying RMB12 ($1.76) will not change, but may also favor large-sized farms.



Source: Ministry of Agriculture