Federal Reserve Bank of Chicago - - Agricultural Letter

July 10, 1959

Number 516

The hog plays a key role in Corn Belt agriculture. In fact, its importance has been depicted in the title of "mortgage lifter." Yet hogs are not "just hogs" when they come to market and when their products show up on the dinner table. Instead, hogs are a composite of many different products, each with unique characteristics and value in the eyes of consumers.

As consumers have made changes in their diets over the years—away from fats toward lean meats—the value of the final products from the hog has similarly changed with lard declining and lean cuts increasing. The hog buyer for a packing firm has reflected this change in the price he pays. However, the question arises whether the price differential for the so-called meat-type hog is adequately reflected to hog producers and, in turn, provides the incentive to breed and raise hogs which provide the more desired products when slaughtered.

In present methods of marketing hogs, according to a University of Minnesota study, "commission salesmen and packer buyers interviewed believed that farmers are generally receiving $0.75-$1.00 per hundred premium for meat-type hogs and are docked about $0.50-$0.75 per hundred for overly fat hogs. If farmers do receive these premiums or discounts, it is doubtful whether they realize it since only the average price for the lot is reported to them." Further, most live grading was only an evaluation of the lot and even when hogs were live graded, no firm interviewed reported the grade to the farmer on his settlement statement. A study by the U. S. Department of Agriculture in Ohio indicates the premium paid for meat-type hogs does not adequately reflect the differential in the cut out value.

"The challenge to hog processors and marketers is to develop a means of recognizing and paying a premium for meat-type hogs," state the economists at the University of Minnesota, and they present three alternatives for the livestock industry:

1. Establish self-imposed grading standards and pay premiums for meat-type hogs.

2. Expand specification buying or vertical integration.

3. Establish compulsory Government grades for use in marketing hogs.

In any grading system many difficulties must be overcome in order to be truly effective. The live grading of animals is still more of an art than a science. Special devices such as the back fat probe and the use of high frequency sound waves have been developed to help improve the accuracy of live grading, but no technique has been developed yet which is completely satisfactory.

However, even with improvements in live grading and the development of USDA marketing reports for hogs by grades, if grading is not used, not understood and not directly related to each hog marketed, the price signal which is supposed to reach the hog producer about meat-type hogs is relatively ineffective.

When the pricing system fails to perform its proper function, other techniques begin to be used. Development of contracting and vertical integration in the production of hogs can, in part, be traced to the desire of retail food chains for steady supplies of lean pork to satisfy desires of their customers. Others who have begun contracting for meat-type hogs apparently rely on their ability to command premium prices for meats produced from these animals.

Grading of both animals and meat cuts has traditionally been a voluntary program in this country. The exception to this was compulsory grading during the war for price control purposes. Canada, on the other hand, has a compulsory grading of hog carcasses "on the rail." It is significant, perhaps, that Canada has gone much further than the United States in developing and producing meat-type hogs adapted to a special market.

A properly developed grading system, with consumer desires translated into price differentials for types of meat and types of meat animals most desired, will benefit both consumers and producers. Consumers would have ample supplies of the quality of meats they want, and farmers would be rewarded for producing these products. Indeed, if the price-grading system were functioning in a satisfactory manner, one of the important inducements for contracting for production of hogs in the Corn Belt would be eliminated.

With large feed supplies and expanding hog production, the swine industry faces a real test of its ability to provide the quality of product desired by consumers, thereby minimizing the price decline. If, due to inadequacies of the marketing mechanism, large quantities of undesirable pork products are produced, hog prices will have to take an abnormally large decline in order to move these products through the markets.

Research Department