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USDA/DOJ Public Workshops on Competition in Agriculture
Comments by Gilles Stockton

Dear Sir;

I suspect that many of the comments received outline the regulatory and antitrust actions that the Departments of Justice and Agriculture should pursue. So, in that respect there is probably nothing new that I can contribute. I will instead explore why it is important that competition in agricultural markets be protected and enhanced.

There are two competing visions as to how U.S. production agriculture should be structured. The vision that has been in the ascendency for the past half century is one that claims, for reasons of efficiency, that agricultural markets should be dominated by a small number of large corporations. Individual farms, under this centralized corporate vision, should be vertically aligned with one of these controlling corporations and the only market that matters is at the retail level. The alternative vision is that the U.S. food system should be diverse and de-centralized. Farms, under this vision, would market their produce in competitive markets and each commercial entity in the chain, from farm to plate, should be responsive to competitive market forces.

If you, as the reader of this comment, and presumably a decision maker for regulatory and anti-trust actions, are not open to the de-centralized vision of agricultural production, than there really is no point to this exercise. Admittedly, it is difficult to ascribe to the de-centralized model because so little of the current structure of U.S. agriculture meets that criteria. Since the end of World War II, a period which incidentally encompasses my lifetime, U.S. agriculture transitioned from one where multitudes of family farms sold into competitive regional markets to one controlled by a small number of globally dominate corporations.

Adherents of the neo-liberal economic ideology applauded this transition at every stage of its de-evolution. Under the centralized corporate vision system, all consolidations in agricultural markets have been rational because the dominate firms are presumed to be exploiting economies of scale. The proof that this is true is that the retail consumer pays less for food. Changes in the structure of agriculture and the disappearance of competitive markets at the production level were never a concern. In the neo-liberal dogma, - because it happened means that it should have happened, because the invisible hand of the market always results in the proper outcome.

However, the transition from de-centralized agriculture to one controlled by what has been described as a chain oligopoly/oligopsony did not happen without considerable influence seeking on the part of the multi-national corporations in question, coupled by active neglect and connivance on the part of Congress, government regulators, and federal judges. As a reluctant participant of this de-evolution, I can attest to the unremitting propaganda. "Get bigger or get out" was the very clear message to all family farmers. In the neo-liberal propaganda story line, corporate control of agriculture is modern and efficient while family farmers are part of folklore. Old MacDonald may have had a cow, pig, horse, and chickens and was a grandfatherly friendly guy but he was not up to the rigors of the market and the science of modern agriculture.

The Future and Climate Change

But conditions are changing and you, as reader and as a consumer of food, must ask yourself if you want to continue to put your future in the hands of a small number of multi-national corporations. Past US farm policy was predicated on the fact that farmers were growing more food than the market could absorb. The various iterations of the farm bill kept food cheap but provided enough production controls and subsidies to prevent the rural economy from going into free fall.

That was the past. The United States is now a net importer of food. Worldwide demand by an ever increasing human population is not being matched by increases in land under cultivation or increases in crop yields. In addition, changes in the world's climate are already negatively affecting agricultural production. It is certain that the future will not have the same food security as did the past. So, we need to ask ourselves whether society will be properly served by an agricultural system controlled by a few dominate firms because one thing is for certain - multi-national agribusiness corporations will exploit food scarcities to their utmost benefit.

If the negative perception of family based agriculture was ever true we would not have an alternative structure to consider. The facts are, as measured by USDA itself, that agricultural efficiency in terms of both yields per acre and return on investment is the same over a large range of farm sizes with the largest farms tending to be least efficient. Throughout the 20th Century and well before horizontal and vertical integration dominated agricultural markets, agriculture had the largest productivity increases of all of the major U.S. industries. Farmers do not need to be coerced by vertical integration to adopt new technologies.

Farm size has increased because farm policy, banking policy, taxation policy, and anti-trust policy encouraged this transition. But the transition did not happen easily because farmers have historically been willing to exploit themselves in order to keep their land and independence. This country now has fewer than one million full time farmers, too few for the Census Bureau to bother counting. The absurdity is that most of these one million farmers own assets worth more than a million dollars, yet many still need to subsidize their farms with off farm employment. When I took over the ranch from my father in 1975, the farmer's share was around 33 cents. Today the farmer's share of the food dollar is down to 20 cents. The implication is clear. Food is cheap for the consumer, not because of efficiencies on the part of the controlling agri-business corporations, but because these corporations are able to keep the costs of the raw materials cheap by forcing farmers to exploit their own labor, mine their equity, and abuse their soil.

The big danger in this centralized agricultural system is that the decisions of what is to be planted are up to a board of directors with no particular interest in the problems that might result to the farmers or society. Their main interest is procuring food's raw materials from farmers at the cheapest price possible and selling the finished product to consumers at the highest price they can manage. Farmers have little say in the matter because they must accept the prices and production contracts offered or they will not get the financing needed to put the next crop in the ground. This is a system that forces specialization and the planting of mono-cultures over vast territories. Precisely the opposite of what we need in a climatic situation that is changing in unpredictable ways. The food consumer of the future would be better served by an agricultural system where the decision maker is knowledgeable about local conditions and flexible enough to experiment with alternative crops and farming systems.

Electronic Markets

Now that just a few firms control the marketing systems for all major food crops it is not necessarily easy to re-impose competition. However, over the last 25 years the development of the worldwide web provides a technological methodology that could be transformative to agricultural markets. Internet based auction and market exchange have the potential of being very inexpensive and efficient price discovery systems for agriculture. One of the beauties of a blind bid market is that it is size neutral. Government regulators and the political system do not have to make a judgment whether a particular size or technology represents the best economies of scale. If the marketplace is truly competitive and the bidding system is blind - small farms, small firms, and small retailers can participate on an equal footing with larger counterparts. The market will, in this case, decide what are appropriate economies of scale and technological innovations.

Unfortunately, you, as an anti-trust regulator, do not have the authority to impose open competitive web based market systems on the agriculture industry – except in one case. The Packers and Stockyards Act (P&SA) states that:

> It shall be unlawful for any packer or swine contractor …or for any live poultry dealer:
>
> - Engage in or use any unfair, unjustly discriminatory, or deceptive practice
> - Make or give any undue or unreasonable preference or advantage …or unreasonable prejudice
> - Sell … or buy … for the purpose or effect of manipulating or controlling prices, or of creating a monopoly

- Engage in any business… for the purpose or with the effect of manipulating or controlling prices.

USDA will soon be publishing proposed rules as to what constitutes *undue preference* under the Packers and Stockyards Act. Presumably this will consist of a long list of practices that the monopoly packers cannot do. However, to my mind, what is more important is what they **can** do that does not constitute undue preference. Packers can bid for live cattle and for forward contacts for the delivery of cattle in an open competitive market. Understandably, they are reluctant to do so because packers prefer the vertically integrated model pioneered by the poultry industry.

Cattle Ranching

The cow-calf segment of the cattle industry has a number of unique aspects not shared by the rest of agriculture. To begin with it utilizes the "left over" land – the land not otherwise suitable for tillage. In the plains adjacent to the Rocky Mountains this gives cow-calf production an extensive rather than intensive character. Cow-calf production can be said to be the only environmentally sustainable aspect of mainstream agriculture. Those involved in organic and natural farming are finding sustainable technologies for what is still a niche aspect of agriculture, but cow-calf operators have been sustainably raising cows, nurturing the growth of range grasses, and protecting watersheds for the better part of the 20th century.

The extensive nature of cow-calf production makes it resistant to the forces that would vertically integrate it as in the case of poultry, hogs, dairy, or cattle feeding. One cannot economically raise beef cows in a "factory farm." The packers probably do not want to assume the high capital costs of owning and operating their own cow-calf system. In that respect they would just as soon have independent ranchers foolish enough to supply them will feeder calves – as long as the ranchers are not too independent.

Another aspect that makes cow-calf ranchers unique is the reliance on auctions for the marketing of the feeder calves and cull cows. Grain farmers were never that tied to a public competitive market because the floor price and loan rates imposed by the government programs determined the prices received. Produce farmers often market through production contracts, not auction markets. Poultry and hog producers are, of course, now vertically integrated and don't have access to any kind of public price discovery system. Only cow-calf producers continue to sell through public organized markets. Besides the physical auction barns that sell for immediate delivery and payment, many feeder calves are sold through satellite/internet video auction markets where contracts for the future delivery are negotiated through a virtual auction.

The problem cow-calf producers face is that the prices we receive are less and less competitively derived. Three packers effectively control the market. The feedlots from which packers procure fat cattle are, for the most part, vertically aligned with one of the three packers. The packers, in turn, sell to a retail grocery system almost as concentrated as they are themselves. Everyone, therefore, calculates from the retail price for beef, adds their margins and profits, and what is left is what is offered for the feeder calves. However, because of the Illinois Brick Decision, cow-calf ranchers do not have standing to complain on an anti-trust basis because theoretically, feedlot operators sit between cow-calf ranchers and the beef packers.

Captive Supplies

Cow-calf ranchers have focused on “captive supply” as the major problem to be fixed in the cattle market. The term “captive supply” encompasses a number of procurement practices but the practical result is that they all amount to formal and informal vertical integration on the part of the feedlots supplying the packers. In 1999 USDA released the “Economic Analysis of Fed Cattle Procurement in the Texas Panhandle” study which found that for each 8.8% increase in “captive supply” there was a $0.69 decrease per hundred weight (cwt) in prices. In a famous admission during one legal complaint brought by cattle producers, the CEO of IBP (the dominant packer at the time – since sold to Tyson) admitted that during some weeks his company had up to 118% of cattle committed through one form of “captive supply” or another.

Clearly “captive supply” harms the market for the feeder calves I sell. Sixty nine cents per cwt may not sound like much, but if one calculates the situation where “captive supplies” are at 88 percent, a 1,250 pound steer at slaughter will have been priced $86.25 less than it should have under a competitive market situation. Historically feedlot operators were generally happy with a $86 profit per head. Selling at a net loss can’t go on for too many years before the independent feedlot owners see that there is little in the business of feeding cattle that benefits them and they either close their feedlot or start feeding exclusively for one packer. Of course, during the process, feedlot operators are very careful about what they are willing to pay me for feeder calves.

The Texas Procurement Study (as it was called) clearly showed harm to the industry but nothing was ever done about it. The harm it showed was in the narrow range of prices in which cattle were selling. The study, however, did not determine whether that selling range was lower than it should have been if the cattle market was not so non-competitive.

In 2003 we had a test of that phenomenon when cattle from Canada were banned from entering the United States because of Mad Cow Disease (Bovine Spongiform Encephalopathy). Once the import ban was imposed there was an immediate 27% jump in fat cattle prices (from $67 to $85 cwt). The standard assumption on the part of livestock economists is that for every 1% increase or decrease in cattle supply, the market will move 1.5 to 2%. Since the Canadian cattle amounted to around 3% of the supply, we expected prices to increase by around 6%. So how can we account for the other 21% increase other than the overall effect of captive supplies on the market—given that all of the Canadian cattle were “captive.” For once something happened in the market that benefited me. What looks to have happened is that with the sudden loss of Canadian captive supply, the packers temporarily lost control of the market. Six years later they have recovered control and cattle prices are again down by 25 to 30%.

Last year we experienced what happens when banks get “too big to fail”. One lesson is that apparently they also become “too big to regulate” because they own the government. It is pretty clear that beef packers have been “owning” their part of the government for the last three decades. The question before us is when will this stop? The tools are clearly in place to restore competition to the cattle markets and it will not require a big, complicated anti-trust case designed to break them up. USDA is already working on proposed rules to define undue preference under the Packers and Stockyards Act. I hope that these proposed rules are comprehensive. All that will be needed in addition is adoption of the petition for rulemaking submitted by the Western Organization of Resource Councils in 1996. This petition is still pending a ruling by the Secretary of Agriculture and basically would require that packers competitively bid for cattle supplies in a public open and competitive electronic market. The WORC rule would amend the Packers and Stockyards Act to:

1) prohibit packers from procuring cattle for slaughter through the use of a forward contract, unless the contract contains a firm base price that can be equated to a fixed dollar amount on the day the contract is signed and the forward contract is offered or bid in an open, public manner and;
2) prohibit packers from owning and feeding cattle, unless the cattle are sold for slaughter in an open, public market.

The beauty of these two proposed rules to amend the Packers and Stockyards Act is that they are purely competition enhancing measures and clarify an already existing law.

Sincerely yours,

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