

From: Bill Bullard [mailto:billbullard@r-calfusa.com]
Sent: Thursday, December 31, 2009 11:11 PM
To: ATR-Agricultural Workshops
Cc: Ferrell, John; Dudley Butler
Subject: R-CALF USA Comments to the Dept. of Justice

Attached please find R-CALF USA's comments to the Department of Justice regarding Agriculture and Antitrust Enforcement Issues in Our 21st Century Economy. Thank you.

Bill Bullard

From: Bill Bullard [mailto:billbullard@r-calfusa.com]
Sent: Monday, January 04, 2010 11:12 AM
To: ATR-Agricultural Workshops
Subject: Word version of R-CALF USA Comments

Hello Mr. Tobey,

I left you a voice message regarding our submission of our comments on the DOJ/USDA workshops in pdf format. Attached is the Word version of the same comments we filed. Please let me know if there is any problem regarding our submission. Thank you.

Bill Bullard
406-252-2516

Fighting for the U.S. Cattle Producer!



R-CALF
USA

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December 31, 2009

Legal Policy Section
Antitrust Division
U.S. Department of Justice
450 5th Street, NW., Suite 11700
Washington, D.C. 20001

Sent Via Electronic Mail: agriculturalworkshops@usdoj.gov

Re: R-CALF USA Comments on Agriculture and Antitrust Enforcement Issues in Our 21st Century Economy

Dear Sirs and Madams:

The Ranchers-Cattlemen Action Legal Fund, United Stockgrowers of America (R-CALF USA) appreciates this opportunity to submit comments to the U.S. Department of Justice, Antitrust Division (the Justice Department) and the U.S. Department of Agriculture (USDA) regarding the agencies' joint notice of public hearing and opportunity to comment on *Agriculture and Antitrust Enforcement Issues in Our 21st Century* published at 74 Fed. Reg. 43725, 726 (Aug. 27, 2009).

R-CALF USA is a national nonprofit association that represents thousands of U.S. cattle farmers and ranchers in 46 states. R-CALF USA works to sustain the profitability and viability of the U.S. cattle industry, a vital component of U.S. agriculture. R-CALF USA's membership consists primarily of cow/calf producers, cattle backgrounders and feedlot owners. Various main-street businesses are associate members of R-CALF USA.

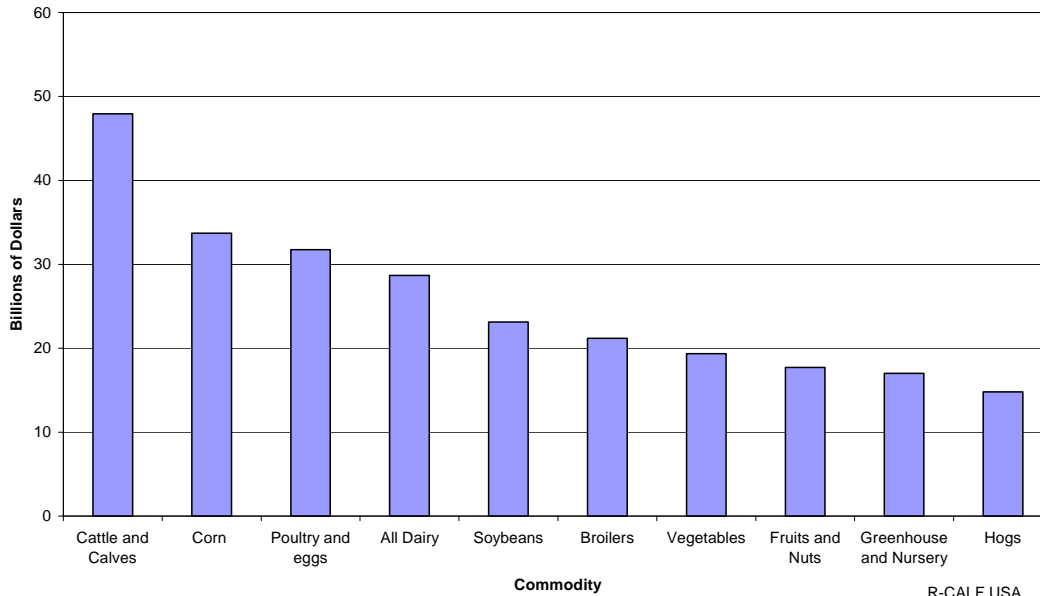
What likely is obvious to the Justice Department and USDA is that the U.S. cattle industry of the 21st Century has undergone profound changes, which began in the latter part of the 20th Century and affected three key industry characteristics: industry structure, industry participants and industry productivity. What may be less obvious are the indices of systemic market failure now manifest in the U.S. cattle industry of the 21st Century and the factors that contributed, and which continue to contribute, to that manifestation.

In these comments, R-CALF USA will describe: 1) the current state of the U.S. cattle industry: its current structure, participants and productivity; 2) the unique vulnerabilities of the U.S. cattle industry that make it particularly susceptible to monopsony power and exploitation; 3) examples of market failure that evince the exercise of monopsony power and exploitation; 4) examples of known and suspected practices within the industry that constitute anticompetitive behavior and/or violations of antitrust statutes; and, 5) recommendations on what action is needed to revitalize the ailing U.S. cattle industry.

I. THE CURRENT STATE OF THE U.S. CATTLE INDUSTRY

Cattle farming and ranching is perhaps the most common and recognizable economic engine throughout all of Rural America. The cattle industry historically is the single largest segment of American agriculture, towering over all other agricultural commodities by contributing nearly \$50 billion in new wealth each year to the U.S. economy (chart 1).

CHART 1: TOP 10 U.S. AGRICULTURE COMMODITIES
(Based on Five-Year Average)



This massive economic engine – the U.S. cattle industry – makes substantial financial contributions in every state of the Union, generating in 2008 approximately \$37 billion in cash receipts in the top 12 cattle-producing states and approximately \$12 billion in the remaining 38 states.¹

This industry can and should, however, be making a much greater and much more widely distributed contribution to the U.S. economy. But for decades, the U.S. cattle industry has been severely neglected by Congress and federal regulators that refused to update livestock-related statutes concerning competitive markets and refused to enforce antitrust laws and laws established to protect cattle farmers and ranchers from the anticompetitive practices of the dominant meatpackers, particularly through the Packers and Stockyards Act. As a result, the viability of the U.S. cattle industry has been severely marginalized.

Unrestrained by a lack of enforcement of antitrust laws and emboldened by the government’s disinterest in prohibiting anticompetitive practices, the dominant beef packers and dominant

¹ See Farm Income: Cash Receipts, States’ Ranking for Cash Receipts, Data Sets, U.S. Department of Agriculture (hereafter “USDA”) Economic Research Service (hereafter “ERS”), 2008, available at <http://www.ers.usda.gov/Data/FarmIncome/firkdmuxls.htm#group>

feedlot companies, which today are often indistinguishable,² have radically changed the structure of the U.S. cattle industry.

A. The Current Structure of the U.S. Cattle Industry

1. Market Concentration in the Final Cattle Market

The purpose of the \$50 billion U.S. cattle industry is to raise cattle for slaughter and subsequent fabrication into consumable beef. The beef packing industry slaughters live cattle and terminates the life cycle of individual cattle. The *final cattle market* is the market where cattle are sold to the beef packer for slaughter and consists predominantly of fed cattle (i.e., steers and heifers that are raised and fed specifically for beef production), but also includes cows and bulls that are purchased by beef packers for slaughter after they have exceeded their useful breeding lives, which may occur months or years after birth. This final cattle market for U.S. cattle farmers and ranchers also is the *buyer-side* of the beef packers' market.

The current structure of the U.S. cattle industry is characterized by unprecedented concentration in the beef packing sector.³ This unprecedented concentration did not happen overnight – it has been acutely chronic for decades and is now fully manifest in both the buyer-side (i.e., the final cattle market) and seller-side (i.e., the initial beef market) of the beef packers' market. On the buyer-side of the beef packers' market, the beef packer purchases for slaughter live steers and heifers and cows and bulls from farmers and ranchers. Latest available data suggest the four-firm concentration for firms that slaughter steers and heifers is over 85 percent (chart 2);⁴ for firms that slaughter cows and bulls, over 50 percent (chart 3).⁵

² See, e.g., Recent Acquisitions of U.S. Meat Companies, Congressional Research Service, 7-5700, RS22980, March 10, 2009, at 2 (“The proposed JBS acquisition of Five Rivers Ranch Cattle Feeding, which was part of the Smithfield deal, also took place, making JBS the largest cattle feeder in the United States.”); see also *id.*, Table 1 (Cargill Cattle Feeders, LLC, was ranked as the third largest cattle feeding company in 2006, marketing approx. 6 percent of the nation’s fed cattle). Based on information and belief, Cactus Feeders, Inc., and Friona Industries, LP, which also are listed in Table 1 as among the largest cattle feeding companies, are considered captive feedlots and predominantly market their cattle to only one meatpacker.

³ See A Review of Causes for and Consequences of Economic Concentration in the U.S. Meatpacking Industry, Clement E. Ward, Current Agriculture Food and Resource Issues, 2001, at 1 (“Concentration levels are among the highest of any industry in the United States, and well above levels generally considered to elicit non-competitive behavior and result in adverse economic performance. . .”).

⁴ See United States of America, et al. v JBS S.A. et al., Complaint, U.S. District Court, Northern District of Illinois Eastern Division, Civil Action No. 08-CV-5992 (The U.S. Dept. of Justice alleged that the top four meatpackers purchased “over 85% - nearly 24 million” of the 27 million fed cattle purchased in 2007.); see also Packers and Stockyards Statistical Report, 2006 Reporting Year, Table 27, USDA Grain Inspection, Packers and Stockyards Administration (hereafter “GIPSA”), GIPSA SR-08-1, May 2008, at 44 (As depicted in Chart 2, GIPSA reported that there were 92 firms in 2006 that controlled 95.6 percent of the total commercial slaughter of steers and heifers.).

⁵ See Packers and Stockyards Statistical Report, 2006 Reporting Year, Table 28, USDA, GIPSA, GIPSA SR-08-1, May 2008, at 45 (As depicted in Chart 3, GIPSA reported that 97 firms in 2006 controlled 93.8 percent of the total commercial slaughter of cows and bulls.).

CHART 2: Decreased Number of Firms that Slaughter Steers and Heifers and Increased Four-Firm Concentration (1980-2006)

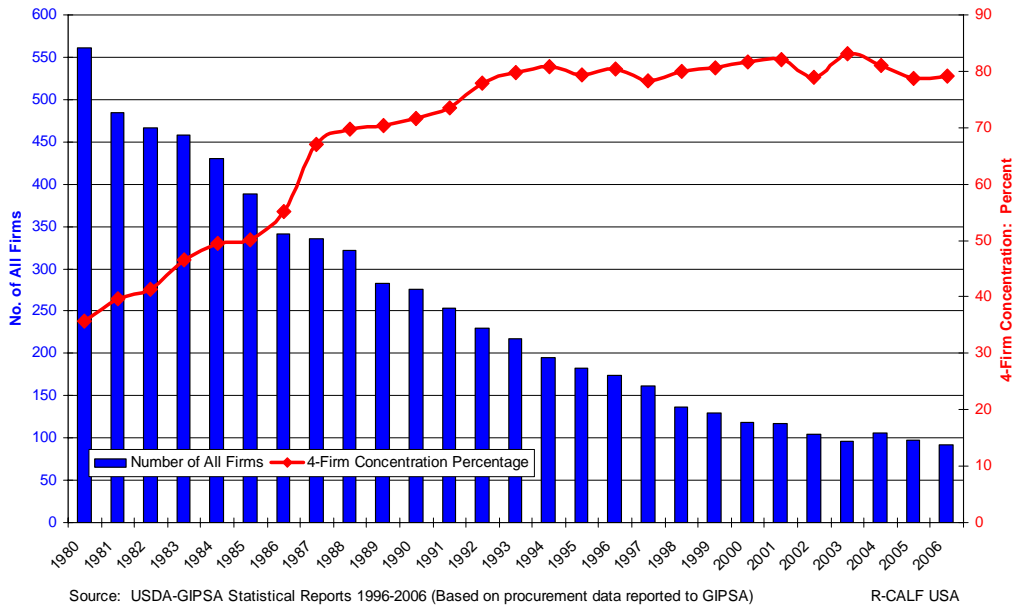
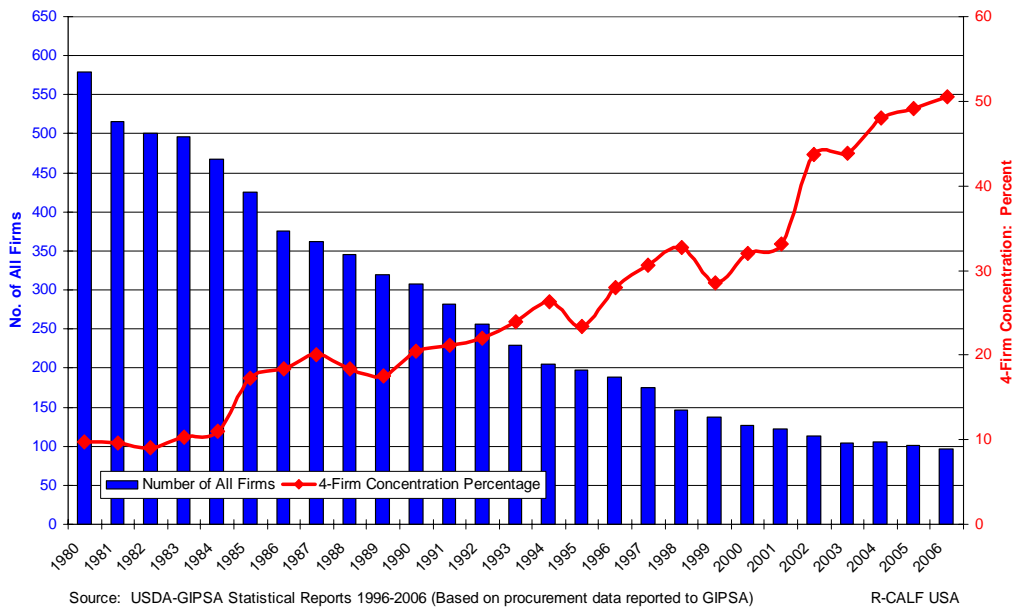


CHART 3: Decreased Number of Firms that Slaughter Cows and Bulls and Increased Four-Firm Concentration (1980-2006)



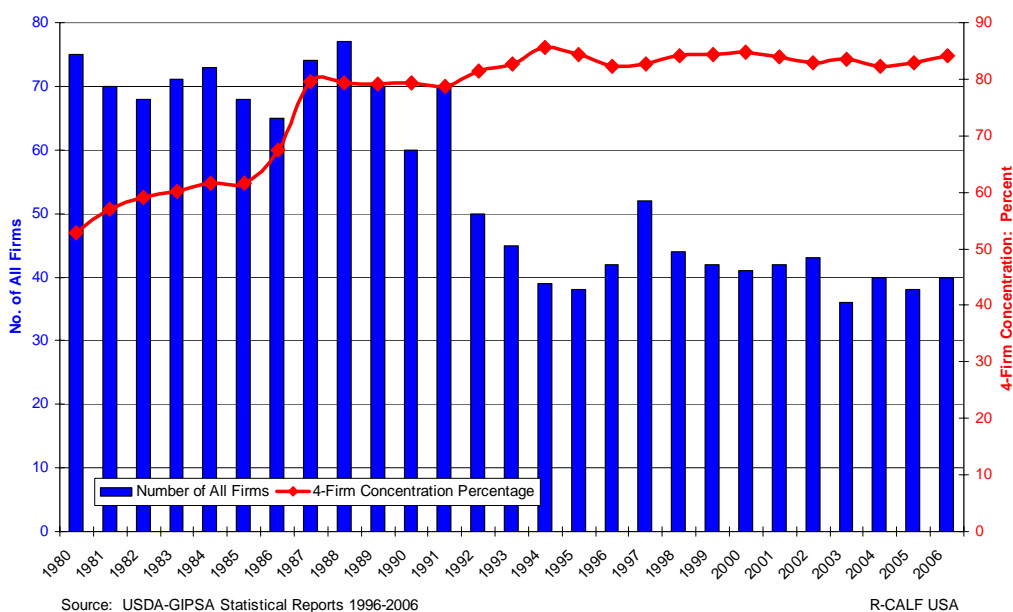
2. Market Concentration in the Initial Beef Market

Following slaughter by the beef packing industry, beef derived from all cattle (i.e., steers, heifers, cows and bulls) is subsequently marketed to additional processors, wholesalers, retailers,

or directly to consumers. This market, from the beef packer to any one of the beef packers' customers, is considered the initial beef market and is the *seller-side* of the beef packers' market.

The unprecedented concentration achieved by dominant beef packers in the buyer-side of their market (i.e., the final cattle market) is mirrored, indeed exacerbated, by the concentration level achieved in the seller-side (or wholesale/retail-side) of their market. By 2006, the top 20 beef packing firms controlled 99.9 percent of all boxed beef production, with just four firms controlling over 84 percent of the nation's boxed beef sold to wholesale and/or retail consumers (representing the control of nearly 22 million of the 26 million head of fed cattle fabricated into boxed beef) (chart 4).⁶ Based on an extrapolation of data compiled by the Justice Department, the current concentration in the U.S. boxed beef market would register approximately 2,000 points using the Herfindahl-Hirschman Index (HHI),⁷ which is well above the highest spectrum of market concentration recognized by the Justice Department and would be characterized as "highly concentrated (HHI above 1800)."⁸

CHART 4: Decreased Number of Firms that Produce Boxed Beef and Increased Four-Firm Concentration (1980-2006)



3. Market Concentration in the Final Feeder Cattle Market

One step upstream from the final cattle market is the *final feeder cattle market*. Feeder cattle are steers and heifers that have been weaned by the farmer or rancher who raised them (i.e., the person whom calved them out (birthed) and reared them until weaning) and typically reared on

⁶ See Packers and Stockyards Statistical Report, Table 33, USDA, GIPSA, GIPSA SR-08-1, May 2008, at 50.

⁷ See United States of America, et al. v JBS S.A. et al., Amended Complaint, U.S. District Court, Northern District of Illinois Eastern Division, Civil Action No. 08-CV-5992 (The Justice Department alleged that the HHI would increase by over 500 points, resulting in a post-acquisition HHI of approximately 2,500" if JBS were to acquire National Beef Packing Co. Thus, it is apparent that the pre-merger HHI is approximately 2,000.).

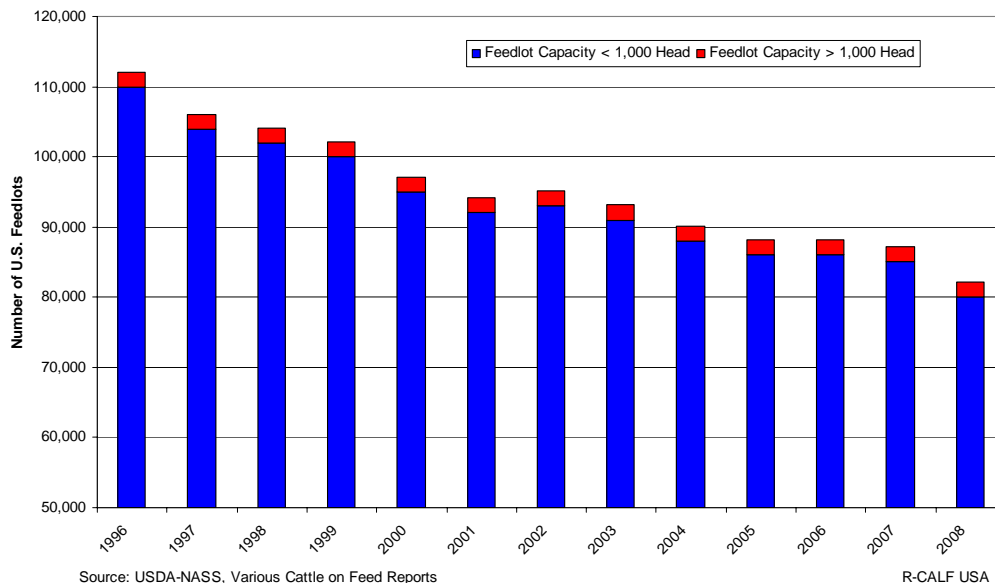
⁸ See Horizontal Merger Guidelines, U.S. Department of Justice and the Federal Trade Commission, Revised April 8, 1997, at 15.

forage for several months until they reach a weight of 600 to 900 pounds (either by the farmer or rancher who weaned them, or a backgrounder or stocker who purchased them after weaning). These cattle, then referred to as feeder cattle, are marketed to feedlots where they are then typically fed a high-energy diet for several months, until they reach their optimal slaughter weight (typically 1,250 pounds) and then marketed to the meatpacker. Thus, the final feeder cattle market is the market in which feeder cattle are sold to feedlots for final finishing (feeding).

Importantly, the market for cows and bulls sold to a feedlot for final finishing functions almost identically to the final feeder cattle market, and for purposes of these comments, R-CALF USA includes steers, heifers, cows and bulls as among the cattle subject to the final feeder cattle market.⁹

The buyer in a final feeder cattle market transaction is a feedlot company, and like the beef packing industry feedlot companies are increasingly concentrated. The number of U.S. feedlots has declined sharply over the past 13 years, with nearly 30,000 feedlots having exited the industry since 1996.¹⁰ Importantly, nearly all the exiting feedlots were smaller feedlots with capacities of less than 1,000 head, as the number of feedlots with capacities of more than 1,000 head has remained relatively constant (chart 5).¹¹

CHART 5: Decline in Numbers of U.S. Feedlots
1996-2008



The individuals who own and operate these smaller feedlots are referred to farmer-feeders. These farmer-feeders contribute greatly to the competitiveness of the feeder cattle market and their drastic decline means that today there are 30,000 fewer bidders for feeder cattle seated in U.S.

⁹ One difference is that feeder cattle are traded in the commodity futures market where cows and bulls are not.

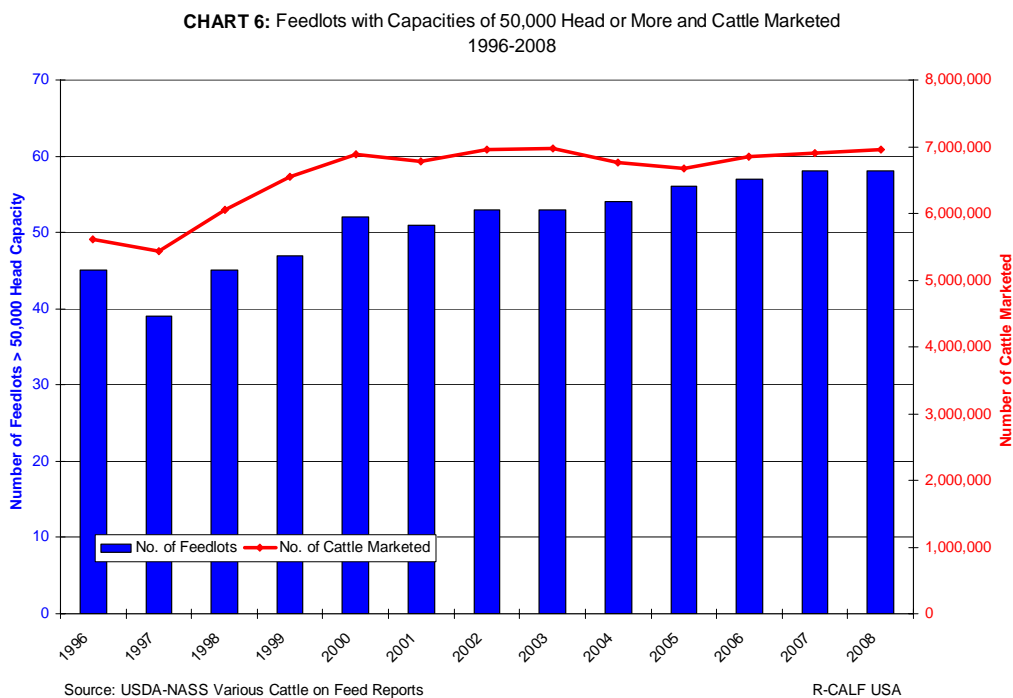
¹⁰ See Cattle, Final Estimates, various reports, 1996-2008, USDA, National Agricultural Statistics Service (hereafter "NASS"); see also Cattle on Feed, USDA, NASS, Feb. 20, 2009.

¹¹ *Ibid.*

auction yards and traveling the rural landscape in search of cattle to feed. As a result, competition has been significantly reduced in the U.S. feeder cattle market.

While the numbers of small feedlots have declined since 1996, the number of cattle marketed by the largest of feedlots, those with capacities of at least 50,000 head, has increased by more than 1.3 million head during this same period.¹²

In 2008, the 58 feedlots with capacities of at least 50,000 head marketed approximately 7 million of the approximately 26 million cattle fed and marketed during that year (chart 6).¹³ These 58 feedlots, therefore, fed and marketed over one-fourth of all the fed cattle in 2008. Included among these 58 feedlots with capacities of at least 50,000 head would be the nation's top four feedlot companies: JBS Five Rivers Ranch Cattle Feeding; Cactus Feeders, Inc.; Cargill Cattle Feeders, LLC; and, Friona Industries, LP.¹⁴ Based on capacities estimated for these top feedlots by Mary Hendrickson and William Heffernan,¹⁵ and using the industry rule-of-thumb for the feedlot turnover rate of 2.5, collectively these four feedlots likely feed approximately 4.7 million cattle annually, or about 18 percent of the total number of feeder cattle purchased, fed and marketed each year.



The concentration achieved by the beef packers in both the final cattle market and initial beef market is worsened because the beef packers have effectively pushed their market dominance

¹² See Cattle, Final Estimates, various reports, 1996-2008, USDA, NASS; see also Cattle on Feed, USDA, NASS, Feb. 20, 2009.

¹³ See Cattle on Feed, USDA, NASS, Feb. 20, 2009, at 14.

¹⁴ See Recent Acquisitions of U.S. Meat Companies, Congressional Research Service, 7-5700, RS22980, March 10, 2009, at 2

¹⁵ See Concentration of Agricultural Markets, Mary Hendrickson and William Heffernan, University of Missouri, Columbia, April 2007.

down through the final cattle market and to the underlying feeder cattle market as well. As stated previously, this dual market dominance is exemplified by JBS’ acquisition of the nation’s largest cattle feeding company and by Cargill’s dominant position as one of the top four feedlot companies.¹⁶

4. Geographic Concentration of the U.S. Cattle Industry

Data reported by USDA show that the top three hog-producing states in 1980 – Iowa, Illinois and Minnesota – captured approximately 44 percent of the nation’s gross income earned that year from the sale of hogs and pigs.¹⁷ Within less than 30 years, concentration in the hog industry resulted in the capture by the top three states – consisting now of Iowa, North Carolina and Minnesota – of over 56 percent of the nation’s gross income earned in 2008 from the sale of hogs and pigs.¹⁸ Thus, concentration in the hog and pig industry resulted in three states capturing within three decades approximately 12 percent of the economic revenues previously generated within 48 states (this is because Illinois is no longer among the top three hog-income earning states) (chart 7).

Chart 7: Change in Percentage of Gross Income from Hogs and Pigs Generated in Top 3 States

1980		2008	
State	Gross Income	State	Gross Income
Iowa	\$2,221,639,000	Iowa	\$4,762,663,000
Illinois	1,042,571,000	Minnesota	2,048,944,000
Minnesota	741,271,000	North Carolina	2,172,213,000
3-State Gross Income	\$4,005,481,000		\$8,983,820,000
Total U.S. Gross Income	\$9,141,911,000		\$16,110,911,000
Percentage	0.4381		0.5576

Source: USDA-NASS

CHART 8



This phenomenon is the result of the nation’s hog production migrating to closer proximity to the location of the concentrated pork packers. The Grain Inspection, Packers and Stockyards Administration (GIPSA) generated a map that identifies the location of the nation’s livestock packers (chart 8).¹⁹ R-CALF USA believes that an investigation would reveal that when the nation’s hog packers concentrated their packing operations in the states of Minnesota, North Carolina and Iowa, the market outlets

¹⁶ See Recent Acquisitions of U.S. Meat Companies, Congressional Research Service, 7-5700, RS22980, March 10, 2009, at 2 (“The proposed JBS acquisition of Five Rivers Ranch Cattle Feeding, which was part of the Smithfield deal, also took place, making JBS the largest cattle feeder in the United States.”); see also *id.*, Table 1 (Cargill Cattle Feeders, LLC, was ranked as the third largest cattle feeding company in 2006, marketing approx. 6 percent of the nation’s fed cattle). Based on information and belief, Cactus Feeders, Inc., and Friona Industries, LP, which also are listed in Table 1 as among the largest cattle feeding companies, are considered captive feedlots and predominantly market their cattle to only one meatpacker.

¹⁷ See Meat Animals, Production, Disposition, Income, 1979-1980, U.S. Department of Agriculture Crop Reporting Board, Economics and Statistics Service, April 1981, at 11, available at <http://usda.mannlib.cornell.edu/usda/nass/MeatAnimPr//1980s/1981/MeatAnimPr-04-00-1981.pdf>.

¹⁸ See Meat Animals, Production, Disposition, and Income 2008 Summary, USDA, NASS, May 2009, at 13, available at <http://usda.mannlib.cornell.edu/usda/current/MeatAnimPr/MeatAnimPr-05-29-2009.pdf>.

¹⁹ See 2008 Annual Report, Packers & Stockyards Program, USDA, GIPSA, March 1, 2009, at 8, available at http://archive.gipsa.usda.gov/pubs/2008_psp_annual_report.pdf.

for independent hog producers in outlying states evaporated, making it economically unfeasible for hundreds of thousands of hog producers to remain in business.

This same phenomenon – whereby the competitive hog market and, hence, hog production profitability, was uprooted from many regions in the U.S. and relegated to the limited geographical regions chosen by the pork packers – also is occurring in the U.S. cattle industry.

CHART 9: Change in Percentage of Gross Income from Cattle and Calves in Top 3 States

1980		2008	
State	Gross Income	State	Gross Income
Texas	\$3,963,247,000	Nebraska	\$7,081,245,000
Kentucky	2,865,037,000	Texas	6,915,837,000
Nebraska	2,798,823,000	Kansas	6,253,151,000
3-State Gross Income	\$9,627,107,000		\$20,250,233,000
Total U.S. Gross Income	\$31,870,419,000		\$48,605,469,000
Percentage	0.3021		0.4166

Source: USDA-NASS

Data reported by USDA show that the top three cattle-producing states in 1980 – Texas, Kentucky and Nebraska – captured 30 percent of the nation’s gross income earned that year from the sale of cattle and calves.²⁰ Within less than 30 years, concentration in the cattle industry resulted in the capture by the top three states –

consisting now of Nebraska, Texas and Kansas – of approximately 42 percent of the nation’s gross income earned in 2008 from the sale of cattle and calves (chart 9).²¹

Thus, like in the hog industry, concentration in the cattle industry resulted in three states capturing within three decades approximately 12 percent of the economic revenues previously generated within 48 states (this is because Kentucky is no longer among the top three cattle-income earning states). This phenomenon is the result of the nation’s cattle production migrating to closer proximity to the locations chosen by the few remaining concentrated beef packers. And, this phenomenon helps explain why rural communities are being hollowed out all across the United States.

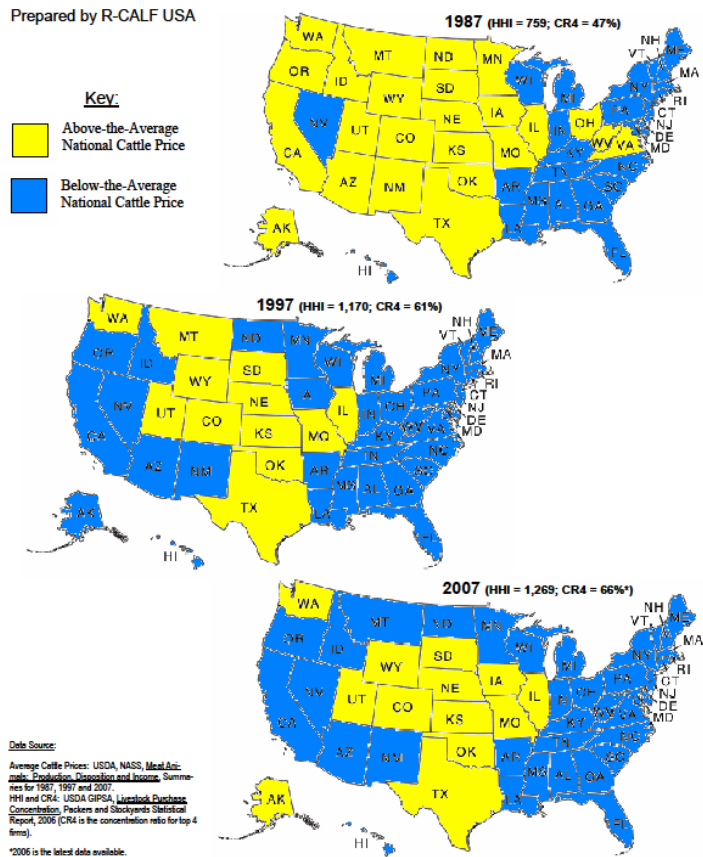
Another indicator of the widespread loss of competitive markets that is leading to the concentration of the cattle industry in an ever shrinking geographic region in the U.S. is that fewer and fewer states are receiving cattle prices that are above the national average. For example, in 1987 nearly one-half the states (24) enjoyed cattle prices that were above the national average. But by 2007, just 20 years later, the number of such fortunate states was reduced to only 13 (chart 10).

²⁰ See Meat Animals, Production, Disposition, Income, 1979-1980, USDA, Agriculture Crop Reporting Board, Economics and Statistics Service, April 1981, at 7, available at <http://usda.mannlib.cornell.edu/usda/nass/MeatAnimPr//1980s/1981/MeatAnimPr-04-00-1981.pdf>.

²¹ See Meat Animals, Production, Disposition, and Income 2008 Summary, USDA, NASS, May 2009, at 13, available at <http://usda.mannlib.cornell.edu/usda/current/MeatAnimPr/MeatAnimPr-05-29-2009.pdf>.

It is now strikingly evident that the profitability of the U.S. cattle industry is being drawn away from many states and many rural communities and is becoming increasingly concentrated in the narrow region where the few remaining beef packers and few remaining feedlots have decided to relocate – in the High Plains region of the United States. This phenomenon further helps explain the widespread economic desecration of rural communities all across the United States.

CHART 10: Effects of Declining Competition on Cattle Prices



5. Market Concentration In the Competing Proteins Market

Beef, pork and poultry are substitute food protein products that compete head-to-head for market share in the consumer meat market. The demand and price for cattle is influenced by the supply and price of competing proteins such as pork and poultry.²² USDA has found that beef prices are particularly susceptible to increased poultry supplies, i.e., poultry broilers at relatively lower prices.²³ USDA further found that “beef, pork, and chicken contributed about 34 percent of total protein available in the U.S. food supply on average in 1990-94;” that “expenditures on red meat and poultry products account for about one-third of the food spending in American households;” and, “if the price of beef goes up while the price of chicken remains lower than beef, consumers

²² See Livestock, Dairy and Poultry Outlook, USDA, ERS, LDP-M-120 (June 17, 2004), at 9 (“Given the present strength in the fed cattle market . . . increased supplies of competing meats . . . would push breakevens into the red quickly.”), available at <http://www.ers.usda.gov/publications/ldp/jun04/LDPM120T.pdf>.

²³ See Livestock, Dairy, and Poultry Outlook, USDA, ERS, LDP-M-139 (Jan. 19, 2006), at 8 (“Large supplies of competing meats at relatively lower prices, particularly broilers, are also expected to pressure beef prices . . .”), available at <http://www.ers.usda.gov/Publications/LDP/2006/01Jan/LDPM139T.pdf>; see also *id.*, at 7 (“Improved grading prospects and larger number of cattle on feed will pressure the market, as will larger supplies of competing meats at relatively lower prices.”).

will likely buy less of the relatively more expensive beef and buy more of the relatively less expensive chicken.”²⁴

Researcher, Desmond A. Jolly, University of California, Davis, in discussing the relationships between beef and its competing food proteins – pork and chicken – found that consumer demand for each of these competing proteins responds to, *inter alia*, consumer income, the price of the product, and the price of substitutes.²⁵ Kansas State University (KSU) researchers found that the decline in retail beef demand experienced from 1980 through 1998 contributed to the reduced size of the U.S. cattle industry, “particularly in relation to competing meat sectors such as poultry and pork,”²⁶ and “[w]hen beef demand increases (i.e., shifts up), say as a result of an increase in the price of poultry that causes consumers to substitute beef for poultry, the result is higher beef prices. . . .”²⁷ Researchers at the University of Nebraska – Lincoln (UNL) found that, “Pork and poultry are generally considered substitute sources of protein for beef.”²⁸ A literature review by USDA reveals that the average response to competing meat price changes is such that a 1 percent decrease in poultry prices would result in a 0.24 percent decrease in beef consumption.²⁹

Despite the obvious reduction in competition that occurs among and between the competing proteins – beef, pork and chicken – if dominant firms control the production, output (i.e., supplies) and the price for each competing protein, dominant meatpackers continue to be unrestrained in their capture of dominant control over each competing protein. For example, the 2007 concentration study by Mary Hendrickson and William Heffernan found that Tyson, Swift & Co. and Cargill each were among the nation’s largest beef packers and pork packers, and additionally, Tyson and Cargill were the largest broiler producers and turkey producers, respectively.³⁰ More recently, the Justice Department declined to initiate antitrust enforcement action against the acquisition by JBS S.A., the world’s largest beef packer, of Pilgrim’s Pride Corp., which controls approximately 22 percent of the U.S. poultry broiler market.³¹

U.S. cattle producers are obligated to pay tens of millions of dollars each year to the government-run beef checkoff program (e.g., \$82.8 million was assessed in 2007³²), and a significant portion of these assessments are devoted to enhancing the competitiveness of beef over poultry. For

²⁴ Price and Income Affect Nutrients Consumed From Meats, Food Review, Kuo S. Huang, FoodReview, USDA, ERS, January-April 1996, at 37, 38 (*FoodReview* was replaced by *Amber Waves* following the Winter 2002 issue).

²⁵ See Reasons for the decline in beef consumption, Health concerns played a part but price was most important, Desmond A. Jolly, University of California, Davis, California Agriculture, May-June 1983, at 14, 15.

²⁶ U.S. Beef Demand Drivers and Enhancement Opportunities: A Research Summary, James Mintert *et al.*, Kansas State University, Department of Agriculture Economics, MF-2876, January 2009.

²⁷ Focus on Beef Demand, Managing for Today’s Cattle Market and Beyond, James Mintert, *et al.*, Kansas State University, March 2002.

²⁸ Improved Beef Demand Benefits Nebraska Cattle Producers, Cornhusker Economics, Institute of Agriculture & Natural Resources, Department of Agricultural Economics, University of Nebraska – Lincoln, September 27, 2000.

²⁹ See Commodity and Food Elasticities: Demand Elasticities from Literature Results, Data Sets, USDA, ERS, available at

<http://www.ers.usda.gov/Data/Elasticities/ShowTable.aspx?geo=United%20States&com=Beef&xcom=Poultry>.

³⁰ See Concentration of Agricultural Markets, Mary Hendrickson and William Heffernan, University of Missouri, Columbia, April 2007.

³¹ See Daily Livestock Report, CME Group, Vol. 7, No. 169, Sept. 2, 2009, available at <http://www.dailylivestockreport.com/>.

³² See <http://www.beefboard.org/financial/files/State-National%20Financials.pdf>.

example, in listing its top 20 accomplishments during the beef checkoff program's first 20 years, the government-run program included producer-paid research that expressly distinguished the superiority of beef over competing chicken for purposes of stimulating consumers to buy more beef:

Beef Nutrition. Checkoff-funded **RESEARCH** has confirmed that, calorie for calorie, lean beef packs a punch. A nutrition parity study between beef and chicken revealed that a 3-ounce cut of lean beef has, on average, only one more gram of saturated fat than the same size serving of a skinless chicken breast. After that, there's no comparison. That 3-ounce serving of lean beef delivers eight times more vitamin B12, six times more zinc and three times more iron than the chicken.³³ (Emphasis in the original.)

The government-run beef checkoff program maintains a plethora of documents that are designed to persuade producers that their mandatory assessments are necessary in order for beef to effectively compete against poultry. For example, a producer-paid beef checkoff advertisement touted by the beef checkoff program explains why the producer-funded beef checkoff program is critically important to the beef industry:

In 2006, increased placements and heavier carcass weights, combined with a significant supply of **inexpensive poultry products** and closed large export markets, make summertime beef promotion more crucial than ever.³⁴ (Emphasis added.)

Moreover, the U.S. Supreme Court case involving the government-run beef checkoff program recently litigated by the Justice Department unequivocally determined that beef and poultry are competitors. In the *amicus curia* brief from the states, it was acknowledged that poultry is a competing product to beef:

Likewise, state beef councils cannot promote a message that disparages a competing product, such as poultry, Trial Tr. 269-70, 273, because the government—in contrast to the beef industry—has an interest in the success of competing agricultural sectors.³⁵

R-CALF USA believes the control by individual, dominant beef packing firms over the production, wholesaling and retailing of competing proteins pork and poultry violates U.S. antitrust laws. Such control reduces, if not eliminates, competition between the competing proteins, as well as between the farmers and ranchers who produce cattle, hogs, chickens and turkeys.

This loss of competition and commensurate increase in market power facilitates the multi-protein meatpackers' ability to exercise market power to the detriment of both U.S. cattle producers and U.S. meat consumers. The foundation for our concern is that beef, pork and poultry are indeed

³³ See http://www.beefboard.org/news/Release_2006_09_25_c.asp.

³⁴ See <http://www.beefboard.org/uDocs/cbbannualreport2006.pdf>, at 11.

³⁵ See <http://www.beefboard.org/uDocs/Amicus%20briefs%20on%20merit%20-%20filed%20by%20state%20AGs.pdf>, at 19.

competing, substitute protein products in the consumer market, and meatpackers in control of each substitute can arbitrarily increase or decrease poultry and/or pork production and/or raise and lower poultry and pork prices within their fully integrated poultry and pork divisions to manipulate both the demand for beef and the price for live cattle.

B. The Remaining Participants in the U.S. Cattle Industry

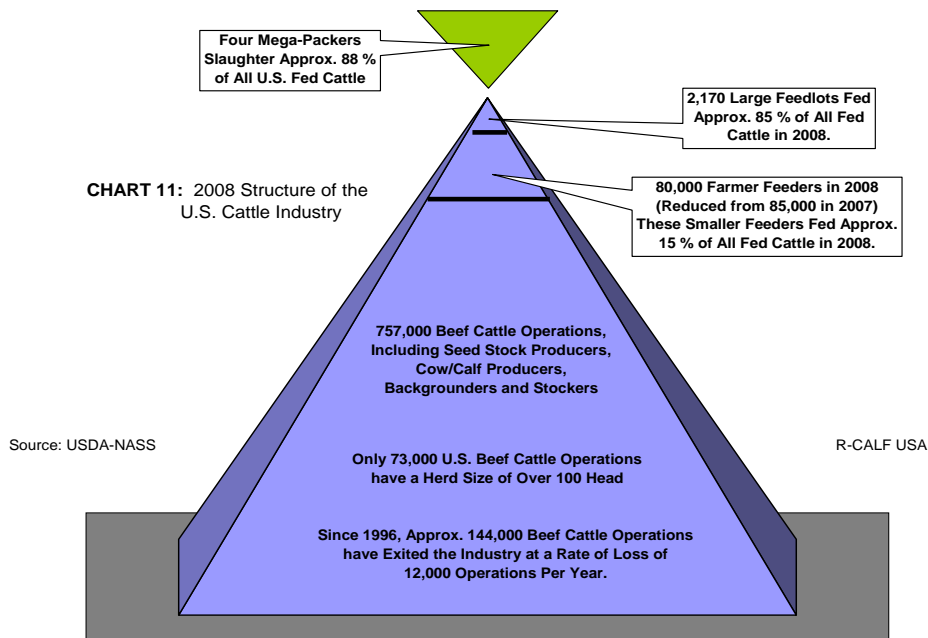
1. The Precarious Structure of U.S. Cattle Industry Participants

What remains today of the U.S. cattle industry is a highly concentrated industry structure that, as stated above, exceeds the level of market concentration “generally considered to elicit non-competitive behavior and result in adverse economic performance.”³⁶ Today, R-CALF USA estimates that 88 percent of all the fed cattle calved and marketed by the remaining 757,000 beef cattle producers are ultimately marketed through only four dominant beef packers. This unprecedented level of market concentration gives the dominant beef packers the ability to control, restrict and manage access to the market. And, this gives the dominant beef packers the ability to control the key determinant for farmer and rancher profitability – the price of their live cattle.

As if this sheer, unprecedented level of market concentration were not enough, the dominant beef packers that are geographically concentrating the cattle industry and that already control the final cattle market, the initial beef market, and the competing proteins market are quickly capturing control of the final feeder cattle market by dominating the feeding segment of the live cattle industry. Today there are 2,170 dominant feedlots that feed approximately 85 percent of all the fed cattle in the United States, while smaller, farmer-feeders feed only about 15 percent of the nations fed cattle (chart 11).³⁷

³⁶ A Review of Causes for and Consequences of Economic Concentration in the U.S. Meatpacking Industry, Clement E. Ward, Current Agriculture Food and Resource Issues, 2001, at 1.

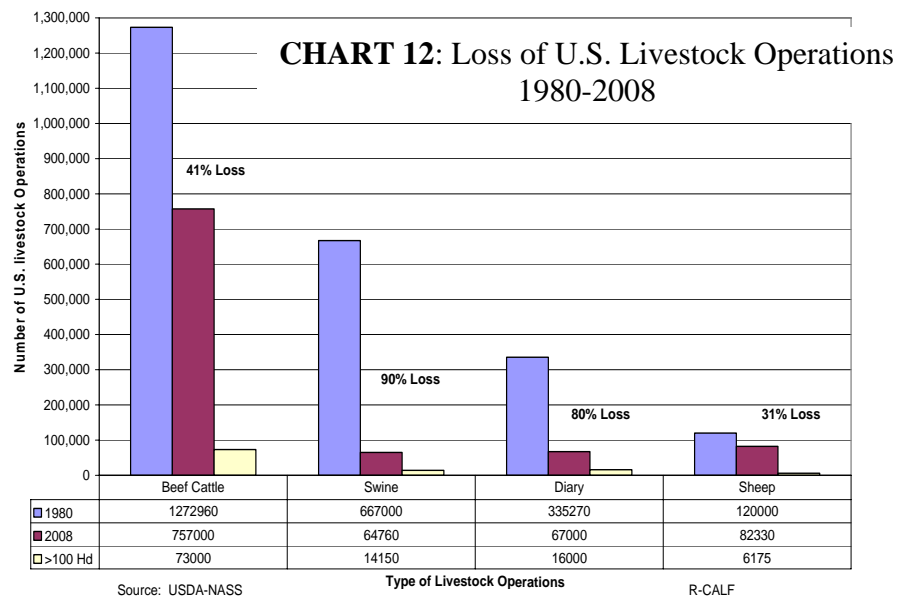
³⁷ See Cattle on Feed, USDA, NASS, Feb. 20, 2009, at 14 (In 2008, 80,000 feedlots with capacities of less than 1,000 head marketed 4.045 million of the 26.449 million cattle marketed. The 2,170 larger feedlots marketed 22.404 million cattle.), available at <http://usda.mannlib.cornell.edu/usda/nass/CattOnFe//2000s/2009/CattOnFe-02-20-2009.pdf>.



2. The Entire U.S. Livestock Industry Is in a Serious Crisis

The cattle industry is fast going the way of the hog and dairy industries that already have lost 90 percent and 80 percent of their respective industries' participants within the past 30 years, since 1980.

It is inexplicable that neither Congress nor federal regulators responded at all to the mass exodus of hundreds of thousands of independent hog producers over the past three decades without determining the extent of the market power exerted by the dominant pork packers that effected such a drastic industry change. The number



of U.S. hog operations fell from 667,000 in 1980 to fewer than 65,000 in 2008. The larger cattle industry is suffering the same fate. It has lost 41 percent of its operations since 1980, falling from about 1.3 million cattle operations to 757,000 cattle operations (chart 12). This horrendous loss of industry participants translates into the centralization of U.S. livestock production, which threatens the nation's food security and explains the ongoing, economic demise of rural communities all across the United States.

3. The Loss Rate of U.S. Cattle Operations Has Not Been Gradual

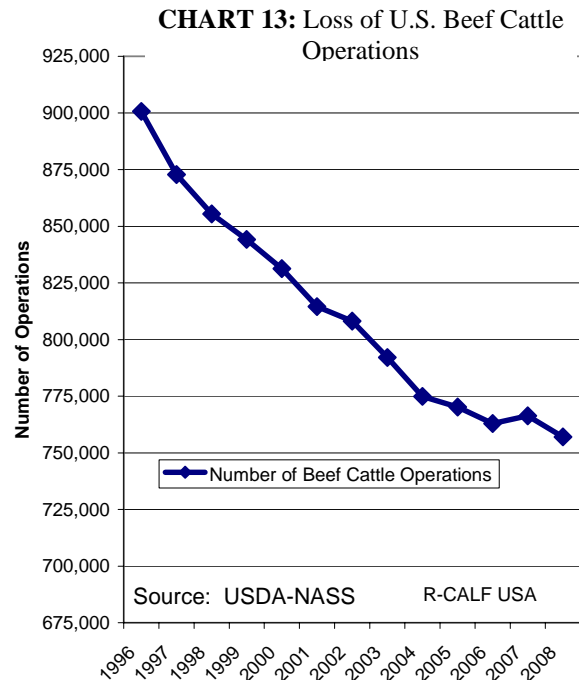
In just the past 12 years, from 1996 to 2008, over 143,000 U.S. cattle operations exited the U.S. cattle industry, representing a rate-of-loss of nearly 12,000 operations per year (chart 13). To put this in perspective, this represents an annual loss of more beef cattle operations than there are in each of the entire states of Arizona, California, Colorado, Idaho, Michigan, Montana, North Dakota, West Virginia, Wisconsin, and several other states.³⁸ Again, this widespread, horrendous loss of U.S. cattle operations helps explain the depressed state of the United States' rural economy.

C. U.S. Cattle Industry Production Remains Stagnant

The beef packing industry and its allied trade associations assert that improvements in genetics, managerial ability, technology and feed efficiency gained by the U.S. cattle industry has negated the need for more cattle and more cattle producers because the U.S. cattle industry is now producing more beef with fewer mother cows. The Texas Cattle Feeders Association (TCFA), for example, claims that, "Productivity gains have offset the need for an additional 5.3 million cows."³⁹ And, it claims the U.S. now has the smallest cow herd since 1949 and yet has experienced a 176 percent growth in beef production since that time.⁴⁰ These claims are highly misleading at best and, unfortunately, are among the chief "efficiency" claims made by the beef packers and their allies to rationalize the exodus of independent U.S. cattle producers while they simultaneously wrest control over the live cattle supply chain away from the competitive marketplace.

The reason these claims are misleading is five-fold:

First, domestic productivity gains have *not* offset the need for an additional 5.3 million cows (which is the number of U.S. beef cows liquidated from the U.S. herd since 1980). The U.S. imported 2.5 million and 2.3 million live cattle in 2007 and 2008, respectively.⁴¹ It also imported 3 billion and 2.5 billion pounds of beef in each of those years, respectively.⁴² Based on a 750-pound carcass weight, the live cattle equivalent of the beef imported in 2007 and 2008 is



³⁸ See Farms, Land in Farms, and Livestock Operations 2008 Summary, USDA, NASS, Feb. 2009, at 18, available at <http://usda.mannlib.cornell.edu/usda/current/FarmLandIn/FarmLandIn-02-12-2009.pdf>.

³⁹ See Charts Distributed by Texas Cattle Feeders Association at the New Mexico Cattle Growers' Annual Meeting held Dec. 5, 2009, attached hereto as Attachment 1.

⁴⁰ *Ibid.*

⁴¹ Livestock and Meat Trade Data, Cattle: Annual and Cumulative Year-to-Date U.S. Trade (Head), USDA, ERS, available at <http://www.ers.usda.gov/data/meattrade/CattleYearly.htm>.

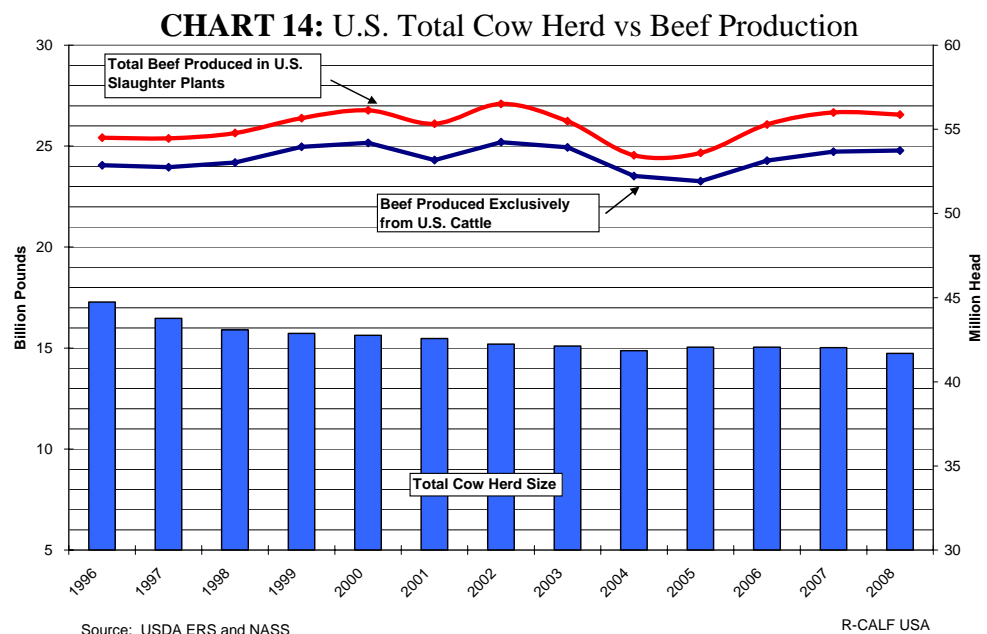
⁴² See Livestock and Meat Trade Data, Beef and Veal: Cumulative Year-To-Date U.S. Trade (Carcass Weight 1,000 Pounds), USDA, ERS, available at <http://www.ers.usda.gov/data/meattrade/BeefVealYearly.htm>.

approximately 4 million and 3 million head, respectively. Thus, the U.S. imported the equivalent of 5.5 million cattle in 2007 and 4.8 million cattle in 2008. Presuming that consumer demand and all export opportunities for beef were met in 2007 and 2008, these imports offset the United States cattle industry’s opportunity to maintain the additional 5.3 million cows liquidated since 1980. Thus, TCFA’s claim that additional U.S. cows are not needed due to productivity increases is baseless. It clearly is not the case that current domestic production is meeting the current demand for beef. The Justice Department and USDA should take a critical look at how the packers are strategically using imports to restrain the domestic cattle industry.

Second, a significant portion of U.S. beef production reported by USDA as “domestic beef production” did *not* originate from the U.S. cow herd – it originated from cattle imported into the U.S. from Canada and Mexico. The estimated amount of beef produced from imported cattle in U.S. slaughtering plants increased from 543 million pounds in 1985 to 1.96 billion pounds in 1995, and was 1.94 billion and 1.78 billion pounds in 2007 and 2008, respectively. This estimate is based on multiplying each year’s average U.S. carcass weight by the number of cattle imported each year.

Third, increased beef production occurs during the liquidation phase of the cattle cycle because liquidation necessarily entails selling off the cow herd – including cows and heifers, as well as bulls – for slaughter. The U.S. has been liquidating its cattle herd since 1996, and the slaughter of liquidated cows, heifers and bulls contributes significant volumes to domestic production that would not otherwise be available if herd liquidation was not occurring.

The production of beef derived from cattle born and raised in the U.S. since 1996 has remained relatively stagnant, rising only slightly above and falling only slightly below the 1996 starting point (chart 14). This is somewhat alarming because the ongoing liquidation of

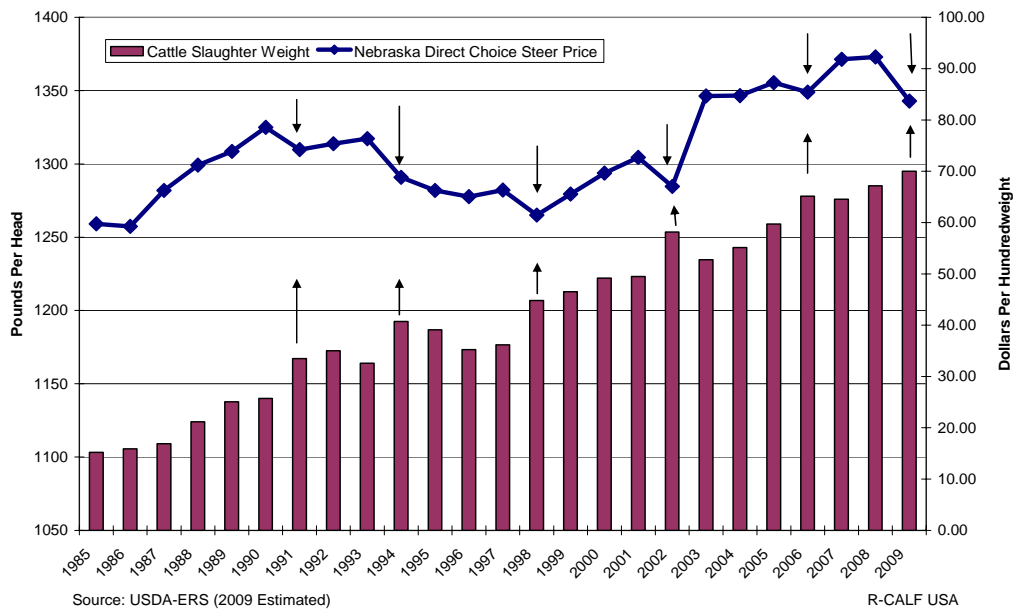


additional cows, heifers and bulls should be increasing domestic beef production even more significantly. The fact that it is not raises the concern that domestic production without the additional liquidated animals may be significantly lower than USDA’s current estimates.

Fourth, beef production increases when individual cattle are fed longer – beyond their optimal slaughter weight – which leads to heavier carcasses of lower quality. The dominant beef packers, because they control access to the market, can effect longer feeding periods simply by limiting their procurement of optimal weight cattle (e.g., by offering only a price lower than what a competitive market would bring), thus forcing the industry to increase carcass weights through longer feeding periods. When cattle supplies are tight, e.g., during the liquidation phase of the cattle cycle, beef packers are incentivized to manipulate the industry to produce overweight cattle, i.e., heavier carcasses, by limiting access to the marketplace through, e.g., the offering of low prices for cattle. The beef packers know that the market response to lower prices is to feed cattle longer, and that action increases the beef packers’ tonnage, thus helping to satisfy demand while insulating the beef packer from a tight-supply market, which would otherwise require them to pay higher prices for cattle.

Each significant downturn in live cattle prices since 1985 resulted in an abrupt increase in the average slaughter weight of cattle when compared to the previous year (chart 15). Contrary to claims made by the TCFA and other packer-aligned trade associations, this does not demonstrate that heavier cattle are solely the result of increased productivity. Instead, this relationship between cattle prices and cattle slaughter weights demonstrates the susceptibility of the cattle industry to price manipulation by the packers – manipulations that enable packers to increase tonnage without increasing costs. The Justice Department and USDA should carefully investigate the beef packer practices that effectively manipulate both the price and weight of fed cattle.

CHART 15: Relationship Between Cattle Prices and Cattle Slaughter Weights



Finally, the purpose of producing beef is to satisfy domestic beef consumption and export opportunities. As will be discussed later in these comments, U.S. beef production has not kept pace with increased domestic beef consumption, even with the heavier carcass weights, and the production potential of the U.S. cattle industry is being severely restrained by the beef packers’ actions that are manipulating the industry’s output.

II. THE U.S. CATTLE INDUSTRY IS UNIQUELY SUSCEPTIBLE TO MONOPSONY POWER AND EXPLOITATION

A. The Final Cattle Market Is the Portal through Which Market Power Invades the Entire U.S. Live Cattle Industry.

Not all of the approximately \$50 billion in annual cash receipts from the sale of cattle and calves is generated in the final cattle market where slaughter-ready cattle are sold to beef packers. In 2008, e.g., over \$48 billion in cash receipts was generated by the U.S. cattle industry from the marketing of over 44 million cattle and nearly 9 million calves.⁴³ However, the beef packers purchased and slaughtered only approximately 34 million cattle in 2008.⁴⁴ Thus, transactions in the final cattle market involved only about 64 percent (i.e., 34 million of the 53 million cattle and calves marketed) of the cattle and calves marketed in 2008.

This informs us that the U.S. cattle industry is much more than just a supply source for the nation's meatpackers, and that the meatpackers are *not* the sole source of revenues for the entire industry. Instead, the U.S. cattle industry is a dynamic industry with numerous sub-markets (e.g., the final feeder cattle market) where economic activity critical to the wellbeing of rural communities all across the United States is generated from within the industry itself.

However, the final cattle market where slaughter-ready cattle, particularly steers and heifers, are sold directly to the beef packer *is* the price-making market for the entire U.S. cattle industry. This is because the price for slaughter-ready steers, heifers, cows and bulls is transferred, at least in part, backward throughout the live cattle production chain, impacting seed stock producers, cow/calf producers, backgrounders, and stockers. Thus, even a small lessening of competition or small price manipulation in the final cattle market has a profound, negative impact on the welfare of the hundreds of thousands of remaining independent cattle producers and the rural communities they support because the reduced competition and reduced price reverberates and compounds throughout the entire industry.

Oklahoma State University economist Clement E. Ward addressed the issue of seemingly small price impacts on the cattle industry and found that “[r]esearch to date suggests price impacts from packer concentration have been negative in general, but small.”⁴⁵ He stated that while most studies found price distortions of 3 percent or less, he explained that “even seemingly small impacts on a \$/cwt. basis may make substantial difference to livestock producers and rival meatpacking firms operating at the margin of remaining viable or being forced to exit an industry.”⁴⁶

⁴³ See Meat Animals Production, Disposition, and Income 2008 Summary, USDA, NASS, May 2009, at 4, 7, available at <http://usda.mannlib.cornell.edu/usda/current/MeatAnimPr/MeatAnimPr-05-29-2009.pdf>.

⁴⁴ See Livestock Slaughter 2008 Summary, USDA, NASS, March 2009, at 13, available at <http://usda.mannlib.cornell.edu/usda/current/LiveSlauSu/LiveSlauSu-03-06-2009.pdf>.

⁴⁵ Packer Concentration and Packer Supplies, Clement E. Ward, Oklahoma Cooperative Extension Service, AGEC-554, at 554-5.

⁴⁶ A Review of Causes for and Consequences of Economic Concentration in the U.S. Meatpacking Industry, Clement E. Ward, Current Agriculture Food and Resource Issues, 2001, at 2.

In 1999, economists at Utah State University found it “surprising in the face of greatly increased packer concentration” that many studies found no or very limited ability of packers to exploit feeders/ranchers and consumers.⁴⁷ These researchers found that most of the studies used to identify market power (reduced-form modeling approaches) focused on market outcomes and “overlooked important elements of the competitive process in the beef packing industry.”⁴⁸

Notwithstanding the potential that most studies have overlooked important elements of the competitive process but nevertheless found “small” negative impacts due to packer concentration and monopsony power, the application of even a 3 percent price distortion on the entire \$50 billion live cattle industry would result in a loss of \$1.5 billion to U.S. cattle producers. It is important for the Justice Department and USDA to recognize that the final cattle market is the portal through which even small market-power induced price distortions can invade and cripple the entire U.S. live cattle industry.

B. The Very Nature of Cattle Makes Their Value Susceptible to Market Power

The very nature of cattle makes them unique when compared to other commodities that also are the subject of the investigation into the competitiveness of agricultural markets. Cattle, e.g., are not a storable agricultural commodity or a commodity suitable for bulk transportation. The Justice Department and USDA, therefore, should not limit its review of the state of competition in the cattle industry based on standards developed for other agricultural commodities. The following are a few unique characteristics of cattle that distinguish them from all other agricultural commodities:

1. Cattle have the Longest Biological Cycle of Any Farmed Animal

The Government Accountability Office (GAO) found that cattle have the longest biological cycle of all meat animals.⁴⁹ This is the characteristic that created the historical phenomenon known as the cattle cycle. According to USDA, the cattle cycle “arises because biological constraints prevent producers from instantly responding to price.”⁵⁰ R-CALF USA believes the vertical integration of the U.S. cattle industry by the major meatpackers has been slower than in the U.S. hog industry due to this unique characteristic combined with the commensurate forage requirements needed to rear cattle. It takes approximately 15 to 18 months to rear cattle to slaughter weight and, unlike hogs, cattle consume considerable volumes of forage (i.e., from grazing) for much of this time. This makes the cattle industry less adaptable to the concentrated production practices common in the hog-rearing industry – practices that are more conducive to vertical integration by meatpackers – at least in the earlier stages of cattle production. However, after cattle reach approximately one-year of age on forage, and weigh approximately 600 to 900 pounds, they then become adaptable to a more concentrated production regime, i.e., they can be finished in large, concentrated feedlots. It is at this stage of the cattle production cycle – the final

⁴⁷ Testing for Market Power in Beef Packing: Where are We and What’s Next?, Lynn Hunnicutt, Quinn Weninger, Utah State University, August 1999.

⁴⁸ *Id.*, at 1.

⁴⁹ Economic Models of Cattle Prices, How USDA Can Act to Improve Models to Explain Cattle Prices, U.S.

Government Accountability Office (formally the General Accounting Office), (GAO-020246, March 2002), at 30.

⁵⁰ Cattle: Background, Briefing Room, USDA, ERS, updated June 7, 2007, available at <http://www.ers.usda.gov/Briefing/Cattle/Background.htm>.

feeding stage – where meatpackers have focused their vertical integration efforts, and it is here that the Justice Department and USDA must focus its attention to identify the various forms of market power exercised by the concentrated beef packers.

The long biological cycle also makes the cattle industry highly susceptible to exploitation by firms that control the production and output of other competing protein sources, i.e., hogs and poultry, which each have much shorter biological cycles that enable their respective industry's to respond quickly to changes in price by quickly adjusting production and output. In addition, because the meats from these competing protein sources are a market substitute for beef, multiple-protein firms can relatively quickly manipulate the output and price of the competing proteins in order to manipulate the demand and price for cattle, while the cattle industry remains constrained from responding due to cattle's prolonged biological cycle.

The inelasticity of supply in the cattle industry compared to the elasticity of supply in the poultry industry⁵¹ gives multiple-protein meatpackers a tremendous, anticompetitive advantage over U.S. farmers and ranchers who sell live cattle. If, e.g., a multiple-protein meatpacker were dissatisfied with the level of profits earned in its beef packing operation, it could increase its poultry production and/or reduce its poultry prices in order to reduce consumption of beef, which would reduce both the demand and price for live cattle. The response by the cattle industry would be limited to liquidation, which likely would accelerate the ongoing liquidation of the U.S. cattle herd and the exodus of U.S. cattle producers from the industry. When the price of cattle falls to the meatpacker's preferred level, the firm can quickly restore higher poultry prices and reduce the volume of poultry production, enabling it to maximize its profits from the sales of both competing proteins until dissatisfaction returns once again and the cycle can be unilaterally restarted. Given the long biological cycle of cattle, the firm could enjoy several years' worth of maximized profits – a period when both cattle producers and beef consumers likely would be exploited.

2. Slaughter-Ready Cattle are Highly Perishable

Unlike many agricultural commodities that are storable, fed cattle that have reached their optimal slaughter weight must be marketed within a narrow window of time (generally within about a two-week period); otherwise, the animals would degrade in quality and value.⁵² This characteristic makes the value of cattle extremely susceptible to manipulation, which beef packers can accomplish simply by restricting timely access to the market.

3. Transportation Costs Limit Marketing Options for Slaughter-Ready Cattle

The feasibility of transporting cattle long distances decreases as cattle approach slaughter weight. Researchers have found that the distance of the seller from the slaughtering plant affects the

⁵¹ See Economic Models of Cattle Prices, How USDA Can Act to Improve Models to Explain Cattle Prices, U.S. Government Accountability Office (formally the General Accounting Office), GAO-020246, March 2002, at 30.

⁵² See GIPSA Livestock and Meat Marketing Study, January 2007, Volume 3, at 5-4, available at http://archive.gipsa.usda.gov/psp/issues/livemarketstudy/LMMS_Vol_3.pdf.

choice of cattle procurement methods⁵³ and “most cattle are purchased for a specific plant from within a 100-mile radius of that facility, whether the owning firm had one or several slaughtering plants.”⁵⁴ The researchers found that the cost of transporting cattle long distances creates a limited procurement area for meat packing plants, resulting in higher packer concentration within certain states than nationally.⁵⁵

These researchers identified nine cattle procurement regions that were based on the geographic proximity of packing plants and the procurement area for those packing plants.⁵⁶ They defined the general procurement area around a 300-mile radius of packing plants based on a finding that some cattle are regularly purchased from between 100 to 300 miles away from a packing plant.⁵⁷ Included as a single region are California and Arizona.⁵⁸

While researchers have found that the wholesale beef market is national in scope, the discussion above suggests that transportation costs combined with the concentration of beef packers function to limit the national purview of the slaughter-ready cattle market. According to a study by John R. Schroeter, “The wholesale beef market . . . is essentially national in scope and insulated, to some extent, from the vagaries of the terms and volume of trade in a single regional fed cattle market.”⁵⁹

C. The U.S. Cattle Market Is Highly Susceptible to Monopsony Power and Exploitation

Corresponding to the unique nature of cattle that makes their value vulnerable to manipulation, the marketplace for cattle likewise is unique when compared to other agricultural commodities and highly susceptible to antitrust activities and anticompetitive practices. The following are key characteristics of the U.S. cattle market that make it uniquely prone to such deplorable behavior.

1. The Beef Packing Industry Is Exceedingly Concentrated

As stated previously, Oklahoma State University Economist Clement Ward asserts that concentration levels in the U.S. meatpacking industry are already among the highest of any industry in the United States, “and well above levels generally considered to elicit non-competitive behavior and result in adverse economic performance.”⁶⁰

⁵³ See Examining Packer Choice of Slaughter Cattle Procurement and Pricing Methods, Oral Capps, Jr., et al., *Agricultural and Resource Economics Review*, April 1999, at 21.

⁵⁴ *Id.* at 15.

⁵⁵ See *id.* at 16.

⁵⁶ *Ibid.*

⁵⁷ See Examining Packer Choice of Slaughter Cattle Procurement and Pricing Methods, Oral Capps, Jr., et al., *Agricultural and Resource Economics Review*, April 1999, at 15.

⁵⁸ See *id.* at 16.

⁵⁹ Captive Supplies and Cash Market Prices for Fed Cattle: A Dynamic Rational Expectations Model of Delivery Timing, John R. Schroeter, Department of Economics, Iowa State University, Working Paper # 07002, January 2007.

⁶⁰ A Review of Causes for and Consequences of Economic Concentration in the U.S. Meatpacking Industry, Clement E. Ward, *Current Agriculture Food and Resource Issues*, 2001, at 1.

2. Regional Competition for Raw Products Like Cattle Is Less Intense than Is Competition in Processed Food Products

Researchers have found that regional competition for raw products, which would include competition for slaughter-ready cattle, is inherently less intense than is competition in processed food products.⁶¹ Thus, the competition for slaughter-ready cattle is inherently fragile, even without the added burden of market power abuses from concentrated beef packers that wield considerable monopsony power.

Further, the Regional Herfindahl-Hirschman Indices (RHHI) are already exceedingly high in all nine cattle procurement regions. In studying regional differences in procurement and pricing methods (resulting in part from transportation constraints) researchers calculated the RHHI for nine regional procurement areas for meatpacking plants.⁶² Values for RHHI in the nine regions ranged from a low of 2,610 to a high of 4,451, though the RHHI values in three regions were deleted to avoid disclosure.⁶³ The researches found that a 1 percent increase in regional firm concentration as measured by the RHHI raises the probability that packers would use packer fed arrangements by 3.18 percent.⁶⁴ These findings suggest that meaningful competition in the final cattle market may well be nonexistent in procurement regions where the RHHI was exceedingly high.

3. The U.S. Cattle Market Is Highly Sensitive to Even Slight Changes in Supply

As confirmed by the United States International Trade Commission (USITC), the U.S. cattle market is highly sensitive to even slight changes in cattle supplies. The USITC found that the farm level elasticity of demand for slaughter cattle is such that “each 1 percent increase in fed cattle numbers would be expected to decrease fed cattle prices by 2 percent.”⁶⁵ Researchers at the University of Nebraska – Lincoln found that fed cattle prices were even more susceptible to changes in supplies and stated that a 1 percent increase in fed cattle supplies would be expected to reduce fed cattle prices by up to 2.5 percent.⁶⁶ As a result, the U.S. cattle market is highly sensitive to the importation of cattle from foreign sources.

Recent experience shows that nominal U.S. fed cattle prices jumped to the highest level in the industry’s history within just five months after the importation into the U.S. of live cattle from Canada was curtailed due to the discovery of bovine spongiform encephalopathy (BSE) in the

⁶¹ See Captive Supplies and the Cash Market Price: A Spatial Markets Approach, Mingxia Zhang and Richard J. Sexton, *Journal of Agricultural and Resource Economics*, 25(1): 88-108, at 90, fn 7.

⁶² See Examining Packer Choice of Slaughter Cattle Procurement and Pricing Methods, Oral Capps, Jr., et al., *Agricultural and Resource Economics Review*, April 1999, at 16.

⁶³ See *id.*, at 16.

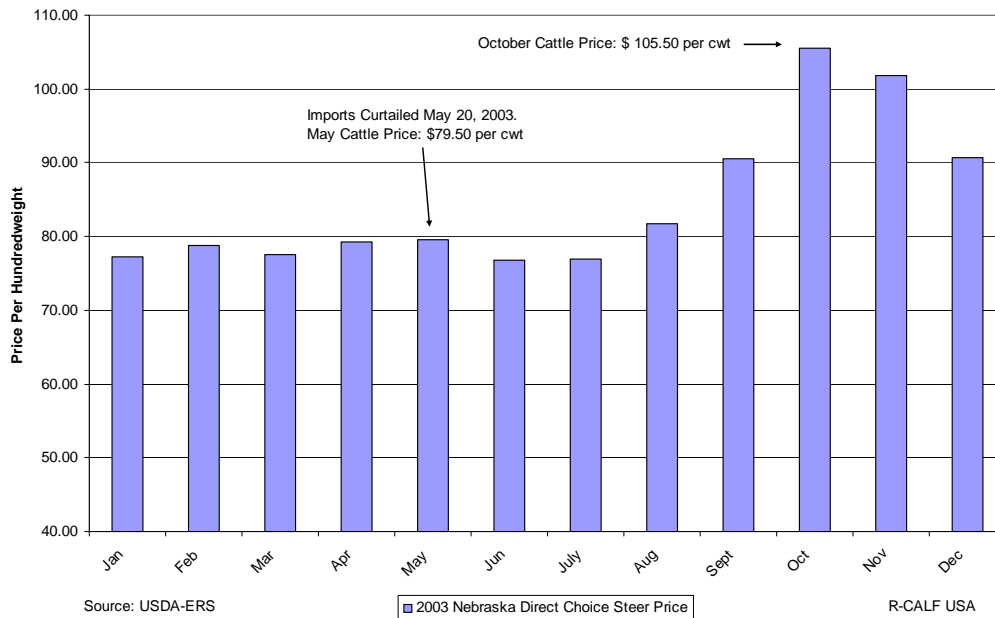
⁶⁴ See Examining Packer Choice of Slaughter Cattle Procurement and Pricing Methods, Oral Capps, Jr., et al., *Agricultural and Resource Economics Review*, April 1999, at 21.

⁶⁵ U.S.-Australia Free Trade Agreement: Potential Economywide and Selected Sectoral Effects, United States International Trade Commission (Publication 3697; May 2004) at 44, fn 26, available at <http://hotdocs.usitc.gov/docs/pubs/2104f/pub3697.pdf>.

⁶⁶ See The Economics of Carcass Weight: A Classic Micro-Macro Paradox in Agriculture, Cornhusker Economics, Institute of Agriculture & Natural Resources, Department of Agriculture Economics, University of Nebraska – Lincoln, March 20, 2002, (“So, if quantity increased one percent from q1 to q2, and if demand remained constant, then price would be expected to decrease 1.4 to 2.5 percent).

Canadian herd. The price for domestic cattle increased a remarkable \$26 per cwt between May 2003, the month when Canadian cattle imports were curtailed, and October 2003, just five months later (chart 16). This domestic price increase occurred even after beef imports from Canada were resumed in August 2003. This price increase represents an unprecedented per head increase of \$325 for an average Nebraska Direct Choice steer weighing 1,250 pounds.

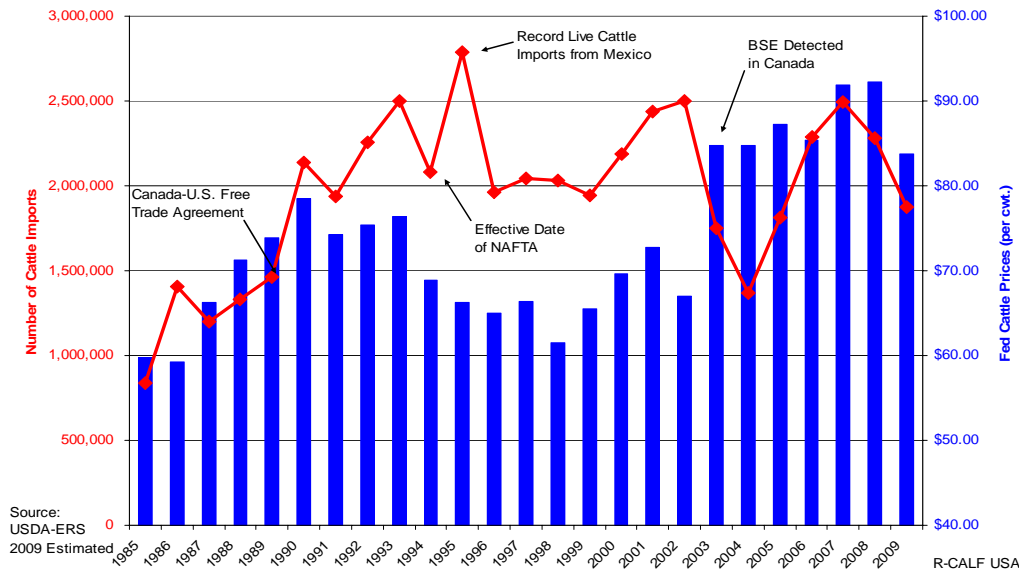
CHART 16: 2003 Cattle Price Response to Curtailment of Canadian Imports



R-CALF USA urges the Justice Department and USDA to investigate the beef packers' practice of strategically using imported cattle to reduce the domestic price of fed cattle. Approximately 1.5 million cattle are imported annually from Canada,⁶⁷ representing approximately 4 percent of the 34 million cattle slaughtered annually in the United States. Yet, there appears a significant negative correlation between the number of head imported and the price of domestic cattle (chart 17).

⁶⁷ Livestock and Meat Trade Data, Cattle: Annual and Cumulative Year-to-Date U.S. Trade (Head), USDA, ERS (Canadian cattle imports totaled 1.4 and 1.6 million head in 2007 and 2008, respectively), available at <http://www.ers.usda.gov/data/meattrade/CattleYearly.htm>.

CHART 17: RELATIONSHIP BETWEEN CATTLE IMPORTS AND FED CATTLE PRICES



It does not appear that USDA currently has accurate modeling capabilities to evaluate the impact to the U.S. cattle industry from the beef packer’s strategic use of imported cattle to manage domestic cattle prices. When USDA issued its 2005 final rule to allow Canadian cattle less than 30 months of age into the United States, it projected that the largest decline in U.S. fed cattle prices would occur in the first or second quarter of the year following the resumption of Canadian cattle imports. USDA estimated price declines during the first and second quarter ranging from a low of \$3.10 per cwt. to a high of \$6.05 per cwt.⁶⁸ However, during the third and fourth quarters following the resumption of Canadian cattle imports, U.S. fed cattle prices fell from \$96.50 per cwt. in December 2005 to \$79.10 per cwt. in May 2006, a decline of \$17.40 per cwt. – nearly three times greater than what USDA projected for the upper boundary of expected losses.⁶⁹

It is evident that imported cattle have a more severe impact on domestic cattle prices than is currently estimated by USDA. Moreover, these imported cattle appear to defy the transportation limits that constrain the majority of shipments of domestic fed cattle to within approximately a 300-mile radius of beef packing plants. Based on information and belief, fed cattle from Canada are transported exceedingly long distances to packing plants in the United States. R-CALF USA speculates that U.S. beef packers likely are slaughtering these imported cattle at a loss in order to satisfy the weekly demand for live cattle, which would enable beef packers to avoid bidding more aggressively for domestic cattle. If this, in fact, is occurring, then the beef packer likely is more than making up the loss from the procurement of the relatively few imported cattle with the greater savings generated from holding prices for the much greater volume of domestic cattle

⁶⁸ See Economic Analysis Final Rule, Bovine Spongiform Encephalopathy: Minimal Risk Regions and Importation of Commodities, USDA, Animal and Plant Health Inspection Services, Dec. 20, 2004.

⁶⁹ See Choice Beef Values and Spreads and the All-Fresh Retail Value, USDA, ERS, available at <http://www.ers.usda.gov/Data/meatpricespreads/Data/beef.xls>, downloaded on December 19, 2006.

below what a competitive market would otherwise dictate. The Justice Department and USDA should investigate the beef packers' procurement practices for imported cattle.

4. Beef Packers Create Market Access Risk for Sellers in the Final Cattle Market

The combination of packer concentration, the perishable nature of slaughter-ready cattle and the weekly bounding of demand creates market access risk for U.S. cattle producers within the U.S. cattle market. The 2007 GIPSA Livestock and Meat Marketing Study (LMMS) defines market access risk as "the availability of a timely and appropriate market outlet."⁷⁰ This risk is particularly significant because fed cattle are perishable commodities that must be sold within a fairly narrow time frame, otherwise they will decrease in value.⁷¹

The beef packers have already achieved the ability to create market access risk and now function as powerful gatekeepers between cattle producers and the final cattle market. Under the current level of beef packer concentration, there is already evidence that cattle feeders are subjected to market power and are foregoing revenues to avoid market access risk. The LMMS found that "[t]ransaction prices associated with forward contract transactions are the lowest among all the procurement methods [including cash market procurement methods],"⁷² and proffered that the results of the study may suggest that "farmers who choose forward contracts are willing to give up some revenue in order to secure market access . . ."⁷³

Based on information and belief, it is market access risk that entices cattle feeders in the final cattle market to enter one or more of the captive supply arrangements offered by the beef packers. Researchers have found that individual producers within the U.S. cattle industry will agree to sign captive supply contracts even while knowing that the aggregate effect of captive supply contracts is to depress the cash market price and make all producers, including him/herself, worse off.⁷⁴ The researchers explained that it is the producer's inability to coordinate action that enables a packer to obtain acceptance for exclusionary contracts, and "as long as the producer is offered at least as much as could be received in the spot market in the equilibrium with captive supplies, the producer's equilibrium strategy is to ACCEPT the contract."⁷⁵ Based on this finding, U.S. live cattle producers are defenseless against the monopsony power exercised by the beef packers to shift ever increasing volumes of cattle from the cash market to one or more of the beef packers' captive supply procurement options.

⁷⁰ GIPSA Livestock and Meat Marketing Study, January 2007, Volume 3, at 5-4, available at http://archive.gipsa.usda.gov/psp/issues/livemarketstudy/LMMS_Vol_3.pdf.

⁷⁰ *See Ibid.*

⁷⁰ *Id.*, at 2-36.

⁷¹ *See Ibid.*

⁷² *Id.*, at 2-36.

⁷³ *Ibid.*

⁷⁴ Captive Supplies and the Cash Market Price: A Spatial Markets Approach, Mingxia Zhang and Richard J. Sexton, *Journal of Agricultural and Resource Economics*, 25(1): 88-108, at 98, attached hereto as Exhibit 8.

⁷⁵ *Ibid.*

5. The Price of Domestic Cattle Is Sensitive to Procurement Practices that Shift Cattle from the Cash Market to Captive Supply Arrangements

As confirmed by the LMMS, the cash cattle market is sensitive to shifts in cattle procurement methods. While beef packers have significantly reduced the number of its market outlet gatekeepers through horizontal consolidation, thus exacerbating market access risk for all cattle producers in the final cattle market, beef packers have simultaneously increased their use of non-traditional contracting and other cattle procurement methods that enable them to more effectively exercise their manifest market power. These non-traditional cattle procurement methods increase the vertical coordination between the live cattle industry and the beef packing industry and include purchasing cattle more than 14 days before slaughter (packer-fed cattle), forward contracts, and exclusive marketing and purchasing agreements, including formula contracts. Together, the four largest beef manufacturers employed such forms of “captive supply” contracting methods for a full 44.4 percent of all the cattle they slaughtered in 2002.⁷⁶ And, use of these captive supply methods has been increasing rapidly, rising 37 percent from 1999 to 2002.⁷⁷ The LMMS found that approximately 38 percent of cattle were procured by such non-traditional methods during the period October 2002 through March 2005.

Captive supplies have been shown to increase the instability of prices for cattle producers and hold down cattle prices.⁷⁸ Over the past 20 years studies have supported the idea that buyer concentration in cattle markets systematically suppressed prices, with price declines found to range from 0.5 percent to 3.4 percent.⁷⁹ As average prices for cattle are artificially depressed and become more volatile, due to these captive supply procurement methods, it is cattle producers who pay the price, even when broader demand and supply trends should be increasing returns to producers.⁸⁰ Despite this negative outcome, cattle producers continue to opt into captive supply arrangements because those producers have few other attractive marketing choices in an industry that effectively reduces access to market outlets.⁸¹ Furthermore, while such captive supply arrangements may appear attractive to an individual producer at a given point in time, the collective impact of these contracting practices on the market as a whole is harmful to the live cattle industry. As previously discussed, producers acting individually are not in the position to change these dynamics of the market.

It is informative for the Justice Department and USDA to analyze the recent transformation of the U.S. hog industry. USDA data suggest that the contraction of the U.S. live hog industry was more severe than was experienced in the U.S. live cattle industry, despite a smaller four-firm concentration ratio in the pork packing industry. This likely is because of the measurable difference in the degree to which the concentrated pork packing industry was able to exercise its inherent market power. For example, the pork packing industry exploited the live hog industry's

⁷⁶ See RTI International, “Spot and Alternative Marketing Arrangements in the Livestock and Meat Industries: Interim Report,” Report Prepared for the Grain Inspection, Packers, and Stockyard Administration, U.S. Department of Agriculture, July 2005 at 3-15.

⁷⁷ See *id.* at 3-17.

⁷⁸ See John M. Connor, “The Changing Structure of Global Food markets: Dimensions, Effects, and Policy Implications,” Staff Paper #3-02, Department of Agricultural Economics, Purdue University, February 2003, at 7-8.

⁷⁹ See *Ibid.*

⁸⁰ See *id.*, at 8.

⁸¹ See *Ibid.*

greater propensity toward vertical integration of its entire live hog production cycle – from birth to slaughter – and captured earlier in the industry’s concentration process a larger proportion of slaughter-ready hogs before they entered the open cash market, where the base-price for all hogs marketed continues to be established. The LMMS found that during the period October 2002 through March 2005, the pork packing industry captured 20 percent of its slaughter-ready hogs through the alternative procurement method of direct ownership;⁸² about 57 percent of hogs were captured through marketing contracts, forward contracts or marketing agreements; and fewer than 9 percent of hogs were procured in the open market.⁸³ Among the conclusions of the LMMS was: “Based on tests of market power for the pork industry, we found a statistically significant presence of market power in live hog procurement.”⁸⁴ Further, the LMMS concluded that there was a casual relationship between the increased use of non-cash hog procurement methods and lower prices for hogs:

Of particular interest for this study is the effect of both contract and packer-owned hog supplies on spot market prices; as anticipated, these effects are negative and indicate that an increase in either contract or packer-owned hog sales decreases the spot price for hogs. Specifically, the estimated elasticities of industry derived demand indicate

- a 1% increase in contract hog quantities causes the spot market price to decrease by 0.88%, and

- a 1% increase in packer-owned hog quantities causes the spot market price to decrease by 0.28%.

A higher quantity of either contract or packer-owned hogs available for sale lowers the prices of contract or packer-owned hogs and induces packers to purchase more of the now relatively less expensive hogs and purchase fewer hogs sold on the spot market.⁸⁵

The LMMS found that procurement methods that facilitated the exercise of market power by the concentrated pork packing industry are currently less developed in the concentrated beef packing industry. For example, the study found that only 5 percent of live cattle were procured through packer-ownership and only 33.3 percent of cattle were procured by forward contracts and marketing agreements, leaving nearly 62 percent of the cattle procured through the open market,⁸⁶ which, like in the hog market, continues to set the base price for all marketed cattle. Although alternative procurement methods for cattle destined for slaughter are currently less developed than for hogs destined for slaughter, the LMMS nonetheless found a causal relationship between the increased use of alternative slaughter-ready cattle procurement methods and a decrease in the cash market price for slaughter-ready cattle under the current structure of

⁸² See GIPSA Livestock and Meat Marketing Study, January 2007, Volume 4, at 2-13, available at http://archive.gipsa.usda.gov/psp/issues/livemarketstudy/LMMS_Vol_4.pdf.

⁸³ See *Ibid.*

⁸⁴ See *id.*, at ES-3.

⁸⁵ See *id.*, at ES-2, 3.

⁸⁶ See *id.*, at ES-4.

the beef packing industry. The LMMS found that a 10 percent shift of the volume of cattle procured in the open market to any one of the alternative procurement methods is associated with a 0.11 percent decrease in the cash market price.⁸⁷ The comprehensive econometric analysis documented in *Pickett v. Tyson Fresh Meats, Inc.*, which covered the period 1994-2004, showed an even greater sensitivity to shifts in cattle procurement. The analysis showed that for each 1% increase in captive supply cattle, cattle prices decreased 0.155%.⁸⁸

Alarming, the beef packers are now shifting unprecedented volumes of cattle from the cash market and to their forward contracts and formula contract schemes. USDA reports that in the Texas-Oklahoma-New Mexico region, the cash market in 2009 has been reduced to less than 34 percent (including cash and negotiated grid transactions) (chart 18). And, forward contracting and formula contracting now represents over 66 percent of all fed cattle transactions in the region. Similar shifts have occurred in the Kansas region while Nebraska remains the only regions where cash transactions represent more than 41 percent of fed cattle transactions.

Not reported in these USDA data are the volumes of packer-owned cattle procured from each of these regions. Nationally, GIPSA reports that in 2007, packer-owned cattle represented between 5 percent and 10 percent of the cattle procured by beef packers.⁸⁹ However, the Justice Department and USDA must be aware that formula contracts accord beef packers nearly identical buying power as do packer-owned cattle. C. Robert Taylor, Auburn University, states that an affidavit contained in the *Pickett v. Tyson* litigation record reveals an acknowledgement by former IBP (now Tyson) CEO Bob Peterson on how formula contracts give beef packers comparable, if not superior, leverage in the market than do packer-owned cattle. Excerpts from Taylor's report of the affidavit include:⁹⁰

CHART 18

Texas-Oklahoma-New Mexico Breakdown of Volume by Purchase Type					
	2005	2006	2007	2008	2009
Cash	47.2%	42.5%	36.7%	31.5%	26.1%
Formula	42.2%	42.2%	48.4%	53.3%	60.7%
Forward Contract	3.1%	5.0%	4.4%	5.8%	5.4%
Negotiated Grid	7.5%	10.3%	10.5%	9.3%	7.8%

Source: USDA Market News, St Joseph, MO

Kansas Breakdown of Volume by Purchase Type					
	2005	2006	2007	2008	2009
Cash	50.6%	47.3%	44.8%	41.7%	39.3%
Formula	44.8%	46.0%	48.5%	48.0%	52.6%
Forward Contract	2.8%	5.4%	5.4%	7.8%	7.1%
Negotiated Grid	1.8%	1.3%	1.3%	2.4%	1.0%

Source: USDA Market News, St Joseph, MO

Nebraska Breakdown of Volume by Purchase Type					
	2005	2006	2007	2008	2009
Cash	64.5%	63.7%	64.7%	61.1%	60.4%
Formula	18.3%	16.8%	17.8%	17.8%	22.6%
Forward Contract	5.9%	9.7%	7.8%	14.7%	9.0%
Negotiated Grid	11.4%	9.7%	9.6%	6.5%	8.0%

Source: USDA Market News, St Joseph, MO

⁸⁷ See GIPSA Livestock and Meat Marketing Study, January 2007, Volume 3, at ES-5, available at http://archive.gipsa.usda.gov/psp/issues/livemarketstudy/LMMS_Vol_3.pdf.

⁸⁸ See Trial Transcript in *Pickett et al. v. Tyson Fresh Meats, Inc. (IBP, Inc.)* Civil No. 96-A-1103 N, U.S. District Court for the Middle District of Alabama, Northern Division.

⁸⁹ See 2008 Annual Report, Packers & Stockyards Program, USDA, GIPSA, March 1, 2009, at 59, available at http://archive.gipsa.usda.gov/pubs/2008_psp_annual_report.pdf.

⁹⁰ The American Antitrust Institute, Working Paper No. 07-08, Legal and Economic Issues with the Courts' Rulings in *Pickett v. Tyson Fresh Meats, Inc.*, a Buyer Power Case, C. Robert Taylor, Auburn University, at 9, available at http://www.antitrustinstitute.org/archives/files/AAI_Taylor_WP07-08_033020070955.pdf.

On July 26, 1994 Peterson stated:

'I don't know if we should be proud or ashamed but I'm telling you we started formula pricing. Why did we do it? So we have the same leverage our competition had. And we feed cattle through the process of formula pricing.'

'Well, we aren't going to change. We will have formula—that is our way of feeding cattle.'

On December 2, 1994, he said:

'... I told your industry right here at the KLA convention (in 1988) that if it allowed packers to feed their own cattle, IBP (Tyson) would do whatever was necessary to level the playing field. Ladies and gentlemen, the leveling is called formula and contract buying. Thus far, we have been able to partially offset the leverage our competitors have by the use of formula cattle and contract buying. Will we stop doing it? No. Will we feed cattle? If we have to. As most of you know, our recent purchase of Lakeside Farm Industries in Canada includes a feedyard. I am only trying to tell you one thing. IBP (Tyson) will do whatever is necessary to remain competitive.'

These quotes directly contradict the belief that formula contracts were developed by cattle producers to provide them with additional marketing options, a belief that has been expressed to R-CALF USA in recent years. R-CALF USA urges the Justice Department and USDA to act swiftly to bring an end to the beef packers' anticompetitive practices of packer ownership of cattle and formula pricing.

6. The Demand for Live Cattle Is Bounded on a Weekly Basis

The packer demand for live cattle is bounded on a weekly basis by available slaughter capacity, which is a limiting factor on demand for cattle, i.e., slaughter capacity sets the weekly slaughter cattle-marketing limit.⁹¹ As a result of this weekly constraint, packers can suppress the weekly demand for cattle offered in the domestic cash market by finishing off their weekly supply needs with green cattle (i.e., cattle that have not yet reached their optimal slaughter weight) pulled from their captive supply holdings or, as stated above, by finishing off their week with imported cattle. The effect of this practice is to hold down or lower domestic prices and prevent a higher starting price for the beginning of each subsequent week.

⁹¹ See Beef Pricing and Other Contentious Industry Issues, Special Report, Kevin Grier and Larry Martin, George Morris Centre, March 16, 2004 (an analysis of the live versus beef price disparity in Canada).

7. Price Transparency is Limited in the U.S. Cattle Market

Transparency in the U.S. live cattle market is already limited as found by the GAO in 2005. The GAO reported on a number of deficiencies in the government's Livestock Mandatory Reporting system with regard to the transparency of the reporting system and accuracy of the data reported.⁹² Included among the deficiencies identified was the exclusion of a large percentage of cattle transaction data.⁹³ In addition to the lack of transparency and accuracy of marketing transaction data already impacting the U.S. live cattle industry, the so-called 3/70/20 confidentiality guidelines that structurally limit reports of transactions in concentrated regions likely are masking critical pricing information. The confidentiality guidelines that likely restrict or eliminate the reporting of currently reported cattle transaction data include the requirement that at least 3 reporting entities provide data at least 50 percent of the time during a 60-day period; no entity may provide more than 70 percent of the data during a 60-day period; and no entity may be the only reporting industry more than 20 percent of the time during a 60-day period.⁹⁴ It is inexplicable that concentrated packers are shielded from disclosing prices in any region in the United States and the Justice Department and USDA should investigate the extent to which unreported pricing data is impacting domestic cattle prices. In addition, the agencies should investigate both the disposition and impact of pricing data that result from transactions that occur outside the daily and weekly price reporting timeframes.

8. Beef Packers Have Superior Market Information, Particularly Those with Substantial Captive Supply Arrangements

As discussed above, the Livestock Mandatory Reporting system shields beef packers from disclosing market information under certain circumstances, thus affording them asymmetric information in the marketplace. In addition, beef packers with captive supplies have superior information than do cattle sellers regarding the number of additional cattle needed each week to maintain plant operations. Also, beef packers with contracts for the sale of beef to retailers are benefited by information regarding weekly output needs and future wholesale beef prices. The beef packers' access to critical marketing information not available to producers gives them considerable leverage over cattle sellers in the U.S. cattle market.

III. EVIDENCE OF EXTREME MARKET FAILURE IN THE U.S. CATTLE AND BEEF INDUSTRIES

The beef packers and their allied trade associations have long justified their ongoing attempts to capture greater control over the live cattle industry. Their claims include the achievement of increased efficiencies through economies of scale. And, as discussed above regarding TCFA's claim, they rationalize the adverse consequences of their actions, e.g., the exodus of industry

⁹² See U.S. Government Accountability Office, *Livestock Market Reporting: USDA Has Taken Some Steps to Ensure Quality, but Additional Efforts Are Needed*, GAO-06-202 (Dec. 2005).

⁹³ See U.S. Government Accountability Office, *Livestock Market Reporting: USDA Has Taken Some Steps to Ensure Quality, but Additional Efforts Are Needed*, GAO-06-202 (Dec. 2005), at 10.

⁹⁴ USDA Announces New Confidentiality Guidelines for Livestock Mandatory Reporting Program, U.S. Department of Agriculture, Release No. 0132.01, August 3, 2001.

participants and the dwindling cow herd, with claims of increased productivity that, they say, negates the need for the industry's previous numbers of either participants or cattle.

For example: in written testimony before the July 16, 2002, United States Senate Agriculture Committee hearing on packer ownership of livestock, the meatpacking industry's trade association, the American Meat Institute (AMI), testified: "Demand for consistent quality product has led many firms to exert greater control over the supply chain."

In its written testimony before the same July 16, 2002, Senate hearing, the National Cattlemen's Beef Association (NCBA) attached the executive summary of the Sparks Study to its testimony. Specifically, the NCBA commissioned Sparks Study states the following:

Packers use ownership of livestock to help control unit costs in a variety of ways. If this management tool is restricted, unit costs can be expected to increase (without increasing the value of the final product).⁹⁵

The Sparks Study asserts that direct ownership of livestock limits the packers' market risk, arguing that the futures market is insufficient for this purpose. Therefore, according to the Sparks Study, one of the few tools available to packers to offset the smaller margins associated with higher livestock prices is through direct ownership of raw production materials, i.e., livestock, which enables them to reduce their margin risk. The Sparks Study states, "The pressure to reduce costs force the search for low-cost livestock supplies (often at the expense of producer returns)."⁹⁶

The Sparks Study adds additional insight into the packing industry's rationale for supporting packer ownership of livestock as well as other means that contribute to vertical integration of their industry. The Sparks Study acknowledges:

For many meat packers, integration between the packing and feeding stages of livestock production is seen as an effective vehicle to reduce market risk exposure and loss of such a valuable tool increases their costs . . .⁹⁷ and,

Vertical integration often attracts investors because of the negative correlation between profit margins at the packing stage and the feeding stage.⁹⁸

It is clear that the current market structure affords beef a distinct pricing advantage over the U.S. cattle market, and this pricing advantage is disrupting the competitiveness of the U.S. cattle industry. Also obvious is the inherent disadvantage faced by domestic cattle feeders that must first compete against the same beef packers when purchasing feeder cattle in the feeder cattle market that they must later sell to in the final cattle market when their cattle are finished.

⁹⁵ Sparks Companies Inc., "Potential Impacts of the Proposed Ban on Packer Ownership and Feeding of Livestock", A Special Study, (March 18, 2002) at 40.

⁹⁶ *Id.* at 22.

⁹⁷ *Id.* at 24.

⁹⁸ *Id.* at 24.

Perhaps the most compelling testimony regarding the onset of packer ownership and the advent of captive supply procurement methods, and their implications, is again provided by C. Robert Taylor, Auburn University, who reports that the affidavit in the *Pickett v. Tyson* litigation record contains quotes from Bob Peterson, former CEO of the nation's largest meatpacker at the time – IBP. According to C. Robert Taylor, the affidavit filed in the *Pickett v. Tyson* lawsuit contains the following record of Peterson's statements:⁹⁹

In a 1988 talk to the Kansas Livestock Association, Peterson maintained,

'...our competitors are promoting contracts ... and seeking more. These (forward) contracts coupled with packer feeding could represent a significant percentage of the fed cattle during certain times of the year... Do you think this has any impact on the price of the cash market? ... you bet! ... We believe that it's having a significant impact on the market—on the cash market place.'

'...we believe that some of those who are feeding cattle and using forward contracting are creating aberrations within the market place by coming in and out of the market; that is not reflecting the true value of the cash market.'

'But with the packers in the feeding business and forward contracting, there's going to be a major, major shift against the leverage system.'

'In my opinion the feeder can't win against the packer in the real fair play if we go into the feeding and the hedging program.'

'Do you think that if we had a million cattle on feed and we thought cattle were going to get higher we'd kill ours first and wait for yours until last? Or do you think we'd kill yours first and wait for ours until last? Do you think if it's going down we're going to buy yours and wait for ours until last? This is pretty basic. Boy Scouts and Girl Scouts are nice, but when you get back to money in the bank and the facts, I'm telling you the facts.'

In 1994, after IBP had entered into extensive captive supply arrangements, Peterson stated:

'... not formula cattle but packer-fed cattle, which can be killed early or late to fill a particular time frame, be it a day or a week grant the packer far greater flexibility to move in and out of the

⁹⁹ The American Antitrust Institute, Working Paper No. 07-08, Legal and Economic Issues with the Courts' Rulings in *Pickett v. Tyson Fresh Meats, Inc.*, a Buyer Power Case, C. Robert Taylor, Auburn University, available at http://www.antitrustinstitute.org/archives/files/AAI_Taylor_WP07-08_033020070955.pdf.

market. On the way down (in price), he kills his cattle first and on the way up, last.'

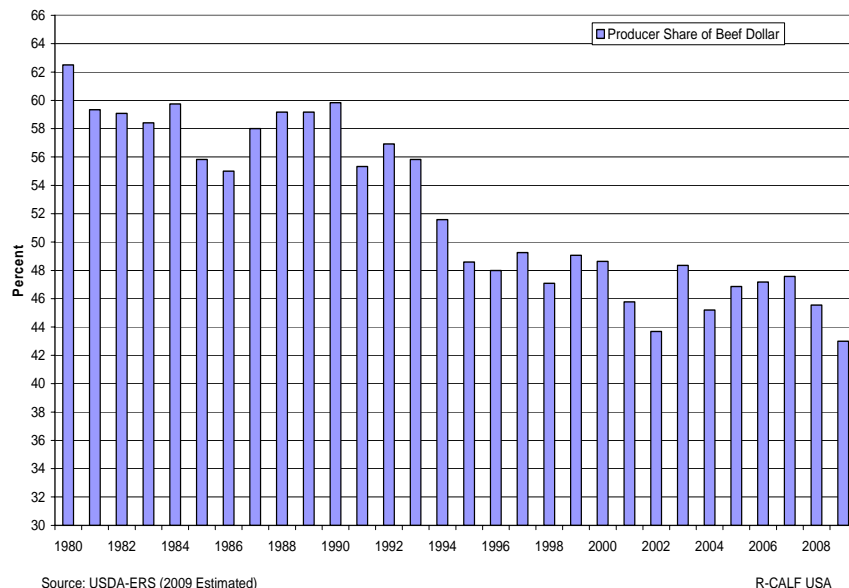
Armed with industry concentration, packer-owned cattle and their new cattle procurement schemes since the late '80s, the dominant beef packers have created a marketplace now replete with evidence of market failure caused by abusive monopsony power that is harming cattle producers and beef consumers alike.

A. The Lost Share of the Consumer's Beef Dollar Is Evidence of Market Failure

In 1980, U.S. cattle farmers and ranchers who sold cattle in the final cattle market received 63 percent of each dollar paid by consumers for retail beef cuts derived from a "standard animal, cut up in a standard way at the packing plant, and sold in standard form through the retail store."¹⁰⁰ R-CALF USA refers to this percentage as the producers' share of the consumers' beef dollar. Based on the producers' monthly average share of the consumers' beef dollar from January 2009 through November 2009, the producers' share of the consumers' beef dollar, for the same standard animal and the same standard cuts that were measured in 1980, will fall to only 43 percent in 2009, representing a 20 percent decline (chart 19).

These data calculated by USDA Economic Research Service (ERS) are not influenced by an increase in value-added beef products.¹⁰¹ The ERS emphatically states: "Analysts who cite increasing value-added as a factor in pork and beef price spreads misunderstand how these are calculated."¹⁰² Thus, the producers' lost share of the consumers' beef dollar indicates that someone in the beef supply chain is capturing the cattle producers' competitive market share of the value of retail beef. This is evidence of severe market failure caused by abusive monopsony power. If U.S. cattle producers in November 2009 received the same share of the consumers' beef dollar they received in 1980, the nominal value of their fed cattle

CHART 19: U.S. Cattle Producers' Share of Consumers' Beef Dollar
1980-2009



¹⁰⁰ Beef and Pork Values and Price Spreads Explained, USDA, ERS, May 2004, at 4, available at <http://www.ers.usda.gov/publications/ldp/APR04/ldpm11801/ldpm11801r.pdf>.

¹⁰¹ See *id.*, at 2.

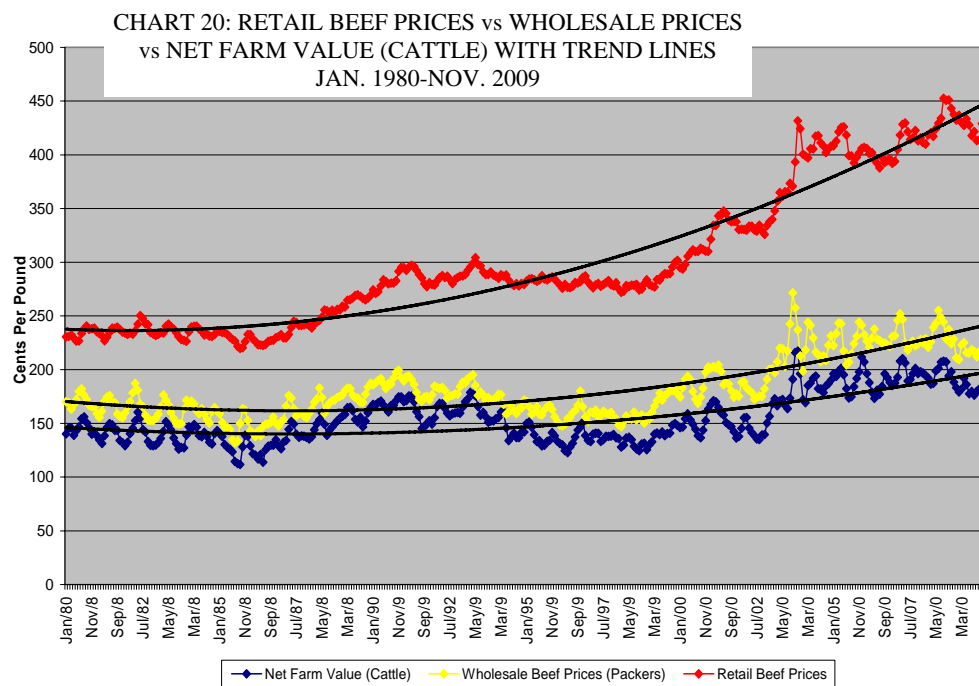
¹⁰² *Ibid.*

would have been \$122 per cwt, which is \$37 above the actual November 2009 5-market steer price of \$84.50 per cwt.¹⁰³

B. Increasing Price Spreads Between Ranch Gate and Wholesale, and Ranch Gate and Retail Are Evidence of Market Failure

In addition to the clarification that its price spread data is not influenced by increased value-added beef products, the ERS further states that its price spread data can be used to “measure the efficiency and equity of the food marketing system,”¹⁰⁴ and “increasing price spreads can both inflate retail prices and deflate farm price.”¹⁰⁵ The price spreads between ranch gate prices (i.e., cattle prices) and wholesale prices (i.e., prices received by beef packers) and ranch gate and retail prices (i.e., prices paid by consumers) have been steadily increasing over time (chart 20). According to ERS, “[h]igher price spreads translate into lower prices for livestock,”¹⁰⁶ innovative technologies can reduce price spreads and economic efficiency increases when price spreads drop,¹⁰⁷ and “[b]oth consumers and farmers can gain if the food marketing system becomes more efficient and price spreads drop.”¹⁰⁸

It is clear that both consumers and producers are being harmed by the current system that is creating increased price spreads, which means the marketplace is becoming less innovative and less inefficient. USDA found in 2004 that “the total price spreads show a weak upward trend when corrected



¹⁰³ See Beef Values and Price Spreads Data Sets, U.S. Department of Agriculture, Economic Research Service (calculation based on Nov. 2009 Choice retail beef value at 429.2 cents per pound: $(429.2 \times .63) + \text{byproduct value of } 22.6 \text{ divided by } 2.4 \text{ ERS conversion factor} = \122.1 per cwt.), available at <http://www.ers.usda.gov/Data/meatpricespreads/>

¹⁰⁴ Beef and Pork Values and Price Spreads Explained, U.S. Department of Agriculture, Economic Research Service, at 3.

¹⁰⁵ *Id.* at 2.

¹⁰⁶ *Id.*, at 8.

¹⁰⁷ *Id.*, at 3.

¹⁰⁸ *Ibid.*

for inflation,”¹⁰⁹ and this upward trend has only worsened since 2004. The ever-increasing price spread between ranch gate values for cattle and retail prices for beef is evidence of market failure caused by the exercise of market power that is exploiting both consumers and producers.

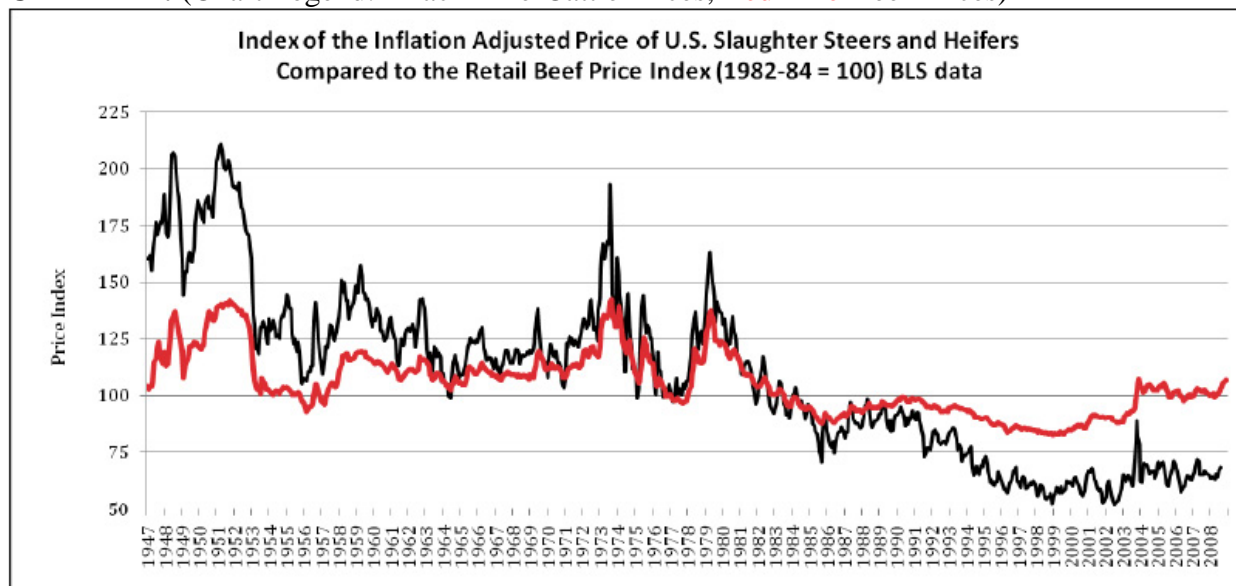
C. The Disconnect Between Cattle Prices and Beef Prices Is Evidence of Market Failure

C. Robert Taylor, economist at Auburn University, compared inflation adjusted prices for fed cattle to the inflation adjusted prices for retail beef from 1947 to 2008 (chart 21). His comparison shows a close, synchronous relationship between the price index for cattle and the price index for beef from about 1960 to 1985, after which two significant changes occurred: First, the beef price index rose above the cattle price index. Second, the synchronous relationship between the two indices ended and the spread between the indices has increased through 2008. These two changes: a clear disconnect between cattle and beef prices and the ever-widening spread between the two indices, is evidence of market failure caused by abusive monopsony power.

Chart 21 reveals another important phenomenon: from the late ‘80s to the 2003-2004 timeframe, the fed cattle price index was in a death spiral, while the beef price index remained comparatively constant. In 2003 an anomaly occurred in the U.S. cattle market when imports of Canadian cattle and beef were temporarily suspended following the discovery of BSE in Canada. Suddenly, U.S. beef packers were unable to access their captive supply cattle in Canada for slaughter in the United States. As indicated by the abrupt upward spike in the fed cattle index in the 2003-2004 timeframe, the death spiral illustrated by the fed cattle price index was reversed. R-CALF USA believes the curtailment of Canadian cattle imports in 2003 caused the beef packers to lose the significant control accorded them by those imports over the price of domestic cattle. As a result, the beef packers’ control over U.S. cattle prices temporarily slipped through their fingers and the U.S. cattle industry was serendipitously granted a temporary reprieve from the beef packers’ abusive market power. The relationship between fed cattle prices and retail beef prices in 2009, however, strongly suggests that U.S. beef packers have now reacquired their significant control over the U.S. cattle market and are again exerting their abusive monopsony power over the U.S. cattle industry.

¹⁰⁹ See Beef and Pork Values and Price Spreads Explained, U.S. Department of Agriculture, Economic Research Service, at 10.

CHART 21: (Chart Legend: Black Line-Cattle Prices, Red Line-Beef Prices)



D. Long-Run Losses In the Final Cattle Market While Retail Beef Prices Remain at or Near Record Levels Is Evidence of Market Failure

According to USDA's High Plains Cattle Feeding Simulator, during the 37-month period from November 2006 through November 2009, U.S. cattle feeders who sold cattle in the final cattle market enjoyed only 7 profitable months and suffered 30 months of losses (chart 22). From July 2007 through March 2009 these cattle feeders suffered 22 months of consecutive losses, with losses at about \$300 per head during October 2008 through January 2009. Meanwhile, Choice retail beef prices, throughout this entire period, increased until reaching record highs in 2008 and have remained near those record high levels through November 2009.

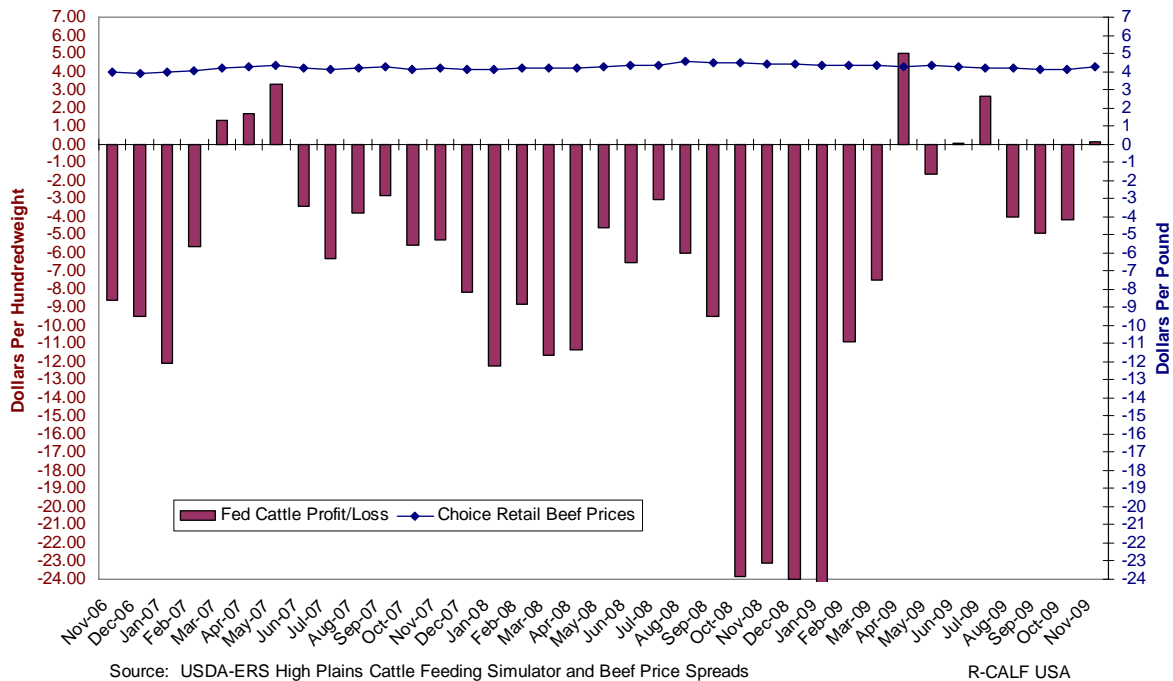
These data show that the U.S. cattle feeding sector alone lost \$6.4 billion since Jan. 1, 2007, which does not begin to include the consequential losses suffered in the feeder cattle market since that time.¹¹⁰ This conservative estimate of loss is based on USDA data that show the average loss from each of the 49 million head of fed cattle sold by U.S. cattle feeders was over \$48 in 2007, over \$150 in 2008, and over \$65 in 2009.¹¹¹

¹¹⁰ The loss of over \$6.4 billion was calculated by adding the average annual losses for each year as reported in the High Plains Cattle Feeding Simulator since Jan. 1 2007, and multiplying each year's loss by the number of fed cattle slaughtered during each year, e.g., the annual loss in 2008 was calculated by multiplying the 27 million fed cattle slaughtered in 2008 by that year's average annual per head loss to cattle feeders of \$150.75 per head for each 1,250 pound animal sold, resulting in a total loss of \$4.07 billion during that year alone.

¹¹¹ See High Plains Cattle Feeding Simulator, Data Sets, USDA, ERS, available at <http://www.ers.usda.gov/Publications/LDP/LDPTables.htm> ; see also, Livestock Slaughter 2008 Summary, USDA, NASS, March 2008, at 13, available at <http://usda.mannlib.cornell.edu/usda/current/LiveSlauSu/LiveSlauSu-03-06-2009.pdf> (The U.S. slaughtered approx. 27 million steers and heifers, not including cows and bulls, in each of the years 2007 and 2008.); see also Livestock Slaughter, USDA, NASS, August 2009, at 10, available at <http://usda.mannlib.cornell.edu/usda/nass/LiveSlau//2000s/2009/LiveSlau-08-21-2009.pdf> (The U.S. slaughtered approx. 15 million steers and heifers from Jan. through July, 2009.).

R-CALF USA is deeply concerned that these persistent losses likely have forced thousands, if not tens of thousands, of farmer-feeders to exit the industry in 2009. These farmer-feeders are less likely to have the deep pockets that their larger, corporate feedlot counterparts have to withstand such persistent and severe losses. These horrendous losses to cattle feeders while consumers continue to pay at or near record prices for beef are evidence of market failure caused by abusive monopsony power.

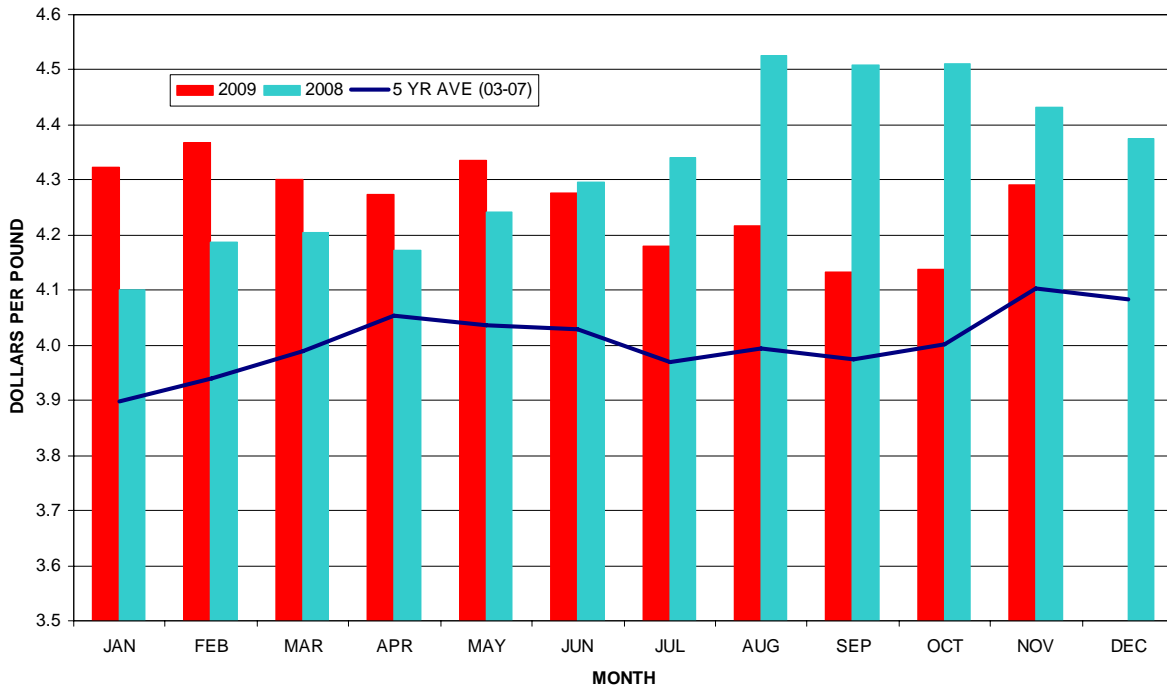
CHART 22: Fed Cattle Returns vs Choice Beef Prices



E. Record Beef Prices Paid by Consumers while Cow/Calf Producers Receive Severely Depressed Prices in the Feeder Cattle Market Is Evidence of Market Failure

While fed cattle sellers in the final cattle market suffered horrendous, long-run losses at the same time consumers continued to pay record and near-record prices for beef, sellers in the feeder cattle market likewise suffered losses due to severely depressed prices for their lighter feeder calves. In 2008 and 2009, the average monthly prices for Choice retail beef remained well above the previous five-year average (2003-2007), reaching record highs in the second-half of 2008 and remaining at historically high levels through November 2009 (chart 23 (a)).

CHART 23 (a): RETAIL CHOICE BEEF PRICES

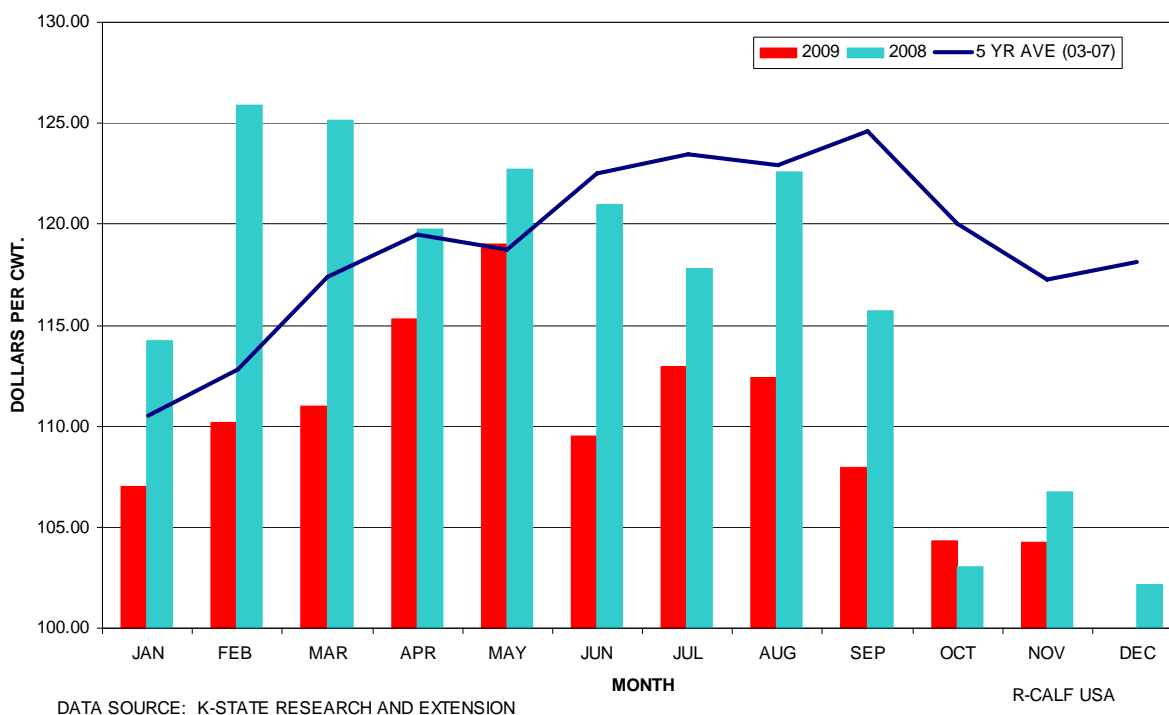


SOURCE: USDA ERS

R-CALF USA

Despite persistently high Choice retail beef prices paid by consumers, U.S. cow/calf producers in 2008 and 2009 who sold their cattle in the feeder cattle market were relegated to a market that returned prices well below the previous five-year average (2003-2007) (chart 23 (b)). Only during the first 5 months of 2008 did cow/calf producers who sold cattle weighing between 500 pounds and 600 pounds receive prices above the previous five-year average. From June 2008 through November 2009, these cattle producers have received persistently low prices. These depressed prices that have now permeated the feeder cattle market while consumers pay record and near record prices for beef is evidence of severe market failure caused by abusive monopsony power.

CHART 23 (b): MONTHLY PRICES FOR KANSAS 5-6 CWT. STEERS



F. The Disruption of the U.S. Cattle Cycle Is Evidence of Market Failure

The GAO explains that the U.S. cattle industry is subject to a historical cycle, referred to by “increases and decreases in herd size over time and [] determined by expected cattle prices and the time needed to breed, birth, and raise cattle to market weight,” factors that are complicated by the fact that “[c]attle have the longest biological cycle of all meat animals.”¹¹² The cattle cycle historically occurred every 10-12 years, a function of the long biological cycle for cattle. USDA reports it consists of about 6 to 7 years of expanding cattle numbers, followed by 1 to 2 years in which cattle numbers are consolidated, then 3 to 4 years of declining numbers before the next expansion begins again.¹¹³ In 2002 USDA acknowledged that “the last cycle was 9 years in duration; the present cycle is in its thirteenth year, with two more liquidations likely.”¹¹⁴

Given its historical responsiveness to the competitive forces of supply and demand, the cattle cycle is the bellwether indicator of the competitiveness of the U.S. cattle industry. The last normal liquidation phase of the U.S. cattle cycle began in 1975 and ended in 1979, lasting the typical four years (chart 24). The next liquidation phase began in 1982 and ended in 1990, lasting

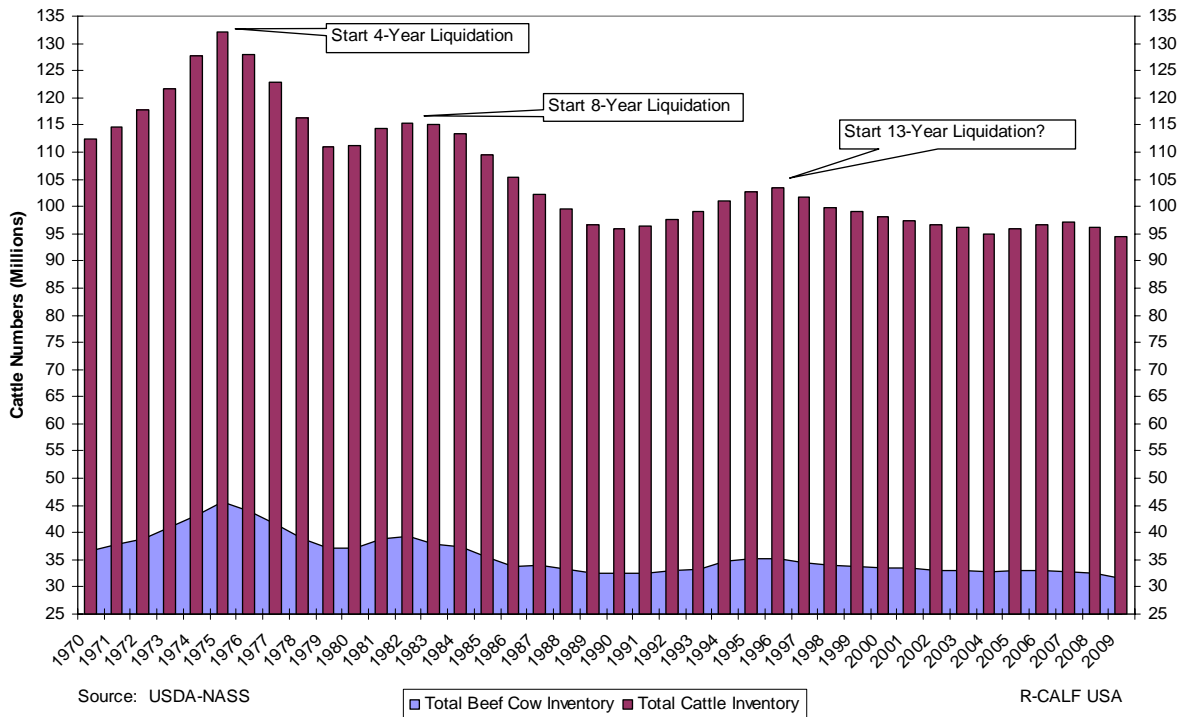
¹¹² Economic Models of Cattle Prices, How USDA Can Act to Improve Models to Explain Cattle Prices, U.S. Government Accountability Office (formally the General Accounting Office), (GAO-020246, March 2002, at 30.

¹¹³ Kenneth H. Mathews, Characteristics of Cattle Cycles, USDA, ERS, U.S. Beef Industry/TB-1874, November 2001.

¹¹⁴ Interagency Agricultural Projections Committee, *USDA Agricultural Projections to 2011, Staff Report WAOB-2002-1, February 2002*, available at <http://www.ers.usda.gov/publications/waob021/waob20021.pdf>, obtained from internet on October 17, 2002.

an unprecedented eight years. The liquidation phase that began in 1996 is ongoing today and has lasted an unprecedented 13 years, though it unsuccessfully tried to recover during 2005 through 2007 in response to the anomalous curtailment of Canadian cattle imports. In late 2007, USDA began cautioning the industry, stating that “[s]ome analysts suggest the cattle cycle has gone the way of the hog and dairy cow cycles.”¹¹⁵

Chart 24: Total U.S. Cattle Inventory and Beef Cow Inventory, January 1



There is no question that the historical cattle cycle is now disrupted, and the obvious trend since 1975 is an ever-shrinking cattle herd. It also is clear that the competition-induced demand/supply signals that once led to expectations about changes in cattle prices are no longer functioning properly. While cattle industry analysts ponder this phenomenon, in February 2008 USDA attributed a similar disruption that was occurring in the U.S. hog cycle to the hog industry’s new structure. USDA declared that the “New Hog Industry Structure Makes Hog Cycle Changes Difficult to Gauge,” and stated, “The structure of the U.S. hog production industry has changed dramatically in the past 25 years.”¹¹⁶ This “dramatically” changed structure includes the consolidation of the industry, where “fewer and larger operations account for an increasing share of total output.”¹¹⁷

¹¹⁵ Livestock, Dairy, & Poultry Outlook, USDA, ERS, Dec. 19, 2007, at 5, available <http://www.ers.usda.gov/Publications/LDP/2007/12Dec/ldpm162.pdf>.

¹¹⁶ Livestock, Dairy, & Poultry Outlook, USDA, ERS, Feb. 15, 2008, at 14, available at <http://www.ers.usda.gov/Publications/LDP/2008/02Feb/ldpm164.pdf>.

¹¹⁷ Hog Operations Increasingly Large, More Specialized, Amber Waves, USDA, ERS, February 2008, available at <http://www.ers.usda.gov/AmberWaves/February08/Findings/HogOperations.htm>.

As *was* the case in the hog industry, a functioning cattle cycle, itself, is recognized by USDA as an indicator of a competitive market. The USDA succinctly explained:

The cattle cycle refers to cyclical increases and decreases in the cattle herd over time, which arises because biological constraints prevent producers from instantly responding to price. In general, the cattle cycle is determined by the combined effects of cattle prices, the time needed to breed, birth, and raise cattle to market weight, and climatic conditions. If prices are expected to be high, producers slowly build up their herd size; if prices are expected to be low, producers draw down their herds.¹¹⁸

The recently acknowledged disruption of the historical U.S. cattle cycle, as discussed above, is clear evidence that competition has been severely reduced in the U.S. cattle market and, as USDA now succinctly concludes for the analogous hog industry cycle disruption, there is a causal relationship between this phenomenon and a changed industry structure marked by increased consolidation. The disrupted cattle cycle is clear evidence of market failure caused by abusive monopsony power.

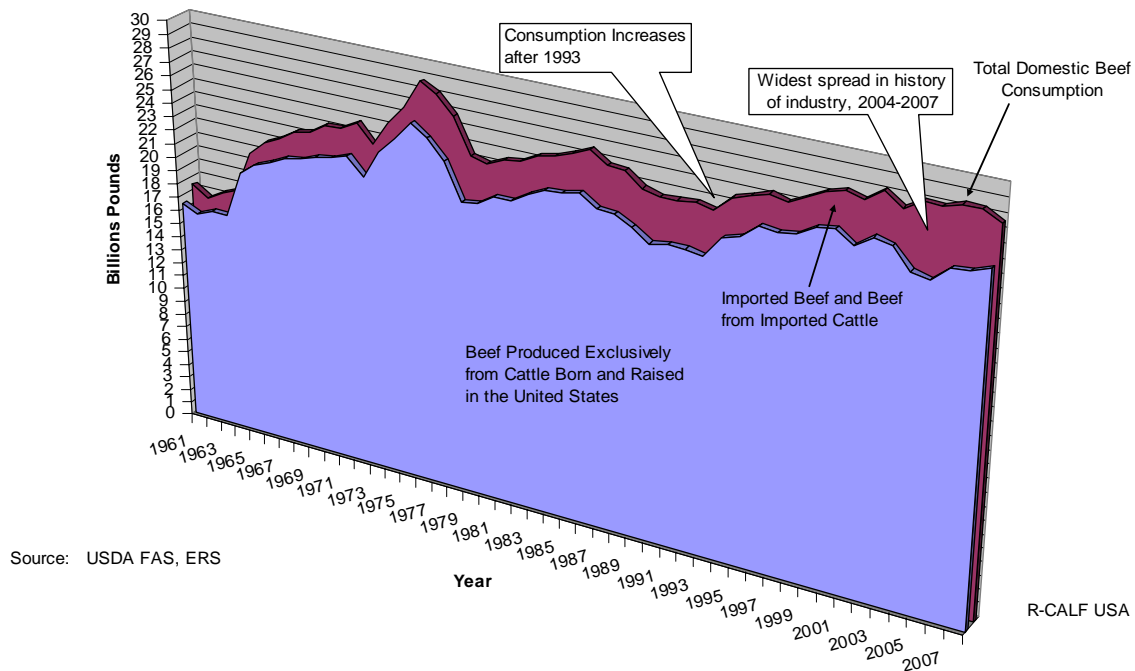
G. A Shrinking Cattle Industry with Stagnant Production in the Face of Growing Domestic Beef Consumption Is Evidence of Market Failure

Total domestic beef consumption peaked in 1976, subsided, and then began increasing significantly after 1993 (chart 25). In a competitive cattle industry, production would be expected to increase when beef consumption increases. However, the production of beef produced from cattle exclusively born, raised and slaughtered in the United States has not kept pace with the nation's appetite for beef. As stated above, since 1996 domestic beef production has remained relatively stagnant, though beef consumption has risen in recent years to nearly its peak 1976 level. In fact, from 2004 through 2007, the U.S. cattle industry experienced the largest shortfall in its history between its domestic beef production and the nation's beef consumption.

The shortfall in domestic production is being satisfied with imported beef and beef derived from imported cattle slaughtered in the United States. Thus a growing shortfall in domestic production means the U.S. cattle industry is losing market share in its own market and U.S. production is being systematically supplanted by foreign production. The domestic cattle industry would not be constrained from meeting the increase in consumption in its own market if the industry were competitive. The fact that the cattle industry is so constrained, as evidenced by the ongoing liquidation of its cattle herd and its stagnant production while consumption has increased, is evidence of severe market failure caused by abusive monopsony power.

¹¹⁸ Cattle: Background, Briefing Room, USDA, ERS, updated June 7, 2007, available at <http://www.ers.usda.gov/Briefing/Cattle/Background.htm>.

**CHART 25: Domestic Consumption in Excess of Domestic Production
 1961-2008**



H. Depressed Cattle Prices While Exports Reach Record Levels is Evidence of Market Failure

The beef packing industry has long assured the U.S. cattle industry that domestic cattle prices increase when U.S. beef exports increase. The NCBA testified before the USITC in November 2007 that, “In fact, the industry ‘rule of thumb’ is that U.S. beef exports in 2003 added about \$15/cwt or \$180 to each and every one of the roughly 27 million steers and heifers marketed that year.”¹¹⁹ The NCBA also asserted that the \$15 per cwt added export value to fed cattle translates into a \$22.20 per cwt (or \$166.50 per head) increase in the value of a 750 pound steer, and an increase of \$28.20 per cwt (or \$155.10 per head) increase in the value of a 550 pound steer.¹²⁰

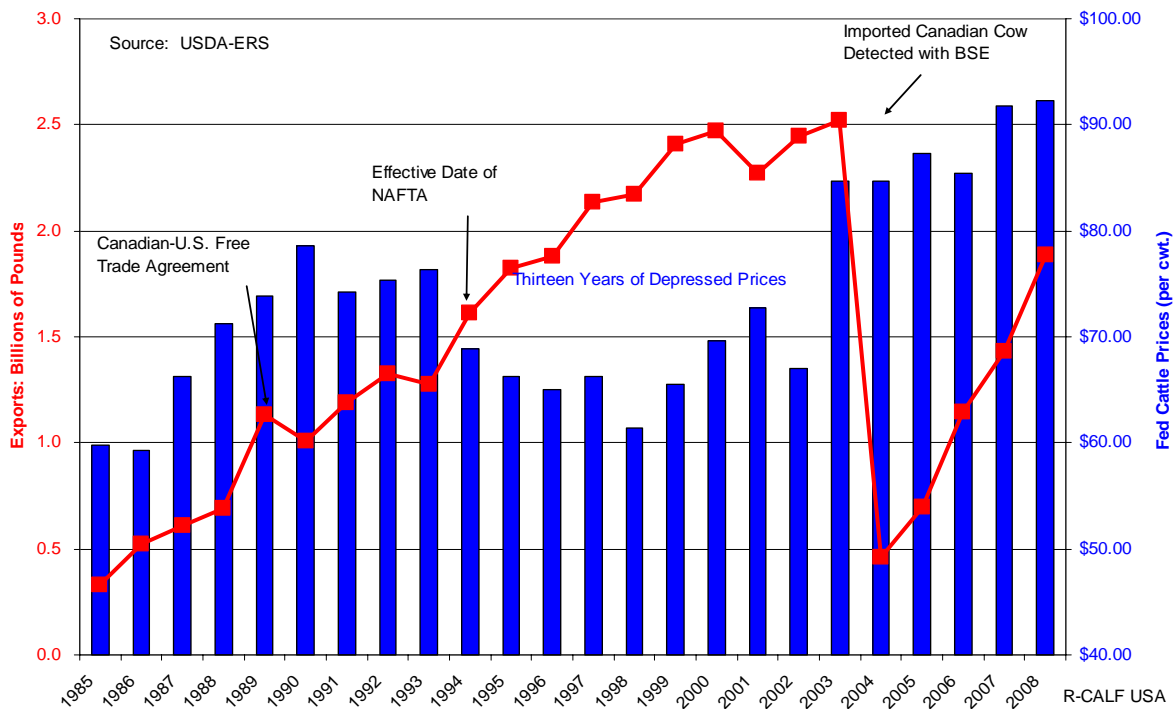
These beef-packing industry assertions regarding the benefits to live cattle producers from exports at 2003 levels are unfounded and demonstrably false. United States beef exports in the years leading up to 2003 were, in fact, comparable to 2003 levels at approximately 2.4 billion pounds in 1999, 2.5 billion pounds in 2000, 2.3 billion pounds in 2001, 2.5 billion pounds in

¹¹⁹ Memorandum of Record, Investigation No. 332-488, Concerning: Global Beef Trade: Effects of Animal Health, Sanitary, Food Safety, and Other Measures on U.S. Beef Exports, U.S. International Trade Commission, Nov. 15, 2007.

¹²⁰ See Special Report: How do Canadian Beef Imports Affect Our Business? Greg Doud, Chief Economist, NCBA, Issues Update 2004, Trade/Marketing/Economics, May-June 2004, available at https://www.beefusa.org/uDocs/canadian_20beef_20imports_20-_20mayjune_202004.pdf.

2002, and 2.5 billion pounds in 2003.¹²¹ Yet, the prices for U.S. fed cattle in the years leading up to 2003 were severely depressed: Per hundredweight Nebraska Direct Choice steer prices were only \$67.56 in 1999, \$69.65 in 2000, \$72.71 in 2001, \$67.04 in 2002, and then jumped to \$84.69 in 2003 following the curtailment of Canadian cattle imports that occurred on May 20 of that year.¹²² However, when U.S. beef exports fell to less than half a billion pounds in 2004, falling to a 19-year low, U.S. fed cattle prices rose to their highest nominal levels in history (chart 26), and so too did prices for all classes of cattle, including 750-weight and 550-weight cattle. Clearly, the economic benefits of increased beef exports are being captured by beef packers *before* they can reach the U.S. cattle market. The fact that historical evidence proves that increased beef exports *do not* translate into increased cattle prices, even when a competitive market would predict they should, is clear evidence of market failure caused by abusive monopsony power.

CHART 26: Relationship Between Export Volumes and Fed Cattle Prices



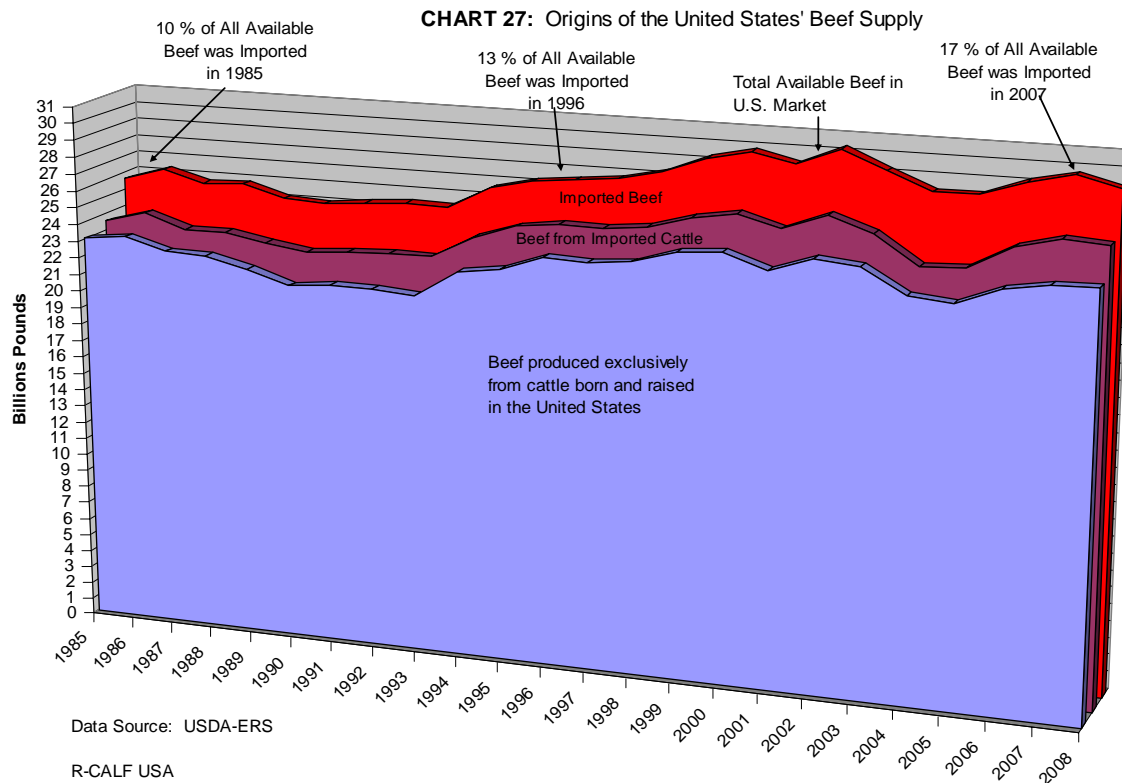
I. A Shrinking Cattle Industry That Is Simultaneously Losing Its Market Share of the Total Available Beef Supply Is Evidence of Market Failure

The total available beef supply includes all beef in the U.S. market that is available for domestic consumption and export. The phenomenon described immediately above, whereby cattle

¹²¹ See Beef and veal: Annual and cumulative year-to-date U.S. trade (carcass weight, 1,000 pounds), Data Sets, U.S. Department of Agriculture Economic Research Service, available at <http://www.ers.usda.gov/data/meattrade/BeefVealYearly.htm>.

¹²² See Livestock Prices, Red Meat Yearbook Data Sets, U.S. Department of Agriculture Economic Research Service, available at <http://usda.mannlib.cornell.edu/MannUsda/viewDocumentInfo.do?documentID=1354>.

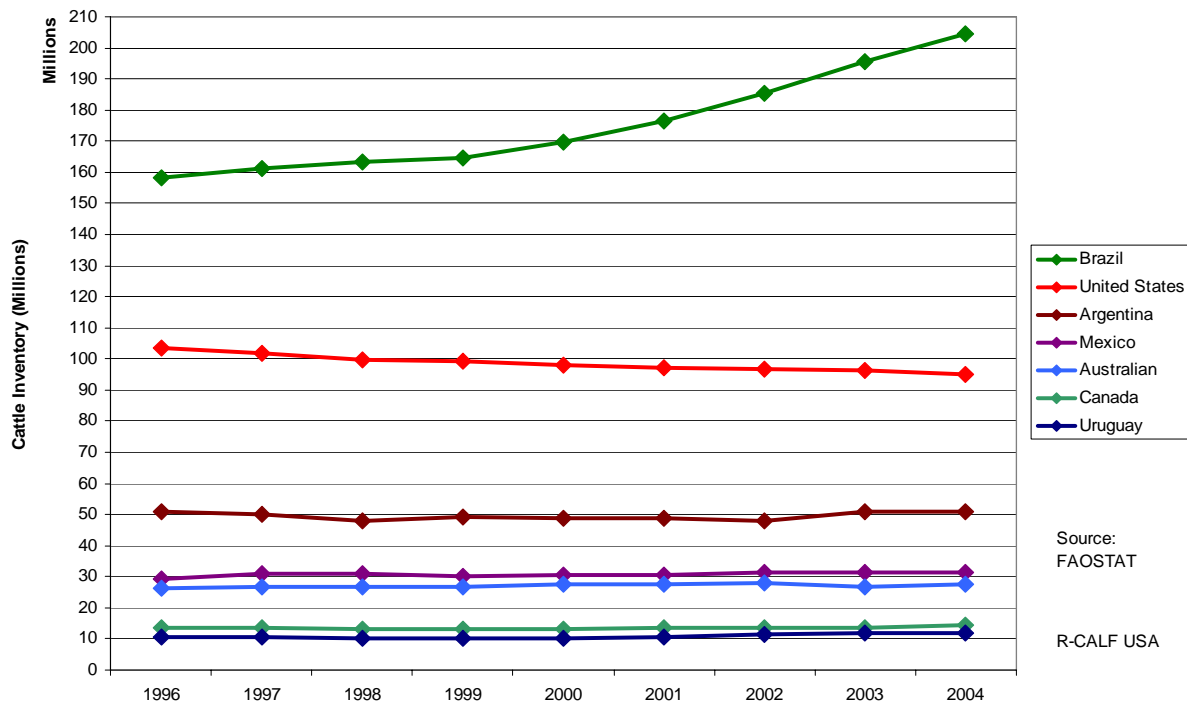
producers are not benefiting from increased exports, can be explained by the cattle industry's lost share of the total available beef supply (chart 27). As is readily discernable from the chart below, the U.S. cattle industry's share of the United States' total available beef supply has been systematically reduced since 1985. Because imports are capturing an ever increasing share of the domestic supply of beef, benefits from increased exports are unable to translate into higher domestic cattle prices. Instead, increased exports are offset by the increased imports and translate into additional profits for the beef packers that are strategically sourcing imported cattle and beef to increase their market leverage over domestic cattle prices, thus constraining domestic cattle production. The U.S. cattle industry's ongoing loss of its share of the United States' total available beef supply is evidence of market failure caused by abusive monopsony power.



J. A Shrinking U.S. Cattle Herd Size While Global Beef Competitors Were Expanding Their Cattle Herds Is Evidence of Market Failure

Beginning in 1996, when the U.S. began liquidating its cattle herd, and continuing through 2004, following the discoveries of BSE in Canadian-born cattle that disrupted global trade patterns, the United States was the *only* major beef exporting country that was appreciably reducing its cattle herd size (chart 28). Other major beef producing countries: Brazil, Mexico, Australia, Canada and Uruguay were all increasing the size of their respective herds, while Argentina's herd size remained relatively stable, decreasing only slightly throughout this period.

CHART 28: Pre-BSE Changes In World Cattle Herd Sizes



The United States is the worlds’ largest beef producer and was, during the period prior to 2004, the worlds’ second largest beef exporting country. It is counterintuitive that the U.S. cattle herd would have been shrinking during this prolonged period when its global competitors were expanding their herd sizes, and consequently their production capacity. The fact that the U.S. was shrinking its cattle herd and its production capacity during this period is indicates that the U.S. cattle industry was being unduly constrained and is evidence of market failure caused by abusive monopsony power.

IV. KNOWN OR SUSPECTED PRACTICES BY BEEF PACKERS THAT CONSTITUTE ANTICOMPETITIVE BEHAVIOR AND/OR VIOLATIONS OF ANTITRUST STATUTES

A. Coercive Threats to Cattle Producers to Advance Beef Packers’ Political Goals

The beef packing industry recently exacted its market power on the U.S. cattle industry for purposes of influencing national public policy; and, in doing so, imposed unnecessary costs and burdens on U.S. cattle producers, which costs and burdens U.S. producers could not avoid without eliminating or severely limiting their marketing options. In March 2003, beef packer IBP, Inc. (now Tyson) notified U.S. cattle producers that it would require producers to, *inter alia*, “Provide IBP, inc. access to your [producers’] records so that we [IBP] can perform random

producer audits . . .” and “Provide third-party verified documentation of where the livestock we [IBP] purchase from you [producers] were born and raised.”¹²³

This coercive threat to impose costly and burdensome requirements on U.S. cattle producers was initiated by IBP for the express purpose of soliciting producers’ help in contacting “Senators or members of Congress,” to whom producers were asked to express their concerns regarding IBP’s plans to impose such onerous conditions on their industry. This was IBP’s response to Congress’ passage of the mandatory country-of-origin labeling (COOL) law.¹²⁴ This abuse of market power was initiated months *before* USDA even published its October 30, 2003, proposed rule to implement the COOL law.

B. Imposition of Arbitrary Production Specifications that Lead to Producer Discounts and Facilitate Preferential Treatment

In addition to the application of price premiums and discounts for contract or grid-priced cattle that are based on standardized USDA yield and quality grades, Tyson and Smithfield (now JBS) had each established different price premiums and discounts for additional factors, such as muscle scoring. For example, Smithfield discounted certain muscle scores between \$5.00 per cwt. and \$10.00 per cwt, and Tyson uses muscle scores to apply varying discounts under a different system.¹²⁵ These discounts and premiums are purported to reflect consumer preferences,¹²⁶ but whether a \$120 discount (i.e., \$10 per cwt. applied to a 1,200 lb. animal) is reflective of the actual discount the beef packer receives upon the sale of the resulting meat, or if it represents a windfall for the beef packing industry, is undeterminable without additional information. Nevertheless, the ability to impose such discounts, without knowing if they are legitimate, is currently facilitated by the limited marketing outlets available to U.S. cattle producers.

In addition, producers that sell cattle “in-the-meat” (meaning they agree to receive payment after the packer slaughters the cattle and evaluates the animal’s carcass traits) rather than “live” (meaning they receive payment based on the live weight of the animal), are literally at the mercy of the beef packer for determinations of carcass traits. There are a host of discounts imposed by packers for “in-the-meat” sales including discounts for hard bone, dark cutters, overweight, underweight and overage. But, it is the beef packer who applies discounts for such factors without the producer being present to contest the beef packers’ determination. This practice puts producers at a serious disadvantage and is ripe for abuse, including preferential treatment whereby some producers may not be assessed the same discounts assessed to others. Also, and based on anecdotal information, some beef packers in some regions do not give cattle producers a choice between selling “in-the-meat” or “live,” and offer only bids for “in the meat” sales.

Also based on anecdotal information, beef packers can use discount schemes to grant preferences to certain cattle feeders by, e.g., paying preferred feeders an average, non-discounted price for

¹²³ Letter from Bruce Bass, IBP, Inc., to Producers, March 2003.

¹²⁴ *Ibid.*

¹²⁵ *See* Muscle Scoring Provides Important Production Tips, Nexus Marketing, Ames, Iowa.

¹²⁶ *See id.*

low quality cattle while taking deeper discounts from non-preferred feeders that sell higher quality cattle.

And, anecdotal information indicates that beef packers do pass over some feeders (i.e., do not offer a bid for cattle on the feeder's show list) until the feeder's cattle become overweight, at which time the beef packer offers a bid with significant discounts for the heavier-weight cattle.

C. Procurement Practices Lead to Pricing Anomalies that Benefit Beef Packers

As part of its investigation, the Justice Department and USDA should determine if pricing strategies of the concentrated beef packers, such as that described in the examples above, are among the reasons for the pricing anomalies disclosed in the LMMS study. The LMMS study states that in direct trade transactions based on a carcass weight valuation, the average cattle price is 1.3 cents lower than the average price for direct trade transactions with live weight valuation.¹²⁷ Even more striking is the difference for grid valuation transactions, where prices average 1.8 cents lower than the average price for direct trade transactions.¹²⁸ Assuming an average dressed weight for cattle of 781 pounds,¹²⁹ this price differential translates into a loss of \$10.15/head for producers selling on a carcass weight basis and a loss of \$14.06/head for producers selling on a cash grid basis compared to producers selling on a live weight valuation. It is important to note that these comparisons hold other explanatory variables for price differentials fixed in the model.¹³⁰ When this price difference is multiplied times the volume of cattle sold during the period examined by the LMMS study, it adds up to a total loss of \$202,631,068 for producers who sold their cattle on the cash market on a carcass weight or grid basis rather than a live weight basis.¹³¹

The LMMS study reveals that cattle producers selling their animals on a carcass weight basis or a grid basis have lost more than \$200 million on these transactions in the period covered by the study. The anomalous price differential for dressed weight and grid basis cattle compared to cattle sold on a live weight basis appears counter-intuitive and contradicts a conclusion that beef packers use purchasing methods that provide an incentive for quality and yield. Instead, it appears that the uncertainty inherent in dressed weight and grid basis transactions, and the transference of that price risk from beef manufacturers to cattle producers through these types of transactions, has only operated to depress prices for live cattle and to deprive cattle producers of a market-based price for their product.

The data suggest that beef manufacturers have been able to manipulate the grid system to engineer a lower overall average return to producers who sell on a grid basis. This practice fails to send the right market signals to producers and feeders, and it creates a counter-intuitive disincentive to sell on a grid basis and to seek premiums for yield and quality characteristics.

¹²⁷ See GIPSA Livestock and Meat Marketing Study, Vol. 3 (Jan. 2007) at 2-39.

¹²⁸ See *Ibid.*

¹²⁹ See *id.*, at 1-21.

¹³⁰ See *id.* at 2-39.

¹³¹ This estimate is based on a total of 58 million head of cattle sold reported to RTI from October 2002 through March 2005 and RTI statistics showing that 61.7% of these cattle were sold on the cash or spot market, 17% of which were on a carcass weight basis and 28% of which were on a grid basis. See *Id.* at ES-3 – ES-4, 2-40.

The LMMS data reveal an unreasonable and unfair depression of cattle prices for those producers who sell on a grid basis that is contrary to competitive market fundamentals.

D. Current Procurement Practices Facilitate a Division of the Market that May Eliminating Competition for Certain Subclasses of Cattle in Certain Regions

Tyson Fresh Meats, Inc., (“Tyson”) recently issued presumably new terms and conditions under which it will purchase cattle for slaughter.¹³² Tyson states that it “does not typically accept for processing at its facilities” cattle that exceed 58 inches in height, cattle that exceed 1,500 pounds, or cattle with horns longer than 6 inches in length.¹³³ The imposition of such restrictions presents a number of competition-related concerns: First, if Tyson is one of only two buyers in the marketing region where such restricted cattle are potentially available (i.e., cattle are approaching but have not yet exceeded any of Tyson’s restrictions) and if the other buyer imposed no comparable restrictions, then the other buyer would have an incentive not to bid on such cattle, which, if Tyson did not purchase, would be available for sale at a discount as soon as Tyson’s restrictions were exceeded. In fact, Tyson would have an incentive to lowball such potentially available cattle knowing that if the producer did not sell to Tyson within a short period of time, there would be no competition for the cattle after the restrictions were exceeded. Second, for cattle that already exceed Tyson’s restrictions, regardless of the demand for beef, the producer would have significantly fewer market outlets for the cattle. Third, as stated above, the beef packers’ can manipulate the weight of cattle simply by limiting market access to a cattle feeder, such as bypassing feeders with slaughter-ready cattle as also discussed above.

The imposition of certain restrictions on the type of cattle a beef packer will purchase could constitute an outright denial of access to the marketplace for producers with only one or two packer buyers. Or, it could result in the division of the marketplace if, e.g., one beef packer were to accept only steers, only heifers, only Holsteins, or only hornless cattle. If this were to occur, or if it is occurring, the marketplace could be sufficiently divided by the few beef packers to severely limit competition for each subclass of cattle, if not eliminate competition altogether.

E. Beef Packers Have Engaged in Coordinated Actions with the Effect of Lowering Domestic Cattle Prices.

Under the existing, concentrated structure of the beef packing industry, empirical evidence shows the U.S. cattle market has been subjected to coordinated entries and exits from the market. In February 2006, all four major beef packers – Tyson, Cargill, Swift (now JBS), and National – withdrew from the cash cattle market in the Southern Plains for an unprecedented period of two weeks. On February 13, 2006, market analysts reported that no cattle had sold in Kansas or Texas in the previous week.¹³⁴ No cash trade occurred on the southern plains through Thursday of the next week, marking, as one trade publication noted, “one of the few times in recent memory when the region sold no cattle in a non-holiday week.”¹³⁵ Market analysts noted that

¹³² See Standard Terms and Conditions for the Sale of Cattle to Tyson Fresh Meats, Inc. (“TFM”), Effective Date – February 4, 2008, attached as Exhibit 16.

¹³³ *Id.*

¹³⁴ “Packers Finally Seriously Cut Kills,” *Cattle Buyers Weekly* (Feb. 13, 2006).

¹³⁵ “Classic Standoff Continues Through Thursday,” *Cattle Buyers Weekly* (Feb. 20, 2006).

“[n]o sales for the second week in a row would be unprecedented in the modern history of the market.”¹³⁶ During the week of February 13 through 17, there were no significant trades in Kansas, western Oklahoma, and Texas for the second week in a row.¹³⁷ Market reports indicated that Friday, February 17, 2006, marked two full weeks in which there had been very light to non-existent trading in the cash market, with many feedlots in Kansas, Oklahoma, and Texas reporting no bids at all for the past week.¹³⁸

The beef packers made minimal to no purchases on the cash market, relying on captive supplies of cattle to keep their plants running for two weeks and cutting production rather than participating in the cash market. The beef packers reduced slaughter rates rather than enter the cash market. Cattle slaughter for the week of February 13 – 17 was just 526,000 head, down from 585,000 the previous week and 571,000 at the same time a year earlier.¹³⁹ According to one analyst, the decision to cut slaughter volume indicated “the determination by beef packers to regain control of their portion of the beef price pipeline.”¹⁴⁰ Another trade publication noted that the dramatic drop in slaughter was undertaken in part to “try and get cattle bought cheaper.”¹⁴¹ At the end of the second week of the buyers’ abandonment of the cash market, one market news service reported, “The big question was whether one major [packer] would break ranks and offer higher money. That has often occurred in the past, said analysts.”¹⁴²

As a result of the beef packers shunning the cash market, cash prices fell for fed cattle, replacement cattle, and in futures markets. Sales took place after feedlots in Kansas and the Texas Panhandle lowered their prices to \$89 per hundredweight, down \$3 from the \$92 per hundredweight price reported in the beginning of February.¹⁴³ The same day, February 17, live and feeder cattle futures fell to multi-month lows.¹⁴⁴ Replacement cattle prices also dropped in response to buyer reluctance.¹⁴⁵ In Oklahoma City, prices for feeder cattle dropped as much as \$4 per hundredweight.¹⁴⁶

The beef packers’ simultaneous boycott of the cash market appears deliberately coordinated. It was a highly unusual event that required simultaneous action in order to effectively drive down prices, which it did. As market analysts observed, the major question in markets during the second week of the buyers’ strike was whether or not any one of the major beef packers would “break ranks” to purchase at higher prices than the other beef packers. No buyer did so until prices began to fall. In fact, beef packers were willing to cut production rather than break ranks and purchase on the cash market.

¹³⁶ “Classic Standoff Continues Through Thursday,” *Cattle Buyers Weekly* (Feb. 20, 2006).

¹³⁷ Curt Thacker, “Cash Cattle Quiet 2-20,” *Dow Jones Newswires* (Feb. 20, 2006).

¹³⁸ Lester Aldrich, “Cash Cattle Standoff 2-17,” *Dow Jones Newswires* (Feb. 17, 2006).

¹³⁹ Curt Thacker, “Cash Cattle Quiet 2-20,” *Dow Jones Newswires* (Feb. 20, 2006).

¹⁴⁰ Jim Cote, “Today’s Beef Outlook 2-17,” *Dow Jones Newswires* (Feb. 17, 2006).

¹⁴¹ “Classic Standoff Continues Through Thursday,” *Cattle Buyers Weekly* (Feb. 20, 2006).

¹⁴² “Classic Standoff Continues Through Thursday,” *Cattle Buyers Weekly* (Feb. 20, 2006).

¹⁴³ Curt Thacker, “Cash Cattle Quiet 2-20,” *Dow Jones Newswires* (Feb. 20, 2006).

¹⁴⁴ Jim Cote, “Live Cattle ReCap – 2/17/2006,” *Dow Jones Newswires* (Feb. 17, 2006).

¹⁴⁵ “The Markets,” *AgCenter Cattle Report* (Feb. 18, 2006), available on-line at <http://www.agcenter.com/cattlereport.asp>.

¹⁴⁶ “The Markets,” *AgCenter Cattle Report* (Feb. 18, 2006), available on-line at <http://www.agcenter.com/cattlereport.asp>.

Abandonment of the cash market in the Southern Plains by all major beef packers for two weeks in a row resulted in lower prices and had an adverse effect on competition. Cattle producers in the Southern Plains cash markets during those two weeks were unable to sell their product until prices fell to a level that the buyers would finally accept. The simultaneous refusal to engage in the market did not just have an adverse effect on competition – it effectively precluded competition altogether by closing down an important market for sellers. The simultaneous boycott of cash markets in the Southern Plains was, however, a business decision on the part of the beef packers that did not conform to normal business practices and that resulted in a marked decline in cattle prices. At the time, market analysts interpreted the refusal to participate in the cash market as a strategy to drive down prices, and purchases only resumed once prices began to fall.

The coordinated action in February 2006 was not isolated and was soon followed by a second, coordinated action. During the week that ended October 13, 2006, three of the nation's four largest beef packers – Tyson, Swift, and National - announced simultaneously that they would all reduce cattle slaughter, with some citing, *inter alia*, high cattle prices and tight cattle supplies as the reason for their cutback.¹⁴⁷ During that week, the packers reportedly slaughtered an estimated 10,000 fewer cattle than the previous week, but 16,000 more cattle than they did the year before.¹⁴⁸ Fed cattle prices still fell \$2 per hundredweight to \$3 per hundredweight and feeder prices fell \$3 per hundredweight to \$10 per hundredweight.¹⁴⁹

By Friday of the next week, October 20, 2006, the beef packers reportedly slaughtered 14,000 more cattle than they did the week before and 18,000 more cattle than the year before – indicating they did not cut back slaughter like they said they would.¹⁵⁰ Nevertheless, live cattle prices kept falling, with fed cattle prices down another \$1 per hundredweight to \$2 per hundredweight and feeder cattle prices were down another \$4 per hundredweight to \$8 per hundredweight.¹⁵¹

The anticompetitive behavior exhibited by the beef packers' coordinated market actions caused severe reductions to U.S. live cattle prices on at least two occasions in 2006. This demonstrates that the exercise of market power is already manifested in the U.S. cattle industry.

F. The Beef Packers' Dual Role as a Feeder and a Packer Enables Them to Force Smaller Feeders Out of Business

Because beef packers now participate in both the feeder cattle market and the final cattle market, they are positioned to drive smaller cattle feeders out of business. This can be accomplished by knowingly overbidding for feeder cattle to force smaller feeders to pay higher than competitive prices in order to fill their feedlots. Though both the packer and the smaller feeder would suffer financial losses as a result of such action, the long-term effect would be the exodus of smaller

¹⁴⁷ See "National Beef Cuts Hours at Two Kansas Plants (Dodge City, Liberal)," *Kansas City Business Journal* (October 10, 2006); "Update 1 – Tyson Foods to Reduce Beef Production," *Reuters* (October 10, 2006); "Swift to Stay with Reduced Production at U.S. Facilities," *Meatpoultry.com* (October 10, 2006).

¹⁴⁸ See "Livestock Market Briefs, Brownfield Ag Network," (October 13, 2006).

¹⁴⁹ See *id.*

¹⁵⁰ See "Livestock Market Briefs, Brownfield Ag Network," (October 20, 2006).

¹⁵¹ See *id.*

feeders from the industry, leaving the packer-feeder with even greater buying power in the feeder cattle market. Moreover, when the packer-feeder's higher priced feeder calves are ready for slaughter, the packer-feeder could use these cattle to avoid purchasing fed cattle in the final cattle market. The effect would be to further depress fed cattle prices, which likely would enable the beef packer to recoup any losses resulting from the higher-priced feeder cattle.

Though this type of predatory purchasing would benefit feeder cattle sellers in the short term, the long-term results would be disastrous as the feeding sector would become even more concentrated and both the final cattle market and the feeder cattle market would become even less competitive. R-CALF USA urges the Department of Justice and USDA to take action to eliminate the beef packer from the feeder cattle market.

G. The Beef Packers' Dominance in the Cash Market Is Mirrored in the Futures Market, Where They Also Can Exercise Market Power

R-CALF USA is concerned that beef packers are able to significantly influence the commodities futures market, rendering it unsuitable for managing the risks of independent cattle producers. Practices such as shorting the market to drive down both cash and futures prices, particularly on the last trading day of the month before futures contracts expire are a form of market manipulation. The October 2009 futures board, e.g., broke the limit down on the last trading day in October, causing an unprecedented number of live cattle deliveries to occur. Based on information and belief, the manipulative practices by the beef packers in the commodities futures market has created a disinterest among speculators who would otherwise participate in long speculative positions in the market. The lack of speculative long positions in the market may well be depressing the cash and futures market by several dollars per hundredweight and reducing the utility of the commodity futures market as a risk management tool for cattle producers. R-CALF USA urges the Department of Justice and USDA to investigate the beef packers' activities in the commodities futures market.

H. Concentrated Beef Packers Are Uniquely Positioned to Manipulate Beef Demand to Prevent U.S. Cattle Prices from Responding to Tight Domestic Supplies

The mandatory country of origin labeling (COOL) law implemented in 2008 was expected to allow a consumer preference for USA beef to translate directly into an increased demand for cattle born, raised, and slaughtered in the United States. However, the nation's beef packers resisted the COOL law and began labeling exclusively USA beef with a multi-country label, e.g., "Product of Mexico, Canada and the U.S." The effect of this action was to thwart consumer demand for exclusively domestic beef from translating into a demand for USA cattle, thus enabling beef packers to continue satisfying only a generic demand for beef and sourcing the cattle needed to satisfy that generic demand from any country.

In addition to the discussion above regarding the beef packers' ability to manipulate beef consumption through its control over the price and output of competing proteins, just as the concentrated beef packers are the gatekeepers to the slaughter market for fed cattle, their tremendous market dominance also makes them gatekeepers to the flow of beef to retail stores

and consumers. Either unilaterally or in concert with retailers, beef packers can suppress domestic demand for beef by maintaining high beef prices. The effect of this action would be to suppress the U.S. cattle market even when cattle supplies are at an all-time low. This appears to be what is taking place in the marketplace today: consumer beef prices are being held at near record levels and despite the tight cattle supply situation, cattle prices remain severely depressed. R-CALF USA urges the Department of Justice and USDA to thoroughly investigate the beef packers wholesale and retail selling practices to determine the extent to which the beef packing industry is manipulating beef demand, hence the price and demand for U.S. cattle.

V. RECOMMENDATIONS AND CONCLUSION

As a first step, R-CALF USA urges the Department of Justice and USDA to take immediate and decisive action to enforce the Packers and Stockyards Act (PSA) and halt the beef packers' anticompetitive use of captive supply cattle to manipulate and control the U.S. cattle market. The beef packers' ongoing use of packer-owned cattle and certain marketing arrangements, particularly formula contracts, in our opinion, is a clear violation of the express language contained in the PSA. Contrary to recent court decisions involving private PSA actions that have focused either on the beef packers' intent to manipulate or control prices, or of creating a monopoly; or that have created a justifiable defense for violators not contained in the statute, we believe Congress has expressly and precisely established a distinct threshold that prohibit acts or practices by the beef packers' that have the effect of manipulating or controlling prices, or of creating a monopoly, even absent a showing of intent.

R-CALF USA greatly appreciates the Department of Justice's and USDA's keen interest regarding the current state of competition in agricultural markets and we would be pleased for the opportunity to work with the Department of Justice and USDA to discuss in more detail a comprehensive solution to the plight of our U.S. cattle industry that is described herein.

Sincerely,

A handwritten signature in black ink, appearing to read "Bill Bullard". The signature is stylized and cursive.

Bill Bullard, CEO

Attachment: 1

Attachment 1

Charts Distributed by the Texas Cattle Feeders Association

