



Testimony of

**J. Patrick Boyle
President and C.E.O.
American Meat Institute**

**Before the
House Committee on Agriculture, Subcommittee on Livestock, Dairy, and Poultry**

**Regarding
Review of Competition in the U.S. Livestock and Meat Markets**

April 17, 2007

Good afternoon Mr. Chairman, Ranking Member, and Members of the Subcommittee. Thank you for allowing me the opportunity to appear before this Subcommittee. My name is Patrick Boyle and I am president of the American Meat Institute (AMI). AMI has provided service to the nation's meat and poultry industry -- an industry that employs more than 500,000 individuals and contributes more than \$100 billion in sales to the nation's economy -- for more than 100 years.

AMI's 250 members include the nation's most well-known meat and poultry food manufacturers. Collectively, they produce 90 percent of the beef, pork, veal and lamb food products and 75 percent of the turkey food products in the U.S. Among AMI's member companies, 60 percent are small, family-owned businesses employing fewer than 100 individuals and some are publicly traded and employ tens of thousands. These companies operate, compete, sometimes struggle and mostly thrive in one of the toughest, most competitive and certainly the most scrutinized sectors of our economy: meat and poultry packing and processing.

AMI appreciates the opportunity to provide perspective and hopefully insight into the competitive pressures and developments facing our member companies. Specifically, members of AMI have concerns about legislative and regulatory efforts to apply government directed controls on an industry whose members compete intensely with each other and for a greater share of the consumer's food dollar from other segments of agriculture. These concerns stem from proposals that would 1) prohibit the ownership of livestock by a packer and unduly regulate investment, 2) prohibit or restrict contracting, marketing agreements, or other livestock marketing arrangements that producers and packers rely on, and 3) establish an arbitrary cash

purchase mandate and an involuntary exposure to the volatility of the cash market. This testimony also highlights some of the findings of one of the most comprehensive and exhaustive studies of the industry, which was recently completed for USDA.

**Ban on Packer Ownership of Livestock and Marketing
Agreements will be Detrimental to the Entire Livestock Sector**

AMI is opposed to legislative and regulatory measures that would restrict livestock producers' marketing options and procurement methods of packer and processors. We believe the strength of the livestock marketing system in the U.S. is the flexibility it provides to producers, packers/processors and retailers in responding to market signals and offering increasing variety of alternatives for the producer through to the consumer. The wide range of options available to producers and packers provides a means for market signals and consumer demands to work rapidly and efficiently, while providing opportunities for all market segments. This flexibility has benefited consumers and for producers. Producer options include: spot market transactions, production contracts, cooperatives, bargaining associations, marketing agreements, and other options that allow them to align themselves with consumer demands through contractual arrangements to manage risk and produce a desired product.

These measures aid a livestock producer's ability to manage price and weather risks, access credit, and participate in value-added, branded product lines. Within the last decade, we have witnessed significant sales growth in branded beef and pork products and the corresponding response to market signals by producers to increase production.

We believe that the most appropriate government role in today's livestock marketing system is to enforce the existing laws and regulations that ensure fair and nondiscriminatory business practices among producers and packers, while allowing producers the freedom of choice on how best to market their livestock. The government should exercise its current and vast authority under the Sherman Act, the Clayton Act, the Robinson-Patman Act, the Packers and Stockyards Act and other state statutes.

Producers and packers utilize contracts, cash negotiations, marketing agreements, and other arrangements for many reasons and often for very different reasons than their neighbors or other producers across the country. Each producer and packer's operation, skills, market position, and experiences are different and require a livestock marketing or procurement plan that is appropriate for their model. Opponents of these agreements would like Congress to believe that there exists a monolithic dogma among producers as to their means of marketing livestock. The truth is better reflected in John Kenneth Galbraith's words which define a market as "a series of opinions." The wide ranging opinions of producers and packers about the market and its direction are what make it work so effectively in allocating risk, reward, and resources.

The many marketing options provide producers the ability to diversify or concentrate their livestock marketing plan to best match their skills, experiences, capital base, or tolerance of weather and price risks. One of the more common reasons producers and packers enter arrangements is to manage price risks to aid in the access of credit and capital. As the graph in

Attachment A shows, agricultural commodity markets can be extremely volatile and experience very wide price swings – sometimes up and sometimes down. Producers and packers recognize that managing this volatility is critical to their long-term economic well-being and livelihood. This is true across agriculture, where more than 40 percent of all agricultural goods are produced via contracts or related agreements.

To illustrate how packer ownership provides mutual benefit to packers and producers, consider this: A producer may have a few empty stalls in his or her operation and the skills to manage additional animals, but he or she may lack the capital to afford the extra livestock. Thus, a producer may seek to enter an agreement with a packer to raise packer-owned livestock in the extra capacity in exchange for economic compensation. In this scenario, the producer benefits by maximizing the utilization and efficiency of his or her farm, improving his/her returns, and gaining additional experiences in raising the extra few head. Without the packer-owned livestock, this producer would be limited by his/her capital and would have an underutilized asset because of an arbitrary state restriction.

Producers, packers, and processors have not been the only beneficiaries of these agreements and arrangements. Consumers have benefited from more products that meet their needs and values as well as price competitiveness from improved efficiencies. According to the Bureau of Labor and Statistics an item such as ground beef has, on average, since 1984 consistently lagged the larger consumer price index increases, thereby, consistently improving the value returned to consumers for their food dollar relative to all other expenditures. Further, the amount of income that consumers spend on all meat and poultry products has shrunk to less than two percent of income!

AMI supports the continuance of free enterprise competitive policies that have served our economy and country so well by ensuring access to broad marketing opportunities for producers and procurement alternatives for packers. Domestic and international history is replete with examples of failures by government attempts to manage the market by limiting relationships that enterprises would mutually, normally, and voluntarily pursue. It is difficult to discern where, if any potential value would accrue to any party by a prohibition on ownership or other restrictions. The suggestion that such a restriction would add value to livestock or meat is without merit. Attempts to limit packers' and producers' abilities to engage in contracts, marketing agreements, and strategic mergers reduce capacity to respond to consumers and pursue economic, social, and environmental goals in rural America.

Requiring 25 Percent Spot Market Purchases

With respect to our views regarding legislation that would require a packer to purchase 25 percent of its daily slaughter from the cash market, AMI cannot see any positive impact from this type of policy recommendations. We are unaware of any evidence that any such proposals would add to the producer's bottom line. The most obvious and immediate impact would be that it would make certain companies' entire business models illegal and force packers to terminate risk management programs with producers. In effect, the proposal would cause packers to essentially fire a producer and force that producer's participation in a highly volatile spot market.

If the proposal were to become law, many producers and packers would experience an immediate devaluation of their assets, in effect a taking and devaluation by the federal government without compensation. AMI believes such proposals would hasten consolidation in the packing industry and lead to an immediate reduction in packing capacity, particularly in the pork sector. The added risk in this type of environment could further trigger a contraction in production and compound adverse impacts on remaining producers.

We are also concerned with the discriminatory nature of legislation that would require only certain packers to purchase 25 percent of their daily slaughter from the cash market. If a packer is a single plant operator, not required to report under the mandatory price reporting statute or the plant is owned by a cooperative – they would be exempt. In a free enterprise economy, everyone should be subject to the same rules - restrictions and freedoms - to compete fairly on a level playing field. To do otherwise results in the government picking winners and losers through non-uniform centrally regulated schemes, rather than through the free market economy. Providing benefits for one over another through state-like regulatory requirements also distorts credit and capital investment. The proposal imposes specific livestock procurement requirements in the beef and pork sectors, while direct competitors in the chicken and turkey sectors retain total flexibility. Further, it discourages smaller operations from growing their businesses and market share or they run the risk of having to comply with the legislation. Legislation that treats packers of various size and cooperatives differently is troubling, at best. Legislation that penalizes people and businesses for being successful is – frightening.

GIPSA/RTI Livestock and Meat Marketing Study Rejects the Proposals

As Congress contemplates possible policy changes to the current marketing system for livestock and meat, we would like to remind you of an important provision included in the Omnibus Appropriations Bill for FY 2003, which provided \$4.5 million to USDA to conduct a comprehensive study on this subject. That study, now complete, is the most comprehensive and far reaching study that has ever been conducted on livestock and meat marketing. On the beef complex alone, transaction data was secured from the 29 largest beef packing plants and the report focused on 58 million cattle and 590,000 business transactions. The “GIPSA Livestock and Meat Marketing Study,” released on February 16, 2007, focused upon, but was not limited to, an examination of various legislative proposals that were debated but not ultimately included in the 2002 Farm Bill. Those legislative proposals included a ban on packer ownership of livestock, a requirement that packers purchase 25 percent of their animals on the spot market, and bills that would either ban or restrict forward contracting and other marketing arrangements.

To conduct this study, the Secretary of Agriculture was required to issue a request for proposals from entities that had the means to conduct this study and the contract was awarded to RTI International through a competitive and open bid process (68 *Fed. Reg.* 32455). This study was conducted with the direct input and peer review of the nations leading business and agricultural universities.

Prior to issuing its notice and request for comments regarding the scope of the study in the *Federal Register*, USDA/GIPSA established a working group with representatives from a wide range of federal agencies with experience and regulatory oversight in the market place. The

working group included representatives from the USDA's Office of the Chief Economist, Economic Research Service, Agricultural Marketing Service and National Agricultural Statistics Service in addition to the Department of Justice, Federal Trade Commission, and Commodity Futures Trading Commission (68 *Fed. Reg.* 32456).

The report found that alternative marketing arrangements (AMAs) increase the economic efficiency of the cattle, hog, and lamb markets, and that these economic benefits are distributed to consumers, as well as to independent producers and packers who use AMAs. Other significant conclusions in the study include the following:

- In aggregate, restrictions on the use of AMAs for sale of livestock to meat packers would have negative economic effects on livestock producers, meat packers, and consumers (RTI Study Vol.1 ES - pg. 3).
- Changing consumer expectations in terms of product quality have led retailers to modify their merchandising and purchasing practices in the meat, fruit, and vegetable sectors. These initiatives in response to consumer demand, have led to increased segmentation of product offerings on store shelves and in the meat case. Retailers now offer, in addition to standard products, differentiated products focusing on health, convenience, taste, and information about how the food was produced (RTI Study Vol. 6 pg. 1-12).
- Many livestock producers and meat packers benefit by using AMAs, and those benefits include (RTI Study Vol.1 ES - pg. 3):
 - Better quality assurance and consistency
 - Better risk management (market access and price risk)
 - Improved cost management.
- The producers surveyed that use AMAs identified the ability to obtain better prices, buy/sell higher quality cattle, and improve supply management as the leading reasons for using AMAs. In contrast, the producers surveyed that use only cash markets identified independence, flexibility, quick response to changing market conditions, and ability to buy at lower prices and sell at higher prices as primary reasons for using only cash or spot markets (RTI Study Vol.1 ES – pg. 4).
- The packers surveyed stated that their top three reasons for using AMAs were to secure higher quality cattle, allow for product branding in retail stores (adding value throughout the chain), and improve week-to-week supply management (RTI Study Vol.1ES – pg. 4).
- The producers and packers surveyed that use AMAs value them as a method of dealing with production, market access, and price risks. More specifically, feedlots believe that AMAs allow them to secure or sell better quality cattle and calves and improve operational management, efficiency, and capacity utilization. Packers identified AMAs as an important element of producing branded products and

meeting consumer demand by producing a higher quality, more consistent product (RTI Study Vol.1 ES – pg. 8).

- Hogs purchased through AMAs are consistently associated with higher quality than hogs acquired through negotiated (spot market) purchases (RTI Study Vol.1 ES – pg.11).
- An analysis of risk associated with different marketing arrangements shows that different types of marketing arrangements exhibit different price volatilities as measured by variance of prices. From the hog producers' perspective, spot/cash market sales pose the greatest level of risk to the producer (RTI Study Vol.1 ES – pg. 12).
- In analyzing the economic effects of hypothetical restrictions on the use of AMAs in the hog and pork industries, the report concluded that hog producers would LOSE because of the offsetting effects of hogs diverted from AMAs to the spot market and consumers would LOSE because of higher wholesale and retail pork prices (RTI Study Vol.1 ES – pg.12).
- Restrictions on the use of AMAs may increase concentration of various segments of the lamb industry (RTI Study Vol.1 ES – pg. 15).

Maturing Industry Increases Specialization

During the past two decades, the American meat and food manufacturing industry has been demonstrating signs of a maturing sector by its increasing specialization, its focus on brand development, value-added products, and its contracting size relative to its customer segment. The packing entities that are most successful in recent years have been those that have been the most agile, disciplined, and focused on providing their customers with the products they demand. To meet these changes, companies developed relationships to minimize the distance between producers and consumers while scaling to the size of business that would allow it to be competitive. Occasionally, criticism of profit or the scale of the top four, five, or twenty leading firms in a segment takes vogue and leads to unjustified incitement and calls for a more active state in participating in the market.

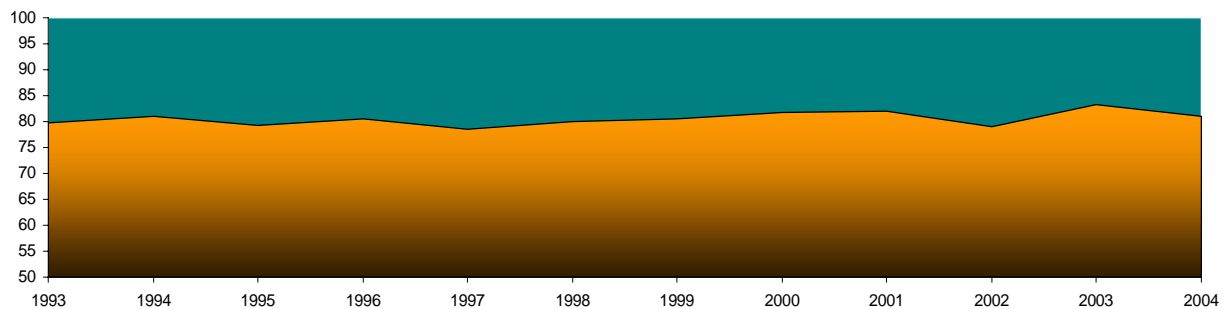
As a regulated industry, the barriers to entry are relatively high compared with the service, knowledge, or light manufacturing segments of our economy. Nevertheless, even with these higher costs it is amazing that there are more than 3,500 meat and poultry plants that are classified as small or very small by USDA and nearly 2,000 state-inspected plants that are mostly very small plants. The smaller operations in the business often focus on very narrowly defined niches and limited offerings. Many will often partner with a large packer or other entities to co-market to larger retailers and gain access to a broader consumer base.

As an industry with a long and diverse heritage, the meat industry has an appreciation for the special responsibilities that it has to its customers, employees, producers, investors, and suppliers. The use of contracting, marketing agreements, and related arrangements provide an

economically beneficial way to assure customers of the claims made. Similarly for producers, the use of modern procurement methods is often viewed favorably by creditors and investors, thereby providing affordable capital resources to farmers. Additionally, the use of modern procurement methods and alignment provide a means for packers to work closely with its retail customers. Three of the largest grocers in the world have more **375 million people each week in their stores**. Meeting the weekly and daily demands of that many consumers requires a very sophisticated and sensitive approach, the tools, and the size to adequately negotiate and provide for these major outlets.

A specific critique that some individuals have pointed to is the level of market share of the leading four enterprises in the beef sector. In the beef industry, a simplistic segmentation of the industry could divide it into two main segments, fed beef and lean beef. Fed cattle are those that are often fed significant amounts of grain and marketed between 18-28 months of age. Lean cattle are often mature animals, some are fed grass or extensively grazed or originate within the 9 million head of dairy animals. The majority of the 33 million head marketed are from the fed side of the business. Since the 1990s as this chart illustrates, the level of market share by these four firms has remained relatively constant. A further study of this data would indicate that fed beef enterprises have historically maintained an economy of scale appropriate for their segment. At a few points during the past 120 years, cattle feeders and packers were even members of the Dow Jones Industrial Average Index's 30 firms. Relative to historical context recent and past, the market share and scale of the four leading enterprises has remained relatively constant with stiff competition among these members and new entrants. It is important to note that these four current firms have not been the same four enterprises that have always participated in this group. The competitive pressures and innovations of enterprises have propelled new firms in this category and others out. Indicating and conferring a robust and competitive marketplace.

Four Companies' Fed Slaughter
as a Percentage of U.S. Commercial Slaughter



Source: US Department of Agriculture.

Finally, a recent report from the Congressionally authorized and funded multi-year bipartisan Antitrust Modernization Commission report released early this month recommended after their hearings, reviews, and work that “government should not displace free market competition absent extensive careful analysis and strong evidence that either 1) completion cannot achieve societal goals that outweigh consumer welfare or 2) a market failure requires the regulation of prices, costs, and entry in place of competition.” This analysis combined with the findings and

careful analysis of the USDA/GIPSA report provides a clear indication that the market is competitive and current oversight and enforcement are effective.

How Congress Can Assist the Livestock and Poultry Sectors in the 2007 Farm Bill

Support for Marketing Flexibility and the Free Enterprise System

Efforts to limit the day-to-day advancements of packers and producers cooperating to meet their customers' values can have adverse consequences on all parties. Past Congresses have attempted to prohibit the use of contracting, marketing agreements, and related arrangements as well as strategic mergers. All of these efforts would have impeded progress, investment, and the American agriculture atmosphere for growth. Should these succeed, the result of these efforts are likely less profit, less employment, less credit and investment, less (if any) progress toward social and environmental goals, and overall adverse impact on the competitiveness of American agriculture. We encourage Congress to reject any attempts to impede livestock marketing options and alternatives for producers, packers, and processors.

Trade

The members of AMI have supported and benefited greatly from the existing free trade agreements (FTA) and expanded market access from our World Trade Organization (WTO) membership. The economic well-being of meat and poultry packers and producers is closely tied to our competitiveness in accessing international markets. From the Uruguay Round Agreement to NAFTA, the U.S. meat and poultry community has consistently benefited from the market access to new, international consumers. In fact, Mexico and Canada are currently two of the largest export destinations for beef and beef variety meats, accounting for more than 2/3 of all beef trade and more than \$1 billion in sales. For AMI pork exporters, nearly 17 percent of U.S. pork production is exported and the value of pork exports has increased by more than 350 percent since NAFTA's passage. AMI is fully prepared to be a strong and vocal supporter of the pending Korea FTA should Korea's ban on beef end and full market access for beef is restored. AMI encourages all countries that maintain restrictions on U.S. beef and other animal products to align their animal health policies with the guidelines of the World Organization for Animal Health (OIE).

Congress should advance policies that contribute to increased trade opportunities for animal agriculture and encourage trading partners to adhere to commerce based on internationally accepted scientific principles.

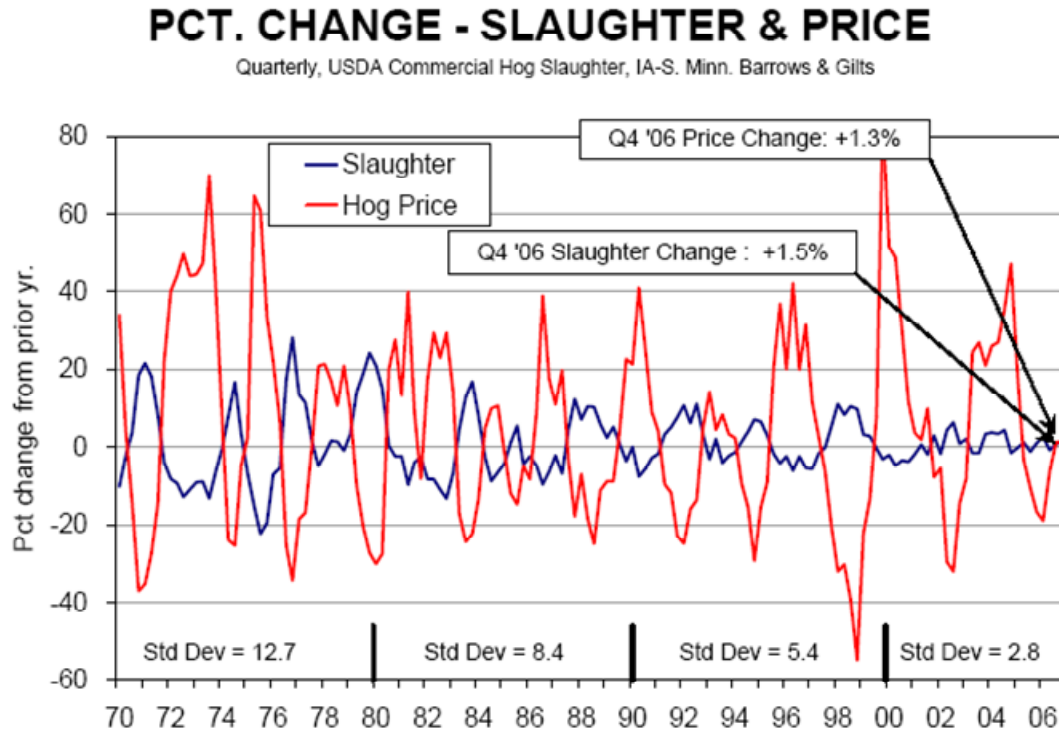
Energy-Based Opportunities

AMI member companies have been carefully observing recent developments in the feed industry, specifically the impacts from the increase in demand for corn from the ethanol industry. This rise in demand for corn has pressed market forces to demand higher corn prices. Consequently, and among other impacts, the change in price and availability has led animal agriculture producers to consider alternatives to their feeding, nutrition, and dietary regimen.

These changes can and do impact meat and poultry quality, consumer offerings, livestock and poultry farm efficiency, and the management of livestock and poultry operations.

It is for these reasons that AMI is asking Congress and the Administration to consider policies to support energy-based opportunities for animal agriculture, minimize adverse impacts on livestock and poultry producers and processors, and ultimately place the United States in a more competitive position in terms of energy availability. Specifically, AMI supports 1) research in ethanol byproduct safety, quality, and usability and renewable energy technologies, 2) equity of incentives for all renewable energy including renewable diesel and methane conversion, 3) a working lands conservation program to encourage environmentally friendly feed stuffs production, and 4) supports exposing consumers to more renewable fuels by allowing the ethanol tariff to expire.

Thank you for the opportunity to provide these perspectives today.



Source: CME Daily Livestock Report, February, 14, 2007

Since 1970 through November 2006, the volatility of live hog prices has moved incrementally some years and dramatically other years to respond to market and seasonal supply and demand changes. Incidentally, in recent years, the live hog, live cattle, and feeder contracts are consistently the largest volume traded agricultural contracts at the Chicago Mercantile Exchange – a reflection of demand for risk management.

Portion of U.S. Farms with Livestock

	1950	1964	1974	1992	2002
Sheep	6.0%	7.4%	4.7%	4.2%	3.5%
Beef	75.5%	72.3%	44.3%	41.7%	37.4%
Hogs	56.0%	34.2%	20.3%	9.9%	3.7%
Dairy	67.8%	35.9%	17.4%	8.1%	4.3%
Chicken	78.3%	38.3%	13.7%	4.6%	3.5%

Source: U.S. Census of Agriculture

As the meat and poultry packing and processing sector matures and specializes, farmers have also increased their specialization. This data from the U.S. Census of Agriculture illustrates that more and more farms are becoming single specie producers and developing well defined expertise in the production of certain animals, breeds, and market segments.

Why production contracts? Start up costs & Risk mgt:

To be fully employed as
an independent hog
farmer requires a
\$700,000 investment and
50% equity

To be fully employed as a
hog contract grower
requires a \$500,000
investment and 15%
equity

\$350,000

Versus

\$75,000

Source: University of Missouri-Columbia, Dr. Ron Plain. *"Why U.S. Animal Agriculture Looks Like It Does."*

Young producers and entities that seek to enter agriculture may have the skills, education, and some initial experience, but lack capital to enter farming. Contracting and other agreements provide a means for entry at a significant but much more achievable entry price. This chart shows the difference in start up capital often required by bankers and creditors of new producers. While there still are a number of operators that inherit farms from previous generations, these are fewer and sometimes have facilities that do not reflect the best in production science, animal well-being, or animal husbandry considerations.

