Testimony Submitted for the Record
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Hearing before the House Agriculture Committee

"An Examination of Price Discrepancies, Transparency, and Alleged Unfair Practices in Cattle Markets"

April 27, 2022

On behalf of the North American Meat Institute (NAMI or the Meat Institute) based in Washington, DC, and its members around the country, thank you for the opportunity to submit this testimony.

The Meat Institute is the United States' oldest and largest trade association representing packers and processors of beef, pork, lamb, veal, turkey, and processed meat products. NAMI members include over 350 meat packing and processing companies, large and small, and account for over 95 percent of the United States' output of meat and 70 percent of turkey production.

Executive Summary

This testimony provides a comprehensive picture of the uniquely complex, dynamic, integrated, and competitive markets in which cow-calf producers, stockers, backgrounders, cattle feeders, beef packers, processors, distributors, wholesalers, retailers, food service operators, and others operate.

The testimony begins with a summary of the complex cattle and beef markets, followed by an examination of the supply and demand fundamentals driving the markets. U.S. Department of Agriculture (USDA) data show record beef production in 2019, 2020, and 2021, despite capacity constraints at packing and processing plants. Data also show cattle prices rebounded as packing capacity came into balance with the cattle supply, highlighted by cattle prices reaching their third-highest January price in the last decade during January 2022.

The testimony also rebuts claims that industry concentration has led to inflation. The four-firm concentration ratio for fed cattle slaughter has not changed

appreciably in nearly 30 years; today's skyrocketing inflation across the economy results from supply chain issues and high demand, not industry concentration.

The testimony addresses proposed legislation and regulation. The cattle cash market mandate proposed by Senators Chuck Grassley and Deb Fischer would increase costs for producers and consumers at a time of high input costs and crippling inflation. Moreover, the mandate would have regional disparities: the Texas-Oklahoma-New Mexico region, Kansas, and Nebraska would shoulder the vast majority of the costs, while the Iowa-Minnesota region would escape relatively unscathed. For these and other reasons, lawmakers should oppose inserting the federal government into the free market.

Finally, USDA is promulgating new proposed rules to regulate packers, which are likely to have far reaching, unintended consequences. At the same time, Congress is considering establishing a politically appointed Special Investigator within USDA to add to the Department's existing enforcement personnel, duplicating resources. With the promulgation of the new rules, the Special Investigator (and staff) would be compelled to bring cases to test the legal limits of the new rules, even if those cases are not warranted. The resulting legal uncertainty and chaos will accelerate changes in livestock and poultry marketing that will up-end the supply chain, adding costs to producers, consumers, and packers.

Congress and USDA should resist making radical changes to the cattle and beef markets.

Overview of the Highly Complex and Dynamic Cattle and Beef Markets

Too often, the policy debate around the cattle and beef industry is an overly-simplified discussion limited to cattle producers versus beef packers. In discussions on these topics, it is imperative policy makers remember: packers don't buy fed cattle from cow-calf producers; nor do packers sell beef to consumers.

As Dr. Dustin Aherin testified before the House Agriculture Committee's Livestock and Foreign Agriculture Subcommittee last summer:

> …[C]attle are not beef. Cattle are one of several inputs into beef production. Other major inputs include labor, physical capital, and technology. These inputs are always seeking, but never finding, the perfect balance between one another.[1]

The policy debate should be focused on a much broader context encompassing the dynamics across the whole value chain. For example, a recent paper published by the Federal Reserve Bank of Kansas City notes that one animal – and the beef

[1] Aherin, Testimony before the House Agriculture Livestock and Foreign Agriculture Subcommittee, July 28, 2021.

produced from it – "could be sold as many as six times before it finally reaches the consumer."[2]

Cattle change hands before they get to the slaughter plant, and for beef, each step in the post-slaughter process that are carried out by a variety of entities, is taken to add value and supply specific products for specific uses in various consumer markets.

Though the fundamentals of supply and demand that drive cattle and beef markets are relatively straightforward, the markets themselves are extremely complex. Although highly integrated, cattle markets and beef markets have their own supply and demand factors.

Derrell S. Peel, PhD, the Charles Breedlove Professor of Agribusiness in the Department of Agricultural Economics at Oklahoma State University, provides context in Chapter 1 of a must-read research paper for policymakers, *The U.S. Beef Supply Chain: Issues and Challenges*, published by The Agricultural and Food Policy Center, Texas A&M University.

Dr. Peel emphasizes the sheer complexity and magnitude of the cattle and beef market.

> It is reasonable to ask why the beef cattle industry should be plagued with so many contentious issues that have persisted for so long. Much of the reason is attributable to the fact that the U.S. cattle and beef industry may well be the most complex set of markets in existence. In its entirety, the cattle and beef industry represents an extraordinarily complicated set of cattle production and marketing activities which provide the source of a massive set of beef products marketed through a diverse set of final markets and all coordinated by a multitude of inter-related market transactions. (p. 3, emphasis added)

Looking at the cattle market first, from the ranch to the slaughter plant, live cattle typically change ownership two to three times – Dr. Peel describes "multiple distinct and separate" cattle production sectors.[3] Cow-calf producers market their calves to cattle feeders, or to backgrounders who in turn sell those cattle to feeders. While calves are an output for a cow-calf producer, they are an input for backgrounders and feedlots who also operate in the cattle market.

The price for cattle at any of those three most common points of transactions is a function of how many cattle are in each respective market segment at a given point

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[2] Cowley, C. Long-Term Pressures and Prospects for the U.S. Cattle Industry, Kansas City Federal Reserve Bank Economic Review, December 17, 2021

[3] See *The U.S. Beef Supply Chain: Issues and Challenges*, p. 3-4

in time. In other words, the price is determined by supply of cattle to sell from one segment and the demand to buy cattle by the next segment. That explains why each segment can experience different margins and why there is a futures contract for two types of cattle: feeder cattle and fed cattle. When any of those segments are out of balance, prices move, and such moves can be dramatic.

But that's just the cattle production side. Once a fed steer or heifer is finished at the feedlot, it is sold to a packer: a feeder's output and one of a packer's inputs are fed cattle. That animal is slaughtered and processed into various primal cuts. Those primal cuts are fabricated by the packers and/or further processors into numerous products, from muscle cuts like steaks, to hamburger or processed beef products. Dr. Peel also shines a light on the complexity and diversity of the processing, retail, and food service sectors:

> Packers fabricate to specific product specifications for various retail grocery customers, further processing and food service customers, and a variety of export markets. As a result, the major packers produce several thousand different products from a basic fabrication process that begins with several hundred carcass products and by-products of slaughter and fabrication. Some packing facilities in certain locations have some or all packing capacity dedicated to value-added programs that operate as sole-source for upstream suppliers and downstream markets. (p. 23)
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> …
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> The COVID-19 pandemic revealed, somewhat to the shock and surprise of both consumers and producers, that the supply chains for retail grocery and food service are largely separate, very specialized, and quite complex. Not only are various beef cuts often used in different supply chains or used differently, but products like ground beef for retail grocery and for food service originate in very different supply chains (Peel, 2021). (p. 24)

That was a lesson learned during COVID: as beef demand skyrocketed but packers' operational capacity to slaughter cattle was constrained, beef prices increased. This was seen across the beef supply chain, from the largest packers down to the local custom slaughter "locker plant."

Supply and Demand Fundamentals at Work in the Beef Industry during COVID.

Last summer, testifying before the Senate Committee on Agriculture, Nutrition, and Forestry, Dr. Glynn Tonsor of Kansas State University highlighted the relationship between cattle prices and the size of the cattle herd, which has too

often been forgotten or conveniently ignored during cattle market policy discussions. Dr. Tonsor testified:

> Perhaps no relationship is currently more central to economic discussions in the U.S. beef-cattle industry than the relationship of fed cattle inventories to processor capacity.[4]

Cattle herd size must remain top-of-mind during any discussion of cattle prices. USDA released its annual cattle inventory report on January 31, 2022, which provides a snapshot of the total cattle herd in the U.S. as of January 1. Compared to a year earlier, the report showed a reduction at every level in the U.S. beef cattle herd:

- Beef cows for breeding down 2 percent;
- Replacement heifers for breeding down 3 percent;
- Calf crop born in 2021 down 1 percent;
- Expected calf crop in 2022 down 3 percent; and
- Feeder steers and heifers for beef harvest down 3 percent.

This, combined with strong beef demand continuing from 2021, suggests that 2022 will be a bullish year for cattle producers. This is especially the case as the supply of fed cattle becomes more aligned with the operational capacity of the packing industry's ability to harvest and process the available supply of cattle.

Indeed, after five years of growth in the cattle supply, combined with the impact that COVID, insufficient labor, and supply chain disruptions had on the packing industry, cattle supply and demand were out of balance.

Cattle prices hit record highs in 2014 and 2015, when the overall cattle herd was at its smallest since 1952 (for context, that was during the Truman Administration). Those record prices incentivized rapid herd expansion among producers.

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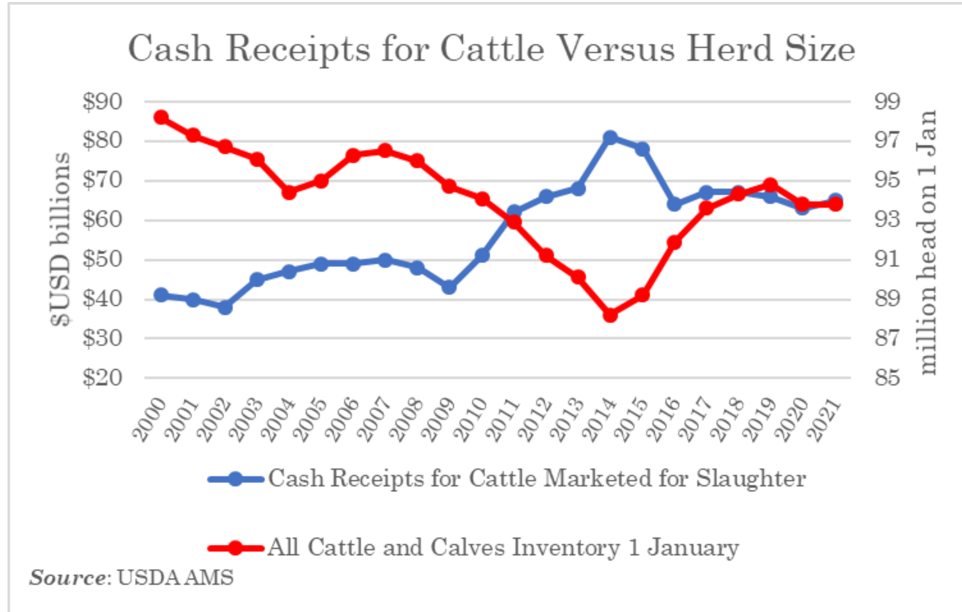
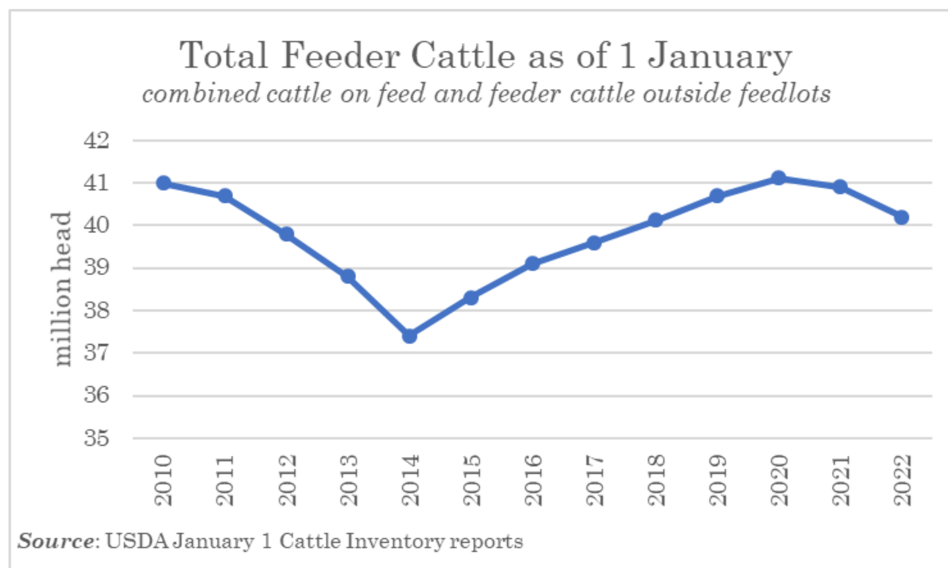
[4] Tonsor, Testimony before the Senate Committee on Agriculture, Nutrition, and Forestry, June 23, 2021



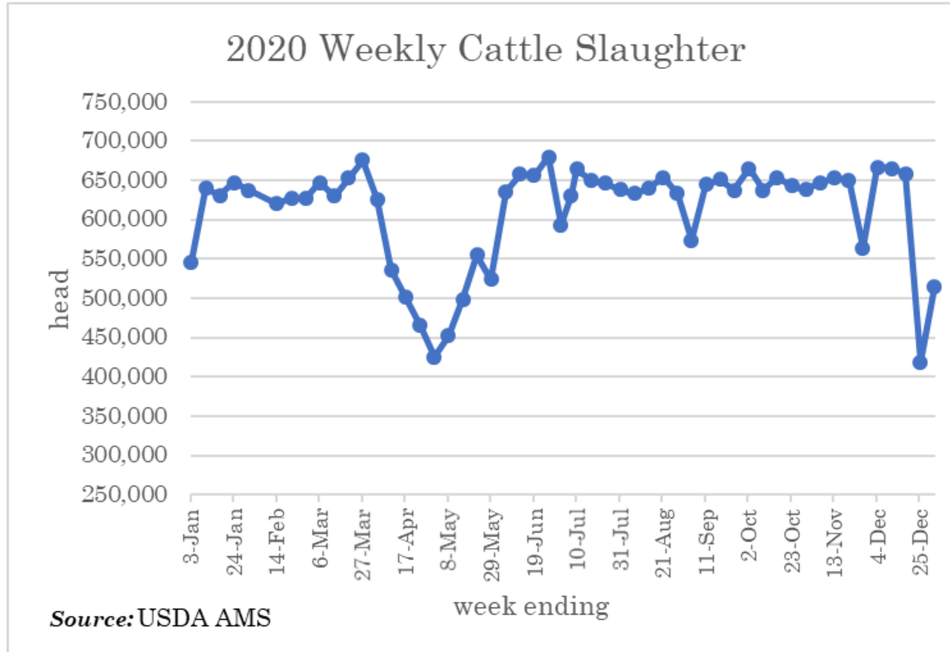
Source: USDA AMS

While the beginning-of-the-year cattle inventory in the U.S. hit its peak in 2019, given the time needed to raise a calf to market weight, the supply of feeder cattle in the herd on the first of the year did not peak until January 2020. Total feeder cattle supply began 2020 at the highest level in more than a decade.

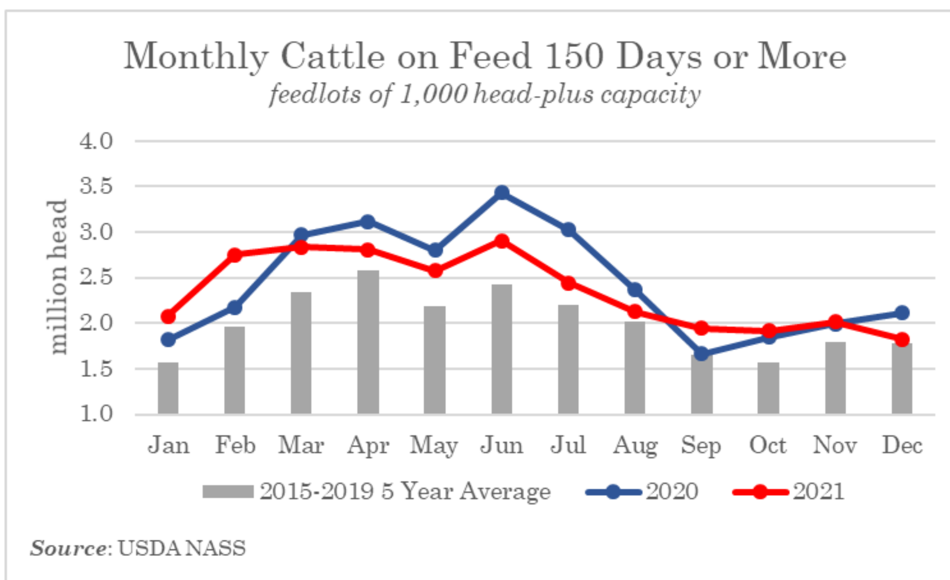


Source: USDA January 1 Cattle Inventory reports

Two and a half months later, in March 2020, COVID hit. Slaughter plants were idled beginning in April. By the week ending May 1, 2020, weekly slaughter dropped by 40 percent and didn't recover until late June, but still lagged behind what would have been normal volumes during the season.



This situation – more cattle and constrained ability to process them – created a backlog of cattle inventory already in feed lots. That can be measured by the number of cattle on feed for 150 days or more. These "long fed" cattle make up the supply of cattle closest to being ready to be marketed to packers for slaughter and processed into beef. The backlogged oversupply resulted in low prices for fed cattle, even as consumer and export demand for beef remained high and resulted in increased wholesale beef prices.

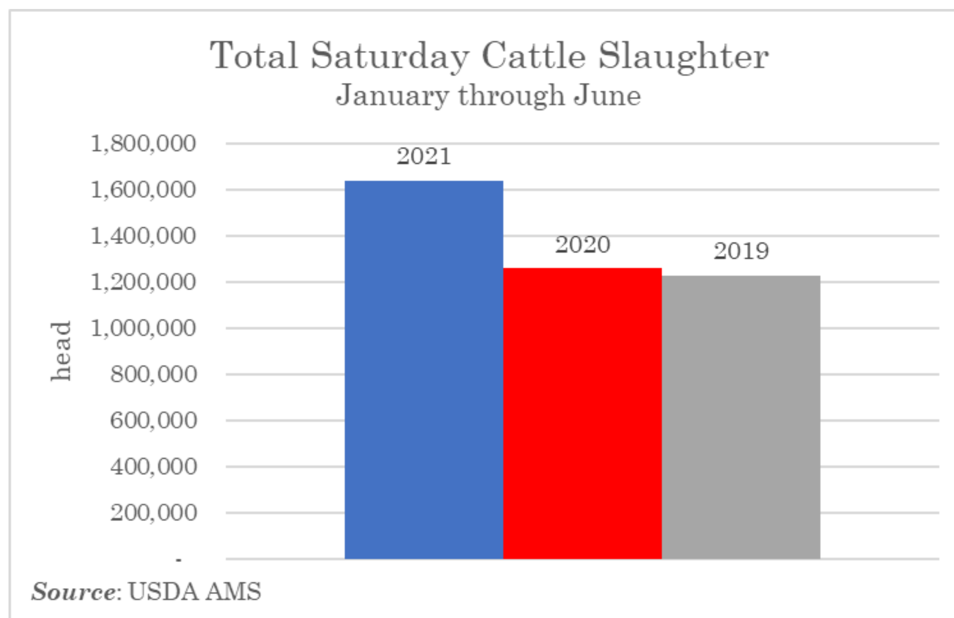


But in the face of the many challenges, the beef packing sector proved resilient. Total beef production in 2020 was a record 27.24 billion pounds, slightly larger than the previous record of 27.22 billion pounds in 2019. The increased volume was based on heavier slaughter weights. As expected, cattle weights increased because of the bottleneck of cattle on feed. Total head of commercial slaughter in 2020 was only down two percent from 2019, despite the dramatic disruption to the cattle harvest during the second quarter of 2020 due to the pandemic.

The supply of cattle remained large in 2021. USDA reports that in 2021, the cattle-on-feed inventory reached the second highest monthly total on record for seven months, each month from February through June, and then again in September and October.

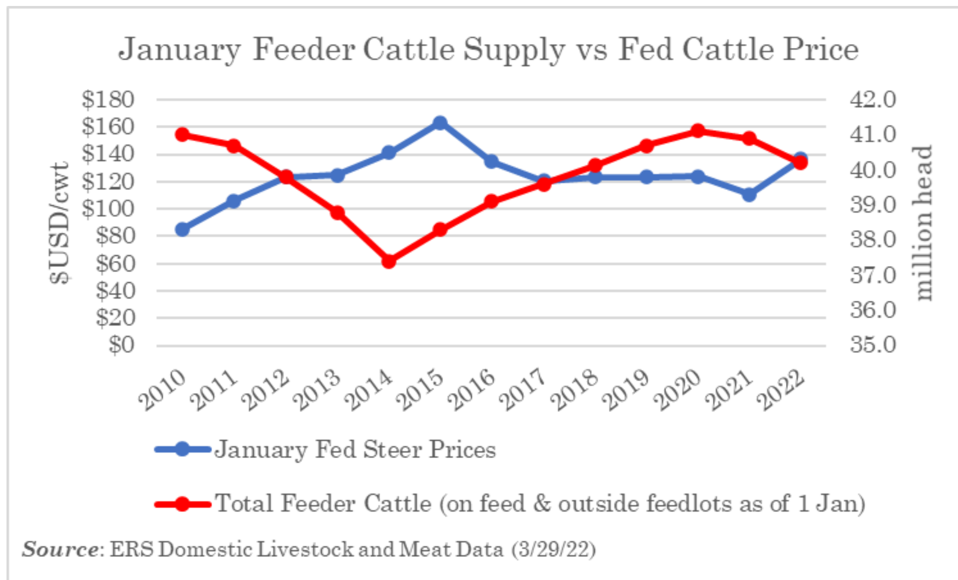
Throughout 2021, even as the comprehensive COVID-19 protections instituted by the meat industry since the spring of 2020 successfully lowered transmission among meatpacking workers and held case rates lower than case rates in the general U.S. population, worker shortages persisted. Through 2021, the Meat Institute regularly heard from member companies having up to 20 percent absenteeism on any day.

However, packers worked their way through the supply of market ready cattle last year, primarily by adding Saturday shifts, especially during the first half of the year. Total Saturday slaughter during January through July 2021 was up 30 percent over 2020 and 33 percent over 2019.



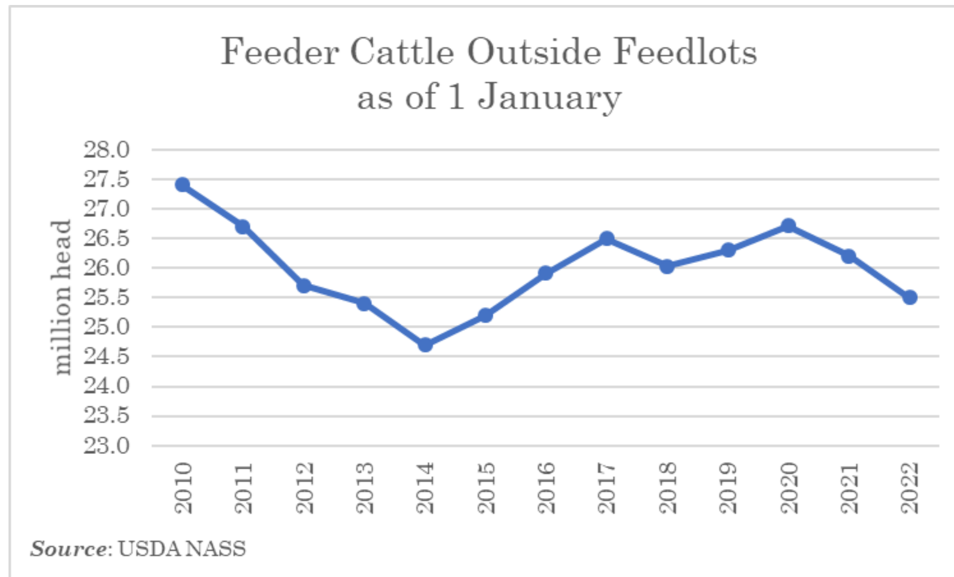
<u>In 2021, beef production and cattle slaughter both were up three percent from 2020, making 2021 another record year for beef production at 28 billion pounds</u>. As slaughter rates recovered, and the industry worked through the backlog of cattle,

supply and demand balance was restored. As a result, in January 2022, fed cattle prices rebounded to the highest January price since 2015, and the third highest January price in the past decade.



For 2022, based on the supply and demand trends for fed cattle, the outlook for cattle prices is bullish across the board. On January 1, 2022, the total number of cattle on feed on all sizes of feedlots was 14.7 million head. That is the same inventory as 2021 and tied for the highest in more than a decade.

However, unlike 2021, the inventory of feeder cattle outside of feedlots to be placed on feed during the year is smaller. Based on the numbers of steers, heifers not intended for cow replacement, and calves under 500 pounds, the beginning of the year supply of feeder cattle outside of feedlots is at its lowest since 2015 when fed cattle prices were at their historical peak.



The beginning of the year supply of feeder cattle outside of feedlots is a reliable indicator of a strong cattle market through 2022 into 2023. Operational capacity at packing plants has increased. In February, cattle slaughter was 2.69 million head, which was a six percent increase over February 2021. Beef production was an all-time record for the month of February.

In addition to seven-year highs for the January average fed cattle price, February, March, and April average fed cattle prices are also at their monthly high since 2015. In short, supply and demand fundamentals continue to drive the cattle and beef markets, as they did throughout the pandemic.

COVID-19 hit as the feeder cattle supply peaked at a point higher than it had been in the previous decade; packers and processors navigated changing markets (far less food service/far more retail), labor shortages, and other supply chain disruptions; all while beef demand boomed. But beef production met the challenge, with record production in 2019, 2020, and 2021.

Today, with the cattle herd contracting, meaning supply is tightening, and operational slaughter capacity increasing, meaning demand is expanding, cattle prices are rising. It is the cattle cycle in action. Policymakers should not intervene and attempt to control the free market fundamentals.

Misplaced Claims about Increasing Consolidation and Concentration.

Members of the Meat Institute – and the entire industry supply chain – benefit from, and depend on, a fair, transparent, and competitive market.

Much of the rhetoric about concentration in the beef packing sector wrongly implies that consolidation is on-going and that packers' market power is becoming more and more concentrated. That is not the case. The four-firm packer concentration ratio for fed cattle slaughter has not changed appreciably in nearly 30 years. According to the Agricultural Marketing Service's (AMS) Packers and Stockyards Division (P&S Division), the four firm concentration ratio was 82 percent in 1994; today it is 85 percent.

The meat packing industry has been, and continues to be, one of the most highly scrutinized industries when it comes to antitrust review. The P&S Division is uniquely charged, by statute, to provide on-going oversight for fair business practices and to ensure competitive markets in the livestock, meat, and poultry industries. Any potential merger or acquisition regulators believe threatens "too much market power" is subject to review by the Justice Department or the Federal Trade Commission. The last proposed merger of two of the "big four" fed cattle slaughterers occurred in 2008 – and it was blocked by the Department of Justice.

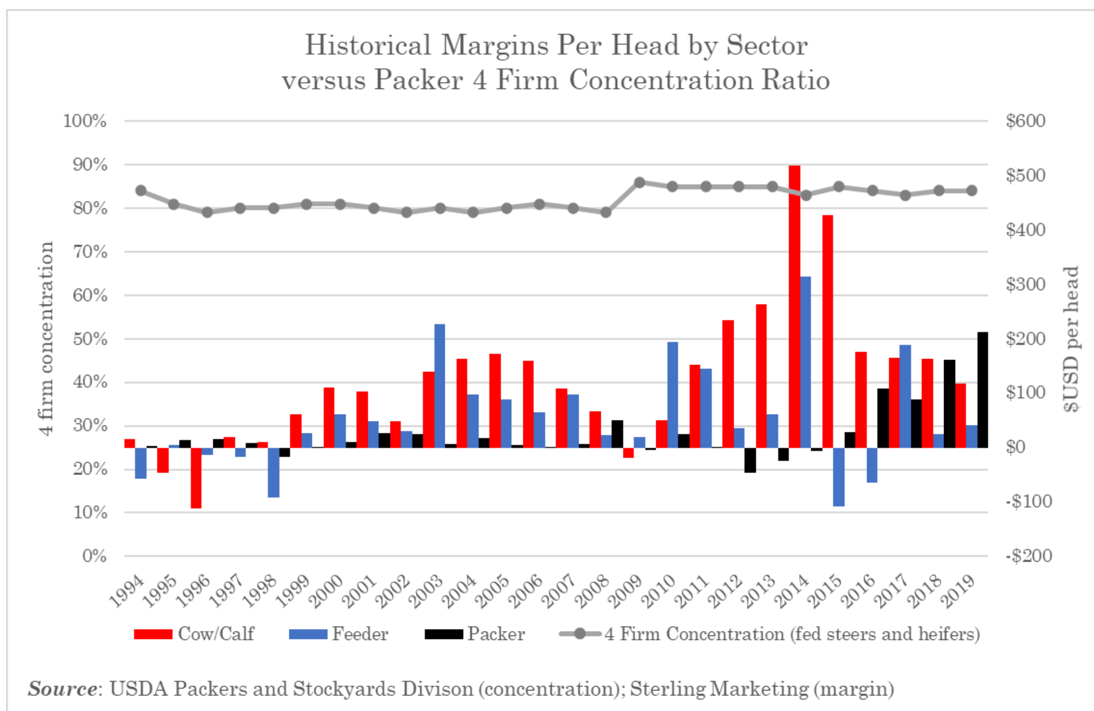
Another clarification is needed. It is frequently claimed that the big four packers control 85 percent of beef production in the U.S. Again, that is not the case and a misleading exaggeration. Fed cattle make up 79 percent of the total cattle slaughter. Cows and other non-fed cattle, make up the balance, primarily slaughtered to be made into hamburger. The lean meat from these animals is a necessary ingredient to be made into America's supply of hamburger produced in combination with the less demanded muscle cuts from the fed cattle. This distinction is important because up to 50 percent of all beef in the U.S. is consumed as hamburger. Even factoring in the non-fed cattle slaughter plants they own; the four largest beef packers represent about 70 percent of total U.S. beef production.

Critics of the industry frequently mistake individual packing plant size with overall industry concentration. The size and location of plants, however, reflect basic economic factors like the cattle supply and the economics of plant operations. Indeed, the cattle supply itself is concentrated. The farms and ranches that produce about half of all beef cattle in the U.S. are in just seven states. Further, more than 70 percent of all fed cattle are in just five states. Economies of scale drive the capacity and production of a packing plant. That is especially true in areas with large numbers of fed cattle. Likewise, cow slaughter plants rely on a supply of cull cows from pasture-based cow-calf farms or dairy farms and are structured based on those factors.

Each packing plant has its own cost structure. Packers bid on cattle based on the supply and demand factors in their own region. Owning a plant in Texas does not change the bottom-line to a company's operation in Iowa or Colorado.

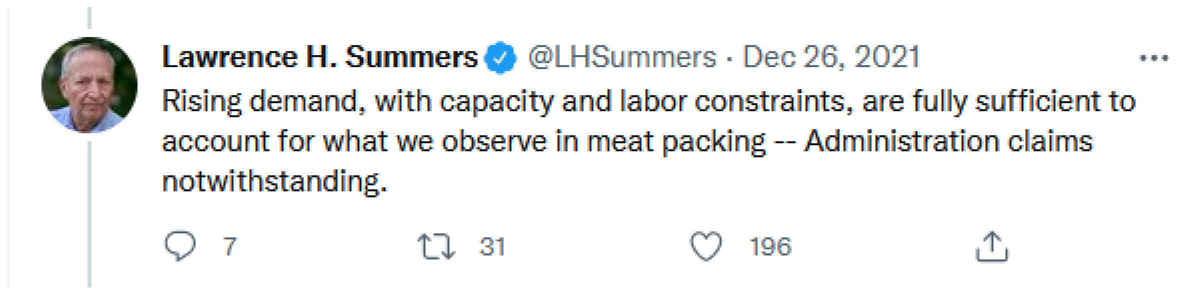
Finally, given that the structure of the beef packing industry is driven by supply and demand factors, the false premise regarding concentration providing undue market power for beef packers must be corrected. The bottom-line is the current level of four-firm concentration has existed for nearly 30 years and it has not ensured packer profitability at the expense of producers.

No sector – cow-calf, feedlot, nor packer – has realized positive margins every year. For example, the four-firm ratio in 2014, when cow-calf and feedlot margins were at record highs, was the same as in 2017 when all three sectors showed positive margins. However, over this more than 25-year timeline, the cow-calf sector suffered negative margins the fewest number of years of the three as the chart below shows.

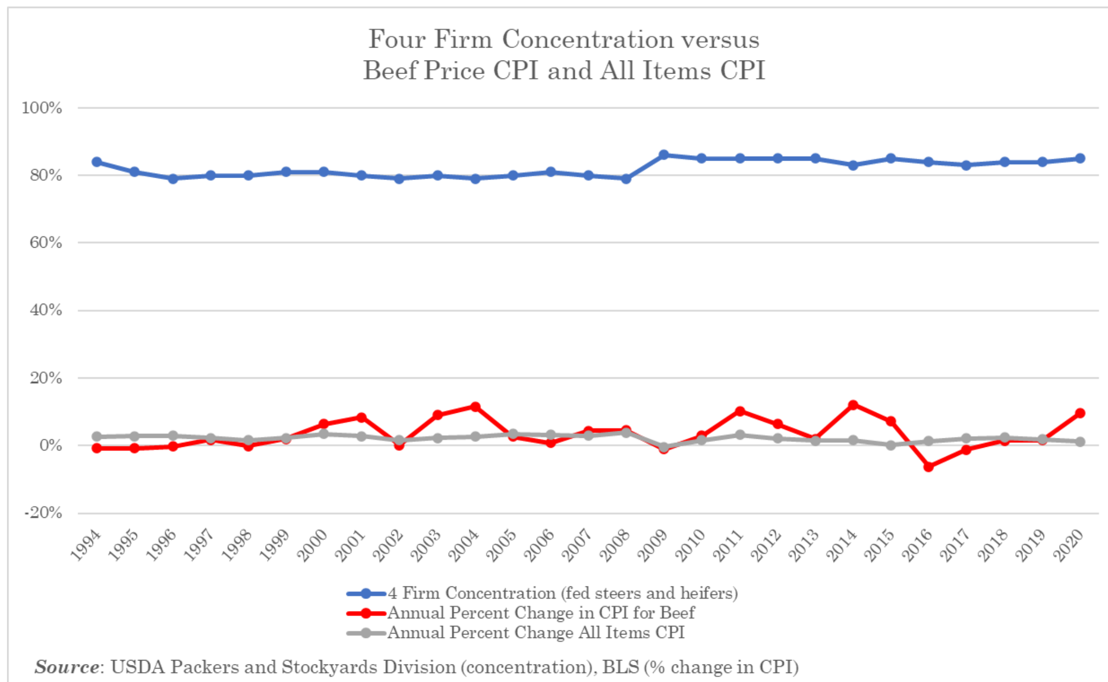


Beef Pricing and Inflation.

Despite claims by the Biden Administration, meat industry concentration is not the cause of inflation. As Larry Summers, Secretary of the Treasury for President Clinton, the Director of the National Economic Council for President Obama, and Charles W. Eliot Professor and President Emeritus at Harvard University tweeted:

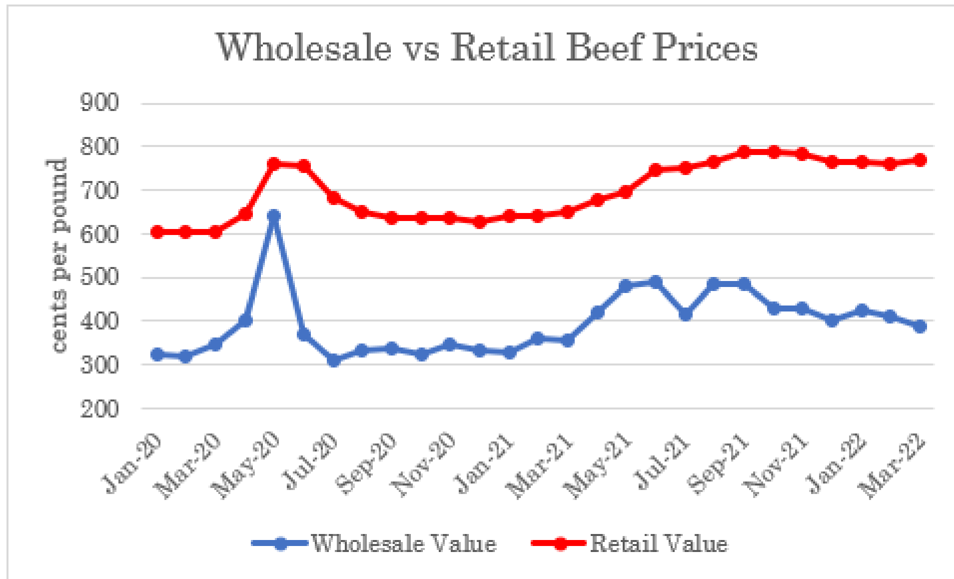


Again, the four firm concentration ratio in beef packing hasn't changed appreciably in nearly three decades, yet meat price inflation has varied from year to year.



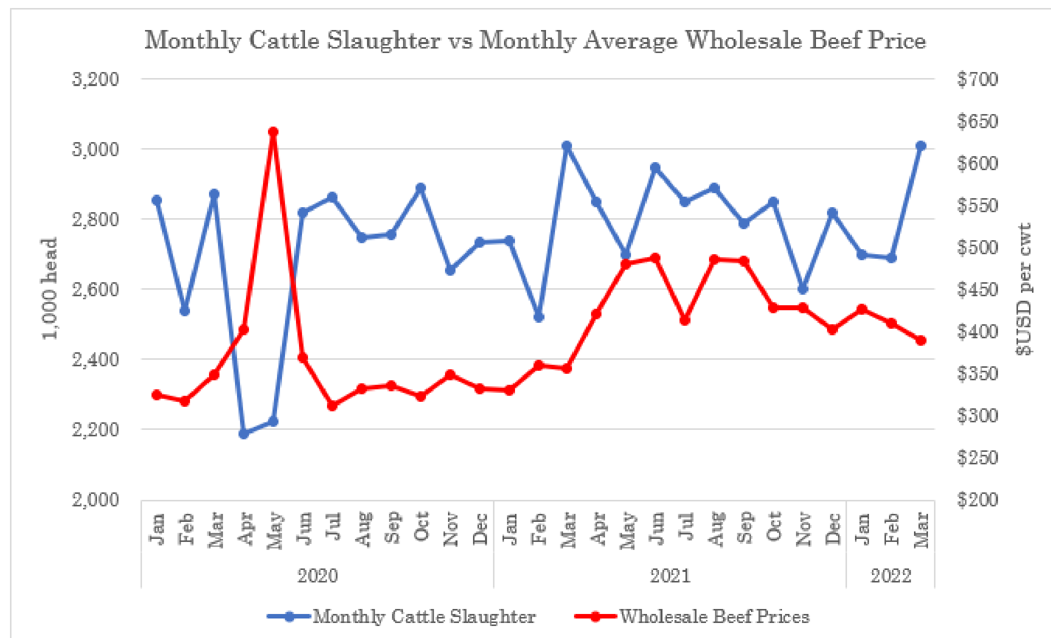
Source: USDA Packers and Stockyards Division (concentration), BLS (% change in CPI)

Further, packers do not set retail prices: packers receive wholesale prices. Retailers, and the prices for which they sell beef to consumers, are affected by all the supply chain issues and input costs facing the broader economy, from trucking availability and diesel prices, to warehousing, labor, and product demand, which all affect their segment of the value chain.



Source: USDA Meat Price Spreads

Last year, wholesale beef prices peaked as would be expected during the heavy demand period for beef from Memorial Day to Labor Day. Those higher prices resulted from still limited supply in the face of strong demand. The slower pace of slaughter – for the reasons discussed above – constrained the beef supply even as retailers demanded more beef to meet consumers' demand. With limited production and supply relative to demand, wholesale prices rose during the seasonal high demand period.



Source: USDA Economic Research Service

Per capita beef consumption during 2021 was above 2020 consumption by a half-pound, and more than three-quarters of a pound above per capita consumption during 2019.

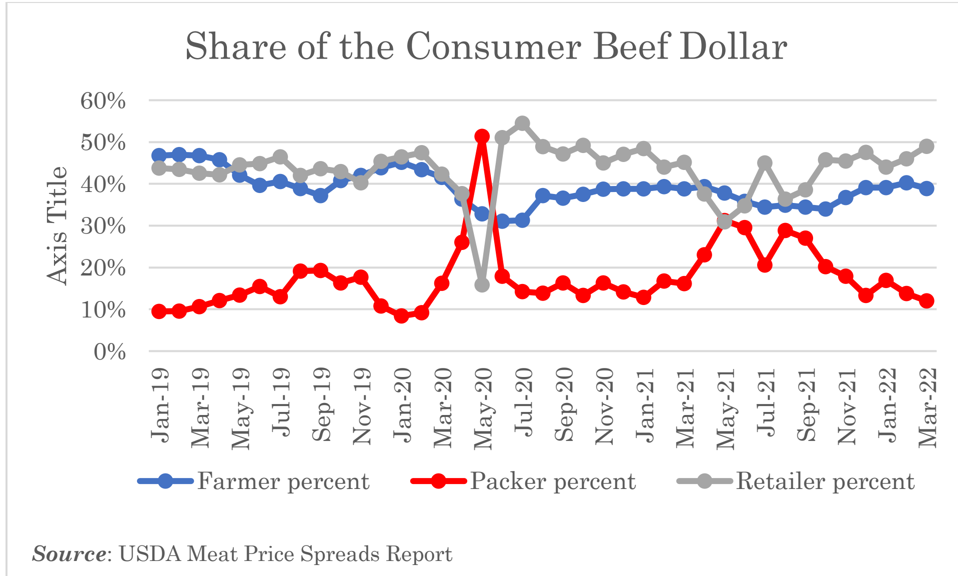
Consumer demand for beef was high based largely on increased consumer income. According to the Bureau of Economic Analysis (BEA), personal expenditures increased in June, July, August, and September 2021, as personal income (from all sources, not just wages and salaries, but including government social benefits including pandemic-related payments) grew – even compared to 2020.

In March 2021, Congress enacted additional COVID relief that included child tax credits, direct payments of $1,400, an increase in nutrition assistance (which supports retail purchases), and extended unemployment benefits. This added $4.232 trillion in government relief payments in addition to that which was paid in 2020. Coupled with economic and job recovery, this added an additional $21 trillion in personal income in 2021, compared to 2020.

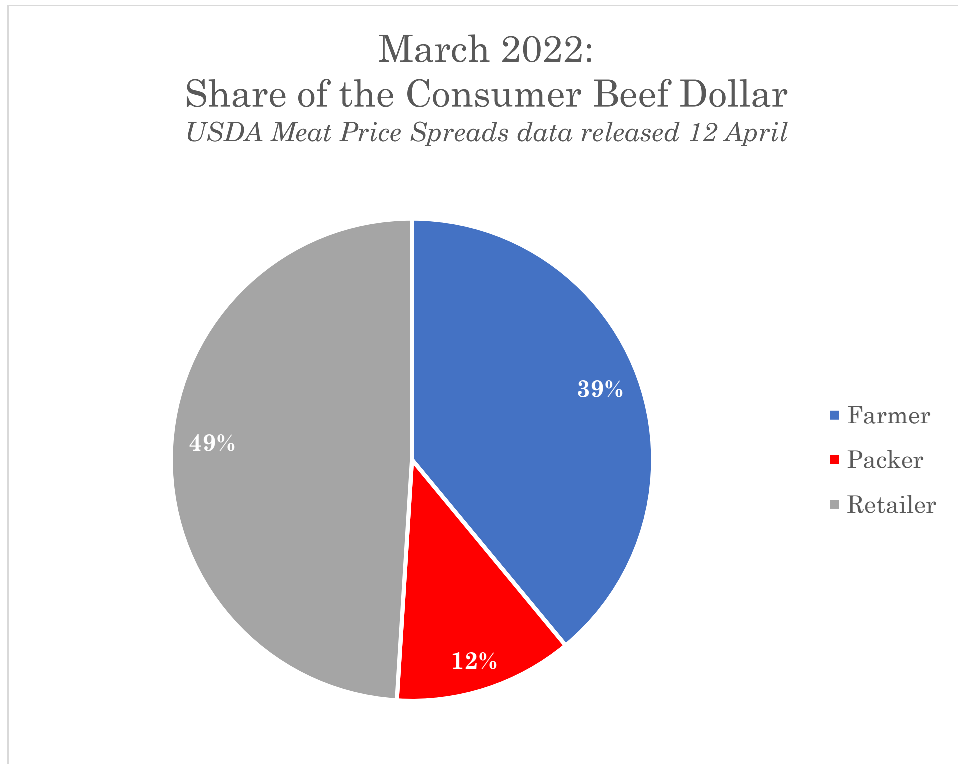
Much of the additional personal income was spent on food, and of that, spending focused on beef. Beef is the protein that is most sensitive to economic changes – consumption increases with higher income and decreases with lower income relative to other proteins. Also, during that time restaurants continued to re-open – increasing demand for wholesale beef. According to BEA spending on food service (restaurant demand) increased through 2021.

The bottom line is neither beef nor industry concentration has driven the record inflation we've experienced. In the calculation of the Consumer Price Index, beef accounts for 0.546%, so even at a 12 month increase of beef prices from January 2021 to January 2022 of 16%, beef added 0.08% inflation to the economy.

Finally, <u>in the 627 months beginning January 1970 through March 2022, packers have received the smallest share of the consumer beef dollar in all months but May 2020, at the peak of the COVID related shutdowns on slaughter which reduced beef supplies</u>.



As of last month, the USDA reported the retail value of Choice beef at $7.685 per pound. The packer share of the retail beef dollar in March was 12 percent.



On January 10, the *Washington Post's* editorial board rightly called out the administration's attempts to blame inflation on businesses:

> President Biden is facing mounting criticism for inflation's rise to its highest level since 1982. Unfortunately, the White House's latest response is to blame greedy businesses.
>
> Economists across the political spectrum are rightly calling out the White House for this foolishness. Even some within the White House are questioning this approach, The Post reports.
>
> Inflation, which was relatively low for years, did not suddenly rise in recent months because businesses decided now was the ideal time to squeeze their customers. What actually happened is that demand soared for many products as the economy recovered. Often, there were not enough products to meet it, thanks to supply chain hiccups and labor shortages, so prices went up. In a surprise to many, consumers kept buying goods such as cars and washing machines even at higher prices.

As explained above, we could add beef to the list of highly demanded products that consumers kept buying at higher prices.

Legislating and Regulating to "Fix the Problem."

There have been several proposals to restructure and regulate the cattle market through significant government intervention. Prominent among the proposals is to require cattle feeders to sell cattle to packers, and packers to buy from feeders, a mandatory minimum volume of fed cattle on a cash, spot market, or "negotiated" basis. These proposals, however, threaten the industry with numerous adverse and unintended consequences.

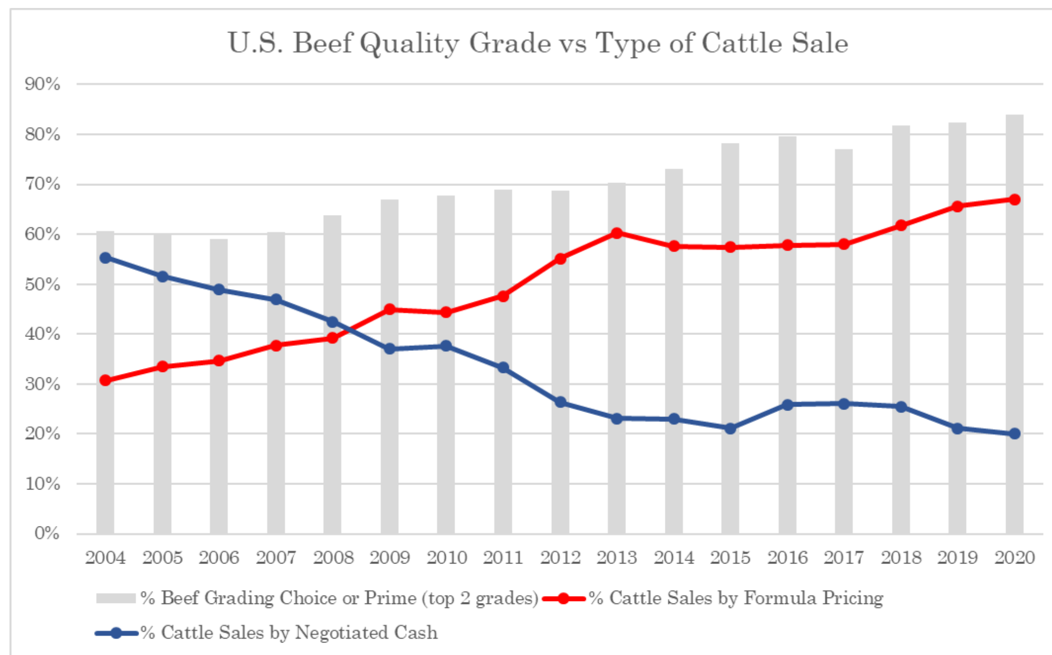
Innovation via formula and contract sales – collectively known as alternative marketing arrangements (AMAs) – originated with cattle feeders attempting to capture value associated with improved quality cattle.

Turning back to Dr. Peel, he describes the advent of AMAs and value-based marketing that shifted packers away from buying cattle on the average:

> Until the 1990s most fed cattle were priced on averages, at the pen level and even entire showlists. Very little quality differentiation meant that high quality cattle were undervalued, and low-quality cattle usually received the average price. Packers had little incentive to differentiate cattle quality since they had to process all the cattle anyway. All that was important to packers was to get the average correct. The lack of quality signals meant that producers had little incentive to improve cattle. The problem was apparent; quality grading

> was low and beef demand was declining. This led to a major push in the industry for "value-based marketing," which aimed to differentiate and value cattle according to quality differences. (p. 32)

The resulting shift towards AMAs and value-based marketing corresponded to an improvement in beef grade quality and has helped drive increased consumer demand.



The success behind value-based marketing and AMAs is based on transmitting market signals about consumers' preferences to producers. The results include increased choices for consumers and premiums and certainty for producers. Yet the black swan events of the past three years have brought calls for change from some producers – even though regulating the terms of fed cattle sales would not have resulted in a fundamental change in the cattle market over that period. The volume of cash market sales is roughly the same today as it was during the record cattle price years of 2014 and 2015.

Again, Dr. Peel:

> Indeed, the emotions, anger and frustration accompanying recent events such as the Holcomb packing plant fire in 2019, the ongoing COVID-19 pandemic beginning in 2020, and the winter storm of February 2021 have fueled demands for an array of potential legislative actions that attempt to jump to a solution without addressing the complex structural and behavioral issues that brought the industry to the current situation. <u>The risk is that these overly</u>

> simplistic solutions will have long term detrimental impacts on cattle producers, the industry, and consumers, and jeopardize the ability of the industry to compete in dynamic global protein markets for a successful future. (p. 2) (emphasis added)

Cattle Price Discovery and Transparency Act

Senators Chuck Grassley and Deb Fischer have introduced the Cattle Price Discovery and Transparency Act. The Grassley-Fischer bill mandates cattle feeders sell and packers buy a certain percentage of cattle on the negotiated, spot market, restricting the use of AMAs. In other words, some cattle producers who want to market their cattle through AMAs would be prohibited from doing so, by government fiat.

The Grassley-Fischer bill requires the Secretary of Agriculture to establish minimum thresholds below which negotiated trade volumes cannot fall. Those minimums would vary by region, cannot be less than the average percent of negotiated sales and negotiated grid sales in each region made during the two-year period between January 1, 2020, and January 1, 2022 – a period when cattle markets were most disrupted by COVID, labor shortages, and supply chain issues.

As expert witnesses have testified, even if 100 percent of fed cattle were sold on the cash market, prices for cattle producers would not have been any higher than what the market allowed in 2020 and the first half of 2021.

Interestingly, under this plan, no region may have a mandatory minimum of negotiated sales that exceeds 50 percent. According to an analysis of the legislation released last week by Texas A&M University's Agriculture and Food Policy Center (AFPC),[5] the upper limit for the mandate in the legislation – 50 percent cash sales – would only affect the Iowa-Minnesota region. Iowa-Minnesota is the only region in which the mandatory minimum would be set below the actual market. The 24-month average of negotiated sales in that region during the 2020-2022 baseline period established in the legislation was 51.3 percent. In short, this bill could reduce – albeit marginally – the percent of cash negotiated sales in Iowa and Minnesota, while forcing dramatic increases elsewhere.

Producers and feeders in Texas, Oklahoma, New Mexico and Kansas, have the most to lose. According to Texas A&M, based on the formula in the legislation, 53 percent of the weekly cattle marketings in 2020-2022 would not meet the mandatory minimum established. In the Texas, Oklahoma and New Mexico region, based on 2020-2022 actual cattle marketings, the proposed minimum would not be met 98 percent of the time. Moreover, the legislation gives the Secretary of

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[5] Benavidez, J., Anderson, D., Fischer, B., Outlaw, J., Analysis of S. 4030 – Cattle Price Discovery and Transparency Act of 2022 Briefing Paper 22-04, Texas A&M AFPC, April 2022

Agriculture authority to set the mandatory minimum as high as 50 percent. In that scenario, the Texas A&M briefing paper projects the number of negotiated sales to "explode, increasing from roughly 1.7 million head…to more than 12 million head from 2022 to 2026," which would make the cost estimates "far greater than the estimates in this report."[6]

At the 2022 American Farm Bureau Federation Annual Convention in Atlanta, Dr. Stephen R. Koontz, professor in the Department of Agricultural and Resource Economics at Colorado State University said, "Mandated cash trade is not going to get you better price discovery. It's going to put a $50 cost on calves impacted."
A January analysis[7] by Texas A&M of an earlier version of the Grassley Fischer bill concludes:

> Mandated levels of negotiated trade are expected to have negative effects on cattle and calf prices. That is to say that the mandate will result in lower short term fed cattle prices due to the increase in the costs of the feeder-packer cattle sale transaction. Research has shown there is a value to AMAs in the form of lower costs, improved logistics, and reduced risk. Mandating higher levels of negotiated trade will result in higher transaction costs. The higher transaction costs will result in lower cattle and calf prices and higher wholesale and retail beef prices. Lower prices will have the long-term effect of reducing cattle and beef production resulting in higher prices. We would suggest that fed cattle and feeder calf prices would increase back to their long-term expected levels, but not necessarily increase to higher levels. The long run price reversion back to earlier equilibrium levels is driven by the reduction in cattle and beef production. Based on this, one might argue that the industry will be smaller.

That paper analyzed the cost of cash market mandates projected over the next five years at the $50 per head cost calculated by Dr. Koontz. While that specific proposal is no longer on the table, a look at the regional disruption and inequity is apt. The Texas-Oklahoma-New Mexico region, at $50 per head cost, stood to lose $123.9 million, followed by Kansas at $102.9 million. Nebraska would have fared better at "only" $75.3 million in losses. As for Iowa, the aggregate five-year cost was projected at a mere $52,520.

Under the revised Grassley Fischer bill, Texas A&M estimates that in the Five Area region, the mandatory minimum if enacted now, would be expected to subject 2.252 million head of fed cattle to the $50 per head loss under the mandatory negotiated sales minimum. Again, the regional inequity is instructive, as shown in the chart below.

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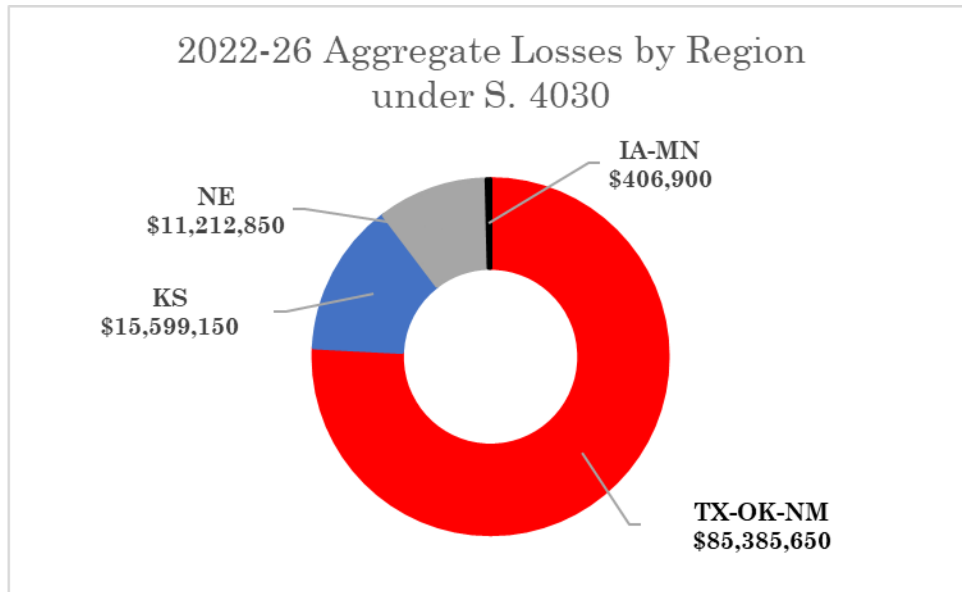
[6] *Ibid*. at p. 6.
[7] Benavidez, J., Anderson, D., Fischer, B., Outlaw, J., Analysis of S. 3229 – Cattle Price Discovery and Transparency Act of 2022 Briefing Paper 22-02, Texas A&M AFPC, January 2022



Based on Texas A&M analysis and estimates

The legislation could have far wider adverse impacts that are yet unknown and currently impossible to analyze. The proposal directs the Secretary to establish five to seven contiguous regions that encompass the entire continental U.S. – from Maine to Arizona, Washington to Florida – that reflect "similar fed cattle purchasing practices." A tall order. This effectively would cause regulatory gerrymandering for no other reason than to impose unnecessary and costly mandatory minimums for negotiated fed cattle sales.

Now, as cattle markets return to balance, is not the time to disrupt the cattle market with a sweeping new government mandate. At the end of 2021, cattle prices were at a five-year high. In the first quarter of 2022, cattle prices were at seven-year highs. And, as discussed below, USDA is drafting proposed regulatory changes under the Packers and Stockyards Act.

<u>Proposals to implement a mandatory minimum volume of negotiated cash sales go far beyond the purported objective of market transparency and price discovery and instead would directly regulate the terms of sale in a private transaction between two businesses, the producers and packers. A cash market mandate would represent the beginning of the Federal government regulating more – or all – terms of sale in the cattle market</u>. Such behavior should be concerning to producers given the number of transactions among the segments of the cattle production supply chain described earlier.

Further, there have been suggestions Congress should amend the confidentiality provisions in the Agricultural Marketing Act applicable to Livestock Mandatory Reporting (LMR). One bill has been introduced that would prohibit USDA from

withholding any "information, statistics, and documents." This concept has data privacy and antitrust implications for both packers and feeders. USDA has examined the LMR confidentiality requirements and determined relaxing the requirements would not ensure anonymity among the market participants. Producers are not the only market participants using the published LMR data: packers and others constantly analyze the data, and any loosening of the confidentiality requirements could provide some market participants full view of their competitors' actions in the market.

By design, a mandate for packers to meet a minimum volume of negotiated cash sales would limit a producer's ability to use other, preferred types of cattle procurement and marketing tools, including forward contracts and various formula-based purchases that comprise the majority of transactions for market-ready cattle. These pricing methods, combined and balanced with the negotiated cash market pricing, have served U.S. cattle producers, the beef industry, and consumers well over the past two decades by:

- Providing producers and cattle feeders with an effective risk management tool;
- Reducing marketing costs for cattle feeders and producers;
- Improving efficiency though the supply chain;
- Improving the quality of U.S. beef;
- Meeting U.S. consumer demand and building trust by incentivizing not only quality, but the safety, sustainability, and consistency of U.S. beef; and
- Enhancing the competitiveness of U.S. beef in global export markets.

The Grassley-Fischer bill contains a Sense of the Senate that begins:

> SENSE OF THE SENATE.—It is the sense of the Senate that—
> (1) <u>all participants in the fed cattle market</u> have a responsibility to contribute to sufficient levels of negotiated trade of fed cattle in all cattle feeding regions in order to achieve competitive bidding and maximum transparency in all relevant markets and robust price discovery for the benefit of all market participants… (emphasis added)

Despite the rhetoric, the latest version of the Grassley-Fischer cash market mandate targets the mandate so it only applies to the largest beef packers. The reduction in the scope of the mandate is illuminating. On one hand, it confirms the benefits and importance of AMAs for producers, packers, and consumers: if the cash market provided the same benefits as AMAs, there would have been no need scale-back the mandate.

But applying the cash market mandate to only the largest packers reveals the proposed mandate for what it is: a punitive tool. Under the latest version of the

bill, if a beef packer gets too large, they will be forced to buy a certain percentage of cattle on the cash market. But per the analysis discussed above, it will be the producers supplying these packers who will pay much of the price. Gone is the illusion that the cash market is somehow more virtuous than other means of marketing cattle; gone is the argument that the cash market is necessary for transparency and price discovery. Instead, the cash market mandate is just that: a government mandate designed to punish the largest companies and their suppliers. In this sense, the mandate is an antitrust tool that could be used in any industry. If a company gets too large, it will be punished with a government mandate directing how the company can purchase inputs. Such a government mandate should elicit opposition from anyone interested in protecting the free market.

The Grassley-Fischer cash mandate is rooted in the belief that a government-managed market is preferable to the free market; in the belief that legislators know the best way for cattle producers to market cattle; in the belief that when black swan events occur, the government, with an inflexible, prescriptive mandate, will be better situated to respond than the resilient free market.

Ultimately, all cattle are purchased by a packer. The packer will buy cattle by whichever method producers want to market them. If cattle marketing become less efficient and transaction costs go up, the packer will spread those costs elsewhere. As Dr. Peel noted, when cattle were purchased on the average, high quality cattle were undervalued, and low-quality cattle were overvalued, receiving the average price. Packers have little incentive to differentiate cattle quality since they have to process all the cattle anyway. All that will be important to packers is to get the average right to generate a margin.

Market Transparency

Despite claims to the contrary, there is robust price discovery in the cattle and beef markets.

Congress established and USDA administers the Livestock Mandatory Reporting Act (LMR) program to facilitate open, transparent price discovery and provide all market participants, both large and small, with comparable levels of market information for slaughter cattle and beef, and other species. Under LMR, packers must report to AMS daily the prices they pay to procure cattle, and other information, including slaughter data for cattle harvested during a specified time period and with net prices, actual weights, dressing percentages, percent of beef grading Choice, and price ranges, and then AMS publishes the anonymized data.

AMS publishes 24 daily and 20 weekly cattle reports each week. Weekly reports start Monday afternoon and end the next Monday morning. These reports cover time periods, regions, and activities and the data include actual cattle prices.

Further, packers report all original sale beef transactions in both volume and price through the Daily Boxed Beef Report. This data is reported twice daily, at 11:00 a.m. and at 3:00 p.m. Central Time. The morning report covers market activity since 1:30 p.m. of the prior business day until 9:30 a.m. of the current business day. The afternoon report is cumulative, including all market activity in the morning plus all additional transactions between 9:30 a.m. and 1:30 p.m., and is on the USDA DataMart website. The boxed beef report covers both individual beef item sales and beef cutout values and current volumes, both of which are derived from the individual beef item sales data.

Few if any other industries have this magnitude of transparency via mandatory reporting of detailed price and product data on an on-going, daily basis, published for all other market participants – including up-stream sellers, downstream buyers, and direct competitors – to view, analyze, and use strategically.

Meat and Poultry Special Investigator Act

The Meat and Poultry Special Investigator Act duplicates existing regulatory enforcement authority and is unnecessary.

The Agricultural Marketing Service's P&S Division currently investigates allegations of impropriety and brings administrative cases and levies fines when warranted. Under certain circumstances, the P&S Division takes civil action working through the Department of Justice (DOJ). Penalties for violations of the Packers and Stockyards Act (P&S Act) can include civil penalties, permanent injunctions, fines, and even jail sentences.

The bill, however, would create a new office led by a political appointee with the same responsibilities for enforcing the same authority, the P&S Act, as the current P&S Division has. A duplicative regulatory office is wasteful and unnecessary, and a political appointee leading a regulatory enforcement office such as this would have to respond to the political whims of the administration.

Just this year, USDA established a complaint portal for producers to use to submit allegations of P&S Act violations to USDA and DOJ. The new tool provides producers and the P&S Division another resource for submitting, evaluating, and, if necessary, prosecuting violations. If the P&S Division staff are not doing their jobs, there are other ways to address it than by adding a political appointee into the regulatory and enforcement mix.

USDA is promulgating new proposed rules under the P&S Act, discussed further below, which are likely to have far reaching, unintended consequences. Establishing a politically appointed Special Investigator at the same time is a regulatory time-bomb. The Special Investigator (and staff) would feel emboldened

and obligated to bring as many cases as possible, whether warranted or not, to test the legal limits of the new rules. The resulting legal uncertainty and chaos will accelerate changes in livestock and poultry marketing that will likely add cost to producers and packers and up-end the supply chain.

The Special Investigator Act is a solution in search of a problem, and would result in a politically-driven, substantial expansion of USDA's regulatory regime.

Proposed Regulatory Actions by USDA Under the Packers and Stockyards Act will Adversely Affect Producers and Packers.

In June 2021, USDA announced plans to propose rules to "strengthen enforcement" of the Packers and Stockyards Act (PSA).[8] The expected proposed regulations would be problematic for several reasons, including their impact on livestock producers' options to market their cattle, as described.

The concepts expressed in USDA's announcement are not new and were considered, and rejected, in the past. When proposed, they will conflict with legal precedent in no less than eight federal appellate circuits, and will hurt livestock producers, packers, and consumers.

For example, USDA plans on re-proposing a rule to clarify that a plaintiff need not demonstrate harm to competition to bring and prevail in Packers and Stockyards Act litigation. Additionally, USDA indicates that it intends to "propose a new rule that will provide greater clarity to strengthen enforcement of unfair and deceptive practices, undue preferences, and unjust prejudices."[9] It is beyond dispute that eliminating the need for a plaintiff to show harm to competition, or likely harm to competition, will encourage litigation, most of it likely specious litigation. That threat will severely limit or terminate AMAs with all the adverse unintended consequences discussed.

One unintended consequence so far overlooked could come in the form of compromising the livestock and meat industry's significant gains and ambitious goals for improving sustainability.

Today, the industry produces more than twice as much beef with roughly the same number of cattle as in 1959, and 18 percent more beef than when the U.S. cattle herd hit its largest size in 1975. Farmers and ranchers produce beef using 33% less land, 12% less water, and with a 16% smaller carbon footprint in 2007 compared to 1977.[10] That is an astounding sustainability success story.

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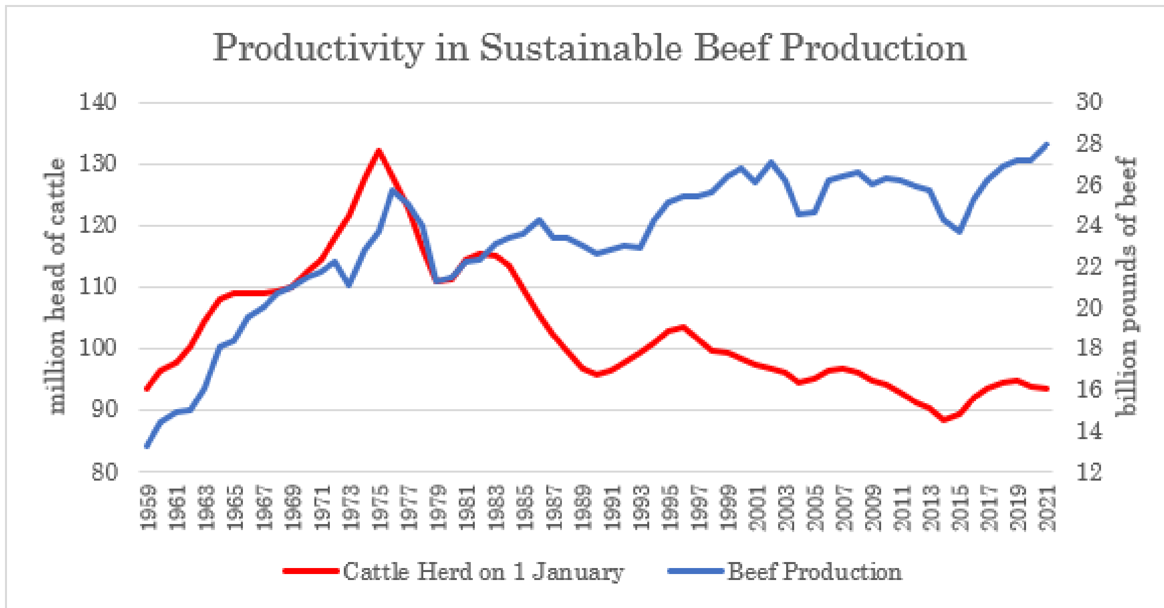
[8] https://www.usda.gov/media/press-releases/2021/06/11/usda-begin-work-strengthen-enforcement-packers-and-stockyards-act

[9] Ibid

[10] Neumeier and Mitloehner doi:10.2527/af.2013-0022



The U.S. meat industry cannot continue to build on this remarkable sustainable productivity growth and meet consumer expectations if the government restricts interactions between packers and producers. By design, USDA's proposed rules will discourage the use of AMAs – the very tools that have improved efficiency, productivity, and risk management over the past two decades and allowed the sector to meet consumer expectations for increased beef quality and sustainably produced cattle and beef.

As multiple agricultural economists[11] and cattle producers[12] have explained, AMAs increase market efficiency by transmitting market signals about consumers' preferences to producers. Restaurants, retailers, food service customers, and investors are moving rapidly to align their product and financial portfolios with environmental, social and corporate governance goals. This realignment – driven by consumers – will not be achieved by eliminating value-based marketing and turning back the clock to the days of commodity cattle purchased on the average.

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[11] See the following: The U.S. Beef Supply Chain: Issues and Challenges, Proceedings of a Workshop on Cattle Markets, Agriculture and Food Policy Center, Texas A&M University, 2021, cattle.pdf (tamu.edu); Anderson, et al, Univ. of Arkansas, 2022, https://cpb-us-e1.wpmucdn.com/wordpressua.uark.edu/dist/6/907/files/2022/01/CPDTA-analysis-01.18.22.pdf; Koontz, S., Costs and Benefits of Mandatory Negotiated Cash Participation in Fed Cattle Markets, 2022; Glynn Tonsor, Ph.D., Professor, Department of Agricultural Economics, Kansas State University, testimony before the Senate Agriculture Committee, June 23, 2021, https://www.agriculture.senate.gov/imo/media/doc/Testimony_Tonsor%2006.23.211.pdf

[12] See Gardiner, Testimony before the Senate Committee on Agriculture, Nutrition, and Forestry, June 23, 2021.

In his testimony before the House Agriculture Committee's Livestock and Foreign Agriculture Subcommittee, Dr. Jayson Lusk stated:

> [S]trengthening of consumer demand for beef over the past several decades has occurred over a period in which there was increased use of formula pricing that rewarded quality improvements. Eroding the ability of consumers, retailers, and packers to incentivize quality through formulas and vertical coordination may have detrimental impacts on demand.[13]

Conclusion

The discussion above demonstrates the complexity of the cattle and beef markets that defy overly simplistic policy prescriptions. Market fundamentals drive the cattle and beef markets, and what we saw before and during the course of the pandemic was to be expected. Indeed, cattle and beef markets were not the only sectors of the economy adversely impacted in the past two years. Congress and USDA should not make radical changes to the cattle and beef markets: such changes will up-end the markets, increase costs for the entire supply chain, including for consumers during this time of record inflation, and bring unintended consequences.

The North American Meat Institute is prepared to discuss these issues and work with the Committee on the issues facing the industry. Thank you for the opportunity to provide this testimony.

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[13] Jayson Lusk, Ph.D., Distinguished Professor and Head, Department of Economics, Perdue University, testimony before the House Agriculture Subcommittee on Livestock and Foreign Agriculture, July 28, 2021, https://docs.house.gov/meetings/AG/AG29/20210728/113973/HHRG-117-AG29-Wstate-LuskJ-20210728.pdf