Statement of the American Farm Bureau Federation

TO THE SENATE COMMITTEE ON THE JUDICIARY

"CONSOLIDATION AND COMPETITION IN THE U.S. SEED AND AGROCHEMICAL INDUSTRY"

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Thank you Mr. Chairman for the opportunity to meet with the Committee. My name is Bob Young, I am the Chief Economist and Deputy Director for Public Policy for the American Farm Bureau Federation (AFBF). Farm Bureau is the largest general farm organization in the country with 50 state organizations plus Puerto Rico. Our members grow apples to zucchini from Maine to Hawaii and everywhere and everything in between. We have conventional farmers, organic farmers, heavy involvement in farmers markets and local foods programs as well as being active in the policy arena.

The timing on this hearing into the effects of the recent wave of merger and acquisition (M&A) activity in the agricultural inputs space could not be better. You are all well aware of the recent Bayer/Monsanto merger, which is only the latest in the list that includes Dow/Dupont/Pioneer, ChemChina and Syngenta as well as Potash and Agrium.

Before going into the individual mergers it is probably wise to understand the driving forces behind this surge in M&A actions at this point in time. Net Farm income peaked in 2013 at $123.8 billion. United States Department of Agriculture (USDA) places 2016 estimates at $71.5 billion. This is one of the steepest declines in farm income on record. Let me just say that if this income situation does not turn around in the next year or so, we will have a sector under a great deal of stress when we write the next farm bill.

Given this fall in income, farmers have—or have attempted—to adjust their spending on inputs. USDA breaks out seed, pesticides and fertilizer/soil amendments. These are the three main areas affected by these mergers. In 2000, these three categories accounted for $26 billion ($32 billion 2009$'s). As recently as 2013 these same three categories totaled $65 billion ($61 billion 2009$'s). As farm income has come down and fertilizer prices in particular have fallen from their earlier peaks, these same three categories have dropped to $58 billion ($53 billion 2009$'s).

Of those three categories, seed costs showed substantial growth as the farm economy improved in the 2000's and early 2010's. Seed costs alone—part of the total above—went from $7 billion in 2000 to $22 billion in 2012. Since 2012, however, seed costs have held in the $21 to $22 billion range.

At the same time input suppliers are facing a flattening or declining revenue environment, they are also facing growing challenges in bringing new products to market. One positive approach a company can take to improve market share for example is to introduce new products, to provide a better service to their customers. Nearly all of the companies involved in the recent M&A activity have been, are, and are expected to continue to be heavily involved in the development of new products. The challenge is the time and money needed to bring a new product—chemical or genetic—to the market. Recent studies suggest it costs $136 million and takes 13 years of research and regulatory oversite before bringing that new seed to market. Further, firms frequently have to wade through litigation as well and that can drag the process out years longer.

This softening of farm income and subsequent efforts on the part of farmers to bring costs under some kind of control is one of the main justifications on the companies' part to look toward M&A activity as a way to continue to show overall sales growth and to increase market share.

AFBF understands the business case for any one of the mergers as well as the China National Chemical Corporation purchase of Syngenta.

At this point in time we have the proposed creation of two major agricultural chemical/genetics companies from what had been effectively two chemical and two genetics companies. As plant genetics technology is ever more connected to the chemistry, there appear to be some real benefits in having a chemical company combine with one more focused on crop genetics. As new chemistries are developed the plant genetics effort can proceed alongside, hopefully reducing the research time needed to bring a fully integrated product to market.

AFBF has had several conversations with the respective companies regarding their plans for research and innovation budgets post-merger. All have indicated the intent to continue funding close to or above where current combined levels are. Again, these are just words to a certain extent, but when one understands the importance of new product development, of reaction to new crop, insect and weed issues, it would seem reasonable that these companies' best business interests are to continue this strong commitment to innovation.

A special word is merited for the Dow/DuPont/Pioneer and the Bayer/Monsanto mergers. Again, the case can be made, both at this point in time as well as from a product development standpoint, for the combination of chemical and plant genetics into one firm. But once one firm emerges, it probably puts the rest of the industry at a disadvantage, until and unless another similarly structured firm is created. In other words, we are better served as an industry with at least two of these chemical/genetics firms, than would be the case with only one. While one can probably envision a future where farmers are faced with choosing one set of chemistry/plant varieties over another, is this so different from the longstanding rivalry between equipment makers John Deere and Case IH? And on the Bayer/Monsanto merger in particular, one can't help but find it interesting we have a German company engaging in the largest takeover in that country's history to acquire a technology that their own farmers are precluded from planting.

The purchase of Syngenta by ChemChina is also has an area of concern. The purchase by and of itself would not probably raise issues. The pending sale provides the firm with substantial capital, allows another country to gain some significant intellectual capital in a legitimate fashion and essentially does not change the number of firms offering services in the United States market. From a standard business case, there would be little cause to object. But it is not just a simple business case—it is a nationally owned company making the purchase. Product approval—new seed traits as an example—is not always straightforward in the Chinese market. Because of the size of the market and the importance to United States grain and oilseed exports, it is critical that all companies work on a level playing field in terms of product approval in the Chinese market. With a Chinese national firm owning one of the leading agricultural innovators, there is reason to be concerned about preferential product approval for that company in the future which could create subsequent challenges and implications back into the United States market.

The Potash/Agrium merger brings a fertilizer company together with a company more focused on direct-to-farmer retailing. Agrium has been acquiring additional farm-retail outlets beyond the Potash merger activity as well, further enhancing its presence in the United States.

Any one of these M&A events would be well understood. Synergies and savings are likely to be generated, market share improved, a stronger corporate structure created for facing the regulations and other hurdles to bringing product to market are just a few examples. The challenge to those involved in the agricultural space from a farmer's perspective is the sheer number and scale of this activity in such a short period of time. We will go from six major companies to three (from Dow, DuPont, Bayer, Monsanto, Potash and Agrium to Dow/DuPont, Bayer/Monsanto and Potash/Agrium) in a period of a few months. Everyone's knee-jerk reaction is to think that increased concentration will lead to higher prices for these inputs. Knees tend to jerk reflexively, but sometimes they jerk with reason. AFBF is suggesting that the review of these mergers consider not only the market concentration/structure that will result from the individual company actions, but examine the structure of the entire industry in a post-merger environment. There will be considerable market capacity in the Dow/DuPont/Pioneer and the Bayer/Monsanto companies. It is good that two will exist in order to drive a level of competition in the space, but will these two be so large that they preclude growth or delivery capacity by other firms?

AFBF understands the business forces driving these mergers. We have been very active in the regulatory space, trying to lower the regulatory hurdles here and abroad for the approval of new technology. Our members know the need to keep that new technology stream as active as possible. We have had several—and repeated—assurances from the companies involved as to their intent to maintain as strong an innovation arm as they can. We have no reason to doubt, but we also are reminded of the old line: trust, but verify.