Concentration in Agriculture and an Examination of the JBS/Swift Acquisitions

Testimony

of the

Ranchers-Cattlemen Action Legal Fund, United Stockgrowers of America (R-CALF USA)

To the

United States Senate Judiciary Subcommittee on Antitrust, Competition Policy, and Consumer Rights

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Presented By

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Thank you, Chairman Kohl and members of the Subcommittee, for this opportunity to testify about important issues affecting the United States cattle industry, particularly the likely effects the proposed JBS/Swift acquisitions would have on cattle industry competition.

I am Bill Bullard, CEO of the Ranchers Cattlemen Action Legal Fund, United Stockgrowers of America (R-CALF USA). R-CALF USA is a membership-based, national, non-profit trade association that represents exclusively United States farmers and ranchers who raise and sell live cattle. We have thousands of members located in 47 states and our membership consists of seed stock producers (breeders), cow/calf producers, backgrounders, stockers and feeders. The demographics of our membership are reflective of the demographics of the entire U.S. cattle industry, with membership ranging from the largest of cow/calf producers and feeders to the smallest of cow/calf producers and feeders. Our organizational mission is to ensure the continued profitability and viability of independent U.S. cattle producers.

Today I will present an overview that will describe the unique characteristics of both the U.S. live cattle industry and the U.S. live cattle market: characteristics that will demonstrate that the JBS/Swift acquisition would both lessen competition within U.S. cattle markets and facilitate the exercise of monopsony power to the detriment of the entire industry. All of the exhibits referenced in my written testimony are available on R-CALF USA's website listed on the cover page under the heading "Competition Issues."

SUMMARY AND RECOMMENDATIONS

The U.S. live cattle industry is a diverse and vibrant value-added industry that is both separate and distinct from the beef packing industry and highly susceptible to any further reduction in competition and any additional exercise of market power. The live cattle industry is the largest segment of U.S. agriculture. With annual revenues of approximately $50 billion, it contributes more to the prosperity of Rural America than any other agricultural segment, and this prosperity is distributed throughout the U.S., with 11 states generating more than $1 billion annually.

It is important that the Subcommittee realize that while the four major beef packers control approximately 80 percent of the market for slaughter-ready steers and heifers, that market represents only 27 million of the 45 million cattle that are marketed each year. In fact, when all slaughter cattle markets are considered, including cow and bull slaughter, the sales of live cattle that occur among and between the various value-added segments of the industry that are *not* sold to beef packers accounted for nearly 30 percent of the industry's annual revenue generation. In other words, though the slaughter-ready steer and heifer market is the industry price-maker, directly impacting the 60 percent of annual cattle marketed to the four major packers and indirectly impacting the remaining 40 percent of cattle sold to smaller packers and other cattle producers, it is a fallacy to believe, as the major packers would like you to believe, that the entire U.S. cattle industry is merely a supplier of packer inventories.

The U.S. cattle industry can be viewed as a pyramid, with 970,000 independent cattle-producing businesses filling its base. Most cattle operations have fewer than 50 head of cattle, and fewer than 80,000 beef cattle operations have herd sizes of more than 100 head. This group of fewer than 80,000 businesses would be at greatest risk of being forced to exit the industry due to the price effects of monopsony power because it is presumed that this group is comprised of more full-time cattle producers wholly dependent on competitive cattle prices for their livelihoods.

Like the packing industry, the feeding sector of the live cattle industry – the sector that fattens cattle in feedlots preparing them for slaughter – has become increasingly concentrated in recent years. Presently, at the apex of the cattle industry pyramid, are less than 2,500 feedlots that feed and sell the lion's share of slaughter-ready cattle, over 23 million head, mostly to the four major beef packers.

These fundamental industry facts are important to this Subcommittee's investigation of the proposed JBS/Swift acquisitions because they help demonstrate how even relatively small impacts on the price of 27 million steers and heifers can have a compounding impact on hundreds of thousands of cattle producers that generate $50 billion annually from the sale of 45 million cattle. A 3 percent price distortion, for example, would result in the loss of $1.5 billion to nearly 970,000 cattle operation, which would be a serious blow to thousands of rural economies. The viability of the numerous value-added segments of the U.S. live cattle industry is intrinsically tied to the price of the industry's principal product – slaughter-ready cattle, and it is this segment of the industry that is most susceptible to monopsony power wielded by an extremely concentrated beef packing industry and that serves as the portal through which monopsony power can invade the entirety of the U.S. live cattle industry.

The U.S. cattle industry has already partially succumbed to the exercise of market power emanating from a highly concentrated beef packing industry – at current concentration levels. The number of U.S. cattle operations is declining rapidly, with 40 percent of the operations in existence in 1980 having already exited the industry. The size of the U.S. cattle herd is contracting and the industry's bellwether cattle cycle, historically the indicator of competitive supply and demand signals, which rose and fell in 10 to 12 year cycles, is now disrupted, if not lost all together. The U.S. hog industry is further advanced in its consolidation with meatpackers and the U.S. Department of Agriculture (USDA) recently attributed the loss of the hog industry's cycle as a function of structural changes to the industry. Thus, there is a causal relationship between the loss of a competitive livestock cycle and a changed industry structure marked by concentration and consolidation.

The alarming irony is that the U.S. cattle industry continued its contraction during the decade after 1993, a period during which domestic beef consumption increased significantly. It is counterintuitive and contrary to competitive market principles that a decade of nearly continuous increases in domestic beef consumption would lead to domestic industry contraction rather than domestic industry revitalization. But, that is precisely what has already happened *without* the added burden of less competition and more market power that would become manifest if the JBS/Swift acquisitions are consummated.

The U.S. hog industry, which lost 90 percent of its participants since 1980, no longer is comprised of the critical mass of participants necessary to sustain a national, competitive market.

The U.S. cattle industry, however, still consists of hundreds of thousands of independent businesses that can, indeed, sustain a robust, competitive market, provided it is protected from further erosion of competition and monopsony power. Despite its present, diminutive size, the U.S. hog industry provides valuable insights into the future of the U.S. live cattle industry should increased concentration in the beef packing industry and increased monopsony power continue unabated. It also reveals the harm to consumers arising from the meatpackers' excessive control over livestock production, which is evidenced by an upward trend in retail pork prices paid by consumers and a downward trend in hog prices paid to producers.

The characteristic nature of cattle and the characteristics of the U.S. live cattle market make the U.S. live cattle industry uniquely susceptible to monopsony power. These characteristics include for cattle:

1. The longest biological cycle of any farmed animal, making it difficult for the industry to react to changes in demand.

2. Slaughter-ready cattle are highly perishable products that must be marketed within a narrow window of time; otherwise, the animals would degrade in quality and value.

3. The feasibility of transporting cattle long distances decreases as cattle approach slaughter weight, resulting in the regionalization of markets defined by transportation constraints.

For cattle markets:

1. Concentration levels in the U.S. meatpacking industry are already among the highest of any industry in the United States and are considered by some researchers to be well above levels generally considered to elicit non-competitive behavior and result in adverse economic performance.

2. The live cattle market is inherently fragile. 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.

3. The U.S. cattle market is highly sensitive to even slight changes in cattle supplies. The U.S. International Trade Commission has found that a 1 percent increase in fed cattle numbers is expected to result in a 2 percent decrease in price.

4. The cattle market is sensitive to shifts in cattle procurement methods, with price distortions ranging up to 3 percent in earlier studies, though some researchers now believe these earlier studies inappropriately focused on market outcomes and overlooked important elements of the competitive process in the beef packing industry.

5. 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.

6. The combination of the perishable nature of slaughter-ready cattle and limited weekly slaughter capacity creates market access risk for U.S. cattle producers within the U.S. cattle market. Market access risk refers to the availability of a timely and appropriate market outlet and evidence suggests that producers who choose forward contracts are willing to give up some revenue in order to secure market access

7. The Regional Herfindahl-Hirschman Indices (RHHI) are already exceedingly high in several regions of the U.S., where RHHI indices ranging from 2,610 to 4,451.

8. Transparency in the U.S. live cattle market is already limited as was reported by the Government Accountability Office (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. And, it is likely the JBS/Swift acquisition would reduce price reporting due to the 3/70/20 confidentiality rule.

9. 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. This phenomenon was found to be a function of the individual producer's inability to coordinate action.

The JBS/Swift acquisitions would significantly increase the concentration of the beef packing industry and would facilitate significantly the exercise of market power. Albeit too late, a USDA study recently acknowledged that market power emanates from the similarly concentrated pork packing industry, concluding there was a "significant presence of market power in live hog procurement." This study also found a causal relationship between the use of captive supply livestock and depressed livestock prices, concluding that a small increase in packer-owned hogs caused cash market prices to decrease. Of particular concern is that the JBS/Swift acquisitions would result in both the increased use and effectiveness of captive supply cattle for purposes of depressing U.S. cattle prices by increasing the beef packing industry's ability to further restrict producer access to market outlets.

The present use of captive supplies and other strategies designed to effect market power by beef packers is already harming the U.S. live cattle industry. Empirical evidence shows that beef manufacturers have used their market power to coerce political support from producers. They have engaged in coordinated actions resulting in reduced prices for live cattle. They have imposed disparate discounts for similar quality specifications. They have imposed pricing strategies that defy competitive market fundamentals. And, they have begun to subdivide the cattle market by denying access to the market for certain subclasses of cattle.

The JBS/Swift acquisitions would exacerbate the monopsony power that presently enables the foregoing anticompetitive practices. To make matters worse, JBS/Swift has a history of being a bad actor, as evidenced by media reports that it engaged in anticompetitive practices against Brazilian cattle producers. Further, the vertical integration component of the JBS/Swift acquisitions – the acquisition of the nation's largest feedlot – would significantly intensify the degree of market power emanating from this holding because, unlike the present owner, JBS/Swift would have packing plants in close proximity to the feedlots and would have the daily slaughter capacity to slaughter all the cattle it feeds, thus increasing the percentage of captive supply cattle that are withheld from the cash market. In addition, JBS/Swift would have access to information regarding the value of feeder cattle it intends to purchase for feeding long before independent producers would have such information. The information available to JBS/Swift would be knowledge of the type and quantity of future purchasing orders for beef – essentially insider information – that would accord JBS/Swift a distinct advantage when competing against independent cattle producers for feeder cattle.

Finally, the JBS/Swift acquisitions would most likely violate both the spirit and express prohibitions contained in the Packers and Stockyards Act of 1921, which was designed to afford the U.S. live cattle industry with protections beyond the traditional concerns of efficiency and market competition. In particular, it was designed to prohibit unfair, deceptive, and manipulative acts and practices that have the effect of manipulating or controlling prices, such as those acts and practices described above, as well as to prohibit the creation of a monopoly. Inasmuch as creation need not occur instantaneously, the JBS/Swift acquisitions would clearly catapult the beef packing industry toward monopolization nationally, and would likely result in complete monopolization in certain geographic regions.

Consummation of the JBS/Swift acquisitions would likely be the proverbial straw that breaks the camel's back. The U.S. cattle industry remains in a continual state of contraction, and evidence of market power deployment abounds. Just as the U.S. live hog industry suffered a mass exodus of hundreds of thousands of producers, without Congress even knowing about it, so too could the U.S. cattle industry suffer the same consequence. Congress would not likely know about a cattle industry exodus either, as it would occur one cattle operation in one rural community at a time.

R-CALF USA appreciates the opportunity to express its concerns regarding the JBS/Swift acquisitions and, for the foregoing reasons, respectfully requests that the Subcommittee conduct a thorough, probing analysis of the JBS/Swift acquisitions and that it expand its investigation to include a thorough, probing analysis of the current market environment in which these acquisitions are proposed. R-CALF USA is confident that such a comprehensive investigation would reveal the need to forestall indefinitely the JBS/Swift acquisitions as well as to initiate immediate remedial action to halt the anticompetitive practices already prevalent within the U.S. live cattle industry.

I. The U.S. Cattle Industry is a Diverse and Vibrant Value-Added Industry that is Both Separate and Distinct from the Beef Packing Industry and Highly Susceptible to Market Power.

As a preliminary matter, it is important that the Subcommittee realize that the U.S. live cattle industry is the largest segment of American agriculture. With gross receipts from the sale of live cattle at approximately $50 billion annually, the live cattle industry contributes more to the prosperity of Rural America than any other agricultural segment, and this prosperity is widely distributed throughout the U.S., with 11 states generating more than $1 billion annually.[1]

It is equally important that the Subcommittee realize that the U.S. live cattle industry is a value-added industry separate and distinct from the U.S. beef packing industry.[2] While the four major beef packers – Tyson, Cargill, JBS/Swift, and National Beef Packing Co. (National) – currently control approximately 80 percent of the steer and heifer slaughter in the United States,[3] these major beef packers are involved in transactions for the purchase of only about 27 million[4] of the 45 million cattle that are marketed each year.[5] Thus, the four major packers that control 80 percent of the U.S. steer and heifer slaughter, and which have worked diligently to perpetuate the misperception that the U.S. live cattle industry is merely a supply source for packer inputs, is involved in the direct purchase of only 60 percent of the 45 million sales transactions that annually contribute $50 billion to the United States' economy. In fact, when total beef packer slaughter is included, which would include U.S. cow and bull slaughter, the sale of live cattle *not* destined for sale to the beef packing industry accounted for over 27 percent of the live cattle industry's annual revenues.[6]

B. Like the Beef Packing Industry, the Feeding Sector of the U.S. Live Cattle Industry has become Increasingly Concentrated.

The structure of the U.S. cattle industry is like that of a pyramid. Filling the base of this pyramid in 2007 were 967,440 cattle operations, including both dairy and beef cattle operations.[7] This represents 40 percent fewer U.S. cattle operations than existed in 1980, which numbered 1.6 million at the time.[8] Of the 967,440 remaining cattle operations, only 757,900 are beef cattle

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[1] *See* U.S. Farm Sector Cash Receipts from Sales of Agriculture Commodities, 2004-2008F, U.S. Department of Agriculture, Economic Research Service, available at http://www.ers.usda.gov/briefing/farmincome/data/cr_t3.htm.

[2] *See* 2007 North American Industry Classification System (NAIS) Codes and Titles, U.S. Census Bureau, available at http://www.census.gov/naics/2007/NAICOD07.HTM (the live cattle industry is a subset of the U.S. agriculture industry whereas beef packers are a subset of manufacturers of nondurable goods).

[3] *See* Packers and Stockyards Statistical Report, 2005 Reporting Year, Table 27 – Steer and Heifer Slaughter Concentration by 4, 8, 20, and 50 Largest Firms for Selected Years 1980-2005, U.S. Department of Agriculture, Grain Inspection Packers and Stockyards Administration, February 2007, at 44, available at http://archive.gipsa.usda.gov/pubs/2005_stat_report.pdf.

[4] *See* Livestock Slaughter 2007 Summary, U.S. Department of Agriculture, National Agricultural Statistics Service, March 2008, at 13 (the actual number of steers and heifers slaughtered was 27,297,800 head and the total number of cattle slaughtered in the U.S. was 33,145,000 head), available at http://usda.mannlib.cornell.edu/usda/current/LiveSlauSu/LiveSlauSu-03-07-2008_revision.pdf.

[5] *See* Meat Animals Production, Disposition, and Income 2006 Summary, U.S. Department of Agriculture, National Agricultural Statistics Service, April 2007, at 8, available at http://usda.mannlib.cornell.edu/usda/current/MeatAnimPr/MeatAnimPr-04-27-2007.pdf.

[6] *See id.* (the percentage was calculated using the 2006 value of production ($35,740,774,000) and the 2006 cash receipts from marketing ($49,148,364,000) (note that the cash receipts from marketing understate the actual cash receipts because it excludes interfarm sales within the same state. *See id.*, at 27.)).

[7] *See* Farms, Land in Farms, and Livestock Operations, U.S. Department of Agriculture, National Agricultural Statistics Service, Sp Sy 4 (08) a, February 2008, at 14.

[8] *See* Federal Register, Vol. 72, No. 152, Wednesday, August 8, 2007, at 44,681, col. 2.

operations, and the vast majority of these operations (585,050) have fewer than 50 head of cattle.[9] Only 78,360 beef cattle operations have herd sizes of more than 100 head.[10] While all 757,900 beef cattle operations would be harmed by the lessening of competition and increased exercise of market power that would result from the JBS/Swift acquisitions, it is most likely that producers within the class of operations with more than 100 head, the class with fewer than 80,000 operations, would be at greatest risk of being forced to exit the industry due to lower cattle prices, based on the presumption that this class is comprised of more full-time cattle producers wholly dependent on competitive cattle prices for their livelihoods.

Moving toward the top of this pyramid are cattle feeders that feed cattle in feedlots until they reach slaughter weight, at which time the cattle would be sold directly to beef packers for slaughter. Like the beef packing industry, feedlots have become increasingly concentrated. In 1995, 41,365 feedlots marketed 23.365 million cattle.[11] By 2002, only 2,209 feedlots marketed 23.637 million cattle.[12] The remaining 4.070 million cattle fed in feedlots in 2002 were fed in 93,000 feedlots with capacities of less than 1000 head.[13]

C. The Concentrated Feeding Sector is the Portal through Which Market Power Invades the Entire U.S. Live Cattle Industry.

Thus, while 45 million cattle are marketed annually within the base of the cattle industry pyramid among and between 967,440 cattle operations, the vast majority of steers and heifers slaughtered each year are funneled through only about 2,200 feedlots, which in turn sell the lion's share of 27 million steers and heifers to only four major beef packers. And it is here, at the apex of the pyramid, where 60 percent of the cattle marketed annually are marketed to only four beef packers, that the price of cattle is established, and this price, whether competitive or not, is the price that becomes the basis for pricing the remaining 40 percent (18 million) of cattle that are *not* sold to the four major meatpackers. This is because the price for slaughter-ready steers and heifers received by cattle feeders is transferred, at least in part, backward throughout the live cattle production cycle, impacting seed stock producers, cow/calf producers, backgrounders, and stockers. The market for slaughter-ready steers and heifers – the market directly impacted by the JBS/Swift acquisitions – is the price-making market for the entire $50 billion U.S. live cattle industry.

The significance of these basic facts about the U.S. live cattle industry is profound, particularly when evaluating the potential impacts from the proposed JBS/Swift acquisitions. For example, if the Subcommittee were to look only at the JBS/Swift acquisitions' direct impacts, i.e., the impacts on the sale of only 27 million cattle annually, and found such impacts to be "small," the Subcommittee would completely miss the compounding impacts that even a

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[9] *See* Farms, Land in Farms, and Livestock Operations, U.S. Department of Agriculture, National Agricultural Statistics Service, Sp Sy 4 (08) a, February 2008, at 14.
[10] *Ibid*.
[11] Structural Changes in Cattle Feeding and Meatpacking, Clement E. Ward and Ted C. Schroeder, Managing for Today's Cattle Market and Beyond, Oklahoma State University and Kansas State University, respectively, attached hereto as Exhibit 1.
[12] Cattle Final Estimates 1999-2003, U.S. Department of Agriculture, National Agricultural Statistics Service, Statistical Bulletin Number 989, April 2004, at 75.
[13] *Ibid*.

small lessening of competition or exercise of market power in the slaughter-ready steer and heifer market would have on the annual sale of 45 million cattle and, consequently, on the welfare of hundreds of thousands of independent cattle producers and thousands of rural communities that depend on a vibrant, competitive U.S. live cattle industry.

Indeed, noted Oklahoma State University economist Clement E. Ward found that "[r]esearch to date suggests price impacts from packer concentration have been negative in general, but small."[14] He found that most studies found price distortions of 3 percent or less, though 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."[15]

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.[16] 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."[17]

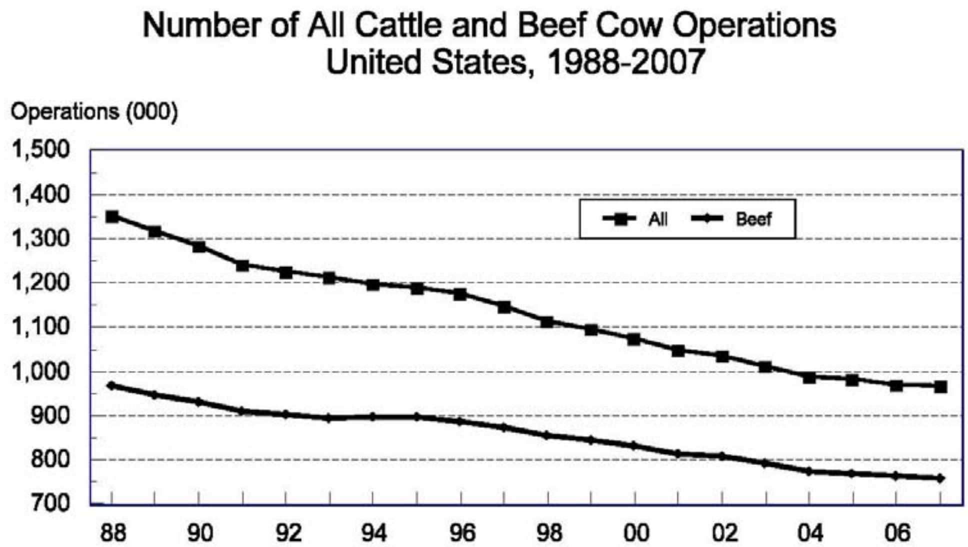
Notwithstanding the potential that most studies have overlooked important elements of the competitive process but nevertheless found "small" negative impacts due to packer concentration and monopsony power, the application of even a 3 percent price distortion on the entire $50 billion live cattle industry would result in a loss of $1.5 billion to U.S. cattle producers. Importantly, this is the level of harm that likely accrues today, even without the additional market concentration and consummate increase in market power that would be expected from the JBS/Swift acquisitions. Importantly, the concentrated feeding sector is the portal through which even small market-power induced price distortions can invade and cripple the entire U.S. live cattle industry.

D. The U.S. Cattle Industry has Already Partially Succumbed to Increased Market Power

The U.S. cattle industry has already partially succumbed to the exercise of market power emanating from the highly concentrated beef packing industry – at current concentration levels, and it is uniquely susceptible to the exercise of market power. The effects of market concentration and market power have contributed to 1) the rapid decline in the number of U.S. cattle operations as discussed above and shown in Figure 1 below:

[14] Packer Concentration and Packer Supplies, Clement E. Ward, Oklahoma Cooperative Extension Service, AGEC-554, at 554-5, attached hereto as Exhibit 2.
[15] 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, attached hereto as Exhibit 3.
[16] Testing for Market Power in Beef Packing: Where are We and What's Next?, Lynn Hunnicutt, Quinn Weninger, Utah State University, August 1999, at 5, attached hereto as Exhibit 4.
[17] *Id.*, at 1

Figure 1

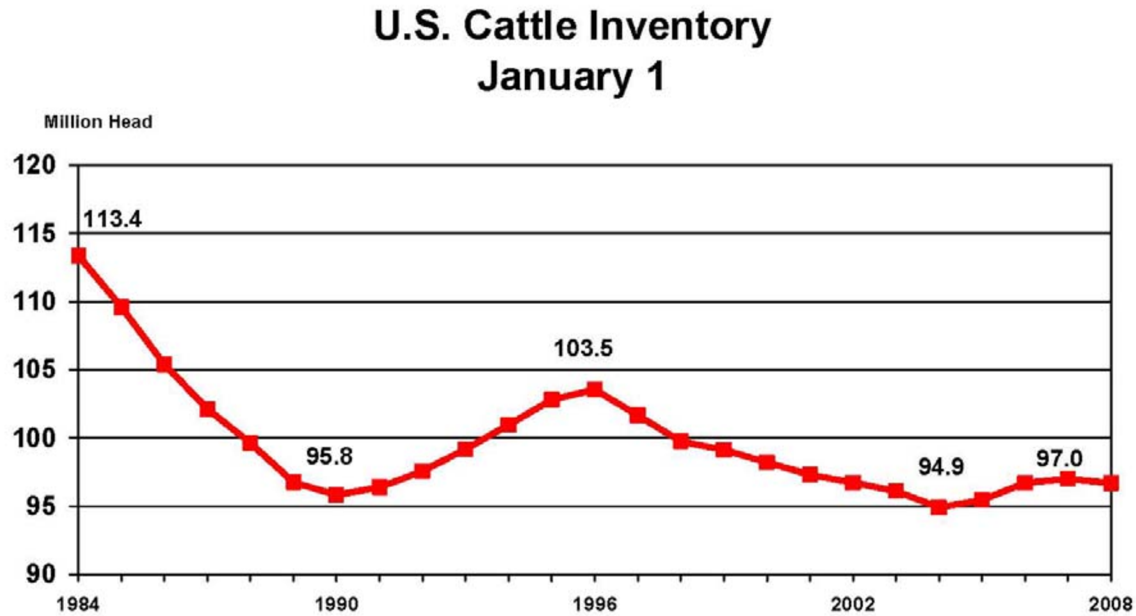


Source: Farms, Land in Farms, and Livestock Operations, 2007 Summary, U.S. Department of Agriculture, National Agricultural Statistics Service, February 2008, at 14.

Figure 1 shows that the U.S. live cattle industry experienced contraction inverse to the increased concentration by the top four steer and heifer slaughter firms, which rose from 35.7 percent in 1980 to 81.1 percent in 2004.[18] The effects of market concentration and market power have contributed also to 2) the contraction of the U.S. cattle herd and the disruption, if not the loss of the historical cattle cycle – itself a bellwether indicator of the declining competitiveness of the U.S. live cattle industry – as shown in Figure 2 below.

[18] Testing for Market Power in Beef Packing: Where are We and What's Next?, Lynn Hunnicutt, Quinn Weninger, Utah State University, August 1999, at 1, attached hereto as Exhibit 4.

Figure 2



Source: Cattle, U.S. Department of Agriculture, National Agricultural Statistics Service, February 2008, at 1.

The U.S. Government Accountability Office ("GAO") explained that the U.S. live 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."[19] The U.S. cattle cycle has historically occurred every 10-12 years.[20] In 2002 the USDA acknowledged that "the last cycle was 9 years in duration; the present cycle is in its thirteenth year, with two more liquidations likely."[21] In late 2005, the USDA declared that the U.S. was "in the early herd expansion stages of the new cattle cycle."[22] However, in late 2007, the 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."[23] These analysts, according to the USDA, "suggested that the cattle cycle has returned to its liquidation phase."[24]

The foregoing discussion reveals that the historical U.S. cattle cycle began to function erratically during the last decade and continues doing so today, suggesting that the competition-

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[19] 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.

[20] *See* The U.S. Beef Industry: Cattle Cycles, Price Spreads, and Packer Concentration, Kenneth H. Mathews et al., U.S. Department of Agriculture, Economic Research Service, April, 1999, at 3, attached as Exhibit 5.

[21] 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.

[22] Livestock, Dairy, & Poultry Outlook, U.S. Department of Agriculture, Economic Research Service, December 16, 2005, at 8, available at http://www.ers.usda.gov/publications/ldp/dec05/ldpm138t.pdf.

[23] Livestock, Dairy, & Poultry Outlook, U.S. Department of Agriculture, Economic Research Service, December 19, 2007, at 5, available http://www.ers.usda.gov/Publications/LDP/2007/12Dec/ldpm162.pdf.

[24] *Id.*

induced demand/supply signals that once led to expectations about changes in cattle prices have been disrupted. While cattle industry analysts ponder this phenomenon, in February 2008 the USDA attributed a similar disruption that was occurring in the U.S. hog industry cycle to the hog industry's new structure. The 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."[25] This "dramatically" changed structure includes the consolidation of the industry, where "fewer and larger operations account for an increasing share of total output."[26]

As *was* the case in the hog industry, a functioning cattle cycle, itself, is 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.[27]

The recently acknowledged disruption of the historical U.S. cattle cycle, as discussed above, is a bellwether indicator that competition has lessened in the U.S. live cattle industry; and, as the 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 alarming irony, as shown in Figure 3 below, is that the U.S. cattle industry was contracting, both in terms of the number of cattle operations and herd size, during the decade after 1993 when domestic beef consumption began increasing significantly. The polynomial trend lines in Figure 3 reveal that domestic beef production could not keep pace with increased domestic beef consumption and the volume of domestic cattle slaughter trended downward in the face of this favorable consumption/demand situation.

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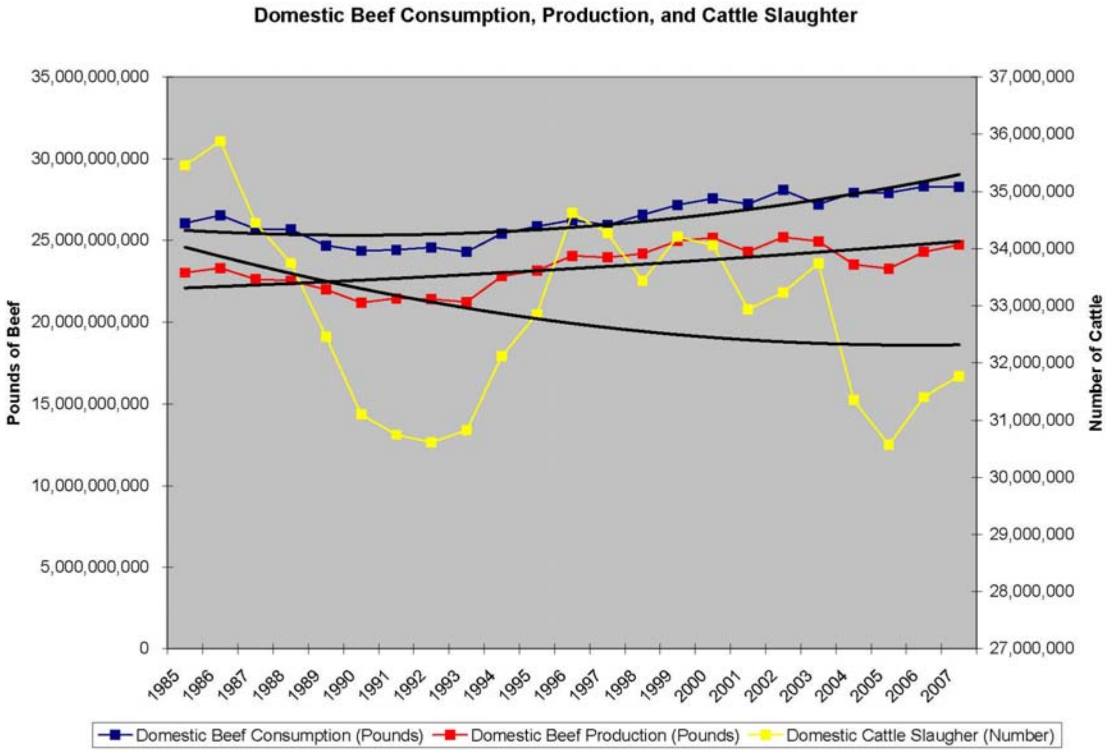
[25] Livestock, Dairy, & Poultry Outlook, U.S. Department of Agriculture, Economic Research Service, February 15, 2008, at 14, available at http://www.ers.usda.gov/Publications/LDP/2008/02Feb/ldpm164.pdf.

[26] Hog Operations Increasingly Large, More Specialized, Amber Waves, U.S. Department of Agriculture, Economic Research Service, February 2008, available at http://www.ers.usda.gov/AmberWaves/February08/Findings/HogOperations.htm.

[27] Cattle: Background, Briefing Room, U.S. Department of Agriculture, Economic Research Service, updated June 7, 2007, available at http://www.ers.usda.gov/Briefing/Cattle/Background.htm.

Figure 3



Data Source: **Domestic beef consumption data obtained from USDA-FAS.**[28]
Domestic beef production calculated by subtracting beef-equivalent weights of imported cattle from production data compiled by USDA-ERS.[29]
Domestic slaughter calculated by subtracting imported cattle numbers from commercial U.S. slaughter.[30]

Another unfavorable phenomenon revealed by Figure 3 is that the shortfall between domestic production and domestic consumption, during each of the years 2004, 2005, 2006, and 2007, was greater than at any time in recent history (at least since 1961).

The foregoing data run counter to competitive market principles that suggest a decade of nearly continuous increases in beef consumption would lead to industry revitalization, not industry contraction. R-CALF USA respectfully requests that the Subcommittee rigorously investigate this counterintuitive profile of the U.S. cattle industry to determine the true extent to which market concentration and market power has irreparably harmed the U.S. cattle industry.

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[28] *See* U.S. Department of Agriculture, Foreign Agricultural Statistics Database, *Production, Supply and Distribution Online*, available at http://www.fas.usda.gov/psd/complete_files/LP-0111000.csv.

[29] *See* Table 94, Beef Supply, Utilization, and Per Capita Consumption, 1970-2005, Red Meat Yearbook, U.S. Department of Agriculture, Economic Research Service, available at http://usda.mannlib.cornell.edu/MannUsda/viewDocumentInfo.do?documentID=1354.

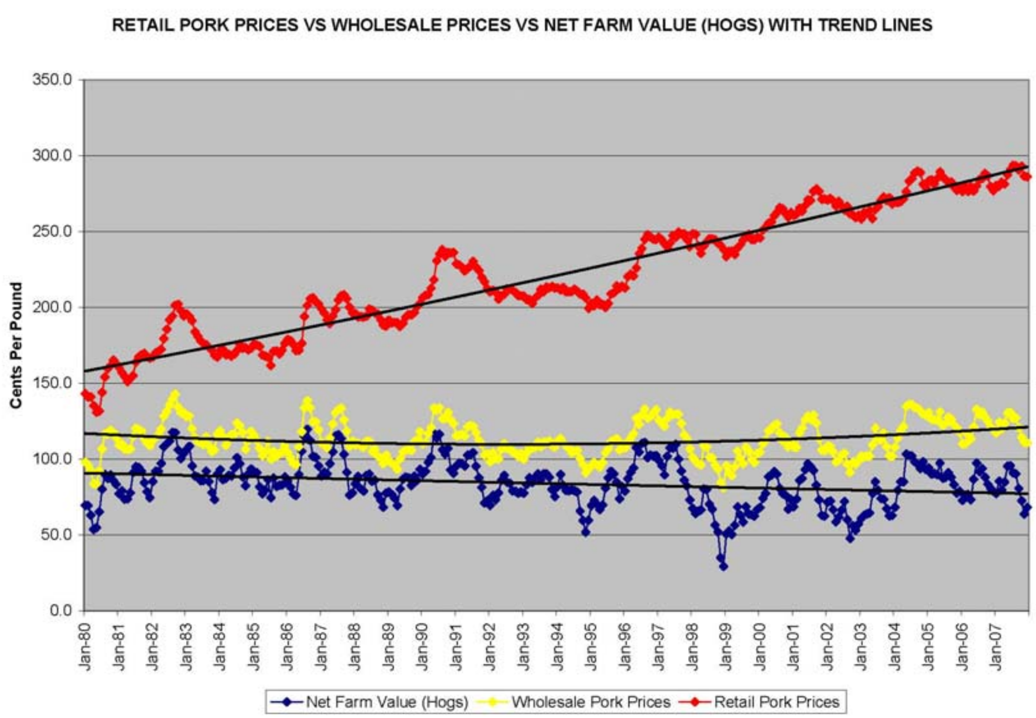
[30] *See* Table 1, Commercial Cattle Slaughter, Red Meat Yearbook, U.S. Department of Agriculture, Economic Research Service, available at http://usda.mannlib.cornell.edu/MannUsda/viewDocumentInfo.do?documentID=1354.

The proposed JBS/Swift acquisitions should not be allowed to proceed without conclusive evidence showing that the U.S. live cattle industry is not already subject to harmful market power exercised by the highly concentrated beef packing industry.

1. The New, More Consolidated Structure of the U.S. Hog Industry Provides Insights For the Future of a Further Consolidated U.S. Live Cattle Industry.

As shown in Figure 4 below, during the past 25-plus years, beginning January 1980, the new, more consolidated hog industry structure has resulted in a downward trend in live hog prices paid to producers and an upward trend in retail pork prices paid by consumers and wholesale pork prices received by packers, along with an ever widening spread between farm prices and wholesale prices and retail prices.

Figure 4



Data Source: USDA Economic Research Service.[31]

[31] *See* Meat Price Spreads, Data Set for Historical Monthly Price Spread Data for Beef, Pork, Broilers, Turkeys, and Eggs, U.S. Department of Agriculture, Economic Research Service, available at http://www.ers.usda.gov/Data/meatpricespreads/.

With respect to the U.S. live cattle industry, the relevant question the Subcommittee should ask when assessing the potential impacts of additional concentration in the beef packing industry, as would occur under the JBS/Swift acquisitions, is whether the merger would likely cause the U.S. live cattle industry to lose the critical mass of participants necessary to sustain current levels of competition that take place among and between its various subparts?

Again, the U.S. live hog industry, once analogous to the U.S. live cattle industry in that it too sustained a vibrant industry consisting of hundreds of thousands of producers, has already experienced such a *fait accompli*. According to the USDA, during the period 1980 to 2004, when the concentration by the top four hog slaughter firms increased from 33.6 percent to 61.3 percent, the number of U.S. hog and pig operations declined from 667,000 in 1980 to only 67,000 by 2005.[32]

The Subcommittee must not ignore this inverse relationship, evinced by historical data, between increased concentration in the meat packing industry and marked decline in the size of the U.S. live hog industry. Fortunately for the U.S. live cattle industry, there were significantly more U.S. cattle operations than U.S. hog and pig operations when the contraction of the two agricultural industries accelerated in 1980. With only 67,000 U.S. hog and pig operations remaining, the diminutive live hog industry lacks diversity and robust competition among and between its various subparts, with only 10 percent of its cash receipts generated from sales other than to pork packers.[33] The U.S. live hog industry's present ability to contribute significantly to the gross domestic product of more than just a handful of states has also been reduced, with only 3 states generating gross incomes of more than $1 billion annually.[34]

In contrast, the U.S. live cattle industry, characterized by the remaining 967,440 cattle operations, still has the critical mass of participants necessary to generate significant revenues among and between its various subparts (as discussed above, 27 percent of the industry's revenues are from sales to buyers other than beef packers).

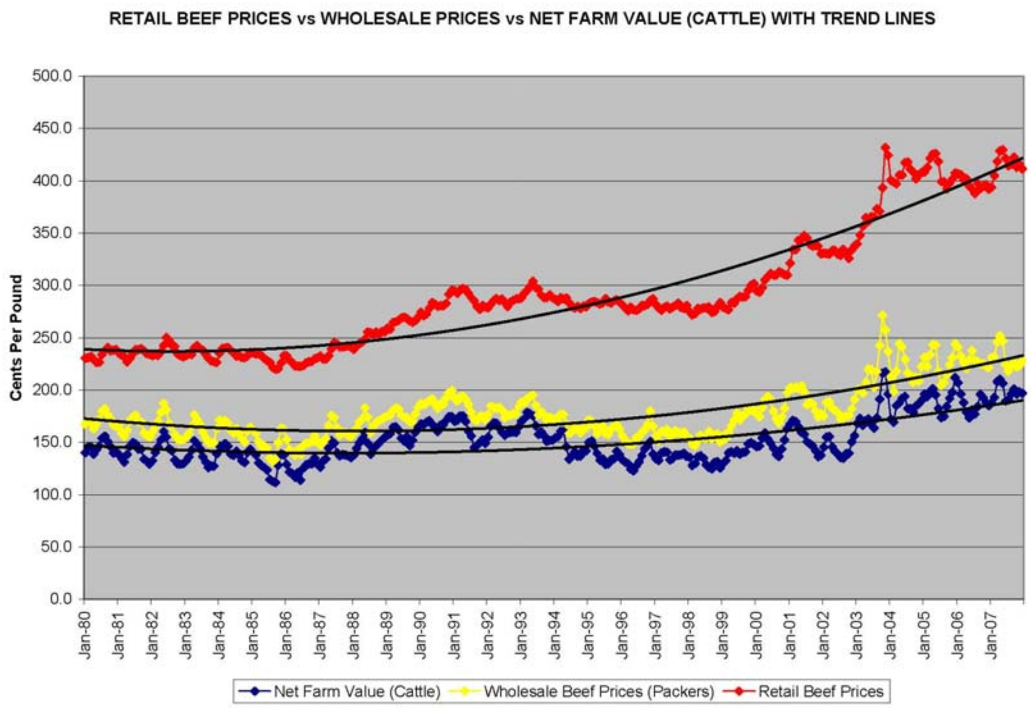
2. Although a Synchronous Trend Appears in the Relationship between Retail Beef Prices and Live Cattle Prices, Warning Signs of Impending Danger are Evident.

Figure 5 below reveals the relationships between retail beef prices paid by consumers, wholesale beef prices received by packers, and live cattle prices received by producers over the same 25-plus years during which the cattle industry, like the hog industry, was contracting. This is also the same period that the beef packing industry began its accelerated concentration. While the trend lines generally show that retail beef prices, wholesale beef prices, and live cattle prices are synchronous and directed upward, thereby lacking the obvious inverse relationship present in the hog and pork prices depicted in Figure 4 above, the trend lines nevertheless show an obvious

[32] *See* Federal Register, Vol. 72, No. 152, Wednesday, August 8, 2007, at 44,681, col. 2.
[33] *See* Meat Animals Production, Disposition, and Income 2006 Summary, U.S. Department of Agriculture, National Agricultural Statistics Service, April 2007, at 16, available at http://usda.mannlib.cornell.edu/usda/current/MeatAnimPr/MeatAnimPr-04-27-2007.pdf.
[34] *See id.* (Only the states of Iowa, Minnesota, and North Carolina generated gross incomes from hogs of over $1 billion in 2006.).

acceleration of the ever-widening spread between retail beef prices and cattle prices and wholesale beef prices and cattle prices. This evidence suggests there is an increased exercise of market power that enables the beef packing industry to extract a disproportionate profit from the sale of beef to retailers when compared to the share of the profits the cattle industry realizes when selling cattle to the beef packer.

Figure 5



Data Source: USDA Economic Research Service.[35]

Both Figures 4 and 5 reveal increasing price spreads. The USDA Economic Research Service (ERS) stated that "increasing price spreads can both inflate retail prices and deflate farm price."[36] Both of these outcomes are evident in Figure 4 that depicts retail pork prices, wholesale pork prices, and net farm hog prices, i.e., the trend lines show that retail pork prices and wholesale pork prices are inflating while net farm prices for hogs are deflating. It is important to note that the ERS explained that increasing price spreads are *not* a function of a

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[35] *See* Meat Price Spreads, Data Set for Historical Monthly Price Spread Data for Beef, Pork, Broilers, Turkeys, and Eggs, U.S. Department of Agriculture, Economic Research Service, available at http://www.ers.usda.gov/Data/meatpricespreads/.

[36] Beef and Pork Values and Price Spreads Explained, U.S. Department of Agriculture, Economic Research Service, at 2, attached as Exhibit 6.

demand shift toward more value-added products.[37] The ERS states that "[a]nalysts who cite increasing value-added as a factor in pork and beef price spreads misunderstand how these are calculated."[38]

The price spreads depicted in Figures 4 and 5 can be used to "measure the efficiency and equity of the food marketing system."[39] Thus, if the price spreads reveal inefficiency and inequity under the present, highly concentrated structure of the food marketing system, as is asserted by R-CALF USA, then this inefficiency and inequity would be expected to worsen should the beef packing system become further concentrated as contemplated by the JBS/Swift acquisitions.

The price spreads in Figures 4 and 5 reveal the costs and profits within the concentrated marketing systems that convert livestock into consumable meat. Innovative technologies can reduce price spreads and economic efficiency increases when price spreads drop.[40] The ERS recognizes that "[b]oth consumers and farmers can gain if the food marketing system becomes more efficient and price spreads drop."[41] And, it states that "[h]igher price spreads translate into lower prices for livestock."[42]

However, Figures 4 and 5 reveal what the USDA found in 2004 – that "the total price spreads show[ed] a weak upward trend when corrected for inflation,[43] has only worsened since 2004. The ever-increasing price spread between net farm values for cattle and hogs and wholesale prices and retail prices for beef and pork demonstrate the presence of market power, and the added harmful element of an inverse relationship between net farm values and wholesale prices and retail prices, which is already evident in the hog industry, portends the negative consequence to the U.S. cattle industry should the JBS/Swift acquisitions be consummated.

The continual increase in the price spread between producer prices, wholesale prices, and retail prices strongly suggests that the marketplace is becoming more inefficient and more inequitable for U.S. cattle producers and U.S. consumers, a condition that would only be expected to worsen under the increased concentration and vertical integration contemplated by the JBS/Swift acquisitions.

E. The U.S. Live Cattle Industry is Uniquely Susceptible to Market Power

The characteristic nature of cattle and the characteristics of the U.S. live cattle market make the U.S. live cattle industry uniquely susceptible to monopsony power. These characteristics include for cattle:

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[37] Beef and Pork Values and Price Spreads Explained, U.S. Department of Agriculture, Economic Research Service, at 2, attached as Exhibit 6.
[38] *Ibid.*
[39] *Id.*, at 3.
[40] Beef and Pork Values and Price Spreads Explained, U.S. Department of Agriculture, Economic Research Service, at 3, attached as Exhibit 6.
[41] *Id.*, at 3.
[42] *Id.*, at 8.
[43] *See id*, at 10.

1. The longest biological cycle of any farmed animal, making it difficult for the industry to react to changes in demand.[44]

2. Slaughter-ready cattle are highly perishable products that must be marketed within a narrow window of time; otherwise, the animals would degrade in quality and value.[45]

3. 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 choice of cattle procurement methods[46] and that "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."[47] 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.[48]

For cattle markets:

1. 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."[49]

2. 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.[50] Based on this finding, the Subcommittee should review the JBS/Swift acquisitions with the understanding that competition for slaughter-ready cattle is inherently fragile, even without the added burden of monopsony power that would be expected to increase following the increased horizontal concentration and vertical integration proposed by the JBS/Swift acquisitions.

3. 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

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[44] 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.
[45] 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.
[46] Examining Packer Choice of Slaughter Cattle Procurement and Pricing Methods, Oral Capps, Jr., et al., Agricultural and Resource Economics Review, April 1999, at 21, attached hereto as Exhibit 7.
[47] *Id*. at 15.
[48] *Id*. at 16.
[49] 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, attached hereto as Exhibit 3.
[50] 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, attached as Exhibit 8.

"each 1 percent increase in fed cattle numbers would be expected to decrease fed cattle prices by 2 percent."[51]

4. As confirmed by the Grain Inspection Packers and Stockyards Administration (GIPSA) Livestock and Meat Marketing Study (LMMS), the cash cattle market is sensitive to shifts in cattle procurement methods. 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.[52] 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 is cattle procurement. The analysis showed that for each 1% increase in captive supply cattle, cattle prices decreased 0.155%.[53]

5. 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.[54]

6. The combination of the perishable nature of slaughter-ready cattle and limited weekly slaughter capacity creates market access risk for U.S. cattle producers within the U.S. cattle market. The GIPSA LMMS study defines market access risk as "the availability of a timely and appropriate market outlet"[55] 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. . ."[56]

7. 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.[57] 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.[58] 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

[51] 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.
[52] *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.
[53] *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.
[54] *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), attached as Exhibit 9.
[55] 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.
[56] *Id.* at 2-36.
[57] Examining Packer Choice of Slaughter Cattle Procurement and Pricing Methods, Oral Capps, Jr., et al., Agricultural and Resource Economics Review, April 1999, at 16, attached hereto as Exhibit 7.
[58] *Id.*, at 16.

by 3.18 percent.[59] Based on this research, the proposed JBS/Swift acquisitions, which would necessarily increase the RHHI in one or more of the nine procurement regions, would be expected to shift more cattle into packer feeding arrangements, which are known to facilitate market power and decrease fed cattle prices, as was more fully discussed in Item 2 above.

8. Transparency in the U.S. live cattle market is already limited as was reported by the Government Accountability Office (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.[60] Included among the deficiencies found was the exclusion of a large percentage of cattle transaction data.[61] 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 may be significantly impacted by the proposed JBS/Swift acquisitions. The confidentiality guidelines that may well restrict or eliminate the reporting of currently reported cattle transaction data following the proposed JBS/Swift acquisitions 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.[62]

9. 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.[63] 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."[64] Based on this finding, U.S. live cattle producers would likely be defenseless against the increased monopsony power expected to be exercised as a result of the proposed JBS/Swift acquisitions. Indeed, the acquisition of Five Rivers feedlots by JBS/Swift would most likely cause such a shift to occur, given that the acquisition would place JBS/Swift in closer proximity to the feedlots than is the current packer-owner.

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[59] Examining Packer Choice of Slaughter Cattle Procurement and Pricing Methods, Oral Capps, Jr., et al., Agricultural and Resource Economics Review, April 1999, at 21, attached hereto as Exhibit 7.

[60] 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).

[61] *Id*., at 10.

[62] USDA Announces New Confidentiality Guidelines for Livestock Mandatory Reporting Program, U.S. Department of Agriculture, Release No. 0132.01, August 3, 2001, attached hereto as Exhibit 10.

[63] 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.

[64] *Ibid*.

II. The JBS/Swift Acquisitions Would Result in Direct Harm to U.S. Cattle Feeders by Reducing Competition, Creating Market Power, and Facilitating the Exercise of Market Power in the Slaughter-Ready Steer and Heifer Market.

Section I above described the U.S. live cattle industry's inherent vulnerability to any further reduction in competition and any increase in market power or increased exercise of market power that would manifest with increased consolidation of the *existing* structure of the beef packing industry. This section describes how the proposed JBS/Swift acquisitions would specifically create additional market power, and facilitate the exercise of that market power in the U.S. steer and heifer market, which, as described in Section I above, is the portal through which the harmful effects of market power would endanger the entire U.S. live cattle industry.

A. The JBS/Swift Acquisitions Would Significantly Increase Concentration and Result in an Extremely Concentrated Market.

As shown in Figure 6 below, the proposed JBS/Swift acquisitions would significantly increase the capacity concentration in the U.S. steer and heifer slaughter by changing the current four-firm capacity concentration, which USDA estimates at 79.1 percent,[65] to an estimated four-firm capacity concentration of approximately 91.2 percent.[66] This estimate represents a 12.1 percent increase in capacity concentration as a result of a 33 percent decrease in the number of firms that would compete for this 91.2 percent share of the market, with the number of competing firms shrinking from 6 to 4.[67]

Figure 6

Pre- and Post-Merger Capacity Concentration in U.S. Steer and Heifer Slaughter

	Tyson	Cargill	JBS-Swift	National	Smithfield	Amercian	Total Capacity
Pre-Merger Daily Slaughter Capacity Estimates							
AMI Data*	30,875	25,850	15,800	13,000	7,600	5,200	98,325
Hendrickson/Heffernan Data**	36,000	28,300	16,759	13,000			94,059
CME Group Data***	32,600	29,000	15,850	13,700	8,350	6,500	106,000
Pre-Merger Average of All Daily Capacity Estimates	33,158	27,717	16,136	13,233	7,975	5,850	104,070
Pre-Merger Average of Daily Capacity for Top Four Firms	33,158	27,717	16,136	13,233			90,244
Post-Merger Average Daily Capacity for Top Four Firms	33,158	27,717	37,345			5,850	104,070

Pre-Merger USDA estimate of Four-Firm Capacity Concentration: 79.1%****
Post-Merger Estimate of Four-Firm Capacity Concentration (Using USDA Estimate Where Current CR-4 = 79.1%): 91.2%

Notes:
* AMI data are attached as Exhibit 2.
** Hendrickson/Heffernan data are attached as Exhibit 3.
*** CME Group data are attached as Exhibit 4.
**** *See* footnote 44.

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65 Packers and Stockyards Statistical Report, 2005 Reporting Year, Table 27 – Steer and Heifer Slaughter Concentration by 4, 8, 20, and 50 Largest Firms for Selected Years 1980-2005, U.S. Department of Agriculture, Grain Inspection Packers and Stockyards Administration, February 2007, at 44, available at http://archive.gipsa.usda.gov/pubs/2005_stat_report.pdf.

66 This estimate assumes that American Foods Group is included as a slaughterer of steers and heifers.

67 Three of the top 6 meatpacking plants are involved in the JBS-Brazil Merger, which would reduce the number of plants that presently control the estimated 91.2 percent of capacity from 6 to 4.

Though R-CALF USA does not venture an estimate of the increased Herfindahl-Hirschman Index ("HHI") that would result from the JBS/Swift Acquisitions, the CME Group did and estimated the increase to be dramatic, growing by 638 points.[68]

B. The Increased Concentration Created by the JBS/Swift Acquisitions Would Facilitate the Increased Exercise of Market Power in the U.S. Steer and Heifer Market.

Although the USDA data discussed in Section I suggests that the contraction of the U.S. live hog industry was more severe than was experienced by the U.S. live cattle industry, despite a smaller four-firm concentration ratio of the pork packing industry, there is a 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 greater propensity toward vertical integration of the 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 recently completed GIPSA Livestock and Meat Marketing Study ("LMMS") found that during the period October 2002 through March 2005, the pork manufacturing industry captured 20 percent of its slaughter-ready hogs through the alternative procurement method of direct ownership;[69] 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.[70] 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."[71] 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%.

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[68] *See* Daily Livestock Report, CME Group, A CME/Chicago Board of Trade Company, Vol. 6, No. 44, March 5, 2008, attached as Exhibit 11.
[69] *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.
[70] *See id.*
[71] *See* GIPSA Livestock and Meat Marketing Study, January 2007, Volume 4, at ES-3, available at http://archive.gipsa.usda.gov/psp/issues/livemarketstudy/LMMS_Vol_4.pdf.

> 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.[72]

The LMMS found that procurement methods that facilitated the exercise of market power by the concentrated pork packing industry are currently less developed by 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,[73] which 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 the beef manufacturing industry. As stated above, 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.[74]

C. The More Regional Scope of the U.S. Steer and Heifer Market When Compared to the Feeder Cattle Market Makes it More Susceptible to Monopsony Power Emanating from a Concentrated Market.

Figure 7 below lists the plant locations for each of the five largest beef packers:

[72] *See* GIPSA Livestock and Meat Marketing Study, January 2007, Volume 4, at ES-2, 3, available at http://archive.gipsa.usda.gov/psp/issues/livemarketstudy/LMMS_Vol_4.pdf.
[73] *See* GIPSA Livestock and Meat Marketing Study, January 2007, Volume 3, at ES-4, available at http://archive.gipsa.usda.gov/psp/issues/livemarketstudy/LMMS_Vol_3.pdf.
[74] *See id.,* at ES-5.

Figure 7

Plant Locations for Five Largest Beef Packers

Tyson[75]	**Cargill**[76]	**JBS-Swift** [77]	**National Beef** [78]	**Smithfield** [79]
Kuna, ID	Fresno, CA	Cactus, TX	Brawly, CA	Souderton, PA
Geneseo, IL	Friona, TX	Greeley, CO	Liberal, KS	Tolleson, AZ
Denison, IA	Dodge City, KS	Hyrum, UT	Dodge City, KS	Plainwell, MI
Emporia, KS	Schuyler, NE	Grand Island, NE		Green Bay, WI
Holcomb, KS	Fort Morgan, CO			
Dakota City, NE	Plainview, TX			
Lexington, NE	Wyalusing, PA			
Norfolk, NE	Milwaukee, WI			
West Point, NE				
Amarillo, TX				
Pasco, WA				

As mentioned above, researchers developed nine cattle procurement regions. These regions were based on the geographic proximity of packing plants and the procurement area for packing plants.[80] These researchers 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.[81] Included as a single region are California and Arizona.[82] The JBS/Swift acquisitions include the purchase of the California beef packing plant presently owned by National and the Arizona packing plant presently owned by Smithfield. Thus, these two competing beef packers that are in the same defined region and located approximately 226 miles from each other would be merged into a single entity under the proposed JBS/Swift acquisitions, resulting in a lessening of competition within that region. In addition, though not in the same defined region, the JBS/Swift packing plant located in Cactus, TX, is approximately 185 miles and 103 miles from Dodge City, KS, and Liberal, KS, respectively. Currently JBS/Swift and National are competitors within this cattle procurement area and the effect of the JBS/Swift acquisitions would be to eliminate a beef-packer competitor within a 300-mile radius of any one of those three beef packing plants.

[75] *See* Tyson Corporate, Our Locations – List, available at http://www.tyson.com/Corporate/AboutTyson/Locations/ListPage.aspx.
[76] *See* Cargill Meat Solutions North American Beef Facilities, available at http://www.cargillmeatsolutions.com/about_us/tk_cms_about_loc_beef.htm.
[77] *See* Meat, Poultry, and Egg Product Inspection Directory, U.S. Department of Agriculture Food Safety Inspection Service, December 7, 2007, available at http://www.fsis.usda.gov/regulations_&_policies/Meat_Poultry_Egg_Inspection_Directory/index.asp.
[78] *See* National Beef: Company Information, available at http://www.nationalbeef.com/.
[79] *See* Meat, Poultry, and Egg Product Inspection Directory, U.S. Department of Agriculture Food Safety Inspection Service, December 7, 2007, available at http://www.fsis.usda.gov/regulations_&_policies/Meat_Poultry_Egg_Inspection_Directory/index.asp.
[80] Examining Packer Choice of Slaughter Cattle Procurement and Pricing Methods, Oral Capps, Jr., et al., Agricultural and Resource Economics Review, April 1999, at 16, attached hereto as Exhibit 7.
[81] *Id*. at 15.
[82] *Id*. at 16.

On a national level, the JBS/Swift acquisitions would combine 11 packing plants now owned by 3 beef packers under the single ownership of JBS/Swift. While researchers have found that the wholesale beef market is national in scope, the discussion above suggests that transportation costs function to limit the national purview of the slaughter-ready cattle market. According to a recent 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."[83]

D. The Pre-existing Market Power that would be Enhanced by the JBS/Swift Acquisitions is Manifest in the Beef Packer' Ability to Limit Producer Access to the Market.

As previously discussed, producers of fed steers and heifers are subject to "market access risk," which refers to "the availability of a timely and appropriate market outlet."[84] 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.[85] Under the current level of beef packer concentration, there is already evidence that 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],"[86] 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 . . ."[87]

The JBS/Swift acquisitions would exacerbate market access risk for steer and heifer producers by effectively shrinking the number of market outlet gatekeepers for the estimated 92.1 percent of market outlet capacity from six firms to only four firms, as was previously discussed above.

E. As Gatekeepers of the Market Outlets, the Concentrated Beef Packing Industry Wields Considerable Market Power Exercised through Captive Supply Arrangements, Novel Purchasing Strategies, and Anticompetitive Behavior.

While the beef manufacturing industry has been limiting the number of its market outlet gatekeepers through horizontal consolidation, thus exacerbating market access risk for cattle producers, the beef manufacturing industry has been simultaneously increasing its use of non-traditional contracting and marketing methods, enabling it to more effectively exercise its 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

[83] 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, attached as Exhibit 12.
[84] 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.
[85] *See id.*
[86] *Id*., at 2-36.
[87] *Id*.

purchasing cattle more than 14 days before slaughter (packer-fed cattle), forward contracts, and exclusive marketing and purchasing agreements. 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.[88] And use of these captive supply methods has been increasing rapidly, rising 37 percent from 1999 to 2002.[89] As stated above, 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.[90] 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.[91] 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.[92] 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.[93] 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.

The JBS/Swift acquisitions would facilitate the exercise of market power by further concentrating control over market access, thus increasing the propensity for live cattle producers to continually enter captive supply arrangements despite their negative impact on the live cattle industry.

1. The JBS/Swift acquisitions would facilitate ongoing market power abuses to the detriment of U.S. cattle producers.

The beef manufacturing 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-related food manufacturer IBP, Inc., 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]

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[88] *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.
[89] *See id.* at 3-17.
[90] *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, attached as Exhibit 13.
[91] *See id.*
[92] *See id*., at 8.
[93] *See id.*

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."[94]

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 political response to Congress' passage of the mandatory country of origin labeling law.[95] This abuse of market power was initiated months *before* the USDA even published its October 30, 2003 proposed rule to implement the country of origin labeling law.

Such abuses of market power would be facilitated by the JBS/Swift acquisitions as U.S. cattle producers' market outlets would become even more limited, particularly in certain geographic areas, and producers would not be able to avoid the arbitrary dictates of any one of the remaining beef packers.

2. The JBS-Brazil Merger would facilitate the imposition of arbitrary product specification, leading to unavoidable cattle price discounts.

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 have each established different price premiums and discounts for additional factors, such as muscle scoring. For example, Smithfield discounts 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.[96] These discounts and premiums are purported to reflect consumer preferences,[97] 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 manufacturing industry receives upon the sale of the resulting meat, or if it represents a windfall for the beef manufacturing industry, is undeterminable without additional information. Nevertheless, the ability to impose such discounts, without knowing if they are legitimate, is facilitated by the currently limited marketing outlets, which would become even more limited under the JBS/Swift acquisitions.

There is a host of potential market power abuses, the propensity toward which would be facilitated by an increased concentration of the steer and heifer market, that would either force producers into compliance or cause them to suffer economic losses. For example: a beef manufacturer in a more concentrated market could establish discounts for cattle that were not conceived by the beef manufacturer's preferred genetic lineage, or that were not fed the beef manufacturer's preferred brand of mineral or feed supplement.

Thus, the potential for the beef manufacturing industry to impose wholly arbitrary product specifications, which directly result in lower cattle prices paid to producers, is a significant concern arising from the JBS/Swift acquisitions.

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[94] Letter from Bruce Bass, IBP, Inc., to Producers, March 2003, attached as Exhibit 14.
[95] *Ibid.*
[96] *See* Muscle Scoring Provides Important Production Tips, Nexus Marketing, Ames, Iowa, attached as Exhibit 15.
[97] *See id.*

3. The JBS-Brazil Merger would increase the potential exercise of pricing strategies that disrupt competitive market fundamentals.

As part of its investigation, the Subcommittee should determine if pricing strategies of the concentrated beef manufacturers, such as that described in the example 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.[98] 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.[99] Assuming an average dressed weight for cattle of 781 pounds,[100] 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.[101] 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.[102]

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 manufacturers 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. 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.

4. The JBS-Brazil Merger would facilitate a division of the market, effectively eliminating competition for certain subclasses of cattle in certain regions.

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[98] *See* GIPSA Livestock and Meat Marketing Study, Vol. 3 (Jan. 2007) at 2-39.
[99] *See id*.
[100] *See id*., at 1-21.
[101] *See id*. at 2-39.
[102] 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.

Tyson Fresh Meats, Inc., ("Tyson") has issued presumably new terms and conditions under which it will purchase cattle for slaughter.[103] 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.[104] 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, this action constitutes an outright denial of access to the marketplace, which is even more egregious than would be a discount for cattle that exceeded Tyson's restrictions, as it automatically eliminates a dominant competitor from the marketplace.

The JBS/Swift acquisitions would potentially exacerbate the division of the marketplace that has already been initiated by Tyson. Should one beef manufacturer declare that it would slaughter only steers, only heifers, only Holsteins, or only hornless cattle, for example, the marketplace could be sufficiently divided by the remaining food manufacturers to severely limit competition for each subclass of cattle, if not eliminate competition altogether.

5. The JBS-Brazil Merger would facilitate strategic entries and exits from the cash market for the purpose and with the effect of lowering cattle prices.

Under the existing, concentrated structure of the beef manufacturing industry, empirical evidence shows that the U.S. cattle market is already susceptible to coordinated and/or simultaneous entries and exits from the market. In February 2006, all four major beef-related food manufacturers – Tyson, Cargill, Swift, 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.[105] 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."[106] Market analysts noted that "[n]o sales for the second week in a row would be unprecedented in the modern history of the market."[107] During the week of February 13 through 17, there were no significant trades in Kansas, western Oklahoma, and Texas for the

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[103] *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.
[104] *Id*.
[105] "Packers Finally Seriously Cut Kills," *Cattle Buyers Weekly* (Feb. 13, 2006).
[106] "Classic Standoff Continues Through Thursday," *Cattle Buyers Weekly* (Feb. 20, 2006).
[107] "Classic Standoff Continues Through Thursday," *Cattle Buyers Weekly* (Feb. 20, 2006).

second week in a row.[108] 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.[109] The beef manufacturers 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 manufacturers 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.[110] 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."[111] Another trade publication noted that the dramatic drop in slaughter was undertaken in part to "try and get cattle bought cheaper."[112] 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."[113]

As a result of the beef manufacturers 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.[114] The same day, February 17, live and feeder cattle futures fell to multi-month lows.[115] Replacement cattle prices also dropped in response to buyer reluctance.[116] In Oklahoma City, prices for feeder cattle dropped as much as $4 per hundredweight.[117]

Whether the beef manufacturers' simultaneous boycott of the cash market was deliberately coordinated or not, 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 manufacturers would "break ranks" to purchase at higher prices than the other beef manufacturers. No buyer did so until prices began to fall. In fact, beef manufacturers were willing to cut production rather than break ranks and purchase on the cash market.

Abandonment of the cash market in the Southern Plains by all major beef manufacturers 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

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[108] Curt Thacker, "Cash Cattle Quiet 2-20," *Dow Jones Newswires* (Feb. 20, 2006).
[109] Lester Aldrich, "Cash Cattle Standoff 2-17," *Dow Jones Newswires* (Feb. 17, 2006).
[110] Curt Thacker, "Cash Cattle Quiet 2-20," *Dow Jones Newswires* (Feb. 20, 2006).
[111] Jim Cote, "Today's Beef Outlook 2-17," *Dow Jones Newswires* (Feb. 17, 2006).
[112] "Classic Standoff Continues Through Thursday," *Cattle Buyers Weekly* (Feb. 20, 2006).
[113] "Classic Standoff Continues Through Thursday," *Cattle Buyers Weekly* (Feb. 20, 2006).
[114] Curt Thacker, "Cash Cattle Quiet 2-20," *Dow Jones Newswires* (Feb. 20, 2006).
[115] Jim Cote, "Live Cattle ReCap – 2/17/2006," *Dow Jones Newswires* (Feb. 17, 2006).
[116] "The Markets," *AgCenter Cattle Report* (Feb. 18, 2006), available on-line at http://www.agcenter.com/cattlereport.asp.
[117] "The Markets," *AgCenter Cattle Report* (Feb. 18, 2006), available on-line at http://www.agcenter.com/cattlereport.asp.

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 manufacturers 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/simultaneous action in February 2006 was not isolated and was soon followed by a second, coordinated/simultaneous action. During the week that ended October 13, 2006, three of the nation's four largest beef manufacturers – 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.[118] 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.[119] Fed cattle prices still fell $2 per hundredweight to $3 per hundredweight and feeder prices fell $3 per hundredweight to $10 per hundredweight.[120]

By Friday of the next week, October 20, 2006, the beef manufacturers 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.[121] 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.[122]

The anticompetitive behavior exhibited by the beef-related food manufacturers' coordinated/simultaneous 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 – a situation that would only worsen if there were even fewer buyers in the marketplace. For example, the reduction in cattle prices that followed the coordinated/simultaneous actions of four beef-related food manufacturers in February 2006 and three beef-related food manufacturers in October 2006 could be accomplished by only three beef manufacturers, and only two beef manufacturers, respectively, should the JBS-Brazil Merger be consummated.

The potential for a recurrence of this type of anticompetitive behavior is considerable and constitutes an empirically demonstrated risk that would likely become more frequent, more intense, as well as extended in duration. Therefore, this anticompetitive behavior is evidence that the JBS/Swift acquisitions would reduce competition in the marketplace.

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[118] *See* "National Beef Cuts Hours at Two Kansas Plants (Dodge City, Liberal)," Kansas City Business Journal (October 10, 2006) attached as Exhibit 17; "Update 1 – Tyson Foods to Reduce Beef Production," Reuters (October 10, 2006), attached as Exhibit 18; "Swift to Stay with Reduced Production at U.S. Facilities," Meatpoultry.com (October 10, 2006), attached as Exhibit 19.
[119] *See* "Livestock Market Briefs, Brownfield Ag Network," (October 13, 2006), attached as Exhibit 20.
[120] *See id.*
[121] *See* "Livestock Market Briefs, Brownfield Ag Network," (October 20, 2006), attached as Exhibit 21.
[122] *See id.*

F. JBS/Swift Has a History of Being a Bad Actor and Should Not Be Permitted to Exploit the U.S. Cattle Industry as It Did the Brazilian Cattle Industry.

On November 28, 2007, Dow Jones Newswires reported that "JBS SA's Friboi Group (JBSS3.BR)" was among a number of Brazilian companies which, after a two-year investigation by the Brazilian Justice Department's antitrust division, were accused of engaging in anti-competitive practices.[123] JBS SA was reportedly charged with "anti-competitive practices for coordinating price agreements among themselves in order to keep cattle prices low when purchasing livestock for slaughter."[124] The report indicated that JBS SA had denied the charges. However, in a subsequent news article, JBS SA reportedly agreed to pay $8.5 million to an antitrust fund as a result of the charges and further agreed to end the practices that were allegedly anti-competitive.[125]

This example demonstrates that it is highly likely that the U.S. live cattle market would be subjected to coordinated interaction by JBS/Swift given that the company was reportedly accused, and was found culpable based on the payment of restitution, of engaging in such anticompetitive behavior in another geographic market, which is comparable to the U.S. market.

G. The JBS/Swift Acquisition Would Significantly Exacerbate the Ongoing Exercise of Market Power Through JBS/Swift's Ownership of the Nation's Largest Cattle Feeding Facility.

If consummated, the JBS/Swift acquisitions would result in the nation's largest beef packer owning Five Rivers, the nation's largest cattle feeding company. Five Rivers currently feed and market approximately 2 million cattle annually and is currently owned by the nation's fifth largest beef packer, Smithfield, under a joint venture.[126] Based on Smithfield's estimated daily capacity of 7,975 cattle (*see* Figure 6), and applying the 260 reporting days established by the USDA Agricultural Marketing Service ("AMS") as the number of annual slaughter days,[127] Smithfield's estimated annual slaughter is 2.1 million. Therefore, Smithfield's ownership of Five Rivers gives it sufficient numbers of fed cattle to meet nearly 100 percent of its annual slaughter capacity. However, it is not likely that Smithfield could coordinate the finishing of cattle to coincide with its daily capacity needs throughout the year from its own feedlots, nor is it likely that Smithfield could economically transport Five Rivers' cattle to its four packing plants, which are far removed from all of Fiver Rivers' feedlot locations. According to Five Rivers'

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[123] "Brazil Justice Department Fines Major Beef Cos In Cartel Case," Kenneth Rapoza, Dow Jones Newswires (November 28, 2007), attached as Exhibit 22.
[124] *Id.*
[125] "Brazil Antitrust Agency Signs Agreements with JBS, Lafarge," Jeb Bount, Bloomberg (November 29, 2007), attached as Exhibit 23.
[126] History of Smithfield Foods, attached as Exhibit 24, available at http://www.smithfieldfoods.com/Understand/History/.
[127] Livestock Mandatory Reporting; Reestablishment and Revision of the Reporting Regulation for Swine, Cattle, Lamb, and Boxed Beef; Proposed Rule, U.S. Department of Agriculture, Agricultural Marketing Service, Federal Register, Vol. 72, No. 152, August 8, 2007, at 44,688-689 (meatpackers are required to report each day for an estimated total of 260 reporting days in a year).

website, its feedlots are located in Colorado, Idaho, Kansas, Oklahoma, and Texas,[128] locations far removed from Smithfield's packing plants in Pennsylvania, Arizona, Michigan, and Wisconsin.

If this assumption is correct, Smithfield likely operates Five Rivers as an independent feeder, not a vertically integrated component of its packing operations. Thus, Smithfield likely contributes to the current competitiveness of the marketplace by marketing Five Rivers cattle to Tyson, Cargill, or National.

Post-merger, however, JBS/Swift would own both Smithfield and Five Rivers, affording it control over approximately 2 million fed cattle annually, representing approximately 7 percent of the nation's annual steer and heifer slaughter. Whereas Smithfield was not likely capable of slaughtering all or most of the cattle fed at Five Rivers due to the combination of limited daily slaughter, the logistics of timing the finishing of cattle, and the long distances between its packing plants and Five Rivers' feedlot locations, JBS/Swift could likely slaughter all of the cattle fed at Five Rivers due to its significantly increased number of plants and capacity. The effect would be a potential increase in the percentage of packer-owned cattle presently slaughtered on a national basis and a potential reduction in the volume of cattle sold in the cash market – a circumstance that would effectively thin the cash market and potentially drive down prices.

In addition to the structural integration Five Rivers would provide JBS/Swift, JBS/Swift also would have access to information regarding the value of feeder cattle it intends to purchase for feeding long before independent producers would have such information. The information available to JBS/Swift would be knowledge of the type and quantity of future purchasing orders for beef – essentially insider information – that would accord JBS/Swift a distinct advantage when competing against independent cattle producers for feeder cattle.

The Subcommittee should investigate both the current practices of Smithfield with respect to the disposition of cattle fed at Five Rivers and the change in this disposition of cattle that would likely occur should the JBS/Swift acquisitions be consummated.

H. The JBS/Swift Acquisitions Would Likely Violate Both the Spirit and Express Language of the Packers and Stockyards Act.

Congress enacted the Packers and Stockyards Act of 1921 ("PSA") to not only prohibit anticompetitive and monopolistic practices, but also to protect livestock producers from unfair, deceptive, and manipulative practices by the animal food manufacturing industry. Thus, the PSA goes well beyond the traditional antitrust concerns of efficiency and market competition. The PSA's central provision for protecting the U.S. live cattle industry is 7 USC § 192. Section 192 provides:

> It shall be unlawful for any packer or swine contractor with respect to livestock, meats, meat food products, or livestock products in unmanufactured form, or for any live poultry dealer with respect to live poultry, to:

[128] Five Rivers website address is available at http://www.fiveriverscattle.com/Index.aspx.

> (a) Engage in or use any unfair, unjustly discriminatory, or deceptive practice or device; or
>
> (b) Make or give any undue or unreasonable preference or advantage to any particular person or locality in any respect, or subject any particular person or locality to any undue or unreasonable prejudice or disadvantage in any respect; or
>
> (c) Sell or otherwise transfer to or for any other packer, swine contractor, or any live poultry dealer, or buy or otherwise receive from or for any other packer, swine contractor, or any live poultry dealer, any article for the purpose or with the effect of apportioning the supply between any such persons, if such apportionment has the tendency or effect of restraining commerce or of creating a monopoly; or
>
> (d) Sell or otherwise transfer to or for any other person, or buy or otherwise receive from or for any other person, any article for the purpose or with the effect of manipulating or controlling prices, or of creating a monopoly in the acquisition of, buying, selling, or dealing in, any article, or of restraining commerce; or
>
> (e) Engage in any course of business or do any act for the purpose or with the effect of manipulating or controlling prices, or of creating a monopoly in the acquisition of, buying, selling, or dealing in, any article, or of restraining commerce; or
>
> (f) Conspire, combine, agree, or arrange with any other person (1) to apportion territory for carrying on business, or (2) to apportion purchases or sales of any article, or (3) to manipulate or control prices; or
>
> (g) Conspire, combine, agree, or arrange with any other person to do, or aid or abet the doing of, any act made unlawful by subdivisions (a), (b), (c), (d), or (e) of this section.

The concerns raised herein demonstrate that the JBS/Swift acquisitions would increase the probability, if not the certainty, that the practices prohibited by the PSA will occur to the detriment of U.S. cattle producers. In fact, the evidence presented demonstrates that many of the prohibited practices are already occurring unabated within the U.S. live cattle industry. Inasmuch as the term "creating" in subdivisions (c), (d), and (e) above need not occur instantaneously, the JBS/Swift acquisitions would clearly catapult the beef packing industry toward monopolization nationally, and would likely achieves complete monopolization in certain geographic regions.

I. The JBS/Swift Acquisitions Present Additional Concerns that Should Be Investigated by the Subcommittee.

In addition to the concerns discussed above, the Subcommittee should consider that the JBS/Swift acquisitions would increase the probability that the following anticompetitive practices would become more frequent and would intensify in the U.S. live cattle industry:

1. Bidding not to buy cattle, i.e., offering a low bid with no intent to buy, but rather, with the intent to lower prices for live cattle.

2. Offering preferential agreements with captive suppliers for prices and terms not available to other sellers of comparable cattle in the market.

3. Entering into strategic alliances that contain special agreements for preferential access to the market and/or special prices.

4. Exercising undue influence over national commodities markets, potentially eliminating this hedging tool for U.S. cattle producers.

III. CONCLUSION

R-CALF USA appreciates the opportunity to express its concerns regarding the JBS/Swift acquisitions and respectfully requests that the Subcommittee conduct a thorough, probing analysis of the JBS/Swift acquisitions and that it expand its investigation to include a thorough, probing analysis of the current market environment in which these acquisitions are proposed. R-CALF USA is confident that such a comprehensive investigation would reveal the need to forestall indefinitely the JBS/Swift acquisitions as well as to initiate immediate remedial action to halt the anticompetitive practices already prevalent within the U.S. live cattle industry.

Thank you.

Bill Bullard
CEO
R-CALF USA