Investigations Into Meat Packers

Issue

Over the last year, the beef and cattle markets have experienced two unique disruptions that impacted the markets in similar ways. The first event was the shutdown of a Tyson packing plant in Kansas for approximately four months after a significant fire. The second event is the spread of COVID-19 throughout the U.S. and its resulting impact on consumer spending and the beef supply chain. Following these events, the wholesale price of beef skyrocketed, while the price producers received for their cattle cratered. This situation highlighted a concern of many. The four largest beef processors handle over 75% of the U.S. market based on volume and revenue. The concern has initiated investigations into the manipulation of cattle pricing by the processing/packing industry from USDA, the Department of Justice, and state attorneys general.

Background

The beef processing/packing industry in the United States has over time been consolidated to the point that four packers handle over 75% of the beef processed: Tyson Foods (23%), JBS Beef Company (21%), Cargill Meat Solutions (19%), and National Beef (12%). A study published in 2000 by the United States Department of Agriculture (USDA) Economic Research Service (ERS) suggests this consolidation had been happening rapidly in the 1980s and 1990s, and slaughter plants became much larger and concentration increased as smaller firms left the industry (authors MacDonald, Ollinger, Nelson, and Handy). The USDA ERS study indicated the main forces behind the consolidation were driven by the roles of scale economies and technological change. According to this study,

> *"Through the 1970's, larger plants paid higher wages, generating a pecuniary scale diseconomy that largely offset the cost advantages that technological scale economies offered large plants. The larger plants' wage premium disappeared in the 1980's, and technological change created larger and more extensive technological scale economies. As a result, large plants realized growing cost advantages over smaller plants, and production shifted to larger plants."*

Like other sectors of the economy and agriculture industry, consolidation itself is not necessarily bad. Many farms have had to increase in size to realize the benefits of economy of scale. However, concern has risen that these companies use their size and market power to manipulate the market, thus potentially causing harm to consumers and farmers. Two recent events have increased suspicion toward the four major players in the beef processing/packing industry.

The markets and processing systems for the beef supply chain were disrupted by two significant events in 2019 and 2020. On August 9, 2019, the Tyson Fresh Meats (Tyson) beef packing plant in Holcomb, Kansas closed for four months following a fire at the facility. Then in the spring of 2020, COVID-19 transmitted throughout the country resulting in further and more significant market disruptions. Following both events, the spread between the boxed beef cutout values and dressed fed cattle prices rose to records levels. These two events spurred the call for investigations into the manipulation of cattle pricing by the processing/packing industry from USDA, the Department of Justice, and state attorneys general.

USDA began its investigation following the Holcomb Tyson fire on August 28, 2019 and was expanded into the COVID-19 price spread in April of 2020. The purpose of the USDA investigation is to examine whether any regulated entities violated the Packers and Stockyards Act (PSA) by taking advantage of the disruptions through price manipulation, collusion, restrictions of competition, or other unfair practices. On May 6, 2020, President Trump indicated that he requested the Department of Justice to look into allegations that meat packers broke antitrust law. The investigations are coordinating efforts but are separate and distinct from each other and are still ongoing.

On July 22, 2020, an economic analysis was released by the USDA's Agricultural Marketing Service (AMS) on the price spread between boxed beef and fed cattle caused by the Tyson fire and COVID-19. This analysis, *Boxed Beef and Fed Cattle Price Spread Investigation Report*, was prepared by AMS in coordination with USDA's office of the chief economist. The report summarizes market conditions in the beef and cattle markets before and after the events and analyzes the events through an economic lens. This report does not examine potential violations of the PSA because that investigation into potential violations is ongoing, limiting AMS' ability to publicly report on it. In addition to the economic analysis portion, the report also delves into some other topics as well as solutions discussed widely by the industry in the aftermath of these events.

The full USDA AMS Report, *Boxed Beef & Fed Cattle Price Spread Investigation Report*, can be found at https://www.ams.usda.gov/sites/default/files/media/CattleandBeefPriceMarginReport.pdf

The remaining portion of this paper is analysis of the *Boxed Beef and Fed Cattle Price Spread Investigation Report* and was adapted from a Market Intel produced by the American Farm Bureau and can be found at https://www.fb.org/market-intel/usda-releases-report-on-investigation-into-beef-and-cattle-price-spread

The Impact of the Packing Plant Fire

On August 9, 2019, a fire broke out at one of the largest beef packing plants in the U.S., significantly impacting beef markets in the days and weeks that followed. The fire, at a plant in Holcomb, Kansas, owned by Tyson Fresh Meats, stressed an already sensitive balance between processing capacity and a growing fed cattle supply. The Holcomb facility had a daily capacity of approximately 6,000 head and accounted for roughly 5%-6% of U.S. slaughter capacity, a significant share for a single plant. In the weeks following the fire, boxed beef values skyrocketed, moving from $216.04/cwt the week of the fire to $230.43/cwt the week after the fire and to $239.87/cwt the week after that. That's a $23.83 jump in the two weeks after the fire. For the month leading up to the fire, both feeder and fed cattle futures were largely holding steady at or slightly above the value the day of the fire. Immediately following the fire, both futures markets exhibited significant bearish activity. Following the declines in fed cattle futures prices, the price of fed cattle declined 6% the week following the fire.

Figure 1. Live-to-Cutout Spread Following Fire

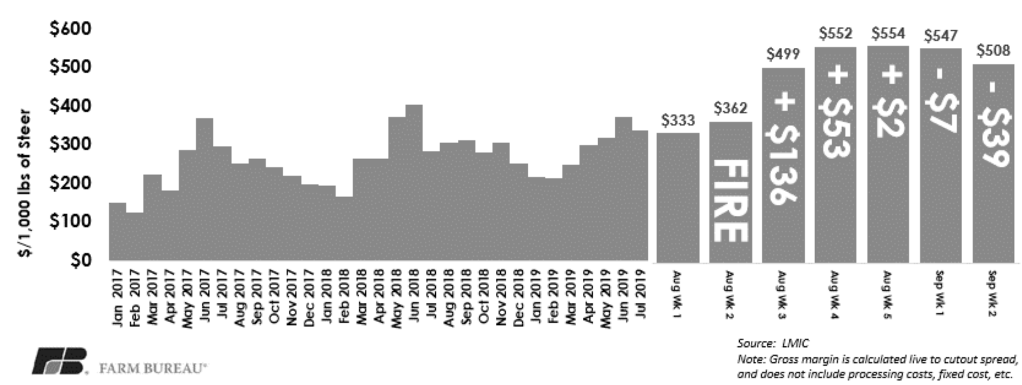


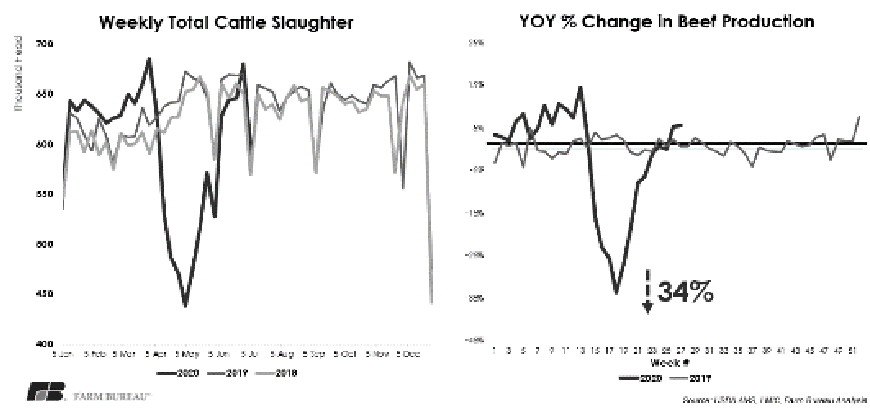
Figure 1 shows the initial impacts of the fire on the live-to-cutout spread. These calculations are the spread between inputs and outputs and do not include processing costs (energy, labor, etc.) and fixed costs. However, they still offer a good measure of the overall relative health of packer margins, and in the weeks following the fire, they were exceedingly healthy. Leading up to the fire, calculated packer margins were healthy relative to the long-run history. In the weeks following the fire, we saw the largest live-to-cutout spread on record since mandatory price reporting began, at least until COVID-19.

The Impact of COVID-19

Fast forward just six months to the meat industry's second unexpected market event in a year with the onset of COVID-19. The pandemic and its resulting impact on the U.S. economy and the way Americans purchase food wreaks havoc on the food supply chain, and in particular the beef and cattle markets.

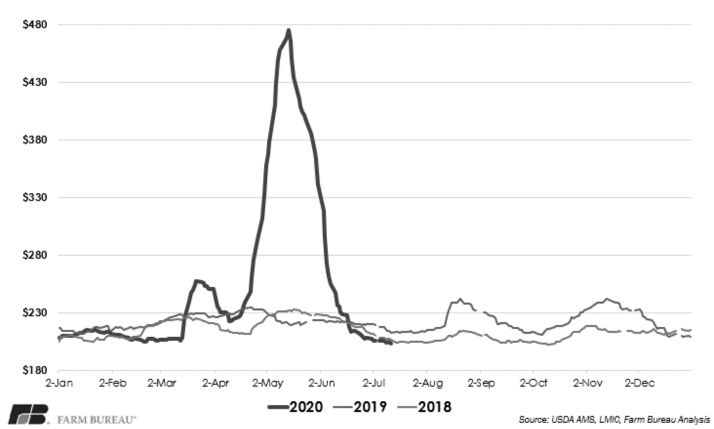
Throughout the late spring, more than two dozen livestock processing plants temporarily closed due to COVID-19-related issues. In some cases, the closures were due to outbreaks among workers at the plants. In others, it was a struggle to keep workers, who were afraid of getting sick, coming into the plant. At the same time, the facilities that were able to remain open had to reduce their throughput significantly. These issues resulted in a significant decline in the number of cattle that were processed, as well as a major reduction in the volume of beef production in the U.S. (Figure 2).

Figure 2. COVID-19 Impacts on Cattle Slaughter and Beef Production



The supply issues in the beef markets caused a dramatic increase in the choice boxed beef cutout, as well as in the live-to-cutout spread. The increases experienced during the height of COVID-19 issues at beef processing facilities were disproportionally higher than the historic levels experienced during the packing plant fire (Figure 3).

Figure 3. Daily Choice Boxed Beef Cutout



These market reactions created much consternation throughout the countryside, resulting in a variety of potential policy responses, as well as triggering USDA to include the COVID-19 market response in its investigation. USDA's report notes that "findings thus far do not preclude the possibility that individual entities or groups of entities violated the Packers and Stockyards Act during the aftermath of the Tyson Holcomb fire and the COVID-19 pandemic. The investigation into potential violations under the Packers and Stockyards Act is continuing." It is also important to note that USDA does not solely own investigatory authority over anticompetitive practices in the meat packing industry. USDA has been engaged in discussions with the Department of Justice regarding this investigation. Both departments will continue to engage as they continue their separate investigations.

Other Considerations in the Report

In addition to the economic analysis portion, the report also includes other considerations that delve into some of the solutions that have been discussed widely by industry in the aftermath of these events. The report notes that at the core of many of these discussions is the desire by many in the industry to see improved price discovery, reinvigorated competition, and a more transparent relationship between the prices for cattle and their further processed products.

Price Reporting and Transparency

Livestock mandatory reporting, which has been in effect for nearly two decades, disseminates market information to the public and has become a key source of information for the industry. One concern voiced by industry about price discovery is the declining number of participants in the negotiated cash market. As the number of participants has faced a steady decline, confidentiality issues have resulted in times when prices cannot be reported in certain regions. An AMS-commissioned study on the current 5-Area cattle reporting regions pinpointed several ways to reduce the incidence of non-reporting due to confidentiality issues. Reducing the incidence of non-reporting will improve price discovery.

AMS is also considering changes made to the way it reports slaughter data. Currently, AMS releases two separate reports, an initial estimated daily livestock slaughter report and a separate report on a two-week lag with the official slaughter numbers that have been gathered by USDA's Food Safety and Inspection Service. The initial report's high degree of accuracy has prompted the department to explore the idea of no longer referring to the initial daily report as an "estimate" and encouraging the market's immediate use of the information.

Risk Management Solutions

The report notes challenges to smaller and medium-sized producers' access to risk management training. Cattle feeders who had hedged when placing cattle on feed prior to the pandemic were able to mitigate the steep decline in live cattle prices once the impacts of COVID-19 hit the economy. Small and medium-sized producers could benefit from products tailored specifically to operations of their size. The report offers an example of reducing the number of pounds per CME feeder and live cattle contract, currently at 50,000 pounds and 40,000 pounds, respectively, to a lower number of pounds to make the contracts more accessible to smaller producers.

Additionally, the report notes the Federal Crop Insurance Corporation board of directors recently approved changes to the Livestock Gross Margin and Livestock Risk Protection crop insurance products to make these instruments more affordable and accessible to producers. Improving these risk management solutions could allow smaller producers to more effectively compete with large producers and weather market disruptions that have a disproportionate impact on smaller producers.

Small Processor and Cooperative Opportunities

The report also touched on issues related to smaller processors and the cooperative model as an option for producer collaboration to enhance marketing power. The current pandemic created a surge in demand for services provided by small and very small processors. In addition, there was a large uptick in consumers interested in buying meat more directly from the producer. The report outlined USDA's commitment to working with stakeholders to balance food safety with these growing consumer preferences and e-commerce platforms.

Packers and Stockyards Act Updates and Enforcement
The report covered recent moves by USDA to update the Packers and Stockyards Act (PSA), as well as potential moves legislators can take to broaden USDA's ability to respond to issues in the market. In January, USDA issued a proposed rule to establish criteria the secretary would consider when determining whether an undue or unreasonable preference or advantage has occurred in violation of the PSA. USDA is currently reviewing the thousands of comments received in response to the proposal as it works to finalize the rule. The report also discussed the idea of creating a beef contract library similar to the swine contract library USDA currently maintains under PSA. The report notes a similar library for beef transactions could potentially help increase price discovery in cattle markets as well as enhance access to market information for all market participants.

The report also noted legislators may consider targeted amendments to the PSA that could provide USDA with investigative and enforcement tools on par with other federal agencies. For example, "the ability to issue Civil Investigative Demands with respect to unfair or deceptive acts or practices would bring USDA's authorities in line with those of the Federal Trade Commission and DOJ." Subpoenas are useful, however the additional authority to require written reports and answers to questions could be very beneficial in some investigations. The report also noted amendments to elevate certain conduct to criminal violations and provide the secretary with the tools necessary to carry out appropriate criminal investigations may also be a very helpful consideration.

Conclusion
The market reaction following both the packing plant fire and the supply chain issues brought on by COVID-19 put many cattle producers at a significant disadvantage. USDA's report outlines the market conditions before, during, and after these events through an economic lens and discusses their ramifications. This report goes beyond analyzing the market reaction to these events to examine other responses, including policy actions proposed by industry groups and steps Congress could take to allow USDA more leverage in conducting investigations and enforcing laws.

This report does not include any details from the investigation into potential violations of the PSA, as that investigation is ongoing and AMS is limited in its ability to publicly report the full scope and status of the investigation.

The report expresses USDA is ready to assist stakeholders and policymakers as the industry continues to explore options to improve price discovery and level the playing field between producers who were harmed and large meatpackers who benefited by the market reactions following these unforeseen and extreme events.

Questions

1. By seeking to improve economies of scale, has the meatpacking industry consolidation negatively impacted farmers and/or consumers?
2. Farm Bureau advocates for the ability to allow the free-market to work within the confines of any applicable law. Are changes to federal laws needed to prevent this level of consolidation in a specific market sector?
3. What could be the impacts to farmers if it is found in these investigations that federal laws have been violated?

TFBF Policy

Packer Concentration and Vertical Integration (Partial)
We are extremely concerned about the effects of packer concentration and vertical integration on the pork and beef industries. The TFBF and AFBF should work to ensure that changes in the structures of the livestock and meat industry do not have an unfairly adverse impact on independent livestock producers. Farm Bureau should:

1. Encourage thorough investigation by the Justice Department in all cases of concentration or integration that may violate antitrust law.
2. Encourage livestock buyers to use premiums/discount schedules that reflect actual carcass value. Quality goals should be as clear as possible and published so independent producers will have a chance of achieving them.
3. Investigate the reasons for the extremely wide farmer-to-retail margins that currently exist in pork and beef and take action (if possible) to keep these margins at reasonable levels.

AFBF Policy

312 / Packers and Stockyards Act (Partial)
2. USDA, in conjunction with the Department of Justice (DOJ), should closely investigate all mergers, ownership changes or other trends in the meat packing industry for actions that limit the availability of a competitive market for livestock producers. Action should be taken to oppose further concentration of meat packers. USDA and DOJ should more aggressively enforce current antitrust laws pertaining to packer concentration.
3. Beef packers who process more than 1,000 head per day should be monitored so they cannot manipulate the market through forward contracting.
4. From a regulatory standpoint, captive supplies should be defined as all cattle owned, or controlled or contracted by a packer seven or more days prior to delivery.
5. The bonding requirement for livestock dealers and packers should be strengthened and more stringently enforced. The requirement should be reviewed on a quarterly basis and be adjusted to reflect the volume of the maximum financial exposure to producers and/or their brokers and then be made available to the public.
6. We believe GIPSA should be accountable to the livestock industry by providing current information concerning license and bond amounts of livestock market, livestock dealers and livestock order buyers.
7. We support:
    - 7.1. Continuation of GIPSA as a separate agency of USDA;
    - 7.2. The addition of dairy cattle and milk processors as named in the Packers and Stockyards Act;
    - 7.3. An amendment to the Packers and Stockyards Act of 1921 that would include the ratite (emu, ostrich and rhea) industry wherever applicable;
    - 7.4. Legislation on a state and national basis, establishing GIPSA as the overall authority and provider of oversight to ensure livestock contracts are clearly-written, confidentiality concerns are addressed, investments are protected, enhanced price transparency and price discovery are enhanced and terms of contracts are honored;
    - 7.5. More vigorous enforcement of U.S. antitrust laws in keeping with original intent; to include the Sherman Act of 1890, Clayton Act of 1914 and Packers and Stockyards Act of 1921;
    - 7.6. Legislation that would prohibit packers from manipulating the number of captive supply cattle slaughtered from week to week in order to manipulate the cash market; and
    - 7.7. Incentives for new meat processing facilities.
8. We oppose:
    - 8.1. Any attempt to lessen the ability of GIPSA to adequately enforce antitrust laws and regulations;
    - 8.2. Prohibiting a packer or livestock buyer from purchasing, acquiring or receiving livestock from another packer, livestock buyer or another packer's or livestock buyer's "affiliate" companies or farms;
    - 8.3. The government making livestock buyers, packers, contractors or livestock owners justify in writing why and how they are buying or selling livestock on the spot market; and
    - 8.4. Any ban on contract livestock buyers purchasing livestock for more than one packer.

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