Negotiated Cattle Trade

Issue

In recent months, there have been many conversations about how cattle are and should be marketed in the United States. Some discussions have focused on the optimal level of cattle transactions through certain marketing channels in order to facilitate greater price discovery. A congressional proposal would require packers to buy a percentage of their weekly cattle purchases on the cash market. This approach conflicts with current Farm Bureau policy and mandatory cash market minimum presents several other problems, not the least of which is the improbability of it providing higher returns for producers. Farm Bureau policy opposes a mandatory minimum for negotiated cattle slaughter because it would restrict producers' ability to enter into progressive, value-added cattle pricing arrangements and contracts.

Background

There are a variety of market transactions through which cattle are marketed. Thankfully, due to Livestock Mandatory Reporting (LMR), we have the data to understand how these animals change hands and how these methods have evolved over time. There are four primary transaction types reported by USDA through LMR.

1) Negotiated purchases, often referred to as the "spot" or "cash" market, are where the price is determined through buyer and seller interaction on the day of sale.
2) Forward contract purchases are agreements for the purchase of cattle transacted in advance of slaughter where the base price is established.
3) Negotiated grid is where the base price is negotiated between buyer and seller and is known at the time the agreement is made. The final net price is determined by applying a series of premiums and discounts based on carcass performance after slaughter.
4) Formula purchases are the advance commitment of cattle for slaughter by any means other than negotiated, negotiated grid, or forward contract. Formula pricing uses a pricing mechanism in which the price is often not known until a future date.

Over the past 15 years, there has been a shift in the way cattle are marketed. In the mid-2000s, roughly 50%-60% of cattle sold were through the negotiated market. Over time, this method of marketing fed cattle has declined and been replaced by formula transactions. We have seen the negotiated market fall from 50%-60% of transactions to roughly 20%. At the same time, we have seen formula transactions increase from roughly 30% to 60%-70% of transactions. Over that same period, we have seen a slight decline in negotiated grid transactions and a fluctuating volume of forward contract transactions.

Cattle can also be marketed on a live or dressed (carcass) basis. Over the previous ten years, there has been a moderate shift even further away from live marketing to dressed marketing. In 2010, just under 60% of fed cattle transactions were on a dressed basis while just over 40% of transactions were on a live basis. Last year, the percentage of dressed transactions had increased to 75% and the percentage of transactions on a live basis had declined to 25%.

There is also significant variation in the types of transactions within each of these marketing channels. Live cattle transactions have traditionally been dominated by negotiated trade and to some extent, formula transactions. These two are followed by forward contract transactions, while negotiated grid has maintained a miniscule share of the trade. Dressed marketing is very much dominated by formula transactions. Given the large share of cattle that are sold on a dressed basis and the fact that dressed cattle are mostly sold through formula pricing, the result is formula making up the majority of transactions for all cattle.

It is also important to understand that types of transactions vary by market regionally. Negotiated trade is more common in certain states, such as Nebraska and Kansas, which have seen negotiated percentage ranges from 40%-75% in recent years. Other states typically have very little negotiated trade. In Texas and Oklahoma, for example, negotiated trade accounts for only 5%-8% of cattle transactions. These discrepancies between regions contrast with the national picture where we see negotiated trade around 20%-23%.

A key point to remember when discussing the optimal level of negotiated transactions is that PRICE DISCOVERY is not the same as PRICE DETERMINATION. While enhanced price discovery is a good thing, it does not necessarily mean it will result in higher prices (as many proponents of minimum thresholds contend). It is critical to note the COVID-19 pandemic and its impact on our country's economy is an unprecedented, exogenous shock to the overall food system and supply chain. No amount of negotiated trade would provide relief from supply chain challenges of this magnitude.

The abundant research by academic faculty at various land-grant institutions on the costs and benefits of alternative marketing arrangements (AMAs) and the impacts of mandatory minimum negotiated trading volumes show that limiting the use of AMAs by the beef industry will decrease efficiency, increase processing and marketing costs, and could potentially reduce beef product quality. One of the most comprehensive research undertakings was the *USDA GIPSA RTI Livestock and Meat Marketing Study*. The six-volume, peer-reviewed report, which represents the work of 30 researchers and nearly three years of effort, indicates there are almost no benefits to a mandatory minimum level of negotiated transactions. Instead, according to the study, a mandatory minimum level of negotiated transactions could create considerable costs due to lost efficiency and product quality. According to the study, these costs would be largely borne by cow/calf producers and consumers. In addition, a recent white paper by Colorado State University's Dr. Koontz indicates a mandatory policy of 50% minimum negotiated cash transactions would result in a $2.5 billion loss to the industry in the first year and an overall loss of $16 billion over ten years.

Further analysis on this issue can be found at www.tnfarmbureau.org/negotiated-cattle-trade

Farm Bureau's current policy supports producers' freedom to enter into value-added cattle pricing arrangements and AMAs. Mandates on negotiated cash trade will ultimately limit the use of AMAs. While more negotiated trade would further bolster price discovery, a minimum negotiated trade threshold means the federal government must monitor and maintain the minimum, inviting further government intrusion into the industry. Furthermore, this additional regulation likely will not solve the problems it is purported to solve and could potentially result in negative consequences for the industry.

Questions
1. Should cattle producers have freedom to enter into value-added cattle pricing arrangements and AMAs?
2. If Congress were to mandate a floor for packers to purchase cattle through negotiated trade, would this ultimately increase prices for cattle producers?

TFBF Policy

Packer Concentration and Vertical Integration (Partial)
The rights of integrators and contractors or those producers who wish to contract with them should not be abridged, but our efforts should be to ensure that independent producers who can efficiently produce high quality hogs and cattle will continue to have local competitive markets for their products.

Production Contracts (Partial)
We support private enterprise and fair market competition where agricultural producers can choose to freely enter into production contracts and marketing agreements, when producers believe it is in their best interest to do so.

When producers have ownership of a commodity, we support their right to enter into any contractual arrangement which they believe is in their best interest, and those contracts should be personal, private, and free from government interference.

We oppose any governmental regulation that limits or adversely affects the rights of producers to work cooperatively with processors, or other entities within the production system to be rewarded as they bring premium value-added products to market.

AFBF Policy

310 / Livestock Marketing (Partial)

1. Livestock producers should have access to competitive markets for price discovery that accurately determines the value of their products.
2. We support:
    - 2.1. Development and implementation of value-based marketing systems which convey the true value of product quality from the retail market to the farm;
    - 2.2. Contracts and marketing regulations should recognize species-specific business and marketing structures;
    - 2.3. Rights of producers and packers to enter into formula pricing, grid pricing and other marketing arrangements and contract relationships. Contracts and marketing arrangements should specify a negotiated base price before commitment to deliver. Such contracts and pricing arrangements should not be used to manipulate the market to the detriment of producers. We encourage producers to retain control over contract delivery and/or contract completion in furtherance of value-added marketing;
    - 2.4. Encouraging co-ops to play a larger role in the meat industry by building or acquiring packing houses;
    - 2.5. Development of new risk management tools to enhance the ability of family livestock farmers to cope with market fluctuations; and
    - 2.6. USDA's efforts to investigate recent beef and pork margins to determine if there is any evidence of price manipulation, collusion, restrictions of competition or other unfair practices.

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