CAPTIVE SUPPLIES IN THE LIVESTOCK INDUSTRY
TESTIMONY FOR USDA PUBLIC FORUM
DENVER, COLORADO
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by: Jim Peterson, Executive Vice President
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Thank you for this opportunity to comment. For the record, my name is Jim Peterson. I am speaking today on behalf of the more than 2,500 livestock producer members of Montana Stockgrowers Association in Montana. Since 1884, the Montana Stockgrowers Association has been representing its members to ensure a fair, competitive and favorable economic climate in the beef industry in Montana and the United States. I am also a cow/calf producer, cattle feeder and farmer from central Montana.

For the last 10 years, I have been executive vice president of the Montana Stockgrowers Association. Prior to that, I was on the staff of the Texas Cattle Feeders Association for 10 years and managed an agriculture lending department for a major bank in Amarillo, Texas. Back in the 1970's, when I was working in the feedlot industry in Texas, feedyards sold their fed cattle one pen at a time to buyers who visited the yard and assessed the value of each pen individually. Cattle sales took place on a "pen by pen basis" and cattle were sold based on a negotiated cash price subject to a visual appraisal of value between buyer and seller.

Today, feedyards typically sell their entire show list, which may include many pens of cattle of differing quality and genetics, at one average price. This sale might take place over a time span of 15 minutes to maybe one hour during an entire week.

Feedyards may also sell, or contract cattle for sale, on a value based "formula" or "grid" with the fed cattle to be delivered at a future date without any negotiated base price. Once the cattle are delivered for processing, the base price may then be determined based on the average cash price for the week of delivery in that marketing area or a "plant average price" for that same week.

The contract cattle are considered part of the "captive supply" in the industry which is estimated to be as much as one-third of the USDA federally inspected fed cattle processed today. In fact, we feel the better cattle sold on a "grid or formula basis" and contracted in advance without a negotiated base price, result in additional "market power" for major processors. Additionally, if the base price is based on an average price made up of the remaining cattle, we wonder what downward bias this may place on the market and the resulting impact captive supply might have on the market.

An example to make my point is the first quarter of 1999 in the graph I have attached to this testimony (Attachment A). During the first quarter of 1999, wholesale beef prices were higher than they had been since 1996 and beef tonnage marketed was higher than it had been since any time in 1996. As you can see from the graph, reported on the DTN Marketing Services on July 16, 1999 the packer-farmer-wholesale spread for the first quarter of 1999 was 69% greater than the previous year and 46% larger than the 4 year average.

The realities of this graph support how captive supply and market power led to extraordinary processing profits by major processors by: 1) disciplined live cattle cost containment as a result of marketing techniques described earlier in larger feedlot offerings, and 2) the successful defense of the highest wholesale beef prices since 1993, which is probably a result of better beef demand. We know that beef demand is better than it has been since 1993; however, cattle producers have not been able to significantly improve prices or "move the market" for the raw commodity we produce...fed beef. During the period I have described in 1999, I estimate that beef producers failed to receive an extra $50 per head because of our inability to "move the market."

We know the four major packers control approximately 70% of all the cattle slaughtered in the US, and they control about 80% of all fed cattle slaughtered. The resulting market power has allowed packers successful cost containment of the raw commodity we produce (fed beef) during the first quarter of 1999 and this situation also exists today with ample supplies of fed beef available.

The question now becomes what do we do? As a result of proposals like the WORC petition to mandate how cattle can be sold, Montana Stockgrowers Association was a major part of the initial effort that led to legislation passing Congress that mandated price reporting. MSGA is very supportive of mandatory price reporting because we feel it will put transparency into the marketing system and level the playing field for everyone. There is a lot of speculation as to what will actually happen, but we know one thing, it is hard to fix something you can't measure. We hope that through price reporting we can begin to deal with the real issue of what is actually happening and ultimately lead to a more meaningful discussion of price discovery and value-based marketing. USDA should implement the reporting rules as soon as possible.

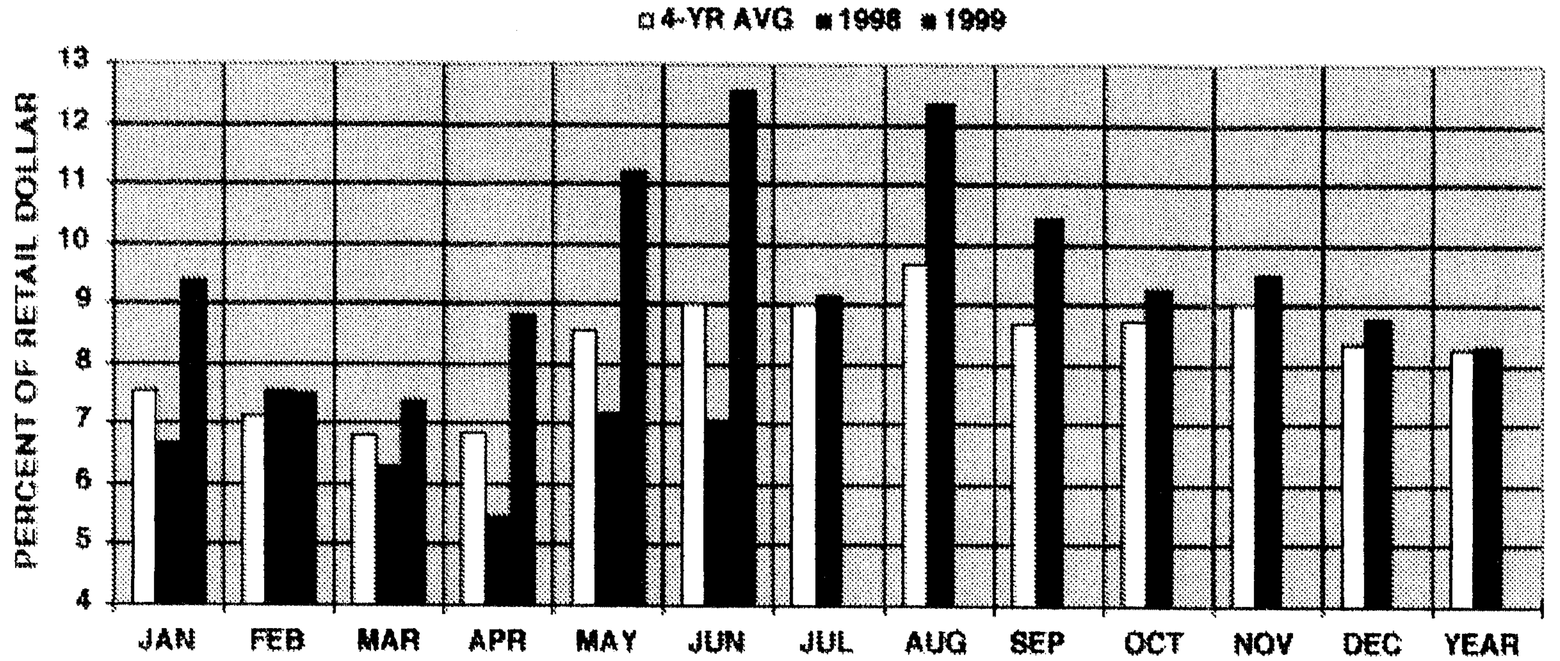
We also feel that once price reporting is implemented and price transparency can be obtained, we can then look at a better system of price discovery and the sale of cattle based on some kind of negotiated base price rather than waiting until after the fact to determine price.

Montana Stockgrowers is opposed to any government regulation that would tell anyone how they must sell their cattle or how they must buy their cattle. However, we feel it is important especially during these tough economic times, with mergers and the concentration that exists in our industry, today, that a mechanism of marketing transparency be implemented. We hope the result will be to measure the impact of various marketing activities and allow us to develop a better system of price discovery and value determination for our product.

There is no question that market power exists. On the other hand, we have not seen any conclusive evidence that anything illegal is taking place.We do feel, however, that the market power that exists in the market today has led to, in several cases, producers not being able to move the market in their favor in a time when beef demand is better than it has been in years.

Thank you for this opportunity to comment.

BEEF PACKER SHARE OF RETAIL DOLLAR



PACKERS REWROTE THE BOOK on the farm-to-wholesale spread last quarter, driving it to levels never seen before (i.e., the spread averaged 30.9¢ in the April-June period, 69% greater than last year and 46% larger than the 4-year average. Two realities supported the size of the spread and extraordinary processing profits: 1) disciplined live cattle cost containment (aided in part by larger feedlot offerings than expected) and 2) the successful defense of the highest wholesale beef values seen since 1993.

Attachment to Jim Petersen testimony Montana Stockgrowers