



# New Market Structure; Old Market Challenges

**Change is not new in the beef marketing system. Here's a look at some of the major events that have shaped the industry into what it is today.** By Jim Robb

**N**ew technology and periodic challenges have shaped the U.S. fed cattle and beef marketing system into what we have today. These changes have resulted in a more competitive industry in the battle with other animal-based proteins, both domestically and globally.

Even though the actors have changed, three constants have been dominant over the decades:

- Producers need processors and vice versa.
- Markets provide the foundation for transactions between producers and packers.
- Short-term interests of all participants along the marketing chain often collide.

When looking ahead to how the cattle/beef marketing chain might evolve, it is informative to look back. Statements like “that will kill the industry” are often made, but those dire assessments have never materialized. The lesson has been this: to keep up with a changing marketing system, price discovery and reporting also had to change.

## **Back in Time: Terminal Markets Like Fort Worth**

Much of the structural change in the U.S. beef industry in the last 40 years involved feedyards and packers. Let's start with a look at a town which was a stopover for South Texas herds being driven to the Chisholm Trail then north to a viable market—Fort Worth, Texas.

When the railroad arrived at Fort Worth, pens were built in 1876 and by the mid-1880s, the city was known for its stockyards and thriving related businesses. In 1902, Armor and Swift were enticed to Fort Worth, where they built packing plants for cattle and hogs and each company was initially given one-third ownership of the stockyards. Hence, Fort Worth became a “terminal” market.

The Fort Worth calf market in 1906 was the second largest in the U.S. behind Chicago. In 1917, a record of more than 3.5 million animals (mostly cattle, hogs, sheep) were sold through that stockyard, with most bought and processed into carcasses by the Fort Worth packers.

Over time, the market power of terminal packers in terms of buying cattle became a concern, resulting in the Packers and Stockyards Act of 1921.

Probably, meat packers denounced those major changes, claiming they would “kill the industry.” However, terminal stockyard receipts were already well on the decline as smaller regional auctions began taking a greater share.

Terminal markets in the U.S. also included Omaha and Chicago. Many plants processed several different species in one facility. Plants developed cost-efficient assembly line operations and brand names for their meats. Selling “swinging beef” in the form of carcasses and efficient rail transportation were the mainstays of terminal markets.

Fort Worth led the decline in the role of terminal market packers as old plants collided with new forces, such as truck rather than rail transportation, and a rapidly growing commercial High Plains feedlot industry in the 1960s. Beef packing began decentralizing to be near the cattle in new commercial feedyards.

In 1971, the last of the packing plants at the Fort Worth stockyards closed. Livestock numbers at the Fort Worth stockyards continued to decline almost every year, and the last auction was held in December 1992.

Other terminal markets followed. The Omaha stockyards closed in 1999. Interestingly, Fort Worth set another standard for terminal markets in the 1970s—in 1976 the Fort Worth National Historic District was established and the stockyards district became a major tourist destination with restaurants and other retail stores. Later, Omaha established a Stockyards Historic District redevelopment project.

## Along Came Boxed Beef

With the next generation of beef-specific packing plants near feedyards, packers began providing boxed beef rather than selling carcasses. That was an important technological and marketing innovation, which helped reshape the wholesale and retail markets.

Boxed beef dramatically changed beef marketing. The old view was that the transaction was over when the carcass was sold, and it became the butcher's problem to deal with.

Boxed beef, however, extended the marketing window and allowed retailers and HRI end users to buy specific cuts and better accommodated seasonal and local marketing considerations. The centralized processing also allowed much more efficient use of beef trimmings and tallow, which sharply reduced spoilage and waste. By pricing beef by individual primal, it increased the value of the overall carcass. What's more, the introduction of individual cuts facilitated forward pricing, giving retailers a better way to manage risk.

Boxed beef involved breaking down a carcass and packaging cuts in cardboard containers. That approach greatly reduced marketing system costs and allowed sale of boxes of one item that the retailer or restaurant wanted. Of course, the technology was opposed by many and eliminated many breakers and local butchers, but the days of carcasses as the wholesale transaction unit disappeared, though some assume it still exists.

Along with boxed beef came self-serve meat counters in grocery stores. That sales system reinforced retailers' ability to fill their needs, especially when featuring beef cuts in newspaper ads. That also spawned more innovations in the wholesale beef marketing system as processors adapted to a changing retail beef counter.

In the 1980s, when industry conferences began discussing the need to offer cuts trimmed to one-half inch of fat, many experts deemed the idea unworkable. Who would pay for the trimming? It turned out to be a non issue, as one-half inch trim quickly transitioned into one-quarter inch of fat remaining on cuts sold by packers. Consumers, packers and retailers ended up all benefiting in what today looks obvious.

But some debates continue. For example, we have been hearing since early in the boxed beef era that, "cattle are getting too big for the box." So far, except in a short-term sense for some middle meats, dire consequences have not happened due to carcass size.

Bigger cattle were processed using innovative machines in packing plants, and cuts were made smaller by creative cutting techniques based on sound research on separating out key individual marketable muscles. And there has yet to be economic incentives for producers to reduce average steer slaughter weight.

## A History of Change

Almost from the beginning, cattlemen have been adjusting to a changing marketing environment. Here's a short timeline of major industry events, courtesy of the book, "Building the Beef Industry: A Century of Commitment 1898-1998" by the late Charlie Ball, TCFA executive vice president emeritus:

**1883** National Cattle Growers Association was organized.

**1884** Bureau of Animal Industry established; was the predecessor to GIPSA.

**1887** American Cattle Trust patterned after the Standard Oil Trust organized with office in New York. Prominent cattlemen from Colorado, New Mexico, Texas and Wyoming organized to fight the packer monopoly with a cattle monopoly of their own.

**1890** Sherman Antitrust Act adopted by Congress.

**1898** National Live Stock Association formed.

**1899** National Live Stock Association President John Springer at the second convention listed the major challenges facing the industry, then noted, "The men, or set of men, who are continually looking backward for inspiration; who are chuck full of calamity forebodings; who thrive on opposition to any and all measures; who are constantly quoting history, are not fit to lead progressive, enterprising, 20th century Americans."

**1860s-1880s** Railroads established, ending cattle drives and providing catalyst for the terminal stockyards and big packing plants.

**1901** NLSA President Springer drew applause with the statement at the annual convention... "It was a great day for our country when Armour, Swift, Morris, Cudahy, Hammond, Sulzberger and others notified the stockmen and the world that they would kill everything offered, waste nothing and supply the world's markets."

**1919** Packer Consent Decree accepted; forced sale of packer interest in terminal markets and railroads.

**1921** Packers and Stockyards Act passed by Congress.

**1922** National Livestock and Meat Board established for first organized promotion of beef.



## A History of Change

**1943** President Roosevelt orders freeze on all wages and prices during WWII.

**1946** Price controls removed and mass strikes for higher wages.

**1949** Secretary of Agriculture Brannan promoted price supports and production controls to raise commodity prices, including cattle. American National Live Stock Association opposes subsidies and controls.

**1953** Dalhart, Texas—500 cattlemen met and organized the United Livestock Producers Association to support parity price supports for cattle and blasted American National Cattlemen's Association stating, "Existing livestock associations don't represent the real sentiment of cattlemen. If we don't get supports at 90% to 100% of parity, we're breeding another depression."

**1954** American National Cattlemen's Association (ANCA) President Hyatt responded at the annual convention, "We've had some awful good times in the cattle business. Now that we've had a bump, are we going to get weak-kneed and go on the dole? I say let's stand on our own and put some sense into the farm program."

**1957** Amalgamated Meat Cutters and Butcher Workmen and the AFL-CIO proclaimed that beef should only be sold between 9 am and 6 pm Monday through Saturday when butchers were on the job.

**1960s** Transportation shifts from rail to trucks; slaughter operations built near feedyards rather than stockyards and leads to demise of central stockyards.

**1962** Rachel Carson's book *Silent Spring* warns of dangers of pesticides and begins the environmental movement.

**1964** CME offers first live cattle contract; membership seat cost \$10,000.

**1960s** Secretary of Agriculture Orville Freeman proposed marketing orders, production controls and subsidies for cattle production to increase prices. Freeman warned ANCA, "If the farm bill fails, cattle prices will plunge 38% to \$8 per cwt."

**1960s** ANCA President Dressler lobbied Congress to "delete from HR 6400 all provisions that would bring the beef cattle industry under any form of production or marketing controls, subsidies or compensatory payments. We do not believe that planned scarcity and artificial prices are in the best interest of our customer, the consuming public."

## Economics Also Shaped Market Structure

Research has quantified and simple observation has shown that economies of size and scale have been important forces in shaping the feedyard and packing industries. That is, in the beef industry, larger firms tend to gain cost advantages. Of course, larger firms raise concerns about concentration and pricing power. While that's not unique to cattlemen—that economic reality exists in any commodity market—cattlemen have been and continue to adjust.

Still, regarding beef packing, the economic research shows trade-offs between the cost reductions embedded in large firms and the lack of competition that can simultaneously occur.

The Livestock Marketing Information Center has been estimating commercial Southern Plains cattle feeding returns since the mid-1970s. In general, those returns show economic distress has been an all-too-common fact of life. In feedyard parlance, we've seen plenty of price wrecks over the years.

In the modern era of cattle feeding, the father of all price wrecks was in 1973. As the late Charlie Ball, TCFA executive vice president emeritus, summarized in his book, "The Finishing Touch," three things together "... inflation, higher grain and more cattle—cut the rug from under cattlemen in 1973." Industry problems were compounded by a government-mandated retail beef price freeze.

The most recent wreck began in 2007 and didn't end until 2009. In between, there have been plenty more. Every wreck has highlighted the importance of risk management and contributed to the development of alternative marketing arrangements (AMAs), such as forward contracting and formulas, as a marketing practice, rather than just relying on the spot market.

## Dealing With Quality and Consumers

The use of grades and standards has helped develop beef industry marketing channels based on valuable quality characteristics. Unbiased grading by USDA provided transparency in the marketplace, from feeder cattle grades to carcass quality grades (e.g. Choice).

Grades combined with commodity-based price signals were not enough to develop markets targeted at some consumers, however. Certified Angus Beef and grid pricing for fed cattle emerged in the 1990s and provided the foundation to reward those producing desired characteristics.

These changes spurred productivity to increase and ultimately raised quality standards across the board. They also more closely linked producers with wholesale markets.

Importantly, those arrangements have allowed several new initially small firms, including those focusing on natural beef, to gain a niche and then a significant role in the beef industry—innovations that commodity-based large packers initially did not participate in.

## What About Price Discovery?

All the transitions described above, plus additional factors, have challenged the process of price discovery and transparency in the marketplace. Transparency—defined as seeing timely and unbiased price linkages throughout the marketing chain—is an ongoing and bumpy process.

For several decades, terminal auction markets like Fort Worth, Omaha and Chicago were the point of market transactions for slaughter-weight cattle.

## A History of Change

Even as those markets declined in relevance, they served an important function of price discovery. In fact, USDA economic analysis officially used the Omaha slaughter steer stockyards auction price as the national benchmark until the mid-1990s.

For several years, market participants decried the loss of price discovery and competition being lost at the terminal markets. But often the better quality cattle already were being sold direct, causing various organizations and eventually USDA to begin focusing on the direct trade in their price reporting.

To deal with the change from selling carcass to boxed beef, the USDA wholesale price reporting system needed to keep up. The result was USDA's development and reporting of cutout values, which are carcass equivalent wholesale prices calculated from wholesale cut values. Eventually, cutout values became the industry standard for wholesale price reporting, but not without initial resistance at both the packer and producer levels.

USDA has had major involvement in livestock price reporting since the 1940s. Until Mandatory Price Reporting (MPR) was legislated for livestock in 1999, the system was based on voluntary price reporting, with collection, evaluation and synthesis by professional market reporters.

MPR was legislated largely because of changes that were occurring in slaughter hog and cattle marketing arrangements, including formulas and forward contracts that weren't being captured with the traditional voluntary system. MPR overhauled fed cattle and wholesale beef price reporting to keep up with industry changes when it was implemented in 2001.

Emergence of large commercial feedyards caused feeder cattle prices to be differentiated by weight groups. Feeder cattle as a classification emerged and non-fed steer and heifer slaughter became an anomaly.

Federal-State Market News reporting was facilitated by the USDA's establishment of feeder cattle grades and unbiased reporting of auction prices. Later, USDA began reporting prices of feeder cattle sold directly, which is still a challenge due to lack of government funding, the resulting number of market reporters, and the need for order buyers to protect their privacy.

### What's Ahead?

With every major change has come major resistance. It's human nature to resist change, but with every challenge that cattlemen and the cattle market have faced, the industry has progressed.

Today we face similar challenges adapting to the current market structure of this industry, including AMAs. At the same time, new technology and forces are on the horizon. For example, packers are beginning to provide "mega retailers" with case-ready products. Will international trade change wholesale products? How will high speed carcass quality grading change incentives to cattle producers?

The price discovery and reporting system will need to keep pace, if we are to maintain a transparent and efficient market-based industry. And given a chance, it will. 🐾

EDITOR'S NOTE—Jim Robb is director of the Livestock Marketing Information Center in Denver.

**1967** Boxed beef introduced; revolutionized beef processing and transportation with enormous efficiencies and savings. Eliminated many brokers, wholesalers and butchers, which led to labor union strikes at packing plants and union blockage of boxed beef into New York City as the largest meat market in the world.

**1969** ANCA accused by members of Congress of possible violations of restraint of trade; Justice Department investigation called to investigate illegal conspiracy "which may be partially responsible for recent increase in retail beef prices."

**1971** Union Stockyards in Chicago closes after 106 years of operation.

**1973** President Nixon implements first peace-time price freeze; leads to "The Wreck" for cattlemen; U.S. cattle inventory peaked at 135 million head.

**1974** Commodity Futures Trading Commission (CFTC) created to prevent price manipulation and unfair practices in commodity futures trading.

**1975** American Beef Packers declares bankruptcy.

**1970s** Cattlemen sue packers, retailers and *The Yellow Sheet* report for beef price manipulation.

**1977** Merger of the American National Cattlemen's Association and the National Livestock Feeders Association created the National Cattlemen's Association (NCA).

**1978** Agriculture Secretary Hardin appoints a *Meat Pricing Task Force* comprised of 10 cattlemen and consumers to investigate price manipulation. The task force concluded that *The Yellow Sheet* was not manipulated and recommended formula trading continue, mandatory price reporting be avoided and electronic meat marketing be explored.

**1980s** Boxed beef essentially replaced carcass beef trading and USDA developed Boxed Beef Cut-Out Values.

**1986** National \$1-per-head beef checkoff was enacted.

**1989** National Cattlemen's Association (NCA) appoints nationally-recognized economists to report on *Competitive Issues In The Beef Industry: Can Beef Compete in the 1990s?* Major conclusion of the study was that beef producers must lower their cost of production in order to remain competitive with other meats.

**1996** Merger of the Beef Industry Council of the National Live Stock and Meat Board and NCA created the National Cattlemen's Beef Association (NCBA).