Fighting for the U.S. Cattle Producer!
R-CALF USA

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June 9, 2010

Marilyn R. Abbott
Secretary to the Commission
U.S. International Trade Commission
500 E Street, S.W.
Washington, D.C. 20436

Re: ***Investigation No. 332-518, "China's Agricultural Trade: Competitive Conditions and Effects on U.S. Exports"***

Dear Ms. Abbott,

The Ranchers-Cattlemen Action Legal Fund, United Stockgrowers of America (R-CALF USA) appreciates the opportunity to submit this pre-hearing brief regarding *China's Agricultural Trade: Competitive Conditions and Effects on U.S. Exports* pursuant to the U.S. International Trade Commission's (USITC's) Investigation No. 332-518.

R-CALF USA, a national, non-profit organization, is dedicated to ensuring the continued profitability and viability of the U.S. cattle industry and represents thousands of U.S. cattle producers on domestic and international trade and marketing issues. R-CALF USA's membership consists primarily of cow-calf operators, cattle backgrounders, and feedlot owners. Its members are located in 46 states and the organization has numerous local and state association affiliates, from both cattle and farm organizations. Various main street businesses are associate members of R-CALF USA.

I. INTRODUCTION

R-CALF USA does *not* represent the entire U.S. beef supply chain. Rather, R-CALF USA exclusively represents the live cattle segment of the beef supply chain, meaning it represents the farmers and ranchers located across the U.S. who breed, birth, and raise live cattle for breeding purposes and beef production. These live cattle are subsequently marketed to beef packers that transform live cattle into the commodity beef, which is then further processed and/or marketed to other entities within the beef commodity industry (e.g., beef processors, beef wholesalers and distributors, and beef retailers), or is exported.

It is critically important that the USITC recognize that the live cattle industry is a distinct industry segment within the U.S. beef supply chain and that a clear demarcation point exists between the live cattle industry and the beef commodity industry – a demarcation point so profound that often there is an inverse relationship between economic prosperity in the live cattle industry and economic prosperity in the beef commodity industry.[1] As explained in more detail below, and in even greater detail in the attached Appendix: Under Siege: The U.S. Cattle Industry, this demarcation point effectively invalidates the premise that increased U.S. beef exports to China will reverse the ongoing contraction of the U.S. cattle industry, which continues to cause the hollowing out of rural communities all across America.

[1] *See*, e.g., Sparks Companies Inc., "Potential Impacts of the Proposed Ban on Packer Ownership and Feeding of Livestock," A Special Study, (March 18, 2002) at 24 ("Vertical integration [of the live cattle industry and the beef commodity industry] often attracts investors because of the negative correlation between profit margins at the packing stage [beef commodity stage] and the feeding stage [live cattle stage].").

As R-CALF USA will demonstrate below and in the attached Appendix, historical data show that: 1) the production of beef derived from the U.S. cattle industry is insufficient to meet domestic beef demand; 2) despite this seemingly favorable supply/demand balance, the U.S. cattle industry continues to shrink at an alarming rate; 3) U.S. cattle prices inexplicably remained severely depressed during prolonged periods of rising – and record – U.S. beef exports; 4) U.S. cattle prices rose to the highest nominal levels in history while exports were substantially reduced; and, 5) any increased benefits from increased exports have been captured by the concentrated beef packers and have not been competitively allocated to either the U.S. cattle industry or to U.S. consumers.[2]

Although the factors that prevent increased U.S. beef exports from contributing to the improvement of the economic condition of the U.S. cattle industry persist today and remain unaddressed by either Congress or the Administration, R-CALF USA nevertheless appreciates this opportunity to address the USITC's specific request for information related to the conditions of competition in China's agricultural market and trade and their effect on U.S. exports of beef and other products derived from cattle. It is R-CALF USA's sincere hope that by engaging in the ongoing process, wherein erroneous cattle industry assumptions continue to facilitate national policies that benefit beef packers at the expense of cattle producers and consumers, we can begin to reform such national policies by correcting the misinformation upon which they are based.

R-CALF USA's position regarding this instant investigation is this: Congress and the Administration are mistaken in their belief that a goal of increasing U.S. beef exports will

[2] Hereafter R-CALF USA respectfully uses the term "U.S. cattle industry" or "cattle industry" to reference and describe the "U.S. live cattle industry," and such term shall mean the industry comprised of U.S. farmers and ranchers who breed, birth and raise live cattle for breeding purposes and beef production.

reverse the economic deterioration that has plagued the entire U.S. cattle industry for the past several decades (the prolonged period when the predominant emphasis already was on export expansion). Until and unless Congress and the Administration address the factors that continue to allow the beef packers and beef retailers to capture the profits that a competitive market would otherwise allocate to cattle producers, their collective efforts to increase exports will not reverse the ongoing contraction of the U.S. cattle industry. Increased U.S. beef exports *should* increase the welfare for U.S. cattle producers, but they have failed, and continue to fail, to do so. This is evidence of the loss of competition in the U.S. cattle industry.

The USITC already has recognized a key factor that helps explain why the profits from increased exports that a competitive market would predictably allocate to cattle producers, are not so allocated. The USITC previously determined that due to the present structure of the U.S. cattle industry, lost profits realized by the beef packing industry as a result of declining beef prices likely will be transferred to the live cattle industry in the form of lower cattle prices:

> U.S. beef packers operate on the margin between wholesale beef prices and slaughter cattle prices. Market structure suggests that processors can eventually pass most, if not all, of any decrease in the price of wholesale beef on to cattle producers in terms of lower slaughter cattle prices.[3]

Because the current structure of the U.S. beef packing industry enables it to defy competitive market forces and pass losses resulting from lower wholesale beef prices directly to the U.S. cattle industry in the form of lower cattle prices, it is obvious that the beef packing industry possess considerable market power that enables it to determine what it will and will not

[3] U.S.-Australia Free Trade Agreement: Potential Economywide and Selected Sectoral Effects, U.S. International Trade Commission, Investigation No. TA-2104-11, USITC Publication 3697 (May 2004), at 44, fn 25.

pass on to the U.S. cattle industry. With such competition-defying market power, the beef packing industry likewise is positioned to defy competitive market forces by capturing increased profits resulting from higher wholesale beef prices, without passing such increased profits on to U.S. cattle producers in the form of higher slaughter cattle prices. *Thus, it is R-CALF USA's firm belief and conviction that the U.S. beef packing industry remains insulated from negative price movements associated with increased import volumes and is capturing for itself any positive prices movements associated with increased exports.*

We, therefore, urge extreme caution in working to increase access for U.S. beef exports in China until reforms are instituted to restore a fully functioning competitive marketplace for U.S. cattle producers. Furthermore, we vehemently oppose the granting of any concession that would facilitate Chinese imports of cattle, beef, or other products derived from cattle as a *quid pro quo* for achieving increased export access.

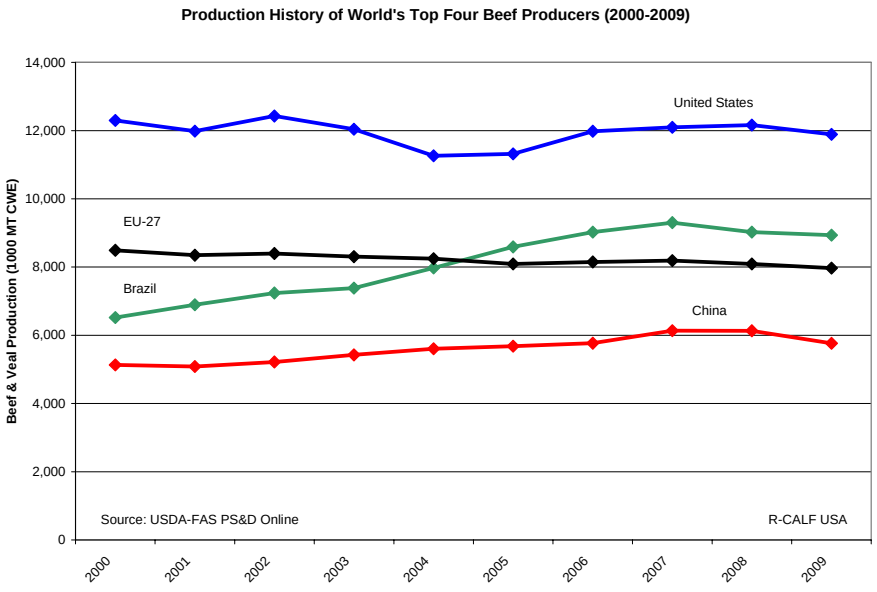
II. COMPETITIVE FACTORS REGARDING TRADE WITH CHINA

In addition to the discussion below, the Appendix attached to this pre-hearing brief provides explanatory information that reinforces R-CALF USA's assertions regarding the consequential impact the lack of competition in the domestic cattle industry has on the competitiveness of the U.S. cattle industry with respect to China.

A. Overview of China's Beef and Cattle Market, Including Recent Trends in Production, Consumption, and Trade

With over 105 million cattle, China controls the world's third largest cattle inventory behind only India and Brazil.[4] The U.S. has the world's fourth largest cattle inventory with approximately 94 million cattle.[5] It is noteworthy as an aside that while the U.S. has been decreasing the size of its cattle herd since 1996, the 17 countries with which the U.S. currently has free trade agreements with have been increasing their collective herd size.[6] China is the world's fourth largest producer of beef and veal, positioned behind the U.S., Brazil, and the European Union (EU-27), respectively.[7] As revealed in Chart 1 below, both China and Brazil increased their production of beef and veal during the past ten years, while the U.S. and the EU-27 both decreased their production during this period.

CHART 1



[4] *See* Cattle Summary, Selected Countries, Production, Supply, and Distribution Online, U.S. Department of Agriculture, Foreign Agricultural Service, available at http://www.fas.usda.gov/psdonline/.
[5] *See id.*
[6] *See* FAOSTAT Production Database, Food and Agricultural Organization of the United Nations, available at http://faostat.fao.org/site/573/DesktopDefault.aspx?PageID=573#ancor.
[7] *See* Beef and Veal, Selected Countries, Production, Supply, and Distribution Online, U.S. Department of Agriculture, Foreign Agricultural Service, available at http://www.fas.usda.gov/psdonline/.

As revealed below in Chart 2, both China and Brazil increased their aggregate domestic consumption of beef and veal while the U.S. and the EU-27 both decreased their aggregate domestic consumption during the past decade.

CHART 2

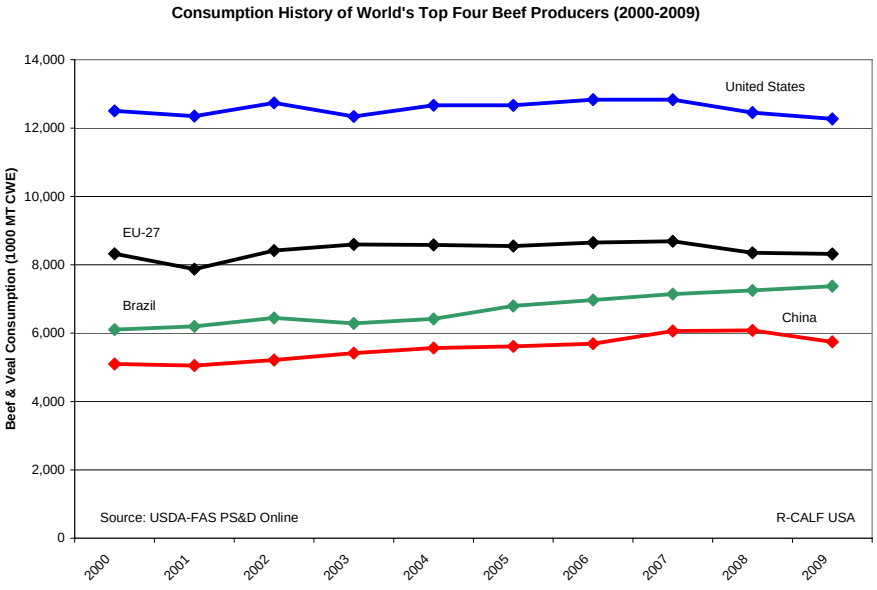
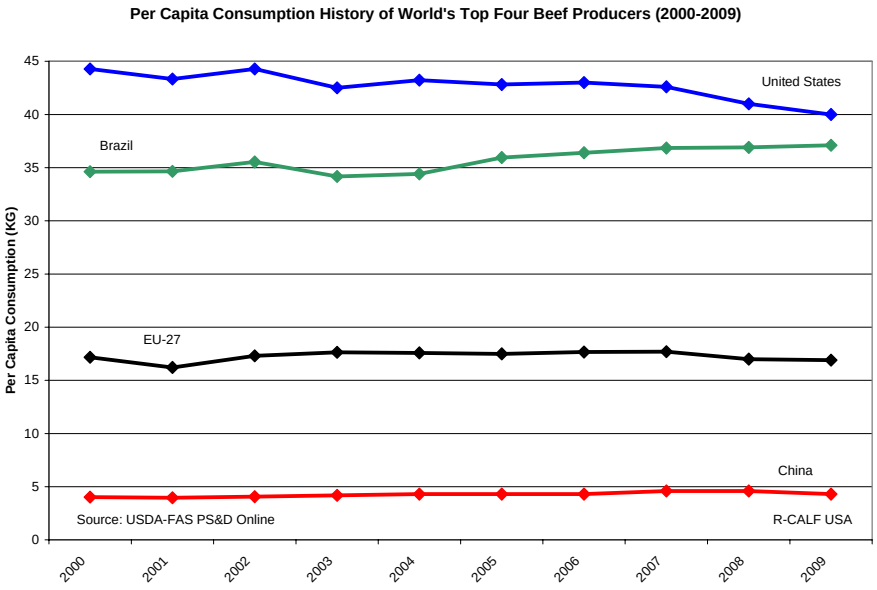


Chart 3 below shows these trends are also consistent with per capita consumption: the per capita consumption of beef and veal has increased in both China and Brazil, but decreased in both the U.S. and the EU-27 over the past ten years. China's per capita consumption of beef and veal has remained exceedingly low during the past decade and increased from only 4.02 kg per person in 2000 to only 4.30 kg per person in 2009.[8] China's per capita beef consumption is nearly ten times less than that of the United States, where per capita beef consumption was 40 kg

[8] Production, Supply, and Distribution Online, U.S. Department of Agriculture, Foreign Agricultural Service, available at http://www.fas.usda.gov/psdonline/.

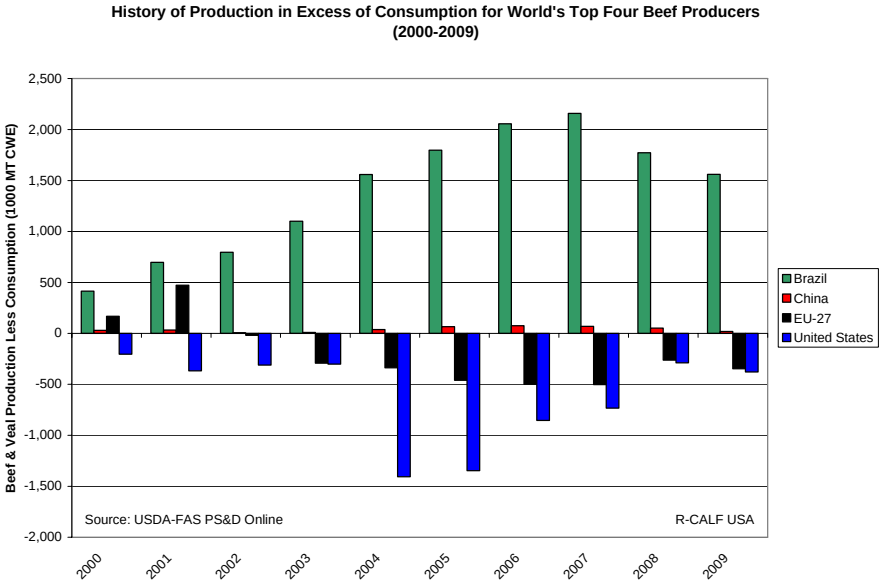
per person in 2009. In contrast, China's per capita consumption of beef substitutes (i.e., pork and poultry) is more substantial: China's 2009 per capita pork consumption at 36.40 kg per person rivals the United States' per capita consumption of beef and China's 2009 per capita consumption of poultry at 9.10 kg per person was more than twice the volume of its per capita beef consumption.

CHART 3



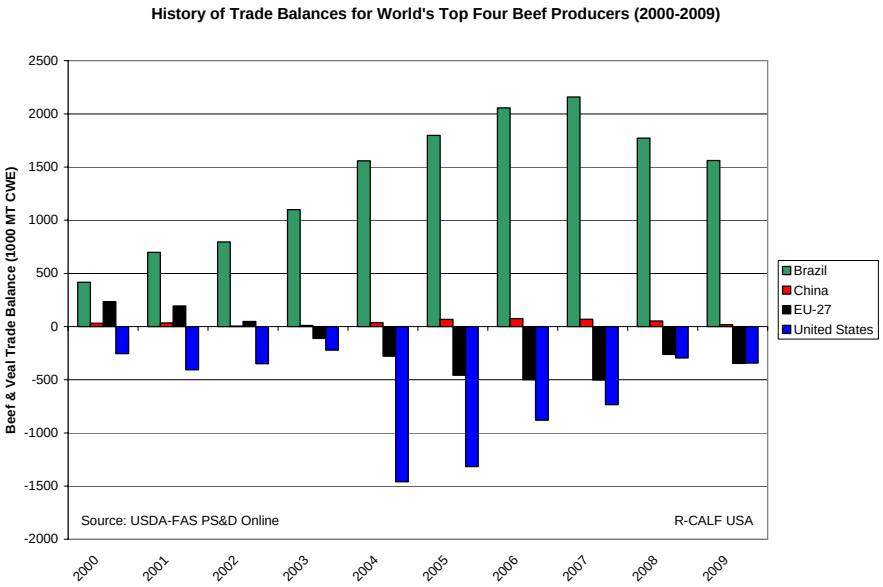
In each of the past ten years, both China and Brazil produced more beef and veal than what could be consumed within their respective countries, as did the EU-27 until 2002. In contrast, Chart 4 below shows the U.S. under-produced for its domestic market in each of the past ten years, while the EU-27 also did not produced sufficient volumes of beef to satisfy its countries' domestic consumption of beef and veal during the past eight years.

CHART 4



Not surprising, particularly in view of its persistent annual production in excess of consumption, China's trade balance regarding beef and veal (i.e., its exports minus its imports), like that of Brazil's, has remained positive over the past ten years as China annually exports more beef and veal than it imports as shown below in Chart 5. In contrast, the U.S. has maintained a persistent trade deficit over the past decade as it annually imported more than it exported, as did the EU-27 in each of the past eight years.

CHART 5



The level of China's beef imports and beef exports reported in USDA's March 2, 2010, GAIN Report (GAIN Report) appear to greatly over-exaggerate China's actual trade flows when compared to data available on USDA's online database. For example, the GAIN Report estimated China's beef imports at "well over 100,000 metric tons in 2009" and estimated that China's beef exports would "decline 26 percent to 280,000 MT."[9] However, USDA's online database indicates that China's beef imports over the past ten years peaked at only 32,000 MT in 2002 and were only 20,000 metric tons in 2009; and, China's beef exports during the past ten years peaked at 85,000 MT in 2006 and were only 38,000 MT in 2009.[10] The USITC should attempt to reconcile these conflicting trade data to ensure it has accurate information to support any conclusions it may reach regarding China's trade in beef and veal.

[9] GAIN Report, China-Peoples Republic of, Livestock and Products Semi-Annual, FAS Beijing 2010, U.S. Department of Agriculture Foreign Agricultural Service, No. CH10009, March 2, 2010.
[10] Production, Supply, and Distribution Online, U.S. Department of Agriculture, Foreign Agricultural Service, available at http://www.fas.usda.gov/psdonline/.

What these data suggest is that unless significant changes occur in China's beef consumption patterns, beef-product distribution patterns, or beef spending patterns, which have not occurred appreciably over the past ten years, China likely will not represent a significant beef and veal export opportunity for the U.S. in the foreseeable future. Indeed, prior to the U.S. detection of bovine spongiform encephalopathy (BSE) in a cow imported from Canada in late 2003, which resulted in immediate and widespread bans of U.S. beef exports by China and most other beef importing countries, the *total* value of U.S. exports of beef, beef variety meat and processed beef to China grew from approximately $15 million in 2000 to approximately $27 million in 2003.[11] The value of U.S. exports of whole hides of cattle to China represented a more substantial market opportunity *for U.S. beef packers*: in 2000 and 2001, the U.S. exported approximately $209 million and $355 million in whole cattle hides, respectively.[12] However, U.S. exports of whole cattle hides to China appear to have ended after 2001, a full two years before the BSE detection that affected China's imports beginning in 2004.[13]

Interestingly, a November 2009 USDA GAIN Report states:

> Fueled by lower Chinese production and strong consumer demand, imports of U.S. beef through gray channels are forecast to approach $200 million in 2009, making China's gray channel trade our fifth largest beef export market.[14]

[11] *See* Global Agricultural Trade System Online, U.S. Department of Agriculture, Foreign Agricultural Service (Includes the following six-digit HS codes: 020110, 020120, 020130, 020210, 020220, 020230, 020610, 020621, 020622, 020629, 021020, and 160250.), available at http://www.fas.usda.gov/gats/default.aspx.
[12] *See id.* (Includes the six-digit HS code 410121.).
[13] *See id.*
[14] GAIN Report, China-Peoples Republic of, Commodity Market Update, U.S. Department of Agriculture, Foreign Agricultural Service, No. CH9089, November 18, 2009, at 2.

This prediction, however, cannot be verified with USDA's online database that instead shows the U.S. exported less than $1 million in beef, beef variety meats and processed beef to China in 2009.[15]

B. Competitive Factors Affecting China's Cattle and Beef Production

According to the Food and Agricultural Organization of the United Nations (FAO) database, the average producer price received for cattle in China was $1,543.13 per tonne (U.S. dollars) in 2007, which is the latest available data.[16] In contrast, the average producer price received for cattle in Brazil in 2007 was much less ($998.17 per tonne (U.S. dollars)), and the average producer price received for cattle in the U.S. was $1,543.13 per tonne (U.S. dollars), which was $438.87 per tonne (U.S. dollars) higher than in China. Thus, from a macro perspective, it would appear that Brazil would have a comparative economic advantage in the Chinese market (i.e., the value of Brazilian cattle, and presumably Brazil's production costs, are comparatively less than in China) and Brazil would expect to receive a higher price for products derived from cattle in the Chinese market compared to what they receive in their domestic market. The U.S., however, does not appear to share this comparative economic advantage as the average value of U.S. cattle, hence the average value of products derived from U.S. cattle, is considerably higher in the U.S. market when compared to the Chinese market.

[15] *See* Global Agricultural Trade System Online, U.S. Department of Agriculture, Foreign Agricultural Service (Includes the following six-digit HS codes: 020110, 020120, 020130, 020210, 020220, 020230, 020610, 020621, 020622, 020629, 021020, and 160250.), available at http://www.fas.usda.gov/gats/default.aspx.
[16] *See* FAOSTAT Database, Prices, Food and Agriculture Organization of the United Nations, available at http://faostat.fao.org.

Data from FAO support the presumption that beef command a lesser price in China than it does in the U.S. as, again, 2007 data show the producer price of cattle meat in China is $3,429.18 per tonne (U.S. dollars) while the producer price of cattle meat in the U.S. is $3,811.50 per tonne (U.S. dollars), which is $382.32 per tonne (U.S. dollars) higher. As with producer prices for cattle, Brazil appears to have the comparative advantage in the Chinese market because, unlike the U.S., Brazilian beef likely would command a higher price in China than in Brazil's domestic market, where the producer price of cattle meat is only $2,037.07 per tonne (U.S. dollars). Therefore, the United States' challenge in the Chinese market would be to effectively promote the non-price attributes of U.S. beef and encourage Chinese consumers to pay significantly more for U.S. beef than they currently pay for their own beef, or for beef imported from Brazil and other low-cost producing countries. If Chinese consumers were unwilling to not only consume more, but also, pay more for U.S. beef, the economic feasibility of exporting beef to China likely would be limited to relatively small, niche markets.

According to a research article published in a 1996 edition of the *Journal of Range Management*, China is blessed with "one of the largest grassland and pastoral areas of the world."[17] This factor alone suggests that China has the potential to significantly increase domestic beef production should the Chinese government decide to do so. The beef production increase realized in Brazil since 1990 exemplifies how an emerging developing country with vast grasslands like China can, in a relatively short period of time, greatly expand its domestic beef production. From 1990 to 2008, Brazil more than doubled its domestic beef production, which

[17] Feasibility Analysis for Development of Northern China's Beef Industry and Grazing Lands, James R. Simpson and Ou Li, Journal of Range Management, Vol. 49, No. 6 (Nov., 1996), pp. 560-564, at 560.

increased during that period from just over 4 million tonnes to over 9 million tonnes.[18] With production at 5.8 million tonnes in 2008,[19] China's beef production is comparable to where Brazil was less than 20 years ago, and it is not beyond the realm of possibilities that China could, at any time, decide to take steps to significantly increase its domestic beef production. Some analysts cite China's ongoing foot-and-mouth disease (FMD) outbreaks as a factor limiting increased beef production in China.[20] However, Brazil also is affected by FMD, having experienced outbreaks since before 1993 that continued through 2000-2001 and 2005-2006.[21] Thus, Brazil has clearly demonstrated that FMD is *not* a factor that would inhibit relatively rapid expansion of a country's beef production should such a goal be established.

During the past decade, China has signaled its intent to increase its domestic beef production, which it could do by emulating cattle production and beef processing practices in the United States, Australia, Brazil, or other major beef producing country. As discussed more thoroughly below, China's currency policy could facilitate this transformation by subsidizing exports and deterring imports of beef, just as it has already done for corn, apples and apple concentrate, and countless other products.

In 2001, China began a $200 million development project (backed by the World Bank) to build an infrastructure of feedlots and slaughterhouses and give assistance to small-scale cattle

[18] *See* FAOSTAT Database, Production, Food and Agriculture Organization of the United Nations, available at http://faostat.fao.org.
[19] *See id*.
[20] *See* GAIN Report China-Peoples Republic of, Livestock and Products Annual, U.S. Department of Agriculture, Foreign Agricultural Service, No. CH9069, September 14, 2009.
[21] *See* APHIS Evaluation of the Status of the Brazilian State of Santa Catarina Regarding Foot-and-Mouth Disease, Classical Swine Fever, Swine Vesicular Disease, and African Swine Fever, U.S. Department of Agriculture, Animal and Plant Health Inspection Service, Veterinary Services, January 16, 2009, at 10.

producers in east-central China to build a competitive beef production industry in the region.[22] In 2003, China initiated a national strategic 'Beef Advantageous Development Area Program' that was intended to shift their marketing focus to higher quality beef production.[23]

In a more recent USDA Foreign Agricultural Service (FAS) report, the agency predicted that 2009 beef consumption was expected to fall in China due to the high price of beef compared to other meats.[24] The FAS report also indicated that beef production, likewise, was expected to decrease due to shrinking profits for Chinese cattle producers. The currency-devalued price of fed cattle in China in 2008 was approximately RMB 6,615 ($965.70 U.S.), and production costs were estimated at RMB 6,340 ($880.50 U.S.), which, according to the report, resulted in a per head profit of about $40 for Chinese cattle producers.[25] In comparison, the 2008 average market price for fed cattle in the U.S. was $1,162.63 per head[26] and the cost of production for U.S. cattle feeders was approximately $1,315.5 per head,[27] representing a per head loss to U.S. cattle feeders of approximately $153 per head that year.

China's current intentions regarding beef production expansion are difficult to gauge. Recent USDA reports indicate that in response to a declining beef herd, the Chinese government reportedly issued a subsidy to increase local beef supplies and improve herd quality, but these

[22] *See* Subsidies Enforcement Annual Report to the Congress, Joint Report of the Office of the U.S. Trade Representative and the U.S. Department of Congress, February 2001.
[23] *See* Subsidies Enforcement Annual Report to the Congress, Joint Report of the Office of the U.S. Trade Representative and the U.S. Department of Congress, February 2004, at 41.
[24] *See* China, Peoples Republic of, Livestock and Products, Semi-Annual Report, 2009, GAIN Report No. CH9017 (March 9, 2009) available at http://www.fas.usda.gov/gainfiles/200903/146327423.pdf.
[25] *See id.* (Note, however, that while the GAIN report estimates the profit at $40.00 per head, the numbers provided in the report to calculate production costs indicate the profit is about $85.00 per head.), available at http://www.fas.usda.gov/gainfiles/200903/146327423.pdf.
[26] *See* Choice Beef Values and Price Spreads and the All-Fresh Retail Value, USDA ERS (Estimate is based on the average 5 market steer price in 2008 and a 1,250 pound steer.), available at http://www.ers.usda.gov/Data/meatpricespreads/.
[27] *See* High Plains Cattle Feeding Simulator, USDA ERS (Estimate is based on the average monthly cost of producing a fed animal in 2008).

measures are considered too moderate by the USDA to stem the current decline of the Chinese cattle herd.[28]

USDA also reports that a subsidy of $73 dollars per head has been put in place to assist the Chinese dairy industry in rebuilding herd numbers after the September 2008 melamine crisis. This crisis resulted in the loss of one million dairy cows, which are expected to be replenished through imports from Australia and New Zealand due to a moratorium on North American cattle for fear of BSE.[29] Subsidies also have been awarded to return grazing land to grassland and it is expected that China is promoting rotational grazing and working to develop the capability to raise livestock in pens and sheds.[30]

C. Principal Measures Affecting China's Imports of Beef and Other Products Derived from Cattle

1. China's Sanitary and Phytosanitary Measures

China imposed a ban on U.S. beef and offal exports following the detection of an imported, Canadian-born BSE-positive cow in the United States in December 2003.[31] In 2006, China first offered to accept U.S. boneless beef from cattle less than 31 months of age; and, later in 2007, it offered to accept both boneless beef and bone-in beef from cattle less than 31 months

[28] *See* GAIN Report China - Peoples Republic of, Livestock and Products Semi-Annual, U.S. Department of Agriculture, Foreign Agricultural Service, No. CH10009, March 2, 2010.
[29] *See* GAIN Report China-Peoples Republic of, Livestock and Products Annual, U.S. Department of Agriculture, Foreign Agricultural Service, No. CH9069, September 14, 2009.
[30] *See* GAIN Report China-Peoples Republic of, 2010 Agriculture Policy Directive U.S. Department of Agriculture, Foreign Agricultural Service, No. 10004, February 18, 2010.
[31] *See* 2009 Report to Congress on China's WTO Compliance, United States Trade Representative, December 2009, at 76.

of age.[32] The U.S., however, rejected China's offer because it believed China should comply with the applicable World Organization for Animal Health (OIE) guidelines that contain no age restriction.[33] The United States refusal to accept China's offer for a partial reopening of its market to U.S. beef is indefensible.

First, it is indefensible because the U.S. believes the closure of the Chinese market cost the U.S. beef industry over $100 million from 2004-2007.[34] If this is true, then the United States has exacerbated the harm to the U.S. beef industry by depriving it of the opportunity to mitigate its losses by regaining at least partial access to the Chinese market. Second, it is indefensible because the U.S. believes that increased exports are paramount to the revitalization of Rural America. Depriving the U.S. beef industry an export market opportunity, albeit limited, would nevertheless constitute a subversion of the goal to stimulate rural economies.[35] Third, it is indefensible because no other significant beef importing country, including major U.S. beef export markets, are willing to assume the risk of introducing the incurable and invariable fatal BSE-agent that is associated with the OIE's woefully inadequate guidelines – except, that is, the United States.

The United States maintains among the weakest BSE standards with respect to Canada, a country with ongoing outbreaks of BSE, when compared to all other major beef importing

[32] *See* 2009 Report to Congress on China's WTO Compliance, United States Trade Representative, December 2009, at 76.
[33] *Ibid*.
[34] *See* Effects of Animal Health, Sanitary, Food Safety, and Other Measures on U.S. Beef Exports, U.S. International Trade Commission, Sept. 2008, at 8-1.
[35] *See* Obama Administration Hosts National Rural Summit on Rebuilding and Revitalizing Rural America, U.S. Department of Agriculture, Release No. 0297.10, June 3, 2010 (Agriculture Secretary Tom Vilsack "continued to outline the framework for building a strong, revitalized rural economy for the 21st Century, which includes. . . Strengthening farm income by increasing agricultural exports. . .").

countries; and the entire world, including China, knows it. Even the European Union refuses to accept the heightened risk of BSE introduction that the U.S. assumes by allowing the importation of Canadian cattle that are older than the multiple BSE-positive cattle that have been detected in Canada. The European Union e.g., prohibits the importation of Canadian cattle born before the date of Canada's last indigenous BSE case,[36] while the United States freely allows the importation of cattle born well before the date when multiple BSE-infected cattle were born.[37] In addition, and as shown in Chart 6 and Chart 7 below, the countries of Japan, South Korea, Mexico, Hong Kong, Taiwan, Vietnam, Russia, United Arab Emirates, and Singapore all have only partially reopened their markets to U.S. beef and all impose a restriction against the importation of beef from cattle over 30 months of age (Japan allows only beef from cattle 20 months of age or younger).[38] Moreover, several of these export markets continue to either disallow exports of beef derived from Canadian cattle or they impose additional restrictions on beef from Canadian cattle.[39] And, as shown in Chart 8 below, numerous markets open to the U.S. remain closed to Canada due to that countries ongoing BSE outbreaks.[40]

[36] *See* Canadian Food Inspection Agency Export Program, Veterinary Health Certificates, Bovine, available at http://www.inspection.gc.ca/english/animal/heasan/export/bovine/bovine.shtml.
[37] The February 25, 2010, case of BSE detected in Canada was the eleventh BSE-positive animal eligible to be exported to the United States under the United States relaxed BSE age requirement scheme.
[38] *See* Effects of Animal Health, Sanitary, Food Safety, and Other Measures on U.S. Beef Exports, U.S. International Trade Commission, Sept. 2008, at 4-9; *see also* Index of Export Requirements for Meat and Poultry Products, U.S. Department of Agriculture, Food Safety and Inspection Service, accessed Dec. 14, 2009.
[39] *See* Index of Export Requirements for Meat and Poultry Products, U.S. Department of Agriculture, Food Safety and Inspection Service, accessed Dec. 14, 2009 (South Korea, Taiwan, and Singapore, e.g., either ban or restrict U.S. exports of beef derived from Canadian cattle.).
[40] *See* Index of Export Requirements for Meat and Poultry Products, U.S. Department of Agriculture, Food Safety and Inspection Service, accessed Dec. 14, 2009; see also Summary of the Situation with Foreign Markets Relative to BSE as of February 17, 2009 (latest available information when accessed on Dec. 14, 2009), Canadian Food Inspection Agency, available at http://www.inspection.gc.ca/english/fssa/meavia/man/ch11/annexre.shtml.

CHART 6

U.S. Has Weak BSE Import Standards for Beef

BSE STANDARDS OF MAJOR BEEF IMPORTING COUNTRIES

Country	Age Restriction	Specified Risk Material (SRM) Definition	Commodity Restrictions
Japan	20 months or younger	Head (excluding tongue and cheek meat), palatine and lingual tonsils, spinal cord and dura matter, distal ileum, vertebral column, and dorsal root ganglia.	No ground beef, processed beef, head meat, finely textured beef, or mechanically separated meat.
Korea	Under 30 months	Skull, brain, eyes, distal ileum, tonsils, spinal cord, vertebral column.	Cattle must be born and raised in the United States, or imported from a country deemed eligible by the Korean government to export beef or beef products to Korea, or raised in the United States for at least 100 days. Traceback records must be maintained for at least 2 years. No mechanically recovered meat or mechanically separated meat.
Mexico	Under 30 months	Skull, brain, eyes, tonsils, spinal cord, and small intestine.	No ground meat, feet, sweetbreads, weasand meat, or head meat.
Hong Kong	Under 30 months	Skull (including brain, eyes and trigeminal ganglia), tonsils, spinal cord, dorsal root ganglia (with the vertebral column) and intestine.	No ground beef. No bone-in beef, edible offal, or beef derived from advanced meat recovery systems.

Source: USITC Publication 4033, September 2008, 4-9.

CHART 7

BSE STANDARDS FOR ADDITIONAL TOP BEEF IMPORTING COUNTRIES

Country	Age Restriction	Specified Risk Material (SRM) Definition	Commodity Restrictions
Taiwan	Under 30 months	If slaughtered before Nov. 1, 2009: brain, skull, eyes, trigeminal ganglia, spinal cord, vertebral column (excluding the vertebrae of the tail, the transverse processes of the thoracic and lumbar vertebrae, and the wings of the sacrum), dorsal root ganglia, the tonsils and the distal ileum of the small intestine. FSIS regulations apply after Nov. 1, 2009.	Cattle must be born and raised in the United States, raised in the United States for at least 100 days prior to slaughter, or legally imported into the United States from a country deemed eligible by Taiwan to export deboned beef to Taiwan. Beef or beef products of cattle from Canada fed less than 100 days prior to slaughter in the United States is limited to deboned beef derived from animals less than 30 months of age.
Vietnam	Under 30 months	Brain, skull, eyes, trigeminal ganglia, spinal cord, vertebral column (excluding the vertebrae of the tail, the transverse processes of the thoracic and lumbar vertebrae, and the wings of the sacrum) and dorsal root ganglia and the tonsils and distal ileum of the small intestine of any cattle regardless of age.	The meat does not contain advanced recovery meat or mechanically separated meat.
Russia	Under 30 months	Brain, spinal cord, eyes, skull, and vertebral column regardless of the age of the animal.	The beef and beef byproducts must be derived from cattle raised in the United States. Ground red meat, packaged in bulk form or in the form of meat patties, is prohibited.
United Arab Emirates	Under 30 months		Ritual: Islamic Halal Slaughter requirements apply.
Singapore	Under 30 months	Tonsils, distal ileum, brains, eyes, spinal cord, skull and vertebral column must be cleanly removed from products shipped to Singapore without contamination of the meat.	Only Fresh/frozen boneless beef derived from animals less than 30 months of age is eligible. Beef derived from cattle imported from Canada is not eligible.

Source: USDA, FSIS, Index of Export Requirements for Meat and Poultry Products, undated, (accessed Dec. 14, 2009).

CHART 8

U.S. EXPORT MARKETS CLOSED TO CANADIAN BEEF

The following 13 countries accept U.S. beef exports; but, according to information provided by the Canadian Food Inspection Agency, these countries continue to ban Canadian beef:

Chile
Colombia
Dominican Republic
Haiti
Jamaica
Jordan
South Korea
Kuwait
Malaysia
Peru
Saint Lucia
Singapore
Ukraine

Sources: USDA, FSIS, Index of Export Requirements for Meat and Poultry Products, undated, (accessed Dec. 14, 2009); Canadian Food Inspection Agency, Summary of the Situation with Foreign Markets relative to BSE as of February 17, 2009 (latest available information), available at http://www.inspection.gc.ca/english/fssa/meavia/man/ch11/annexre.shtml.

It is entirely indefensible for the United States to demand that China comply with the very OIE guidelines that are deemed woefully inadequate by much, if not most, of the world to prevent the introduction and spread of BSE.

China and the rest of the world also know that there is evidence of continued, frequent violations of BSE mitigation measures in the U.S., as evidenced by the numerous recalls by the United States Food Safety and Inspection Service (FSIS). From April 2008 through January 2010, the U.S. recalled nearly 144.5 million pounds of beef that entered the U.S. food system and involved firms operating in at least 10 separate states, all in violation of U.S. BSE mitigation requirements. These recalls undercut USDA's assertion that BSE risk pathways to humans associated with the importation of older Canadian cattle and beef from older Canadian cattle

have been effectively alleviated in the United States.[41] Moreover, USDA's own risk modeling for its current BSE regulations that allow the importation into the U.S. of older Canadian cattle and beef from older Canadian cattle, which harbor a higher-risk for BSE, predicted that, based even on overly optimistic assumptions, the U.S. would import between 19 to 105 BSE-infected cattle, which would subsequently produce BSE infections in 2 to 75 U.S.-born cattle, over a 20-year period.[42] It is unconscionable that the U.S. would demand that China, or any other country, expose its citizens to the heightened level of risk that the U.S. has chosen to impose on its citizens by maintaining lax import restrictions on Canadian beef and cattle.

It is equally indefensible for the United States to continue prohibiting U.S. beef packers from voluntarily testing for BSE. Allowing such voluntary testing likely would assist in the restoration of consumer confidence in U.S. beef, both here and abroad.

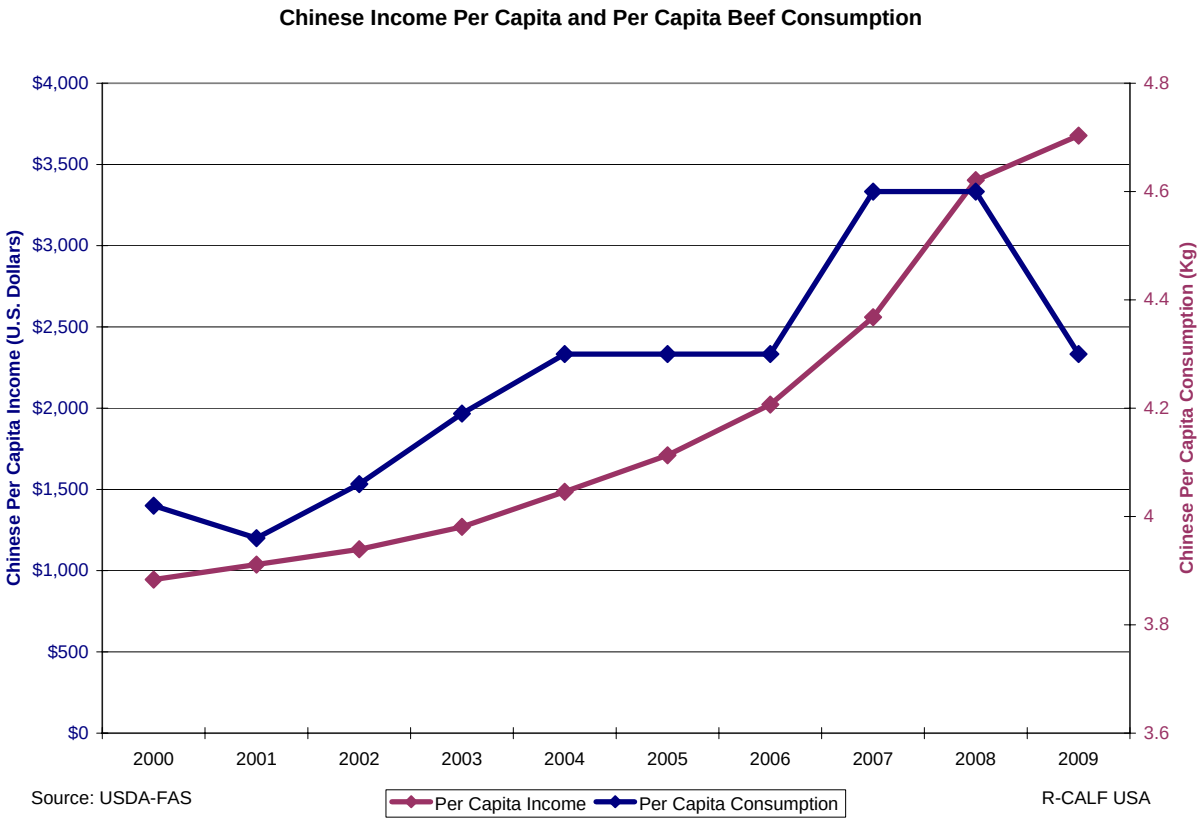
2. China's Income Growth In Relation to Its Per Capita Beef Consumption

Although China's per capita income has steadily increased over the past decade, suggesting that Chinese consumers may soon have sufficient income to afford purchases of higher priced beef, Chart 9 below shows that per capita beef consumption in China has not steadily increased over the same period, and the 10-year trend in per capita beef consumption in China is characterized by fits and starts. Over the past 10 years, while per capita income experienced uninterrupted year-to-year growth, per capita beef consumption in China experienced four years of year-to-year increases, three years of year-to-year decreases, and three

[41] *See* Current Recalls & Alerts, USDA Food Safety and Inspection Service, available at http://www.fsis.usda.gov/Fsis_Recalls/Open_Federal_Cases/index.asp; *see also id*., Recall Case Archive 2008-2010.
[42] *See* 72 Fed. Reg., 1109, col. 2; 72 Fed. Reg., 53347, col. 1.

years of year-to-year stagnation. Thus, factors other than income appear to have significant influence over Chinese beef consumption patterns.

CHART 9



3. China's Currency Policy

China is viewed by many in the U.S. as a potential customer for U.S. beef, but the distortion created by China's undervaluation of its currency likely would price U.S. beef beyond the reach of even China's middle-income population. In 2009, the U.S. cattle producer received

less than 43 percent of the value of Choice beef sold at retail.[43] Thus, in order for U.S. cattle producers to at least maintain the economic returns realized in 2009 (note that as shown in the attached Appendix, in 2009 the U.S. cattle producer received the smallest share of the consumer's beef dollar in 30 years), they would need to continue receiving approximately $1.81 per pound retail weight from each carcass that actually sold at retail for $4.26 per pound in 2009.[44] However, with an estimated per-capita income of only $6,500 in 2009 U.S. dollars,[45] the Chinese population is not likely to consume significant volumes of U.S. beef at the price U.S. cattle producers must receive to maintain economic par with 2009 (i.e., $1.81 per pound retail weight), let alone at the average 2009 retail price of $4.26 per pound, which *is* the retail price necessary for U.S. cattle farmers and ranchers to maintain the economic returns realized in 2009 under the current structures of the U.S. cattle and beef industries.

China's currency undervaluation is an effective tariff on U.S. beef exports. When China's undervalued currency is factored into the consideration of China as a potential market for U.S. beef, the prospect of exporting beef to China at prices necessary to sustain the U.S. cattle industry at even the 2009 economic level (albeit a level that is insufficient to reverse the ongoing contraction of the domestic cattle industry) is dismal. China's currency is undervalued between 30 and 50 percent. [46] The effect is that the $4.26 per pound Choice beef price in the U.S. (which, again, is the price necessary to sustain the economic condition of U.S. cattle producers at the 2009 level) becomes anywhere from $5.54 per pound to $6.39 per pound when sold to Chinese

[43] *See* Choice Beef Values and Price Spreads and the All-Fresh Retail Value, USDA ERS, available at http://www.ers.usda.gov/Data/meatpricespreads/.
[44] *See id*. (These values reflect the 2009 average Choice beef retail value (retail beef price) and the 2009 average net farm value (the average price paid to U.S. cattle producers based on the retail beef price.).
[45] *See* The World Factbook: China, U.S. Central Intelligence Agency, available at https://www.cia.gov/library/publications/the-world-factbook/geos/ch.html.
[46] *See* Hearing Advisory, Web Site of Committee on Ways & Means, available at http://waysandmeans.house.gov/press/PRArticle.aspx?NewsID=11060.

buyers because of the currency tariff. The effect is to price U.S. beef beyond the reach of the Chinese population, which already has limited purchasing power in a country that produces more beef than it consumes.

Should China increase its domestic beef production and/or begin exporting beef to the U.S. while its currency undervaluation remains unaddressed, the likely effect would be an accelerated contraction of the U.S. cattle industry. China's currency undervaluation alone would enable it to sell beef in the U.S. market for 30-50 percent less than the value of domestic beef, not to mention the effect on the price of beef due to other internal government subsidies that may significantly lower the market price of Chinese beef.

The adverse effects of China's undervalued currency become more apparent to the U.S. cattle industry when costs and prices for live cattle are considered. For example, using the 2008 production costs and prices for fed cattle discussed above, a hypothetical Chinese fed steer sold in the U.S. market would net the Chinese producer about $282 per head (U.S. price of $1,162.63 less Chinese production cost of $880.50). Thus, with China's subsidized currency, a hypothetical Chinese steer sold in the 2008 U.S. market would have given China a $435 per head advantage over U.S. cattle producers whom sold cattle in the U.S. that year (calculated by adding China's $282 profit to the United States' $153 per head loss).

The introduction of increased supplies of lower-cost beef resulting from China's undervalued currency would have a tremendous, negative impact on the viability of the U.S. cattle industry that is extremely price-sensitive to increased supplies due to the industry's farm

elasticity of demand. The USITC had previously determined that the farm level elasticity of demand for slaughter cattle is such that "each 1 percent increase in fed cattle numbers would be expected to decrease fed cattle prices by 2 percent."[47] By extension, increases in the supply of beef that is derived from fed cattle likewise would be expected to depress fed cattle prices in the same manner.

III. IMPORTANT CONSIDERATIONS REGARDING INCREASED TRADE WITH CHINA

As is more thoroughly described in the attached Appendix, the current structure of the U.S. cattle and beef market does not, in any way, ensure that any benefits derived from increased beef exports to China would translate into increased prices for U.S. cattle producers. To substantiate this claim, R-CALF USA offers that in 2007 the U.S. imported 851,477 cattle from Canada and Mexico for slaughter.[48] Based on the average carcass weight of 776 pounds in 2007, those foreign cattle imported for slaughter in the U.S. roughly produced over 600 million pounds, or 272,000 metric tons, of beef. Based on the average all-fresh beef price in 2007 of 377.4 cents per pound,[49] the total value of the beef derived from those imported cattle was about $2 billion. This amount and value of beef far exceeds the pre-BSE volume of U.S. beef exports

[47] 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.
[48] *See* Livestock and Meat Trade Data, Cattle: Annual and cumulative year-to-date U.S. trade (head), U.S. Department of Agriculture, Economic Research Service, available at http://www.ers.usda.gov/data/meattrade/CattleYearly.htm.
[49] *See* Beef Values and Price Spreads, Meat Price Spreads, U.S. Department of Agriculture, Economic Research Service, available at http://www.ers.usda.gov/Data/meatpricespreads/.

to China, which consisted of 11,651 metric tons of beef valued at $27.4 million.[50] Thus, in 2007 U.S. beef packers could have exported 20 times more beef to China than they exported in 2003 using only beef derived from cattle they imported for immediate slaughter, without a single dime being paid to U.S. cattle producers. This is because the U.S. cattle industry does not add any value to cattle imported for slaughter in the U.S. and, nevertheless, the resulting beef from imported cattle is designated as having a U.S. origin for export purposes.[51] Clearly, U.S. beef packers were accorded a significant and unjust trade advantage over the U.S. cattle industry when U.S. trade negotiators adopted the current rule of origin now in place for international trade purposes.

The likely argument against R-CALF USA's assertion that beef packers can exploit foreign export markets by procuring beef for export from imported cattle, without the risk that at least some of the benefits would be allocated to U.S. cattle producers in the form of higher cattle prices, is that by deflecting some of the beef produced in U.S. slaughtering plants (i.e., the beef derived from imported cattle) to export markets, U.S. cattle producers would benefit indirectly because beef derived from their cattle could then be sold in the domestic market without having to compete with beef derived from imported cattle. Such an argument, however, cannot stand against the 20-year history of the U.S. cattle industry that shows: 1) the value of U.S. imports of beef, cattle, and processed beef exceeded the value of U.S. exports of these products in each year except one during the past 20 years (Chart 10); 2) the value of U.S. imports of beef, cattle, processed beef and beef variety meat (offal) exceeded the value of U.S. exports of these products

[50] *See* Effects of Animal Health, Sanitary, Food Safety, and Other Measures on U.S. Beef Exports, U.S. International Trade Commission, Sept. 2008, at 8-9.
[51] *See* 73 Fed. Reg., 45116, col. 2 ("Substantial Transformation," e.g., the point of slaughter, is the underlying basis for determining the country of origin under the World Trade Organization's Rules of Origin.).

in 14 of the past 20 years (Chart 11); 4) The U.S. cattle industry suffered severely depressed prices during the period when export volumes were the highest in history, which also was the same period when the U.S. experienced a positive value-based trade balance in the trade of beef, cattle, beef variety meat and processed beef (Chart 12 contrasted with Chart 11); and, 5) the share of the United States' total available beef supply that is represented by imports has increased steadily from approximately 10 percent in 1985, to approximately 13 percent in 1996 (when export volumes were reaching new record highs and when the U.S. enjoyed the most favorable value-based trade balance in the last 20 years of our industry's history), to approximately 17 percent in 2009 (when exports had rebounded significantly from their low in 2004) (Chart 13).

CHART 10

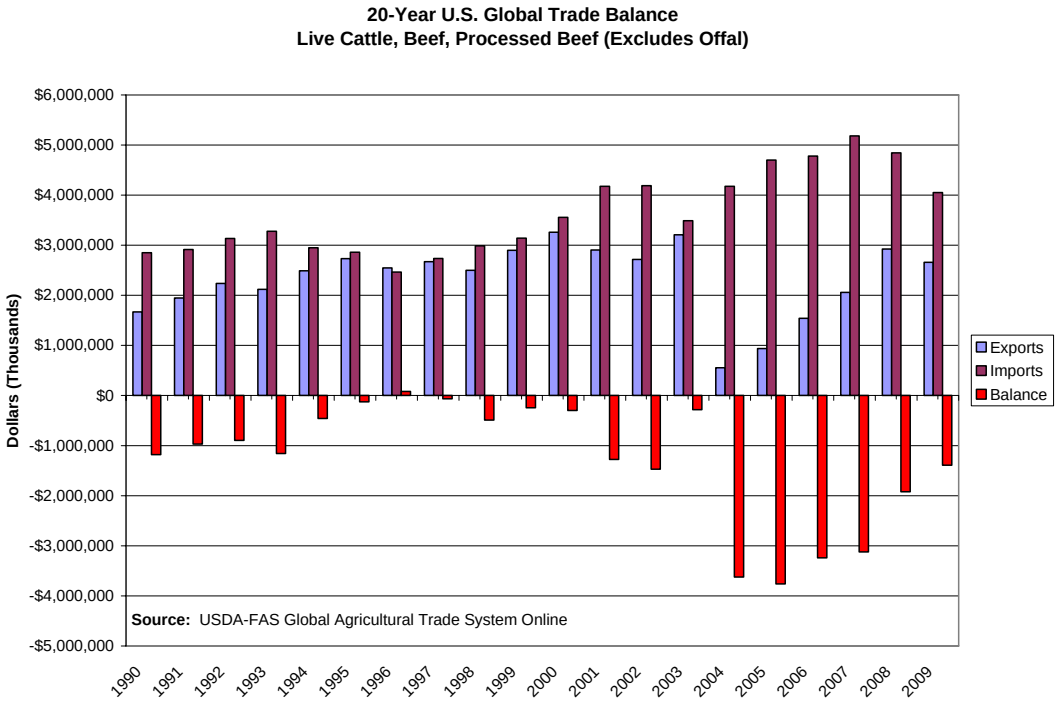


CHART 11

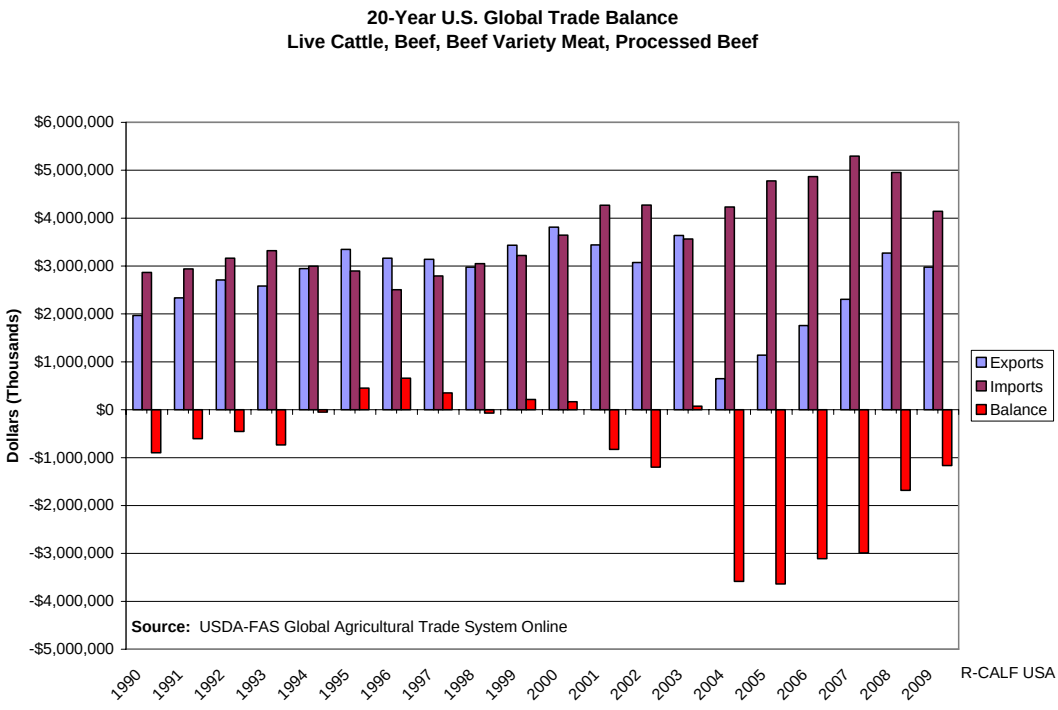


CHART 12

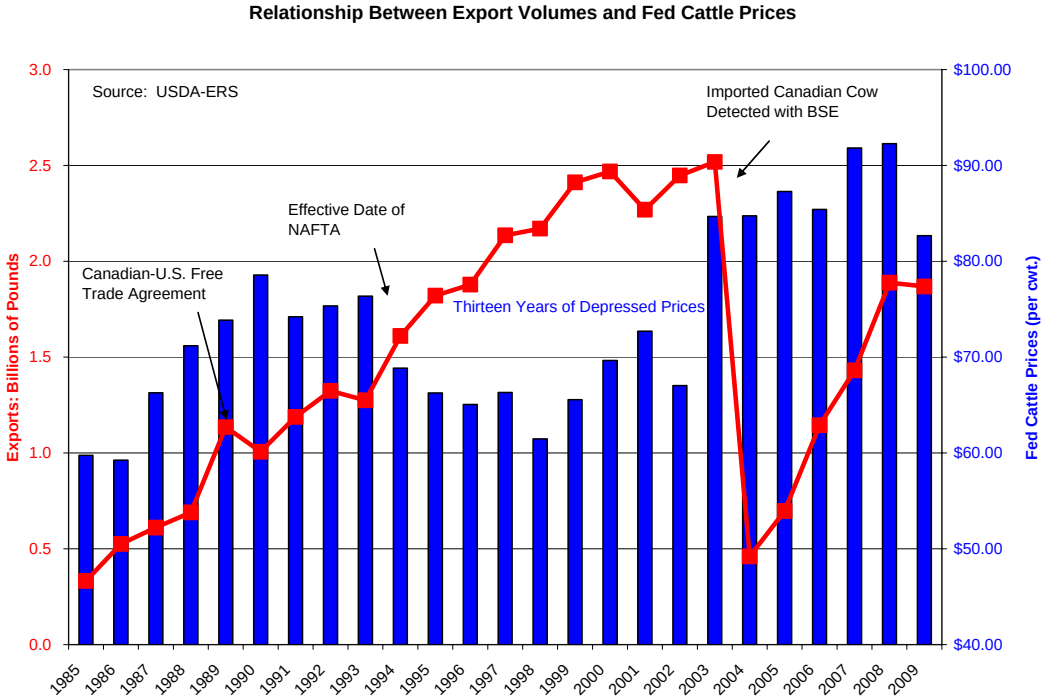
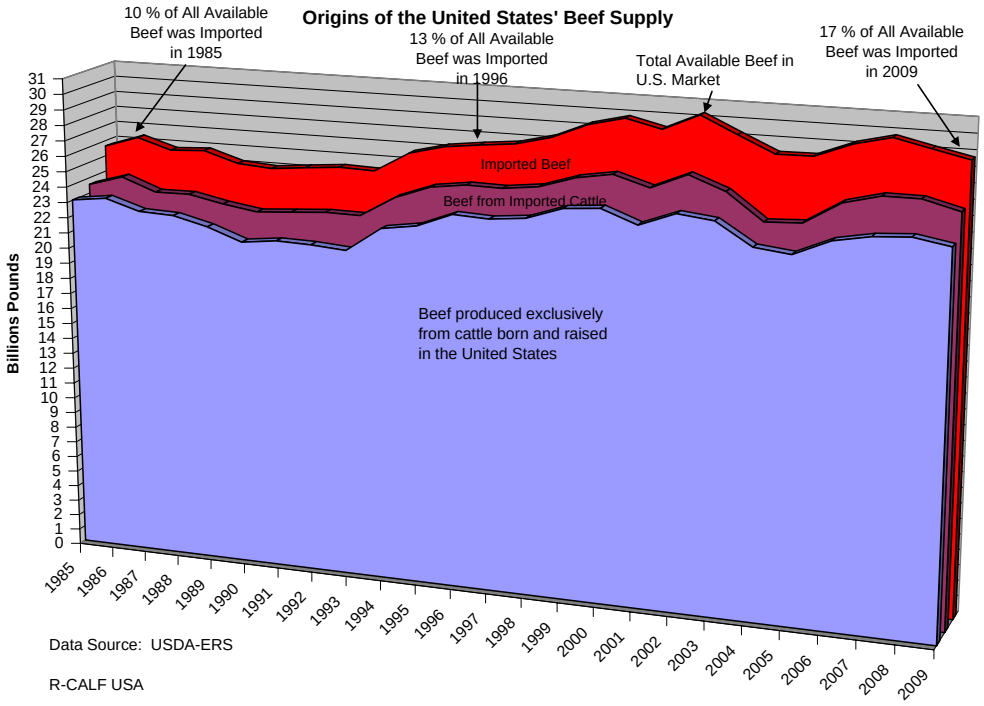


CHART 13



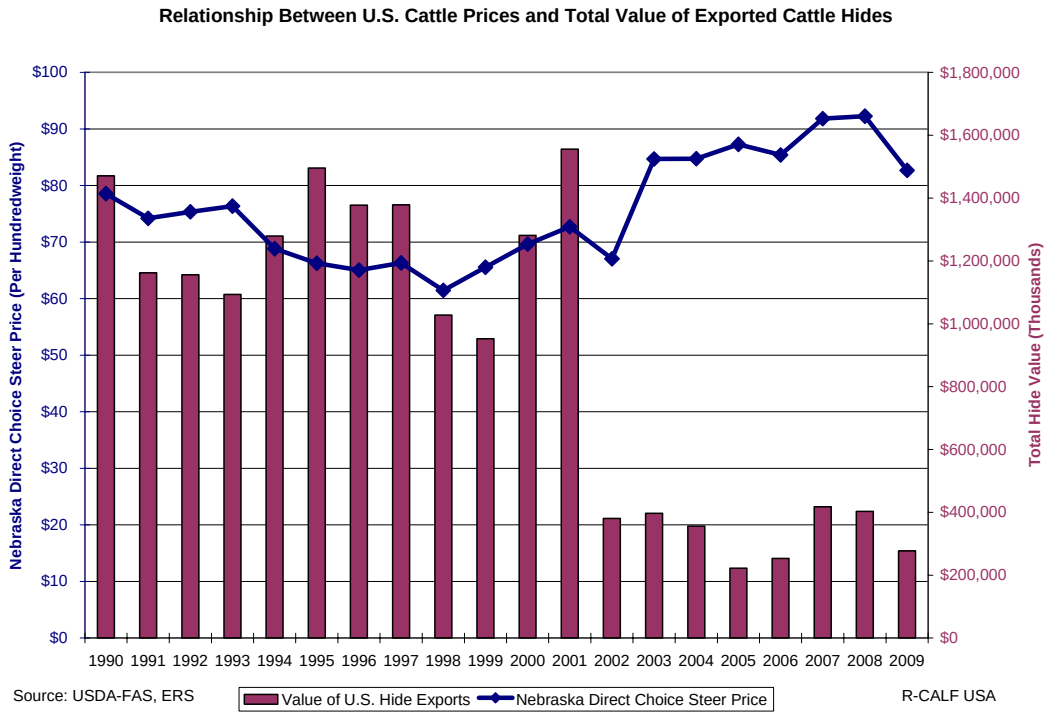
History shows that increased beef exports not only fail to translate into higher domestic cattle prices, but also, domestic cattle prices fell and remained severely depressed during the period when U.S. exports were rapidly increasing and reaching new record highs (1994-2003). Thus, history shows that today's focus on increased exports as a means of revitalizing the U.S. cattle industry is the wrong approach. Until and unless the forces described in the attached Appendix that continue to contract the U.S. cattle industry are addressed, increased exports will serve primarily to benefit the highly concentrated beef packers that are contributing to the ongoing contraction of the U.S. cattle industry.

The beneficiaries of increased beef exports, principally the beef packers, make glowing claims regarding how the demand and price of cattle byproducts, e.g., offal, tongues, and hides,

add significantly to the price beef packers pay for U.S. cattle. These claims are based on the assumption that higher byproduct values are passed to cattle producers in the form of higher cattle prices. Beef industry analyst CattleFax, e.g., recently asserted that 2008 hide values were contributing $5 per cwt to the value of fed cattle: "Had hide and offal values held steady since July, fed cattle trade could have been $92/cwt this week instead of $87/cwt," and CattleFax called this $5 per cwt price a "staggering dollar amount."[52] However, historical data do not support this assertion. Chart 14 below shows the relationship between U.S. fed cattle prices and the total value of hide exports. If it were true that export hide values contributed significantly to the price of fed cattle, one would expect a strong, positive correlation between increased hide prices and increased fed cattle prices. Yet, such a correlation does not exist. Instead, the U.S. cattle producer experienced declining prices when the total value of hide exports increased (e.g., cattle prices experienced year-to-year declines between 93-94, 94-95, and 95-96, while the total value of exported hides experienced year-to-year increases between 93-94 and 94-95). And, the U.S. cattle producer experienced increased cattle prices while the value of hide exports decreased between 91-93 and 98-99. Beginning in 2003, cattle prices reached and sustained historical highs after the value of hide exports had fallen dramatically.[53]

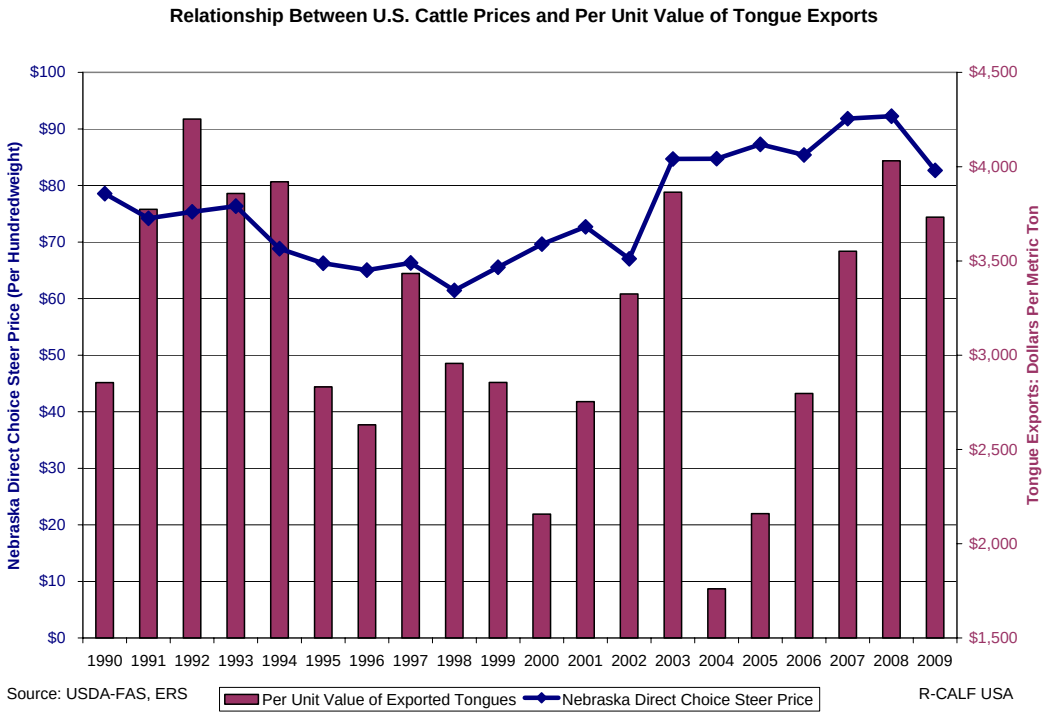
[52] Hide and Offal Values Plummet, CattleFax Insight, Vol. 22 No. 1, Jan/Feb 2009.
[53] See Global Agricultural Trade System Online, U.S. Department of Agriculture, Foreign Agricultural Service (Based on world totals for the following HS-6 digit codes: 410110, 410120, 410121, 410122, 410129, and 410130), available at http://www.fas.usda.gov/gats/default.aspx.

CHART 14



The same lack of correlation also is evident in the beef tongue export market, though beef packers and their allied organizations often cite the benefits to U.S. cattle producers from selling beef tongues for higher prices abroad. As Chart 15 below shows, an inverse relationship between a higher per unit value of exported tongues and U.S. cattle prices exists between years 90-91, 93-94, 98-00, 01-02, and 05-06.

CHART 15



R-CALF USA previously informed the USITC of its concern that for far too long U.S. trade polices have been unduly influenced by the mere rhetoric from beef commodity industry representatives who claim tangible benefits for cattle producers of well over one hundred dollars per head of cattle from increased exports. The National Cattlemen's Beef Association (NCBA), e.g., testified before the USITC in November 2007 that, "In fact, the industry 'rule of thumb' is that U.S. beef exports in 2003 added about $15/cwt or $180 to each and every one of the roughly 27 million steers and heifers marketed that year."[54] The NCBA also asserted that the $15 per cwt added export value to fed cattle translates into a $22.20 per cwt (or $166.50 per head) increase in the value of a 750 pound steer, and an increase of $28.20 per cwt (or $155.10 per head) increase

[54] Memorandum of Record, Investigation No. 332-488, Concerning: Global Beef Trade: Effects of Animal Health, Sanitary, Food Safety, and Other Measures on U.S. Beef Exports, U.S. International Trade Commission, Nov. 15, 2007.

in the value of a 550 pound steer.[55] In addition, The NCBA states, e.g., "Many cuts of beef are underutilized in the U.S. Exporting cuts like liver and short ribs can add between $20-$25 to the price producers receive per head of cattle."[56] Similarly, the U.S. Meat Export Federation states,

> The industry is losing $26 per head without the ability to export liver, intestine, tongue and tripe to most markets. The tongue has lost significant value, dropping from $4.25 per pound in 2003 to 70 cents per pound one year later – a staggering $3.55 per-pound loss.[57]

These beef commodity industry assertions regarding the economic benefits to live cattle producers from exports, including the claim of huge benefits arising from exports at 2003 levels, are unfounded and demonstrably false. As evidenced in Chart 12 above, U.S. beef exports in the years leading up to 2003 were, in fact, comparable to the 2003 level of about 2.5 billion pounds. Export volumes were approximately 2.4 billion pounds in 1999, 2.5 billion pounds in 2000, 2.3 billion pounds in 2001, and 2.5 billion pounds in 2002.[58] Yet, the prices for U.S. fed cattle in the years leading up to 2003 were severely depressed: Per hundredweight Nebraska Direct Choice steer prices were only $67.56 in 1999, $69.65 in 2000, $72.71 in 2001, and $67.04 in 2002.

It is obvious that the "industry" and the "producers" referenced as beneficiaries of increased exports by these beef commodity industry representatives are the beef packers and beef

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[55] *See* Special Report: How do Canadian Beef Imports Affect Our Business? Greg Doud, Chief Economist, NCBA, Issues Update 2004, Trade/Marketing/Economics, May-June 2004, available at https://www.beefusa.org/uDocs/canadian_20beef_20imports_20-_20mayjune_202004.pdf.

[56] Trade: Open Markets and Level Playing Fields, National Cattlemen's Beef Association, available at http://www.beefusa.org/uDocs/tradeleavebehind.pdf.

[57] Variety Meats Vital to Boosting U.S. Beef Exports, Issues Update, Trade/Marketing Economics, Cheryl Kamenski, U.S. Meat Export Federation, March-April 2006, available at http://www.beef.org/uDocs/varietymeatsvitaltoexports.pdf

[58] *See* Beef and veal: Annual and cumulative year-to-date U.S. trade (carcass weight, 1,000 pounds), Data Sets, U.S. Department of Agriculture Economic Research Service, available at http://www.ers.usda.gov/data/meattrade/BeefVealYearly.htm.

exporters who are participants in the beef commodity industry. They are not the participants within the U.S. live cattle industry. The evidence above show that increased values of, and prices for, beef exports and beef byproduct exports do not competitively transfer beyond the demarcation point that separates the highly concentrated beef packing industry from the disaggregated U.S. live cattle industry. It is the highly concentrated beef packers that are engaged in exporting and importing who capture the increased value associated with exports without allowing a competitive allocation of that increased value to cattle producers.

R-CALF USA belabors this point for good reason: For far too long Congress and the Administration have uncritically accepted the false assumption that increased exports of beef and other products derived from cattle benefit the nation's hundreds of thousands of U.S. cattle producers in the form of higher cattle prices. While this assumption should be true, historical data do not support this claim. And, despite the overwhelming evidence to the contrary, Congress and the Administration persist in pursuing increased exports as the quintessential strategy for improving the economic conditions of U.S. cattle farmers and ranchers. Indeed, that is the impetus for this USITC hearing on China's agricultural trade. Those who believe the benefits from increased exports flow to the U.S. cattle industry do not understand the dynamics of the U.S. cattle market under its current, highly concentrated structure. The trade policies currently pursued by Congress and this Administration continue to benefit the highly concentrated U.S. beef packers, at the expense of U.S. cattle farmers and ranchers and consumers.

There is an equally erroneous assumption underlying current trade policies regarding the potential for increased exports to offset the harm arising from rising imports. Empirical evidence

demonstrate that due to the supply sensitive nature of the U.S. cattle industry, and the industry's intrinsic supply inelasticity with respect to demand, the harm arising from increased imports is *not* negated by countervailing export levels. This phenomenon was empirically demonstrated during the extended period when beef demand was increasing from 1998-2002 (Chart 15 below), domestic beef consumption was increasing from 1993-2002 (Chart 16 below), and U.S. exports were increasing to record levels from 1993-2002 (Chart 12 above). Despite such favorable market fundamentals, U.S. cattle prices remained severely depressed and below the cost of production and the U.S. cattle industry contracted rapidly.

CHART 15

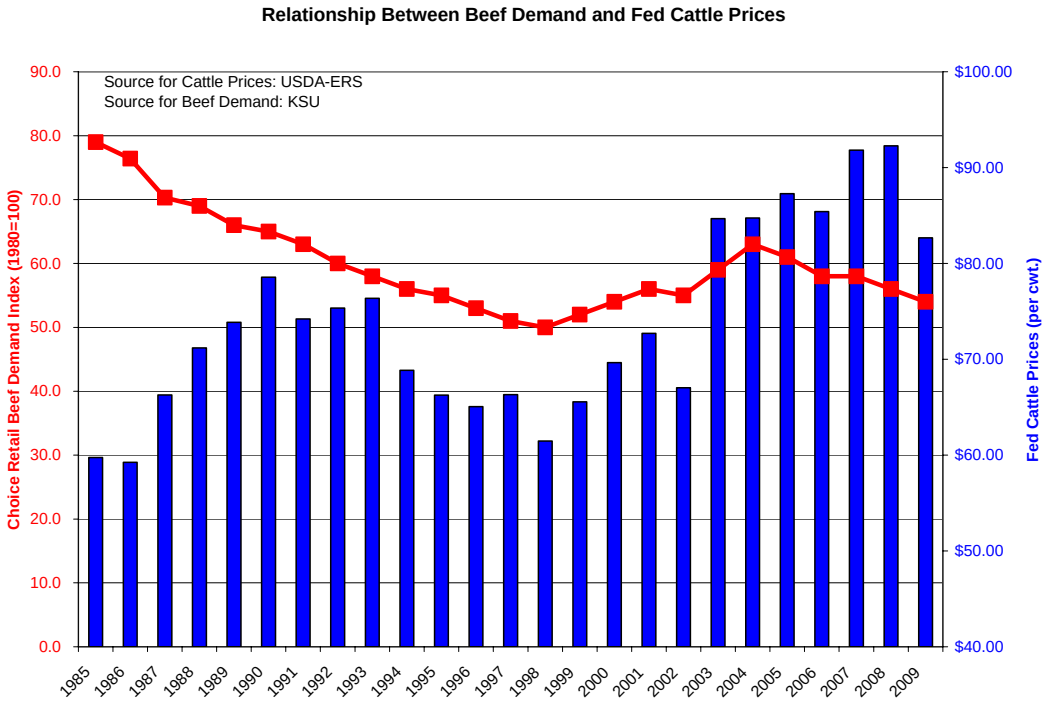
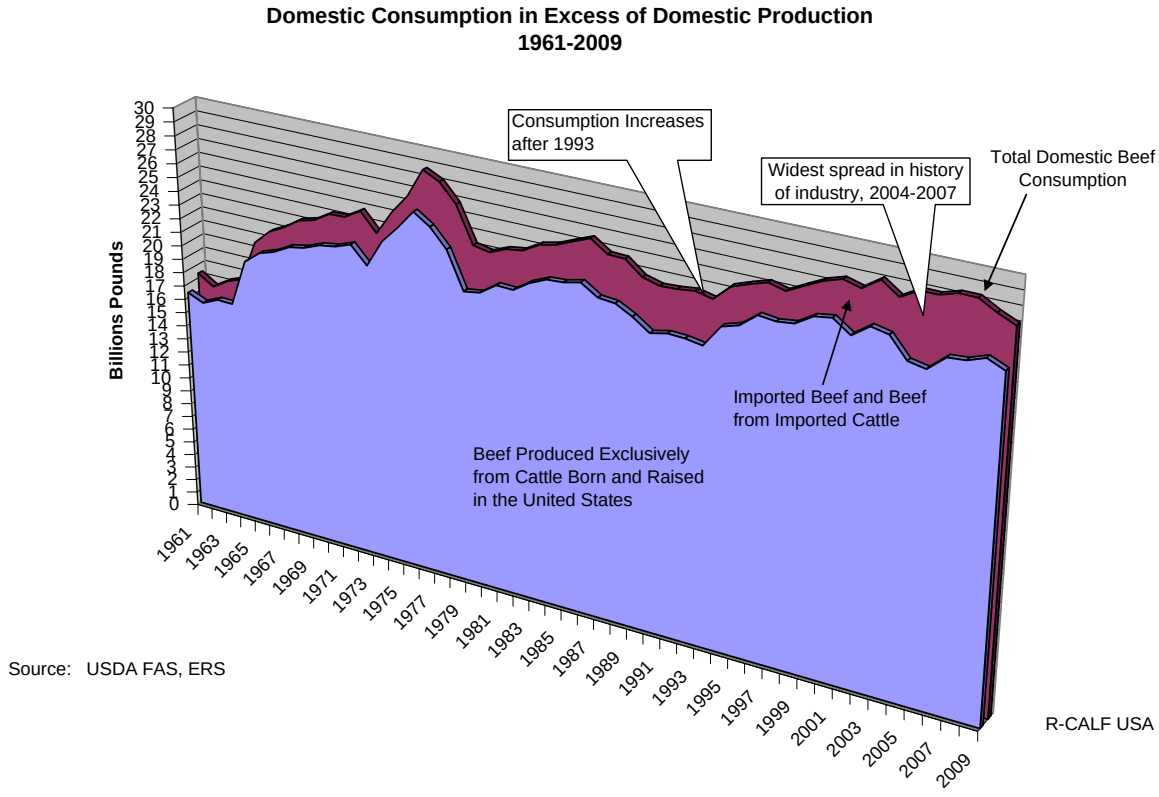


CHART 16



IV. RECOMMENDATIONS AND CONCLUSION

R-CALF USA recommends that the United States work aggressively to: 1) reverse the United State's recently weakened disease import standards for countries with ongoing BSE outbreaks; 2) accept China's 2007 offer to partially lift its current ban on U.S. beef; 3) facilitate the voluntary testing for BSE by private beef packers; 4) revise the current standard of "substantial transformation" used to determine the country of origin for international trade purposes by establishing that the origin for beef and products derived from cattle shall be the country where the animal from which the beef is derived was born, raised, and slaughtered; 5)

thoroughly assess the impacts that current trade policies and trade agreements are having on the profitability and viability of the U.S. live cattle industry and take into account the market concentration and cattle procurement practices in the industry as well as the perishable nature of live cattle and the cyclical nature of the live cattle industry in the assessment; 6) thoroughly investigate and determine why U.S. cattle prices have responded inversely to rising and falling exports; and, 7) neutralize the tariff caused by China's undervalued currency.

R-CALF USA strongly urges USTR to refrain from making any concessions with China that would, in any way, weaken the United States already weakened import standards and restrictions to facilitate the importation into the U.S. of Chinese cattle, beef, or products derived from cattle in return for increased export access in the Chinese market.

R-CALF USA greatly appreciates the opportunity to address this important matter.

Sincerely,

Bill Bullard
CEO

Attachment: Appendix: Under Siege: The U.S. Cattle Industry

Fighting for the U.S. Cattle Producer!
R-CALF USA

R-CALF United Stockgrowers of America
P.O. Box 30715
Billings, MT 59107
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Phone: 406-252-2516
Website: www.r-calfusa.com
E-mail: r-calfusa@r-calfusa.com

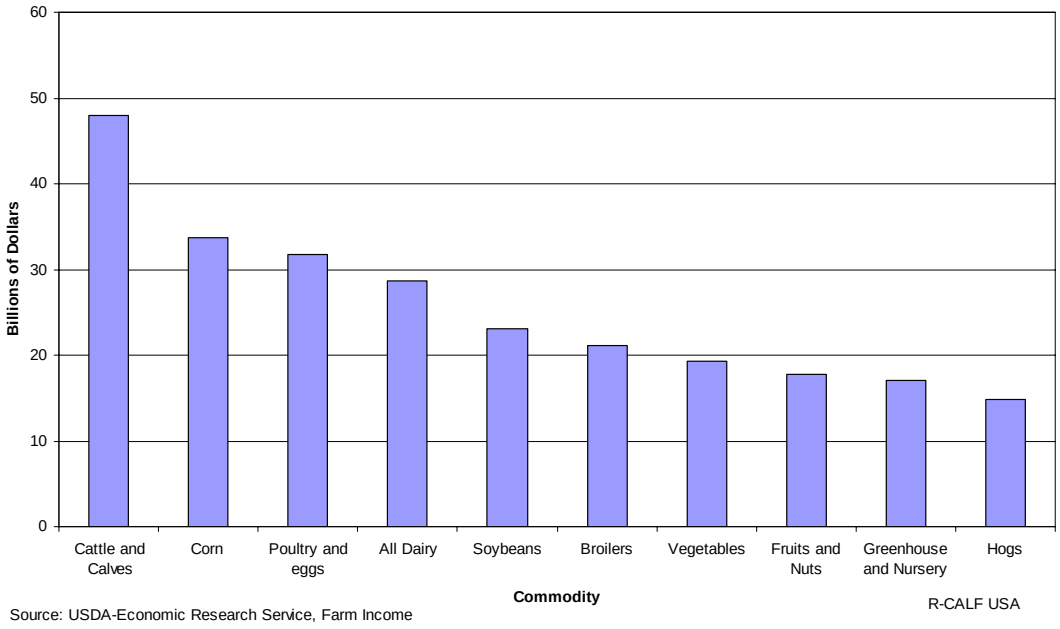
APPENDIX

UNDER SIEGE: THE UNITED STATES LIVE CATTLE INDUSTRY

I. THE CURRENT STATE OF THE U.S. CATTLE INDUSTRY

Cattle farming and ranching is perhaps the most common and recognizable economic engine throughout all of Rural America. The cattle industry historically is the single largest segment of American agriculture, towering over all other agricultural commodities by contributing nearly $50 billion in new wealth each year to the U.S. economy (chart 1).

CHART 1: TOP 10 U.S. AGRICULTURE COMMODITIES
(Based on Five-Year Average)



Source: USDA-Economic Research Service, Farm Income

This massive economic engine – the U.S. cattle industry – *is* the economic engine with the greatest potential to either stimulate economic prosperity or facilitate continued economic poverty for many, if not most, rural communities across the United States. It is, unfortunately, the latter outcome – economic poverty – that continues to describe much of Rural America. This is due, in large part, to the long-term, severe economic crisis that plagues the U.S. cattle industry

– a crisis that inhibits the potential of the U.S. cattle industry to contribute to the revitalization of our nation's economy, and particularly our rural economy.

The U.S. cattle industry makes substantial financial contributions in every state of the Union, generating in 2008 approximately $37 billion in cash receipts in the top 12 cattle-producing states and approximately $12 billion in the remaining 38 states.[1]

This industry can and should, however, be making a much greater and much more widely distributed contribution to the U.S. economy. But for decades, the U.S. cattle industry has been severely neglected by Congress and federal regulators that refused to: 1) recognize the unique characteristics of the U.S. cattle industry when trade policies were formulated; 2) update livestock-related statutes concerning competitive markets; and, 3) enforce antitrust laws and laws established to protect cattle farmers and ranchers from the anticompetitive practices of the dominant meatpackers, particularly through the Packers and Stockyards Act. As a result, the viability of the U.S. cattle industry has been severely marginalized.

Unrestrained by ill-conceived trade policies, a lack of enforcement of antitrust laws, and emboldened by the government's disinterest in prohibiting anticompetitive practices, the dominant beef packers (which also are dominant importers and dominant exporters) and dominant feedlot companies, which today are often indistinguishable,[2] have radically changed the structure of the U.S. cattle industry.

A. The Current Structure of the U.S. Cattle Industry

1. Market Concentration in the Final Cattle Market

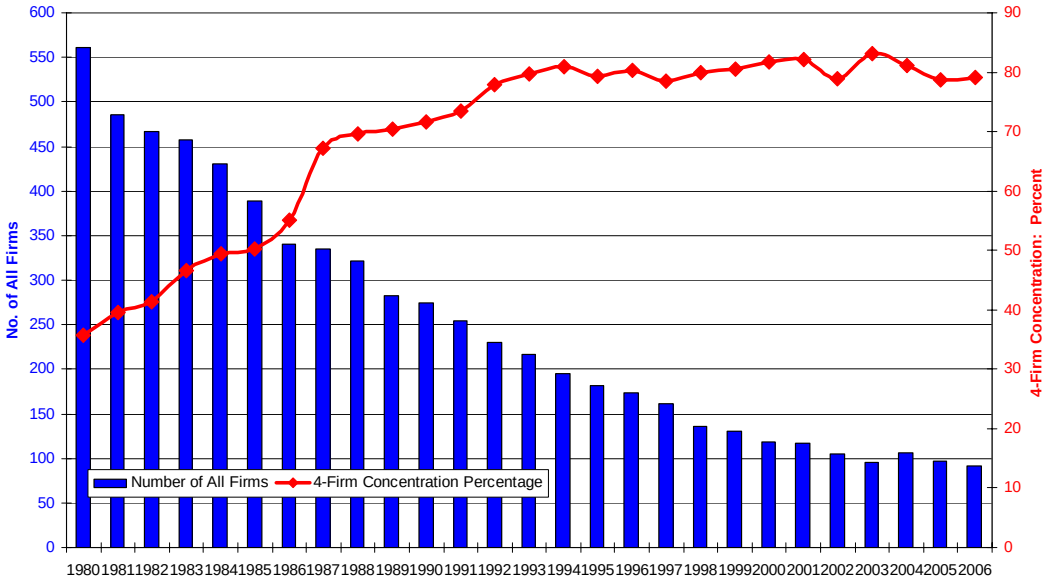
The purpose of the $50 billion U.S. cattle industry is to raise cattle for slaughter and subsequent fabrication into consumable beef. The beef packing industry slaughters live cattle and terminates the life cycle of individual cattle. The *final cattle market* is the market where cattle are sold to the beef packer for slaughter and consists predominantly of fed cattle (i.e., steers and heifers that are raised and fed specifically for beef production), but also includes cows and bulls that are purchased by beef packers for slaughter after they have exceeded their useful breeding lives, which may occur months or years after birth. This final cattle market for U.S. cattle farmers and ranchers also is the *buyer-side* of the beef packers' market.

[1] *See* Farm Income: Cash Receipts, States' Ranking for Cash Receipts, Data Sets, U.S. Department of Agriculture (hereafter "USDA") Economic Research Service (hereafter "ERS"), 2008, available at http://www.ers.usda.gov/Data/FarmIncome/firkdmuxls.htm#group

[2] *See*, e.g., Recent Acquisitions of U.S. Meat Companies, Congressional Research Service, 7-5700, RS22980, March 10, 2009, at 2 ("The proposed JBS acquisition of Five Rivers Ranch Cattle Feeding, which was part of the Smithfield deal, also took place, making JBS the largest cattle feeder in the United States."); *see also id*., Table 1 (Cargill Cattle Feeders, LLC, was ranked as the third largest cattle feeding company in 2006, marketing approx. 6 percent of the nation's fed cattle). Based on information and belief, Cactus Feeders, Inc., and Friona Industries, LP, which also are listed in Table 1 as among the largest cattle feeding companies, are considered captive feedlots and predominantly market their cattle to only one meatpacker.

The current structure of the U.S. cattle industry is characterized by unprecedented concentration in the beef packing sector.[3] This unprecedented concentration did not happen overnight – it has been acutely chronic for decades and is now fully manifest in both the buyer-side (i.e., the final cattle market) and seller-side (i.e., the initial beef market) of the beef packers' market. On the buyer-side of the beef packers' market, the beef packer purchases for slaughter live steers and heifers and cows and bulls from farmers and ranchers. Latest available data suggest the four-firm concentration for firms that slaughter steers and heifers is over 85 percent (chart 2);[4] for firms that slaughter cows and bulls, over 50 percent (chart 3).[5]

CHART 2: Decreased Number of Firms that Slaughter Steers and Heifers and Increased Four-Firm Concentration (1980-2006)



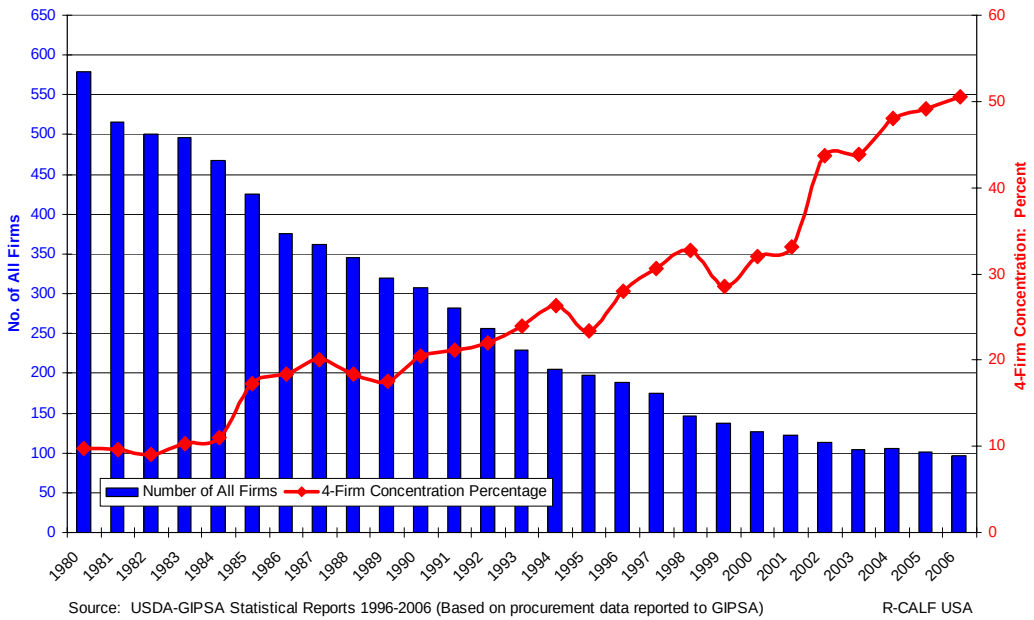
Source: USDA-GIPSA Statistical Reports 1996-2006 (Based on procurement data reported to GIPSA) R-CALF USA

[3] *See* 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("Concentration levels are 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. . .").

[4] *See* United States of America, et al. v JBS S.A. et al., Complaint, U.S. District Court, Northern District of Illinois Eastern Division, Civil Action No. 08-CV-5992 (The U.S. Dept. of Justice alleged that the top four meatpackers purchased "over 85% - nearly 24 million" of the 27 million fed cattle purchased in 2007.); *see also* Packers and Stockyards Statistical Report, 2006 Reporting Year, Table 27, USDA Grain Inspection, Packers and Stockyards Administration (hereafter "GIPSA"), GIPSA SR-08-1, May 2008, at 44 (As depicted in Chart 2, GIPSA reported that there were 92 firms in 2006 that controlled 95.6 percent of the total commercial slaughter of steers and heifers.).

[5] *See* Packers and Stockyards Statistical Report, 2006 Reporting Year, Table 28, USDA, GIPSA, GIPSA SR-08-1, May 2008, at 45 (As depicted in Chart 3, GIPSA reported that 97 firms in 2006 controlled 93.8 percent of the total commercial slaughter of cows and bulls.).

CHART 3: Decreased Number of Firms that Slaughter Cows and Bulls and Increased Four-Firm Concentration (1980-2006)



Source: USDA-GIPSA Statistical Reports 1996-2006 (Based on procurement data reported to GIPSA) R-CALF USA

2. Market Concentration in the Initial Beef Market

Following slaughter by the beef packing industry, beef derived from all cattle (i.e., steers, heifers, cows and bulls) is subsequently marketed to additional processors, wholesalers, exporters, retailers, or directly to consumers. This market, from the beef packer to any one of the beef packers' customers, is considered the initial beef market and is the *seller-side* of the beef packers' market. The unprecedented concentration achieved by dominant beef packers in the buyer-side of their market (i.e., the final cattle market) is mirrored, indeed exacerbated, by the concentration level achieved in the seller-side (or wholesale/retail-side) of their market. By 2006, the top 20 beef packing firms controlled 99.9 percent of all boxed beef production, with just four firms controlling over 84 percent of the nation's boxed beef sold to wholesale and/or retail consumers (representing the control of nearly 22 million of the 26 million head of fed cattle fabricated into boxed beef) (chart 4).[6] Based on an extrapolation of data compiled by the Justice Department, the current concentration in the U.S. boxed beef market would register approximately 2,000 points using the Herfindahl-Hirschman Index (HHI),[7] which is well above the highest spectrum of market concentration recognized by the Justice Department and would be characterized as "highly concentrated (HHI above 1800)."[8]

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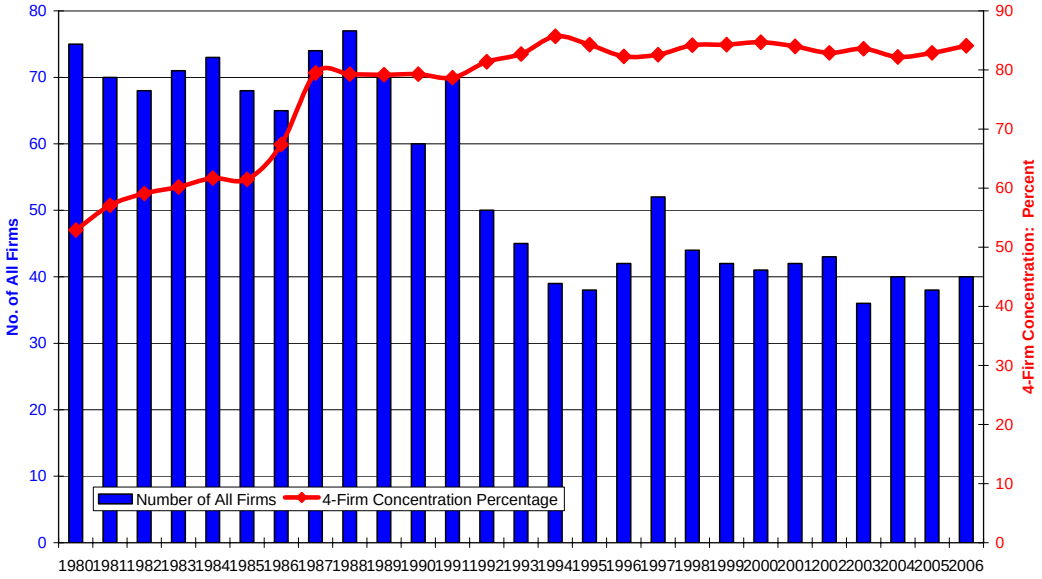
[6] *See* Packers and Stockyards Statistical Report, Table 33, USDA, GIPSA, GIPSA SR-08-1, May 2008, at 50.
[7] *See* United States of America, et al. v JBS S.A. et al., Amended Complaint, U.S. District Court, Northern District of Illinois Eastern Division, Civil Action No. 08-CV-5992 (The Justice Department alleged that the HHI would increase by over 500 points, resulting in a post-acquisition HHI of approximately 2,500" if JBS were to acquire National Beef Packing Co. Thus, it is apparent that the pre-merger HHI is approximately 2,000.).
[8] *See* Horizontal Merger Guidelines, U.S. Department of Justice and the Federal Trade Commission, Revised April 8, 1997, at 15.

CHART 4: Decreased Number of Firms that Produce Boxed Beef and Increased Four-Firm Concentration (1980-2006)



Source: USDA-GIPSA Statistical Reports 1996-2006 R-CALF USA

3. Market Concentration in the Final Feeder Cattle Market

One step upstream from the final cattle market is the *final feeder cattle market*. Feeder cattle are steers and heifers that have been weaned by the farmer or rancher who raised them (i.e., the person whom calved them out (birthed) and reared them until weaning) and typically reared on forage for several months until they reach a weight of 600 to 900 pounds (either by the farmer or rancher who weaned them, or a backgrounder or stocker who purchased them after weaning). These cattle, then referred to as feeder cattle, are marketed to feedlots where they are then typically fed a high-energy diet for several months, until they reach their optimal slaughter weight (typically 1,250 pounds) and then marketed to the meatpacker. Thus, the final feeder cattle market is the market in which feeder cattle are sold to feedlots for final finishing (feeding).

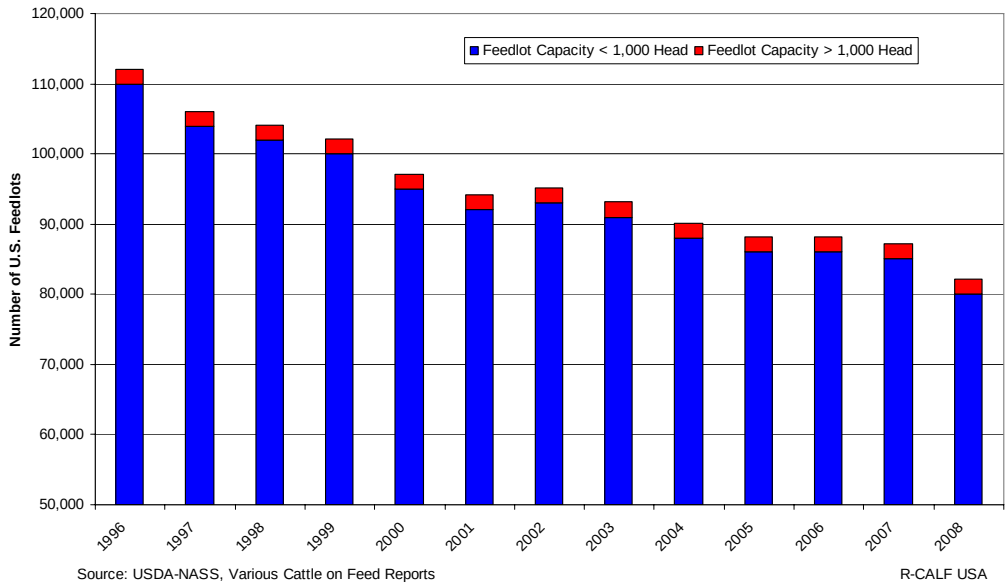
Importantly, the market for cows and bulls sold to a feedlot for final finishing functions almost identically to the final feeder cattle market, and for purposes of these comments, R-CALF USA includes steers, heifers, cows and bulls as among the cattle subject to the final feeder cattle market.[9]

The buyer in a final feeder cattle market transaction is a feedlot company and like the beef packing industry, feedlot companies are increasingly concentrated. The number of U.S. feedlots has declined sharply over the past 13 years, with nearly 30,000 feedlots having exited the

[9] One difference is that feeder cattle are traded in the commodity futures market where cows and bulls are not.

industry since 1996.[10] Importantly, nearly all the exiting feedlots were smaller feedlots with capacities of less than 1,000 head, as the number of feedlots with capacities of more than 1,000 head has remained relatively constant (chart 5).[11]

CHART 5: Decline in Numbers of U.S. Feedlots
1996-2008



The individuals who own and operate these smaller feedlots are referred to farmer-feeders. These farmer-feeders contribute greatly to the competitiveness of the feeder cattle market and their drastic decline means that today there are 30,000 fewer bidders for feeder cattle seated in U.S. auction yards and traveling the rural landscape in search of cattle to feed. As a result, competition has been significantly reduced in the U.S. feeder cattle market.

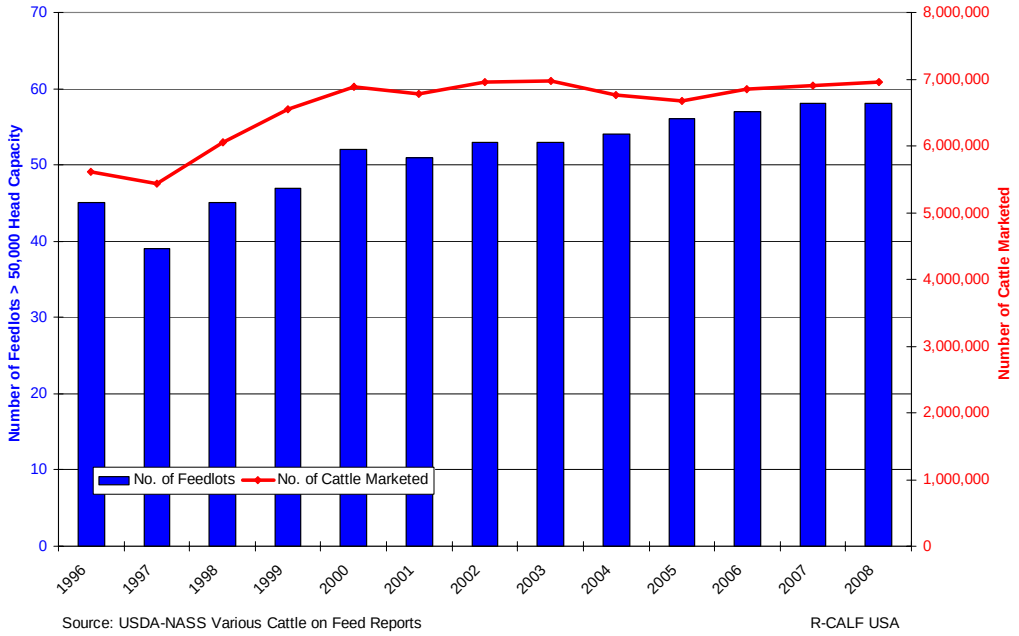
While the numbers of small feedlots have declined since 1996, the number of cattle marketed by the largest of feedlots, those with capacities of at least 50,000 head, has increased by more than 1.3 million head during this same period.[12]

In 2008, the 58 feedlots with capacities of at least 50,000 head marketed approximately 7 million of the approximately 26 million cattle fed and marketed during that year (chart 6).[13] These 58 feedlots, therefore, fed and marketed over one-fourth of all the fed cattle in 2008. Included among these 58 feedlots with capacities of at least 50,000 head would be the nation's top four feedlot companies: JBS Five Rivers Ranch Cattle Feeding; Cactus Feeders, Inc.; Cargill Cattle

[10] *See* Cattle, Final Estimates, various reports, 1996-2008, USDA, National Agricultural Statistics Service (hereafter "NASS"); *see also* Cattle on Feed, USDA, NASS, Feb. 20, 2009.
[11] *Ibid*.
[12] *See* Cattle, Final Estimates, various reports, 1996-2008, USDA, NASS; *see also* Cattle on Feed, USDA, NASS, Feb. 20, 2009.
[13] *See* Cattle on Feed, USDA, NASS, Feb. 20, 2009, at 14.

Feeders, LLC; and, Friona Industries, LP.[14] Based on capacities estimated for these top feedlots by Mary Hendrickson and William Heffernan,[15] and using the industry rule-of-thumb for the feedlot turnover rate of 2.5, collectively these four feedlots likely feed approximately 4.7 million cattle annually, or about 18 percent of the total number of feeder cattle purchased, fed and marketed each year.

CHART 6: Feedlots with Capacities of 50,000 Head or More and Cattle Marketed
1996-2008



Source: USDA-NASS Various Cattle on Feed Reports R-CALF USA

The concentration achieved by the beef packers in both the final cattle market and initial beef market is worsened because the beef packers have effectively pushed their market dominance down through the final cattle market and into the underlying feeder cattle market as well. As stated previously, this dual market dominance is exemplified by JBS' acquisition of the nation's largest cattle feeding company and by Cargill's dominant position as one of the top four feedlot companies.[16]

4. Geographic Concentration of the U.S. Cattle Industry

[14] *See* Recent Acquisitions of U.S. Meat Companies, Congressional Research Service, 7-5700, RS22980, March 10, 2009, at 2

[15] *See* Concentration of Agricultural Markets, Mary Hendrickson and William Heffernan, University of Missouri, Columbia, April 2007.

[16] *See* Recent Acquisitions of U.S. Meat Companies, Congressional Research Service, 7-5700, RS22980, March 10, 2009, at 2 ("The proposed JBS acquisition of Five Rivers Ranch Cattle Feeding, which was part of the Smithfield deal, also took place, making JBS the largest cattle feeder in the United States."); *see also id.*, Table 1 (Cargill Cattle Feeders, LLC, was ranked as the third largest cattle feeding company in 2006, marketing approx. 6 percent of the nation's fed cattle). Based on information and belief, Cactus Feeders, Inc., and Friona Industries, LP, which also are listed in Table 1 as among the largest cattle feeding companies, are considered captive feedlots and predominantly market their cattle to only one meatpacker.

Data reported by USDA show that the top three cattle-producing states in 1980 – Texas, Kentucky and Nebraska – captured 30 percent of the nation's gross income earned that year from the sale of cattle and calves.[17] Within 30 years, concentration in the cattle industry resulted in the capture by the top three states – consisting now of Nebraska, Texas and Kansas – of approximately 43 percent of the nation's gross income earned in 2009 from the sale of cattle and calves (chart 9).[18]

CHART 9

Change in Percentage of Gross Income from Cattle and Calves Generated in Top 3 States

1980		2009	
State	**Gross Income (1,000 Dollars)**	**State**	**Gross Income (1,000 Dollars)**
Texas	$3,963,247	Texas	$6,938,721
Kentucky	2,865,037	Nebraska	6,239,571
Nebraska	2,798,823	Kansas	5,546,577
3-State Gross Income	$9,627,107		$18,724,869
Total U.S. Gross Income	$31,870,419		$43,776,568
Percentage	0.3021		0.4277

Source: USDA-NASS

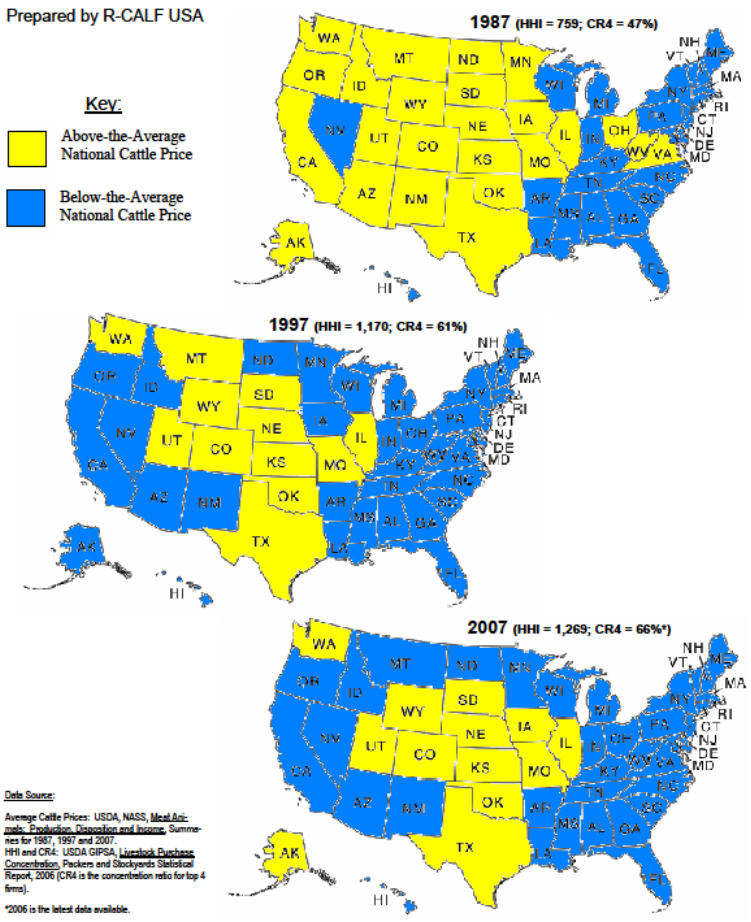
Thus, concentration in the cattle industry resulted in three states capturing within three decades approximately 13 percent of the economic revenues previously generated within 48 states. This phenomenon is the result of the nation's cattle production migrating to closer proximity to the locations chosen by the few remaining concentrated beef packers. And, this phenomenon helps explain why rural communities are being hollowed out all across the United States.

Another indicator of the widespread loss of competitive markets that is leading to the concentration of the cattle industry in an ever shrinking geographic region in the U.S. is that fewer and fewer states are receiving cattle prices that are above the national average. For example, in 1987 nearly one-half the states (24) enjoyed cattle prices that were above the national average. But, by 2007, just 20 years later, the number of such fortunate states was reduced to only 13 (chart 10).

[17] *See* Meat Animals, Production, Disposition, Income, 1979-1980, USDA, Agriculture Crop Reporting Board, Economics and Statistics Service, April 1981, at 7, available at http://usda.mannlib.cornell.edu/usda/nass/MeatAnimPr//1980s/1981/MeatAnimPr-04-00-1981.pdf.

[18] *See* Meat Animals, Production, Disposition, and Income 2008 Summary, USDA, NASS, May 2009, at 13, available at http://usda.mannlib.cornell.edu/usda/current/MeatAnimPr/MeatAnimPr-05-29-2009.pdf.

CHART 10: Effects of Declining Competition on Cattle Prices



It is now strikingly evident that the profitability of the U.S. cattle industry is being drawn away from many states and many rural communities and is becoming increasingly concentrated in the narrow region where the few remaining beef packers and few remaining feedlots have decided to relocate – in the High Plains region of the United States. This phenomenon further helps explain the widespread economic desecration of rural communities all across the United States.

5. Market Concentration In the Competing Proteins Market

Beef, pork and poultry are substitute food protein products that compete head-to-head for market share in the consumer meat market, both here and abroad. The demand and price for cattle is influenced by the supply and price of competing proteins such as pork and poultry.[19] USDA has found that beef prices are particularly susceptible to increased poultry supplies, i.e., poultry

[19] *See* Livestock, Dairy and Poultry Outlook, USDA, ERS, LDP-M-120 (June 17, 2004), at 9 ("Given the present strength in the fed cattle market . . . increased supplies of competing meats . . . would push breakevens into the red quickly."), available at http://www.ers.usda.gov/publications/ldp/jun04/LDPM120T.pdf.

broilers at relatively lower prices.[20] USDA further found that "if the price of beef goes up while the price of chicken remains lower than beef, consumers will likely buy less of the relatively more expensive beef and buy more of the relatively less expensive chicken."[21]

Researcher, Desmond A. Jolly, University of California, Davis, in discussing the relationships between beef and its competing food proteins – pork and chicken – found that consumer demand for each of these competing proteins responds to, *inter alia*, consumer income, the price of the product, and the price of substitutes.[22] Kansas State University (KSU) researchers found, "When beef demand increases (i.e., shifts up), say as a result of an increase in the price of poultry that causes consumers to substitute beef for poultry, the result is higher beef prices. . ."[23] Researchers at the University of Nebraska – Lincoln (UNL) found that, "Pork and poultry are generally considered substitute sources of protein for beef."[24] A literature review by USDA reveals that the average response to competing meat price changes is such that a 1 percent decrease in poultry prices would result in a 0.24 percent decrease in beef consumption.[25]

Despite the obvious reduction in competition that occurs among and between the competing proteins – beef, pork and chicken – if dominant firms control the production, output (i.e., supplies) and the price for each competing protein, dominant U.S. meatpackers continue to be unrestrained in their capture of dominant control over each competing protein. Moreover, these same dominant firms are engaged in the import and export markets for these competing proteins, where they likewise can exert their dominant control to influence prices, supply, and demand among and between the substitute proteins.

The dominance of U.S. meatpackers over each of the substitute proteins is exemplified in the 2007 concentration study by Mary Hendrickson and William Heffernan who found that Tyson, Swift & Co. (now JBS S.A.) and Cargill each were among the nation's largest beef packers and pork packers, and additionally, Pilgrim's Pride (now JBS S.A.) and Tyson were the largest broiler producers.[26] Chart 12 depicts the concentration that exists in the substitute protein markets.

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[20] *See* Livestock, Dairy, and Poultry Outlook, USDA, ERS, LDP-M-139 (Jan. 19, 2006), at 8 ("Large supplies of competing meats at relatively lower prices, particularly broilers, are also expected to pressure beef prices . . ."), available at http://www.ers.usda.gov/Publications/LDP/2006/01Jan/LDPM139T.pdf; *see also id*., at 7 ("Improved grading prospects and larger number of cattle on feed will pressure the market, as will larger supplies of competing meats at relatively lower prices.").

[21] Price and Income Affect Nutrients Consumed From Meats, Food Review, Kuo S. Huang, FoodReview, USDA, ERS, January-April 1996, at 37, 38 (*FoodReview* was replaced by *Amber Waves* following the Winter 2002 issue).

[22] *See* Reasons for the decline in beef consumption, Health concerns played a part but price was most important, Desmond A. Jolly, University of California, Davis, California Agriculture, May-June 1983, at 14, 15.

[23] Focus on Beef Demand, Managing for Today's Cattle Market and Beyond, James Mintert, *et al*., Kansas State University, March 2002.

[24] Improved Beef Demand Benefits Nebraska Cattle Producers, Cornhusker Economics, Institute of Agriculture & Natural Resources, Department of Agricultural Economics, University of Nebraska – Lincoln, September 27, 2000.

[25] *See* Commodity and Food Elasticities: Demand Elasticities from Literature Results, Data Sets, USDA, ERS, available at http://www.ers.usda.gov/Data/Elasticities/ShowTable.aspx?geo=United%20States&com=Beef&xcom=Poultry.

[26] *See* Concentration of Agricultural Markets, Mary Hendrickson and William Heffernan, University of Missouri, Columbia, April 2007.

CHART 12

BEEF PACKERS CR4 = 83.5%* 1. Tyson 36,000 head 2. Cargill 28,300 head 3. Swift & Co. 16,759 head (Now JBS) 4. National Beef Packing Co. 13,000 head	**PORK PACKERS CR4 = 66% (Est.)*** 1. Smithfield Foods 102,900 2. Tyson Foods 72,800 3. Swift & Co. 46,000 (Now JBS) 4. Cargill 36,000
BROILERS CR4 = 58.5%* 1. Pilgrim's Pride (Now JBS) 2. Tyson 3. Perdue 4. Sanderson Farms	**Source:** Mary Hendrickson and William Heffernan, University of Missouri, Columbia, April 2007

R-CALF USA believes the control by dominant beef packing firms over the production, wholesaling, importing, exporting, and retailing of substitute proteins pork and poultry distorts the competitive marketplace, disadvantages U.S. cattle producers, and violates U.S. antitrust laws. Such control reduces, if not eliminates, competition between and among the substitute proteins, as well as between and among the farmers and ranchers who produce cattle, hogs, chickens and turkeys.

This loss of market competition and commensurate increase in market power facilitates the multi-protein meatpackers' ability to exercise market power to the detriment of both U.S. cattle producers and U.S. meat consumers. The foundation for our concern is that beef, pork and poultry are indeed competing, substitute protein products in the consumer market, both here and abroad. And, meatpackers in control of the multiple protein substitutes can arbitrarily increase or decrease poultry and/or pork production and/or raise or lower poultry and/or pork prices within their fully integrated poultry and pork divisions to manipulate both the demand for beef and the price for live cattle. In addition, R-CALF USA believes the market power exerted by these dominant meatpackers is exacerbated due to their dominance in the import and export markets where they likewise can manipulate demand for a particular protein source by managing supplies.

B. The Remaining Participants in the U.S. Cattle Industry

1. The Precarious Structure of U.S. Cattle Industry Participants

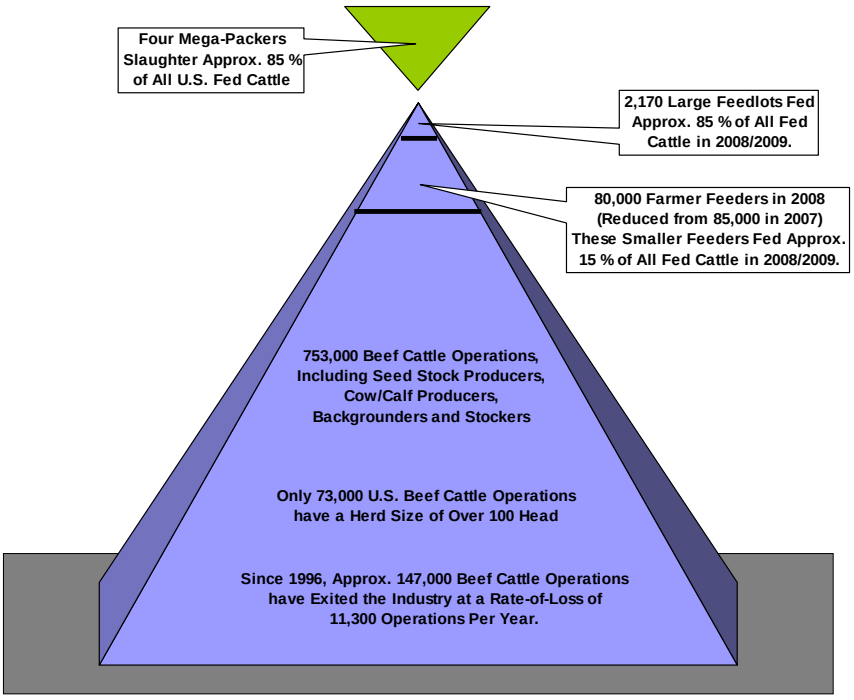
What remains today of the U.S. cattle industry is a highly concentrated industry structure that, as stated above, exceeds the level of market concentration "generally considered to elicit non-competitive behavior and result in adverse economic performance."[27] Today, R-CALF USA estimates that 85 percent of all the fed cattle calved and marketed by the remaining 753,000 beef

[27] 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.

cattle producers are ultimately marketed through only four dominant beef packers. This unprecedented level of market concentration gives the dominant beef packers the ability to control, restrict and manage access to the market. And, this gives the dominant beef packers the ability to control the key determinant for farmer and rancher profitability – the price of their live cattle.

As if this sheer, unprecedented level of market concentration were not enough, the dominant beef packers that are geographically concentrating the cattle industry and that already control the final cattle market, the initial beef market, and the competing proteins market are quickly capturing control of the final feeder cattle market by dominating the feeding segment of the live cattle industry. Today there are 2,170 dominant feedlots that feed approximately 85 percent of all the fed cattle in the United States, while smaller, farmer-feeders feed only about 15 percent of the nations fed cattle (chart 11).[28]

CHART 11



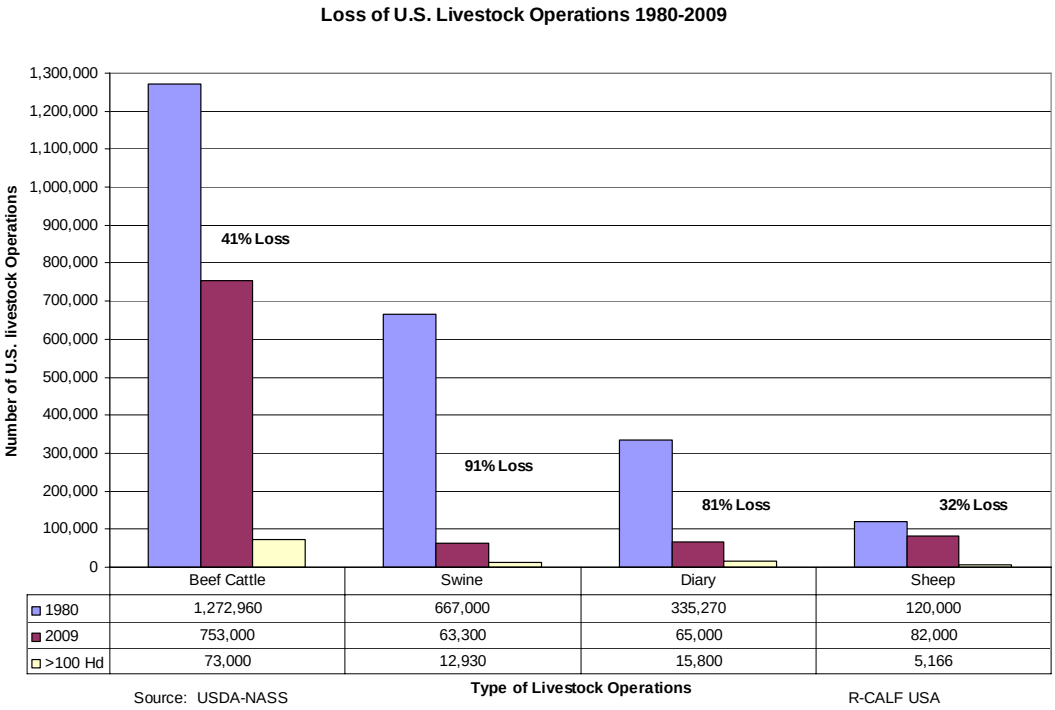
2. The Entire U.S. Livestock Industry Is in a Serious Crisis

The cattle industry is fast going the way of the hog and dairy industries that already have lost 90 percent and 80 percent of their respective industries' participants within the past 30 years, since

[28] *See* Cattle on Feed, USDA, NASS, Feb. 20, 2009, at 14 (In 2008, 80,000 feedlots with capacities of less than 1,000 head marketed 4.045 million of the 26.449 million cattle marketed. The 2,170 larger feedlots marketed 22.404 million cattle.), available at http://usda.mannlib.cornell.edu/usda/nass/CattOnFe//2000s/2009/CattOnFe-02-20-2009.pdf.

1980. It is inexplicable that neither Congress nor federal regulators responded at all to the mass exodus of hundreds of thousands of independent hog producers over the past three decades without determining the extent of the market power exerted by the dominant pork packers that effected such a drastic industry change. The number of U.S. hog operations fell from 667,000 in 1980 to fewer than 65,000 in 2008. The larger cattle industry is suffering the same fate. It has lost 41 percent of its operations since 1980, falling from about 1.3 million cattle operations to 757,000 cattle operations (chart 12). This horrendous loss of industry participants translates into the centralization of U.S. livestock production, which threatens the nation's food security and explains the ongoing, economic demise of rural communities all across the United States.

CHART 12

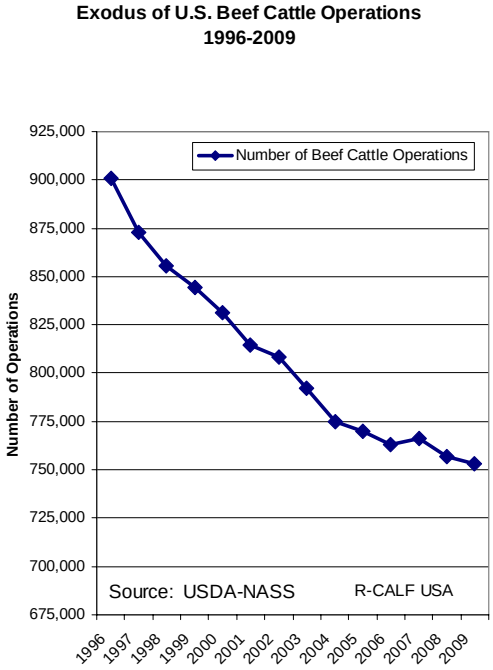


3. The Loss Rate of U.S. Cattle Operations Has Not Been Gradual

In just the past 12 years, from 1996 to 2009, over 147,000 U.S. cattle operations exited the U.S. cattle industry, representing a rate-of-loss of over 11,000 operations per year (chart 13). To put this in perspective, this represents an annual loss of more beef cattle operations than there are in each of the entire states of Arizona, California, Colorado, Idaho, Montana, North Dakota, and several other states.[29] Again, this widespread, horrendous loss of U.S. cattle operations helps explain the depressed state of the United States' rural economy.

[29] *See* Farms, Land in Farms, and Livestock Operations 2008 Summary, USDA, NASS, Feb. 2009, at 18, available at http://usda.mannlib.cornell.edu/usda/current/FarmLandIn/FarmLandIn-02-12-2009.pdf.

CHART 13



C. U.S. Cattle Industry Production Remains Stagnant

The beef packing industry and its allied trade associations assert that improvements in genetics, managerial ability, technology and feed efficiency gained by the U.S. cattle industry has negated the need for more cattle and more cattle producers because the U.S. cattle industry is now producing more beef with fewer mother cows. The Texas Cattle Feeders Association (TCFA), for example, claims that, "Productivity gains have offset the need for an additional 5.3 million cows."[30] And, it claims the U.S. now has the smallest cow herd since 1949 and yet has experienced a 176 percent growth in beef production since that time.[31] These claims are highly misleading at best and, unfortunately, are among the chief "efficiency" claims made by the beef packers and their allies to rationalize the exodus of independent U.S. cattle producers while they simultaneously wrest control over the live cattle supply chain away from the competitive marketplace.

The reason these claims are misleading is five-fold:

First, domestic productivity gains have *not* offset the need for an additional 5.3 million cows (which is the number of U.S. beef cows liquidated from the U.S. herd since 1980). The U.S. imported 2.5 million and 2.3 million live cattle in 2007 and 2008, respectively.[32] It also imported

[30] *See* Charts Distributed by Texas Cattle Feeders Association at the New Mexico Cattle Growers' Annual Meeting held Dec. 5, 2009, attached hereto as Attachment 1.
[31] *Ibid*.
[32] Livestock and Meat Trade Data, Cattle: Annual and Cumulative Year-to-Date U.S. Trade (Head), USDA, ERS, available at http://www.ers.usda.gov/data/meattrade/CattleYearly.htm.

3 billion and 2.5 billion pounds of beef in each of those years, respectively.[33] Based on a 750-pound carcass weight, the live cattle equivalent of the beef imported in 2007 and 2008 is approximately 4 million and 3 million head, respectively. Thus, the U.S. imported the equivalent of 5.5 million cattle in 2007 and 4.8 million cattle in 2008. Presuming that consumer demand and all export opportunities for beef were met in 2007 and 2008, these imports offset the United States cattle industry's opportunity to maintain the additional 5.3 million cows liquidated since 1980. Thus, TCFA's claim that additional U.S. cows are not needed due to productivity increases is baseless. It clearly is not the case that current domestic production is meeting the current demand for beef. The USITC should take a critical look at how the packers are strategically using imports to restrain the domestic cattle industry.

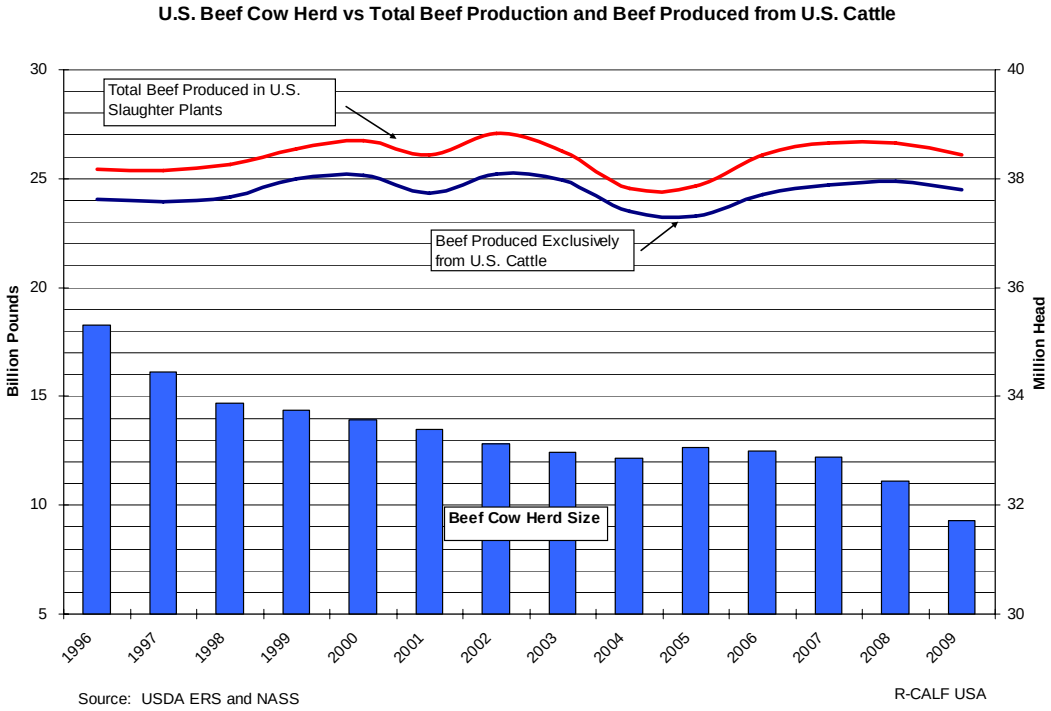
Second, a significant portion of U.S. beef production reported by USDA as "domestic beef production" did *not* originate from the U.S. cow herd – it originated from cattle imported into the U.S. from Canada and Mexico. The estimated amount of beef produced from imported cattle in U.S. slaughtering plants increased from 543 million pounds in 1985 to 1.96 billion pounds in 1995, and was 1.94 billion and 1.78 billion pounds in 2007 and 2008, respectively. This estimate is based on multiplying each year's average U.S. carcass weight by the number of cattle imported each year. Thus, USDA significantly overstates U.S. beef production by including beef derived from imported cattle in its production estimates.

Third, increased beef production occurs during the liquidation phase of the cattle cycle because liquidation necessarily entails selling off the cow herd – including cows and heifers, as well as bulls – for slaughter. The U.S. has been liquidating its cattle herd since 1996, and the slaughter of liquidated cows, heifers and bulls contributes significant volumes to domestic production that would not otherwise be available if herd liquidation was not occurring.

The production of beef derived from cattle born and raised in the U.S. since 1996 has remained relatively stagnant, rising only slightly above and falling only slightly below the 1996 starting point (chart 14). This is somewhat alarming because the ongoing liquidation of additional cows, heifers and bulls should be increasing domestic beef production even more significantly. The fact that it is not raises the concern that domestic production without the additional liquidated animals likely is significantly lower than the baseline that USDA has used for its future production estimates.

[33] *See* Livestock and Meat Trade Data, Beef and Veal: Cumulative Year-To-Date U.S. Trade (Carcass Weight 1,000 Pounds), USDA, ERS, available at http://www.ers.usda.gov/data/meattrade/BeefVealYearly.htm.

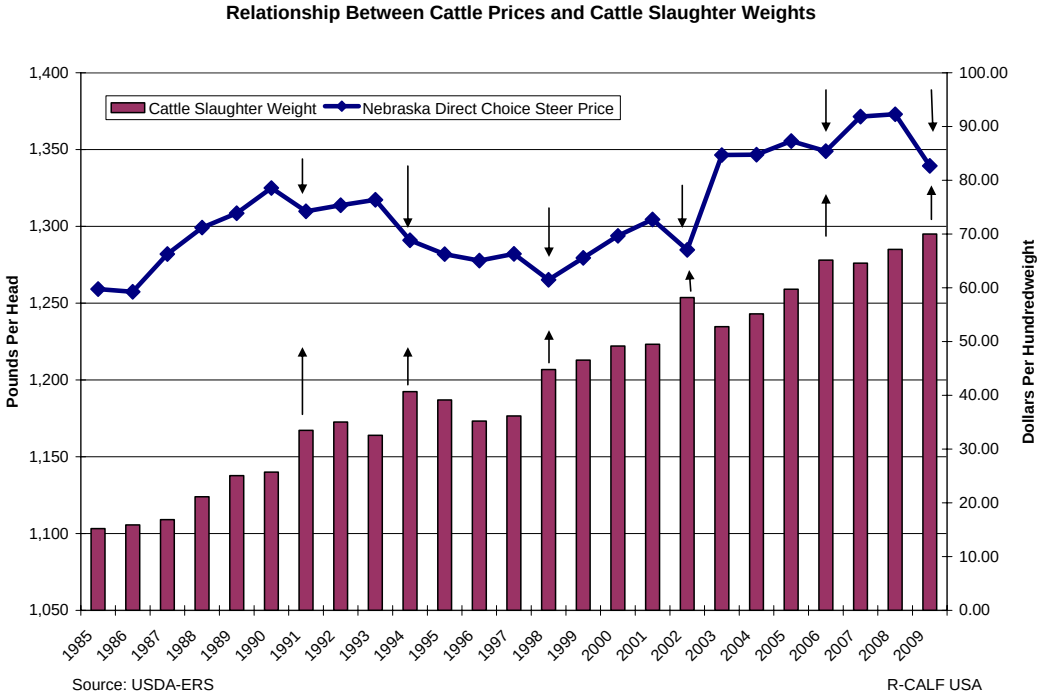
CHART 14



Fourth, beef production increases when individual cattle are fed longer – beyond their optimal slaughter weight – which leads to heavier carcasses of lower quality. The dominant beef packers, because they control access to the market, can effect longer feeding periods simply by limiting their procurement of optimal weight cattle (e.g., by offering only a price lower than what a competitive market would bring or strategically importing live cattle or beef to reduce demand for U.S. live cattle), thus forcing the industry to increase carcass weights through longer feeding periods. When cattle supplies are tight, e.g., during the liquidation phase of the cattle cycle, beef packers are incentivized to manipulate the industry to produce overweight cattle, i.e., heavier carcasses, by limiting access to the marketplace through, e.g., the offering of low prices for cattle or satisfying their immediate needs with imported cattle and beef. The beef packers know that the market response to lower prices is to feed cattle longer, and that action increases the beef packers' tonnage, thus helping to satisfy demand while insulating the beef packer from a tight-supply market, which would otherwise require them to pay higher prices for cattle.

Each significant downturn in live cattle prices since 1985 resulted in an abrupt increase in the average slaughter weight of cattle when compared to the previous year (chart 15). Contrary to claims made by the TCFA and other packer-aligned trade associations, this does not demonstrate that heavier cattle are solely the result of increased productivity. Instead, this relationship between cattle prices and cattle slaughter weights demonstrates the susceptibility of the cattle industry to price manipulation by the packers – manipulations that enable packers to increase tonnage without increasing costs.

CHART 15



Finally, the purpose of producing beef is to satisfy domestic beef consumption and export opportunities. As will be discussed later in these comments, U.S. beef production has not kept pace with increased domestic beef consumption, even with the heavier carcass weights, and the production potential of the U.S. cattle industry is being severely restrained by the beef packers' actions that are manipulating the industry's output.

II. THE U.S. CATTLE INDUSTRY IS UNIQUELY SUSCEPTIBLE TO MONOPSONY POWER AND EXPLOITATION

A. The Final Cattle Market Is the Portal through Which Market Power Invades the Entire U.S. Live Cattle Industry.

Not all of the approximately $50 billion in annual cash receipts from the sale of cattle and calves is generated in the final cattle market where slaughter-ready cattle are sold to beef packers. In 2008, e.g., over $48 billion in cash receipts was generated by the U.S. cattle industry from the marketing of over 44 million cattle and nearly 9 million calves.[34] However, the beef packers purchased and slaughtered only approximately 34 million cattle in 2008.[35] Thus, transactions in the final cattle market involved only about 64 percent (i.e., 34 million of the 53 million cattle and calves marketed) of the cattle and calves marketed in 2008.

[34] *See* Meat Animals Production, Disposition, and Income 2008 Summary, USDA, NASS, May 2009, at 4, 7, available at http://usda.mannlib.cornell.edu/usda/current/MeatAnimPr/MeatAnimPr-05-29-2009.pdf.
[35] *See* Livestock Slaughter 2008 Summary, USDA, NASS, March 2009, at 13, available at http://usda.mannlib.cornell.edu/usda/current/LiveSlauSu/LiveSlauSu-03-06-2009.pdf.

This informs us that the U.S. cattle industry is much more than just a supply source for the nation's meatpackers, and that the meatpackers are *not* the sole source of revenues for the entire industry. Instead, the U.S. cattle industry is a dynamic industry with numerous sub-markets (e.g., the final feeder cattle market) where economic activity critical to the wellbeing of rural communities all across the United States is generated from within the industry itself.

However, the final cattle market where slaughter-ready cattle, particularly steers and heifers, are sold directly to the beef packer *is* the price-making market for the entire U.S. cattle industry. This is because the price for slaughter-ready steers, heifers, cows and bulls is transferred, at least in part, backward throughout the live cattle production chain, impacting seed stock producers, cow/calf producers, backgrounders, and stockers. Thus, even a small lessening of competition or small price manipulation in the final cattle market has a profound, negative impact on the welfare of the hundreds of thousands of remaining independent cattle producers and the rural communities they support because the reduced competition and reduced price reverberates and compounds throughout the entire industry.

Oklahoma State University economist Clement E. Ward addressed the issue of seemingly small price impacts on the cattle industry and found that "[r]esearch to date suggests price impacts from packer concentration have been negative in general, but small."[36] He stated that while most studies found price distortions of 3 percent or less, 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."[37]

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.[38] 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."[39]

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. It is important for the USITC to recognize that the final cattle market is the portal through which even small market-power induced price distortions can invade and cripple the entire U.S. live cattle industry.

B. The Very Nature of Cattle Makes Their Value Susceptible to Market Power

[36] Packer Concentration and Packer Supplies, Clement E. Ward, Oklahoma Cooperative Extension Service, AGEC-554, at 554-5.
[37] 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.
[38] Testing for Market Power in Beef Packing: Where are We and What's Next?, Lynn Hunnicutt, Quinn Weninger, Utah State University, August 1999.
[39] *Id.*, at 1.

The very nature of cattle makes them unique when compared to other agricultural commodities. Cattle, e.g., are not a storable agricultural commodity or a commodity suitable for bulk transportation. The USITC, therefore, should not limit its review of the trade impacts to the cattle industry based on standards developed for other agricultural commodities. The following are a few unique characteristics of cattle that distinguish them from all other agricultural commodities:

1. Cattle have the Longest Biological Cycle of Any Farmed Animal

The Government Accountability Office (GAO) found that cattle have the longest biological cycle of all meat animals.[40] This is the characteristic that created the historical phenomenon known as the cattle cycle. According to USDA, the cattle cycle "arises because biological constraints prevent producers from instantly responding to price."[41] R-CALF USA believes the vertical integration of the U.S. cattle industry by the major meatpackers has been slower than in the U.S. hog industry due to this unique characteristic combined with the commensurate forage requirements needed to rear cattle. It takes approximately 15 to 18 months to rear cattle to slaughter weight and, unlike hogs, cattle consume considerable volumes of forage (i.e., from grazing) for much of this time. This makes the cattle industry less adaptable to the concentrated production practices common in the hog-rearing industry – practices that are more conducive to vertical integration by meatpackers – at least in the earlier stages of cattle production. *However*, after cattle reach approximately one-year of age on forage, and weigh approximately 600 to 900 pounds, they then become adaptable to a more concentrated production regime, i.e., they can be finished in large, concentrated feedlots. It is at this stage of the cattle production cycle – the final feeding stage – where meatpackers have focused their vertical integration efforts, and it is here that pricing strategies by the packers can permeate the entire cattle industry, giving packers considerable control over the entire industry.

The long biological cycle also makes the cattle industry highly susceptible to exploitation by firms that control the production and output of other substitute protein sources, i.e., hogs and poultry, which each have much shorter biological cycles that enable their respective industry's to respond quickly to changes in price by quickly adjusting production and output. In addition, multiple-protein firms can relatively quickly manipulate the output and price of their substitute proteins in order to manipulate the demand and price for cattle, while the cattle industry remains constrained from responding due to cattle's prolonged biological cycle.

The inelasticity of supply in the cattle industry compared to the elasticity of supply in the poultry industry[42] gives multiple-protein meatpackers a tremendous, anticompetitive advantage over U.S. farmers and ranchers who sell live cattle. If, e.g., a multiple-protein meatpacker were dissatisfied with the level of profits earned in its beef packing operation, it could increase its poultry production and/or reduce its poultry prices in order to reduce consumption of beef, which would reduce both the demand and price for live cattle. The response by the cattle industry

[40] 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.
[41] Cattle: Background, Briefing Room, USDA, ERS, updated June 7, 2007, available at http://www.ers.usda.gov/Briefing/Cattle/Background.htm.
[42] *See* 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.

would be limited to liquidation, which likely would accelerate the ongoing liquidation of the U.S. cattle herd and the exodus of U.S. cattle producers from the industry. When the price of cattle falls to the meatpacker's preferred level, the firm can quickly restore higher poultry prices and reduce the volume of poultry production, enabling it to maximize its profits from the sales of both substitute proteins until dissatisfaction returns once again and the cycle can be unilaterally restarted. Given the long biological cycle of cattle, the firm could enjoy several years' worth of maximized profits – a period when both cattle producers and beef consumers likely would be exploited.

2. Slaughter-Ready Cattle are Highly Perishable

Unlike many agricultural commodities that are storable, fed cattle that have reached their optimal slaughter weight must be marketed within a narrow window of time (generally within about a two-week period); otherwise, the animals would degrade in quality and value.[43] This characteristic makes the value of cattle extremely susceptible to manipulation, which beef packers can accomplish simply by restricting timely access to the market.

3. Transportation Costs Limit Marketing Options for Slaughter-Ready Cattle

The 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[44] and "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."[45] 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.[46]

These researchers identified nine cattle procurement regions that were based on the geographic proximity of packing plants and the procurement area for those packing plants.[47] They 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.[48]

While researchers have found that the wholesale beef market is national in scope, the discussion above suggests that transportation costs combined with the concentration of beef packers function to limit the national purview of the slaughter-ready cattle market. According to a study by John R. Schroeter, "The wholesale beef market . . . is essentially national in scope and

[43] *See* 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.
[44] *See* Examining Packer Choice of Slaughter Cattle Procurement and Pricing Methods, Oral Capps, Jr., et al., Agricultural and Resource Economics Review, April 1999, at 21.
[45] *Id*. at 15.
[46] *See id*. at 16.
[47] *Ibid*.
[48] *See* Examining Packer Choice of Slaughter Cattle Procurement and Pricing Methods, Oral Capps, Jr., et al., Agricultural and Resource Economics Review, April 1999, at 15.

insulated, to some extent, from the vagaries of the terms and volume of trade in a single regional fed cattle market."[49]

C. The U.S. Cattle Market Is Highly Susceptible to Monopsony Power and Exploitation

Corresponding to the unique nature of cattle that makes their value vulnerable to manipulation, the marketplace for cattle likewise is unique when compared to other agricultural commodities and highly susceptible to ill-conceived trade policies, antitrust activities and anticompetitive practices. The following are key characteristics of the U.S. cattle market that make it uniquely prone to such deplorable behavior.

1. The Beef Packing Industry Is Exceedingly Concentrated

As stated previously, 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."[50]

2. Regional Competition for Raw Products Like Cattle Is Less Intense than Is Competition in Processed Food Products

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.[51] Thus, the competition for slaughter-ready cattle is inherently fragile, even without the added burden of market power abuses from concentrated beef packers that wield considerable monopsony power.

Further, 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.[52] 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.[53] 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 by 3.18 percent.[54] These findings suggest that meaningful competition in the final

[49] 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.
[50] 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.
[51] *See* 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.
[52] *See* Examining Packer Choice of Slaughter Cattle Procurement and Pricing Methods, Oral Capps, Jr., et al., Agricultural and Resource Economics Review, April 1999, at 16.
[53] *See id*., at 16.
[54] *See* Examining Packer Choice of Slaughter Cattle Procurement and Pricing Methods, Oral Capps, Jr., et al., Agricultural and Resource Economics Review, April 1999, at 21.

cattle market may well be nonexistent in procurement regions where the RHHI was exceedingly high.

3. The U.S. Cattle Market Is Highly Sensitive to Even Slight Changes in Supply

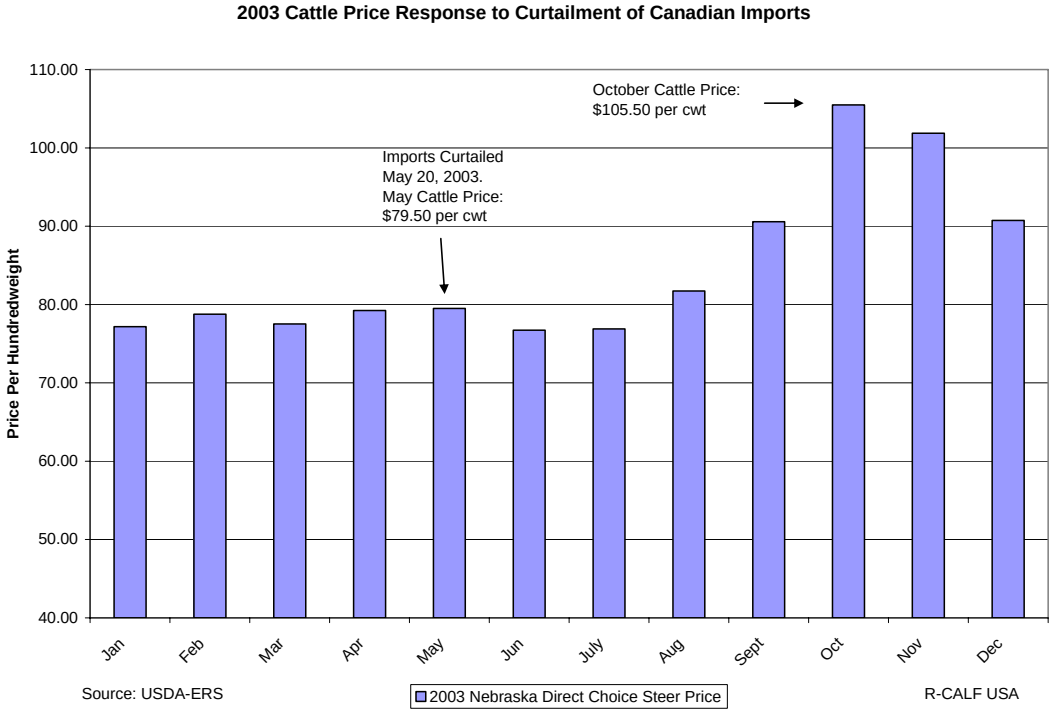
As confirmed by the USITC, the U.S. cattle market is highly sensitive to even slight changes in cattle supplies. The USITC found that the farm level elasticity of demand for slaughter cattle is such that "each 1 percent increase in fed cattle numbers would be expected to decrease fed cattle prices by 2 percent."[55] Researchers at the University of Nebraska – Lincoln found that fed cattle prices were even more susceptible to changes in supplies and stated that a 1 percent increase in fed cattle supplies would be expected to reduce fed cattle prices by up to 2.5 percent.[56] As a result, the U.S. cattle market is highly sensitive to the importation of cattle from foreign sources, and by extension, the importation of beef from foreign sources.

Recent experience shows that nominal U.S. fed cattle prices jumped to the highest level in the industry's history within just five months after the importation into the U.S. of live cattle from Canada was curtailed due to the discovery of bovine spongiform encephalopathy (BSE) in the Canadian cattle herd. The price for domestic cattle increased a remarkable $26 per cwt between May 2003, the month when Canadian cattle imports were curtailed, and October 2003, just five months later (chart 16). This domestic price increase occurred even after beef imports from Canada were resumed in August 2003. This price increase represents an unprecedented per head increase of $325 for an average Nebraska Direct Choice steer weighing 1,250 pounds.

[55] 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.

[56] *See* The Economics of Carcass Weight: A Classic Micro-Macro Paradox in Agriculture, Cornhusker Economics, Institute of Agriculture & Natural Resources, Department of Agriculture Economics, University of Nebraska – Lincoln, March 20, 2002, ("So, if quantity increased one percent from q1 to q2, and if demand remained constant, then price would be expected to decrease 1.4 to 2.5 percent).

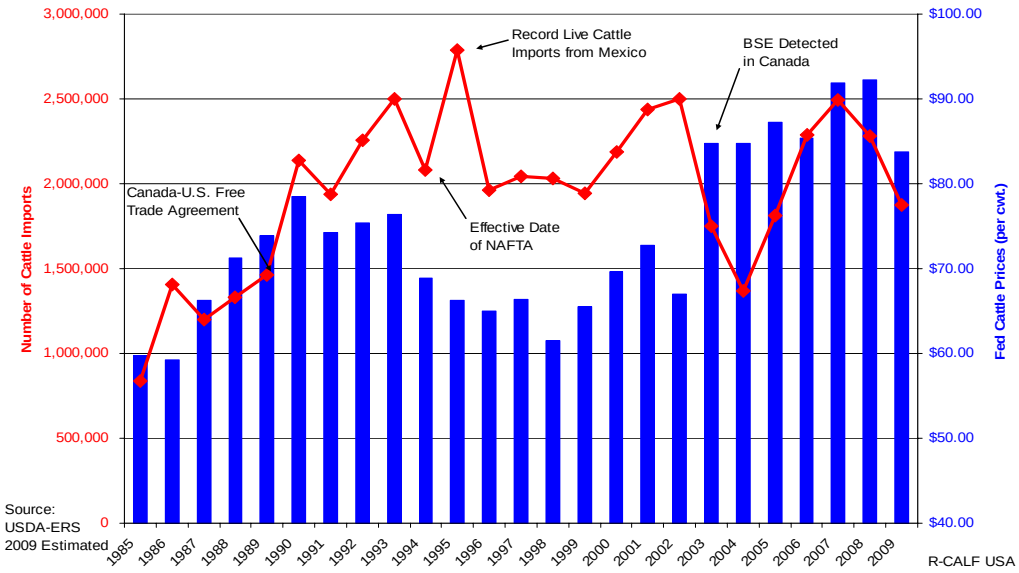
CHART 16



R-CALF USA urges the USITC to investigate the beef packers' practice of strategically using imported cattle to reduce the domestic price of fed cattle. Approximately 1.5 million cattle are imported annually from Canada,[57] representing approximately 4 percent of the 34 million cattle slaughtered annually in the United States. Yet, there appears a significant negative correlation between the number of head imported and the price of domestic cattle (chart 17).

[57] Livestock and Meat Trade Data, Cattle: Annual and Cumulative Year-to-Date U.S. Trade (Head), USDA, ERS (Canadian cattle imports totaled 1.4 and 1.6 million head in 2007 and 2008, respectively), available at http://www.ers.usda.gov/data/meattrade/CattleYearly.htm.

CHART 17: RELATIONSHIP BETWEEN CATTLE IMPORTS AND FED CATTLE PRICES



It does not appear that USDA currently has accurate modeling capabilities to evaluate the impact to the U.S. cattle industry from the beef packer's strategic use of imported cattle to manage domestic cattle prices. When USDA issued its 2005 final rule to allow Canadian cattle less than 30 months of age into the United States, it projected that the largest decline in U.S. fed cattle prices would occur in the first or second quarter of the year following the resumption of Canadian cattle imports. USDA estimated price declines during the first and second quarter ranging from a low of $3.10 per cwt. to a high of $6.05 per cwt.[58] However, during the third and fourth quarters following the resumption of Canadian cattle imports, U.S. fed cattle prices fell from $96.50 per cwt in December 2005 to $79.10 per cwt in May 2006, a decline of $17.40 per cwt – nearly three times greater than what USDA projected for the upper boundary of expected losses.[59]

It is evident that imported cattle have a more severe impact on domestic cattle prices than is currently estimated by USDA. Moreover, these imported cattle appear to defy the transportation limits that constrain the majority of shipments of domestic fed cattle to within approximately a 300-mile radius of beef packing plants. Based on information and belief, fed cattle from Canada are transported exceedingly long distances to packing plants in the United States. R-CALF USA speculates that U.S. beef packers likely are slaughtering these imported cattle at a loss in order to satisfy the weekly demand for live cattle, which would enable beef packers to avoid bidding more aggressively for domestic cattle. If this, in fact, is occurring, then the beef packer likely is more than making up the loss from the procurement of the relatively few imported cattle with the greater savings generated from holding prices for the much greater volume of domestic cattle below what a competitive market would otherwise dictate.

[58] *See* Economic Analysis Final Rule, Bovine Spongiform Encephalopathy: Minimal Risk Regions and Importation of Commodities, USDA, Animal and Plant Health Inspection Services, Dec. 20, 2004.
[59] *See* Choice Beef Values and Spreads and the All-Fresh Retail Value, USDA, ERS, available at http://www.ers.usda.gov/Data/meatpricespreads/Data/beef.xls, downloaded on December 19, 2006.

4. Beef Packers Create Market Access Risk for Sellers in the Final Cattle Market

The combination of packer concentration, the perishable nature of slaughter-ready cattle and the weekly bounding of demand creates market access risk for U.S. cattle producers within the U.S. cattle market. The 2007 GIPSA Livestock and Meat Marketing Study (LMMS) defines market access risk as "the availability of a timely and appropriate market outlet."[60] 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.[61]

The beef packers have already achieved the ability to create market access risk and now function as powerful gatekeepers between cattle producers and the final cattle market. Under the current level of beef packer concentration, there is already evidence that cattle 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],"[62] 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 . . ."[63]

Based on information and belief, it is market access risk that entices cattle feeders in the final cattle market to enter one or more of the captive supply arrangements offered by the beef packers. 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.[64] 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."[65] Based on this finding, U.S. live cattle producers are defenseless against the monopsony power exercised by the beef packers to shift ever increasing volumes of cattle from the cash market to one or more of the beef packers' captive supply procurement options.

5. The Price of Domestic Cattle Is Sensitive to Procurement Practices that Shift Cattle from the Cash Market to Captive Supply Arrangements

As confirmed by the LMMS, the cash cattle market is sensitive to shifts in cattle procurement methods. While beef packers have significantly reduced the number of its market outlet gatekeepers through horizontal consolidation, thus exacerbating market access risk for all cattle

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[60] 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.
[60] *See Ibid.*
[60] *Id*., at 2-36.
[61] *See Ibid.*
[62] *Id*., at 2-36.
[63] *Ibid*.
[64] 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.
[65] *Ibid*.

producers in the final cattle market, beef packers have simultaneously increased their use of non-traditional contracting and other cattle procurement methods that enable them to more effectively exercise their 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 purchasing cattle more than 14 days before slaughter (packer-fed cattle), forward contracts, and exclusive marketing and purchasing agreements, including formula contracts. 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.[66] And, use of these captive supply methods has been increasing rapidly, rising 37 percent from 1999 to 2002.[67] 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.[68] 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.[69] 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.[70] 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.[71] 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.

It is informative for the USITC to analyze the recent transformation of the U.S. hog industry. USDA data suggest that the contraction of the U.S. live hog industry was more severe than was experienced in the U.S. live cattle industry, despite a smaller four-firm concentration ratio in the pork packing industry. This likely is because of the 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 its 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 LMMS found that during the period October 2002 through March 2005, the pork packing industry captured 20 percent of its slaughter-ready hogs through the alternative

[66] *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.
[67] *See id.* at 3-17.
[68] *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.
[69] *See Ibid.*
[70] *See id*., at 8.
[71] *See Ibid.*

procurement method of direct ownership;[72] 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.[73] 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."[74] 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%.
>
> 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.[75]

The LMMS found that procurement methods that facilitated the exercise of market power by the concentrated pork packing industry are currently less developed in 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,[76] which, like in the hog market, 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 packing industry. 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.[77] The comprehensive econometric analysis documented in *Pickett v. Tyson Fresh Meats, Inc.*, which covered the period 1994-2004, showed

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[72] *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.
[73] *See Ibid.*
[74] *See id*., at ES-3.
[75] *See id*., at ES-2, 3.
[76] *See id*., at ES-4.
[77] *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.

an even greater sensitivity to shifts in cattle procurement. The analysis showed that for each 1% increase in captive supply cattle, cattle prices decreased 0.155%.[78]

CHART 18

Texas-Oklahoma-New Mexico Breakdown of Volume by Purchase Type					
	2005	2006	2007	2008	2009
Cash	47.2%	42.5%	36.7%	31.5%	26.1%
Formula	42.2%	42.2%	48.4%	53.3%	60.7%
Forward Contract	3.1%	5.0%	4.4%	5.8%	5.4%
Negotiated Grid	7.5%	10.3%	10.5%	9.3%	7.8%

Source: USDA Market News, St Joseph, MO

Kansas Breakdown of Volume by Purchase Type					
	2005	2006	2007	2008	2009
Cash	50.6%	47.3%	44.8%	41.7%	39.3%
Formula	44.8%	46.0%	48.5%	48.0%	52.6%
Forward Contract	2.8%	5.4%	5.4%	7.8%	7.1%
Negotiated Grid	1.8%	1.3%	1.3%	2.4%	1.0%

Source: USDA Market News, St Joseph, MO

Nebraska Breakdown of Volume by Purchase Type					
	2005	2006	2007	2008	2009
Cash	64.5%	63.7%	64.7	61.1%	60.4%
Formula	18.3%	16.8%	17.8%	17.8%	22.6%
Forward Contract	5.9%	9.7%	7.8%	14.7%	9.0%
Negotiated Grid	11.4%	9.7%	9.6%	6.5%	8.0%

Source: USDA Market News, St Joseph, MO

Alarmingly, the beef packers are now shifting unprecedented volumes of cattle from the cash market and to their forward contracts and formula contract schemes. USDA reports that in the Texas-Oklahoma-New Mexico region, the cash market in 2009 has been reduced to less than 34 percent (including cash and negotiated grid transactions) (chart 18). And, forward contracting and formula contracting now represents over 66 percent of all fed cattle transactions in the region. Similar shifts have occurred in the Kansas region while Nebraska remains the only regions where cash transactions represent more than 41 percent of fed cattle transactions.

Not reported in these USDA data are the volumes of packer-owned cattle procured from each of these regions. Nationally, GIPSA reports that in 2007, packer-owned cattle represented between 5 percent and 10 percent of the cattle procured by beef packers.[79] However, it is critical that decision makers understand that formula contracts accord beef packers nearly identical buying power as do packer-owned cattle. C. Robert Taylor, Auburn University, states that an affidavit contained in the *Pickett v. Tyson* litigation record reveals an acknowledgement by former IBP (now Tyson) CEO Bob Peterson on how formula contracts give beef packers comparable, if not superior, leverage in the market than do packer-owned cattle. Excerpts from Taylor's report of the affidavit include:[80]

On July 26, 1994 Peterson stated:

> *'I don't know if we should be proud or ashamed but I'm telling you we started formula pricing. Why did we do it? So we have the same leverage our competition had. And we feed cattle through the process of formula pricing.'*

[78] *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.
[79] *See* 2008 Annual Report, Packers & Stockyards Program, USDA, GIPSA, March 1, 2009, at 59, available at http://archive.gipsa.usda.gov/pubs/2008_psp_annual_report.pdf.
[80] The American Antitrust Institute, Working Paper No. 07-08, Legal and Economic Issues with the Courts' Rulings in Pickett v. Tyson Fresh Meats, Inc., a Buyer Power Case, C. Robert Taylor, Auburn University, at 9, available at http://www.antitrustinstitute.org/archives/files/AAI_Taylor_WP07-08_033020070955.pdf.

> *'Well, we aren't going to change. We will have formula—that is our way of feeding cattle.'*

On December 2, 1994, he said:

> *'… I told your industry right here at the KLA convention (in 1988) that if it allowed packers to feed their own cattle, IBP (Tyson) would do whatever was necessary to level the playing field. Ladies and gentlemen, the leveling is called formula and contract buying. Thus far, we have been able to partially offset the leverage our competitors have by the use of formula cattle and contract buying. Will we stop doing it? No. Will we feed cattle? If we have to. As most of you know, our recent purchase of Lakeside Farm Industries in Canada includes a feedyard. I am only trying to tell you one thing. IBP (Tyson) will do whatever is necessary to remain competitive.'*

These quotes directly contradict the belief that formula contracts were developed by cattle producers to provide them with additional marketing options, a belief that has been expressed to R-CALF USA in recent years. R-CALF USA urges decision makers to act swiftly to end the beef packers' anticompetitive practices of packer ownership of cattle and formula pricing.

6. The Demand for Live Cattle Is Bounded on a Weekly Basis

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.[81] As a result of this weekly constraint, packers can suppress the weekly demand for cattle offered in the domestic cash market by finishing off their weekly supply needs with green cattle (i.e., cattle that have not yet reached their optimal slaughter weight) pulled from their captive supply holdings or, as stated above, by finishing off their week with imported cattle. The effect of this practice is to hold down or lower domestic prices and prevent a higher starting price for the beginning of each subsequent week.

7. Price Transparency is Limited in the U.S. Cattle Market

Transparency in the U.S. live cattle market is already limited as found by the 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.[82] Included among the deficiencies identified was the exclusion of a large percentage of cattle transaction data.[83] In addition to the lack of transparency and accuracy of marketing

[81] *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).
[82] *See* 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).
[83] *See* U.S. Government Accountability Office, Livestock Market Reporting: USDA Has Taken Some Steps to

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 likely are masking critical pricing information. The confidentiality guidelines that likely restrict or eliminate the reporting of currently reported cattle transaction data 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.[84] It is inexplicable that concentrated packers are shielded from disclosing prices in any region in the United States and an investigation should be initiated to determine the extent to which unreported pricing data is impacting domestic cattle prices. In addition, the investigation should assess the disposition and impact of pricing data that result from transactions that occur outside the daily and weekly price reporting timeframes.

8. Beef Packers Have Superior Market Information, Particularly Those with Substantial Captive Supply Arrangements

As discussed above, the Livestock Mandatory Reporting system shields beef packers from disclosing market information under certain circumstances, thus affording them asymmetric information in the marketplace. In addition, beef packers with captive supplies have superior information than do cattle sellers regarding the number of additional cattle needed each week to maintain plant operations. Also, beef packers with contracts for the sale of beef to retailers are benefited by information regarding weekly output needs and future wholesale beef prices. The beef packers' access to critical marketing information not available to producers gives them considerable leverage over cattle sellers in the U.S. cattle market.

III. EVIDENCE OF EXTREME MARKET FAILURE IN THE U.S. CATTLE AND BEEF INDUSTRIES

The beef packers and their allied trade associations have long justified their ongoing attempts to capture greater control over the live cattle industry. Their claims include the achievement of increased efficiencies through economies of scale. And, as discussed above regarding TCFA's claim, they rationalize the adverse consequences of their actions, e.g., the exodus of industry participants and the dwindling cow herd, with claims of increased productivity that, they say, negates the need for the industry's previous numbers of either participants or cattle.

For example: in written testimony before the July 16, 2002, United States Senate Agriculture Committee hearing on packer ownership of livestock, the meatpacking industry's trade association, the American Meat Institute (AMI), testified: "Demand for consistent quality product has led many firms to exert greater control over the supply chain."

Ensure Quality, but Additional Efforts Are Needed, GAO-06-202 (Dec. 2005), at 10.

[84] USDA Announces New Confidentiality Guidelines for Livestock Mandatory Reporting Program, U.S. Department of Agriculture, Release No. 0132.01, August 3, 2001.

In its written testimony before the same July 16, 2002, Senate hearing, the National Cattlemen's Beef Association (NCBA) attached the executive summery of the Sparks Study to its testimony. Specifically, the NCBA commissioned Sparks Study states the following:

> Packers use ownership of livestock to help control unit costs in a variety of ways. If this management tool is restricted, unit costs can be expected to increase (without increasing the value of the final product).[85]

The Sparks Study asserts that direct ownership of livestock limits the packers' market risk, arguing that the futures market is insufficient for this purpose. Therefore, according to the Sparks Study, one of the few tools available to packers to offset the smaller margins associated with higher livestock prices is through direct ownership of raw production materials, i.e., livestock, which enables them to reduce their margin risk. The Sparks Study states, "The pressure to reduce costs force the search for low-cost livestock supplies (often at the expense of producer returns)."[86]

The Sparks Study adds additional insight into the packing industry's rational for supporting packer ownership of livestock as well as other means that contribute to vertical integration of their industry. The Sparks Study acknowledges:

> For many meat packers, integration between the packing and feeding stages of livestock production is seen as an effective vehicle to reduce market risk exposure and loss of such a valuable tool increases their costs . . .[87] and,
>
> Vertical integration often attracts investors because of the negative correlation between profit margins at the packing stage and the feeding stage.[88]

It is clear that the current market structure affords beef a distinct pricing advantage over the U.S. cattle market, and this pricing advantage is disrupting the competitiveness of the U.S. cattle industry. Also obvious is the inherent disadvantage faced by domestic cattle feeders that must first compete against the same beef packers when purchasing feeder cattle in the feeder cattle market that they must later sell to in the final cattle market when their cattle are finished.

Perhaps the most compelling testimony regarding the onset of packer ownership and the advent of captive supply procurement methods, and their implications, is again provided by C. Robert Taylor, Auburn University, who reports that the affidavit in the *Pickett v. Tyson* litigation record contains quotes from Bob Peterson, former CEO of the nation's largest meatpacker at the time – IBP. According to C. Robert Taylor, the affidavit filed in the *Pickett v. Tyson* lawsuit contains the following record of Peterson's statements:[89]

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[85] Sparks Companies Inc., "Potential Impacts of the Proposed Ban on Packer Ownership and Feeding of Livestock", A Special Study, (March 18, 2002) at 40.
[86] *Id*. at 22.
[87] *Id*. at 24.
[88] *Id*. at 24.
[89] The American Antitrust Institute, Working Paper No. 07-08, Legal and Economic Issues with the Courts' Rulings in Pickett v. Tyson Fresh Meats, Inc., a Buyer Power Case, C. Robert Taylor, Auburn University, available at http://www.antitrustinstitute.org/archives/files/AAI_Taylor_WP07-08_033020070955.pdf.

In a 1988 talk to the Kansas Livestock Association, Peterson maintained,

> *'…our competitors are promoting contracts … and seeking more. These (forward) contracts coupled with packer feeding could represent a significant percentage of the fed cattle during certain times of the year… Do you think this has any impact on the price of the cash market? … you bet! … We believe that it's having a significant impact on the market—on the cash market place.'*
>
> *'…we believe that some of those who are feeding cattle and using forward contracting are creating aberrations within the market place by coming in and out of the market; that is not reflecting the true value of the cash market.'*
>
> *'But with the packers in the feeding business and forward contracting, there's going to be a major, major shift against the leverage system.'*
>
> *'In my opinion the feeder can't win against the packer in the real fair play if we go into the feeding and the hedging program.'*
>
> *'Do you think that if we had a million cattle on feed and we thought cattle were going to get higher we'd kill ours first and wait for yours until last? Or do you think we'd kill yours first and wait for ours until last? Do you think if it's going down we're going to buy yours and wait for ours until last? This is pretty basic. Boy Scouts and Girl Scouts are nice, but when you get back to money in the bank and the facts, I'm telling you the facts.'*

In 1994, after IBP had entered into extensive captive supply arrangements, Peterson stated:

> *'… not formula cattle but packer-fed cattle, which can be killed early or late to fill a particular time frame, be it a day or a week grant the packer far greater flexibility to move in and out of the market. On the way down (in price), he kills his cattle first and on the way up, last.'*

Armed with industry concentration, packer-owned cattle and their new cattle procurement schemes since the late '80s, the dominant beef packers have created a marketplace now replete with evidence of market failure caused by abusive monopsony power that is harming cattle producers and beef consumers alike.

1. The Disparity in Economic Power Between Disaggregated U.S. Cattle Producers and the Highly Concentrated Beef Commodity Industry has all but Destroyed the Competitiveness of the U.S. Cattle Industry

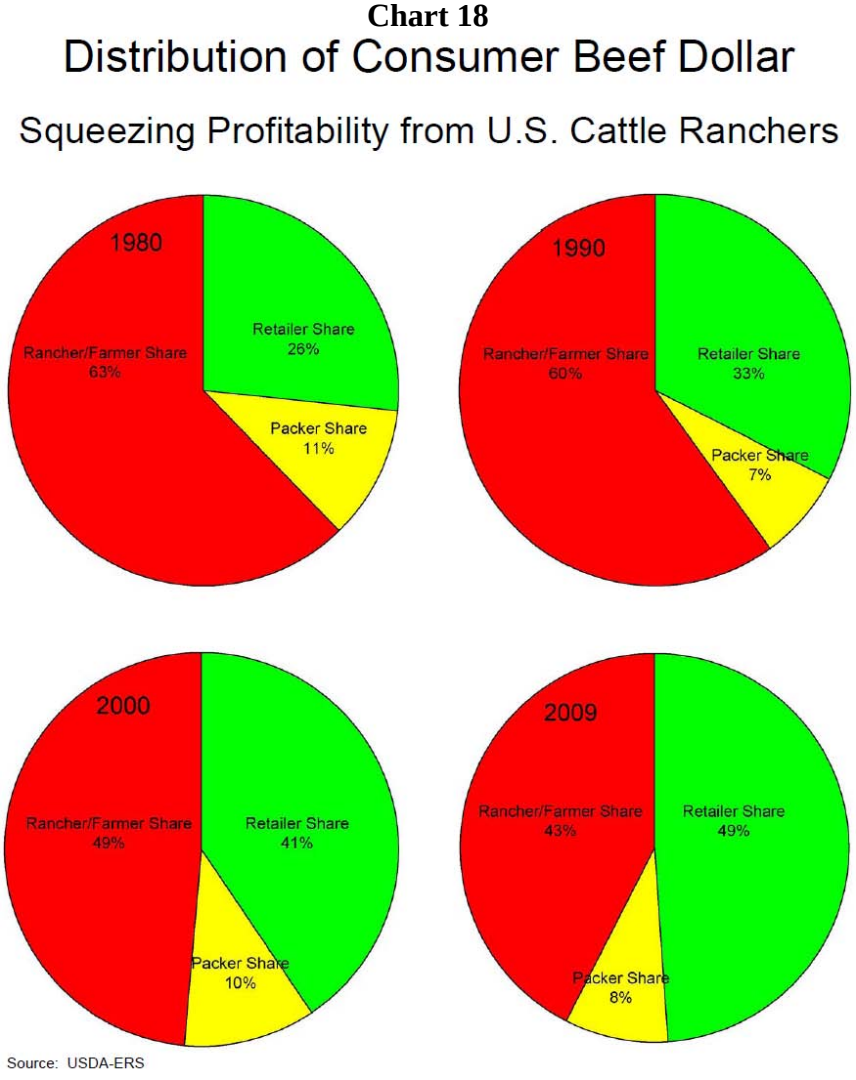
In 1980, U.S. cattle producers who sold cattle into the beef commodity industry received 63 percent of each dollar paid by consumers for retail beef cuts derived from a "standard animal, cut up in a standard way at the packing plant, and sold in standard form through the retail store."[90] R-CALF USA refers to this percentage as the producers' share of the consumers' beef dollar. The producers' share of the consumers' beef dollar fell in 2009 to the lowest level in history. In 2009, the producers' share of the consumers' beef dollar, for the same standard animal and the same standard cuts that were measured in 1980, fell to only 42.5 percent[91] (chart 18).

Data calculated by USDA Economic Research Service (ERS) to determine the producers' share are not influenced by an increase in value-added beef products.[92] The ERS emphatically states: "Analysts who cite increasing value-added as a factor in pork and beef price spreads misunderstand how these are calculated."[93] Thus, the producers' lost share of the consumers' beef dollar indicates that someone in the beef supply chain is capturing the cattle producers' competitive market share of the value of retail beef. This is evidence of severe market failure, which failure is exacerbated by increased imports and a price-depressing deficit. If U.S. cattle producers received the same share of the consumers' beef dollar in 2009 that they received in

[90] Beef and Pork Values and Price Spreads Explained, USDA, ERS, May 2004, at 4, available at http://www.ers.usda.gov/publications/ldp/APR04/ldpm11801/ldpm11801r.pdf.
[91] *See* Beef Values and Price Spreads Data Sets, U.S. Department of Agriculture, Economic Research Service, available at http://www.ers.usda.gov/Data/meatpricespreads/
[92] *See* Beef and Pork Values and Price Spreads Explained, USDA, ERS, May 2004, at 2, available at http://www.ers.usda.gov/publications/ldp/APR04/ldpm11801/ldpm11801r.pdf.
at 2.
[93] *Ibid.*

1980, the value of their fed cattle would have been $120 per cwt, which is $36.50 per cwt above the actual 2009 five-market steer price of $83.50 per cwt.[94] The restoration of the producers' lost share of the consumers' beef dollar would have resulted in an increase of over $450 for each head of fed cattle sold in 2009, an increase that would have jumpstarted the economies of rural communities all across America.

Chart 18



[94] *See* Beef Values and Price Spreads Data Sets, U.S. Department of Agriculture, Economic Research Service (calculation based on 2009 Choice retail beef value at 426.0 cents per pound: (426.0 x .63) + byproduct value of 19.4 divided by 2.4 ERS conversion factor = $120 per cwt.), available at http://www.ers.usda.gov/Data/meatpricespreads/

In addition to its clarification that the price spread data used to calculate the producers' share of retail beef is not influenced by increased value-added beef products, the ERS further states that its price spread data can be used to "measure the efficiency and equity of the food marketing system,"[95] noting that "increasing price spreads can both inflate retail prices and deflate farm price."[96] The price spreads between ranch gate prices (i.e., cattle prices) and wholesale prices (i.e., prices received by beef packers) and ranch gate and retail prices (i.e., prices paid by consumers) have steadily increased over time (chart 19). According to ERS, "[h]igher price spreads translate into lower prices for livestock,"[97] innovative technologies can reduce price spreads and economic efficiency increases when price spreads drop,[98] and "[b]oth consumers and farmers can gain if the food marketing system becomes more efficient and price spreads drop."[99]

It is clear that both consumers and producers are being harmed by the current system that is creating increased price spreads, which means the marketplace is becoming less innovative and less efficient. USDA found in 2004 that "the total price spreads show a weak upward trend when corrected for inflation,"[100] and this upward trend has only worsened since 2004. The ever-increasing price spread between ranch gate values for cattle and retail prices for beef is evidence of market failure caused by the exercise of market power, which is exacerbated by increased imports, that is exploiting both U.S. consumers and U.S. cattle producers.

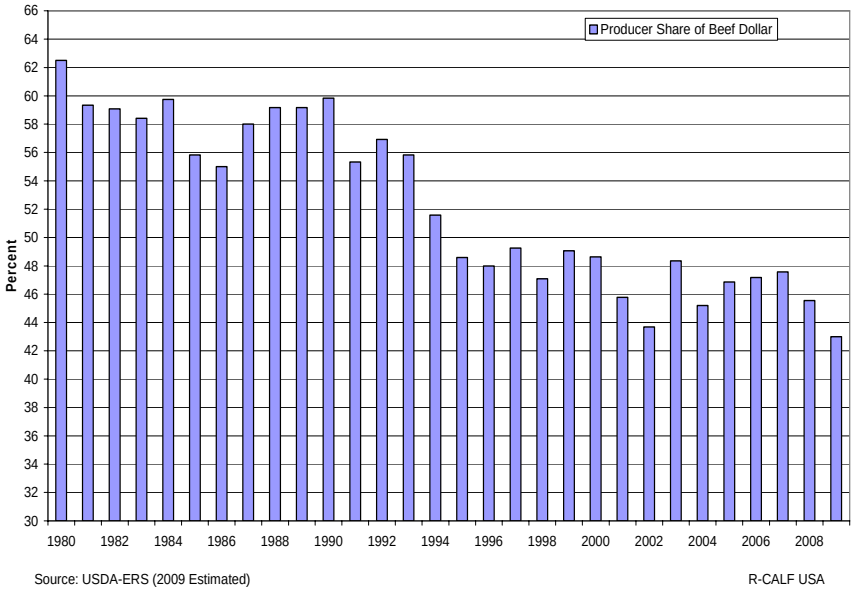
[95] Beef and Pork Values and Price Spreads Explained, U.S. Department of Agriculture, Economic Research Service, at 3.
[96] *Id*. at 2.
[97] *Id.*, at 8.
[98] Id., at 3.
[99] *Ibid*.
[100] *See* Beef and Pork Values and Price Spreads Explained, U.S. Department of Agriculture, Economic Research Service, at 10.

A. The Lost Share of the Consumer's Beef Dollar Is Evidence of Market Failure

In 1980, U.S. cattle farmers and ranchers who sold cattle in the final cattle market received 63 percent of each dollar paid by consumers for retail beef cuts derived from a "standard animal, cut up in a standard way at the packing plant, and sold in standard form through the retail store." [101] R-CALF USA refers to this percentage as the producers' share of the consumers' beef dollar. Based on the producers' monthly average share of the consumers' beef dollar from January 2009 through November 2009, the producers' share of the consumers' beef dollar, for the same standard animal and the same standard cuts that were measured in 1980, will fall to only 43 percent in 2009, representing a 20 percent decline (chart 19).

These data calculated by USDA Economic Research Service (ERS) are not influenced by an increase in value-added beef products.[102] The ERS emphatically states: "Analysts who cite increasing value-added as a factor in pork and beef price spreads misunderstand how these are calculated."[103] Thus, the producers' lost share of the consumers' beef dollar indicates that someone in the beef supply chain is capturing the cattle producers' competitive market share of the value of retail beef. This is evidence of severe market failure caused by abusive monopsony power. If U.S. cattle producers in November 2009 received the same share of the consumers' beef dollar they received in 1980, the nominal value of their fed cattle would have been $122 per cwt, which is $37 above the actual November 2009 5-market steer price of $84.50 per cwt.[104]

CHART 19: U.S. Cattle Producers' Share of Consumers' Beef Dollar
1980-2009



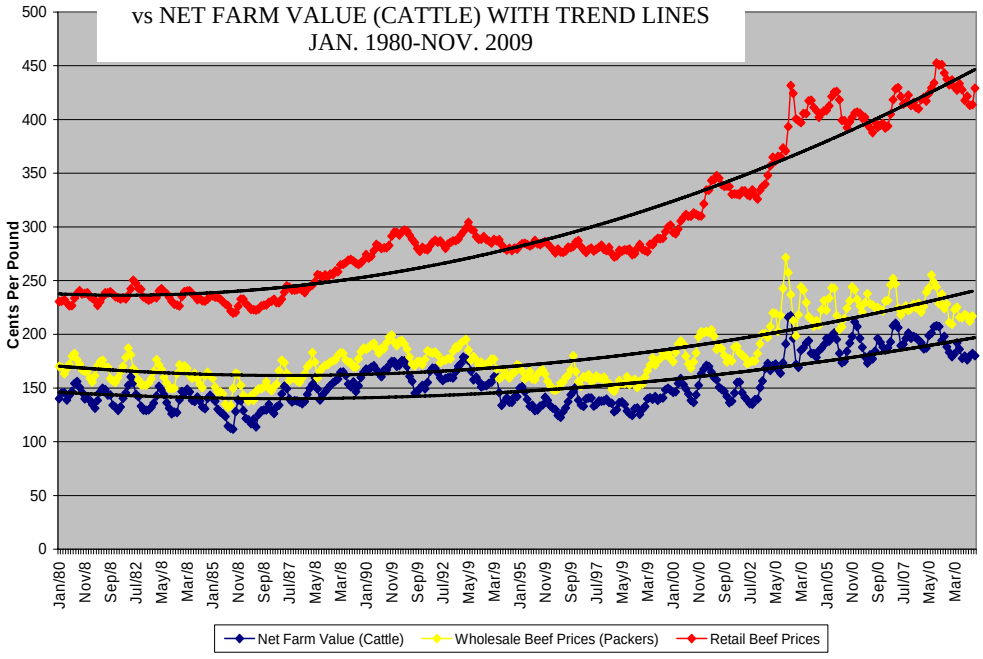
Source: USDA-ERS (2009 Estimated) R-CALF USA

[101] Beef and Pork Values and Price Spreads Explained, USDA, ERS, May 2004, at 4, available at http://www.ers.usda.gov/publications/ldp/APR04/ldpm11801/ldpm11801r.pdf.
[102] *See id*., at 2.
[103] *Ibid.*
[104] *See* Beef Values and Price Spreads Data Sets, U.S. Department of Agriculture, Economic Research Service (calculation based on Nov. 2009 Choice retail beef value at 429.2 cents per pound: (429.2 x .63) + byproduct value of 22.6 divided by 2.4 ERS conversion factor = $122.1 per cwt.), available at http://www.ers.usda.gov/Data/meatpricespreads/

B. Increasing Price Spreads Between Ranch Gate and Wholesale, and Ranch Gate and Retail Are Evidence of Market Failure

In addition to the clarification that its price spread data is not influenced by increased value-added beef products, the ERS further states that its price spread data can be used to "measure the efficiency and equity of the food marketing system,"[105] and "increasing price spreads can both inflate retail prices and deflate farm price."[106] The price spreads between ranch gate prices (i.e., cattle prices) and wholesale prices (i.e., prices received by beef packers) and ranch gate and retail prices (i.e., prices paid by consumers) have been steadily increasing over time (chart 20). According to ERS, "[h]igher price spreads translate into lower prices for livestock,"[107] innovative technologies can reduce price spreads and economic efficiency increases when price spreads drop,[108] and "[b]oth consumers and farmers can gain if the food marketing system becomes more efficient and price spreads drop."[109]

CHART 20: RETAIL BEEF PRICES vs WHOLESALE PRICES vs NET FARM VALUE (CATTLE) WITH TREND LINES JAN. 1980-NOV. 2009



It is clear that both consumers and producers are being harmed by the current system that is creating increased price spreads, which means the marketplace is becoming less innovative and less inefficient. USDA found in 2004 that "the total price spreads show a weak upward trend when corrected for inflation,"[110] and this upward trend has only worsened since 2004. The ever-increasing price spread between ranch gate values for cattle and retail prices for beef is evidence of market failure caused by the exercise of market power that is exploiting both consumers and producers.

C. The Disconnect Between Cattle Prices and Beef Prices Is Evidence of Market Failure

[105] Beef and Pork Values and Price Spreads Explained, U.S. Department of Agriculture, Economic Research Service, at 3.
[106] *Id*. at 2.
[107] *Id.*, at 8.
[108] Id., at 3.
[109] *Ibid*.
[110] *See* Beef and Pork Values and Price Spreads Explained, U.S. Department of Agriculture, Economic Research Service, at 10.

C. Robert Taylor, economist at Auburn University, compared inflation adjusted prices for fed cattle to the inflation adjusted prices for retail beef from 1947 to 2008 (chart 21). His comparison shows a close, synchronous relationship between the price index for cattle and the price index for beef from about 1960 to 1985, after which two significant changes occurred: First, the beef price index rose above the cattle price index. Second, the synchronous relationship between the two indices ended and the spread between the indices has increased through 2008. These two changes: a clear disconnect between cattle and beef prices and the ever-widening spread between the two indices, is evidence of market failure caused by abusive monopsony power.

Chart 21 reveals another important phenomenon: from the late '80s to the 2003-2004 timeframe, the fed cattle price index was in a death spiral, while the beef price index remained comparatively constant. In 2003 an anomaly occurred in the U.S. cattle market when imports of Canadian cattle and beef were temporarily suspended following the discovery of BSE in Canada. Suddenly, U.S. beef packers were unable to access their captive supply cattle in Canada for slaughter in the United States. As indicated by the abrupt upward spike in the fed cattle index in the 2003-2004 timeframe, the death spiral illustrated by the fed cattle price index was reversed. R-CALF USA believes the curtailment of Canadian cattle imports in 2003 caused the beef packers to lose the significant control accorded them by those imports over the price of domestic cattle. As a result, the beef packers' control over U.S. cattle prices temporarily slipped through their fingers and the U.S. cattle industry was serendipitously granted a temporary reprieve from the beef packers' abusive market power. The relationship between fed cattle prices and retail beef prices in 2009, however, strongly suggests that U.S. beef packers have now reacquired their significant control over the U.S. cattle market and are again exerting their abusive monopsony power over the U.S. cattle industry.

CHART 21: (Chart Legend: Black Line-Cattle Prices, Red Line-Beef Prices)

D. Long-Run Losses In the Final Cattle Market While Retail Beef Prices Remain at or Near Record Levels Is Evidence of Market Failure

According to USDA's High Plains Cattle Feeding Simulator, during the 37-month period from November 2006 through November 2009, U.S. cattle feeders who sold cattle in the final cattle market enjoyed only 7 profitable months and suffered 30 months of losses (chart 22). From July 2007 through March 2009 these cattle feeders suffered 22 months of consecutive losses, with losses at about $300 per head during October 2008 through January 2009. Meanwhile, Choice retail beef prices, throughout this entire period, increased until reaching record highs in 2008 and have remained near those record high levels through November 2009.

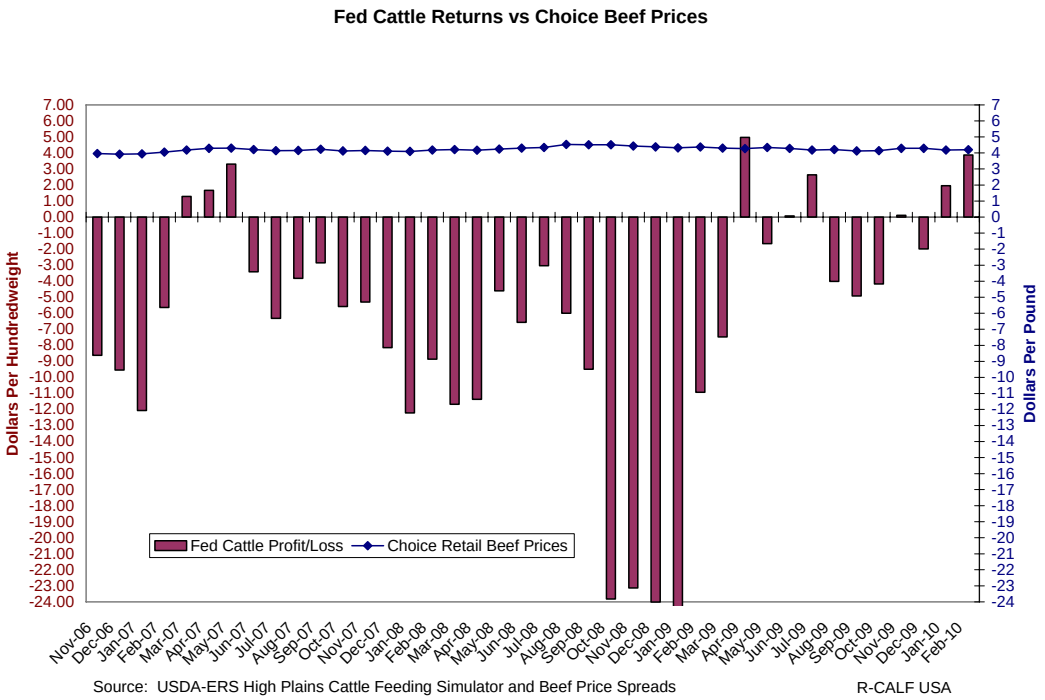
These data show that the U.S. cattle feeding sector alone lost $6.4 billion since Jan. 1, 2007, which does not begin to include the consequential losses suffered in the feeder cattle market since that time.[111] This conservative estimate of loss is based on USDA data that show the average loss from each of the 49 million head of fed cattle sold by U.S. cattle feeders was over $48 in 2007, over $150 in 2008, and over $65 in 2009.[112]

R-CALF USA is deeply concerned that these persistent losses likely have forced thousands, if not tens of thousands, of farmer-feeders to exit the industry in 2009. These farmer-feeders are less likely to have the deep pockets that their larger, corporate feedlot counterparts have to withstand such persistent and severe losses. These horrendous losses to cattle feeders while consumers continue to pay at or near record prices for beef are evidence of market failure caused by abusive monopsony power.

[111] The loss of over $6.4 billion was calculated by adding the average annual losses for each year as reported in the High Plains Cattle Feeding Simulator since Jan. 1 2007, and multiplying each year's loss by the number of fed cattle slaughtered during each year, e.g., the annual loss in 2008 was calculated by multiplying the 27 million fed cattle slaughtered in 2008 by that year's average annual per head loss to cattle feeders of $150.75 per head for each 1,250 pound animal sold, resulting in a total loss of $4.07 billion during that year alone.

[112] *See* High Plains Cattle Feeding Simulator, Data Sets, USDA, ERS, available at http://www.ers.usda.gov/Publications/LDP/LDPTables.htm ; *see also*, Livestock Slaughter 2008 Summary, USDA, NASS, March 2008, at 13, available at http://usda.mannlib.cornell.edu/usda/current/LiveSlauSu/LiveSlauSu-03-06-2009.pdf (The U.S. slaughtered approx. 27 million steers and heifers, not including cows and bulls, in each of the years 2007 and 2008.); *see also* Livestock Slaughter, USDA, NASS, August 2009, at 10, available at http://usda.mannlib.cornell.edu/usda/nass/LiveSlau//2000s/2009/LiveSlau-08-21-2009.pdf (The U.S. slaughtered approx. 15 million steers and heifers from Jan. through July, 2009.).

CHART 22



E. Record Beef Prices Paid by Consumers while Cow/Calf Producers Receive Severely Depressed Prices in the Feeder Cattle Market Is Evidence of Market Failure

While fed cattle sellers in the final cattle market suffered horrendous, long-run losses at the same time consumers continued to pay record and near-record prices for beef, sellers in the feeder cattle market likewise suffered losses due to severely depressed prices for their lighter feeder calves. In 2008 and 2009, the average monthly prices for Choice retail beef remained well above the previous five-year average (2003-2007), reaching record highs in the second-half of 2008 and remaining at historically high levels through November 2009 (chart 23 (a)).

Despite persistently high Choice retail beef prices paid by consumers, U.S. cow/calf producers in 2008 and 2009 who sold their cattle in the feeder cattle market were relegated to a market that returned prices well below the previous five-year average (2003-2007) (chart 23 (b)). Only during the first 5 months of 2008 did cow/calf producers who sold cattle weighing between 500 pounds and 600 pounds receive prices above the previous five-year average. From June 2008 through November 2009, these cattle producers have received persistently low prices. These depressed prices that have now permeated the feeder cattle market while consumers pay record and near record prices for beef is evidence of severe market failure caused by abusive monopsony power.

CHART 23 (a)

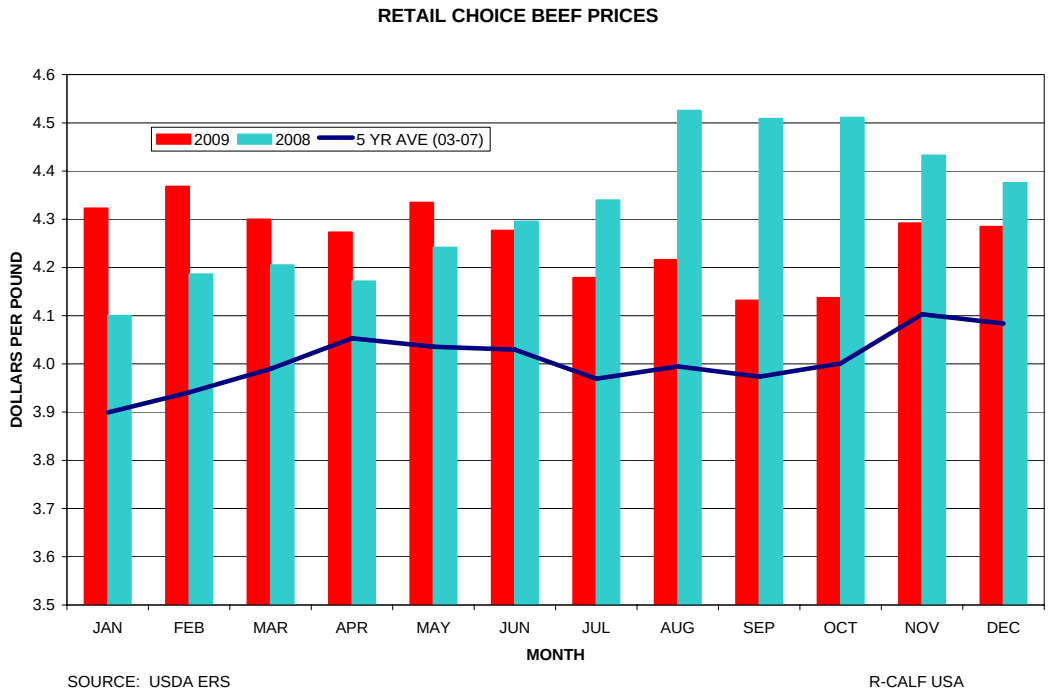
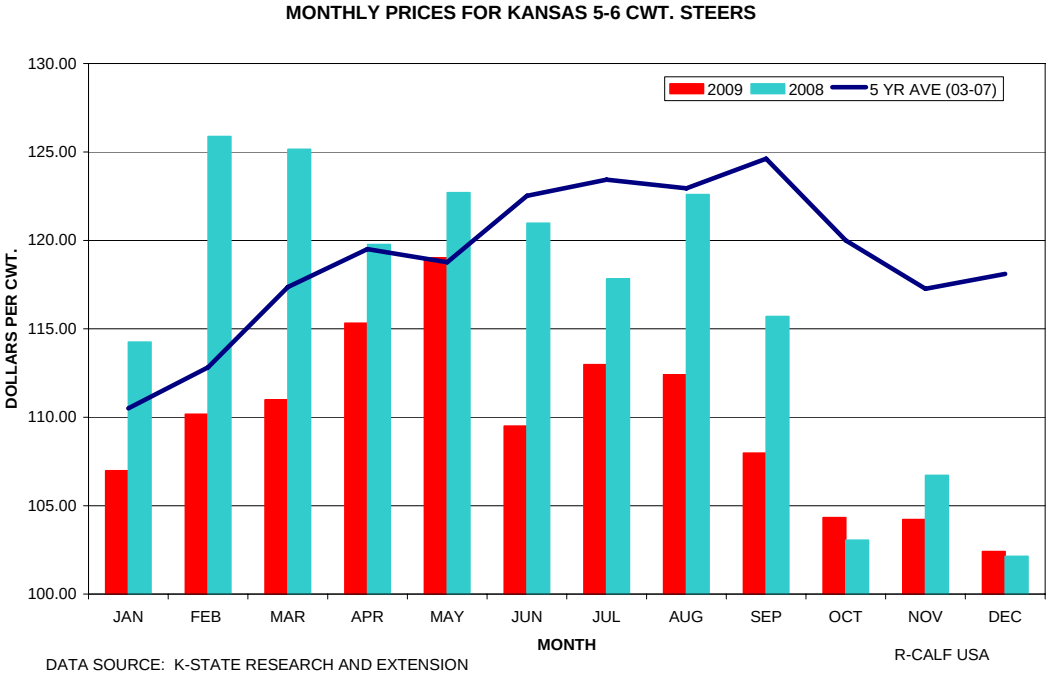


CHART 23 (b)



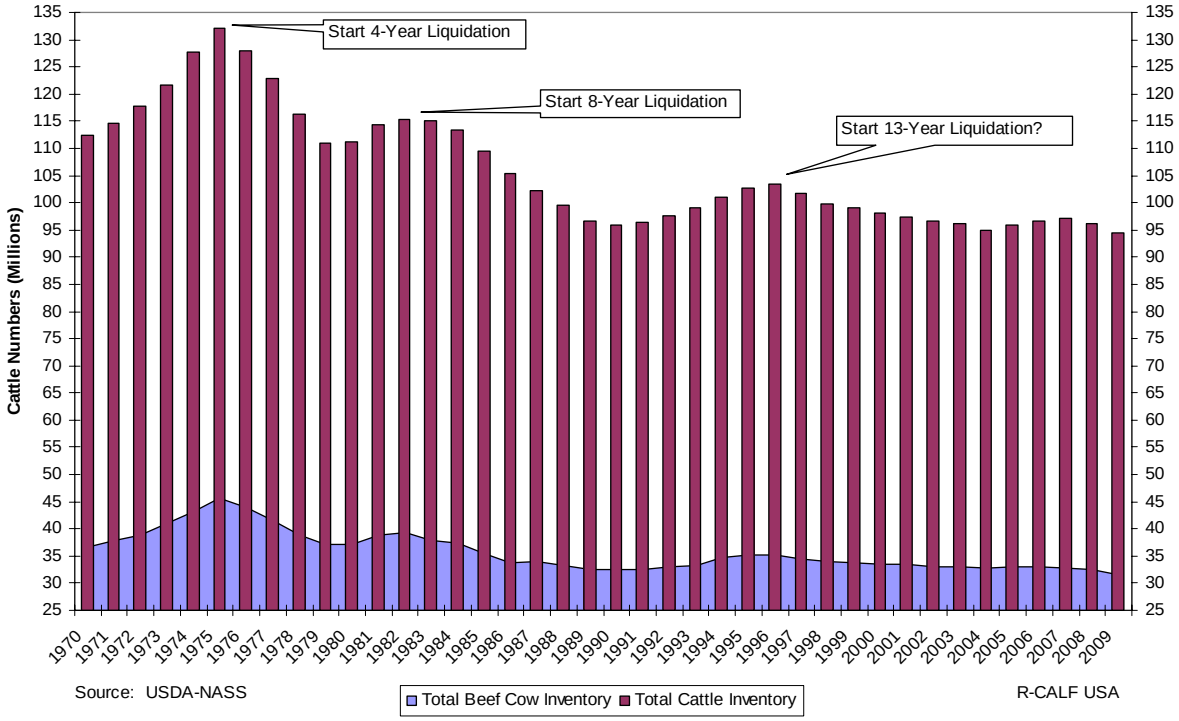
F. The Disruption of the U.S. Cattle Cycle Is Evidence of Market Failure

The GAO explains that the U.S. 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."[113] The cattle cycle historically occurred every 10-12 years, a function of the long biological cycle for cattle. USDA reports it consists of about 6 to 7 years of expanding cattle numbers, followed by 1 to 2 years in which cattle numbers are consolidated, then 3 to 4 years of declining numbers before the next expansion begins again.[114] In 2002 USDA acknowledged that "the last cycle was 9 years in duration; the present cycle is in its thirteenth year, with two more liquidations likely."[115]

Given its historical responsiveness to the competitive forces of supply and demand, the cattle cycle is the bellwether indicator of the competitiveness of the U.S. cattle industry. The last normal liquidation phase of the U.S. cattle cycle began in 1975 and ended in 1979, lasting the typical four years (chart 24). The next liquidation phase began in 1982 and ended in 1990, lasting an unprecedented eight years. The liquidation phase that began in 1996 is ongoing today and has lasted an unprecedented 13 years, though it unsuccessfully tried to recover during 2005 through 2007 in response to the anomalous curtailment of Canadian cattle imports. In late 2007, 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."[116]

[113] 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.
[114] Kenneth H. Mathews, Characteristics of Cattle Cycles, USDA, ERS, U.S. Beef Industry/TB-1874, November 2001.
[115] 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.
[116] Livestock, Dairy, & Poultry Outlook, USDA, ERS, Dec. 19, 2007, at 5, available http://www.ers.usda.gov/Publications/LDP/2007/12Dec/ldpm162.pdf.

Chart 24: Total U.S. Cattle Inventory and Beef Cow Inventory, January 1



There is no question that the historical cattle cycle is now disrupted, and the obvious trend since 1975 is an ever-shrinking cattle herd. It also is clear that the competition-induced demand/supply signals that once led to expectations about changes in cattle prices are no longer functioning properly. While cattle industry analysts ponder this phenomenon, in February 2008 USDA attributed a similar disruption that was occurring in the U.S. hog cycle to the hog industry's new structure. 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."[117] This "dramatically" changed structure includes the consolidation of the industry, where "fewer and larger operations account for an increasing share of total output."[118]

As *was* the case in the hog industry, a functioning cattle cycle, itself, is recognized by USDA as 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

[117] Livestock, Dairy, & Poultry Outlook, USDA, ERS, Feb. 15, 2008, at 14, available at http://www.ers.usda.gov/Publications/LDP/2008/02Feb/ldpm164.pdf.
[118] Hog Operations Increasingly Large, More Specialized, Amber Waves, USDA, ERS, February 2008, available at http://www.ers.usda.gov/AmberWaves/February08/Findings/HogOperations.htm.

> 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.[119]

The recently acknowledged disruption of the historical U.S. cattle cycle, as discussed above, is clear evidence that competition has been severely reduced in the U.S. cattle market and, as 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 disrupted cattle cycle is clear evidence of market failure caused by abusive monopsony power.

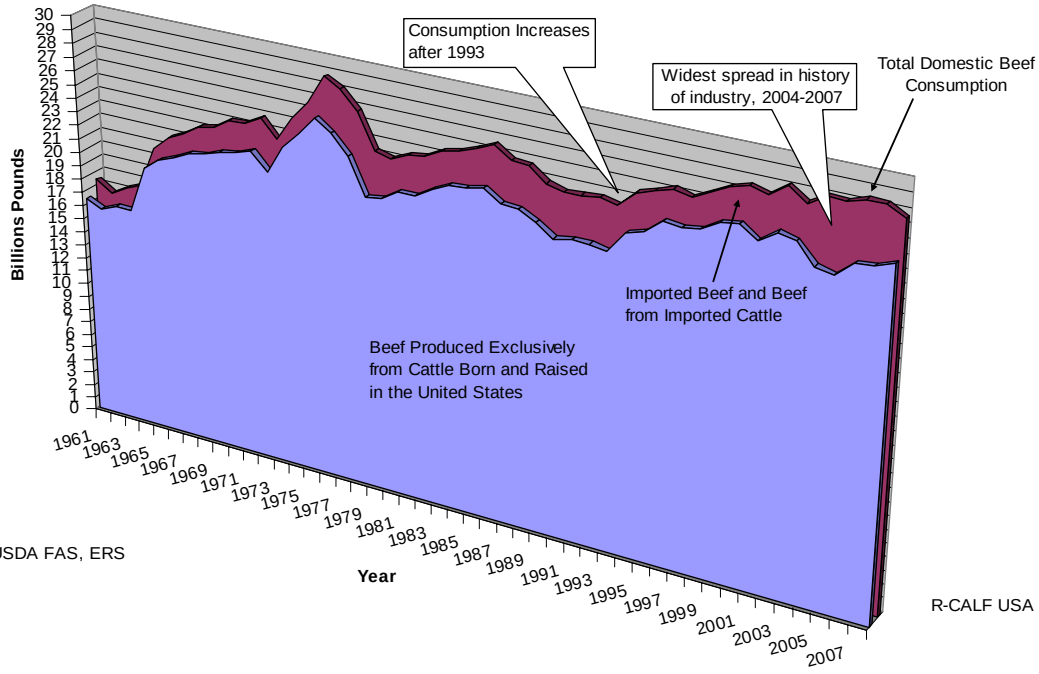
G. A Shrinking Cattle Industry with Stagnant Production in the Face of Growing Domestic Beef Consumption Is Evidence of Market Failure

Total domestic beef consumption peaked in 1976, subsided, and then began increasing significantly after 1993 (chart 25). In a competitive cattle industry, production would be expected to increase when beef consumption increases. However, the production of beef produced from cattle exclusively born, raised and slaughtered in the United States has not kept pace with the nation's appetite for beef. As stated above, since 1996 domestic beef production has remained relatively stagnant, though beef consumption has risen in recent years to nearly its peak 1976 level. In fact, from 2004 through 2007, the U.S. cattle industry experienced the largest shortfall in its history between its domestic beef production and the nation's beef consumption.

The shortfall in domestic production is being satisfied with imported beef and beef derived from imported cattle slaughtered in the United States. Thus a growing shortfall in domestic production means the U.S. cattle industry is losing market share in its own market and U.S. production is being systematically supplanted by foreign production. The domestic cattle industry would not be constrained from meeting the increase in consumption in its own market if the industry were competitive. The fact that the cattle industry is so constrained, as evidenced by the ongoing liquidation of its cattle herd and its stagnant production while consumption has increased, is evidence of severe market failure caused by abusive monopsony power.

[119] Cattle: Background, Briefing Room, USDA, ERS, updated June 7, 2007, available at http://www.ers.usda.gov/Briefing/Cattle/Background.htm.

CHART 25: Domestic Consumption in Excess of Domestic Production
1961-2008



H. Depressed Cattle Prices While Exports Reach Record Levels is Evidence of Market Failure

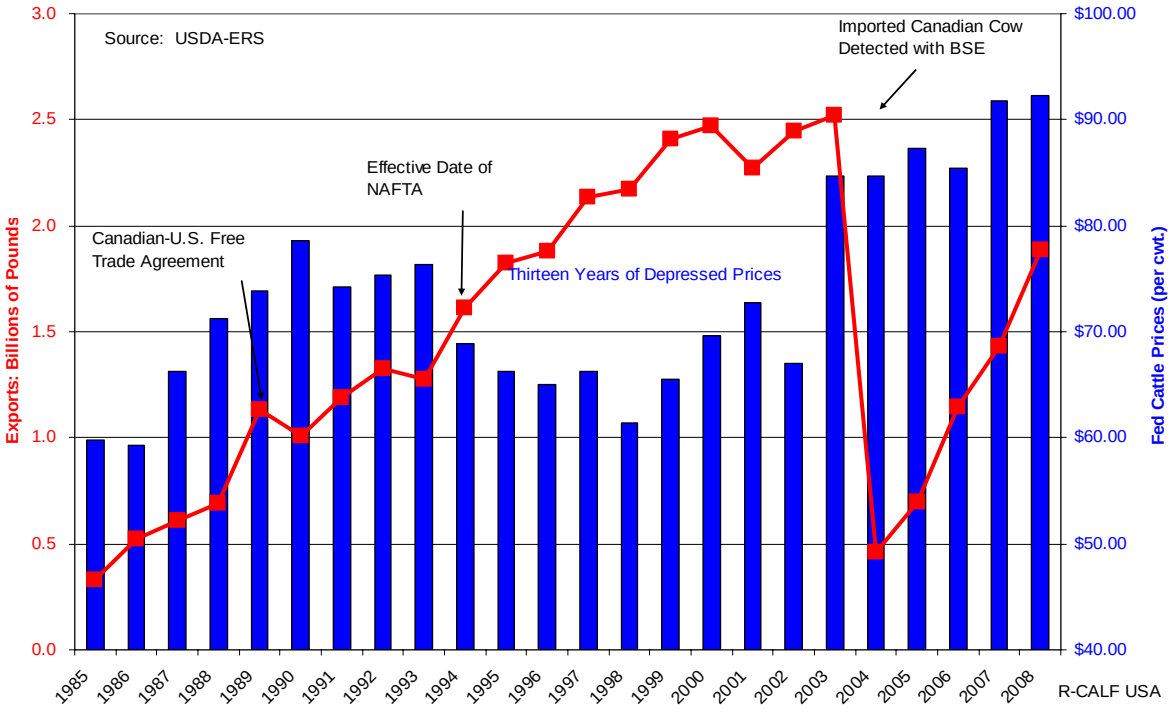
The beef packing industry has long assured the U.S. cattle industry that domestic cattle prices increase when U.S. beef exports increase. The NCBA testified before the USITC in November 2007 that, "In fact, the industry 'rule of thumb' is that U.S. beef exports in 2003 added about $15/cwt or $180 to each and every one of the roughly 27 million steers and heifers marketed that year."[120] The NCBA also asserted that the $15 per cwt added export value to fed cattle translates into a $22.20 per cwt (or $166.50 per head) increase in the value of a 750 pound steer, and an increase of $28.20 per cwt (or $155.10 per head) increase in the value of a 550 pound steer.[121]

These beef-packing industry assertions regarding the benefits to live cattle producers from exports at 2003 levels are unfounded and demonstrably false. United States beef exports in the years leading up to 2003 were, in fact, comparable to 2003 levels at approximately 2.4 billion pounds in 1999, 2.5 billion pounds in 2000, 2.3 billion pounds in 2001, 2.5 billion pounds in

[120] Memorandum of Record, Investigation No. 332-488, Concerning: Global Beef Trade: Effects of Animal Health, Sanitary, Food Safety, and Other Measures on U.S. Beef Exports, U.S. International Trade Commission, Nov. 15, 2007.
[121] *See* Special Report: How do Canadian Beef Imports Affect Our Business? Greg Doud, Chief Economist, NCBA, Issues Update 2004, Trade/Marketing/Economics, May-June 2004, available at https://www.beefusa.org/uDocs/canadian_20beef_20imports_20-_20mayjune_202004.pdf.

2002, and 2.5 billion pounds in 2003.[122] Yet, the prices for U.S. fed cattle in the years leading up to 2003 were severely depressed: Per hundredweight Nebraska Direct Choice steer prices were only $67.56 in 1999, $69.65 in 2000, $72.71 in 2001, $67.04 in 2002, and then jumped to $84.69 in 2003 following the curtailment of Canadian cattle imports that occurred on May 20 of that year.[123] However, when U.S. beef exports fell to less than half a billion pounds in 2004, falling to a 19-year low, U.S. fed cattle prices rose to their highest nominal levels in history (chart 26), and so too did prices for all classes of cattle, including 750-weight and 550-weight cattle. Clearly, the economic benefits of increased beef exports are being captured by beef packers *before* they can reach the U.S. cattle market. The fact that historical evidence proves that increased beef exports *do not* translate into increased cattle prices, even when a competitive market would predict they should, is clear evidence of market failure caused by abusive monopsony power.

CHART 26: Relationship Between Export Volumes and Fed Cattle Prices



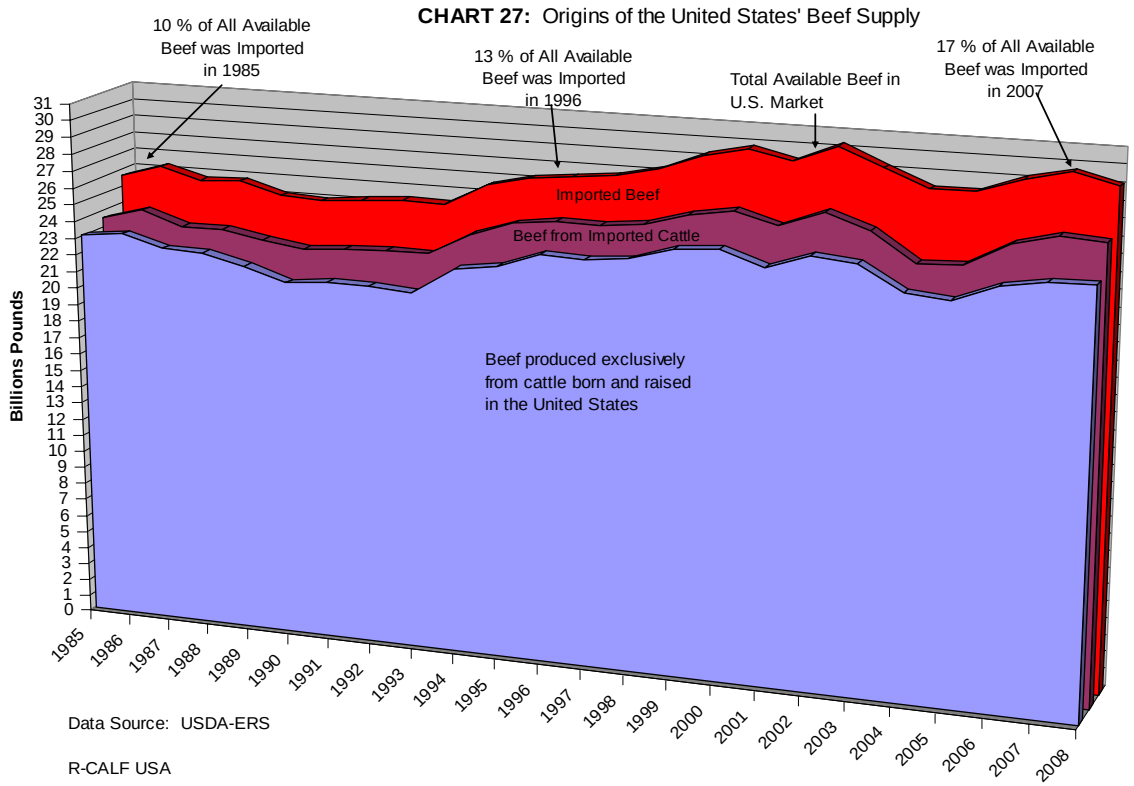
I. A Shrinking Cattle Industry That Is Simultaneously Losing Its Market Share of the Total Available Beef Supply Is Evidence of Market Failure

The total available beef supply includes all beef in the U.S. market that is available for domestic consumption and export. The phenomenon described immediately above, whereby cattle

[122] *See* Beef and veal: Annual and cumulative year-to-date U.S. trade (carcass weight, 1,000 pounds), Data Sets, U.S. Department of Agriculture Economic Research Service, available at http://www.ers.usda.gov/data/meattrade/BeefVealYearly.htm.

[123] *See* Livestock Prices, Red Meat Yearbook Data Sets, U.S. Department of Agriculture Economic Research Service, available at http://usda.mannlib.cornell.edu/MannUsda/viewDocumentInfo.do?documentID=1354.

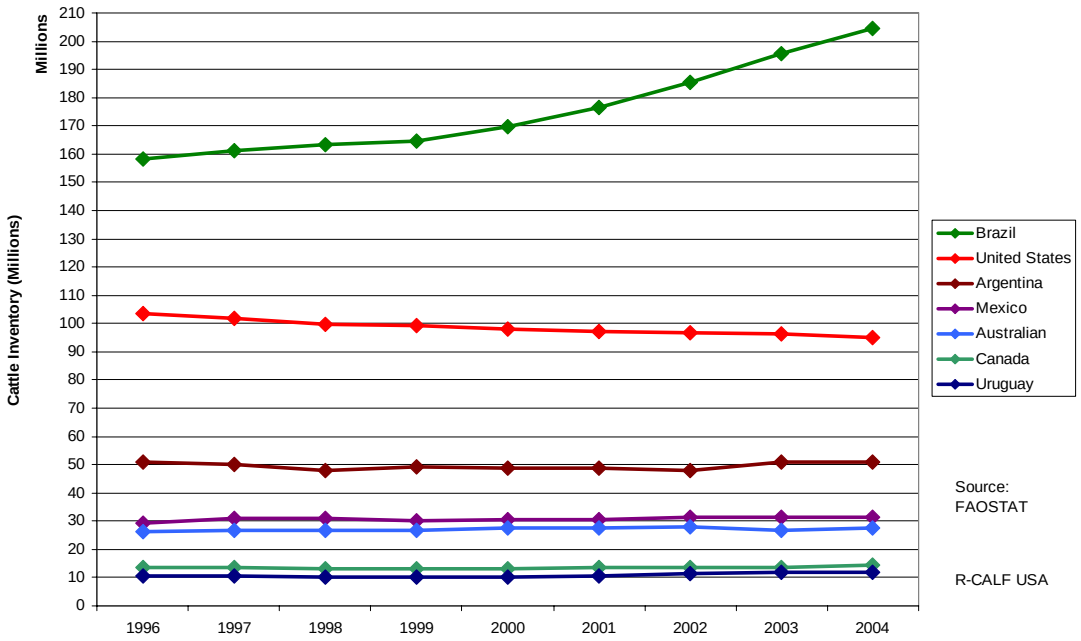
producers are not benefiting from increased exports, can be explained by the cattle industry's lost share of the total available beef supply (chart 27). As is readily discernable from the chart below, the U.S. cattle industry's share of the United States' total available beef supply has been systematically reduced since 1985. Because imports are capturing an ever increasing share of the domestic supply of beef, benefits from increased exports are unable to translate into higher domestic cattle prices. Instead, increased exports are offset by the increased imports and translate into additional profits for the beef packers that are strategically sourcing imported cattle and beef to increase their market leverage over domestic cattle prices, thus constraining domestic cattle production. The U.S. cattle industry's ongoing loss of its share of the United States' total available beef supply is evidence of market failure caused by abusive monopsony power.



J. A Shrinking U.S. Cattle Herd Size While Global Beef Competitors Were Expanding Their Cattle Herds Is Evidence of Market Failure

Beginning in 1996, when the U.S. began liquidating its cattle herd, and continuing through 2004, following the discoveries of BSE in Canadian-born cattle that disrupted global trade patterns, the United States was the *only* major beef exporting country that was appreciably reducing its cattle herd size (chart 28). Other major beef producing countries: Brazil, Mexico, Australia, Canada and Uruguay were all increasing the size of their respective herds, while Argentina's herd size remained relatively stable, decreasing only slightly throughout this period.

CHART 28: Pre-BSE Changes In World Cattle Herd Sizes

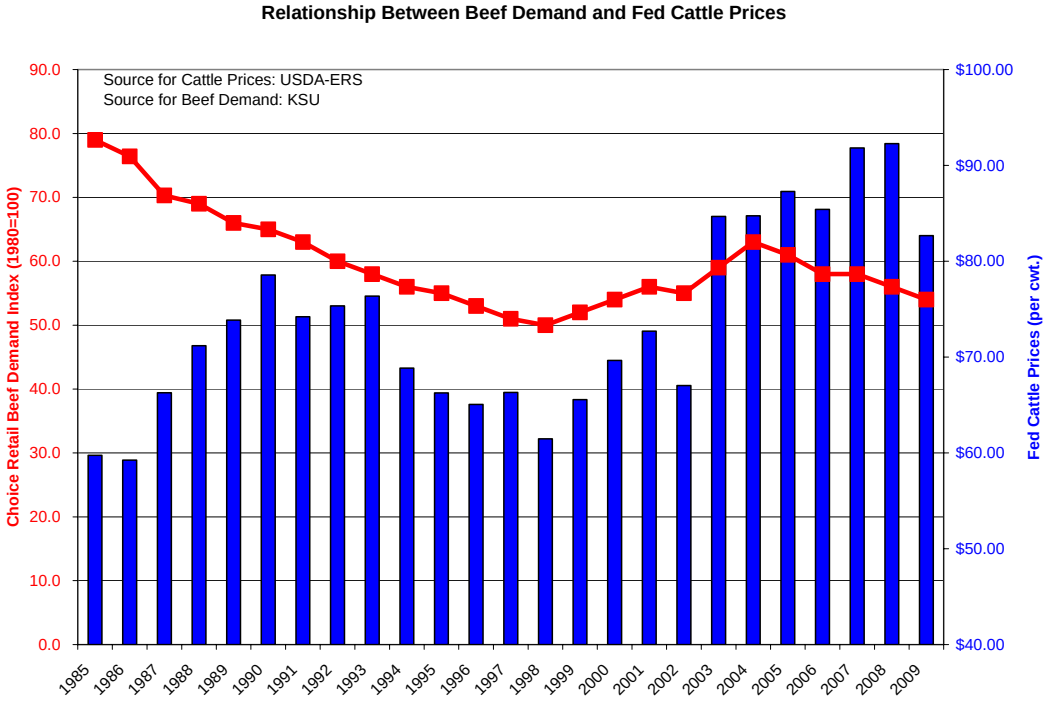


The United States is the worlds' largest beef producer and was, during the period prior to 2004, the worlds' second largest beef exporting country. It is counterintuitive that the U.S. cattle herd would have been shrinking during this prolonged period when its global competitors were expanding their herd sizes, and consequently their production capacity. The fact that the U.S. was shrinking its cattle herd and its production capacity during this period is indicates that the U.S. cattle industry was being unduly constrained and is evidence of market failure caused by abusive monopsony power.

K. Cattle Prices Disassociated with Beef Demand Is Evidence of Market Failure

If beef demand is the principal factor in determining the direction of cattle prices, as the cattle industry has been repeatedly told by beef industry analysts, then a strong, positive correlation should exist between beef demand movement and cattle price movement. However, over the past 25 years, there have been numerous periods in which a negative correlation existed in the relationship between cattle price movement and beef demand movement (chart 29). The frequent, inverse relationship between beef demand and cattle prices is suggestive of market failure in the U.S. cattle market.

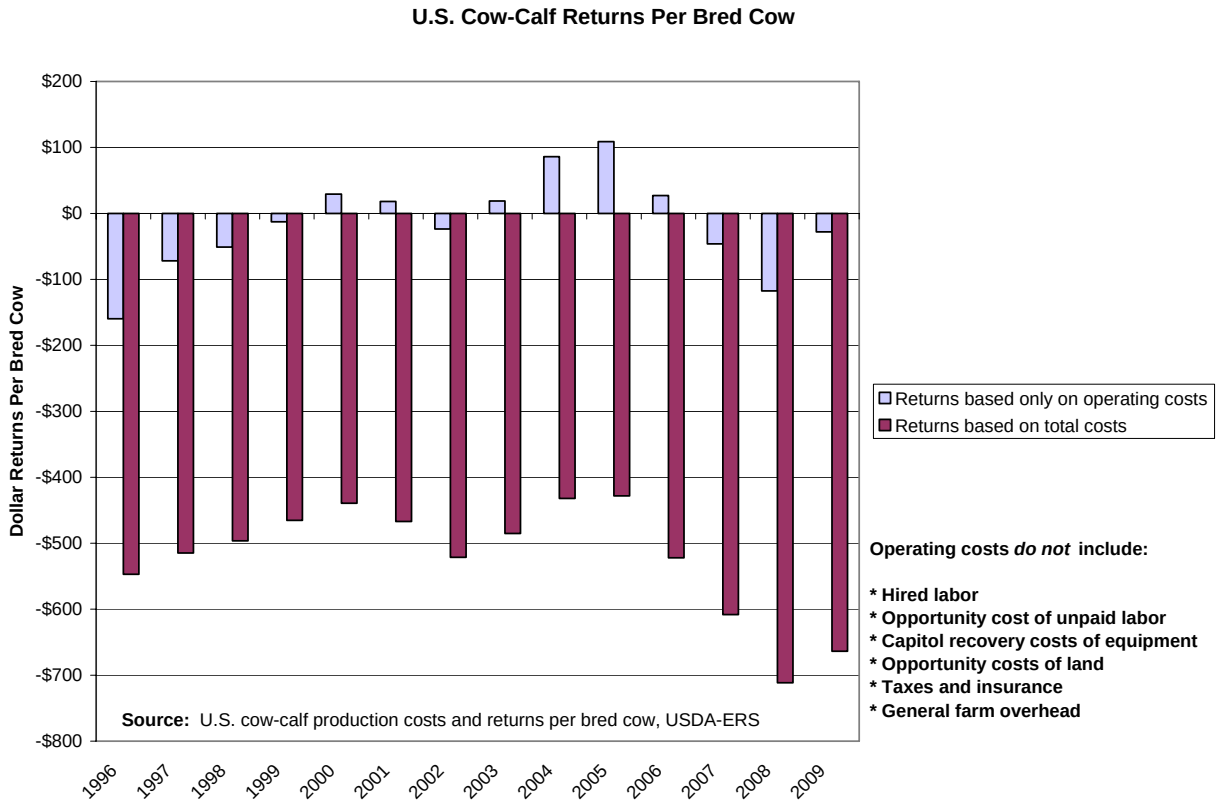
Chart 29



L. Systemic, Below Cost-of-Production Prices for U.S. Cow/Calf Producers while Consumers Continued Paying Record and Near Record Retail Beef Prices is Evidence of Market Failure

Chart 30 below not only explains why the U.S. cattle industry has been contracting at an alarming pace, but also, it clearly demonstrates that the U.S. cattle industry lacks sufficient competition to ensure that profits from the sale of beef are competitively allocated to those who contributed the most time, effort and money to bring that beef to the consumers table. The losses horrendous losses experienced by U.S. cattle farmers and ranchers over the past 14 years while retail beef prices rose to new record levels and continue to remain at near record levels demonstrates severe market failure in the U.S. cattle industry.

CHART 30



IV. OUTLINE OF KNOWN OR SUSPECTED PRACTICES BY BEEF PACKERS THAT CONSTITUTE ANTICOMPETITIVE BEHAVIOR AND/OR VIOLATIONS OF ANTITRUST STATUTES

A. Coercive Threats to Cattle Producers to Advance Beef Packers' Political Goals

B. Imposition of Arbitrary Production Specifications that Lead to Producer Discounts and Facilitate Preferential Treatment

C. Procurement Practices Lead to Pricing Anomalies that Benefit Beef Packers

D. Current Procurement Practices Facilitate a Division of the Market that May Eliminating Competition for Certain Subclasses of Cattle in Certain Regions

E. Beef Packers Have Engaged in Coordinated Actions with the Effect of Lowering Domestic Cattle Prices.

F. The Beef Packers' Dual Role as a Feeder and a Packer Enables Them to Force Smaller Feeders Out of Business

G. The Beef Packers' Dominance in the Cash Market Is Mirrored in the Futures Market, Where They Also Can Exercise Market Power

H. Concentrated Beef Packers Are Uniquely Positioned to Manipulate Beef Demand to Prevent U.S. Cattle Prices from Responding to Tight Domestic Supplies

V. RECOMMENDATIONS AND CONCLUSION

The United States must act quickly and decisively to initiate enforcement of U.S. antitrust laws and the Packers and Stockyards Act (PSA) to halt the highly concentrated beef packers' exercise of abusive market power. The beef packers exercise of abusive market power is facilitated by: 1) the current structure of the U.S. cattle market, procurement practices that afford them large supplies of captive supply cattle, both packer-owned and un-priced formula cattle; 2) trade policies that enable them to export and import strategically while passing losses to cattle producers and capturing profits from cattle producers; 3) limited government oversight over trading practices both in the cash market and the commodity futures market; 4) access to superior market information; and 5) their tremendous influence over the development of both national and international policies that impact the U.S. cattle industry, which is a function of their sheer economic size and virtual unlimited recourses with which to dominate the political process.

The United States must immediately neutralize each of the foregoing five factors that facilitate the beef packers' exercise of abusive market power to prevent the U.S. cattle industry from succumbing to the degree of corporate control and dominance already pervasive in the U.S. poultry and hog industries.

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China's Agricultural Trade:

Competitive Conditions and Effects on U.S. Exports

(Investigation No. 332-518)

Testimony

of the

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

Before the

United States International Trade Commission

Presented by

Bill Bullard, CEO

June 22, 2010

Madam Chairwoman, esteemed members of the Commission, thank you for this opportunity to provide information regarding China's agricultural trade; and, more specifically, the competitive conditions concerning China's beef and cattle, and the effects these conditions would be expected to have on U.S. beef exports.

R-CALF USA exclusively represents U.S. farmers and ranchers who raise and sell cattle within the multi-segmented beef supply chain. With approximately 8,000 all-voluntary members in 46 states and 34 state and county organizational affiliates with thousands more members, R-CALF USA is the largest U.S. trade association exclusively dedicated to representing the interests of the live cattle industry in trade and marketing matters. R-CALF USA's members include cow/calf producers, cattle backgrounders and stockers, and feedlot owners.

It is critically important that the U.S. International Trade Commission (USITC) recognize that the live cattle industry is a distinct industry segment within the U.S. beef supply chain and that a clear demarcation point exists between the live cattle industry and the beef commodity industry – a demarcation point so profound that not only is the economic prosperity of the two industries unrelated, but often, the economic prosperity in the live cattle industry and economic prosperity in the beef commodity industry are inversely related.[1]

I testify today on behalf of a domestic industry that is in severe crisis and contracting rapidly, with domestic beef cattle operations exiting the industry at a rate of more than 11,000 per year. There are several factors contributing to the decline of the U.S. cattle industry. As documented in my pre-hearing brief, these factors include a highly concentrated market structure that facilitates the exercise of abusive market power by dominant beef packers to prevent increased profits earned in the beef wholesale and beef retail markets from being competitive allocated to U.S. cattle producers.

Increased beef exports *should* increase the welfare of U.S. cattle producers, but historical data show this expectation has not been met. Accordingly, the goal of focusing on increased exports as the principal means of reversing the economic deterioration of the U.S. cattle industry is misplaced.

At the outset, it is R-CALF USA's position that increased beef exports to China likely would present at least some economic opportunities for the U.S. cattle industry, though under the U.S. cattle industry's present market structure, those opportunities are likely to be small and most if not all benefits would be expected to flow directly to, and be captured by, beef packer exporters. In addition, if as a result of trade liberalization, China were to ramp up beef production and begin exporting beef and products derived from cattle to the U.S., China's export advantage as discussed in my pre-hearing brief would work to worsen the U.S. beef trade deficit and harm U.S. cattle producers.

[1] *See*, e.g., Sparks Companies Inc., "Potential Impacts of the Proposed Ban on Packer Ownership and Feeding of Livestock," A Special Study, (March 18, 2002) at 24 ("Vertical integration [of the live cattle industry and the beef commodity industry] often attracts investors because of the negative correlation between profit margins at the packing stage [beef commodity stage] and the feeding stage [live cattle stage].").

It is for these reasons that R-CALF USA urges extreme caution in working to increase U.S. beef exports to China until reforms are instituted to restore a fully functioning marketplace for U.S. cattle producers – one free from anticompetitive market forces that prevent the competitive allocation of profits to each segment of the domestic cattle supply chain. It is also for these reasons that R-CALF USA strongly opposes the granting of any concession that would facilitate Chinese imports of cattle, beef, or other products derived from cattle as a *quid pro quo* for achieving increased export access.

Testimony Outline

A. Recommendations and Conclusion

- Reverse the United State's recently weakened disease import standards for countries with ongoing BSE outbreaks;
- Accept China's 2007 offer to partially lift its current ban on U.S. beef;
- Facilitate the voluntary testing for BSE by private beef packers;
- Revise the current standard of "substantial transformation" used to determine the country of origin for international trade purposes by establishing that the origin for beef and products derived from cattle shall be the country where the animal from which the beef is derived was born, raised, and slaughtered;
- Thoroughly assess the impacts that current trade policies and trade agreements are having on the profitability and viability of the U.S. live cattle industry and take into account the market concentration and cattle procurement practices in the industry as well as the perishable nature of live cattle and the cyclical nature of the live cattle industry in the assessment;
- Thoroughly investigate and determine why U.S. cattle prices have responded inversely to rising and falling exports; and,
- Neutralize the tariff caused by China's undervalued currency.

B. China's Beef and Cattle Market Including Recent Trends in Production, Consumption, and Trade

- China has 105 million head of cattle. It ranks third in the world behind India and Brazil.
- China is the fourth largest beef producer, behind the US, Brazil, and EU 27.
- China has increased its beef production for the past ten years.
- Beef consumption in China increased only marginally over the past ten years (per capita consumption increased from 4.02 kg in 2000 to 4.3 kg in 2009.
- China's per capita consumption of pork (36.4 kg) and poultry (9.10 kg) far exceeds beef.
- China has produced more beef than it consumes over each of past ten years and remains a net beef exporter.
- Imports in China reached 32,000MT in 2002 and 20,000 MT in 2009.
- Unless significant changes occur in Chinese consumption patterns, China is unlikely to represent a significant U.S. export market opportunity, though niche market opportunities are likely.

- The only other country that, like China, overproduces for its domestic beef market and, yet, is a significant importer of U.S. beef is Canada. However, the U.S. maintains a significant deficit in cattle and beef trade with Canada that has averaged well over $1 billion per year over the past ten years.
- Based on historical trade data, exports of hides represent a more substantial market opportunity than beef.

C. Competitive Factors Impacting China's cattle and Beef Production

- The United States' producer price (i.e., wholesale/retail price) received for cattle is $438.87 higher than in China (China = $1,543 USD; US=$1,982 USD).
- Comparative advantage would be with Brazil, with a producer price of $998 USD.
- Price for fed cattle in China in 2008 was $965.70 USD per head, with production costs estimated at $880.50 USD per head.
- Price for fed cattle in the U.S. in 2008 was $1,162.63 USD per head, with production costs estimated at $1,315.50 per head.
- Because beef commands a lesser price in China than the U.S. (U.S. beef prices are $382.32 per tonne higher in the U.S. than in China), the U.S. would need to promote non price aspects of U.S. beef in China.
- China is blessed with one of the world's largest grasslands that could support expansion of China's cattle and beef production (e.g., Brazil doubled its beef production from 1990-2008, from 4 million tonnes to 9 million tones).
- China's beef production similar to that of Brazil 20 years ago.
- China's intentions regarding beef production expansion are difficult to gauge.
    - $200 million development project in 2001.
    - Recent subsidies are reported as moderate.
    - Subsidies of $73 dollars per head to rebuild dairy herd following melamine outbreak.

D. Principle Measure Impacting China's Imports of Beef and Other Products Derived from Cattle

1. China's Sanitary and Phytosanitary Measures

- China imposed a ban on U.S. beef and offal after the U.S. detected a BSE in a cow imported from Canada in 2003.
- China offered to accept boneless beef from cattle less than 31 months of age in 2007.
- The U.S. inexplicably rejected this offer for market access.
- Indefensible because the U.S. estimated the cost to the U.S. beef industry was $100 million from 2004-2007.
- The U.S. maintains among the weakest BSE standards in the world with respect to Canada, and it is unreasonable to demand that China increase its risk for BSE.

2. China's Income Growth in Relation to Its Per Capita Beef Consumption.

- China's per capita beef consumption grew marginally, but not steadily, over the past ten years.
- In contrast, China's per capita income, which was estimated at $6,500 USD in 2009, experienced uninterrupted growth during this period.
- Data suggest other factors have significant influence over Chinese beef consumption patterns.

3. China's Currency Policy

- China's currency is estimated to be undervalued between 30 and 50 percent.
- China's undervalued currency is an effective tariff on U.S. beef and likely would result in pricing U.S. beef beyond the reach of even China's middle-income population.
- Under the United States' current industry structure, the U.S. must sell beef for $4.26/lb to maintain returns for U.S. cattle producers at 2009 levels.
- Should China export lower cost beef to the U.S., the supply-sensitive U.S. cattle industry would be harmed.

E. Important Considerations Regarding Increased Trade with China

- Historical data do not support the contention that increased beef exports to China would result in increased cattle prices for U.S. cattle producers.
    - Exports of beef derived from cattle imported into the U.S. for immediate slaughter provide no benefit to U.S. cattle producers.
    - This is because the U.S. cattle industry adds no value to those cattle and, yet, current rules of origin allow the beef from those cattle to be considered a USA product.
    - The U.S. could export 20 times more beef to China than was exported to it in 2003 without any benefits flowing to U.S. cattle producers.
- The value of U.S. imports of beef, cattle, beef variety meat (offal) and processed beef exceeds the value of U.S. exports of these products.
- Imports are capturing an ever-increasing share of the total available beef supply in the United States.
- Historical data show that U.S. cattle prices remained inexplicably depressed during the extended period between 1994-2002 when domestic beef consumption was increasing, U.S. beef exports were reaching new highs, and the U.S. trade balance was most favorable.
- Claims by beef packers and their affiliated associations that an increased demand and price for cattle byproducts add significantly to the price beef packers pay to U.S. cattle producers for cattle are unfounded:
    - Anecdotal industry commentary suggests that sales of cattle by-products are a significant contributor to beef packers' profitability.

- AgJournal.com reported that the estimated value of unbranded hides is about $5 per head higher than for branded hides and though beef packers pushed for unbranded hides in 1994, premiums never materialized[2]
- Beef packer Creekstone Farms Premium Beef, LLC, which slaughters approximately 1,000 cattle per day, claimed that the beef export bans by Japan and South Korea, prior to their partial lifting of the bans in 2006, cost the company $200,000 per day in revenues (representing a loss of approximately $200 per head or approximately $16 per cwt).[3] However, U.S. cattle producers were then receiving the highest actual cattle prices for their cattle in their industry's history. This indicates that prior to the bans, when exports were strong and U.S. cattle producers were suffering from severely depressed prices, U.S. cattle producers were not enjoying a significant share of the benefits associated with increased beef packer profitability.
- Researches have documented even a negative price relationship between increased by-product exports and live cattle prices. In a 1980 study regarding the impact of beef by-product exports on live cattle prices, researchers found a negative price impact of inedible tallow exports on cattle prices.[4] Though this study was completed prior to the significant concentration in the U.S. beef packing industry, it found that, "Prior to 1972, the negative price impact of inedible tallow exports exceeded the sum of the positive price impacts of the other three by-product exports [edible tallow, skins and hides, and offal].[5]
- In my pre-hearing brief are charts showing the relationships between annual domestic cattle prices and the total value of exported cattle hides and the per unit value of tongue exports (Charts 14 and 15). Both these charts show periods when the year-to-year movement of cattle prices was opposite the year-to-year change in by-product values, suggesting a lack of any strong correlation.

F. Conclusion

Thank you, again, for the opportunity to present this information that demonstrates that Congress and the Administration need to conduct a more critical and thorough evaluation regarding the actual impacts current and planned trade policies have, and are having, on the economic wellbeing of the hundreds of thousands of independent U.S. cattle producers that comprise the single largest segment of U.S. agriculture – the U.S. live cattle industry.

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[2] *See* Branding is still key form of identification, Candace Krebs, La Junta Tribune-Democrat, AgJournal.com (June 20, 2010).

[3] *See* Creekstone Farms Premium Beef, L.L.C. v. U.S. Department of Agriculture, et al., Memorandum, U.S. District Court for the District of Columbia, Civil Action No. 06-0544 (JR), March 29, 2007, at 4 ("The bans in Japan and South Korea, for example, cost Creekstone $200,00 per pay in revenues when they were in effect.") (the Memorandum further states at 1 that Creekstone slaughters 300,000 head each year, which would equate to approximately 1,000 head per day).

[4] *See* The Impact of Beef By-Product Exports on Live Cattle Prices, Martin Blake and Tom Clevenger, American Journal of Agricultural Economics, Vol 62, No. 1 (Feb., 1980), pp. 103-106.

[5] *Ibid.*