Fighting for the U.S. Cattle Producer!

R-CALF

USA

R-CALF USA Overview of Proposed JBS-Brazil Acquisitions

Presented by
Bill Bullard
CEO, R-CALF USA
September 5, 2008

Merger Benefit Claims

- Merger would revitalize the ailing U.S. beef packing sector – new blood, new capital.
- Merger would create improved economies of scale.
- JBS is an aggressive global exporter and will teach the U.S. beef industry how to compete globally.
- JBS will increase beef demand, resulting in greater demand for live cattle.
- JBS will introduce new technologies
- JBS will hire more workers.
- Three major packers is all that is needed in the U.S. market to maintain robust competition.

PRODUCT MARKET

A. The Relevant Product Market (Supply side)

1. **Direct Products: fed steers and heifers, slaughter cows and bulls.**

2. **Indirect Products: feeder steers and heifers, calves, breeding cows and bulls.**

B. The Relevant Geographic Market (Supply Side)

1. For Direct Products: Approximately a 300-mile radius from plant.

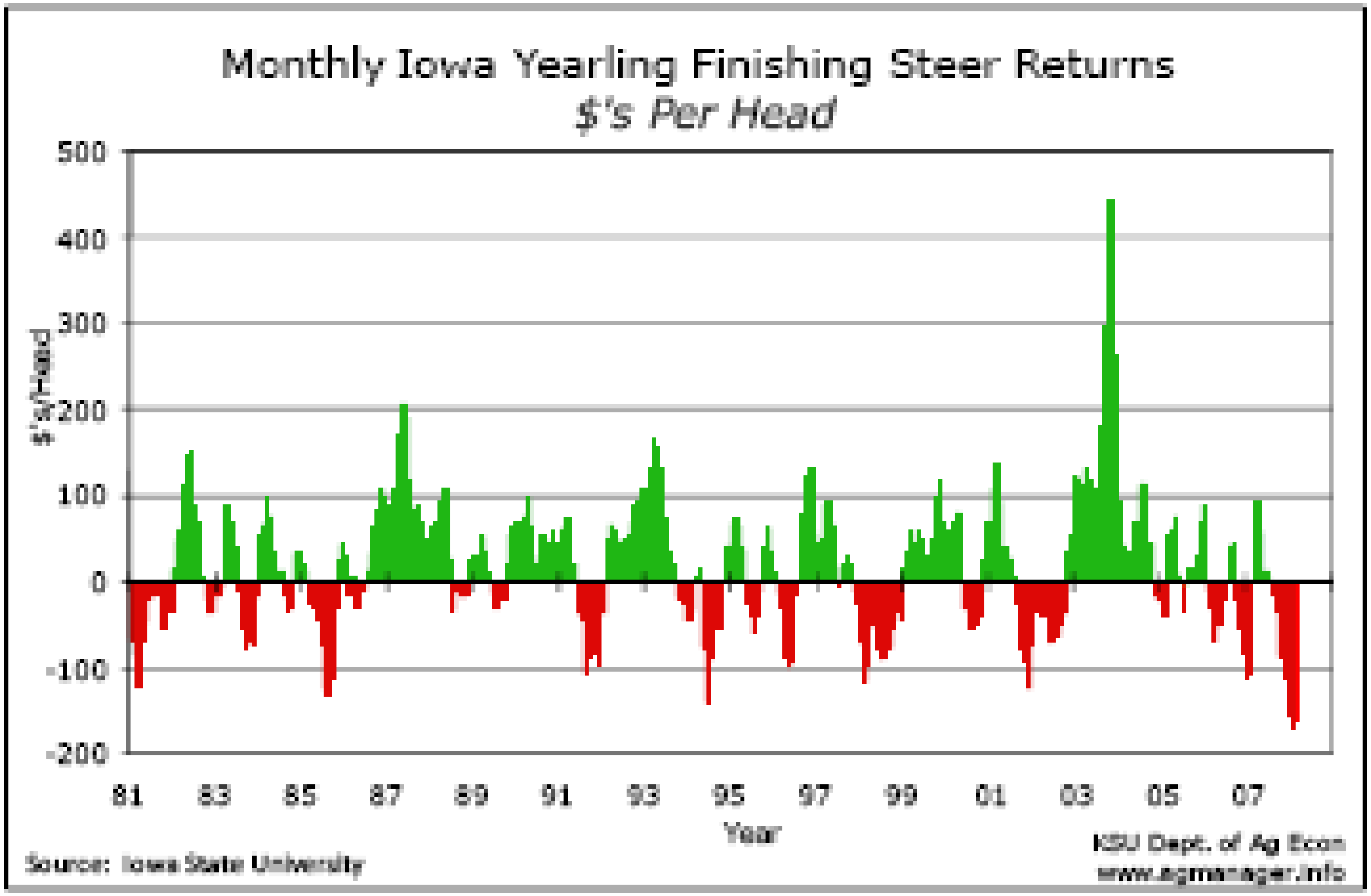
2. For Indirect Products: Beyond a 300-mile radius and extending nationally.

What would happen if the merger caused about a 5% decrease in prices?

For Direct Products: the net returns (in current dollars) from feeding yearling steers averaged less than only $14 per head over the 1994-2008 period. For a $1,000 per head fed steer, the 5 percent test would allow a merger that would decrease price by $50 per head, which would mean that cattle feeders would be losing $36 per head compared to the historical average profit of about $14 per head. A price decrease of only 1.4 percent would completely eliminate the modest profits realized by cattle feeders over the period 1994-2008. Therefore, criteria typically used to define markets and to define an acceptable level of market power in the merger approval process are inappropriate to the U.S. fed cattle market.

Record Losses for Cattle Feeders

1st Quarter '08 Losses Averaged $160/Head

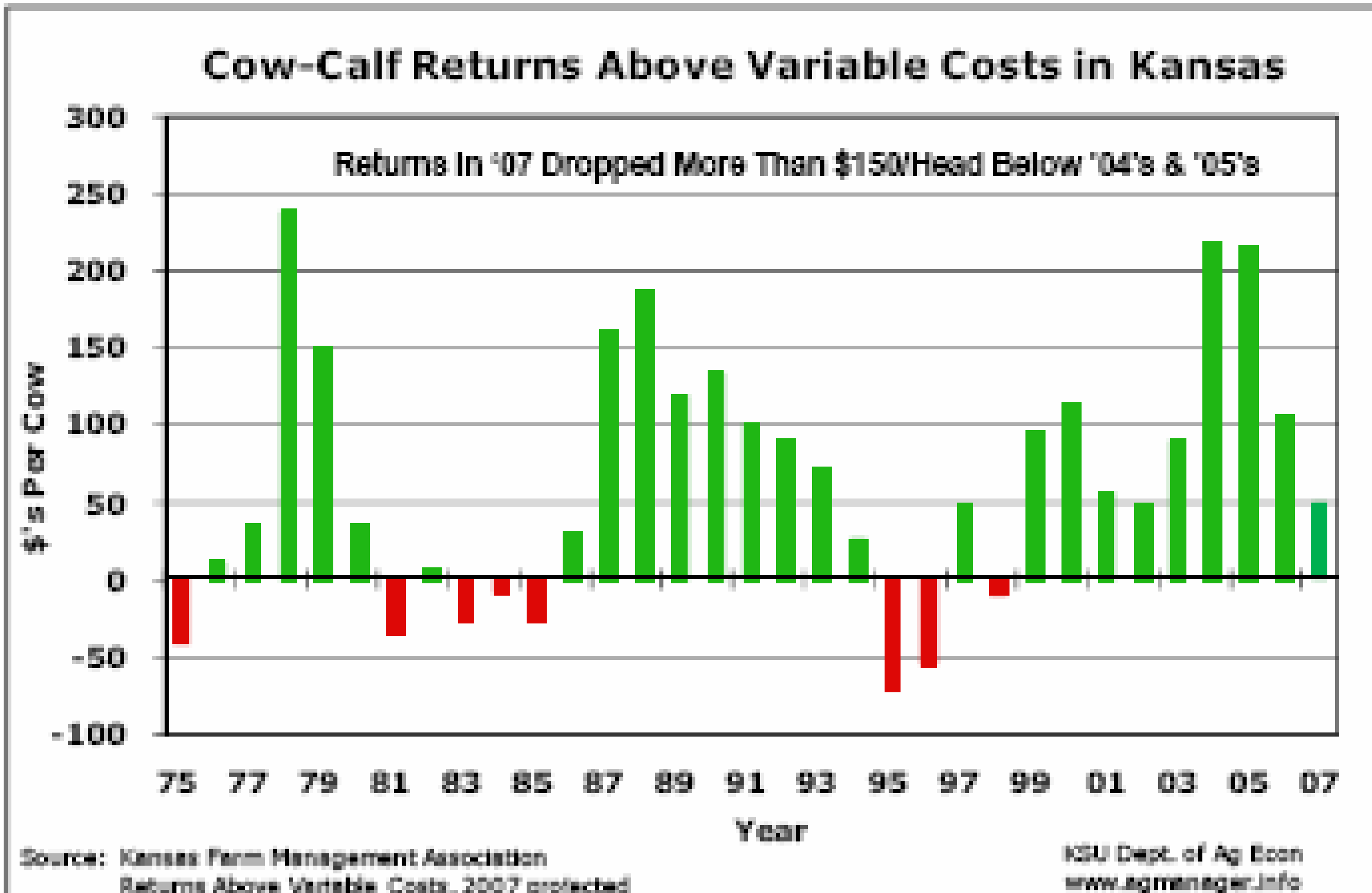


What would happen if the merger caused about a 5% decrease in prices?

- For Indirect Products:
  - Continued and perhaps accelerated reduction in U.S. cattle operations.
  - Continued and perhaps accelerated liquidation of U.S. cattle herd.
  - Continued and perhaps exaggerated disruption of U.S. cattle cycle.

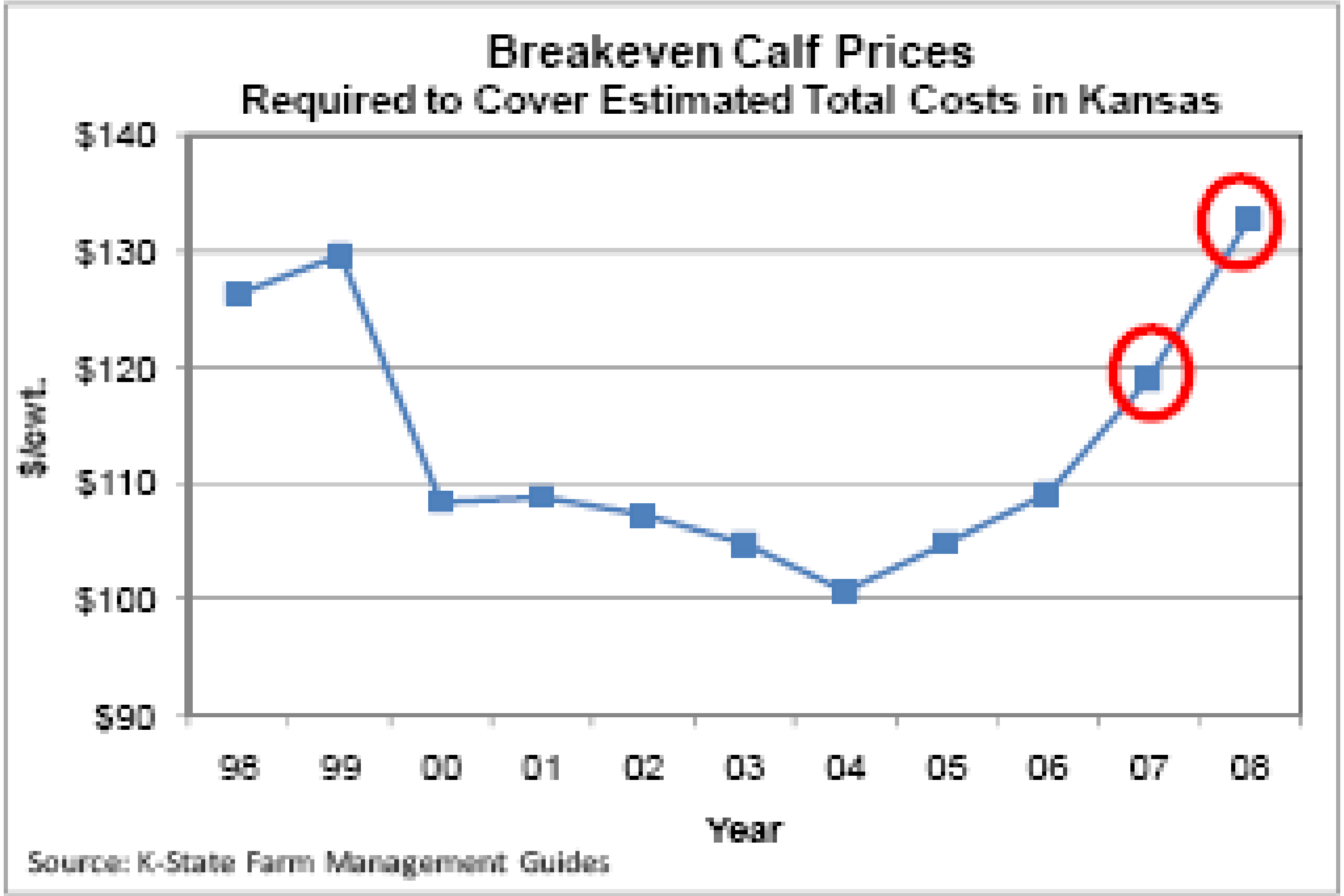
Returns Declining Rapidly

Returns Could Dip Into The Red During 2008

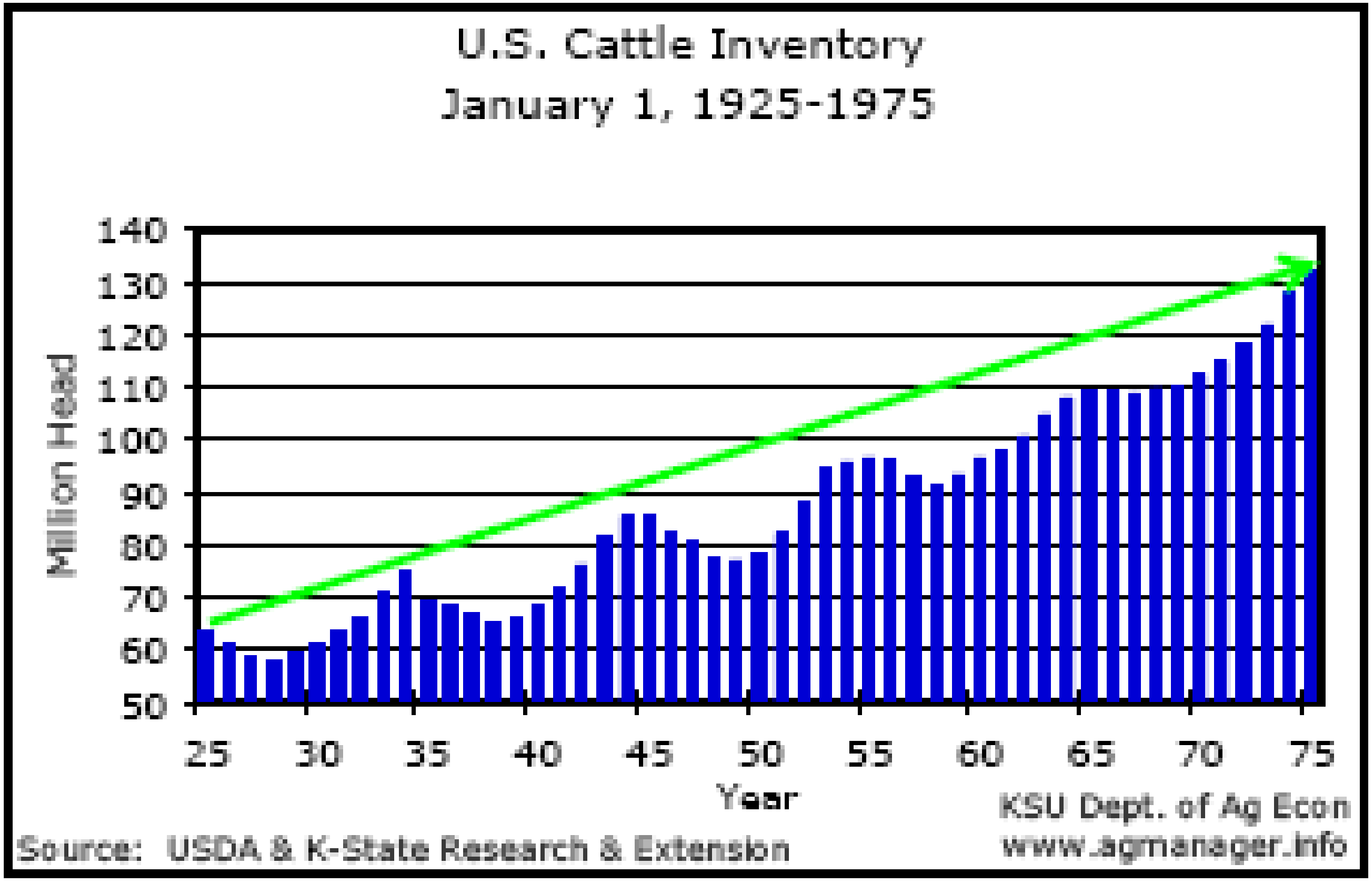


Rising Breakevens Putting Pressure On Cow-Calf Sector

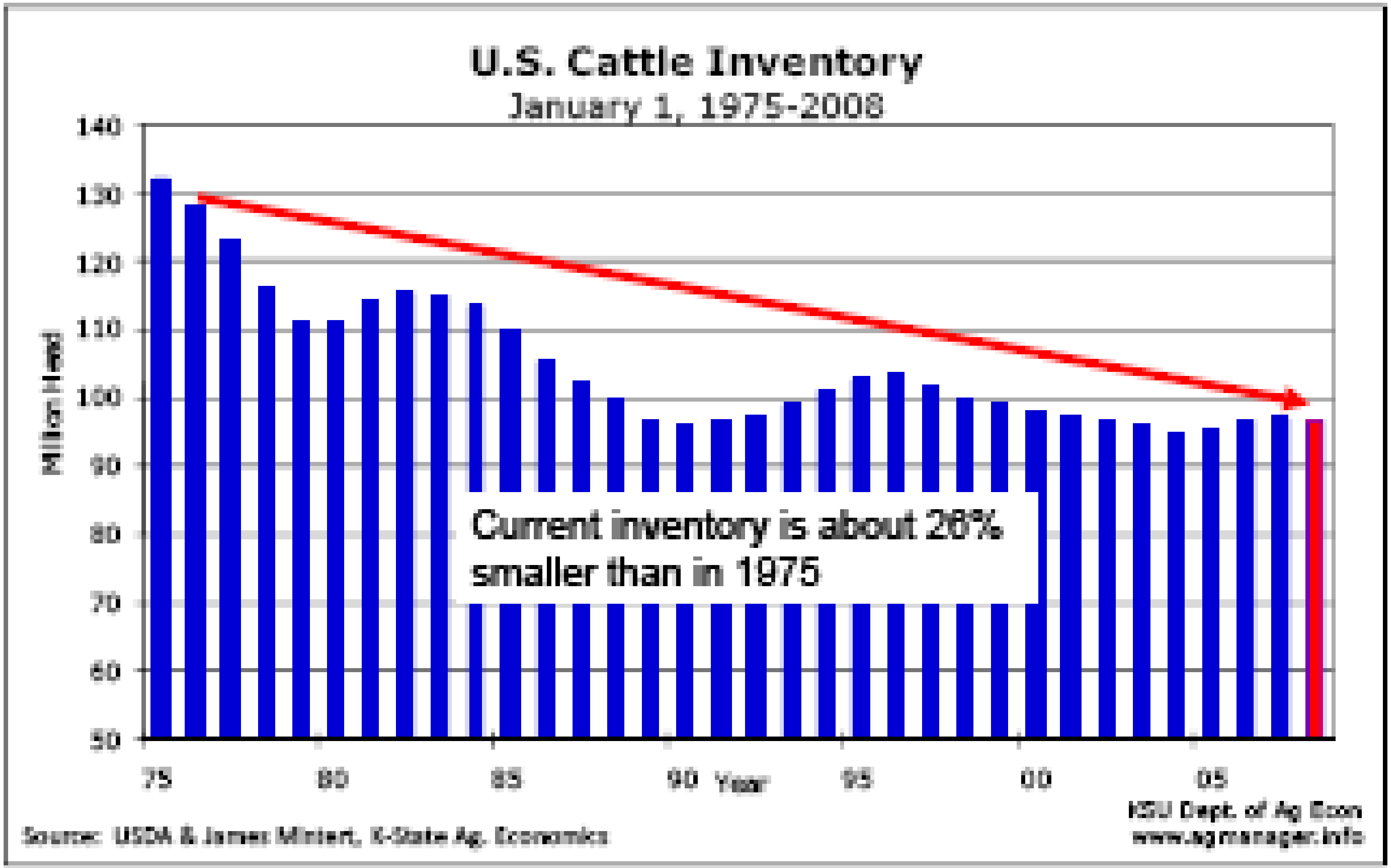
'08 Breakevens Up 12% Compared to '07



A Picture of A Healthy Industry



A Shrinking Industry
Responding to a Long-Run Lack of Profitability



Why Cattle Industry Highly Sensitive to Price Changes

- Longest biological cycle of any farmed animal – inelastic supply.
- Finished cattle are highly perishable.
- Demand for cattle bounded on weekly basis – Packers set weekly limits by choice and by capacity constraints.
- Transportation costs limit marketing options.
- Packing industry already well above levels considered to elicit noncompetitive behavior.
- Competition for raw products, e.g., cattle, is inherently less intense than is competition for processed food products.
- Cattle market highly sensitive to slight changes in cattle supplies (1 percent increase in supplies causes 2 percent decrease in price).
- Marginal transparency in cattle markets.
- Packers have superior marketing information, particularly those with substantial captive supply arrangements.

The 5 Percent Test is Too High for the U.S. Cattle Industry

- Oklahoma State University economist Clement E. Ward found that "[r]esearch to date suggests price impacts from packer concentration have been negative in general, but small." He found that most studies found price distortions of 3 percent or less, though 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.

- 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. 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.

C. Firms that Participate in the Relevant Market

1. Total Packing Plants: 5 largest firms own 30 plants in 14 states.
2. Plants Subject to Merger: 3 merging firms own 11 plants in 10 states.
3. Feedlots: 2,160 feedlots>1,000 hd.; 85,000 feedlots<1,000 hd.
4. Cattle Operations: 757,900 beef cattle operations. 585,050<50 head and 78,360>100 head.

D. Market Share

1. **Pre-Merger: Four firms purchased 66 percent of livestock (2006).**

2. **Pre-Merger: Four firms slaughtered 80.9 percent of steers and heifers (2006).**

3. **Post-Merger: Four firms will slaughter estimated 91.2 percent of steers and heifers.**

E. Post-Merger Market Concentration Using HHI

1. Pre-Merger livestock purchases by meatpackers: HHI = 1,269 (2006).
2. Pre-Merger steer and heifer slaughter concentration: HHI = 1,826 (2006).
3. Pre-Merger HHI indices in regional procurement areas are much higher, ranging from 2,610 to 4,451. Data show substantial price differences among regions – nearly $6.00 per cwt. according to July 21, 2008 AMS report.
4. Post-Merger steer and heifer slaughter concentration: CME Group estimates an increase of 638 points.

III. POTENTIAL ADVERSE COMPETITIVE EFFECTS

A. Coordinated Interaction (e.g. tacit or express collusion)

1. **Evidence of strategic entry and exit from cash market for the purpose and with the effect of lowering cattle prices.**

   i. In February 2006, all four major beef packers – Tyson, Cargill, Swift, and National – withdrew from the cash cattle market in the Southern Plains for an unprecedented period of two weeks.

   ii. Week ending October 13, 2006 three of the nation's four largest beef manufacturers – Tyson, Swift, and National - announced simultaneously that they would all reduce cattle slaughter, with some citing, *inter alia,* high cattle prices and tight cattle supplies as the reason for their cutback.

A. Coordinated Interaction (e.g. tacit or express collusion)

1. Evidence of propensity for express collusion

i. A November 28, 2007, Dow Jones Newswires reported that "JBS SA's Friboi Group (JBSS3.BR)" was among a number of Brazilian companies which, after a two-year investigation by the Brazilian Justice Department's antitrust division, were accused of engaging in anti-competitive practices, including coordinating with other firms to purchase livestock cheaper.

ii. Anecdotal evidence reveals that packer buyers contact cattle sellers to learn what prices other packers are offering.

A. Coordinated Interaction (e.g. tacit or express collusion)

1. **Ongoing and predicted strategies to lower cattle prices.**

   iii. **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.**

   iv. **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.**

   v. **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. The proposed merger, which would increase the RHHI in one or more of the nine procurement regions, would be expected to shift more cattle into packer feeding arrangements.**

A. Coordinated Interaction (e.g. tacit or express collusion)

1. **Ongoing and predicted strategies to lower cattle prices.**

   vi. The merger would significantly increase the volume of captive supply cattle controlled by JBS/Swift by combining two principal market outlets for U.S. feeder cattle – Five Rivers and U.S. Premium Beef. Together, these entities feed about 2.68 million, or nearly 10 percent, of the 27 million steers and heifers slaughtered annually in the United States.

   vii. The volume of cash cattle procurements has already dropped significantly since 2005, falling 15.2 percent in the TX/OK/NM market, with a corresponding increase in captive supply procurements. Studies have found that producers participate in counterproductive marketing arrangements because they are unable to coordinate actions with other producers.

   viii. Producers already subject to 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],” 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 . . .”

B. Unilateral Effects

1. **Evidence of market power abuses**

   i. **Using producers to advance political goals: In March 2003, IBP, Inc., notified U.S. cattle producers that it would require producers to, *inter alia*, "Provide IBP, inc. access to your [producers'] records so that we [IBP] can perform random producer audits . . ." and "Provide third-party verified documentation of where the livestock we [IBP] purchase from you [producers] were born and raised."**

   ii. **Imposition of arbitrary discounts: Tyson and Smithfield have each established different price premiums and discounts for additional factors, such as muscle scoring. For example, Smithfield discounts certain muscle scores between $5.00 per cwt. and $10.00 per cwt, and Tyson uses muscle scores to apply varying discounts under a different system.**

   iii. **Anticompetitive pricing strategies: The LMMS study states that in direct trade transactions based on a carcass weight valuation, the average cattle price is 1.3 cents lower than the average price for direct trade transactions with live weight valuation. Even more striking is the difference for grid valuation transactions, where prices average 1.8 cents lower than the average price for direct trade transactions.**

B. Unilateral Effects

1. **Evidence of market power abuses**

   iv. **Anticompetitive division of the market: Tyson Fresh Meats, Inc., (“Tyson”) has issued presumably new terms and conditions under which it will purchase cattle for slaughter. Tyson states that it “does not typically accept for processing at its facilities” cattle that exceed 58 inches in height, cattle that exceed 1,500 pounds, or cattle with horns longer than 6 inches in length.**

   v. **Actions to coerce producers to waive rights under P&S Act: On April 23, 2008, JBS/Swift originated a one-year contract for the sale of slaughter-ready cattle to JBS/Swift. Under the contract terms, feedlots must grant JBS/Swift the right to withhold payment for “grade and yield” cattle for three days after the “final grade” and feedlot owners and managers must additionally waive any rights they have “under the trust provisions of Section 206 of the Packers and Stockyards Act, 1921, as amended (7 U.S.C. 106, Pub. L. 94-410).”**

B. Unilateral Effects

1. Evidence of market power abuses

vi. Each of the merging packer firms have been accused of unilateral engaging in anticompetitive practices: Swift & Co. accused of underpaying on hot carcass weights; National paid $50,000 penalty involving failure to disclose freight charge deductions and data errors; and Smithfield paid $325,000 penalty involving improper rounding of hot carcass weights.

vii. Anecdotal evidence reveals that meatpackers with multiple plants deny access to plants that are offering a higher price and require producers to deliver to the plant offering a lower price.

III. ENTRY ANALYSIS

A. Can entry achieve significant market impact in timely period?

B. Would committed entry be profitable?

C. Would timely and likely entry be sufficient to return market prices to premerger levels?

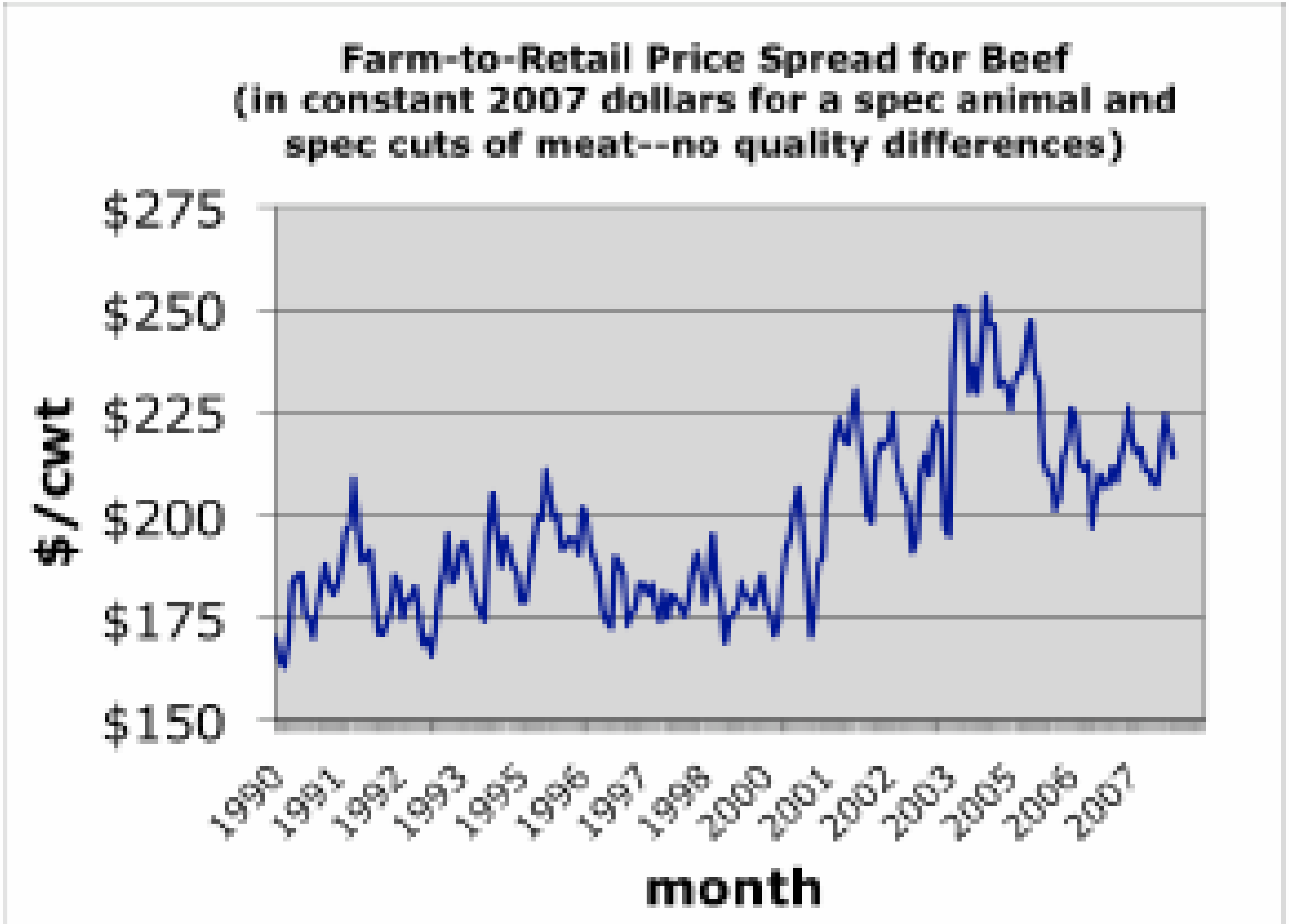
POTENTIAL ADVERSE COMPETITIVE EFFECTS

Imagine if you will, the day before the merger is announced, that three buyers from Swift, National and Smithfield meet together to discuss their plans to buy slaughter cattle. If that occurred, those buyers would be in violation of antitrust laws against collusion

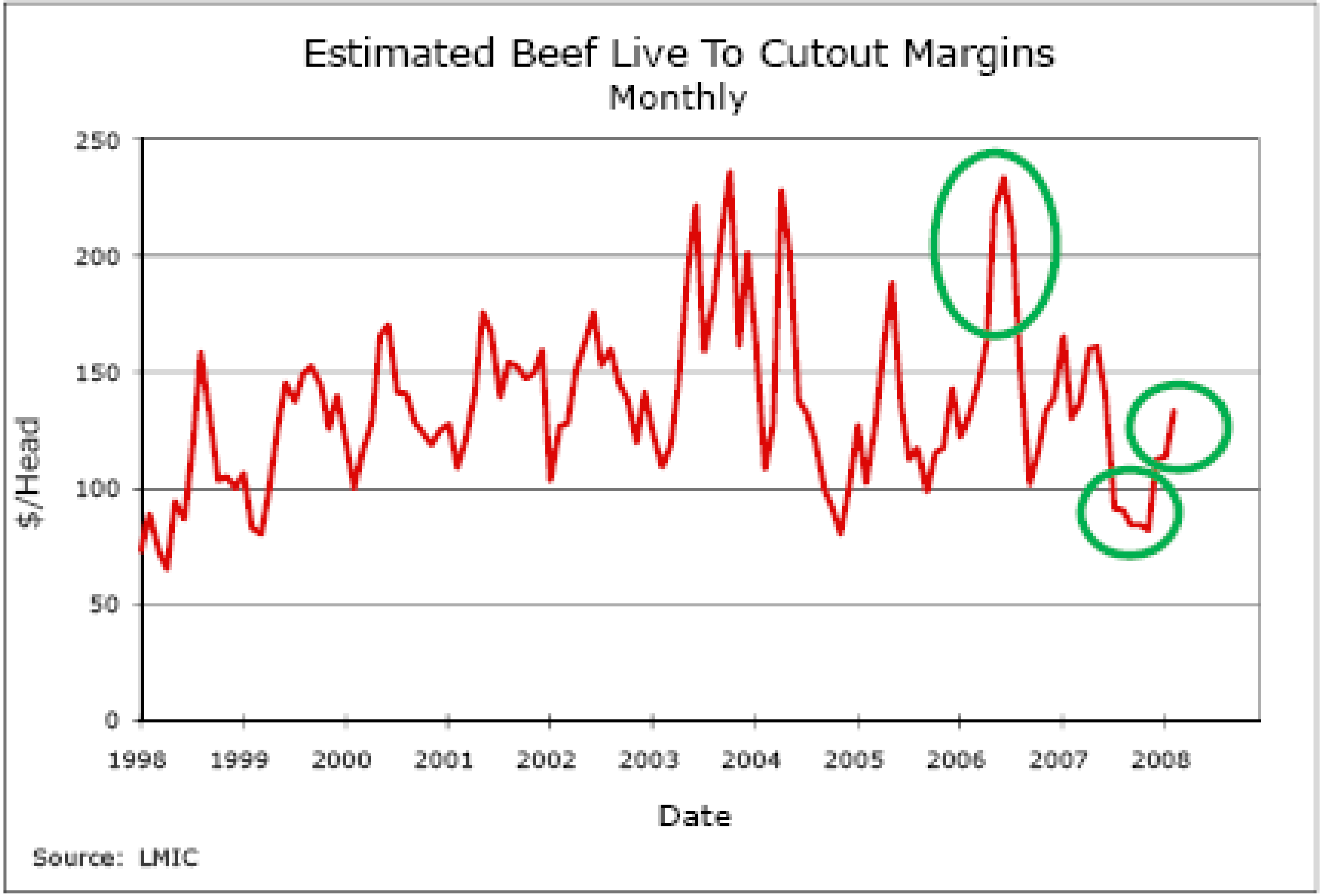
The activities of three buyers of the third, fourth and fifth largest beef processors colluding would most certainly hurt the price of live cattle. But, on the day after the merger, the same three buyers could discuss their plans without violating the law.

IV. REVIEW EFFICIENCIES

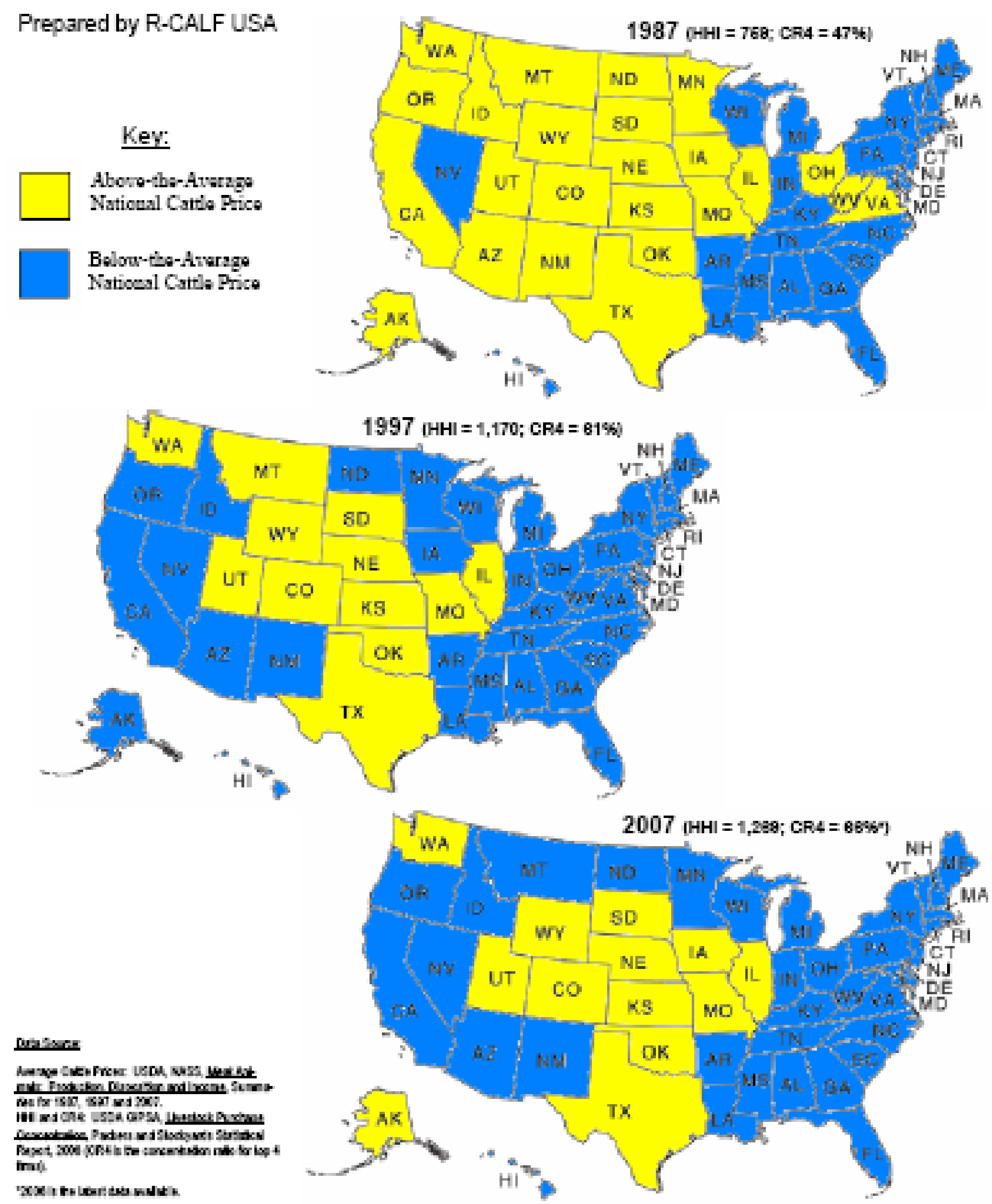
A. On July 11, 2008, the Associated Press issued a news article stating that National Beef had attributed its higher third-quarter profits to, *inter alia*, increased beef demand and lower cattle prices. This is a counter-intuitive outcome for a properly functioning competitive market as higher demand for beef should translate into higher prices for the fed cattle from which the beef was derived.


Farm-to-Retail Price Spread for Beef
(in constant 2007 dollars for a spec animal and spec cuts of meat--no quality differences)
$275
$250
$225
$200
$175
$150
$/cwt
1990
1991
1992
1993
1995
1996
1997
1998
2000
2001
2002
2003
2005
2006
2007
month

Processor Margins Still Narrow, But Are Starting to Recover



Effects of Declining Competition on Cattle Prices 1987 - 2007



Additional Concerns

- **Many of the practices described above are inconsistent with the provisions of the Packers and Stockyards Act of 1921. Specifically 7 USC § 192 *et seq*.**

- **Additionally, the following practices should be investigated:**
  - **Bidding not to buy cattle, i.e., offering a low bid with no intent to buy, but rather, with the intent to lower prices for live cattle.**
  - **Offering preferential agreements with captive suppliers for prices and terms not available to other sellers of comparable cattle in the market.**
  - **Entering into strategic alliances that contain special agreements for preferential access to the market and/or special prices.**
  - **Exercising undue influence over national commodities markets, potentially eliminating this hedging tool for U.S. cattle producers.**

Packing Industry Exceeds Optimal Economy of Scale

Beef Packer Operating Income as a Percent of Sales (GIPSA/USDA data) by Size

Time Period	Big Four	5th to 8th	9th to 20th	21st to 40th
2006	-0.2	2.3	2.22	5.42
2005	0.92	1.69	4.47	3.51
Average 1992-2006	**1.46**	**2.34**	**3.86**	**1.77**

Fighting for the U.S. Cattle Producer!

R-CALF USA

P.O. Box 30715

Billings, MT 59107

406-252-2516

r-calfusa@r-calfusa.com

www.r-calfusa.com