

Fighting for the U.S. Cattle Producer!



R-CALF
USA

R-CALF United Stockgrowers of America
P.O. Box 30715
Billings, MT 59107
Fax: 406-252-3176
Phone: 406-252-2516
Website: www.r-calfusa.com
E-mail: r-calfusa@r-calfusa.com

September 21, 2009

The Honorable Eric Holder
United States Attorney General
U.S. Department of Justice
950 Pennsylvania Avenue, NW
Washington, DC 20530-0001

The Honorable Christine Varney
Assistant Attorney General
U.S. Department of Justice
950 Pennsylvania Avenue, NW
Washington, DC 20530-0001

Re: R-CALF USA's Request to the U.S. Department of Justice for Enforcement Action Against the Proposed Acquisition of Pilgrim's Pride Corporation by JBS S.A.

Dear Attorney General Holder and Assistant Attorney General Varney:

R-CALF USA¹ is a national non-profit association that represents U.S. farmers and ranchers who raise and sell cattle. R-CALF USA urges the U.S. Department of Justice to take immediate enforcement action to prevent the proposed acquisition of Pilgrim's Pride Corporation ("Pilgrim's Pride") by JBS S.A. ("JBS/Pilgrim's Pride merger"). The proposed JBS/Pilgrim's Pride merger would reduce competition for U.S. cattle producers and U.S. beef consumers and would result in the increased exercise of market power by JBS S.A. that would cause lower-than-competitive prices paid to U.S. cattle producers for their cattle and higher-than-competitive prices paid by U.S. consumers for beef and poultry.

Cattle sold by R-CALF USA members are purchased by and subsequently converted to consumable beef by JBS S.A. and other slaughtering plants. Beef derived from R-CALF USA member-cattle sold to JBS S.A. is a protein food product that competes directly with other protein food products such as pork and poultry.² The demand and price for R-CALF USA member-cattle is influenced by the supply and price of competing proteins such as pork and poultry.³ However, prices received by R-CALF USA members for their cattle are particularly susceptible to increased poultry supplies, i.e., poultry broilers at relatively lower prices.⁴ The

¹ R-CALF USA is the acronym for the Ranchers Cattlemen Action Legal Fund United Stockgrowers of America.

² See Livestock, Dairy and Poultry Outlook, U.S. Department of Agriculture Economic Research Service (hereafter "USDA-ERS"), LDP-M-154 (April 18, 2007), at 13 (explaining that the demand for imported seafood is influenced by "prices of competing protein products, such as beef, pork, and poultry."), available at <http://www.ers.usda.gov/Publications/LDP/2007/04Apr/LDPM154.pdf>.

³ 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>.

⁴ 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.").

product produced by Pilgrim's Pride, therefore, is a competing, substitute protein product capable of directly influencing the price and demand for cattle and beef through changes in the supply and price of poultry. A 2002 study by Sparks Companies, Inc., e.g., stated that "each 1% decline in poultry prices causes a 0.02% reduction in beef consumption,"⁵ and vice-versa.

Pilgrim's Pride is one of the largest chicken companies in the United States and Mexico, with a capacity to process more than 45 million birds per week for a total of more than 9 billion pounds of poultry per year.⁶ In 2008 the United States produced approximately 43.2 billion pounds of poultry in federally inspected plants.⁷ Thus, Pilgrim's Pride has the capacity to produce and control approximately 21 percent of all the poultry production in the United States. Pilgrim's Pride is a vertically integrated poultry firm that owns and controls poultry production from the egg to the consumer's plate.⁸ According to Sparks Companies, Inc., firms like Pilgrim's Pride that integrated the poultry industry reduced costs by coordinating production at each stage. As a result of this coordination, the U.S. poultry industry, "once characterized by tens of thousands of small, specialized businesses became characterized by hundreds of vertically integrated firms," which number was further reduced to about 50 in the 1990's through horizontal integration.⁹ The study claimed that the advantages of vertical integration to the integrating firm include, *inter alia*, lower cost of production from shifting capital investment in grow-out facilities to other parties, i.e., contract poultry growers.¹⁰

Pilgrim's Pride's complete control over every aspect of production of more than 20 percent of the nation's poultry production enables the company to fiercely compete with the cattle and beef industries. Due to the substitute relationship between poultry and beef products discussed above, Pilgrim's Pride can reduce the demand for beef, which would lead to reduced demand and prices for live cattle, by decreasing the price of its poultry products, thus increasing demand for its poultry products over beef. Pilgrim's Pride, because it is vertically integrated and no longer has to compete for live poultry produced by independent poultry farmers, is free to unilaterally decide whether the price it establishes to compete with beef includes any profits for the growing, or live poultry, production stage – the production stage historically performed by independent farmers. This factor gives Pilgrim's Pride a potential advantage in the competition over competing proteins when compared to the U.S. beef industry.

⁵ Potential Impacts of the Proposed Ban on Packer Ownership and Feeding of Livestock, Sparks Companies, Inc., McLean, VA, March 18, 2002, at 38.

⁶ See Pilgrim's Pride webpage available at <http://www.pilgrimspride.com/aboutus/>.

⁷ See Total Poultry: Supply and disappearance (millions of pounds) and per capita disappearance (pounds), USDA-ERS, available at <http://www.ers.usda.gov/Publications/LDP/LDPTables.htm>.

⁸ See Pilgrim's Pride webpage ("Pilgrim's Pride is a leading provider of retail poultry products for consumers. . ."), available at <http://www.pilgrimspride.com/business/>; see also *id.* (Pilgrim's Pride has 39 hatcheries that support the company's 31 chicken processing plants and it has approximately 5,000 growers that supply poultry for the company's operations), available at <http://www.pilgrimspride.com/aboutus/>; see also *En Banc* Brief for 54 Farming, Ranching, and Consumer Organizations as *Amici Curiae* in Support of Plaintiffs-Apellees, *Wheeler v. Pilgrim's Pride Corp.*, Case No. 5:02-CV-136 (explaining that Pilgrim's Pride enters into contracts with independent growers who raise Pilgrim's Pride chickens, known as broilers, under strict contractual standards set by Pilgrim's Pride.).

⁹ Potential Impacts of the Proposed Ban on Packer Ownership and Feeding of Livestock, Sparks Companies, Inc., McLean, VA, March 18, 2002, at 60.

¹⁰ See *id.*, at 61.

In 2008, before its acquisition of Smithfield Beef Group, JBS S.A.'s share of fed cattle packing capacity in the U.S. was close to 20 percent.¹¹ Following its acquisition of Smithfield Beef Group, R-CALF USA estimates that JBS S.A.'s share of fed cattle packing capacity in the U.S. is now over 25 percent.¹² Given JBS S.A.'s sizable share of the U.S. beef packing market, JBS S.A. currently is a dominant competitor to Pilgrim's Pride in the competing U.S. protein products market. But, unlike Pilgrim's Pride, JBS S.A. must compete with other packers for its live cattle supplies and, at least theoretically, JBS S.A. is not free to unilaterally decide whether the price it establishes for its beef includes any profits for the hundreds of thousands of U.S. farmers and ranchers from among whom JBS S.A. acquires its live cattle – theoretically, it is a competitive market that determines whether the suppliers of live cattle, i.e., cattle farmers and ranchers, receive a profit from the price of their cattle sold to JBS S.A. and other packers.

However, if JBS S.A. were to acquire its protein product competitor – Pilgrim's Pride – JBS S.A. would secure the means to manipulate both live cattle and beef prices by unilaterally varying the output of its Pilgrim's Pride poultry operation and the price of its poultry. Because of the inelasticity of supply in the cattle industry compared to the elasticity of supply in the poultry industry,¹³ this acquisition would give JBS S.A. a tremendous, anticompetitive advantage over U.S. farmers and ranchers who sell live cattle. For example, if JBS S.A. were dissatisfied with the level of profits earned in its beef packing operation – which profits are influenced by the “competitive” price it must pay for live cattle, JBS S.A. 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. But, unlike poultry, cattle have an extended biological cycle – in fact, the longest biological cycle of all meat animals¹⁴ – which would prevent cattle producers from adjusting supplies to timely respond to reduced demand. Instead, there would likely be acceleration in the ongoing liquidation of the U.S. herd and exodus of U.S. cattle producers from the industry.¹⁵ When the price of cattle falls to a level more to JBS S.A.'s liking, the firm can quickly restore higher poultry prices and reduce the volume of poultry production, enabling JBS S.A. to maximize its profits from the sales of both competing proteins until dissatisfaction returns once again and the cycle can be unilaterally restarted. Again, given the long biological cycle of cattle, JBS S.A. could enjoy several years' worth of maximized profits – a period when both cattle producers and beef consumers likely would be exploited.

In addition to the more specific concerns addressed above, R-CALF USA strongly believes the horizontal integration of competing protein products by market-dominant firms is inherently detrimental not only to competition among and between competing proteins, but also, to the hundreds of thousands of farming and ranching businesses that raise and grow the

¹¹ See *United States of America et al. v. JBS S.A. et al.*, United States District Court Northern District of Illinois Eastern Division, Complaint, at ¶3.

¹² Estimate based on data contained in the chart included in R-CALF USA's April 9, 2008, submission to the U.S. Dept. of Justice regarding the then proposed JBS S.A. merger with National Beef Packing Company, at 11.

¹³ 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.

¹⁴ See *id.*

¹⁵ On July 30, 2009, R-CALF USA submitted a presentation to the U.S. Department of Justice, Antitrust Division, that contained charts at pages 2, 9, and 23 that document the ongoing contraction of the U.S. cattle industry in terms of both the declining number of cattle operations and the shrinking size of the U.S. cattle herd.

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livestock and poultry needed to produce them. The result also would be fewer choices for consumers as the market presently defined as, e.g., the poultry market and beef market would be redefined as an “animal protein” market wherein, because there would be fewer close substitutes, firms could more readily exert market power and impose anticompetitive price increases for consumers.

R-CALF USA firmly believes that the proposed JBS/Pilgrim’s Pride merger would reduce competition and result in the exploitation of both producers and consumers. We respectfully request that the U.S. Department of Justice vigorously investigate the antitrust and anticompetitive aspects of this proposal and take all necessary enforcement action to prevent its consummation. R-CALF USA would appreciate the opportunity to provide any additional information to the Department of Justice that may be helpful in this case.

Sincerely,

A handwritten signature in black ink, appearing to read "Bill Bullard". The signature is stylized and cursive, with the first name "Bill" and last name "Bullard" clearly distinguishable.

Bill Bullard

CEO

Cc: The Honorable Herb Kohl
Select Members of Congress