Those of us involved in researching livestock markets and educating others about these markets have faced the challenge of doing so in an era of unprecedented change in these industries. We all sense the historical as well as the economic significance of these changes and must stand at least a bit in awe of what has been experienced. The challenge of preparing ourselves and those we serve to address these changes has been large. As a profession, we have had failures and successes in our attempts to accomplish our research, education, and extension missions during the last two decades.

The authors have done a good job of laying out many of the main areas of concern relating to changes in the price discovery process in livestock markets. If I have any criticism it would be their lack of attention to the what this market may look like in the future and what we need to do to fulfill our role in a new marketing system that could be substantially different than even what it looks like now. The other points I wish to make along with the author(s) are that

1) There is little scientific evidence that producers have been significantly harmed by non-cash pricing methods but this does not lessen the concerns of many of our constituencies. Thus we need to continue to talk to people about these issues while helping them adjust to a new market environment.
2) The market is more complex now and our programs need to address this complexity.
3) We are uncertain what the “proper” price discovery mechanism should be now and research needs to address this question.
4) Our role remains basically the same but our research and educational programs must rise to the new level of complexity and new market situations and opportunities producers face.

Over time, economic principles, although sometimes grinding slowly, continue to explain many of the changes in markets and industries. Beef and hog markets have been moving from open-market pricing to pricing mechanisms such as production and marketing contracts and formula pricing. This suggest that cash markets in these industries have become relatively ineffective in delivering products demanded by the market. Agricultural economists have long argued the inefficiencies that existed in average pricing of live animals. Since the mid-1990s, price differences between choice and select have been increasing suggesting greater incentives for packers to price based on quality (Figure 1). In an environment where quality has started to mean more and markets are more differentiated, it appears appropriate for the market to seek the means to reward high quality.
Another argument for increased integration and coordination is to reduce transactions costs (Williamson). In instances where transaction costs are high, and they are high in livestock markets (e.g., Bailey, Peterson, and Brorsen), inefficiencies can sometimes be reduced through integration or coordination. In such case, relationships within markets become increasingly important and stable. This may be what is occurring in livestock markets and suggests that transaction cost economics will emerge as one of the principal methodologies to explain these changes.

At least at present, there isn’t conclusive evidence to suggest that increasing non-cash transactions have had much negative impact on cattle producers. Schroeder and Ward’s statement that cash markets become less efficient (i.e., variance increases) as they become more thin is supported by past research (e.g., Stigler; Tomek; Ward et al.). Obviously, other moments of the price distribution are also important including the effect of thin markets on average prices (mean), and if any changes in market power have occurred (skewness). Schroeter and Azzam suggest that increases in non-cash transactions tend to depress spot market prices. This result does not necessarily indicate an abuse of market power on the part of packers. Its importance to individual producers depends on whether average prices actually received by producers are reduced as a result. Conceivably a good producer participating in non-cash transactions could achieve average net prices that are unaffected or perhaps even higher as a result of contracts or formulas rewarding quality. However, formula and contract prices tied to the cash market do pose a potential problem in thin markets since an incentive for manipulating cash prices in order to influence non-cash prices paid could exist. However, Schroeter and Azzam found no evidence in their study of packers in the Texas Panhandle to support the notion that the packers attempted to manipulate formula prices through their pricing strategies in cash markets.

In the absence of credible research results proving significant harm to livestock producers as a result of increased non-cash pricing activity, extension economists should focus on helping producers understand this new environment and provide them tools and analysis to identify management and marketing alternatives just as we always have. I appreciated Lawrence’s thoughts concerning the need to include management/marketing decision making tools in our extension programs as well as raising producers’ awareness about what has and is happening in these markets.

Feuz’s work on grid pricing shows that different grid pricing scheme’s offer different premiums and discounts for quality and is an example of how research can be used to teach producers the need to examine pricing alternatives based on quality. Since different pricing opportunities exist, producers should search for the optimal pricing scheme for the cattle they produce whether it is in the cash or contract market. These research results illustrate that the market is much more complex now and that the optimum pricing scheme may be different for each set of cattle. The number of variables involved (quality variables, premiums, discounts, etc.) in the pricing decision suggest the decision is probably made most efficiently using computer software decision-making tools of some kind. As long as feedlot operators maintain at least some
independence from packers, they will need to make these types of decisions and an educational opportunity is present.

To be effective, all these non-cash market pricing opportunities require an efficient pricing mechanism and transparency. Schroeder and Ward, suggest the need for research to determine the appropriate price discovery mechanisms in a declining cash market. If publicly available pricing information (futures, cash market, etc.) is not used to discover prices then it becomes difficult if not impossible for producers and researchers to reconstruct how a price was developed. Even now some of the formulas used to derive prices are so complex and it is virtually impossible to reconstruct these prices (Schroeter and Azzam). Being able to understand how a price is constructed (discovered) is fundamental to transmitting pricing information within the marketing channel and should be a requirement in any pricing scheme.

As Mintert points out, the tools and analysis we provide to producers must be research based and of high quality. The art of extension work is providing this information in ways lay audiences can understand and use to make decisions. Even with increased research sophistication, there is still no substitute for information skillfully presented in a manner average people can use. At the same time, extension economists need to expand their sources for research information. This means drawing on research results from a broad range of economics, agricultural economics, and other academic and trade journals as well as developing working relationships with researchers in our departments and with industry.

Koontz and Purcell discussion of research needs is important and gives us direction about some of the new theoretical directions we are being pointed to as livestock markets evolve. These new directions include examining the effect of thin cash markets on futures markets and the price discovery process in general and answering questions more adequately about how prices are formed. In a more applied vein, I believe we still need to focus on the forces for change in the livestock sector. By this I mean helping producers and other agribusiness understand better how to provide consumers with the types of products they want. Two forces in our economy seem to be changing how we live more rapidly than anything else. These forces are technology and increasing incomes (Figure 2). As one looks at the future, it seems almost certain that these forces will lead to more differentiation in food products including pork and beef. The consequences of this will be increasing management of supply chains. This suggests we will see even more integration in meat industries. Research and extension efforts will need to provide information not only about today’s market but also about what tomorrow’s market may look like. In short, I believe we need to be careful not to miss emerging opportunities by focusing too much on past issues. For example, opportunities and challenges appear to be materializing in the areas of product differentiation, quality assurance, and identity preservation and research and extension programs need to recognize the potential impact this could have on how business is done in meat supply channels.

Many opportunities exist for our profession to be involved in addressing issues relating to changing meat markets. There are many researchable questions and extension programs that can
and should be formed around the ideas presented at this symposium. Our challenge is to help each other limit the influence of politics surrounding the monumental changes which have and continue to occur in these industries and attempt to focus on programs that will give the proper decision-making tools and guidance that producers and agribusinesses need. I think this can only be accomplished by a supply chain approach since current and future changes will certainly be driven by technological change and downstream events.

References


Figure 1. Price Spread Between Boxed Beef Cutout Values in $/cwt, for Choice and Select Steers, 1986-2000 Regressed on a First and Second Order Time Trend.