Food, Agriculture, and Antitrust: Looking at the Recent Past

James MacDonald
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Why This Title?

• USDA-DOJ Task Force and Workshops
  – Has drawn a lot of interest
  – I can’t speak for them, or report on them

• But I can provide a framework
  – What are antitrust issues?
  – What antitrust issues have arisen in the food system?
  – How might concentration fit?
Basic Antitrust Topics of Coverage

• Explicit collusion (conspiracy)
• Mergers
• Practices that facilitate tacit collusion
• Practices that create or extend unilateral monopoly
The Starting Point is Welfare: Consumer and Producer Surplus
Explicit Collusion

• Agreements to fix prices or limit output
  – Criminal violation: jail time, fines, treble damages
  – Focus is on detecting conspiracy (The Informant!)

• There was a major policy change in the 1990’s
  – Increased use of jail time
  – Increased fines
  – Leniency programs
Explicit Collusion—Important Food System Cases

• Lysine (1990’s)
  – 3 jail terms, $100m in fines, plus treble damage suits

• Animal & human vitamins (1990’s)
  – 1 jail term, $875m in fines, plus treble damage suits

• Herbicides (2003)
  – 3 prison terms, $30m in fines

• Smaller cases in school milk, NYC school lunch (16 jail terms), cattle buyers, mushrooms (civil)
Collusion Policy Isn’t Overtly Ideological

• No significant shifts between Clinton & Bush

• Potential policy shifts are subtle
  – Resources
  – Carrots & sticks (ie, leniency programs)

• No change in U.S. legal standards in many years
Mergers: Background

- Charge to DOJ/FTC is to prevent those mergers *likely to reduce competition*

- Focus is on *likely price effects of merger*

- Merger guidelines focus on relevant market, level and change in concentration, ease of entry, and buyer behavior
Some More Merger Background

• Elite opinion matters for merger policy
  – Judges, academic lawyers, economists, & practitioners

• Elite opinion changed a lot over 40 years
  – Toward less of idea that ↑ concentration necessarily means ↓ competition
  – Based on plenty of evidence. But partly on ideology?

• Also, merger policy has become more regulatory
  – Negotiated settlements common
More Mergers Background

• Why should we care about mergers? Because collusion policy is about conspiracy, not prices or market power

• In principle, existing monopolies may be attacked (eg, AT&T)
  – But remedies are radical, & actions are costly & rare
Mergers: Food System Cases

- Seeds: Monsanto-DeKalb; Monsanto-Delta & Pineland; Syngenta-Advanta
- Equipment: Case-New Holland
- Grain: Cargill-Continental Grain
- Packing: JBS/Swift-Smithfield-National & Smithfield-Premium Standard
- Dairy: Dean Foods-Suiza
JBS Case Provides Useful Background

• 5/07: Brazilian-based JBS buys Swift (#3)
• 3/08: JBS/Swift buys National Beef (#4)
• 3/08: JBS/Swift buys Smithfield beef assets
  – Four slaughter plants (#5) & ten feedlots
• Steer and heifer CR4 would go to 85 from 81
• 10/08: DOJ files suit against acquisition of National; does not oppose Smithfield purchase.
• 2/09: JBS drops acquisition of National
The Smithfield Part of the Merger: Interesting but Irrelevant

• Irrelevant for antitrust purposes
  – Smithfield owned cow plants
  – Different input market (cows vs. s&h)
  – Different product market (ground beef)
  – Different locations (PA, WI, AZ, MI)
  – Implies no effect on prices

• Relevant market is steers&heifers/boxed beef
  – For s&h, a regional market?
National Beef was Relevant for Antitrust

• S&H procurement market is regional
  – Most cattle sellers (feedlots, usually) would see 3 potential buyers instead of 4, and DOJ argued that a CA/AZ market would go from 2 to 1.

• Boxed beef market is national and global
  – US boxed beef CR4 would rise a little
  – But really it would mean 3 sellers instead of 4
Would the Merger Lead to Efficiencies?

• There is evidence of scale economies...
  – 1980’s consolidation led to lower costs, prices

• But...
  – 1980’s consolidation realized bigger plants
  – Limited evidence of further scale economies
  – And you don’t need mergers for bigger plants
  – And authorities are sceptical of efficiency claims
Would One Less Competitor Affect Prices?

• Broad empirical evidence: Cournot matters
  – Numbers matter, but at diminishing rate
  – But judges often want to believe in pure Bertrand

• Lots of cattle and beef studies, but they weren’t directly relevant
  – Limited evidence of market power at existing levels of concentration
  – But, there’s a mystery to that (why do packers compete?)
  – And, this deal would remove a competitor
Aside: Stock Market Evidence

- If the merger were to make Swift/National a lower cost competitor…
  - What should happen to the profits and stock prices of Tyson and Cargill (#2 and #3 packers)?
- Alternatively, if the merger were to lead only to reduced competition…
  - What should happen to the profits and stock prices of Cargill and Tyson?
Aside: Stock Market Evidence

• Cargill is privately held (no stock quotes)
• But Tyson Foods stock…
  – Rose 8.5% on announcement of deal
  – Fell 4.0% on announcement of DOJ opposition
  – (each is relative to overall market)
• And Smithfield (competes as pork processor)
  – Rose 4.5% on announcement of deal
Compare to Smithfield-Premium Standard

• 9/06 Smithfield announces purchase of PSF
  – DOJ closes investigation in 4/07
• PSF raised about 4.5% of US hogs, and had slaughter plants in MO and NC (4% of US capacity).
• Smithfield raised 14% of U.S hogs, and processes about 27% in NC and Midwest
• Procurement CR4 would ↑ to 66 from 62
Issues in Smithfield-Premium Standard

• Pork market: national
  – Multiple competitors and recent entry (Triumph)

• Key issues fell to procurement markets
  – Independent, for hogs, and contract, for growers
  – Regional markets for market hogs, larger for pigs

• DOJ argued that merger would not affect prices in MO—other packers and growers

• NC: DOJ argued that producers could ship to Midwest
Merger Policy Summary

• Defining the market is crucial
  – Then, will removal of this competitor impact prices?
  – Small numbers (4, 3, 2) matter
    • Specific relevant price evidence usually lacking
  – Evidence on entry barriers matter
  – Evidence on buyer mobility matters
    • Can they find alternatives?
Comments on Merger Policy

• There’s a broad elite consensus, and change happens at the margins
  – You can lessen enforcement by not bringing cases
  – To expand enforcement, need to convince judges
    • That is, you need to win the case
  – You also need merger attempts to develop an expanded policy
That Brings Us to Practices

- **Facilitating practices** that limit the intensity of price competition among competitors.
  - Example (Rich Sexton): whole-dollar bids and MFN clauses in markets for fed cattle

- **Practices that create or extend monopoly**
  - Tying, network refusals to deal, exclusionary pricing, exclusive dealing
  - Example: Dentsply (dominant seller of false teeth refused to provide top line to dealers who carried other brands).
Price-fixing is per se illegal, but mergers and practices are rule of reason

• That means weighing efficiency and market power elements—particularly for practices.

• Concentration & market power matter a lot: it’s easier to facilitate among a small number of players, and easier to create/extend if there are few options for players on the other side.
Food and Agriculture are Interesting in this Regard

• Lots of concentrated markets
  – Input markets: seeds (& chemicals), some equipment, rail transport,
  – Product markets: livestock & dairy processing; some grain processing, retail?

• Lots of changing markets
  – Shifts to larger farms everywhere

• Lots of politics, especially this year
Food and Agriculture are Interesting…

- Lots of distinctive contractual relationships and business practices
  - Production contracts
  - Some marketing contracts
  - Markets for seed and for associated ag chemicals
  - Coop exemptions
  - Retailer procurement arrangements
What’s Coming?
(my opinion)

• Workshops can provide more information on practices, which are poorly understood
  – Will also generate complaints, some relevant

• Practices are where policy change can be made

• Mergers: need test cases for more aggressive policy