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The Proceedings of Economic and Policy Implications of Structural Realignment in Food and Ag Markets

**A Case Study Approach
(Proceedings Include Revisions)**

The Food and Agricultural Marketing Consortium Research Conference
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Discussant's Comments on:

**WHAT CAN WE LEARN FROM THE
ADM GLOBAL PRICE CONSPIRACIES?**

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I would like to compliment John Connor on the excellent documentation and analysis he has provided, in articles and papers, of the major price fixing cases during the 1990s involving Archer Daniels Midland (ADM) as a lead conspirator. He has clearly shown the degree to which ADM richly deserves to be called "price-fixer to the world". In this paper, John asks what we can learn from the ADM global conspiracies and provides many answers. I will comment on these lessons and pose some further questions.

The case study focuses on the price fixing conspiracy in the citric acid market. In 1990, there was new entry accompanied by technical change when Cargill began production in a lower cost, integrated feedstock plant. Cargill went immediately from 0% to 33% of U.S. production capacity. In response, ADM accelerated its entry into the market by acquiring plants

owned by Pfizer, significantly upgrading and expanding one of the plants. Other major players who were to join the price fixing conspiracy with ADM were less able to respond to the changed environment.

As Cargill entered the market, it used low introductory prices to signal its status as low cost producer and initial tough stance. The stage could have been set for a price war but Cargill increased its prices and other major players in the market formed a price fixing conspiracy. Why a conspiracy? One way to explain it is that the short-term losers in the new market structure and environment tried to protect their positions. Cargill was not an active participant in the conspiracy but a beneficiary of higher prices all the same. Thus the conspiracy served to prevent an outbreak of competition in a highly concentrated but changing industry. In fact, the conspirators actually socialized their part of the market through a system of side payments to companies who did not achieve their assigned market shares.

While this is an interesting lesson to learn, it is fascinating to compare ADM's role in the citric acid case to its role in the contemporaneous lysine conspiracy (Connor 1997). There ADM was the disruptive entrant, opening a new plant in 1991 that doubled world capacity. It punished competitors with very low prices for more than a year until they entered into a worldwide market sharing agreement. Thus, in a position similar to that of Cargill in the citric acid market, ADM acted very differently in the lysine market. It turned to explicit price fixing rather than simply using its market power in the market.

Why the difference in behavior between Cargill and ADM? The market structure in the two industries, technological considerations, and trade conditions were similar in many respects. Both involved homogeneous goods and highly concentrated markets. Is it simply a matter of differences in corporate culture, with ADM taking a cooperative stance towards its competitors while Cargill does not? I will look forward to further analysis and comparison across markets from John and other economists studying these conspiracies.

John draws three key lessons from the citric acid case itself. First, market structure matters. The players operate in highly concentrated markets, with high entry barriers and a history of tacit collusion. At a time of industry change, more explicit collusion in the form of price fixing was the strategy of choice for some of the players. Second, setting up and operating a market sharing cartel proved to be surprisingly easy in this type of industry. Cheating could be easily monitored and the small number of players facilitated coordination. Third, the penalty for getting caught is now five times the cartel's illegitimate profits, which is much stiffer than in the past. It includes a two-times felony penalty in the government case and triple damages in private cases. However, as noted below, the overall size of the penalty continues to depend on the methodology for estimating the overcharges and the determination of the time during which the conspiracy was operating.

There are further questions to be answered, or to be answered more fully, and lessons to be learned from case studies of the price conspiracies in which ADM was involved. The first is how landmark conspiracy cases such as these can be used to predict future conspiracies. A corollary question is the likelihood of conspiracies in industries with somewhat different characteristics. Certainly market structure matters in this prediction but the key to the ADM conspiracies appears to be this plus other factors. These factors include new entry, with technical change and expanded capacity, resulting in a period of realignment of competitive relationships in a market that remains highly concentrated. In the period of disruption that follows, companies adopt different strategies to adapt. Perhaps the losers and the less well positioned companies join a price conspiracy. In the citric acid case this group included ADM and they were part of the conspiracy. Cargill, the advantaged disrupter, was not an active member. However, in the lysine case ADM was the advantaged disrupter and there, too, it joined a conspiracy. A comparative case study may be able to explain this difference in strategic approaches between the two companies.

The second and continuing question is the measurement over time of the performance impacts of tacit and explicit collusion. If we can expect to see more of the agricultural ingredient markets become or remain concentrated, what will be the performance of these markets and what are the possibilities for changes in performance? The markets involved are highly concentrated and ripe for tacit collusion and elevated prices. Technical change and entry may occur but it is frequently by the same set of major players who have ample experience with each other across many markets. Although a period of disruption may ensue, and an explicit conspiracy may operate for a period, when the cartel ends the same environment for tacit collusion remains.

In this situation it is difficult to estimate the overcharges due to the explicit collusion, as John points out in his case study and analyzes in depth. For example, in what sense is the perfectly competitive price a realistic measure of the "but-for" price that would have prevailed if the cartel had not been operating? If the realistic comparison is to the prevailing price under

tacit collusion, then the degree of price elevation will be much smaller, although it may still be significant. In the end, where will real competitive pressure come from in these ingredient markets? Will it come from fringe importers, powerful buyers, or alternative ingredients? John notes that fringe importers had an impact on the operation of the citric acid cartel but does not fully discuss the nature of that impact. How much competition will alternative ingredients provide if the structure of those markets is also highly concentrated?

The third question is the conditions under which more globalized markets are likely to facilitate or discourage explicit and tacit collusion. John suggests the conspirators in the ADM case were surprisingly able to conspire across distance and culture. With better communication and detection technologies, it may now be easier to conspire but it could also be harder if detection by outsiders, including government, is easier. In the ADM cases, the conspirators were able to elevate prices and avoid price wars that could have erupted as new capacity entered the market. This leads to a fourth question: Would the conspiracies ADM was involved in have been detected, and how soon, if the Department of Justice had not had Mark Whitacre as a mole within ADM?

John's case study and other papers underscore the age old attraction of a well-greased price conspiracy to companies in concentrated markets. They also underscore the need for vigilance by antitrust agencies and the desirability of significant penalties for those companies and individuals who violate the law.

Reference

Connor, John M. 1997. The Global Lysine Price-Fixing Conspiracy of 1992-1995. *Review of Agricultural Economics* 19 (Fall/Winter):158-174.