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A Comparative Assessment of Marketing Arrangements Employed in Livestock and Meat Industry Supply Chains

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Overview of Presentation

- Background and purpose of the GIPSA Livestock and Meat Marketing Study
- Supply chain segments in the livestock and red meat industries
- Classification system for characterizing spot and alternative marketing arrangements
- Key comparisons in use of alternative marketing arrangements across
 - Livestock species (horizontal comparisons)
 - Supply chain segments (vertical comparisons)
- Key terms defining alternative marketing arrangements

Background and Purpose of the Livestock and Meat Marketing Study

- Funded by Congress in 2003; awarded to RTI International in July 2004
- Purpose: conduct a broad study of the effects of **alternative marketing arrangements** in the livestock and meat industries
 - Fed cattle and beef
 - Hogs and pork
 - Lambs and lamb meat
- Results will be used by the Grain Inspection, Packers and Stockyards Administration (GIPSA) to determine what policy changes are needed to address concerns about marketing practices in the livestock and meat industries

What is an Alternative Marketing Arrangement (AMA)?

■ Cash or spot markets

- Auction barns
- Video/electronic auctions
- Dealers or brokers
- Direct trade
 - ◆ Order buyers
 - ◆ Buying stations

■ AMAs

- Forward contracts
- Marketing agreements
- Marketing contracts
- Production contracts
- Packer-owned farms
- Custom feeding
- Custom slaughter

Status of the LMMS Study

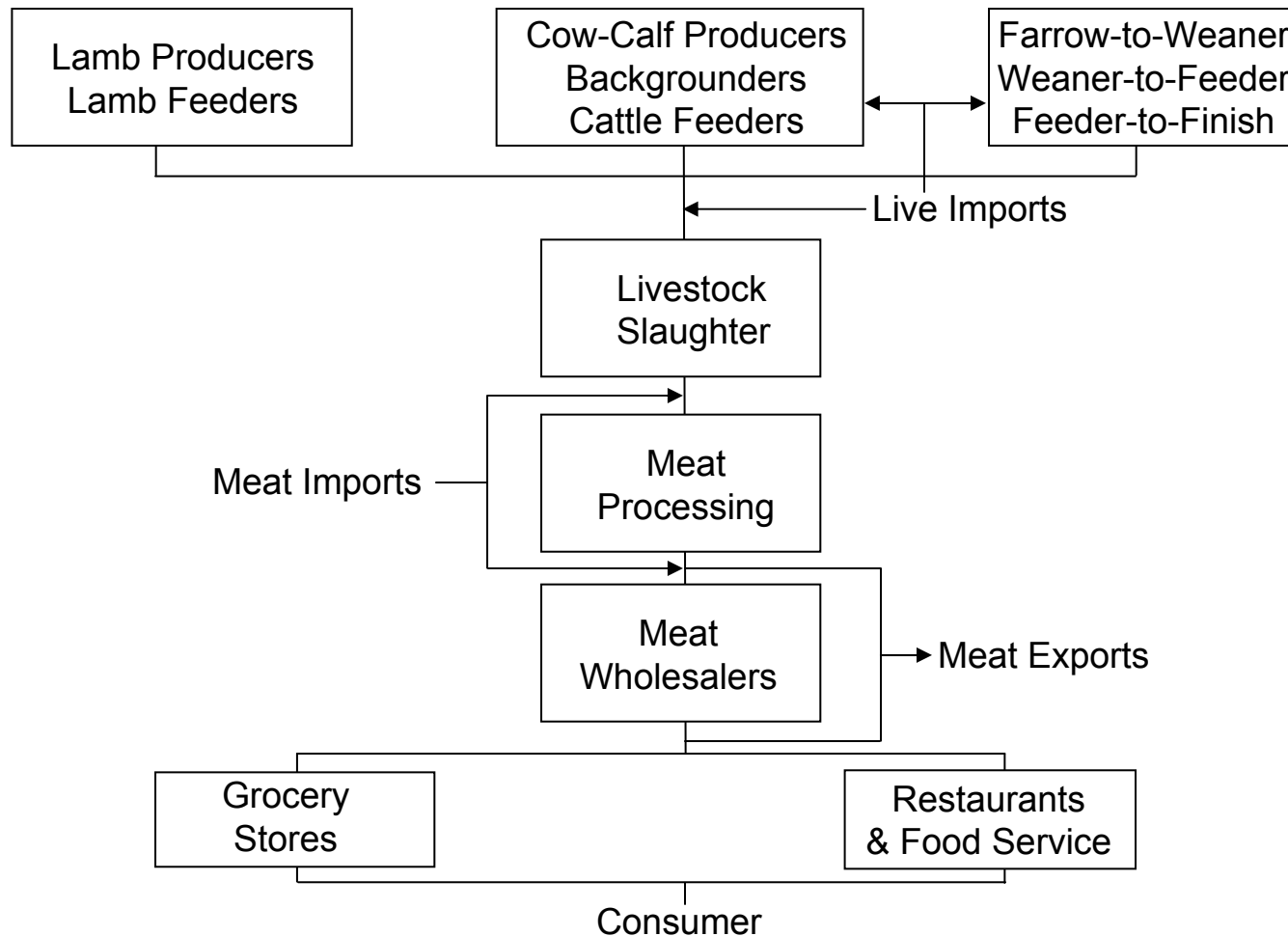
■ Completed activities

- Development of red meat industry profiles
- Review of economic and applied studies on use of AMAs
- In-depth interviews with industry participants
- Description and classification of AMAs
- Qualitative assessment of reasons for using and effects of AMAs

■ In-progress activities

- Compilation of industry survey results
- Compilation of transactions, profit & loss, and contract settlement data
- Analysis of price effects of AMAs
- Analysis of costs and benefits of AMAs
- Analysis of implications of AMAs

Red Meat Industry Supply Chains



Market Participants in Livestock and Meat Supply Chains

Livestock producers	Breeding, growing, and feeding operations
Slaughter establishments	Single or multiple species
Meat processors/breakers	Single or multiple species
Wholesalers	Meat, frozen food, grocery, and food service wholesalers
Exporters	Meat exporters
Food service operators	Full-service restaurants, limited service operations, and institutions
Retailers	Supermarket chains, independent grocers, club stores, mass merchandisers, meat markets

Basic Characteristics of Alternative Marketing Arrangements

- Procurement or sales method
- Ownership method of the animal or product
- Pricing method (or practices)
 - Includes specifying formula base if formula pricing
 - Includes internal transfer pricing method if internal transfer
- Valuation method (applies to livestock)



Source: USDA

Spot (or Cash) Markets: Livestock Transactions

Feeder & Fed Cattle	Weaner, Feeder, & Finished Hogs	Feeder & Fed Lambs
<ul style="list-style-type: none">■ Auction barns■ Video/electronic auctions■ Dealers or brokers■ Direct trade including order buyers	<ul style="list-style-type: none">■ Similar to beef but direct trade also includes buying stations operated by packers	<ul style="list-style-type: none">■ Similar to beef but fewer auction locations

- Pricing methods:
 - Public auction bids (and some sealed bids)
 - Individually negotiated pricing
 - Posted prices

AMAs under Producer or Feeder (but not Retained) Ownership: Livestock Transactions

Feeder & Fed Cattle	Weaner, Feeder, & Finished Hogs	Feeder & Fed Lambs
<ul style="list-style-type: none"> ■ Forward contracts ■ Marketing agreements 	<ul style="list-style-type: none"> ■ Forward contracts ■ Marketing agreements ■ Procurement or marketing contracts 	<ul style="list-style-type: none"> ■ Forward contracts ■ Marketing agreements

- Pricing method is generally formula pricing:
 - Usually based on publicly reported prices
 - Valuation is on a per head or per pound (live weight or carcass weight)

AMAs under Producer or Feeder Retained Ownership: Livestock Transactions

Feeder & Fed Cattle	Weaner, Feeder, & Finished Hogs	Feeder & Fed Lambs
<ul style="list-style-type: none">■ Custom feeding for producer■ Custom slaughter	<ul style="list-style-type: none">■ Production contracts with sow operator as integrator	<ul style="list-style-type: none">■ Custom feeding for producer■ Custom slaughter

- Pricing methods:
 - Custom feeding = fee for service
 - Custom slaughter = fee for service
 - Production contracts = compensation formula for services

AMAs under Packer Ownership: Livestock Transactions

Feeder & Fed Cattle	Weaner, Feeder, & Finished Hogs	Feeder & Fed Lambs
<ul style="list-style-type: none"> ■ Packer feeding in producer-owned feedlot ■ Packer feeding in packer-owned feedlot 	<ul style="list-style-type: none"> ■ Production contract with packer ■ Company-owned farms 	<ul style="list-style-type: none"> ■ Packer feeding in producer-owned feedlot ■ Packer feeding in packer-owned feedlot

- Pricing methods:
 - Custom feeding = fee for service
 - Production contracts = compensation formula for services
 - Packer or company owned = internal transfer price

AMAs Used for Meat Transactions (Except Custom Slaughter)

Procurement or Sales Method	Pricing Method
<ul style="list-style-type: none">■ Direct trade■ Dealers and brokers	<ul style="list-style-type: none">■ Individually negotiated pricing■ Price lists
<ul style="list-style-type: none">■ Forward contracts■ Marketing agreements	<ul style="list-style-type: none">■ Formula pricing (various bases)
<ul style="list-style-type: none">■ Internal company transfers	<ul style="list-style-type: none">■ Internal transfer pricing

- Other pricing practices might also be used: two-part pricing, volume discounts, exclusive dealings, bundling

Additional Terms of Marketing Arrangements

- Oral or written agreements
- Transportation arrangements
- Time period in advance of delivery
- Contract duration
- Quantity requirements
- Quality requirements
- Measurement of quality
- Information provided to seller
- Dispute resolution
- Termination options



Source: USDA

Examples of Differences in Contract Terms Between Cash Markets and AMAs

	Cash Markets	AMAs
Format	All oral	Oral or written
Negotiation period	Negotiated <2 weeks ahead for livestock; <3 weeks ahead of meat	Negotiated weeks, months, or years prior to delivery
Duration	Not applicable	Single lot to multiple months, multiple years, or evergreen
Quality measurement	Often based on visual inspection	Based on carcass quality grading or other measures
Information exchange	No information provided back to seller	Might include individual lot or animal quality measures

Other Considerations in AMAs

- Role of other organizational arrangements:
 - Alliances for production or marketing objectives
 - Cooperatives
 - ◆ Slaughter operations
 - ◆ Meat processing operations



Source: USDA

Relationship between AMAs and Alliances

- Alliances are common in the beef industry but rare in the pork and lamb industries
- Most alliances are vertical relationships
- Alliances are relationships formed by two or more industry participants
 - To meet common production or marketing objectives (e.g., associated with seedstock or product branding)
 - To improve information flow along the supply chain

Cooperatives for Packing and Processing

- Common in the lamb industry but also occurs in the beef and pork industries
- Producers own cooperative shares that designate the number of head delivered for slaughter annually
- The cooperative sells carcasses or meat products on behalf of the producer-owners
 - Often involves agreements to sell product to specific restaurants or grocery stores

Conclusion

- Characterization of marketing arrangements will provide a foundation for the next stage of the Livestock and Meat Marketing Study.
- The next stage focuses on analyzing the effects of AMAs on
 - Prices and quality of livestock and meat
 - Costs and efficiency of production and marketing
 - Risk shifting among industry participants
 - Economic welfare
- At the producer and packer levels, more similarities in use of AMAs exist between beef and lamb than between beef and pork.
- Fewer types and somewhat less complex marketing arrangements are used in downstream meat markets compared to the producer and packer levels.

July 2005 Livestock and Meat Marketing Interim Report

The report can be accessed at:

[http://archive.gipsa.usda.gov/psp/issues/
livemarketstudy/LMMS_Interim_Report.pdf](http://archive.gipsa.usda.gov/psp/issues/livemarketstudy/LMMS_Interim_Report.pdf)