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

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USDA Economists Group Talk

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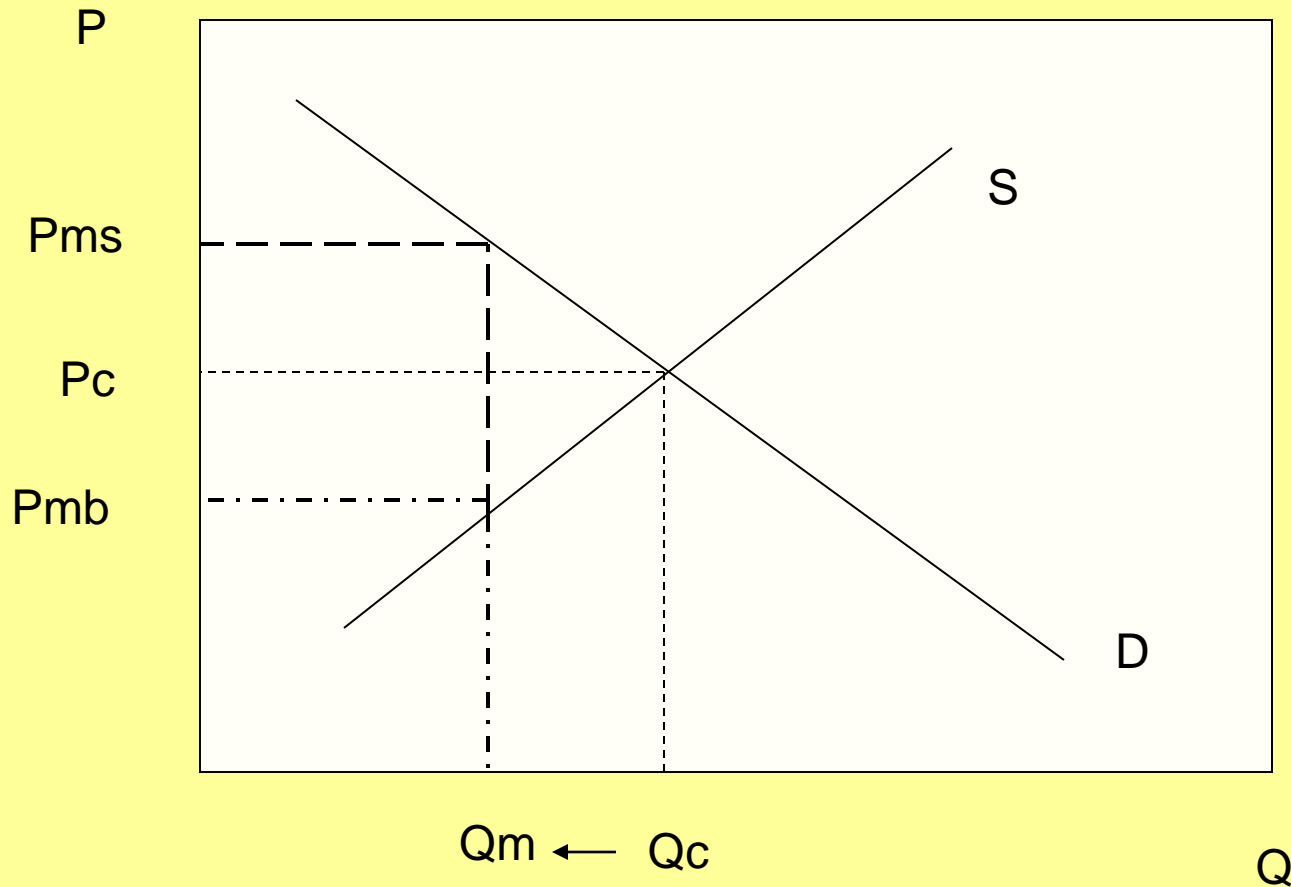
# Why This Title?

- 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  $\uparrow$  concentration necessarily means  $\downarrow$  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