

# Organization for Competitive Markets Briefing Paper

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## When Small Is Big

Livestock economists who look only at cash movement and do not analyze profitability outcome sometimes conclude that the effect of market power and captive supplies is “small.” They dismiss this “small” impact lightly, but ignore the fact that the impact they concede is the difference between profit and loss – the economic equivalent of the difference between life and death. The “small” impact of market power and captive supplies has the same life-stifling impact on many producers, as does the difference between healthy and dangerous oxygen levels in a person’s blood. Three (3%) percent can mean life or death.

Clem Ward, livestock economist at Oklahoma State University, in a DOJ submission, concludes the small negative impact of captive supplies is 3% of the gross sale price of slaughter cattle.<sup>1</sup> The 3% goes to the packer but should go to the producer. 3% of a \$1,000 animal is \$30. Iowa State University's John Lawrence's estimated returns to feeding a No. 1 steer calf to choice grade averages \$24/head over the past 30 years (in current dollars).

Over the 1981-1994 period—essentially before captive supply—inflation adjusted returns averaged \$42/head. A “small” captive supply impact of 3% means a downward loss of more than 71% of total profit! This is a whopping sum! Consider, Mr. Economist, the impact of a 71% decline in your university salary! Small? Indeed!

This is not the only commonplace mistake made by economists who discount the debilitating impact of market power and concentration on cattle prices. Some livestock economists like Ward assume the antitrust SSNIP test (5%) applies to Packers & Stockyards Act (PSA) issues.<sup>2</sup> SSNIP means Small but Significant and Non-transitory Increase in Price. (Applied to buyer power this would refer to a decrease in price.) The economists are Wrong again! The SSNIP test is not a part of PSA or body of PSA case law.

In competitive markets it is reasonable to expect returns averaged over business cycles to be about the same. But, this has not been observed in the fed cattle industry. Lawrence’s feeder returns in current dollars, in essence averaged over cattle cycles, are:

- \$42/head averaged over Jan.1981-Dec. 1994
- \$8/head averaged over Jan. 1995-May 2010
- -\$13/head (loss) averaged over Jan. 1995-May 2010 omitting the spike in returns due to the Canadian ban.

The difference in results before and after captive supplies dried up the cash market for fed cattle is \$55/hd (+\$42 vs -\$13). That is about 5% of selling price for fed cattle. It represents a sum most producers would love to earn on an ongoing basis. Three percent (3%) is a huge sum economically. Anyone trying to live on a fixed investment income knows the difference between a 5% and a 2% return on certificates of deposit.

So, why is it so hard for pro-concentration livestock economists to get it?

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<sup>1</sup> Clem Ward, “Economics of Competition in the U.S. Livestock Industry,” DOJ submission, Jan. 26, 2010, p. 25.

<sup>2</sup> Ward, p. 25.