Friday, April 29, 2022

Chairwoman Debbie Stabenow
Senate Agriculture, Nutrition & Forestry Committee
328-A Russell Senate Office Building
Washington, DC 20510

Ranking Member John Boozman
Senate Agriculture, Nutrition & Forestry Committee
328-A Russell Senate Office Building
Washington, DC 20510

RE: Comments of the National Pork Producer Council (NPPC) on Senate Agriculture Hearing to Review S. 3870, The Meat and Poultry Special Investigator Act of 2022

Chairwoman Stabenow and Ranking Member Boozman,

The National Pork Producers Council (NPPC), which represents the interests of America's more than 60,000 pork producers, respectfully submits the following comments for the record in response to the April 26 hearing covering S. 3870 titled, "The Meat and Poultry Special Investigator Act." While NPPC remains supportive of antitrust enforcement, specifically for the Packers and Stockyards Act (PSA or the Act), significant concerns exist regarding the proposal to create a new position within the United States Department of Agriculture (USDA) specifically tasked with the Act's enforcement.

Concentration in Pork Packing and Lack of a Clear Need

The fundamental understanding that this bill is based on is that meatpacking is an overly concentrated sector that has allowed its largest participants to put downward pressure on producer prices and upward pressure on consumer prices. Indeed, meat prices have played a central role in discussions surrounding rising consumer costs over the course of the pandemic. According to the Bureau of Labor Statistics (BLS), pork prices have increased, on average, 15.3% over the past year.[1] As discussed below, these price increases are attributable to a number of non-concentration causes. Nevertheless, this bill follows the current administration's contention that high levels of concentration within the meatpacking sector are to blame for these price increases, even though data regarding the industry's level of concentration, comparative global prices, and packer margins do not substantiate these claims.

Analyzing Industry Consolidation

Regarding concentration within the pork packing industry, it is important to analyze the current status of the industry, as well as its direction in terms of consolidation. The Herfindahl-Hirschman Index (HHI) is a widely accepted measurement utilized by the Department of Justice (DOJ) when evaluating the consolidation of a given industry. The index ranges from 0 to 10,000, with the Department considering HHI values less than 1,500 to be "unconcentrated" while values between 1,500 and 2,500 are "moderately concentrated" and an HHI above 2,500 is "highly concentrated."[2] Based on packing capacity estimates, the HHI for the pork packing sector currently sits at 1,345, which would be considered unconcentrated by DOJ classifications.[3]

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[1] https://www.bls.gov/news.release/cpi.t02.htm
[2] https://www.justice.gov/atr/file/810276/download
[3] https://nppc.org/wp-content/uploads/2021/06/Competition_Paper_FINALWD.pdf

Moreover, the pork packing industry isbecoming progressively less concentrated since 2016. The current HHI value of 1,345 is down from 1,528 in 2016. This deconcentration is also evidenced by other measures of industry consolidation. The CR-4, another commonly used measure of concentration, measures the market share of an industry's four biggest participants. The CR-4 for pork processing has fallen from 72% to 64.5% since 2016 – a figure closer to the levels of concentration in the mid-2000s. This deconcentration is largely attributable to the opening of new cooperative and independently owned packing plants that have grown in popularity.

Looking at the healthy competitive position of pork packing and its continued deconcentration, it is difficult to justify a need for an office specifically charged with new antitrust enforcement powers. It is even more difficult to understand when comparing concentration levels of other industries. For example, the CR-4 for meatpacking across all animal verticals measured 63.4% in 2017. Looking at other sectors at the 6-digit North American Industry Classification System (NAICS) code level for the same year, there are over 100 industries that had a higher CR-4, including courier and delivery services, computer storage manufacturing, aircraft manufacturing, and car rental services.[4] Were Congress to create new political appointments for any of these more concentrated industries at the Departments of Commerce or Transportation to individually handle civil enforcement outside of the existing DOJ framework, it would be cumbersome to enforce and complex to regulate. It is confusing that Congress would consider a move towards a sector-specific model like this for any industry, especially for an industry that is not highly concentrated.

Meat Price Increases Compared Internationally

Looking at food prices globally can also reveal whether price increases that American consumers face are unique to our food system. Recently the United Nations Food and Agriculture Organization (FAO) reported a year-over-year increase in global meat prices of 19%.[5] Comparing this to the Bureau of Labor Statistics report of year-over-year domestic meat price increases of 14.8%, demonstrates that rising prices found at home are not just in line with global trends, but rather better than them.[6]

It is likely that the efficiency of U.S. food manufacturing – specifically livestock production and meat processing economies of scale – has allowed American consumers to avoid further effects of global supply chain interruptions that are the evident culprits for high food prices. This is not suggesting that high food prices are not an intense issue facing American consumers. However, it strongly indicates that the causes of elevated food prices domestically – at least within the meat sector – are likely not due to a factor that is unique to the structure of our domestic industry.

Analysis of Packer Margins During the Pandemic

At the core of the drive to increase competitive scrutiny of the meat industry is the idea that processors are utilizing power derived from their purported market domination to widen their margins dramatically and at the expense of both consumers and producers. Pork producers are highly sensitive to the margin between farm and wholesale prices as, like every other agricultural producer, growers seek to maximize

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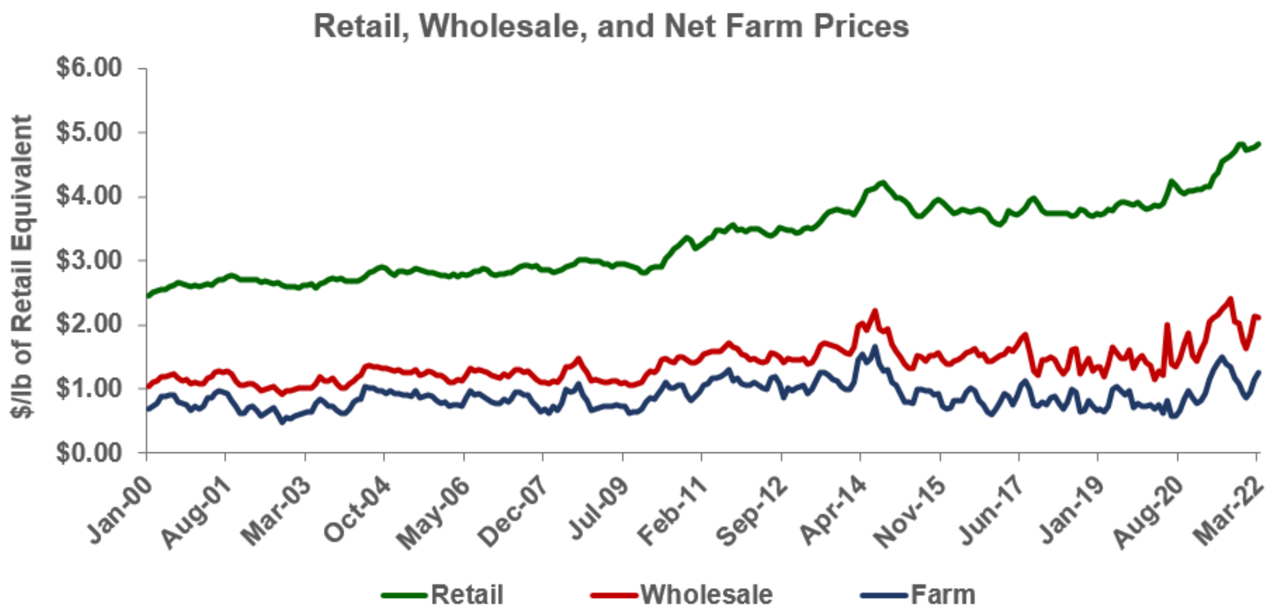
[4] https://itif.org/publications/2021/06/07/no-monopoly-has-not-grown
[5] https://www.fao.org/worldfoodsituation/foodpricesindex/en/
[6] https://www.bls.gov/news.release/cpi.t02.htm

their profits. However, there is little evidence to suggest that packers have utilized any market power, even during the pandemic.

The farm-to-wholesale price spread, which includes the operating costs of the packer as well as the packer's profit margins, widens when wholesale price increases outpace farm prices. The wholesale-to-retail price spread, which includes the retailer's costs and profit margins, becomes narrower when wholesale prices rise faster than retail prices. If packers were exercising market power to capture greater profits, the expectation would be for the farm-to-wholesale price spread to grow and the wholesale-to-retail price spread to shrink.

Instead, the opposite has occurred. As indicated in *Figure 1* below, the farm-to-wholesale price spread has declined and is down nearly 5% over the last twelve months despite average weekly wages, transportation costs, and packaging costs rising within the industry. The wholesale-to-retail price spread was up 28% over the same period due to added retailer costs and a potentially lagged response to high wholesale prices.

Figure 1



Source: USDA Economic Research Service

<u>Concerns Relating to the Proposed Packers and Stockyards Enforcement Structure</u>

Pork producers are not against enforcement of the Packers and Stockyards Act. Producers understand there needs to be government intervention when processors engage in price-fixing, fraud, or retaliation against growers. However, in addition to the question of whether the meat industry's current concentration levels justify a special investigator, NPPC has significant concerns as to whether or not the change in structure would be a positive one, as the Packers and Stockyards Division (PSD) at the Agricultural Marketing Service (AMS) already plays a key enforcement role. Additionally, creating a political appointee role for this task invites a significant degree of concern.

The Existing Framework is Sufficient to Enforce the Packers & Stockyards Act

PSD is the arm of AMS charged with monitoring compliance with the Packers and Stockyards Act. As it currently stands, the Division enjoys a significant amount of authority to investigate whether entities subject to the Act are violating any of its provisions. Enforcement actions under the authority of the Secretary and without interaction with the DOJ include entering stipulation agreements outside of formal legal action, issuing public notices of violation, and administrative actions taken within USDA. While issues relating to the major change of giving the newly created position the ability to bring civil action outside of DOJ are discussed below, PSD already has a significant amount of authority and enforcement powers. Additionally, the PSD is making good use of its authority. Based on PSD published statistics, the number of administrative actions it has brought has been substantial across both the Trump and Biden administrations.[7] The White House seems to agree that PSD has significant ability to meaningfully enforce the Packers and Stockyards Act. In its FY2023 budget, the White House asks for a 40% increase in PSD funding and outlines the wide-reaching and important work of the Packers and Stockyards Division.[8]

As it currently stands, the DOJ Antitrust Division has over $192 million appropriated to it in the recent Omnibus package (and a $273 million request from the White House for FY2023).[9] [10] While that number is currently less than what many antitrust enforcers would like to see allocated to the Division, it is significantly more than all of the resources that would be theoretically marshalled to USDA in support of this new enforcement regime – especially given the current sharing of responsibilities and funding with the Federal Trade Commission (FTC) and the PSD. If funding for the DOJ Antitrust Division increases even partially towards the President's request, enforcement abilities will be even more substantial. It is clear that the proposed changes would not improve and would perhaps reduce the resources allotted to pursue antitrust action in agriculture – including under the Packers and Stockyards Act – as it currently stands, as the new office would not come close to matching DOJ's resources.

One example of the intense resources necessary to allocate to this new office just to get close to the enforcement level that DOJ brings, is the need for a national structure to pursue civil actions. Currently, Packers and Stockyards Act suits are brought either in the district in which the violations occur or the district in which a defendant has its principal place of business or resides, depending on the nature of the suit. This means that the new office will either continuously travel from their DC office or limited field offices or create new offices around the country to argue in front of district courts. In either case, the financial and human costs will be exceptionally high. The DOJ, on the other hand, is already experienced, equipped, and accustomed to bringing antitrust actions and actions for violations of the Packers and Stockyards Act in district courts nationwide.

What seems to be the administration's primary concern is a lack of prioritization in enforcing the Act, not the structure itself. As evidenced by the President's Executive Order on Promoting Competition in the American Economy and the DOJ/USDA joint statement on prioritizing matters related to competition in agriculture, the administration has made significant investments in operating within that structure. New measures taken by the administration within the existing structure include the USDA and DOJ's joint

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[7] https://www.ams.usda.gov/services/enforcement/psd
[8] https://www.whitehouse.gov/wp-content/uploads/2022/03/agr_fy2023.pdf
[9] https://www.congress.gov/bill/117th-congress/house-bill/2471/text?q=%7B%22search%22%3A%5B%22hr2471%22%2C%22hr2471%22%5D%7D&r=1&s=5
[10] https://www.whitehouse.gov/wp-content/uploads/2022/03/jus_fy2023.pdf

creation of the new Packers and Stockyards Act violation reporting tool that allows parties to submit complaints to both the USDA and the DOJ, and a review of possible improvements to information sharing.[11] [12] This bill would effectively remove the DOJ – which has substantial experience enforcing the antitrust laws in the agriculture industries – from most enforcement of the Act. Considering the recent commitments to increasing the focus on enforcement within the agriculture space, it seems premature to change the framework under which the enforcement operates.

Concerns with the Position Being a Senate Confirmed, Political Role

Perhaps producers' largest underlying objection to this bill is giving substantial unilateral authority to this new political role. This position, especially with its first nominee, will face enormous pressure to justify their appointment and the existence of the office as a whole. One of the many benefits of the DOJ's handling civil action is that they must evaluate the likelihood of a legal action's success. The decision-making process to pursue a case is simple, fact-based, and comes with significantly fewer financial barriers to action. Moreover, DOJ antitrust enforcement decisions are made independent of political influence. This allows for the most efficient allocation of federal government resources for civil and criminal action. Substituting this system with funding solely to bring actions under one specific law, regardless of the volume of alleged violations, is inefficient – especially within the larger scheme of antitrust enforcement.

Additionally, the proposed change creates extensive privacy and due process implications. USDA should not be in the business of enforcement through judicial proceedings, and farmers might be reluctant to share information with an organization that ultimately has enforcement authority against them in this manner. Further, in developing a new enforcement regime, USDA is going to be a need to construct sufficient institutional controls to protect the privacy and confidentiality of materials from leaks, misuse, and general abuse. This is not merely an abstract problem and other agencies with mature enforcement divisions, such as the Securities & Exchange Commission, still run into this significant due process concern.[13]

Outside of the difference between the current enforcement structure and a new one administered directly by a political appointee, the concern is the timing with making this change now. Pork producers understand and appreciate the administration's willingness to try and find solutions to combat high consumer prices. Initiatives, such as the recently announced funding for expanding meatpacking capacity, are great examples of the administration making concrete moves to decrease consumer prices and increase the value of hogs. However, as shown in the previous section, concentration is demonstrably not the cause of price inflation within the meat sector. The culprits of increased consumer prices across the economy are increased transportation costs, labor shortages, and the input cost increases driven by those factors. Additionally, within the meat sector, slowdowns from the New Swine Inspection System ruling in Spring 2021 reduced national processing capacity by an estimated 3.6%.[14]

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[11] https://www.whitehouse.gov/briefing-room/presidential-actions/2021/07/09/executive-order-on-promoting-competition-in-the-american-economy/
[12] https://www.justice.gov/opa/pr/justice-department-and-agriculture-department-issue-shared-principles-and-commitments-protect
[13] https://www.sec.gov/news/statement/commission-statement-relating-certain-administrative-adjudications
[14] https://nppc.org/wp-content/uploads/2021/05/Impacts-of-NSIS-Decision-on-Pork-Producers-Dr.-Hayes.pdf

Creating a new position to pursue action under a flawed urgency underscores the political nature of proposing this new role now. Discussions of how the Packers and Stockyards Act should be enforced have been deliberated since the Grain Inspection, Packers and Stockyards Administration (GIPSA) rules were proposed in 2011. Since then, proposed changes have all been made through the rulemaking process to act within the current structure, not to change it. The only thing that has changed since then has been placing responsibility on packers. Creating an appointee position for this purpose, at this moment, effectively codifies this flawed understanding. Again, pork producers are perhaps the most skeptical of the actions of packers, but the data simply does not support the premise under which these changes are proposed.

Concern Regarding Timing with the "GIPSA" Rules

The last issue that has clouded discussions over the special investigator bill is the overlapping timing with the upcoming rules on the definitions under the Packers and Stockyards Act (hereafter referred to as the new GIPSA rules). The new GIPSA rules, at least as they relate to pork producers, will likely state USDA's position on whether harm to competition must be established in order to bring a suit under the Packers and Stockyards Act and the definitions of key terms under sections 202(a) and 202(b) of the Act. While the specific rules have not yet been published and thus it is premature for NPPC to comment on them, both rules clearly have the potential to dramatically reshape USDA's position on the proper interpretation of the Packers and Stockyards Act. Moreover, any regulations asserting USDA's position on the competitive harm requirement will likely face significant legal challenges stemming from U.S. District Courts' unanimous precedent on this matter.

Aside from the debated merits of changing the enforcement structure to be centered under this new office, the timing would undoubtedly be incredibly challenging for the special investigator. USDA will be undergoing paradigm-shifting rulemaking that will alter USDA's legal position in nearly every action that the new office would be responsible for at the same time that the office would be establishing its role. AMS writes these rules and has the Packers and Stockyards Division under its control. Keeping all activity on the Act under one agency as these rules are being developed is critical. For both the regulators and the regulated parties, the timing of multiple changes to the structure of Packers and Stockyards Act enforcement without any clear precedent would be extremely challenging. At minimum, lawmakers should delay consideration of this measure until after the new GIPSA rulemaking process is complete.

Conclusion

Pork producers rely on enforcement of the Packers and Stockyards Act to ensure that they operate on a level playing field with their counterparts in the middle of the supply chain. However, the proposal to create a new, politically appointed position at USDA that takes the authority to bring civil action from DOJ establishes a series of complications with the enforcement structure of the Act, all under a fundamentally flawed premise of urgency. While legitimate debate exists on the current funding levels of both the Packers and Stockyards Division at AMS and the DOJ Antitrust Division, there seems to be significant consensus that the current enforcement structure already divides responsibilities effectively and efficiently. Moreover, all of this is being proposed during an overhaul of the rules promulgated under the Packers and Stockyards Act – changes that will undoubtedly be complicated by a revised enforcement structure.

We urge that Senators considering this bill to find other opportunities to improve market conditions for pork producers, and we appreciate the committee's commitment to American agriculture. If you have any questions regarding our position, do not hesitate to contact Jack Detiveaux, NPPC Manager for Competition, Labor, and Tax, at detiveauxj@nppc.org.

Regards,

Terry Wolters
President
National Pork Producers Council

Appendix A

US Retail Pork Price Inflation
December 2021
Holly Cook, Dermot Hayes, and Barry Goodwin

U.S. Retail Pork Price Inflation

December 2021

Holly Cook, Dermot Hayes, and Barry Goodwin

Table of Contents

Executive Summary

Meat prices, including retail pork prices, have increased rapidly in 2021. This appreciation was particularly notable during the fall of this year. This report explores the forces that have contributed to this increase. Wholesale and farm level prices were high during the summer due to strong domestic and international demand, but they have since fallen to more normal levels. Pork production costs also increased during this period such that farm level profitability remained within a normal range. Packer margins are right at their five-year average. The increase in retail prices this fall at a time when wholesale and farm level prices were falling was likely driven by a lagged response to high wholesale prices during the summer, increased transportation costs, supply bottlenecks and delays, and increased labor costs in retail outlets and distribution centers.

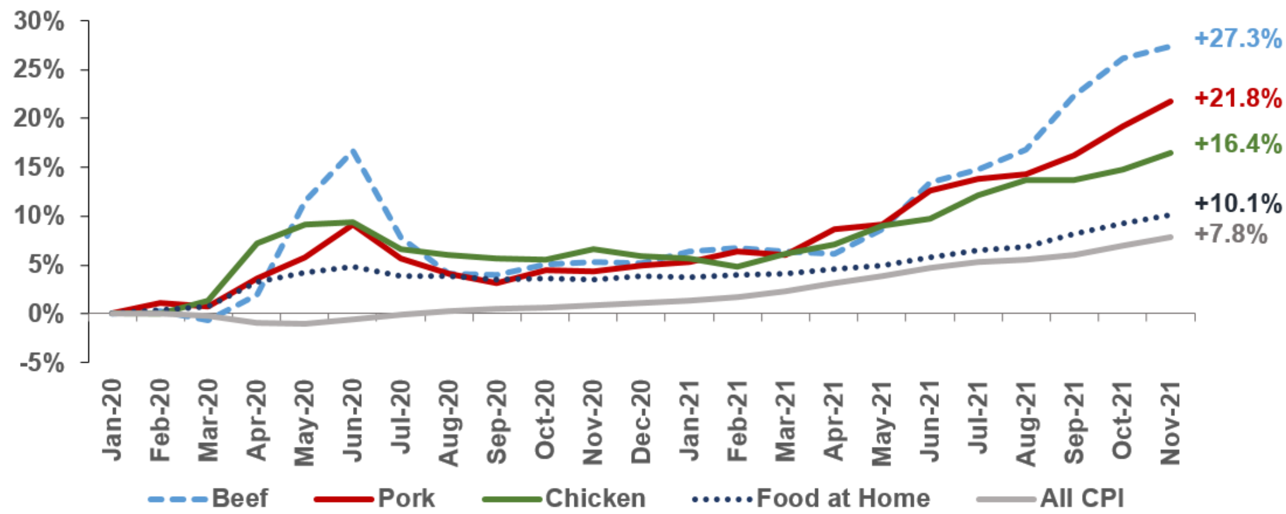
Introduction

The seasonally adjusted consumer price index (CPI) for all goods and services was 6.9 percent higher in November than the 12 months prior, representing the greatest year-over-year increase in 30 years. As prices for all goods continue to rise, recent news headlines have taken a particular interest in the factors impacting food and meat prices. The purpose of this report is to document the size and sources behind the recent increase in pork prices.

Pork Price Inflation

Figure 1 shows the retail price index for beef, pork, and chicken as a percent change since January 2020. Since that time, beef prices have increased 27.3 percent, pork prices have increased 21.8 percent, and the price of chicken is 16.4 percent higher. A sharp increase in prices is observed from March to June of 2020 as many large packing plants shut down or slowed production due to COVID-19 outbreaks. At this time, the price of hogs and cattle saw dramatic movement in the opposite direction. Pork and beef prices then stabilized as the industry regained processing capacity, falling by 4.7 and 10.8 percent respectively from June to August 2020. Prices for all three meat commodities have begun rising more steeply in recent months and have outpaced the rising food-at-home price index (+10.1 percent) and the CPI for all goods (+7.8 percent) over the same period.

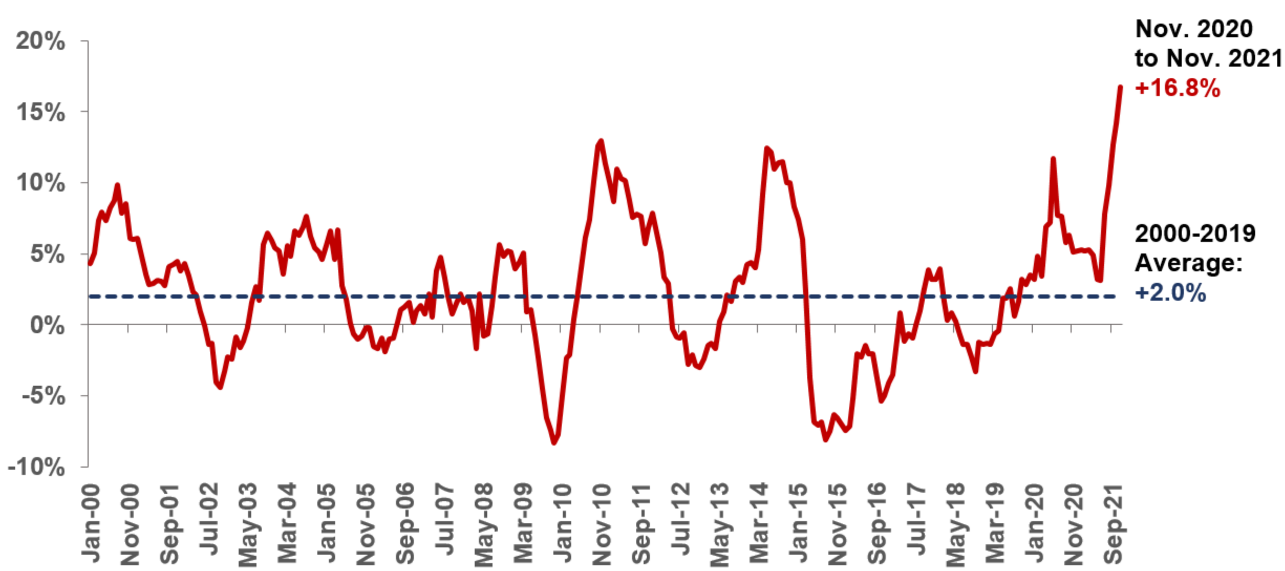
Figure 1: Price Changes since January 2020, Seasonally Adjusted



Source: Bureau of Labor Statistics

Looking specifically at pork, Figure 2 shows the year-over-year change in monthly pork prices. From November 2020 to November 2021, pork prices increased 16.8 percent. Prior to the pandemic, consumers had not seen such a sharp annual increase in prices since 2014 when disease-related death losses from PEDV significantly reduced the supply of hogs, resulting in higher hog and eventually higher pork prices. Given the low food inflation rates in recent memory, it is no wonder that current meat prices have been causing sticker shock across the country.

Figure 2: Price of Pork, Year Over Year Percent Change, Seasonally Adjusted



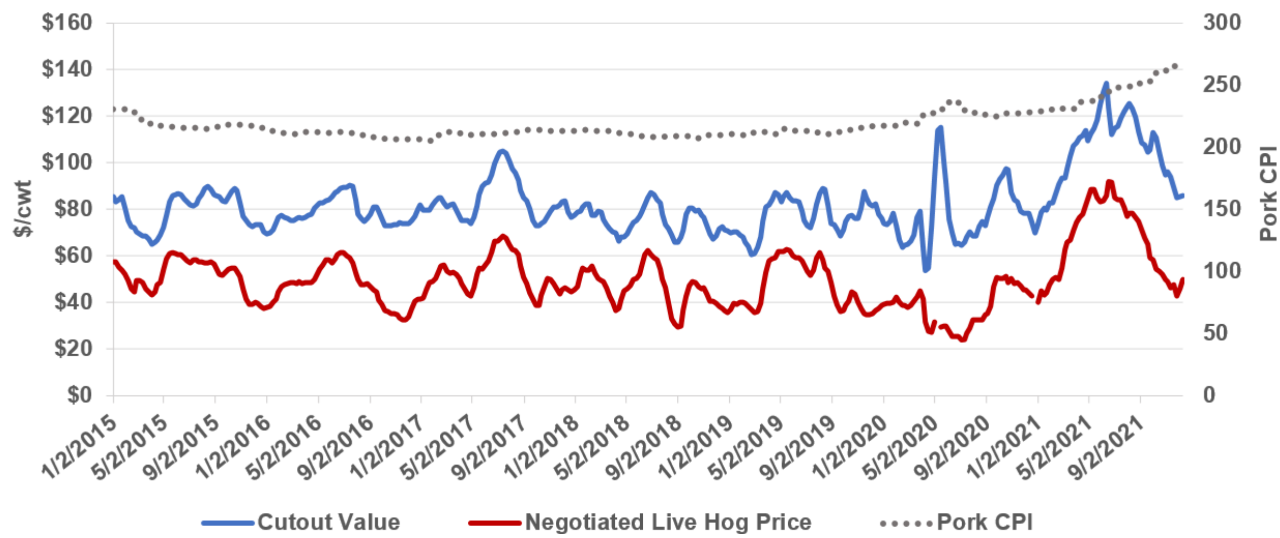
Source: Bureau of Labor Statistics

Factors Driving the Increase in Retail Pork Prices

Retail pork prices are determined by the supply of hogs and demand for pork. The farm-level supply of hogs, though relatively fixed in the short run, is determined by the cost of production and expected returns. While pork producers are not able to directly raise prices and pass their costs along to retail consumers, higher input costs and negative returns will impact the supply of hogs over longer periods of time which can lead to higher prices. In the long run, producers who are not profitable will exit the industry or reduce their breeding herds.

Figure 3 below shows the cutout values (the value of the meat sold by packers) and farm level live hog prices as well as the pork CPI. As supply chain disruptions moderated in early 2021, strong domestic and export demand supported the strengthening of pork and hog commodity prices. Live hog prices and cutout values have fallen from summer highs, but retail prices continue to climb.

Figure 3: Weekly Cutout Values, Weekly Negotiated Hog Prices, and Monthly Pork CPI

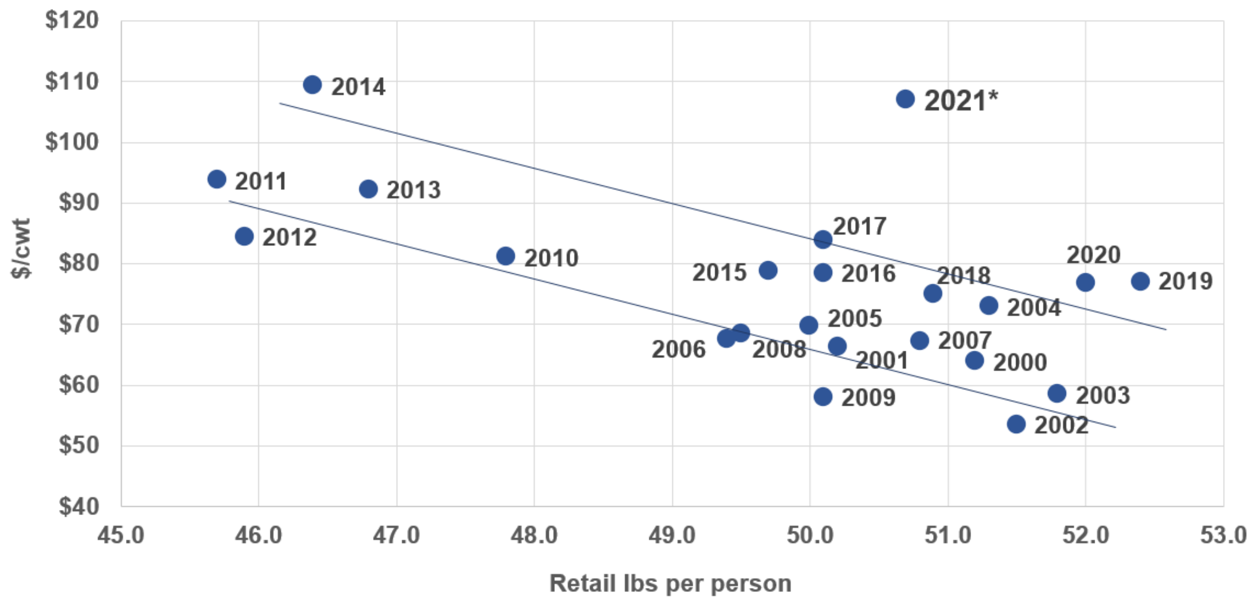


Source: AMS, LMIC, BLS

Demand for Pork

Strong pork demand is best depicted by Figure 4, which shows negotiated cutout values relative to per capita pork availability. In most years, when the quantity of pork supplied to the market increases or decreases, the price adjusts and there is movement up and down the demand curve. In 2014, the pork demand curve shifted as consumers showed they were willing to pay higher prices for pork after PEDV. In 2021, consumers again showed that they were willing to purchase greater quantities of pork at alternative prices and income levels. Not shown in Figure 4 is the fact that U.S. pork exports also reached record levels of volume and value in 2020 and 2021.

Figure 4: Per Capita Pork Consumption vs. Negotiated Carcass Cutout Values

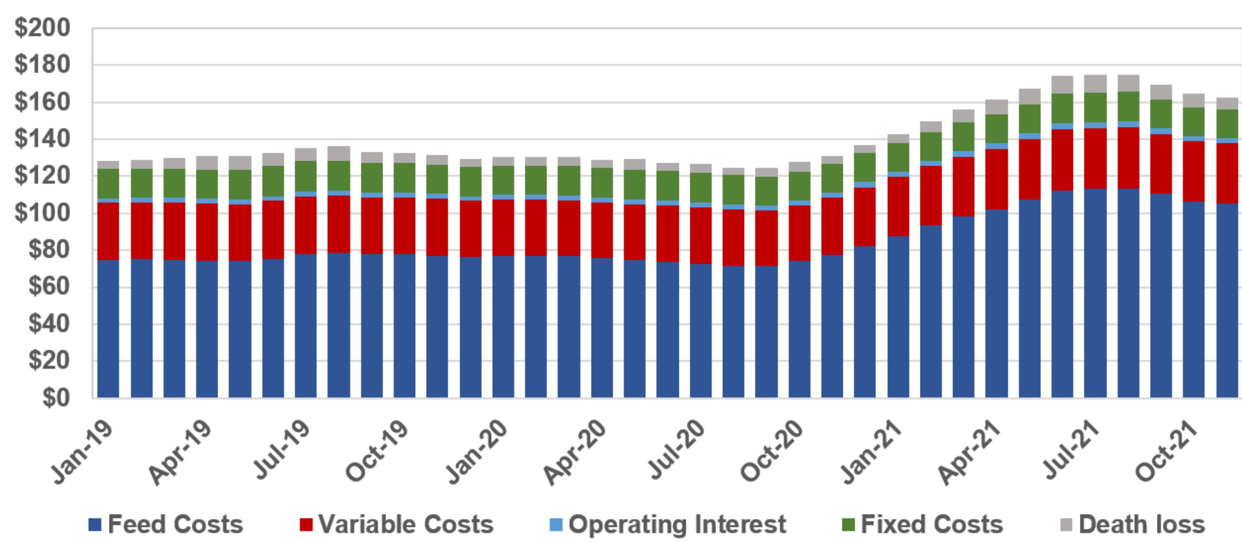


Source: AMS, LMC, Dr. Steve Meyer

Cost of Production

Figure 5 shows farm level production costs for hogs. From January 2020 to November 2021, the estimated cost of farrow-to-finish hog production increased 24.6 percent, led primarily by an increase in feed prices. Over the past 12 months, total costs have increased 23.9 percent and feed costs have risen by 35.5 percent.

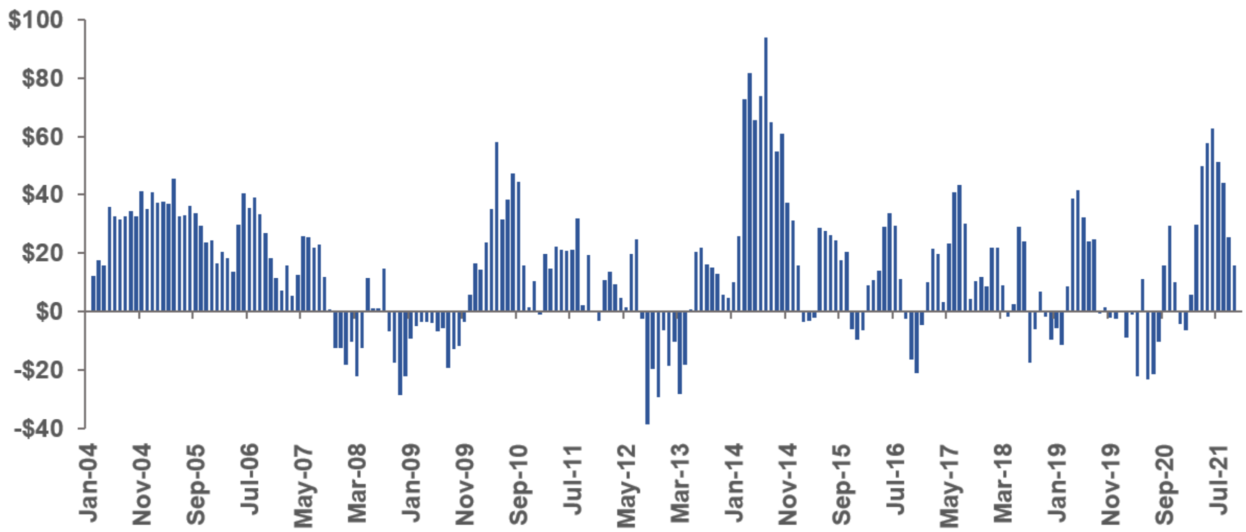
Figure 5: Total Farrow-to-Finish Production Costs, Measured in Dollars per Head



Source: ISU Extension Estimated Livestock Returns

Figure 6 shows the returns to pork production. After a disastrous year in 2020, pork production was profitable in the summer of 2021 and continued to be mildly profitable through the fall of 2021 even as live hog prices fell. The most recent estimates for November 2021 show estimated returns settling around the breakeven level.

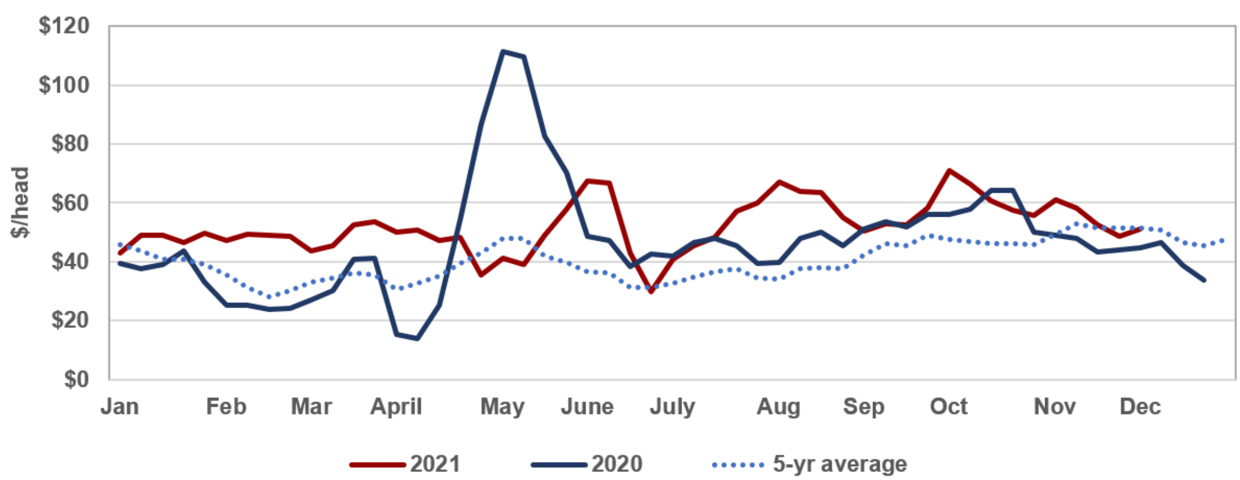
Figure 6: Pork Producer Returns, Measured in Dollars per Head



Source: ISU Extension Estimated Livestock Returns

If pork producers are not benefiting from the surge in retail prices, who is? Figure 7 shows the gross margins that packers are earning and compares current margins to the five-year average. As was true for pork producers, pork packers are making near normal margins.

Figure 7: Estimated Packer Gross Margins



Source: LMIC, AMS

Labor Shortage

Perhaps the greatest current challenge to all food supply chains is a lack of available labor. Despite rising wages, all industries are currently struggling to fill open positions. As of October 2021, there were more than 11 million job openings in the U.S. While recently released employment measures show signs of improvement, the civilian labor force is still about 2.4 million people less than it was in January 2020, indicating a smaller pool of potential workers now than before the start of the pandemic.

A lack of available workers throughout the pork industry has been long-standing issue that was made worse by the pandemic and is one of the reasons packing plants have had capacity issues. Anecdotally, producers report worker shortages ranging from 10 to 20 percent for sectors with well-established visa pipelines for skilled-workers and up to 30 percent for those, including packing plants, that require less-skilled labor. Though larger plants have been able to implement more advanced levels of automation over the years, packers still report that labor shortages restrict their ability to add value through downstream tasks, such as boning or offal recovery, which in turn lowers packer margins and, ultimately, the value of hogs.[1]

The tight and competitive labor market is impacting every aspect of the pork supply chain, including the transportation of hogs and pork. The American Trucking Association reports that the trucking industry is currently short about 80,000 drivers which could worsen to 160,000 by 2030.[2] Employers in the food service and retail industries have also struggled to rebuild their workforce back to pre-pandemic levels.

Many industries hit hardest by labor shortages have significantly increased wages to attract more workers. Through October, average weekly wages for truck drivers were up 4.3 percent year-over-year and up 10.0 percent since January 2020. Average weekly earnings for production and non-supervisory workers in the animal slaughter and processing industry were up 10.1 percent this year and up 19 percent since January 2020. As of October, average weekly earnings were up 17.2 percent for full-service restaurant workers, 18.3 percent for quick service restaurant workers, and up 9.1 percent for grocery store workers since January 2020.[3] In some sectors, wage growth has outpaced the current inflation rates, but labor market recovery remains slow.

Slower Line Speeds and Reduced Packing Capacity

One key issue specific to the pork industry is the slowing of pork production lines at six major packing plants. On July 1, 2021, a federal court order went into effect, eliminating a provision of

[1] https://www.nationalhogfarmer.com/marketing/us-slaughter-capacity-settles-even-keel

[2] https://www.trucking.org/sites/default/files/2021-10/ATA%20Driver%20Shortage%20Report%202021%20Executive%20Summary.FINAL_.pdf

[3] https://beta.bls.gov/dataQuery/find?st=0&r=100&fq=survey:%5bce%5d&fq=mg:%5bMeasure+Category%5d&fq=mc:%5bPay+and+Benefits%5d&fq=mcd:%5bEarnings%5d&fq=cg:%5bOccupation%5d&more=0&q=animal

USDA's New Swine Inspection System (NSIS) that had allowed pork packing plants to run faster processing line speeds.[4]

Although implemented in 2019, the NSIS was more than 20 years in the making, with five pork plants operating faster line speeds through the HACCP-Based Inspection Models Project (HIMP) – a pilot program started in 1997 during the Clinton administration. A sixth plant joined the original five in operating faster lines on implementation of the NSIS. At all six plants, the faster line speeds led to an increase in capacity. According to Iowa State University economist Dr. Dermot Hayes, slowing line speeds to the pre-1997 level reduced the capacity at these six plants by up to 25 percent, equating to a nationwide capacity loss of 3 percent, or 2.5 percent after impacted facilities adjusted operating hours.[5]

This loss of capacity not only reduced the volume of pork that could be produced, but it also led to lower hog prices and increased transportation costs for producers near the impacted plants. Additionally, reduced line speeds exacerbated an already tenuous labor situation. Many plants, and especially those that relied on overtime and Saturday shifts to help make up for slower line speeds, saw an increase in resignations and absenteeism for Monday and Friday shifts.

USDA recently announced a time-limited trial program that would allow NSIS plants to operate at higher line speeds as worker safety data is collected. Allowing plants to increase line speeds under this program will help add pork packing capacity after months of slower line speeds.

Transportation Challenges

In addition to widespread labor shortages and reduced packing capacity, the pork industry is also dealing with transportation bottlenecks and higher prices for fuel, energy, and packaging materials. Figure 8 below shows the producer price index (PPI) for truck transportation, which was 16.1 percent higher year-over-year through October. High diesel fuel costs and a shortage of truck drivers have also made it more costly to transport not only animals, but pork products from top-pork-producing regions to stores and restaurants across the country. Data from the Energy Information Administration shows highway diesel prices up more than 50 percent over the last 12 months.[6]

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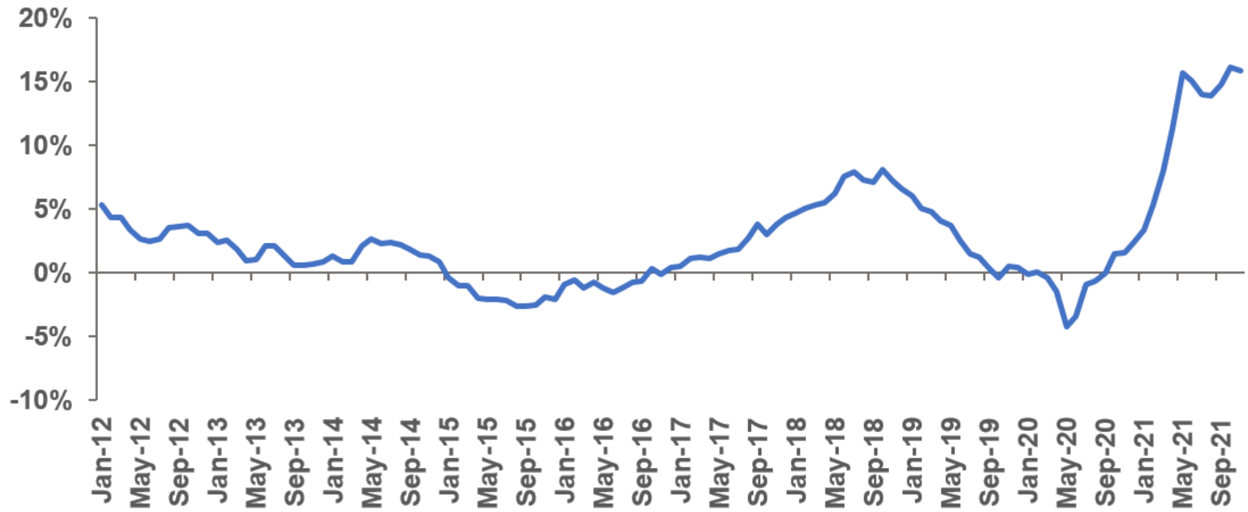
[4] https://www.porkbusiness.com/news/ag-policy/pork-industry-seeks-waivers-plants-impacted-line-speed-ruling

[5] https://nppc.org/wp-content/uploads/2021/05/Impacts-of-NSIS-Decision-on-Pork-Producers-Dr.-Hayes.pdf

[6] https://www.eia.gov/petroleum/gasdiesel/

Figure 8: Producer Price Index for Truck Transportation

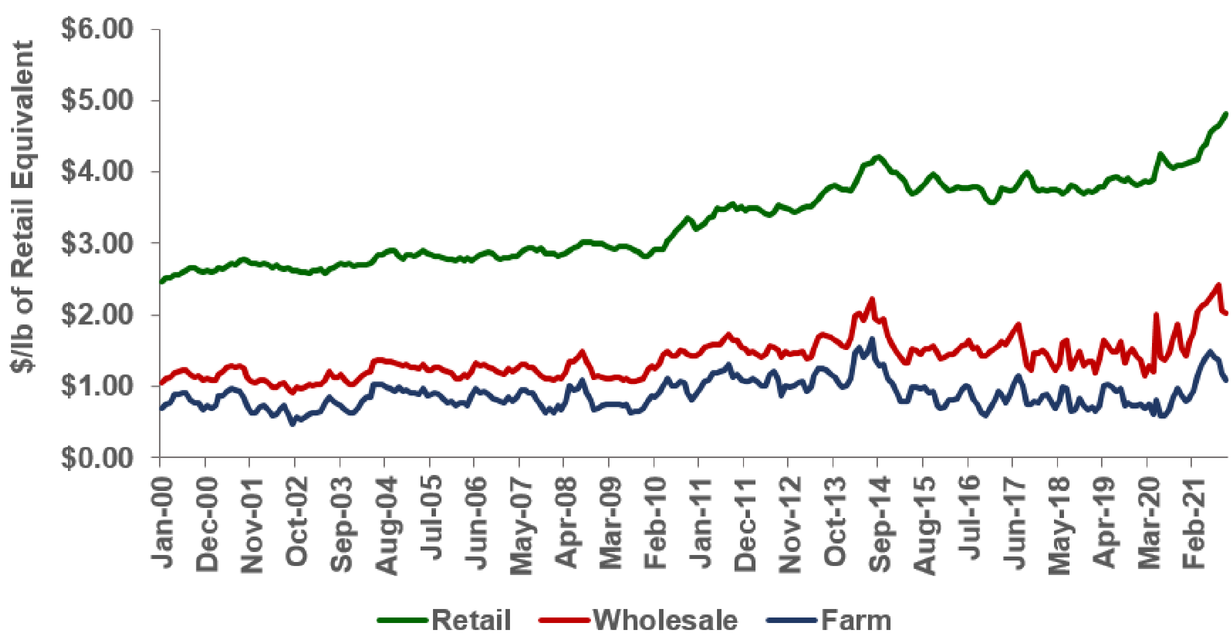


Source: BLS, FRED

Retail, Wholesale, and Farm Values and Price Spreads

Figure 9 shows monthly retail, wholesale, and net farm prices from 2000 to 2021 using the ERS measure of retail price, which includes only composite meat products and excludes boneless or value-added products. As mentioned earlier, farm and wholesale prices were strong in the summer of this year and have since fallen. Retail prices continue to increase rapidly.

Figure 9: Monthly Retail, Wholesale, and Net Farm Prices



Source: ERS, CARD

Price spreads represent the difference in prices at various stages of the supply-chain. USDA ERS produces monthly reports on the per pound value of pork at the farm, wholesale, and retail level, as well as the farm-to-wholesale and wholesale-to-retail price spreads.

The farm-to-wholesale spread is the difference between the wholesale price (received by packers) and the net farm price (gross farm price received by producers minus the value of byproducts). This spread contains the processing and operating costs of the packer as well as the packer's profit margins. The wholesale-to-retail price spread is the difference between the wholesale price (received by packers) and the retail price (paid by consumers). This spread includes the retailer's costs and profit margins.

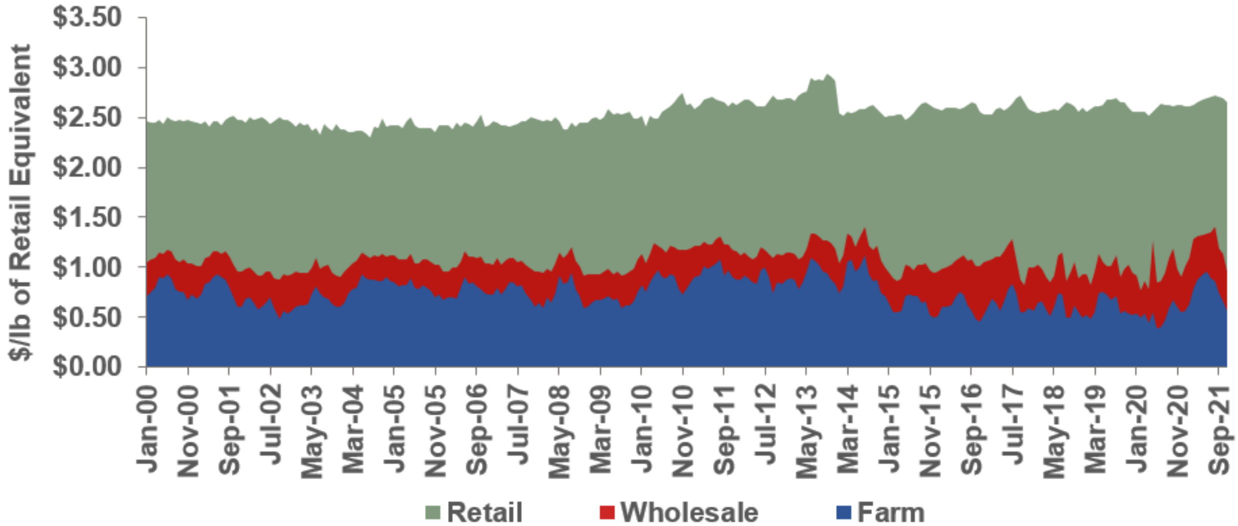
Questions about increasing spreads arise because it is impossible to infer from the ERS statistics whether price spreads are widening to cover higher costs or to extract greater profits. For the clearest picture of price spread movements, it is helpful to adjust all values for inflation.[7] If adjusted price spreads remain constant over time, then any additional margin can be attributed to general inflation. If spreads widen over time, then either more profits are being extracted or prices are rising to offset higher costs.

Figure 10 shows inflation adjusted prices and spreads for pork from 2000 to 2021. From 2000 to 2013, pork price spreads were relatively constant. The farm-to-wholesale price spread became thinner for parts of 2013 and 2014 when PEDV losses supported higher hog prices, but this widened out as production recovered in 2015 and 2016 and at times challenged packing capacity. Although temporary, the widest farm-to-wholesale margins can be observed in early 2020 when COVID-19 shutdowns limited processing capacity, causing a backup of hogs on farms at a time when retail meat demand was ramping up.

Consistent with the price data in Figure 9, the retail price spread has recently widened. This price spread has to compensate for transporting pork to retail outlets, labor in retail stores and distribution centers, and any costs associated with delays and bottlenecks. It appears likely that retailers are passing extra costs of these inputs on to consumers. Retailers are typically slow to adjust prices to reflect changes in their input costs. It is also possible that some of the recent increases in retail prices are a one-time response to high wholesale prices this summer.

[7] https://www.card.iastate.edu/ag_policy_review/article/?a=48

Figure 10: Retail, Wholesale, and Farm Prices and Spreads for Pork in 2000 Constant Dollars



Source: ERS, CARD

Food Inflation Outlook

While it is clear that there are many factors contributing to food price inflation, it is still difficult to predict how long these challenges will persist. There is also much debate about whether current inflation and price trends are structural, meaning they are caused by permanent changes, or cyclical, meaning higher prices are being caused by short-term problems that will be resolved once supply-chain bottlenecks subside and businesses resume “normal” production levels.

The answer likely lies somewhere in the middle. Food and commodity prices are historically cyclical and have experienced periods of high inflation in the past, though consumers have not been faced with this in quite some time. Though there are significant production, processing, and distribution challenges, there are likely no permanent, structural barriers in the way of getting back to cheaper food. It is unclear whether the same can be said about energy prices, wage inflation, and other current challenges.

Labor is one of, if not the most, critical factor in easing supply-chain challenges and high prices. Despite higher wage offerings and bonuses, the civilian labor force is still down 2.4 million workers since the start of the pandemic. Some labor challenges will be partially solved as disaster assistance and personal savings run out and rising wage levels draw workers back into the labor force. However, with slowing domestic population and labor force growth, the long-term outlook on labor is highly dependent on future immigration policy and ag labor reform. If not addressed, labor will continue to be a limiting factor in food and pork production for the foreseeable future even as other sectors see improvement.

Appendix B

Concentration in the US Pork Industry
January 2022
Holly Cook, Dermot Hayes, and Barry Goodwin

Concentration in the U.S. Pork Industry

January 2022

Holly Cook, Dermot Hayes, and Barry Goodwin

Contents

Executive Summary

The pork packing industry is more concentrated now than it was 50 years ago. However, due to new packing plants entering the market from 2017 to 2020, concentration levels are lower now than they were just five years ago. Additionally, concentration levels in the meatpacking industry are far from the highest among U.S. industries, and concentration has not significantly increased over the past 15 years. Retail pork prices have increased rapidly due to strong demand for U.S. pork as well as added costs and labor shortages at every level of the supply chain. Historically, changes in retail prices are not correlated with changes in concentration level. Despite rapid increases in 2021, pork prices in the U.S. are still comparable to or lower than prices in other countries.

Introduction

As meat prices have increased over the last several months, there has been increasing discussion about the structure of the U.S. meatpacking industry and the relationship between consolidation, industry profits, supply-chain disruptions, and high retail prices. The purpose of this analysis is to examine how trends in consolidation and profit margins within the pork packing industry relate to consumer retail prices as well as how concentration levels in the pork industry compare to other sectors.

Concentration in the Pork Packing Industry

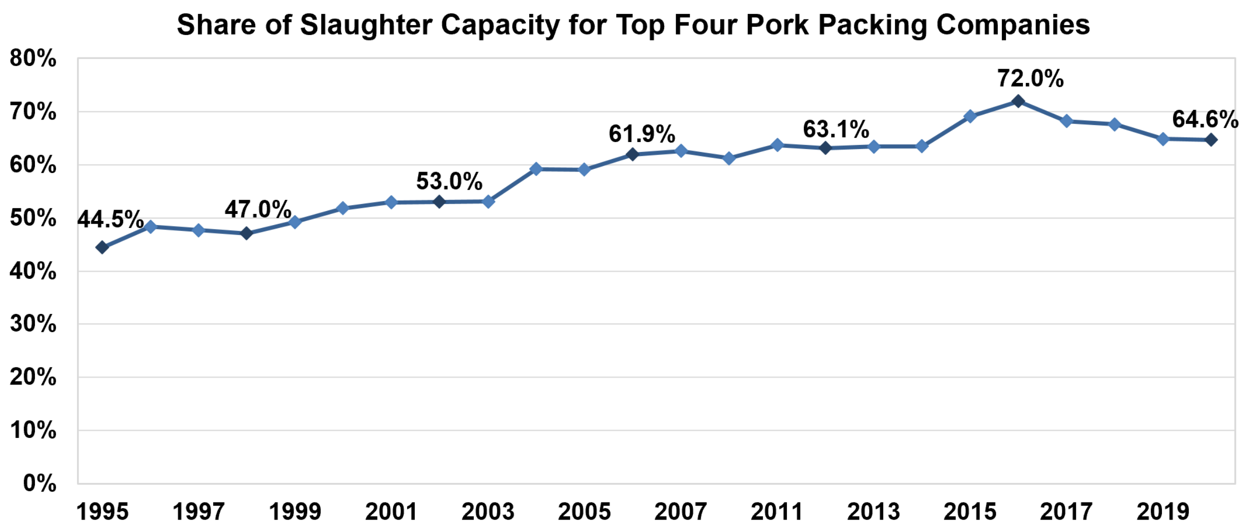
Like most U.S. industries, the structure of the pork packing sector has evolved over several decades resulting in fewer, larger plants. This change was primarily driven by technological advancements and the cost savings associated with economies of scale. Packers buy hogs and sell meat products at market prices and earn profits on their margins, or the difference in these prices after accounting for acquisition, production, and operating costs. Because individual meatpackers do not control market prices or the supply and demand of hogs and pork, profits depend greatly on the ability to minimize costs.[1] Over time, companies have achieved lower costs per unit by operating larger and more efficient plants, and this has led to consolidation within the industry.

There are several ways to examine concentration in the pork processing industry over time. The chart below shows the four-firm concentration ratio of hog slaughter capacity from 1995 to 2020. The four-firm concentration ratio, or CR-4, is a commonly used measure of concentration that is calculated by adding the market share of an industry's four largest firms.

From 1995 to 2016, the CR-4 of the U.S. pork packing industry increased from 44.5 percent to 72.0 percent due to company mergers and growth. Over the past five years, however, new packing plants have opened, and the CR-4 has fallen back down to 64.6 percent, which is

[1] https://www.justice.gov/sites/default/files/atr/legacy/2011/09/09/AGW-15639-a.pdf

comparable to the industry's concentration ratio in the early-to-mid-2000s. This chart uses physical slaughter capacity to calculate market share which is not necessarily the same as the market share of total revenue, though these measures should be comparable because packers tend to run plants at capacity.



Source: Dr. Steve Meyer Packing Capacity Tables (1995-2020)

Another measure of industry concentration is the Herfindahl-Hirschman Index (HHI). This measure is used by the Department of Justice (DOJ) when evaluating the impact of proposed mergers on industry competition and market power and is calculated by finding the sum of squared market shares for all companies within an industry. DOJ considers an HHI less than 1,500 to be "unconcentrated" while values between 1,500 and 2,500 are "moderately concentrated" and an HHI above 2,500 is "highly concentrated."[2]

In 2016, the same year the CR-4 reached its highest value on record, the HHI for pork packing was 1,538 based on slaughter capacity estimates. The opening of new packing plants in 2017, 2019, and 2020 allowed the HHI to fall to its current estimated level of 1,345 which, by DOJ classifications, is considered to be "unconcentrated".[3]

Concentration in Other Sectors

The pork packing industry is not the only industry that has changed in structure over time. The U.S. Census Bureau's Economic Census, last updated in 2017, provides data on the market share of firms in NAICS coded industries. Unfortunately, these data are five years old and do not allow all industries of interest to be disaggregated from similar sectors. For example, the animal slaughter industry excludes poultry but does not differentiate between pork and beef

[2] https://www.justice.gov/atr/file/810276/download
[3] https://nppc.org/wp-content/uploads/2021/06/Competition_Paper_FINALWD.pdf

slaughter. Nevertheless, this is the best available data source to make comparisons across many industries.

From 2002 to 2017, the CR-4 for the animal slaughter industry (NAICS 311611) increased from 58.7 percent in 2002 to 63.4 percent in 2017, a 4.7 percent overall increase. Recall from the previous section that the CR-4 for pork packing fell by more than 7 percent from 2016 to 2020. When compared to other industries, both the CR-4 of meatpacking and the increase in concentration over the 15-year period are not among the highest of U.S. industries. In fact, more than 100 industries had a CR-4 greater than 63.4 in 2017. [4]

Industries with some of the highest levels of concentration include secondary market financing (100%), home centers (96%), warehouse clubs and supercenters (94%), couriers and express delivery services (91%), tobacco manufacturing (91%), newsprint mills (90%), computer storage device manufacturing (90%), aircraft manufacturing (90%), and passenger car rentals (90%).[5]

Within the food industry, breweries (68.6%), specialty canners (70.4%), as well as manufacturers of dog and cat food (67.7%), malt (68.0%), breakfast cereals (81.8%), creamery butter (79.0%), beet sugar (79.5%), other snack food (74.9%), bottled water (72.5%), and ice (60.7%) all have concentration ratios greater than the animal slaughter industry (63.4%).

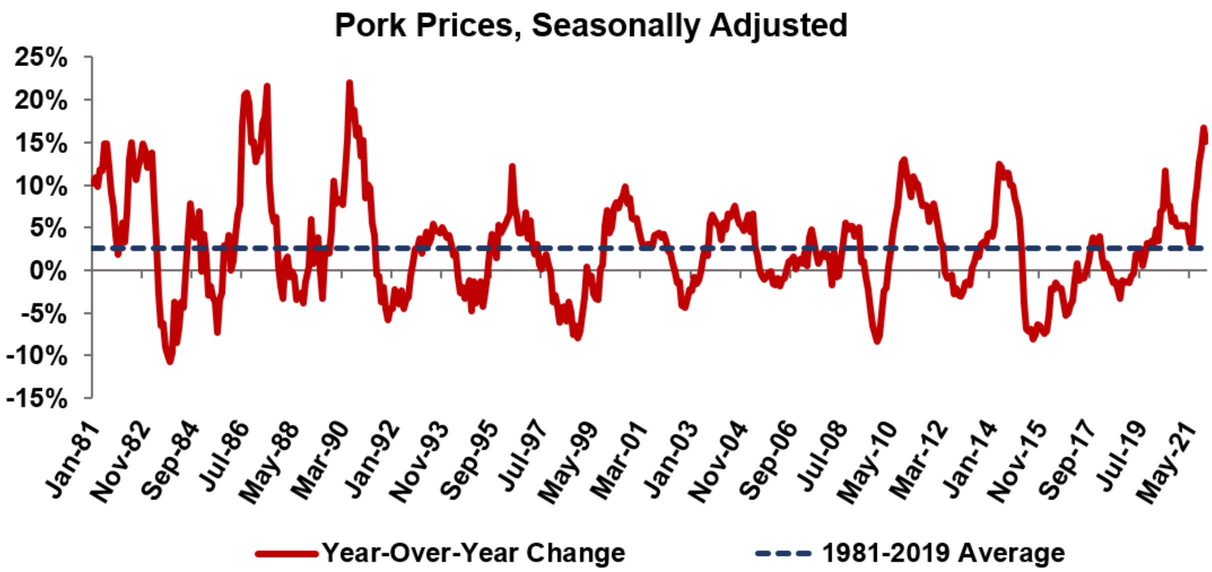
In terms of increased concentration over the 15-year period, top changes occurred in newsprint mills (+36.5%), radio networks (+29.2%), ammunition manufacturing (+29.9%), luggage and leather goods stores (+31.7%), taxi services (+59.6%), passenger air transportation (+37.5%), travel agencies (+27%), and other gas stations (+27.9%). Among other food manufacturers, changes in concentration ranged from a decline of 23.1 percent to an increase of 21.5 percent.[6]

Retail Pork Prices

Retail meat prices in the U.S. increased rapidly in 2021, drawing the attention of consumers and policymakers alike. As of December 2021, pork prices were up 15.1 percent year-over-year while beef and chicken prices were up 18.6 and 10.4 percent respectively based on the Bureau of Labor Statistics Consumer Price Index (CPI). The elevated price levels observed in recent months are a drastic change from the prices consumers grew accustomed to over the five years preceding the pandemic. However, despite the moderate prices observed in the recent past, pork prices have a history of sharp increases and significant volatility.

[4] Industries are classified by 6-digit NAICS codes.
[5] https://itif.org/publications/2021/06/07/no-monopoly-has-not-grown
[6] https://www.census.gov/programs-surveys/economic-census.html

The chart below shows year-over-year pork price changes from 1981 to 2021. The greatest price increases occurred in 1986, 1987, and 1990 with annual price increases exceeding 20 percent at times during each of these years. The four-firm concentration ratio of pork packing was at or below 40 percent from 1986 to 1990, compared to roughly 64 percent today.[7] Furthermore, retail prices today are much higher now than they were in December of 2016, despite a reduction in the concentration level of more than seven percent over this period. If concentration was a primary driver of increased pork prices, the chart below would likely reflect a clearer, positive trend over time that was more closely related to trends in industry consolidation.



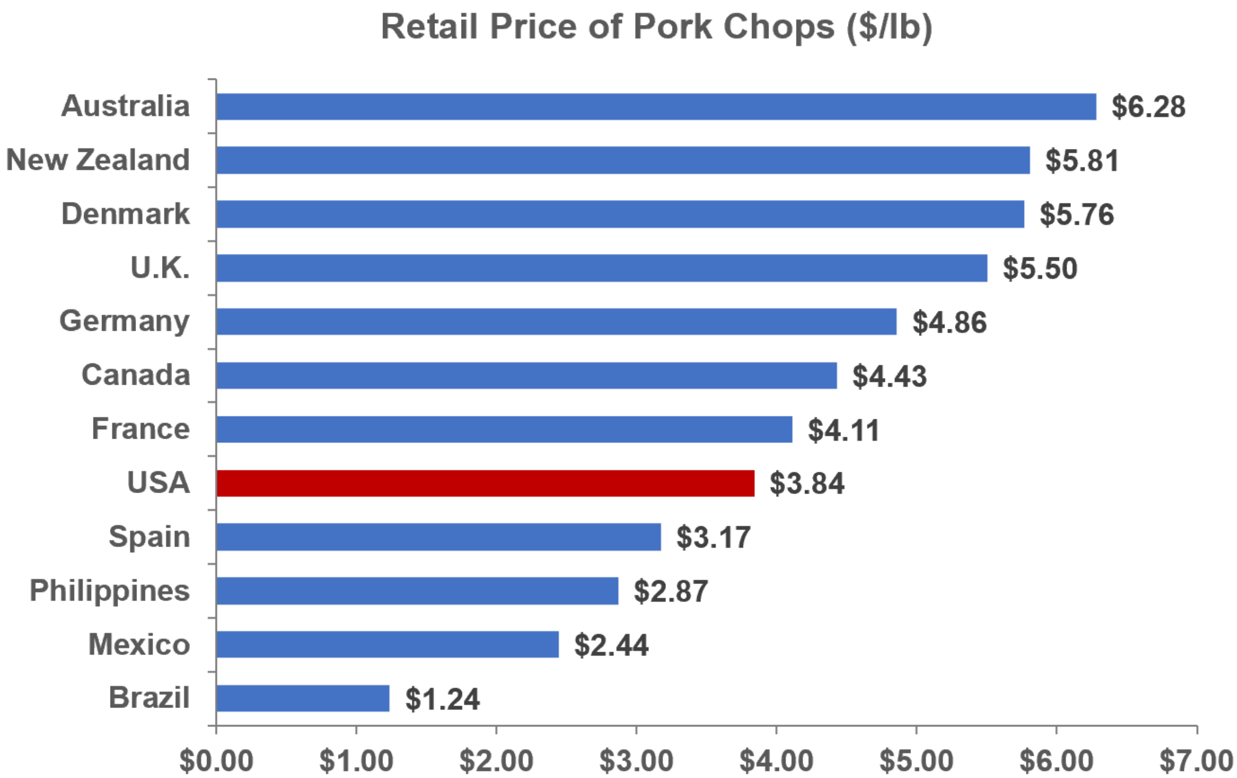
Source: Bureau of Labor Statistics, Consumer Price Index

Cross Country Comparison of Pork Prices

The U.S. is not the only country to see higher pork prices in recent months. The FAO Food Price Index (FFPI) measures monthly changes in the international price of five commodity groups, including meat.[8] The meat price index is based on average export values for bovine, pig, poultry, and ovine meat from 10 representative markets with meat types weighted by their share of global trade. From December 2020 to December 2021, the FAO meat price index increased by 17.4 percent. In July 2021, the meat price index reached its highest level of year-over-year increase since 2008 at 23.7 percent. The FAO overall food price index was at 98.1 in 2020 and by the end of 2021, it stood at 133.7. The rate of increase in international dairy, cereals and oilseed prices was far higher than for meats.

[7] https://www.ers.usda.gov/webdocs/publications/41108/18011_aer785_1_.pdf?v=0
[8] https://www.fao.org/worldfoodsituation/foodpricesindex/en/

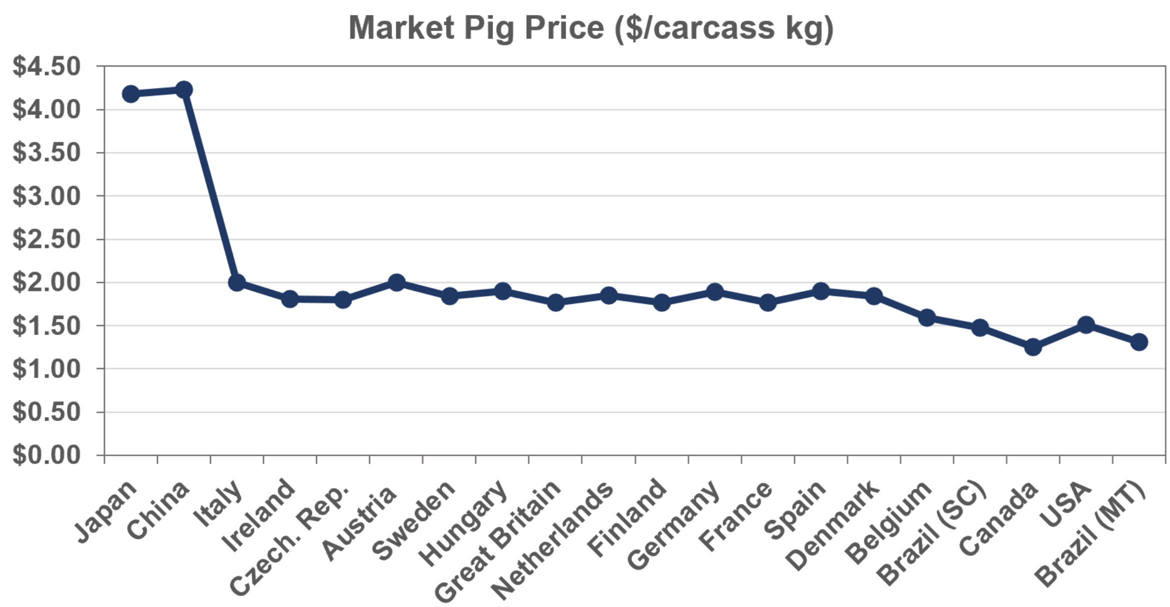
In terms of consumer prices, the chart below shows a cross-country comparison of the price of pork chops, converted to dollars per pound. Price estimates are the average of a small sampling of major grocery retailers within each country for comparable products. Note that these prices were only collected for stores with online prices available and may not represent prices in every region. The average retail price of pork in the U.S. ranks similarly to many European nations and is much lower than the price in Australia and New Zealand.



Source: Online grocery retailers in selected countries
*Note that product specifications vary, and some products may be enhanced, injected, or "pumped"

The figure shown below compares pork carcass values across several countries.[9] As was true with retail pork prices, the value of pork carcasses in the US is among the smallest in this group.

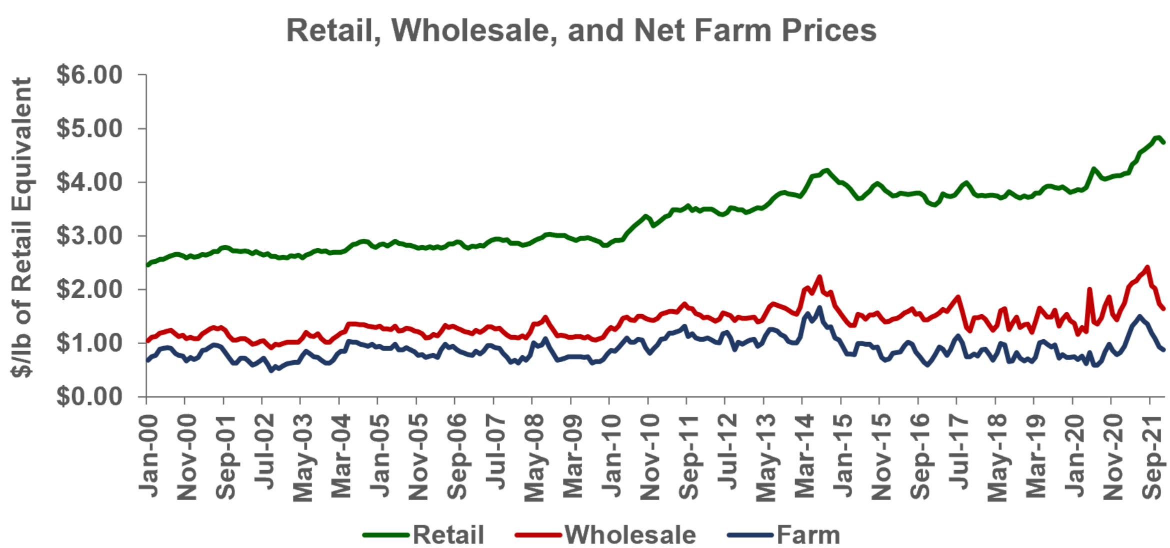
[9] Key Performance Indicators in Pork Production: An International Comparison Using 2019 Data
Derald J. Holtkamp, Dermot J. Hayes, and Lee L. Schulz Based on data from InterPig and Merck Animal Health.



Source: InterPig and Merck Animal Health

Price Spreads and Gross Margins

Given the current high price of pork in the U.S., it is natural to wonder if additional profits are being captured in the middle of the supply chain. The chart below shows monthly retail, wholesale, and net farm prices from 2000 to 2021 using the ERS measure of retail price, which includes only composite meat products and excludes boneless or value-added products. In recent months, farm and wholesale prices have fallen sharply while retail prices remain elevated.

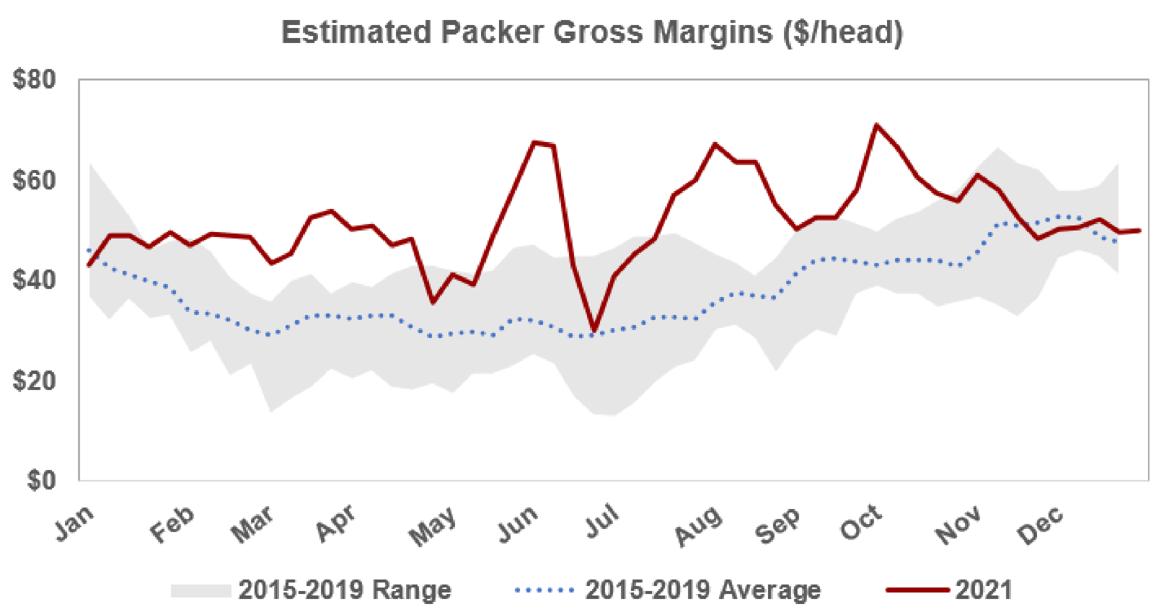


Source: USDA Economic Research Service

The farm-to-wholesale price spread, which includes the operating costs of the packer as well as the packer's profit margins, widens when wholesale price increases outpace farm prices. The wholesale-to-retail price spread, which includes the retailer's costs and profit margins, becomes narrower when wholesale prices rise faster than retail prices. If packers were exercising market power to capture greater profits, one would expect the farm-to-wholesale price spread to grow and the wholesale-to-retail price spread to shrink.

Instead, the opposite has occurred. The farm-to-wholesale price spread has been declining and is down 15 percent over the last six months despite average weekly wages, transportation costs, and packaging costs rising within the industry. The wholesale-to-retail price spread was up more than 35 percent over the same period due to added retailer costs and a potentially lagged response to high wholesale prices this summer.

Packer gross margins, another indicator of profitability, are calculated as the difference between the price paid for hogs and the wholesale pork price received plus the value of byproducts. The gross margin does not include the cost of labor, utilities, or any other administrative and variable costs nor does it identify net profits for meatpackers. The chart below shows that packer gross margins have approached their 5-year average in recent months and are within their normal, pre-pandemic range despite rising retail prices.



Source: USDA AMS, LMIC