

## GEORGE MORRIS CENTRE SPECIAL REPORT:

### **Mandatory Price Reporting - Another Example of Misplaced Government Effort in Agriculture?**

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The United States Department of Agriculture's Mandatory Price Reporting regulations were published in the US Federal Register late last winter. Given the fact that some, particularly western hog producers, are arguing for mandatory price reporting in Canada, it is worth looking at the proposed regulations.

The 40 page proposal will require reporting of market information by packers that slaughter an average of 125,000 cattle, 100,000 hogs or 75,000 lambs per year. Packers are required to report both live animal and product prices twice daily. More specifically, here are some of the data that US meat packers are required to report:

- prices per hundred weight
- type of purchase (negotiated, formula or forward contract)
- quantity purchased on live or dressed weight basis
- premiums or discounts
- terms of trade (financing, producer ability to specify date and time of delivery...)
- meat product prices
- type of sale
- branded product characteristics
- grade, cut, trim specifications

Under the proposed Mandatory Price Reporting system, failure to provide this information will result in heavy penalties. The section on enforcement establishes a civil penalty -- \$10,000 -- for each violation and provides for the Secretary's issuance of cease and desist orders.

The USDA's Agricultural Marketing Service (AMS) currently operates an extensive, successful and highly respected price and sales collection and market reporting operation. This voluntary system provides price and sales volume on hundreds of thousands of livestock each day. The following are some of the key prices and sales volumes that are currently reported on a voluntary basis:

- livestock prices
- individual beef and pork cut prices
- daily beef and pork load counts
- contracted and spot market volume
- premiums and discounts

In addition, AMS provides daily and weekly market commentary.

In fact, AMS deserves a great deal of praise for the excellent job that they do. The system of voluntary price reporting that is in place in the US now has served the industry well. Furthermore, there are many strong producer organizations in the US such as the Texas Cattle Feeders and Nebraska Cattlemen, in

which members voluntarily report prices. Quite frankly, the livestock and meat industry already reports far more information than any other industrial sector. In fact, most industries would consider it incredible to have to report the prices that they pay or receive.

With that said, the new mandatory reporting program will go beyond the current system. The new mandatory system will provide USDA with new information that has never been collected under the existing voluntary market news reporting program.

The new data combined with the old data is a veritable smorgasbord of market information. For market analysts, this is the equivalent of being a kid in a candy store. For those who are not data addicts, however, what difference is this going to make?

### **WHAT IS THE PROBLEM? WILL MANDATORY PRICE REPORTING HELP?**

This initiative springs from attempts by politicians to be seen to be “doing something” about low farm prices during 1998 and 1999. Of course politicians and government cannot do anything about the underlying supply and demand forces that are at the root of low prices. As a result they search instead for anything simple, but visible in order to be seen to be “doing something” to help.

The cold reality however is that price reporting, whether mandatory or voluntary, cannot ease low prices and the USDA at least, knows it. Even the stated purpose of the USDA initiative has now become a very humble, “to ensure that small farmers and ranchers have a full and fair opportunity to compete in an increasingly concentrated agricultural economy.”

USDA Ag Secretary Glickman said. "This new mandatory price reporting program will help producers by making the market more transparent, giving them better information about what's happening in the marketplace." As noted above, the livestock and meat industry is one industry that is not short of data and transparency is not an issue. As noted, the USDA already operates an excellent market reporting system. If a producer, isolated or not, is not informed now, she is certainly not going to be more informed because there is a thrice daily report on “trim specifications.”

Furthermore, what impact can this measure really have? Overall price levels are determined by broad forces of supply and demand. The world-wide supply of meat and consumer demand for that meat will determine the overall price level. Within that broad price level, producers and packers as well as packers and retailers then individually seek to discover a price at which they will trade livestock or meat. Needless to say, information is the most crucial component of the price discovery process. The most informed participant in the process often has the greatest advantage.

As we noted above, if the rancher or farmer is not informed now, even with the wealth of information available, providing him with even more data is not going to help. For the most part, even the smallest, most isolated producer knows the overall broad price level and if not, it is easily accessible (the USDA reports two or three times daily already). After that, regardless of the amount of price reporting, it is still incumbent on the individual producer to seek-out and find the buyer that will provide the highest return at any given time or over time.

This last concept needs to be expanded upon in reference to Canada. With the demise of the mandatory

hog marketing systems in the west, there are many who are calling for mandatory price reporting in Canada. They say that with the mandatory boards gone, there is a shortage of pricing information. In fact, even in Manitoba, where Manitoba Pork only reports prices to its clients, any producer can find out current prices. All any producer needs to do is to phone packers in his marketing region to determine offer prices as well as terms and conditions of sale. From that point the producer can conduct informed negotiations with his chosen customer. That process would occur with or without mandatory price reporting. Furthermore, other organizations such as the Western Hog Exchange or SPI provide price reports on their websites.

Another motivating force behind the regulations is the fact that as livestock markets get more concentrated, the markets from which prices are reported may become too “thin” to be meaningful. As such, the idea is to force large participants to report all transaction prices, not just open negotiated transactions. Of course in that case, the benefits of seeing such reported prices would be subject to misunderstanding. That is as a result of the likely attachment of many terms and conditions to private transactions or contracts. In other words, if we don’t know the terms and conditions, then the prices themselves are meaningless. In addition some are concerned that large players in concentrated markets may willfully report misleading prices. As such, they assert there is a need for mandatory price reporting. Even if there was a clear motivation to mislead, there are not enough auditors in the world to stop such a practice, especially in a mandatory system.

Further to that last point, mandatory reporting of all prices could in fact lead to lower *reported* prices. The only work we have ever seen that relates to the impact of this measure was a USDA Packers and Stockyards study of Texas Panhandle cattle pricing during the mid-1990's. The study found that prices that were lower than the average for the period in question were eight times less likely to be reported than prices that were higher than the average. It is no stretch to see that if lower prices are eventually reported in greater number, then the overall trading range could then fall to lower levels. The law of unintended consequences kicks-in again.

The biggest problem in the livestock industry relates to quality and product specifications. Many serious observers believe that the old way of pricing is inefficient and impedes progress in this regard. As such, another important question is whether or not this initiative is going to stymie the willingness or ability of producers and packers to work together on new or progressive price and supply chain relationships. As the industry moves to more sophisticated, vertical alignments, why should government encourage reporting of old-style sales and price transactions? In fact, won't price reporting just encourage a reliance on the old way of doing business? Furthermore, will producers and packers back away from these initiatives if they must be reported?

In “new-style” transactions, packers and producers negotiation transaction terms, conditions and specifications as partners working towards a goal (increased final product sales based on quality, for example). Transaction prices and values are based on negotiations and the contribution of each party toward the goals. The concept of mandatory price reporting in such an environment is totally foreign. The old way of producers and packers agreeing to a price for an average lot may be more amenable to mandatory price reporting, but it already occurs in the voluntary system.

As with most efforts like this, the benefits to farmers will be either slim or none, but the costs will be burdensome for taxpayers and other participants along the supply chain. To the extent that this will

eventually put a cost burden on the industry, it also means that the cost will be passed on to producers or consumers or both Congress provided USDA with \$4.7 million for FY2000 to launch the program. USDA has requested Congress fund \$5.9 million for FY2001.

The measure will also impose costs on industry as well. As usual, the costs will be most burdensome on smaller firms. The USDA says reporting compliance costs expressed on a per head basis will be eight times larger for the seven smallest beef packers than for the three largest. It will be 28 times larger for the 12 smallest pork packers than for the seven largest pork packers. Meat packing is a margin industry. If the sector incurs higher costs, they will be passed on to the producer in the form of lower prices or the consumer in the form of higher prices. Higher prices to the consumer means less consumption. Is that going to help the producer? If smaller packers cannot pass along the costs, they will exit the industry. Is fewer industry participants going to help transparency? So if the so-called solution imposes an inordinate cost on the smaller packers, this will inevitably lead to fewer small packers, thereby making the solution part of the problem.

Furthermore, as with nearly all government forays into agricultural markets, this initiative will take hold after the need, real or imagined, has passed. That is, the livestock cycles are now in the upswing and producers are once again enjoying profitable returns.

Finally, and most importantly, we have to question why the government would consider it necessary to infringe on the rights of individuals and companies. In the case of price reporting, unlike health and safety, there is no identifiable public risk or threat. With the proposal in its current form, five years from now, there will be much more data and information, but absolutely nothing else will have changed.

## **ALTERNATIVES**

Hopefully, this initiative will be quashed before it moves forward in its current form. If, however, Secretary Glickman feels compelled to spend \$5 million dollars per year, there are more productive uses that could actually move the industry forward instead of backward.

A key livestock pricing issue is the fact that many formula and vertical pricing arrangements rely too heavily on thinning spot markets. Perhaps the focus of the spending should be on research into new and improved pricing formats. USDA could fund research into consumer based pricing, whereby prices to livestock producers are based on consumer driven attributes. USDA could provide analysis and reports on progressive supply chain linkages. In that way, even isolated producers could be informed as to the direction the industry is moving. More importantly, the isolated producer could then decide how to adjust his production and marketing systems.

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