



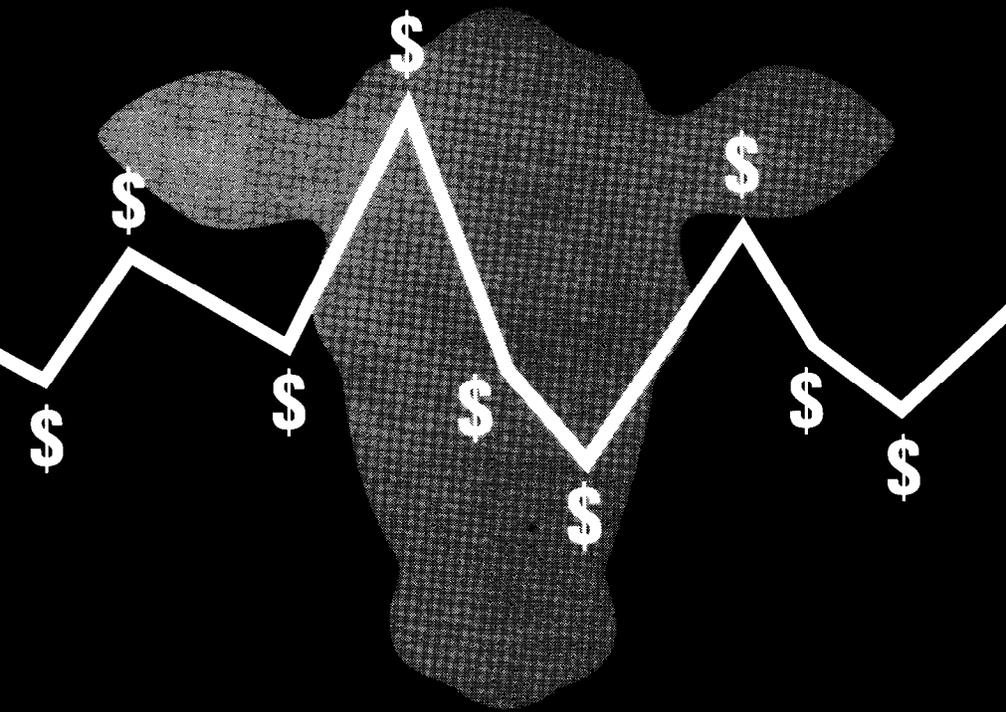
United States
Department of
Agriculture

Agricultural
Cooperative
Service

Service
Report 38

Marketing Fed Cattle

Cooperative Opportunities



Abstract

Marketing Fed Cattle: Cooperative Opportunities

Clement E. Ward,
Timm J. Bliss,
Julie A. Hogeland

Clement E. Ward, professor and Extension economist, Oklahoma State University; Timm J. Bliss, former Extension assistant, Oklahoma State University; and Julie A. Hogeland, agricultural economist, Agricultural Cooperative Service, U.S. Department of Agriculture.

Structural changes in cattle feeding and meatpacking have affected cattle feeders. As a result, some cattle feeders have become increasingly concerned about market access and pricing methods. This report explores one response available to cattle feeders: to collectively market cattle by forming a marketing cooperative. Three alternative types of fed cattle cooperatives are discussed: bargaining cooperatives, electronic marketing cooperatives, and integrated cattle feeding-meatpacking cooperatives.

Keywords: cooperative, marketing, cattle feeding, bargaining cooperatives, electronic marketing, vertical integration

ACS Service Report No. 38

September 1993

Preface

Highlights	ii
Background and Objectives	1
History of Livestock Marketing Cooperatives	3
Recent Interest in Fed Cattle Marketing Cooperatives . .	4
Alternative Fed Cattle Marketing Cooperatives	7
Cattle Feeders' Decision Process	8
Hypothetical Market Environment	11
Perceived Marketing Problems	12
Marketing Cooperative Solutions	13
Description of Potential Alternatives	17
Bargaining Cooperatives	18
Electronic Marketing Cooperatives	28
integrated Cattle Feeding-Meatpacking Cooperatives	39
Concluding Remarks	49

Highlights

In response to structural changes in meatpacking and cattle feeding, cattle feeders have expressed increased interest in cooperatives as a marketing alternative. Livestock producers have long recognized that cooperatives enable them to do collectively what they cannot do individually. Producers acting together can offset the inherent disadvantages of acting alone. Cooperatives provide a wide range of marketing services for livestock producers.

Three alternative types of cooperatives are discussed in this report: (1) bargaining cooperatives; (2) electronic marketing cooperatives; and (3) integrated cattle **feeding-meatpacking** cooperatives. No single type of fed cattle marketing cooperative is endorsed. Cattle feeders must weigh the advantages and disadvantages of each type to see if it can address their perceived problems and can meet their objectives with the resources they have.

Cattle feeders considering a cooperative marketing effort must go through a planning process. Initially, planning is required to identify the type of cooperative that best fits the needs and objectives of the group considering a cooperative venture. Additional planning and study are required after identifying the preferred type.

The suggested steps proposed here in deciding whether or not to organize a fed cattle cooperative modify the problem-solving process slightly. They may be followed by an individual assuming leadership in this venture or by a core group of feeders providing leadership. The decisionmaking steps are as follows:

- (1) Understand the production and marketing environment in which you operate.
- (2) Identify the problems that need to be addressed.
- (3) Identify which problems alternative types of fed cattle cooperatives can realistically reduce or eliminate.
- (4) State clearly the objectives of the cooperative.

(5) Select the type of cooperative that can meet the objectives and realistically address the perceived marketing problems.

(6) Analyze pros and cons of each alternative type of cooperative.

(7) Determine the potential interest among prospective members.

(8) Develop a ballpark estimate of investment and operating capital requirements.

(9) Conduct a detailed feasibility study and business plan.

(10) Implement the plan if prospects for success continue to be favorable.

Each type of cooperative alternative discussed can address one or more perceived marketing problems or concerns. The following summarizes which concerns could best be addressed by each type of cooperative.

Bargaining Cooperatives

A bargaining cooperative could address the following concerns to some degree:

1. Low or inadequate profits from cattle feeding - to the extent that feeders bargain for higher fed cattle prices, improve cattle quality, and reduce end-of-the-feeding-period cost of gain;

2. Low or volatile feeder and fed cattle prices - to the extent that feeders receive higher prices for fed cattle from improvements in marketing efficiency and being customer (buyer) oriented;

5. High costs of feeding cattle - to the extent that feeders reduce the length of the feeding period and thus reduce the marginal cost of holding cattle on feed for excessive periods;

6. Inadequate buyer competition for fed cattle - to the extent that feeders contact all potential buyers and provide

them an opportunity to purchase cooperatively marketed cattle; and

7. Failure of price signals to reach cattle producers from consumers - to the extent that receiving kill sheets on cattle allows cattle feeders to better understand the extent to which their cattle are meeting consumer preferences for lean beef.

Electronic Marketing Cooperatives

A cooperative sponsoring an electronic market could address the following concerns at least to some degree:

1. Low or inadequate profits from cattle feeding - to the extent that increased buyer competition and increased marketing efficiency result in higher prices;

2. Low or volatile feeder and fed cattle prices - to the extent that cattle feeders receive higher prices for fed cattle;

3. Inadequate buyer competition for fed cattle - to the extent that each potential buyer is given an opportunity to purchase cattle via the electronic market;

4. Failure of price signals to reach cattle producers from consumers - to the extent that more detailed descriptions of cattle sold and subsequent analysis may reveal buyer preferences for selected fed cattle characteristics; and

5. Thinly reported cattle and beef markets - to the extent that market information from electronic markets is accurate, timely, and more detailed than market information from most public and private price reporting services.

While electronic marketing cannot resolve all market deficiencies perceived in agricultural marketing, it has an impressive array of potential benefits. Therefore, the incentive to develop and operate an electronic marketing cooperative for fed cattle rests primarily with cattle feeders, as they stand to gain more than meatpackers in most cases.

Integrated Cattle Feeding-Meatpacking Cooperatives

A large meatpacking cooperative owned by feeders could address the following concerns:

1. Low or inadequate profits from cattle feeding - to the extent the increased buyer competition resulted in higher prices for fed cattle and/or the cooperative returned some of its profits from meatpacking to member-feeders;
2. Low or volatile feeder and fed cattle prices - to the extent that additional buyer competition resulted in higher fed cattle prices; and
3. Inadequate buyer competition for fed cattle - to the extent that the meatpacking cooperative adds buyer competition without causing existing packers to exit the industry.

An alternative cattle feeding-meatpacking cooperative might be organized exclusively to capitalize on niche markets for beef products. A niche-marketing cooperative might address the following cattle feeder concerns:

1. Low or inadequate profits from cattle feeding - to the extent that the cooperative could profitably penetrate or expand beef markets and pay cattle feeders higher prices for fed cattle or share cooperative profits with cattle feeders;
2. Low or volatile feeder and fed cattle prices - to the extent new product and market development efforts of the cooperative lead to higher fed cattle prices;
3. Poor beef demand by consumers - to the extent that the cooperative identifies and meets consumers' beef demands with new products or services;
4. Inadequate buyer competition for fed cattle - to the extent that a niche-marketing cooperative provides an additional buyer for fed cattle; and
5. Failure of price signals to reach cattle producers from consumers - to the extent the cooperative could better identify consumer demands and reflect that demand to cattle feeders through market prices.

Each of the three types of cooperatives could benefit cattle feeders under certain circumstances. Each could also fail under certain circumstances. Always, cattle feeders interested in exploring marketing cooperative alternatives for fed cattle must understand what they can realistically accomplish via a cooperative. A cooperative is not automatically the solution to marketing problem(s). Cattle feeders must consider a cooperative with open eyes and an open mind. There are economic reasons why the existing market structure has evolved to what it is today. Likewise, there are economic reasons why the existing market structure did not evolve in a manner that accords cooperatives a bigger role in fed cattle marketing. Cattle feeders, by organizing a cooperative, are attempting to alter the existing market structure in some way. They must understand the economic reasons that may be working against successfully organizing a fed cattle marketing cooperative. Once those reasons are identified and a plan developed to overcome them, the probability of success for a fed cattle marketing cooperative should increase.

Marketing Fed Cattle: Cooperative Opportunities

Clement E. Ward,
Timm J. Bliss,
Julie A. Hogeland

BACKGROUND AND OBJECTIVES

Structural changes in cattle feeding and meatpacking have had major implications for cattle feeders.¹ An increasing percentage of fed cattle are marketed directly to packers, bypassing public terminal and auction markets. In 1990, 94 percent of reported steer and heifer slaughter by packers was procured by direct methods.² Smaller cattle feeders are in an unenviable bargaining position relative to packer-buyers. Even the largest **feedlots** are relatively small compared with most major packers. Direct trading has formed the basis for market price reporting as public market transactions decline. There are fewer direct transactions between feeders and packers to report, however, as packer-feeding, forward contracting, and exclusive feeder-packer marketing arrangements become more common. While the number of meatpackers has declined, both plant and firm size has increased, and concentration, a measure of market dominance by a few firms, has increased sharply in the 1980's.³ Cattle feeders, as a result,

¹ In this report cattle feeders include cattle producers who feed cattle in custom **feedlots** as well as managers of cattle feedlots.

² Packers and Stockyards Administration, Statistical Report. U.S. Department of Agriculture, November 1992.

³ Clement E. Ward, "Structural Change: Implications for Competition and Pricing in the Feeder-Packer Subsector," Structural Change in Livestock: Causes, Implications, Alternatives. Wayne D. Purcell, ed. Blacksburg, Virginia: Research Institute on Livestock Pricing, February 1990

have become increasingly concerned about market access and price determination.⁴

One response by cattle feeders to pricing and competition concerns is to form collectively a marketing cooperative. The Agricultural Cooperative Service, U.S. Department of Agriculture, started this project in conjunction with Oklahoma State University. The objective was to outline alternative fed cattle marketing cooperatives that cattle feeders might consider in responding to structural changes. The purpose of this report is to provide to cattle feeders information about how cooperatives may help improve their marketing situation.

Alternative types of marketing cooperatives discussed will not reduce or eliminate numerous types of problems facing cattle feeders but are intended to resolve or diminish competition and pricing concerns in fed cattle marketing. Alternatives discussed in this report were chosen because each potentially increased marketing efficiency for cattle feeders. Marketing fed cattle via cooperatives has the potential to increase cattle feeders' returns, especially where poor marketing conditions exist.

Three general types of cooperatives are: (1) bargaining cooperatives; (2) electronic marketing cooperatives; and (3) integrated cattle feeding-meat-packing cooperatives. No single type of fed cattle marketing cooperative is endorsed. Interested cattle feeders must weigh the advantages and disadvantages of each type for their particular situation and in light of their objectives and resources. This report should direct cattle feeders to the alternative that offers the highest probability of responding appropriately to the existing market environment. Additionally, the report should provide guid-

⁴ Julie A. Hogeland, Market Access in an Era of Structural Change in the Livestock Industry. Washington, D.C.: Agricultural Cooperative Service, U.S. Department of Agriculture. Technical Assistance Report, September 1988.

ance in obtaining the detailed information required to organize and implement the chosen alternative.

While this report focuses on the marketing problems and potential alternatives for cattle feeders, other livestock producers may experience similar problems. The process of identifying specific problems and assessing alternatives also applies to other livestock classes and species.

HISTORY OF LIVESTOCK MARKETING COOPERATIVES

Marketing cooperatives are organized in response to changing needs of producers, and changing economic conditions and technology.⁵ Livestock producers have long recognized that cooperatives enable them to do collectively what they cannot do individually. Producers act together to offset the inherent disadvantages of acting alone. For decades, relatively small family farmers and ranchers have found themselves buying supplies from or marketing products to larger agribusinesses. Therefore, acting alone, individual farmers and ranchers have virtually no market power. One response is to organize farm supply or marketing cooperatives.

Collective actions by livestock producers began about 1785 when societies were organized to import purebred cattle. Later, cooperative livestock drives were organized to move livestock from farm to slaughter. Cooperative public auctions were organized in the 1830's. In the early 1900's, livestock producers in Nebraska and Kansas organized shipping associations to ship livestock by rail to central markets. These early cooperatives enabled small livestock producers to pool their

⁵ John T. Haas, David L. Holder, and Clement E. Ward, Livestock and Wool Cooperatives. U.S. Department of Agriculture, Economics, Statistics, and Cooperatives Service, Cooperative Information Report 1, Section 14. May 1979.

small sale lots into carload lots for more efficient shipment to terminal markets.

The first cooperatives engaged in livestock slaughtering and processing began in 1914, but these early meatpacking cooperatives failed. Following the success of shipping associations, cooperative sales agencies were organized at terminal markets. Such cooperative marketing agencies still operate today. Initially, they grouped small sale lots into larger lots, and bargained with meatpackers for the best price.

Cooperative livestock marketing agencies broadened their activities in the 1950's and 1960's to order buying and order selling for members, both directly and through public markets. Livestock cooperatives broadened their activities in other ways. Some cooperatives now operate local auction facilities and have formed successful livestock credit cooperatives. Innovative cooperatives were the first adopters of electronic trading techniques such as telephone auctions, and even experimented with photorama auctions, the predecessor of today's growing satellite video auctions. Cooperatives were organized to feed livestock as well as to slaughter livestock and process meat. The oldest and largest meatpacking cooperative still operating today is Farmland Foods, which began in 1959.

In summary, cooperatives have provided a wide range of marketing services to livestock producers. As conditions changed over time, cooperatives adapted to the changes. Conditions continued to change in the 1990's, and interest in forming cooperatives responsive to change also has continued.

RECENT INTEREST IN FED CATTLE MARKETING COOPERATIVES

The changing economic environment resulting from several factors caused livestock producers to again consider cooperative marketing as a possible response to change. Most interest has been expressed by cattle feeders, rather than other livestock producers, largely because structural changes have occurred most dramatically in cattle feeding and meatpacking.

In 1975, a group of Iowa cattle feeders organized the **Tama** Producers Marketing Association to market fed cattle using an innovative approach to beef marketing. Cattle were custom slaughtered; carcasses were cut, packaged, and frozen; and frozen beef products were marketed to consumers, often through unconventional retail outlets such as gas stations and beauty salons. Consumers, however, did not respond to frozen beef products as expected by the innovators, and after more than a year-long effort and several thousand dollars, the cooperative failed. Although the marketing cooperative was innovative, cattle producer-organizers were unfamiliar with consumer demands, and successful marketing begins with understanding customers' wants and needs.

Other efforts were undertaken in the 1980's. A group known as the Better Beef Marketing Committee began developing a cooperative marketing organization with the assistance of a hired consultant in 1986.⁶ At the encouragement of the consultant, a cooperative known as Better Beef Marketing, Inc., was organized. Before its inception, while still in the study and developmental phase, Better Beef Marketing encountered problems.

Serious fundamental conflicts arose among potential members over the objectives and direction of the cooperative. One group of producers wanted to organize a large cooperative meatpacking company to be a competitive force in the marketplace with large existing packers **such as** IBP, the largest meatpacking firm. Another group wanted a cooperative that could provide the structure and operating support for exploring relatively small niche markets for beef and for new beef products, such as natural or lite beef products. Such diverse objectives merited two cooperatives, but only a single cooperative was proposed. Perhaps as a result of internal conflicts and unclear direction for the organization, combined

⁶J.C., **Bigler** (Consulting Team Leader), "The Better Beef Marketing Alpha Report. "Confidential consulting report, May 1986.

with attempts to raise investment capital during a period of financial hardship in the agricultural sector, the cooperative failed to accumulate the needed capital to begin operating. Eventually, the effort ended unsuccessfully, again at a cost of several thousand dollars to interested cattle producers.

Another attempt was made to form a fed cattle marketing cooperative in 1986. Most previous attempts to organize fed cattle cooperatives involved smaller sized cattle feeders, i.e., farmer feeders primarily. Unlike previous efforts, this one involved commercial cattle **feedlots** in the High Plains feeding area. Commercial **feedlot** managers began exploring the possibility of some type of group marketing effort through the Texas Cattle Feeders Association. A consulting study was completed, but a cooperative never **materialized**.⁷ One reason for not forming the cooperative was the poor image cooperatives had among some of the **feedlot** managers. In fact, the discussions were of "group marketing," rather than "cooperative marketing." As with Better Beef Marketing, potential participants disagreed on the objectives of a group marketing venture. The initial concept was to pool cattle on paper and hire a management team to bargain with packers over price and terms of trade. Many **feedlot** managers, however, were unwilling to transfer marketing decisions to a hired management team.

In 1988 and 1989, several Iowa cattle feeders organized cooperatives to market fed cattle and make cattle feeding in Iowa more competitive with commercial **feedlots** in the Plains States. The objectives of the newly organized cooperatives were to pool management services and create more competitive custom **feedlots** in Iowa. Consequently, the cooperatives were not marketing cooperatives per se. Their principal focus was on improving management of the cattle feeding enter-

⁷ LBAS Consulting Group, "Economic, Organizational, and Marketing Aspects of a Cattle Feeders Group Marketing Program." Confidential consulting report, October 1986.

prise in member feedlots. These cooperatives, however, are examples of producers using cooperatives to respond to structural changes that affected Iowa and other Midwestern States.

ALTERNATIVE FED CATTLE MARKETING COOPERATIVES

Cooperatives can assume several marketing functions, all of which depend on the structure and competitive environment in which cattle feeding and meatpacking exist. Cattle were fed in more than 44,000 **feedlots** in the United States in 1990, but 85 percent of the cattle were marketed from just 1,634 **feedlots**.⁸ Each of those larger **feedlots** had a one-time capacity of 1,000 or more cattle. The largest **feedlots** (one-time capacity of 32,000 or more cattle) marketed an average of 88,474 cattle, still a far cry from the average slaughter of 945,278 cattle per year among the 18 largest steer and heifer slaughtering plants in 1990.⁹ Consequently, there is a wide size disparity between cattle **feedlots** and packing plants.

Cooperatives offer an opportunity for smaller cattle feeders to counter some of the size advantages enjoyed by **packer-buyers**. A bargaining cooperative or association may increase feeders' returns by increasing their competitive position relative to packer-buyers. The association could negotiate prices and terms of trade for the pooled livestock of its members. Included in the bargaining agreement could be carcass characteristics on cattle marketed by members, with the purpose of improving the cattle fed and marketed. Likewise, the association may bargain for contract terms, either in production or marketing, and provide other marketing services.

⁸ National Agricultural Statistics Service, Cattle on Feed. U.S. Department of Agriculture, January 1990.

⁹ Packers and Stockyards Administration. Statistical Report.

A cooperative could be formed to develop a centralized electronic market in which to sell fed cattle. An electronic market could encourage competition among existing buyers and provide complete and timely market information on sales, also including carcass data for members. An electronic market, using satellite communication and computer technology, might increase the efficiency of marketing fed cattle from smaller feedlots and of procuring fed cattle by smaller packers.

Cooperatives have vertically integrated forward into processing and brand label marketing in many commodity areas.¹⁰ Cooperatives can be organized to vertically integrate into meatpacking, but cooperative meatpacking is not a panacea. The history of cooperative meatpacking is largely one of failure and disappointment, with few success stories. Two diverse avenues seem to be available to cattle feeders, both of which surfaced in the discussions leading to the Better Beef Marketing cooperative. The first avenue is to develop a large, integrated cooperative whose purpose is to compete with its large competitors. The second avenue is to develop a smaller, integrated cooperative which seeks to identify and capitalize on market niches, i.e., producing products which satisfy segmented and targeted customer markets.

CATTLE FEEDERS' DECISION PROCESS

Cattle feeders must systematically approach the decision of whether or not to organize a marketing cooperative. Essentially, cattle feeders should follow the problem-solving approach. While different authors may present the problem-solving process differently, most would agree on the following: (1) identify the problem; (2) determine alternatives; (3) analyze pros and cons of each alternative; (4) make a decision; and (5) implement the decision.

¹⁰ Julie A. Hogeland, Cooperative Brands of Processed Foods. Washington, D.C.: Agricultural Cooperative Service, U.S. Department of Agriculture. Special Report 14, 1985.

The suggested steps proposed here in deciding whether or not to organize a fed cattle cooperative modify the problem-solving process slightly. They may be followed by an individual assuming leadership in this venture or by a core group of feeders providing leadership. The decisionmaking steps are as follows:

(1) Understand the production and marketing environment in which you operate.

Marketing means being customer oriented. Cattle feeders need to understand the needs and wants of buyers. Cattle feeders can either interpret consumers or purchasers of fed cattle, i.e., packers, as being ultimate users of beef products. In either case feeders need a perspective of the marketplace in which they feed and market cattle

(2) Identify the problems that need to be addressed.

(3) Decide which problems alternative types of fed cattle cooperatives can *realistically* reduce or eliminate.

Many cattle feeders can identify problems, and it is easy to say that a cooperative is the answer to those problems. It is much more difficult, however, to specifically identify which problems can be addressed by which type of cooperative. Further, which type of cooperative has a realistic chance, i.e., a high probability of reducing or eliminating the problems? Why invest time and money organizing and implementing a cooperative that has a low probability of effectively addressing the primary problems you need resolved?

(4) State clearly the objectives of the cooperative.

Previous efforts to organize fed cattle cooperatives clearly indicate the importance of this step. Potential members must agree on the objectives at the outset, or the probability of organizing a successful cooperative is reduced significantly from the beginning. Objectives should be tied to the most pressing problems or most clearly identified opportunities.

(5) Select the type of cooperative that can meet the objectives and realistically address the perceived marketing problems.

Conceivably, more than one type of cooperative will be considered at this point. Preferably, however, the range of possible alternatives will be narrowed to no more than two by this time.

(6) Analyze pros and cons of each alternative type of co-op.

Pros and cons may only need to be identified for one or perhaps two types of cooperatives in this step.

(7) Determine the potential interest among prospective members.

How many feeders are probable members initially? How much business volume do they represent? How much growth potential is there, both in terms of cooperative membership and business volume?

(8) Develop a ballpark estimate of investment and operating capital requirements.

Without doing a detailed feasibility study or developing a detailed business marketing plan, does the expressed interest of prospective members (number of members and business volume) match closely the rough estimate of capital and volume needs? Is there enough interest to continue analyzing the feasibility of a cooperative? Can prospective members muster the capital requirements, given their potential for collective equity capital and borrowing capacity? Do they have the needed volume to be cost competitive with existing firms and to meet customers' needs?

(9) Conduct a detailed feasibility study and business plan.

Ideally, only one type of cooperative will be considered at this time. Private, community, university, and government resources can be tapped to assist in developing a detailed business development plan.¹¹

¹¹ Melvin J. Stanford, *New Enterprise Management*. Reston, VA: Reston Publishing. 1982.

¹² Gene Ingalsbe, *Farmer Cooperative Publications*. Washington, D.C.: Agricultural Cooperative Service, U.S. Department of Agriculture. Cooperative Information Report 4, September 1992.

(10) Implement the plan if prospects for success continue to be favorable.

The Agricultural Cooperative Service of the U.S. Department of Agriculture provides assistance and considerable information to groups of producers interested in organizing **cooperatives**.¹²

Subsequent sections of this report provide information of the type necessary for steps 1-8. Admittedly, the information here will be of more help in undertaking some steps than others. Beyond step 8, groups of cattle feeders will have to develop the necessary detail in conjunction with other resource groups for their specific situation.

Hypothetical Market Environment

To facilitate thought and to illustrate the process that cattle feeders must follow in choosing the alternative that best fits their situation, a hypothetical market environment is presented here. This market environment assumes a group of cattle feeders from that area have voiced concerns about marketing fed cattle in their area.

Cattle feeders in this hypothetical market are located in a 20-county area, referred to as Region X, which is roughly a rectangular area 120 miles x 150 miles in size. Within Region X are 90 cattle feeders marketing 250,000 fed cattle per year. Fifteen **feedlots** with a one-time capacity of 1,000 head or more account for 85 percent of the cattle marketed. The largest **feedlot** has a one-time capacity of 10,000 head and markets 25,000 cattle annually. The remaining 75 feeders market 37,500 cattle annually. Cattle feeders on average market about 2,000 cattle per month or about 500 cattle per week.

West of Region X are several commercial **feedlots** with a one-time capacity exceeding 8,000 head and a few smaller **feedlots**. In the remaining areas adjacent to Region X, there are several smaller **feedlots**, but cattle feeding has declined in those areas and there are no **feedlots** with a one-time capacity of 2,000 head or more.

No meatpacking plants are within Region X, but five packers purchase cattle for slaughter in plants outside the area. Two of the five packers have large, efficient slaughter plants located within 100 miles of Region X. Together, the two firms slaughter 75 percent of the cattle marketed by cattle feeders in the region. One of the remaining three packers operates a large, efficient plant located about 200 miles from Region X. The other packers operate smaller plants within 50 miles of Region X.

No terminal markets are within Region X or located within 200 miles of the region. Two public auction markets operate within the region but handle mostly feeder cattle and slaughter cows. Consequently, nearly all fed cattle are purchased directly from cattle feeders by packer-buyers. One of the two larger packers feeds cattle in three of the largest feedlots in Region X on a custom basis, a total of 20,000 packer-fed cattle per year. All three of the larger packers offer forward basis contracts to feeders as a means of pricing their cattle. The extent of forward contracting varies but has been as high as 15 percent of annual marketings from Region X over the past 3 years.

Perceived Marketing Problems

Cattle feeders considering a marketing cooperative as a means of resolving marketing problems must identify specifically those marketing concerns or problems. Although referred to here as problems and probably perceived initially by cattle feeders as problems, they may in fact be opportunities rather than problems. Cooperatives are a means of reducing or resolving some types of marketing problems, but cooperatives cannot begin to reduce or resolve others. In our hypothetical example, several concerns or complaints can be heard by listening to cattle feeders in Region X, including:

1. Low or inadequate profits from cattle feeding;
2. Low or volatile feeder and fed cattle prices;
3. Poor beef demand by consumers;

4. Excessive beef imports;
5. High costs of feeding cattle;
6. Inadequate buyer competition for fed cattle;
7. Ineffective beef quality grades;
8. Failure of price signals to reach cattle producers from consumers;
9. Thinly reported cattle and beef markets;
10. Futures markets adversely affecting cash prices;
11. Inadequate regulation of large packers;
12. Forward contracting and packer integration into cattle feeding; and
13. Inaccurate cattle inventory reports.

Some of those concerns must be resolved primarily by individual cattle feeders, some by industry-wide efforts of cattle feeders' trade associations, and some by government policies. The remainder can potentially be addressed by cattle feeder-owned cooperatives.

Marketing Cooperative Solutions

A key question cattle feeders must answer is, "Which concerns can be addressed *realistically* by fed cattle marketing cooperatives?" Recall that three categories of marketing cooperatives are discussed in this report: (1) bargaining cooperatives; (2) electronic marketing cooperatives; and (3) integrated cattle feeding-meatpacking cooperatives. Each can address selected concerns from the list but not all concerns.

Bargaining Cooperatives

A bargaining cooperative may enable a group of cattle feeders, especially smaller feeders, to increase their ability to negotiate better prices and terms of trade with packers. Pooling cattle from smaller cattle feeders into truckload lots and timing deliveries to fit buyers' slaughter schedule will increase marketing efficiency and may increase sale prices for cattle feeders by reducing procurement costs for packers. This result may be especially true for smaller packers who need to

reduce operating costs and offset the size advantage of larger competitors. Cattle feeders might negotiate with packers to return kill sheets on cattle marketed to improve the quality of cattle marketed and select a better time to market cattle without producing excess fat.

Therefore, a bargaining cooperative could conceivably address the following concerns from the list at least to some degree:

1. Low or inadequate profits from cattle feeding - to the extent that feeders bargain for higher fed cattle prices, improve cattle quality, and reduce end-of-the-feeding-period cost of gain;
2. Low or volatile feeder and fed cattle prices - to the extent that feeders receive higher prices for fed cattle from improvements in marketing efficiency and being customer (buyer) oriented;
3. High costs of feeding cattle - to the extent that feeders reduce the length of the feeding period and thus reduce the marginal cost of holding cattle on feed for excessive periods;
4. Inadequate buyer competition for fed cattle - to the extent that feeders contact all potential buyers and provide them an opportunity to purchase cooperatively marketed cattle; and
5. Failure of price signals to reach cattle producers from consumers - to the extent that receiving kill sheets on cattle allows cattle feeders to better understand how their cattle are and are not meeting consumer preferences for lean beef.

Electronic Marketing Cooperatives

A cooperative organized to establish an electronic market for cattle may increase buyer competition for cattle by ensuring that all packers have an opportunity to purchase cattle feeders' cattle. An electronic market can provide instant and accurate market information about cattle sold, and additional information to what is normally publicly reported. Pooling and marketing truckload lots of fed cattle through an electronic market increases marketing efficiency, just as it does in a bar-

gaining cooperative. Cattle feeders, especially smaller feeders, may receive higher prices as the cooperative enables packers to reduce their procurement costs. Electronic markets often provide additional information on cattle sold, which may be useful in interpreting prices for fed cattle. For example, additional characteristics may be used to describe fed cattle sold besides estimated weight, percent quality grade Choice, percent yield grade 1-3, and dressing percentage. Then statistical procedures can be used to analyze prices and determine packer preferences for selected cattle characteristics.

Therefore, a cooperative sponsoring an electronic market could address the following concerns from the above list at least to some degree:

1. Low or inadequate profits from cattle feeding - to the extent that increased buyer competition and marketing efficiency gains result in higher prices;

2. Low or volatile feeder and fed cattle prices - to the extent that cattle feeders receive higher prices for fed cattle;

3. Inadequate buyer competition for fed cattle - to the extent that each potential buyer is given an opportunity to purchase cattle via the electronic market;

4. Failure of price signals to reach cattle producers from consumers - to the extent that more detailed descriptions of cattle sold and subsequent analysis may reveal buyer preferences for selected fed cattle characteristics; and

5. Thinly reported cattle and beef markets - to the extent that market information from electronic markets is accurate, timely, and more detailed than market information from most public and private price reporting services.

Integrated Cattle Feeding-Meatpacking Cooperatives

An integrated cattle feeding-meatpacking cooperative could also address some of the problems facing cattle producers, but identifying which problems is more difficult without knowing how such a cooperative would be organized. Given that difficulty, the concerns typically addressed by two types of integrated cooperatives will be identified.

The first type, a large cooperative organized to compete directly with the largest meatpackers, represents an additional potential buyer for fed cattle marketed from the region. If its primary purpose is to compete with large packers, it might operate no differently on a day-to-day basis than competitors. Alternatively, it might require some level of guaranteed supply of fed cattle from its members. In either case, the cooperative would be governed by member-owners, and profits from the cooperative could be repatriated to member-owner cattle feeders.

Thus, a large meatpacking cooperative owned by feeders could address the following concerns:

1. Low or inadequate profits from cattle feeding - to the extent the increased buyer competition resulted in higher prices for fed cattle and/or the cooperative returned some of its profits from meatpacking to member-feeders;
2. Low or volatile feeder and fed cattle prices - to the extent that additional buyer competition resulted in higher fed cattle prices; and
3. Inadequate buyer competition for fed cattle - to the extent that the meatpacking cooperative adds buyer competition without causing existing packers to exit the industry.

An alternative cattle feeding-meatpacking cooperative might be organized exclusively to capitalize on niche markets for beef products. This cooperative would likely be smaller than the first type. The express purpose of the niche-oriented cooperative would be to identify specialty market opportunities in domestic and foreign markets and to develop unique marketing approaches to reach those markets more effectively than existing firms.

Thus, a niche-marketing cooperative might address the following cattle feeder concerns:

1. Low or inadequate profits from cattle feeding - to the extent that the cooperative could profitably penetrate or expand beef markets and pay cattle feeders higher prices for fed cattle or share cooperative profits with cattle feeders;

2. Low or volatile feeder and fed cattle prices - to the extent new product and market development efforts of the cooperative lead to higher fed cattle prices;

3. Poor beef demand by consumers - to the extent that the cooperative identifies and meets consumers' beef demands with new products or services;

4. Inadequate buyer competition for fed cattle - to the extent that a niche-marketing cooperative provides an **additional** buyer for fed cattle; and

5. Failure of price signals to reach cattle producers from consumers - to the extent the cooperative could better identify consumer demands and reflect that demand to cattle feeders through market prices.

Summary

Marketing cooperatives can address only selected cattle feeder concerns, and then only to varying degrees. Even for those concerns which cooperatives can address, concerns or problems may be reduced but likely will not be eliminated in most cases. The problems identified as those which the three types of cooperatives could most frequently address (table 1) were:

- Low or inadequate profits from cattle feeding;
- Low or volatile feeder and fed cattle prices;
- Inadequate beef quality grades;
- Inadequate buyer competition for fed cattle; and
- Failure of price signals to reach cattle producers from consumers.

DESCRIPTION OF POTENTIAL ALTERNATIVES

The following sections contain a general discussion of various aspects of each cooperative alternative and its strengths and weaknesses. The discussion should assist cattle feeders with steps 4-8 previously mentioned. Considerable detailed analysis will be required, however, for each specific

situation faced by cattle feeders before implementing any of the alternatives discussed here, particularly step 9.

Bargaining Cooperatives

Cattle feeders who face relatively few and larger buyers, such as those in our hypothetical Region X, may achieve improved terms of trade merely by organizing together to bargain with buyers. A bargaining cooperative would likely do little or no actual handling of cattle, but would attempt through collective bargaining to improve the price that cattle producers receive from meatpacker-buyers. A bargaining

Table 1— Cattle Feeder Concerns Addressed by Alternative Types of Fed Cattle Cooperatives.

Producer Concerns	Cooperative Type		Integrated	
	Bargaining	Electronic Market	Large Packer	Niche Market
1. Low profits	X	X	X	X
2. Low prices	X	X	X	X
3. inadequate beef demand				X
4. Excessive beef imports				
5. High costs of feeding	X			
6. Inadequate buyer competition	X	X	X	X
7. Inadequate info. on quality grades				
8. Failure of price signals		X	X	
9. Inadequate price reporting		X		
10. Speculation in futures markets				
11. Increased contracting and packer feeding				

cooperative is a special type of marketing cooperative. Its members coordinate their *selling* activities, but the cooperative usually does not affect other stages of marketing or production.

Factors Influencing Bargaining Effectiveness

Many factors influence the probability of successfully organizing a bargaining cooperative. One factor is the approach taken by cooperative members. The goal of the cooperative should be to improve coordination between cattle feeders and buyers. Improved coordination should reduce buyer costs or improve the buyer's ability to procure desired cattle types and quantities, which in turn might persuade a packer to pay higher prices for cattle purchased. At the same time, the opportunity to bid on specific quantities of cattle may result in added buyer competition and higher prices for fed cattle.

The success of a bargaining cooperative hinges largely on its ability to organize and control a sufficient volume of cattle to evoke a higher price or improve terms of trade with buyers. The cooperative may perform functions that assist packers in the procurement process and increase marketing efficiency, such as delivering at specified times (e.g., Sunday evening for the early-Monday slaughter schedule), in given quantities (e.g., X truckloads each Friday), meeting quality standards (e.g., a high percentage of Select, YG 2 cattle), etc. A critical factor is that members must commit to marketing through the cooperative so that it has control over marketing the cattle.

The principal types of leverage a bargaining cooperative might exercise are (1) pitting buyers against one another to seek the highest bid and (2) threatening to divert cattle from a given buyer's plant to a competing plant for slaughter. The former can be accomplished by seeking bids from all available buyers before selling members' cattle. For the latter to be effective, the cooperative must have arrangements with another packer. For example, cattle could be slaughtered by a com-

peting packer, custom slaughtered for the cooperative, or slaughtered in a cooperative-owned or leased plant.

The cooperative will likely have more difficulty negotiating favorable prices or terms of trade on the basis of volume alone than if it could also improve coordination of fed cattle supplies with meatpackers' needs. Force or threats are unlikely to be effective because cattle are fed over a broad geographic area and by a large number of feeders. A single cooperative is unlikely to control enough fed cattle to affect significantly a meatpacker's needed supply for even a single plant, given the trend toward larger plants resulting from economies of size.¹³ In our example, assume a new bargaining cooperative controlled 10 percent of the available fed cattle in Region X, or about 25,000 head. That number would amount to 500 head a week or about 100 head per day. Although such a number might command a small price premium, the 25,000 cattle would account for only about 2.5-5 percent of the annual slaughter needs of one large packing plant.

Volume combined with improved coordination offers potential benefits to meatpackers, which might translate into higher fed cattle prices. An effective bargaining cooperative is likely to be one that exercises some control over the quantity, quality, and timing of fed cattle marketed. Then the cooperative can merchandise those services to a meatpacker. In essence, cattle feeder-members of a bargaining cooperative must transfer some of their decisionmaking autonomy to the cooperative's hired management.

The cooperative's market volume will likely be directly related to the success of negotiating favorable contracts with meatpackers. A larger volume will increase the probability that the cooperative can successfully negotiate favorable contract terms with meatpackers. Large volume also increases the probability that the cooperative can provide meatpackers with

¹³ Clement E. Ward, *Meatpacking Competition and Pricing*. Blacksburg, VA; Research Institute on Livestock Pricing. 1988.

the quantity, quality, and type of cattle desired where and when the cattle are needed. Many cattle feeders, even smaller ones, ship fed cattle in truckload lots (about 35 cattle/truckload). Simply by pooling smaller sale lots into truckload size lots may enable a packer to pay a higher price. The cooperative will likely have more success bargaining for a price premium, however, if it controls several truckloads of cattle on a regular basis. For example, perhaps it could guarantee to deliver 500 cattle each Friday afternoon for slaughter on Saturday, or whenever the packer needs the cattle. If the cooperative could guarantee to supply a high percentage of a packer's cattle needs on a given day (e.g., 100 percent) or to supply 20 percent of each day's slaughter volume, the packer will likely be more interested in negotiating a price premium for the cooperative's cattle. Market volume will depend upon the willingness of feeders to commit cattle to the cooperative and to honor their commitment. Cattle feeders' commitment of cattle, in turn, will affect how much efficiency gains the packer achieves and how much price premium it can afford to pay. Traditionally, independent cattle feeders have been reluctant to transfer usual marketing decisions or functions to cooperatives. In addition, a bargaining cooperative will almost certainly meet resistance from established buyers who may feel their competitive advantage is threatened by the cooperative. Buyers may offer above-market prices or better contracts, or engage in other practices to discourage feeders from organizing or participating in a bargaining cooperative. The cooperative will need strong member commitment to counter such resistance.

Another factor affecting success will be the response by cooperative members and nonmembers to measurable gains from bargaining. If the cooperative consistently increases returns to members, its success will attract additional feeders to the cooperative. The added volume of cattle may improve the cooperative's bargaining position by enabling it to make larger and more exact commitments to packers. If measurable

gains are not visible initially, however, it may be difficult to retain members and volume. If volume declines, the buyer will view the cooperative as a less reliable source of cattle, and the cooperative's bargaining effectiveness will also decline.

Several factors affect fed cattle prices, e.g., wholesale and futures market prices, cattle quality and sale lot characteristics, day of the week, time between purchase and delivery of cattle, number of buyers, and which buyers purchase **cattle**.¹⁴ Whether or not packers pay a price premium may not be immediately obvious, and may have to be determined by statistical analysis of prices received over time. The cooperative might bargain for a base price or tie a base price to a reported live weight or wholesale price and then bargain for an \$X/cwt. premium. The \$X/cwt. premium may appear to be the gain from bargaining, but whether or not it is may only be determined by further analysis.

Bargaining is more likely to be successful in markets with many cattle feeders (sellers) but few meatpackers (buyers), such as our hypothetical Region X, and/or where a high proportion of cattle are procured via some form of vertically integrated arrangement by meatpackers. Such markets are likely to provide a greater incentive for feeders to implement a bargaining cooperative and to remain committed to it. Markets like Region X, with few buyers and a larger number of sellers, tend to provide a disproportionate advantage to meatpackers because packers have relatively more bargaining power than feeders. These markets also tend to be less responsive to change than when more buyer competition is present.

Overall, bargaining cooperatives can potentially improve the relative market power of feeders and increase cattle **feed-**

¹⁴ Clement E. Ward, "Re-Examining Fed Cattle Pricing Models after a Decade of Structural and Behavioral Changes in Meatpacking." Invited paper presented at the Western Agricultural Economics Association meetings, July 1991.

ers' returns. They may also increase market coordination and efficiency, thereby also benefiting packer-buyers.

Organizational Structure and Operating Costs

Organizational structure refers to the internal arrangements by which a group begins and carries on collective bargaining. Two basic approaches are possible: (1) Existing organizations can be modified for bargaining purposes; and (2) New organizations can be organized in response to changing attitudes and objectives of producers. An established organization will likely have a cost advantage because it may already have office space and a staff. The reputation of the existing cooperative, however, must be considered. There may be reasons to organize a new cooperative rather than work through an established cooperative that has a questionable reputation.

Bargaining organizations take many forms, but all involve the transfer of some individual prerogatives from the producer to the cooperative. For example, members may "give up" the ability to decide when to ship cattle. If the buyer is willing to pay a premium to have cattle delivered on Sunday, members must deliver on Sunday. If a packer wants cattle fed to a given weight and finish and will pay a price premium for that specified quality of cattle, members must meet the terms of the agreement. Success in bargaining depends frequently on the integrity of the decision-making transfer. The transfer places important responsibilities on both cooperative leadership and the general membership.

Cooperative leadership includes the elected board of directors and hired management. Leaders must be able to establish the cooperative's organizational structure, including staff, budget, office space and equipment, and operating procedures and policies. They must be able to develop a specific marketing plan for selling and pricing all fed cattle committed to the cooperative. Leaders walk a tightrope between meeting the buyers' needs and meeting the sellers' needs. Leaders are

largely responsible for recruiting and retaining members. Lastly, leaders need to develop and implement a successful public relations program to enhance the image, effectiveness, and success of the cooperative.

Therefore, the dependability, integrity, technical competence, and trustworthiness of the cooperative's leadership are critically important. In the long run, bargaining success depends upon the ability of cooperative leaders to achieve the organization's goals, effectively hold members together, and reconcile conflicting interests.

Bargaining cooperatives cannot be organized and operated without capital. Many costs for organizing and operating the cooperative are organization-wide, affecting all members. Most bargaining cooperatives will have a fee structure associated with services provided to members. In our example, if a **\$3/head** charge is levied for marketing members' cattle, a cooperative marketing 25,000 cattle annually would generate **\$75,000/year**. From that revenue, the cooperative must pay for a salaried manager, travel expenses, office space and supplies, and any other operating expenses. Additional costs may be borne by individual members in fulfilling the terms of their membership contracts (e.g., hiring labor to load trucks on a weekend). Organizational costs are incurred in recruiting cattle feeder-members, providing information services, negotiating with meatpackers, and carrying on other marketing-related activities. How high the costs are depends on the size of the cooperative, its objectives and operations, and efficiency of its hired management.

How small and still economically viable a cooperative can be is not known. A cooperative may be able to start with a part-time manager working from his/her home and with virtually no hired staff. In the example, if the costs of bargaining to market 25,000 cattle a year are little different from the costs of bargaining for 50,000 cattle, then doubling the volume means halving the cost per head or doubling the revenue to the cooperative. Consequently, volume is important from a

cost-and-revenue standpoint as well as from the viewpoint of bargaining effectiveness.

Getting and holding membership requires considerable effort in many cooperatives. Cattle feeders' longstanding hesitancy to delegate decisionmaking prerogatives to hired management not only is an attitudinal barrier to group unity but also adds to the cost of forming and maintaining a bargaining cooperative.

Cattle feeders belonging to a bargaining cooperative must fulfill the terms of their contracts if the group as a whole is to be successful. If the cooperative agrees to deliver 500 cattle each week, one or more members cannot independently decide to ignore the shipment schedule and deliver cattle at another time. Yet it is difficult to achieve equity in the demands placed upon individual members. Arriving at acceptable terms of member marketing agreements is important. Feeders linked together for bargaining will need to decide numerous questions about what is expected of each member and how association costs will be allocated to establish equitable marketing charges to members. Substantial agreement on these issues before bargaining with buyers will reduce conflicts later and increase the likelihood of a successful cooperative.

A successful bargaining cooperative may encounter a nonmember problem. If collective bargaining is successful in raising cattle prices or improving terms of trade with meatpackers, nonmembers who have not shared the costs may benefit as much or more than members. This situation makes membership recruiting and retention more difficult and expensive, and may cause strife among existing members. Moreover, resentment may develop between members and nonmembers, especially if pressure is placed on nonmembers to join. The potential for such conflict needs to be considered when organizing the cooperative.

Advantages/Disadvantages of Bargaining

Bargaining success or effectiveness should be evaluated based on its net impacts, thereby considering both advantages and disadvantages. Foremost among potential benefits is the opportunity to obtain higher prices and better terms of trade for cattle feeders. If feeders unite to market large numbers of fed cattle, the cooperative has an opportunity to increase the price received for fed cattle. The cooperative may not be able to increase the number of meatpackers to which members sell cattle, but it can ensure that all available meatpackers have an opportunity to bid on fed cattle marketed, thus increasing buyer competition.

The cooperative may bargain with the packer to return slaughter results to members. This is one benefit bargaining cooperatives can achieve but which is difficult to measure. With slaughter results from packers, members can evaluate how their cattle performed in carcass or boxed beef form. As a result, feeders can make necessary changes in type of cattle fed, feeding programs, animal management and health care programs, etc. This type of information can be important and valuable to feeders over time, but measuring how important is difficult.

A bargaining cooperative can reduce the number of sellers that packer-buyers must contact to procure their slaughter supplies, which can reduce procurement costs for packers. For example, a packer might procure 1,000 cattle from 5 individual feeders after traveling to 8-10 feedlots. The packer could save procurement costs by bargaining for the 1,000 cattle with a single seller representative, the bargaining cooperative. Thus, a bargaining cooperative could better coordinate fed cattle flows from member **feedlots** with meatpackers' needs, which can improve feeder-packer efficiency, and can in turn be translated into higher prices paid for fed cattle.

The cooperative also has more resources to accumulate market information and to develop and implement alternative marketing strategies. The cooperative may market cattle on a

dressed weight and grade basis, thus better matching price with product quality. As a result, there could be enhanced pricing accuracy and an improved flow of market information and price signals from packers to producers.

The cooperative could assure members of market access before some marketing decisions are made. Bargaining in advance to supply one packer X number of cattle of a certain type may allow feeders to feed cattle of the type most preferred by the packer. Member-feeders also have guaranteed input in determining acceptable terms of trade for cattle marketed.

Bargaining cooperatives provide distinct advantages to cattle feeders if their price enhancement goals are attained. Typically, the financial commitment to form and operate a bargaining cooperative is relatively low compared with some other types of marketing cooperatives because there is less investment in physical facilities. The \$3/head marketing fee used in an example earlier is considerably lower than for some other types of cooperatives, especially those with extensive physical facilities such as a slaughter and processing plant.

An indirect benefit of bargaining is the effect it may have on the price of cattle throughout the area served by the cooperative. Although that may present nonmember problems, as already noted, it is still a benefit derived from bargaining. Bargaining also may have wider consequences than for just the area where the cooperative is organized. Such benefits, if they result, will evolve only from a bargaining cooperative that controls a substantial portion of all fed cattle marketed.

Among the potential disadvantages (costs) to cattle feeders from effective bargaining, perhaps the primary one is the reduced individual decisionmaking and transfer of specific marketing-related decisions to hired management. The commitment of members' cattle is vital for success, as is transferring the authority to market members' cattle. The commitment by individual members means putting the collective good of

the cooperative ahead of personal preferences at times. Giving up that individualism could be difficult for many cattle producers.

A bargaining cooperative will likely mean increased marketing costs for members. Since most fed cattle are marketed by direct methods currently, a commitment of capital will be necessary, to hire a manager and staff to perform cooperative functions such as member recruiting, negotiating with buyers, collecting and analyzing data, recordkeeping, and distributing information to members. The cooperative initially may only need a part-time manager with part-time staff assistance. Thus, marketing costs may be small, but will still likely be greater than marketing directly to a packer. For example, **\$3/head** for marketing through a cooperative, which was assumed earlier, is still **\$3/head** more than marketing cattle directly to a packer.

Some members will have to serve on the board of directors, and all members should become involved in their cooperative's activities in some way. Thus, this increased time commitment for organizational activities will be considered a disadvantage or cost to some members.

Electronic Marketing Cooperatives

Electronic marketing (used interchangeably here with electronic trading) provides a mechanism to centralize the price discovery process for fed cattle without the physical assembly of buyers, sellers, and fed cattle at a single location. As such, prices should reflect more accurately supply-demand conditions in the area served by the electronic market. Electronic markets may increase access to buyers and enhance buyer competition, which may lead to higher prices. They can also improve market information and reduce marketing costs for buyers and sellers.

An electronic marketing cooperative can combine many of the advantages of direct buying and decentralized (local)

markets with the pricing accuracy normally associated with centralized (regional) price discovery. An electronic marketing cooperative would make it possible for meatpackers to bid on fed cattle located outside their normal procurement area and more distant from their slaughter plants. In turn, each cattle feeder's cattle would be exposed to all available buyers, diminishing the tendency toward regional pricing by a few buyers. An electronic marketing cooperative offers the opportunity to centralize the pricing process on even a small volume of trading, enabling smaller cattle feeders to compete more effectively with larger feedlots.

Types of Electronic Marketing Systems

Several electronic marketing systems have been developed for livestock and meat.¹⁵ Some were implemented successfully and have operated for many years, such as feeder pig teleauctions and computer auctions for slaughter lambs. Others were designed, pilot tested, and perhaps operated for some time before failing, such as a computer-assisted trading system for wholesale meat. Here, electronic marketing systems for fed cattle are categorized into two types, based on electronic marketing systems operating in the late-1980's for other livestock species: (1) electronic (telephone or computer) auctions, and (2) satellite video auctions.

Electronic auctions use either telephones or computers. Conference telephone calls have been used since the early 1970's to market feeder pigs and slaughter lambs. With teleauctions, as they are called, buyers are connected with a seller representative by a conference telephone call. Livestock for sale are described over the telephone (including number of

¹⁵ James B. Bell, Dennis R. Henderson, David L. Holder, Wayne D. Purcell, Maes R. Russell, Thomas L. Sporleder, and Clement E. Ward. *Electronic Marketing: What, Why How*. Oklahoma Cooperative Extension Service, Circulate E-833, May 1984.

head, sex, estimated weight, grade, and location of the livestock). All pertinent terms of trade, such as weighing conditions, shrink, freight costs, etc., are given to buyers by the sponsoring organization. Then livestock are auctioned over the conference telephone call. Buyers bid by an identification number to preserve buyer anonymity in the bidding process. After the teleauction is completed, livestock are delivered to the successful buyer according to the sale agreement, and sellers are paid by the buyer.

Generally, telephone auctions have given way to computer auctions, though in some instances, telephone auctions may still be the most viable marketing alternative. Computer auctions operate similarly to teleauctions; only computers receive, store, process, and send information about the livestock being offered for sale. Potential buyers have access to the description of livestock being offered for sale via computer terminal. Computers are programmed to conduct an auction among buyers, and can also be programmed to sell livestock by other pricing methods, such as bid-offer or private treaty (also called private negotiation).

Satellite video auctions are auction sales where buyers view videotapes of livestock being offered for sale, rather than seeing the livestock live or having only a written or verbal description of the livestock. In satellite video auctions, a camera operator visits each farm or ranch to videotape the livestock being offered for sale. Videotapes are edited to adequately show the livestock to buyers. On sale day, buyers may sit in their homes or offices to view on television the videotapes of the lots offered. Buyers may also assemble at predetermined sites (often motel conference rooms) to view the cattle on large-screen televisions. Buyers receive the auction via a satellite dish. Verbal descriptions of the livestock are included on each videotape, and the seller often explains on the videotape how the livestock will be delivered and other pertinent terms of trade. The auctioneer then starts the auction and sells the livestock to the highest bidder. Buyers simply telephone a

number shown on the television screen and bid while on the telephone. At an agreed-upon time after the sale, livestock are shipped directly from each seller's farm or ranch to the buyer.

Factors Influencing Electronic Marketing Effectiveness

As with bargaining cooperatives, several factors affect the effectiveness of an electronic marketing cooperative. Also, an electronic marketing cooperative can be structured in numerous ways to meet the needs of a particular group of market participants, i.e., buyers and sellers.

A primary objective of an electronic marketing cooperative is to expose fed cattle to more potential buyers and, simultaneously, to facilitate better access by buyers to more fed cattle. In our hypothetical Region X, many cattle feeders, sometimes even the larger ones, may only have one or two packers stop regularly at their **feedlot** to bid on cattle. It is not cost-effective for all five packers to send a buyer to each **feedlot**. Yet, an electronic market can expose each feeder's fed cattle to all five buyers. An electronic marketing cooperative may be especially helpful to cattle feeders in situations where a market power imbalance exists in favor of buyers. An electronic market does not create buyers; it only gives each available buyer an opportunity to bid on cattle offered for sale. It has little to offer in situations where a single buyer dominates a market.

As with bargaining cooperatives, trading volume is important in electronic markets for two reasons. First, large volume can reduce operating costs of the cooperative, just as was true with a bargaining cooperative. Regardless of the type and design of the electronic market, it incurs costs which are borne by sellers. Such costs, while not necessarily large for individual sellers, are a visible cost to cattle feeders when compared with direct marketing to packers. As with a bargaining cooperative, if a **\$3/head** marketing fee is assessed to sellers using the electronic market, that amounts to **\$3/head** more than marketing directly to packers.

A second volume-related aspect deals with maintaining meatpacker and cattle feeder participation over time. Volume attracts buyers. Buyers' interest, in turn, attracts additional volume from feeders. A successful teleauction might be established to sell one or a few truckloads of cattle. If meatpackers learn, however, that they can consistently purchase several truckloads of cattle from an electronic market, which in turn helps them meet their procurement requirements, they are more apt to participate in an electronic market. In our Region X example, offering 500 cattle weekly, about 14 truckloads, will be more inviting to packers than only offering 3 loads every 2 or 3 weeks.

Conversely in our example, if only one or two of the five available meatpackers participate in the electronic market, sellers may lose interest and discontinue marketing through the cooperative. Lack of adequate trading volume reduces meatpacker interest, causing them to cease buying through the cooperative. There have been instances where even small-volume electronic markets organized in a low-cost manner have been successful, but other factors offset the small volume to make the electronic market successful.¹⁶ As with bargaining, a cooperative may represent successfully a few sellers and a small volume of cattle. Greater volume, however, will likely increase the probability of greater success for the cooperative, its members, and buyers.

Commodities traded electronically must have characteristics that can be communicated to buyers, and buyers and sellers must be willing to accept a common system for describing the commodity. Typically, livestock buyers are unable to physically examine the livestock offered for sale through electronic markets. Consequently, buyers must rely on accurate

¹⁶ Clement E. Ward, "An Empirical Study of Price Discovery and Competition for Slaughter Lambs." *Western Journal of Agricultural Economics*. 9(1984): 135-44.

and meaningful livestock descriptions by the sponsoring cooperative. Fed cattle may change quality appreciably if there is a several-day lag between the time cattle are described and when they are delivered to the buyer. A third party may be employed to describe fed cattle, such as a State or Federal grader. Also, a procedure is needed for reconciling differences between how the cattle were described and what the buyer expected to receive based on that description. Commonly accepted terminology understood by buyers and sellers may need to supplement standard or official sex, weight, and grade descriptions. The key is helping buyers evaluate fed cattle being offered for sale so that they can better match price and quality.

Participants in any given electronic market transaction may be unknown to each other. Since face-to-face communication does not occur in electronic markets, the cooperative must provide a means of identifying and certifying all potential buyers and ensure that sellers will deliver what was offered. Consequently, some method of warranting buyer and seller behavior is needed. Thus, appropriate performance guarantees must be provided both for cattle feeders and meatpackers, so all are assured they are dealing with reliable individuals and firms.

A mechanism must be provided to facilitate sale negotiations between feeders and meatpackers. The pricing mechanism in an electronic market is typically either an English (ascending bid) auction, which is common in the United States, or a Dutch (descending bid) auction, which is common in Europe and Canada. Cattle feeders must know when and how to offer their fed cattle for sale, and meatpackers must know about the fed cattle offered for sale, and when and how to bid.

The cooperative will arrange for title transfer, payment, and other functions necessary to legally transfer fed cattle from member-feeders to meatpacker-buyers. It may or may not arrange to ship fed cattle physically from feedlots to pack-

ers. Many of these functions may be handled much as they have been traditionally. But there may be opportunities to reduce fed cattle handling and movement, lower transportation and shrink costs, and otherwise streamline the physical transfer process.

Organizational and Operational Costs

Investment and operating costs of electronic marketing systems vary widely. Both types of electronic marketing systems have been found to be feasible economically under certain operating environments. Investment and operating costs for a fed cattle electronic market will depend on several factors. Among them are (1) telecommunications used; (2) services provided by the cooperative and need for staff to provide those services; (3) volume marketed; and (4) an educational effort to recruit members.

Some existing organizations market livestock via **teleauction**, computer, or by satellite for the same or less cost than if livestock producers used a public livestock market. The cost, however, will still exceed direct marketing of cattle from feeder to packer. Relatively little cost is involved in hiring a **part-time** market coordinator or manager to organize a once a week or less frequent teleauction. Major operating costs include travel by the coordinator to cattle **feedlots** to see the cattle, phone contacts with potential buyers and successful buyers, and the cost of the conference telephone. Larger volume operations will increase costs. As volume increases, the part-time manager may need to become a full-time manager. While costs increase as volume increases, so does revenue from per head marketing charges.

Cooperatives using a network of computers and/or satellite communications will incur higher total costs and require a higher volume of fed cattle to keep per head costs competitive. Again, volume marketed by the cooperative is a key to keeping operating costs low or competitive with other marketing alternatives, as there are economies of size associated with

electronic marketing. For example, if a cooperative needs \$20,000 in electronics equipment, marketing 25,000 fed cattle compared with 5,000 cattle reduces the initial investment cost from **\$4/head** (for 5,000 cattle) to just **\$0.80/head** (for 25,000 cattle).

Services provided and expected volume marketed will determine to a considerable extent the staff size needed by the cooperative and the cost of providing those services. In general, investment costs in an electronic market are relatively low, since investment costs require little capital requirements for physical facilities. Even the cost of computers and video equipment has declined substantially from the earliest use of computers and videotapes in electronic markets. Consequently, the primary costs are operating costs, including a hired manager, staff, travel, telephone, and related business costs.

Electronic marketing, while not a new concept to some cattle feeders, will be a relatively new and innovative concept to others. Many potential participants do not understand how electronic markets function, much less their potential benefits and costs. An investment in education will be required by the cooperative. Members must be educated in both operating procedures of the cooperative, as well as potential benefits and costs associated with electronic marketing.

Advantages/Disadvantages of Electronic Marketing

Evaluations of several electronic marketing systems reveal a number of rather consistent observations about their benefits to buyers and sellers.¹⁷ The magnitude and relative importance of each of these benefits can vary because of differences in geographic locations, commodity traded, market structure, type of electronic marketing system, and other factors. Nevertheless, three benefits have been realized in most

¹⁷ Bell, *Electronic Marketing: What, Why, How*.

instances: (1) improved market information and pricing accuracy; (2) higher prices from reduced marketing costs and enhanced buyer competition; and (3) improved market access for buyers and sellers.

Market information is generally considered to be a “public good,” in that the availability of accurate, complete, and timely information creates benefits to all market participants. Because electronic markets are organized and centralized trading mechanisms, the collection of accurate and comprehensive price information is facilitated, which helps producers judge the true market value of their cattle. Because they use electronic and satellite communications, timely dissemination of that information is also improved. Market information from electronic markets can be tied directly to how fed cattle are described. Statistical methods can then analyze the price and volume data to determine the value of specific types of fed cattle or of specific animal characteristics. Such analyses can improve the price-signalling process between packers and feeders, thus moving toward value-based marketing.

Theoretically, buyers can pay higher prices when they operate more cost-efficient plants.¹⁸ To the extent that electronic markets can reduce procurement costs for fed cattle, some of those cost savings may be passed back to feeders in the form of higher fed cattle prices, without increasing meatpackers’ procurement costs. Without statistical analysis, however, the higher prices may not be evident to members.

Increased competition is a major objective of most electronic markets. An electronic market for fed cattle is intended to increase effective competition among buyers by exposing fed cattle to available buyers and by creating trading procedures that encourage competitive interaction. Ideally, a cattle feeder who sells by private treaty to one or two buyers might

18 Clement E. Ward, “Meatpacking Plant Capacity and Utilization: Implications for Competition and Pricing.” *Agribusiness: An International Journal*. 6(1990a): 1.

sell through an electronic auction to four or more buyers. The same potential competition exists in private-treaty selling as in electronic markets, but an electronic market converts what may be termed latent competitive potential into effective competition by ensuring that each potential buyer has the opportunity to purchase cattle offered for sale. Higher prices from enhanced buyer competition and reduced procurement costs are some of the most consistent findings from electronic livestock **markets**.^{19 20 21}

Access by cattle feeders to an electronic market and description-selling via an electronic marketing cooperative can facilitate access to the marketplace for geographically dispersed or isolated sellers and buyers. Because of the centralized nature of these markets, a greater number of potential trading opportunities exist than is typical in many direct trading situations. Thus, market opportunities for smaller producers are enhanced. In some cases, they can combine their fed cattle with cattle owned by other feeders to provide more attractive purchasing packages for meatpackers with **large-volume** needs. Because of increased competition, improved information, and expanded market access, prices paid by buyers may more accurately reflect supply-demand conditions in the area served by the cooperative.

An electronic marketing cooperative also has costs or disadvantages for cattle feeders. Some **disadvantages** are nearly

¹⁹ David L. Holder, "Benefits of a Sheep and Lamb Teleauction in Virginia and West Virginia." U.S. Department of Agriculture, Economics, Statistics, and Cooperatives Service. Selected paper at the Southern Agricultural Economics Association meetings. February 1979.

²⁰ Thomas L. Spoleder and Phil L. Colling. "Competition and Price Relationships for an Electric Market." Texas A&M University, Department of Agricultural Economics. Selected paper for the American Agricultural Economics Association meeting August 1986.

²¹ Ward, "An Empirical Study of Price Discovery and Competition for Slaughter Lambs."

identical to those for a bargaining cooperative. Cattle feeder-members must transfer some decisionmaking authority regarding fed cattle marketing to hired management. Thus, cattle feeders will have to subjugate their individual decision-making freedom for the collective good of cooperative members. Cattle feeders also must make a commitment of fed cattle to the cooperative. Volume marketing is important, and cattle feeders need to support the cooperative by marketing all their fed cattle through the cooperative unless the cooperative chooses not to market certain types of cattle for its members.

Cattle feeders may experience increased marketing costs, especially relative to direct marketing to buyers. Depending on the type of electronic marketing cooperative, there may be a capital commitment for equipment such as video cameras and editing machines, satellite receiving and transmitting equipment, and computers. This investment is likely in addition to the marketing charge for hiring a manager and staff to perform the cooperative's marketing and operating functions.

An electronic marketing cooperative, like all cooperatives, requires a time commitment by its members. Time and effort are required to organize the cooperative, recruit and retain members, and govern the cooperative via the board of directors.

A major difficulty with organizing and implementing an electronic marketing cooperative will be meatpacker resistance. Any effort to increase competition and potentially raise prices, unless it simultaneously provides buyers with acknowledged additional benefits (such as access to more cattle or lower procurement costs), will be resisted. Meatpackers will bid higher for fed cattle in the area, both for members' and nonmembers' cattle, to discredit the cooperative and divide its membership. Sufficient member commitment must be present during the early implementation of the cooperative to offset meatpackers' attempts to break the cooperative before it becomes well established.

Electronic marketing cannot resolve all fed cattle marketing problems but existing electronic markets offer several potential benefits. Clearly, the incentive to develop and operate an electronic marketing cooperative for fed cattle rests with cattle feeders, since they expect to gain more than meatpackers in most cases. If the cooperative, however, simultaneously increases access to fed cattle for meatpackers and reduces procurement costs or in some way meets their needs, an electronic marketing cooperative has a better chance of succeeding.

Integrated Cattle Feeding-Meatpacking Cooperatives

Vertical integration into meatpacking allows cattle feeders to maintain control of fed cattle and resulting products further in the marketing channel. Theoretically, vertical integration enables cattle feeders to participate in profits generated by slaughtering fed cattle and by processing and marketing beef products and cattle byproducts.

Cattle feeders can take essentially two paths to develop an integrated cattle feeding-meatpacking cooperative. These divergent paths are referred to here as “high-volume cooperatives” and “niche-market cooperatives.” A high-volume cooperative would be organized if the cattle feeders’ objective is to compete head-to-head with the largest meatpackers in the industry. A niche-market cooperative would be preferred if their objective is to capitalize on new market development opportunities stemming from new customer markets, new products, new processes, or new packaging methods.

Factors Influencing Meatpacking Cooperatives’ Success

Before vertically integrating into meatpacking, cattle feeders must consider carefully the nature of the meatpacking industry, requirements for a successful meatpacking operation, and the goals and objectives of prospective cattle feeder-members. Disagreement among cattle feeders over the type of

meatpacking cooperative to organize will likely destine the venture to failure from the beginning.

High-Volume Cooperatives - Meatpacking is typically characterized as a high-volume, high-risk, low-profit industry. For a successful high-volume cooperative, cattle feeders must enter meatpacking on a large enough scale to be cost-competitive with large existing firms and to serve high-volume beef customers such as retail supermarkets and food service firms. Cattle feeders may enter meatpacking in one of three ways or some combination of the three: (1) build one or more new plants; (2) purchase one or more existing plants; or (3) contract with one or more existing plants to have cattle custom slaughtered and fabricated.

The primary limitation to building a new plant is that livestock producers may be effective cattle feeders, but not effective meatpackers. Understanding and managing a meatpacking firm is considerably different than managing a cattle feeding enterprise. A new plant requires skill in site selection, developing plans with architectural and engineering firms, working with governmental units to meet necessary Federal, State, and local regulations, and hiring competent meatpacking management, just to name a few requirements. Cattle feeders will invest numerous hours selecting and hiring firms with the necessary expertise to carry out their general plans.

Plant location is critical. A new plant must be located close to large numbers of fed cattle and where cattle feeding numbers may potentially increase in future years. New plants also must be near adequate water supplies, and the cooperative must address environmental quality issues (e.g., air quality, sewage treatment, water quality, etc.). It is likely that other firms will already have one or more plants located close to the selected site. Market penetration then becomes a major issue. Even if an efficient new plant can be built, a new plant must purchase fed cattle from cattle feeders that currently market their cattle to other meatpackers. Existing meatpackers may compete more vigorously for supplies of fed cattle, raising

prices paid for cattle for some period of time. On the surface that is precisely what cattle feeders would like to experience. Higher fed cattle prices, however, put gross margin pressure on the new cooperative. A cooperative may circumvent some of the pressure placed on it by existing firms if cattle feeder-members of the cooperative agree to market all or most of their fed cattle through the cooperative. A strong commitment by cattle feeder-members to market all cattle through their cooperative will also reduce procurement costs for the new cooperative, particularly if marketing agreements are implemented.

The new cooperative also must market its beef products and cattle byproducts. Those products will likely be sold to existing firms that are currently purchasing from established meatpackers. Again, existing meatpackers are not going to relinquish their customers without resistance. Existing meatpackers may lower their beef product prices to customers for some period of time. Again, on the surface, lower beef prices are desirable for consumers and have a positive effect on beef demand. But lower beef prices also put gross margin pressure on the new cooperative. An alternative for the cooperative is to sign supply-contracts with customers to provide beef products and/or cattle byproducts over several months. Supply contracts can reduce sales costs and help the cooperative remain more competitive with existing firms.

To compete effectively for fed cattle, cattle feeders will likely have to commit their fed cattle to the cooperative to generate sufficient volume for the cooperative to operate efficiently. The cooperative should consider using marketing agreements that specify that all or nearly all fed cattle controlled by member-feeders will be marketed through the cooperative. In this way, procurement costs can be reduced, and the cooperative can secure cattle with lower procurement costs. The cooperative will still have to purchase cattle from other cattle feeders, however. In our hypothetical Region X, even if a new cooperative successfully recruited all cattle feed-

ers as members, it would only market about 250,000 cattle annually. Most large meatpacking plants in 1990 slaughtered about 750,000 or more cattle annually. Thus, two-thirds or more of the fed cattle needed by the cooperative must be purchased from feeders who are currently marketing cattle to the five packers in our example.

How a new meatpacking cooperative effectively enters the market for beef products and cattle byproducts is even more difficult. A new firm will not likely produce the same quality of products initially as established meatpackers. Consequently, a new cooperative may have to significantly discount prices for its products to penetrate existing customer-supplier relationships. Such price discounts will likely mean unprofitable operations for some period until product quality can be improved, customer confidence secured, and prices raised to competitive levels consistent with customer services. A new cooperative must budget for startup costs and unprofitable operations for some period, which requires increased capital requirements.

A new plant requires a substantial labor force. Wages and salaries comprise nearly half of the operating costs for large packers.²² While some meatpacking activities require relatively low skills, some skilled labor is required. If an area selected for a plant has high unemployment, perhaps adequate competitively priced labor, and possibly other cost-reducing State or local government incentives, would be available. However, unless an adequate pool of trained labor is available, the cooperative must attract employees from existing firms or from other geographic areas by paying higher wages than competing employers. The higher the labor wage rate, the higher operating costs will be, also putting pressure on meatpacking margins. Reasonably high wage rates will attract many workers to meatpacking plants. Many workers, however, will find

²² American Meat Institute, Annual Financial Review of the Meatpacking Industry. Washington, D.C., 1985.

meatpacking jobs unpleasant or dissatisfying and will not stay long. Labor turnover and training will significantly add to the startup costs for a new plant.

New meatpacking plants also must comply with myriad Government regulations. A few examples of agencies that regulate meatpackers to varying degrees include the Environmental Protection Agency (EPA), Occupational Health and Safety Administration (OSHA), Food Safety and Inspection Service (FSIS), Agricultural Marketing Service (AMS), and Packers and Stockyards Administration (P&SA).

Significant capital will be required to finance each new large slaughtering and fabricating plant. A 1-million-head-per-year plant could cost \$70 million or more. Cattle feeders can expect to invest some amount per head in advance of the plant being built, based on the number of fed cattle expected to be sold to the plant, and some amount per head to pay off the significant debt required to build and operate the cooperative. The higher the initial equity capital investment, the less burdensome will be the debt load. Cattle feeders will have to anticipate, however, a substantial return on their investment to justify the investment cost, given the risk associated with operating meatpacking plants. Access to low-interest capital may have to be found to ensure financial success of the cooperative.

An alternative to building a new meatpacking plant is to purchase an existing meatpacking plant or firm. Purchasing existing slaughtering and fabricating capacity rather than building it has both advantages and disadvantages. The primary advantages are in market penetration. If an existing plant is operating, it has a management team, labor force, feedlot-suppliers from which it purchases fed cattle, and regular customers to whom it markets beef products and byproducts. Several aspects of market penetration may be easier than starting from scratch.

But there may be significant disadvantages. Cattle feeders considering purchasing an existing firm must always ask why the existing firm is selling the plant. Maybe the plant is not well managed, not well located, not cost-competitive, has poor

employee relations and low-quality production, cannot secure adequate supplies of fed cattle, or does not have a cadre of satisfied customers. Some problems may be addressed with new management, but some problems may be inherent in the plant. The cooperative may simply be purchasing existing problems for which there are no satisfactory solutions.

If the existing plant is idle, several of the same questions as to why it closed must be asked. In addition, an idle plant has some of the same market penetration problems associated with it as does a new plant. On the positive side, an idle plant may be purchased for considerably less than the cost of building a new plant. Even with extensive remodeling, the existing plant may offer significant capital investment savings, if related problems are not inherited.

Finally, custom slaughtering and fabricating are options worth exploring. As with a closed plant or one for sale, cattle feeders must ask why an existing firm would consider custom slaughtering and fabricating for a group of cattle feeders rather than slaughtering and fabricating for itself. There may be reasons why a custom-processing arrangement could benefit both the existing meatpacking firm and a new cooperative. The existing firm would only concentrate on plant operations such as slaughtering, fabricating, and byproducts processing, and not be concerned with cattle procurement or product sales. The custom arrangement would stabilize income flow and reduce price risk to the custom processor.

The cooperative could potentially benefit by acquiring control of product without investing large amounts of capital for a processing facility. Cattle feeder-members could market cattle to the custom plant, and the cooperative could market beef products and byproducts. Investment capital requirements would be considerably lower than building or purchasing a plant, though operating costs (custom fees) may be higher unless the custom plant is cost-competitive with existing firms.

A custom-slaughtering and fabricating arrangement with an existing meatpacker would also ease market penetration

problems, as was discussed for purchase of an existing meat-packer. One disadvantage would be convincing beef product and byproduct customers that they could continue purchasing the same consistent-quality products from the cooperative that they had previously purchased from the existing meat-packer. A good working arrangement with the cooperative and custom operator could ease that potential problem.

Niche-Market Cooperatives - Not all meatpacking operations serve the same market segments or customer groups. Cattle feeders may not have to enter the meatpacking industry on a large-volume scale to be successful. Cattle feeders may find a small target market or niche market to serve and effectively improve their marketing position.

Markets can be segmented or targeted in various ways. Most could be categorized into two broad groups: (1) products; and (2) services. Either of these may have geographic market opportunities or limitations as well. Several specialized product niches can be mentioned. Among them are slaughtering and/or processing cattle that larger meatpacking plants might prefer not to handle. Examples include (1) Holstein cattle; (2) cattle for the Certified Angus Beef program; (3) Prime quality grade, Yield grade 4-5 cattle for export; and (4) cows and bulls, among other types of cattle.

A broad range of specialized products and services includes (1) food service or portion-controlled products; (2) religious slaughter and processing; (3) products for Government purchase programs, such as school lunch and defense; (4) cooked and pre-cooked products for frozen food vendors; (5) private label retail products; (6) products exclusively for export markets; (7) custom services (such as store-door and small-lot deliveries) for local or small ethnic markets; (8) custom slaughtering and processing to others' specifications; and (9) "natural" beef or other products targeted to health-conscious consumers.

First, a niche-market cooperative must identify one or more target or niche market segments. Cattle feeders considering a niche market must ask why other firms have not identi-

fied the same niche and pursued the business venture. Again, there may be reasons why other firms have chosen not to venture into the seemingly untapped niche market. If so, cattle feeders must evaluate whether or not those economic obstacles can be overcome with a new cooperative.

A niche-market cooperative may organize in a manner that enables it to explore several niche-market alternatives. Innovation coupled with careful study may uncover several opportunities. In some cases, unique physical facilities may be required. Much of the discussion about building or buying a large-volume meatpacking plant applies to niche-market cooperatives, but on a smaller scale. As indicated earlier, a niche-market cooperative, while concerned about procurement and processing costs, may need to devote comparatively more resources to product and market development, customer service, promotion and advertising, and product distribution than a high-volume cooperative.

Capital investment in a niche-market cooperative may be significantly less than a large-volume cooperative because of the smaller size of facilities and overall operation. Significant capital will still be required, however, for product development and market development activities. Equity capital requirements may be less than for a high-volume cooperative, but operating capital requirements may be as much or more for a niche-market cooperative. There will also be considerable risk in penetrating untapped market niches.

Organizational Structure and Operating Costs

Providing guidelines for organizing and operating an integrated cattle feeding-meatpacking cooperative is difficult. Successful models are few, and the costs of organizing and operating an integrated cattle feeding-meatpacking cooperative depend on many factors, including (1) type of integrated cooperative; (2) size of the cooperative; and (3) organization of the cooperative, whether new or formed from an existing organization. Few guidelines are possible without having some specifics concerning these three factors. In general, a

cooperative organized to be a yardstick for comparison with noncooperative meatpackers (i.e., a high-volume cooperative) will require more investment capital than a niche-market cooperative. Extensive capital needs also will accrue with a niche-market cooperative as it pursues innovative or high-risk product development and market development activities. More capital, more membership recruitment, and more time and effort will likely be required to organize a new cooperative than to modify an existing cooperative.

Advantages/Disadvantages of Integrated Cooperatives

Both alternatives for vertically integrating into meatpacking offer producers several potential benefits. Each can guarantee cattle feeders located in the cooperative's normal supply area access to a market for their fed cattle. Cattle feeders would also retain ownership of beef products and byproducts through the wholesale market stage. Thus, cattle feeders would be positioned to participate in potential profits generated from slaughtering, fabricating, and marketing value-added products.

If the present meatpacking industry is not as competitive as possible in fed cattle procurement, cooperative meatpacking would inject additional competition into the market for fed cattle, especially the high-volume cooperative alternative. The result could be higher prices paid for fed cattle.

Potentially, cattle feeder-suppliers of the cooperative would benefit as well as other cattle feeders. By being in the meatpacking business, a cooperative could provide a yardstick against which to measure performance of large proprietary meatpackers.

A cooperative meatpacker could benefit cattle feeders significantly by increasing the flow of information back to its cattle feeder-members. Cattle feeders need to know the quality and quantity of beef their cattle produce and how their cattle and feeding regimes measure up to a "standard" or "desired" animal. A meatpacking cooperative would be in a unique position to provide this needed information to its cattle feeder-members. Perhaps a cooperative could more quickly

and efficiently move the industry toward value-based marketing and pricing than under the current market structure, since the cooperative's primary purpose is serving its members' best interests.

Vertical integration, however, is not a panacea.

Implementing a vertically integrated cooperative is not without problems. One of the most serious anticipated problems is cattle feeder commitment, which is a three-pronged problem, consisting of cattle commitment, capital commitment, and time commitment.

Cattle feeder-members would likely have to sign marketing agreements, which limit them to marketing fed cattle solely through the cooperative. Without such commitment of volume, the cooperative will experience higher procurement costs. Insufficient volume also may result in the cooperative's not being cost-competitive with existing firms in slaughtering and fabricating. Insufficient volume could potentially restrict the cooperative in guaranteeing customers the volume and quality of products needed to adequately penetrate markets and retain customers.

As was mentioned, organizing an integrated cooperative will likely require a significant capital commitment by cattle feeder-members. Persuading cattle feeders to invest in a new cooperative that will engage in a high-risk activity will be difficult. A competitive return on investment may be difficult to estimate and impossible to guarantee. Imputing a value for market access, innovation, or progressiveness is difficult. Some of these difficult-to-quantify objectives may be why the cooperative should be organized.

Finally, significant amounts of time and effort must be forthcoming by a leadership group within the larger group of cattle feeders interested in forming an integrated cooperative. Time will be required to develop the organizational structure, formulate the bylaws and articles of incorporation, raise capital, recruit members, and hire management to carry out members' objectives. Subsequent time will be required to serve on

committees and the cooperative's governing body, the board of directors.

Vertical integration by cattle feeders into meatpacking offers potential opportunities along with assured risks. Perhaps the single most important factor affecting the success or failure of such a venture is understanding clearly the objectives of the new cooperative. Having unclear objectives or attempting to persuade cattle feeders to organize a cooperative to achieve divergent objectives will most likely doom the initiative from the outset. Clear specific objectives are a must for the cooperative to have a reasonable chance of succeeding.

Integration into meatpacking is often thought by producers to be the answer to their market access and buyer competition problems. Meatpacking cooperatives, however, historically have not enjoyed much success. Legitimate opportunities may exist, but cattle feeders must carefully study the feasibility of such a venture.

CONCLUDING REMARKS

Three broad types of alternative fed cattle marketing cooperatives were discussed in this report. Each could benefit cattle feeders under certain circumstances, and each could fail under certain circumstances. Sexton and Iskow studied 61 relatively newly organized cooperatives. From that study, they identified "ten steps to success" for emerging cooperatives.²³ The following draws heavily from their ten steps.

1. Analyze market conditions with a keen understanding of what a cooperative can and cannot do. What is the problem or are the problems which a cooperative can realistically reduce or resolve? Identify clearly the objectives of the cooperative. Specify the realistic benefits stemming from the cooper-

²³ Richard Sexton and Julie Iskow, Factors Critical to the Success or Failure of Emerging Agricultural Cooperatives. University of California, Giannini Foundation Information Series 88-3, June 1988.

ative. This requirement relates directly to steps 1-4 discussed in this report.

2. Conduct a feasibility study questioning whether sufficient membership, business volume, and equity capital can be obtained to realize the expected benefits of forming a cooperative. Develop a business development plan for the entire venture. What are pros and cons for each alternative type of marketing cooperative, given the objectives of the new cooperative? This requirement involves steps 5-9 discussed in this report.

3. Organize the cooperative to maximize membership size. To achieve this, be flexible regarding financial commitments and voting procedure. Organize the cooperative in a manner which ensures commitment by members, i.e., cattle, capital, and time commitment. To accomplish this, use **long-term** member contracts with stiff penalties for violations.

4. Estimate carefully the cooperative's business volume and plan capital facilities that will efficiently handle that volume. Consider remodelling existing facilities and purchasing used equipment before investing in new plant and equipment.

5. Hire full-time professional management to operate the cooperative whenever possible. Consider part-time management, however, if insufficient volume is expected for a **cost-effective** full-time operation.

6. Finance initial capital requirements and generate a sufficient equity capital base by using flexible membership fees and grants (if possible).

7. Develop a plan to refund retained equities to members.

8. Establish pricing policies consistent with the cooperatives' objectives.

9. Consider carefully membership policies, especially open versus closed membership and accepting or not accepting nonmember business.

10. Identify and capitalize on the relative strengths of the cooperative. Work to overcome the relative weaknesses of the cooperative.

These 10 steps are appropriate to developing nearly any cooperative. Step 1 is critical to success. Cattle feeders interested in exploring marketing cooperative alternatives for fed cattle must understand what they can realistically accomplish via a cooperative. By organizing a cooperative, cattle feeders are attempting to alter the existing market structure in some way. While they must understand the economic reasons which may favor their cooperative's success, they must also understand the economic reasons which may be working against successfully organizing a fed cattle marketing cooperative. Once those reasons are identified and a plan developed to overcome them, the probability of success for a fed cattle marketing cooperative will increase.

**U.S. Department of Agriculture
Agricultural Cooperative Service**

P.O. Box 96576

Washington, D.C. 20090-6576

Agricultural Cooperative Service (ACS) provides research, management, and educational assistance to cooperatives to strengthen the economic position of farmers and other rural residents. It works directly with cooperative leaders and Federal and State agencies to improve organization, leadership, and operation of cooperatives and to give guidance to further development.

The agency (1) helps farmers and other rural residents develop cooperatives to obtain supplies and services at lower cost and to get better prices for products they sell; (2) advises rural residents on developing existing resources through cooperative action to enhance rural living; (3) helps cooperatives improve services and operating efficiency; (4) informs members, directors, employees, and the public on how cooperatives work and benefit their members and their communities; and (5) encourages international cooperative programs.

ACS publishes research and educational materials and issues *Farmer Cooperatives* magazine. All programs and activities are conducted on a nondiscriminatory basis, without regard to race, creed, color, sex, age, marital status, handicap, or national origin.