

Vertical Coordination in the Pork and Broiler Industries

Implications for Pork and Chicken Products

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Introduction

The U.S. broiler (or young chicken) industry was the last of the poultry (for example, turkeys) and egg industries to develop, but now surpasses beef as the leader in meat production. After World War II, the broiler industry grew into one of the most integrated of U.S. agricultural industries. Today, integrators produce nearly all broilers under contract with growers. Per capita consumption of broilers in the United States increased more than 100-fold, from 0.7 pound in 1935 to 72 pounds in 1997, surpassing beef consumption for the first time in 1993.

The industrialization of the U.S. pork industry, currently under way, is also characterized by major changes in structure and organization, including changing methods of vertical coordination. Contracts and, to a lesser extent, vertical integration are replacing hog purchases on the open market. Approximately 40 percent of hog sales to packers were coordinated by contracts and integrated operations in 1998, compared with 11 percent in 1993 and only 3 percent in 1980.

Past studies of organizational changes in the pork industry have focused solely on the pork industry or have been largely descriptive in nature (for example, Rhodes; Hurt; Hyk). Few studies provided a comprehensive comparison of changing coordination in the pork and broiler industries. Yet, there are many similarities between current changes in the pork industry and past developments in the broiler industry. For

example, contracting and vertical integration in both industries have been associated with new technology and new areas of production.

What can be gained by comparing vertical coordination in the pork and broiler industries? For one thing, such information can be used by policymakers to facilitate decisions regarding antitrust matters. Major changes in coordinating arrangements in the broiler industry occurred years ago. If similar incentives exist for contracting and integration in the pork industry, we might expect their effects to be similar as well.

Efficiency-improving policies can be better formulated if firm behavior and factors influencing decision-making are better understood. In addition, useful input into current policy decisions in the pork industry may be gained by revisiting policymakers' response to changing coordinating arrangements in the broiler industry.

The major objective of this report is to compare, using transaction cost economics and other theories of firm organization, current changes in vertical coordination in the U.S. pork industry with past changes in the U.S. broiler industry. This comparison can be used to obtain a better perspective of the reasons for current changes in the pork industry and their potential effects. In the process, this report also examines the relationship between increased vertical coordination, retail prices, and market adjustments in response to consumer preferences for convenient, high-quality products.