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Vertical Communication: The Aligning of Beef Industry Segments

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INTRODUCTION

Relative to competing proteins, the beef industry has lagged in its ability to integrate productions segments. The inherent nature of protein production from ruminants dictates that some obstacles to vertical integration in the beef industry are relatively permanent in nature. Simply the vast differences in environments across the country and the way seedstock producers, cow-calf producers, backgrounders and feedyards respond by implementing more localized production and management practices creates a setting where "one-size-fits-all" is virtually impossible. True vertical integration requires control from start to finish. Control from start to finish of production and marketing occurs most readily with complete ownership. This gives the ability to make quick, serious and lasting changes in either or both. Without complete ownership, the look of vertical integration can be achieved through means such as relationships, partnering, alliances, coordination or communication to name a few. Because control is hard to achieve without complete ownership and ownership is too capital intensive, the beef industry generally remains quite segmented. This is especially true when expressed on a sheer numbers or volume basis. Two traditions in the beef industry, namely independence and trust are seriously tested when approaches to vertically integrate without complete ownership are implemented. Still, relative to just 10 years ago, the industry has changed remarkably in it's attempt to create the efficiencies of vertical integration while still recognizing the limitations imposed by the inherent nature of the industry. The Strategic Alliances Demonstration Study conducted by NCBA in 1992 served as the definitive impetus for the industry to explore and create relationships and alliances that acted like a vertically integrated industry. Change in the beef industry is nothing new. However, change at the pace we are experiencing it today coupled with impact on the core "look" of the industry is almost impossible to grasp. Who in the beef industry, 10 years ago wold have predicted:

1. The largest poultry integrator is also the largest beef packer.
2. The largest pork integrator has become a major player in the beef industry with recent and imminent acquisitions potentially moving them to the second largest beef packer.
3. Virtually every major packing company and branded beef program offers a value-based system to purchase cattle.
4. Carcass data is the norm rather than the exception for cattle sold on a dressed basis.

VERTICAL INTEGRATION – ENHANCED PRODUCTION AND MARKETING

Whether termed communication, coordination, alignment, relationships or alliances, the end result is to create an industry that sees the benefits of vertical integration without complete ownership. Two distinct benefits result from vertical integration. First, production efficiency is increased as a result of better communication among the production segments, less duplication of costs and more efficient use of resources to optimize production. Second, control throughout production greatly enhances marketing power to the consumer by ultimately guaranteeing source, specific production and management practices, food safety and eating quality.

EVOLUTION INTO INTER-RELATED ENTITIES

Historically, the view of vertical integration in the beef industry has been one-dimensional with information flowing to and from each distinct segment. For example, seedstock producers communicate with cow/calf producers, cow/calf producers communicate with backgrounders and feedyards, and feedyards communicate with packers. In reality, each segment is evolving into a dynamic entity that has relationships throughout the industry. The model has networked into multi-dimensional relationships with coordination within and among segments simultaneously. For example, multiple seedstock producers with like genetics and goals join forces to create a larger seedstock entity. Cow-calf producers have pooled resources to gain market access and power with greater numbers of cattle to increased uniformity. This cooperation also gives them the power to decrease input costs by eliminating duplication (sharing resources) and procurement of inputs in greater quantities at lower costs. Feedyards have found benefit in marketing power with greater numbers and in procurement of inputs in larger quantities. Finally, there are many non-production entities such as breed or cattlemen’s associations, pharmaceutical or feed companies, livestock identifications systems, branded beef companies, retailers or even private individuals that provide a venue to link some or all industry segments. These “supply networks” then have the ability to vertically integrate and provide an efficient, wholesome and safe product to the consumer. Arguably, the most encompassing are specific, branded companies that have a marketing niche to create, sustain and expand. These companies tend to be highly consumer driven and thus facilitate an avenue for cattle to be created, managed and harvested under very precise specifications that reward production that most closely matches consumer demand.

HORIZONTAL INTEGRATION TO FACILITATE VERTICAL INTEGRATION

In many cases, as great of a challenge lies within industry segments as does among them. Because of the generally extensive nature of production of cattle, production and management practices, genetics and overall profitability are extremely varied across environments. Greatest in the cow-calf sector, the differences that exist are enormous when compared to pork and poultry production. Because the West, the High Plains, the humid Southeast or the Midwest cornbelt are so different, they require different genetics and production/management practices to optimize production and maximize profit. Integration horizontally within this segment has the potential to enhance uniformity and consistency in the industry but has to be done with overall efficiency in mind. Because of these limitations, uniformity of product may better be realized post-mortem as opposed to ante-mortem. The swift move to case-ready, precooked or complete meal products has lent credence to the view that production of highly efficient, low cost, high retail product cattle will be the mainstay of the industry in the future. Others contrast this view with one of a high quality, uniform, guaranteed product that the consumer views as an event, not just a food staple. Still, the predictions of 100+ breeds becoming less than 10 have not materialized and the disparity remains. The seedstock industry has embraced horizontal coordination to a high degree through their respective breed associations and Beef Improvement Federation. Standardization of genetic parameters, benchmarking production results and economic analysis of traits selection have become commonplace among progressive genetic suppliers and serve to attenuate the environmental variation across the country. Further horizontal coordination within the feeding and packing industry in areas such as automated individual identification, standardized performance analysis and objective end product assessment of quantity and quality would greatly speed up the move toward vertical integration in the entire industry.

SEGMENT FITNESS FOR VERTICAL INTEGRATION

As has been discussed, each segment in the beef industry already has some degree of integration occurring within that segment. The cow-calf segment is undoubtedly the most loosely coordinated and least fit for vertical integration given the wide array of environments across the country. However, seedstock production, cattle feeding and beef packing can potentially do much more to standardize and integrate their segments to increase production efficiency and garner marketing power to the consumer. The industry may best be served by a diverse but efficient cow herd that maximizes production in "marginal" areas of the country that are well suited for grazing cattle. Further, like genetics, similar feeding and management programs and a uniform packing industry that utilizes objective measures of product quantity and quality would create a consistent, uniform, safe and wholesome end product for the consumer.

LAURA'S LEAN BEEF – A SUSTAINABLE APPROACH TO MEET CONSUMER DEMANDS

Laura's Lean Beef founder Laura Freeman and partner John Tobe, former CEO of Long John Silvers, have developed a branded beef market that is unique in the industry. The focus of the company is without question the consumer. Consumer demand for a lean, healthy, tender, all-natural beef product dictates what Laura's Lean Beef does day to day. A supply network of producers with the right type of cattle and the ability to produce those cattle without added growth hormones or antibiotics is our starting point. From there, Laura's Lean Beef facilitates the movement of those cattle through the production chain with contractual agreements and a value based grid for finishers and cow-calf producers alike. The focus of the supply network is to work with family farm and producers practicing sustainable agriculture practices. Laura's Lean Beef markets lean, all natural beef and to achieve this, cattle must be Exotic or Exotic cross (Limousin, Charolais, Gelbvieh, Simmental, etc.) and raised without growth hormones or antibiotics. Producers are able to receive a premium to market and receive forward contract cattle. All cattle are purchased on a value-based grid based on carcass merit. Both a finisher bonus and a cow-calf bonus are paid and individual carcass information provided free of charge. This carcass information can be tied back to the home or ranch tag and identity preserved. Finally, Laura's Lean Beef is aggressive regarding implementation of new technologies such as vitamin B feeding, instrument grading, aggressive vaccination programs, castration at weaning or later with banding and deterring genetic differences in tenderness. These factors all contribute to creating a sustainable, integrated supply network to meet consumer demand.