

The Effect of BSE on Market Power

IN THE ALBERTA RED MEAT PACKING INDUSTRY

PROJECT TITLE Market Power in the Alberta Red Meat Packing Industry

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In May 2003, North America's first case of Bovine Spongiform Encephalopathy (BSE or "mad cow disease") was diagnosed in a cow born and raised in Canada. As was standard practice at the time, countries that did not have a diagnosed case of BSE closed their borders to exports of Canadian live cattle and beef. This included the United States, Canada's largest export market (the U.S. announced its first case of BSE in a U.S.-born animal in June 2005).

In September 2003 the U.S. reopened its border to Canadian boneless beef from cattle under 30 months (UTM) of age. This meant that finished beef (the vast majority of which comes from cattle that are under 30 months) could be exported, but live cattle could not. Prior to the closure of the U.S. market Canada had been exporting approximately 14,000 head of fed/finished cattle each week to the U.S. With the border closure, these animals would have to be slaughtered in Canada, with the beef exported to the U.S.

Concern arose over the market power (ability to dictate prices for live cattle) that this would give the Canadian packing industry. This study was commissioned to investigate how much market power the Canadian packing industry was exercising. Because feedlot data was only available for Alberta,



the study only examined market power in Alberta. Three of Canada's largest beef packing plants (Cargill, Tyson Foods/Lakeside and XL Foods) are also located in Alberta.

Prior to May 2003, Alberta feedlot operators had the option of marketing their fed cattle for slaughter in Alberta or exporting them to the U.S. This integration of the U.S. and Alberta markets limited the market

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power of Alberta packers because Alberta feedlots could sell to U.S. buyers if Alberta packers exercised market power and reduced the price they would pay for fed cattle. Prior to May 2003, the average Alberta price for fed cattle was less than the U.S. price, but the two prices were highly correlated and moved together.

When the border closed completely to beef and live cattle in May 2003, Alberta fed steer prices declined dramatically while U.S. fed steer prices saw a sharp increase. When the border reopened to UTM beef but remained closed to live cattle, Alberta fed steer prices increased but no longer moved in correlation with U.S. prices. The markets were no longer integrated. Thus, the fed steer market was altered post-BSE with the separation of the Alberta and U.S. markets. The

packers exercised their potential market power. The results indicated that during the time that the U.S. border was open to UTM beef but closed to live cattle, the packers could have exercised market power but did not do so to any significant level. The



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level of market power did increase slightly but the researchers believed that the range of margins was reasonable during that time period. Prices were not consistent with the coordinated exercise of market power and indicated that the actual behaviour by the Alberta packing industry was more competitive than might have been expected.

competitive conditions for fed cattle in Alberta had changed resulting in a market structure conducive to the exercise of market power by packers in Alberta. The study then measured the extent to which Alberta

This study provides valuable insight into the functioning of the Canadian cattle market during one of the most volatile periods of its history. The U.S. border reopened to live Canadian cattle in July 2005 and since that time the U.S. and Canadian markets have once again become integrated, although not to the same extent as they were prior to BSE.

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