The Changing Structure of Agriculture: Implications for Bargaining

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The structure, conduct and performance of American agriculture are rapidly changing.

This is easily seen in the agribusiness sector where firms are becoming much larger and more industrialized, causing industries to become more concentrated.

This change in the agribusiness sector's structure is being driven partly by economies of scale.

The location-specific nature of agricultural production is likely to prevent that sector from becoming as concentrated as the agribusiness sector.

Thus, the current imbalance in the bargaining positions of commodity sellers and buyers is expected to get worse in the future.

Vertical Coordination is Increasing

- Vertical coordination refers to the synchronization of successive stages of production and marketing, with respect to quantity, quality, and timing of product flows.

- Vertical coordination is part of industrialization – it lowers costs

Methods of Vertical Coordination Along the Spectrum of Control

Control offered to contractor or integrator

Least			Most
Open production	Marketing contract	Production contract	Vertical integration

Contracting is Expanding

The overall share of U.S. agricultural production under contract was

- 12% in 1969
- 29% in 1991
- 39% in 2003

Marketing Contracts

In 2003 the share of U.S. production under marketing contracts was

- 29.7% of total crop value
- 13.7% of total livestock value

Production Contracts

In 2003 the share of U.S. production under production contracts was

- 1.1% of total crop value
- 33.7% of total livestock value

Producer Motives for Production Contracting

In 1963 a study found four reasons to contract:

- To increase efficiency
- To obtain (or reduce the cost of) financing
- To reduce uncertainty
- To gain market advantage

Producer Motives for Production Contracting

In 2005 a study found two most common reasons to contract:

- Risk management
- Minimization of production and/or transaction costs

Bargaining Power Increases Profit Margins

- Power is present in markets with unbalanced supply and demand
- Agriculture's current structure leads to unbalanced markets
- Economies of scale lead to industry concentration
- The agribusiness sector is becoming more concentrated

Food Manufacturing Industry Concentration

Commodity	*CR4 1987*	*CR4 1992*	*CR4 1997*	*CR4 2002*
	%	*%*	*%*	*%*
Broilers	29	34	56	54
Hogs	20	25	64	68
Cattle	39	50	84	86
Dairy	21	22	21	30
Soybeans	71	71	75	95
Corn	74	73	80	69
Wheat	44	56	62	49
Oats	27	33	64	70
Barley	19	23	46	87
Rice	41	51	69	57
Cotton	18	19	20	26
Sugar beets	83	85	85	85

Production Contracts Thin Spot Markets

As production contracting becomes more common in a commodity market:

- Fewer transactions occur “in the open”
- Access to buyers is more difficult for producers not contracting (transaction costs increase)

Remaining producers may be forced to contract

Financial Effects?

Contracting has led to mixed results across commodity markets:

- Some producers have higher annual sales
- Variability of sales over time may decrease (reduced risk)
- Commodity specialization raises household income risk
- Profit margins and levels may be lower

Implications for Bargaining

- Production contracts lead to specialization
- A commodity's physical attributes influence the potential for industrialization
- Buyer bargaining power increases with industrialization
- Local/regional commodity industries (like CA's fruit and vegetable markets) are most likely to experience increased use of production contracts because of limited number of buyers (concentrated buying power), thus creating incentives for cooperative, concentrated selling arrangements

Implications for Bargaining

- Research has shown that producers prefer autonomy, thus they will resist delegating power to a bargaining group
- So, the bargaining power of a group must be demonstrated to potential members
- What benefits can a bargaining group offer to members?