



# Cattle Markets, Price Discovery, and Emerging Issues

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## Market Reporting and Transparency

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### **Overview**

The reliable reporting of trusted market data is critical for cattle market participants. Market price levels, especially as they relate to other markets, are the key driver of resource allocation and price discovery. This process can be hindered if available market information is limited or irregular. Without regular price reporting in which participants are confident, the dynamic process of cattle buyers and sellers discovering the market-clearing price would be subject to inefficiency. Market reporting alone is not price discovery; however, it certainly contributes to the price discovery process.

Regular and reliable reporting of live cattle transactions provides a more transparent view of supply and demand conditions than would be possible without it. Publicly reporting market transactions increases the information available to all participants. Live cattle market reporting is generally a public good in that everyone can consume it, and any one participant's use of it does not exclude others from using it. A primary motivation for government involvement in collecting and disseminating this information is that the private sector would be unlikely to provide these data at a socially optimal level.

Market information available to everyone can improve market efficiency and help markets more quickly reach the market clearing price (C-FARE, 2013). Market participants generally look to public sources of data for information because they have confidence the data are reliable, complete, and free of any manipulation. Seminal research in this area has shown that when market participants possess incomplete information, price dispersion can occur (Stigler, 1961) – that is, prices are more variable. Reductions in public cash market information have also been found to increase price variance and decrease production efficiency (Anderson et al., 1998). So, the regular and reliable provision of price data perceived by market participants as credible and accurate can speed up market convergence, which is the process by which prices gravitate to an equilibrium level.

Publicly-reported market information can also reduce uncertainty. The C-FARE 2013 publication noted that many agricultural producers and processors are risk averse. For a risk averse participant, increased uncertainty tends to lead to lower output than the competitive level (Newberry and Stiglitz, 1981). Boyer and Brorsen (2013) showed that cattle sellers benefit from publicly available data because it reduces price uncertainty. This reduction in uncertainty led to reduced bid shading and more competitive bidding from buyers.

There are many motivations for the collection and public dissemination of market data for agricultural markets, including live cattle markets.

### ***Summary of Reporting and Transparency Issues***

Market reporting is crucial to the price discovery process. It is, therefore, important that an effective reporting system remain in place. Reliable and transparent price reporting may not be a sufficient condition for desirable market qualities, but in most all cases, it is a necessary condition. Most of the present issues surrounding price discovery are not new, and calls for action to improve price discovery have previously occurred with varying degrees of intensity. It was producer and producer group concerns, in the name of improving price discovery, that led to producer support for the mandatory price reporting system that is in place today. It is easy to take the market reporting system for granted, but to do so is to risk losing a key element for efficient markets. Required Livestock Mandatory Reporting (LMR) reauthorization keeps this issue on the forefront about every five years. LMR provides much of the data to allow for informed discussions about price discovery to occur.

Second, one must also understand what can realistically be expected from LMR. While a lot of the issues of concern today are not new, the current setting of increased concern of live cattle marketing issues is different from past decades because of the presence of LMR data. In particular, LMR data on transaction type was not available under the voluntary framework prior to LMR. Many of the current proposals focus on these data and would rely on them for regulation. It is crucial to recognize that while these transaction types are informative, they were not designed to support a regulatory framework. LMR is a reporting tool and cannot be expected to deal with many of the issues that are often mentioned in pricing discussions such as market concentration, margins at different levels of the marketing chain, etc.

Third, opportunities likely do exist to improve the information made available through market reporting. One potential step toward increased transparency could be the development of a contract library for cattle, similar to the Swine Contract Library. Contract trades can take on many different forms, and a catalog of these contracts would increase transparency in the industry. While a contract library would not disclose contracts being offered by individual firms, or even whether a specific contract is available in a given region, informing the public about markets that formula prices are based upon, how formulas are calculated, premiums and discounts, and other contract provisions would provide a deeper understanding of formula trades than prices (either base or net) alone. Clearly the cost of developing the library should be weighed against the benefits of its existence, but benefits in the form of increased transparency would exist.

Fourth, confidentiality should be reviewed through the filter of the current market environment. Confidentiality requirements have been a concern for LMR since inception and these concerns will only increase as the cattle industry continues to evolve. It has been 20 years since reporting guidelines related to confidentiality were last revised, and marketing conditions have drastically changed during that time. A basic question that could be asked is simply if all trades are worthy of being reported, even if the potential exists for those prices to be linked back to an individual entity? Clearly, confidentiality concerns are less of an issue in more competitive markets.

Overall, the relaxation of confidentiality requirements, combined with a better understanding of contracts, has the potential to benefit price discovery. In a setting where all proposed prescriptions to improve price discovery likely exhibit increased costs and/or unintended consequences, relaxing confidentiality, and improving descriptions of formula/contract trades might lead to the largest net benefit as compared to other proposals. This is likely especially true for cattle producers who would benefit from better price discovery without absorbing the larger costs associated with other proposed prescriptions.

Finally, it is certain that technological advances will continue to impact all aspects of the cattle industry, including how cattle are marketed. Efforts exist to use online auctions for fed cattle which would allow buyers and sellers to observe the negotiation process and see posted prices. This may, in fact, illustrate the most important point of all: the cattle marketing system is continually evolving and LMR must continue to find a way to evolve if it is going to continue to provide the reliable and transparent data that is necessary for efficient markets.

### References

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