New Generation Cooperatives:
Case Study

U.S. Premium Beef

by Mary Holz-Clause

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The New Generation Cooperatives: *Case Studies* are made possible with support from the Illinois Council on Food and Agricultural Research (C-FAR) and the Illinois Institute for Rural Affairs (IIRA).

Published by Illinois Institute for Rural Affairs
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www.iira.org

A collection of ten case studies with an introduction is available from IIRA in print and on the IIRA web page.

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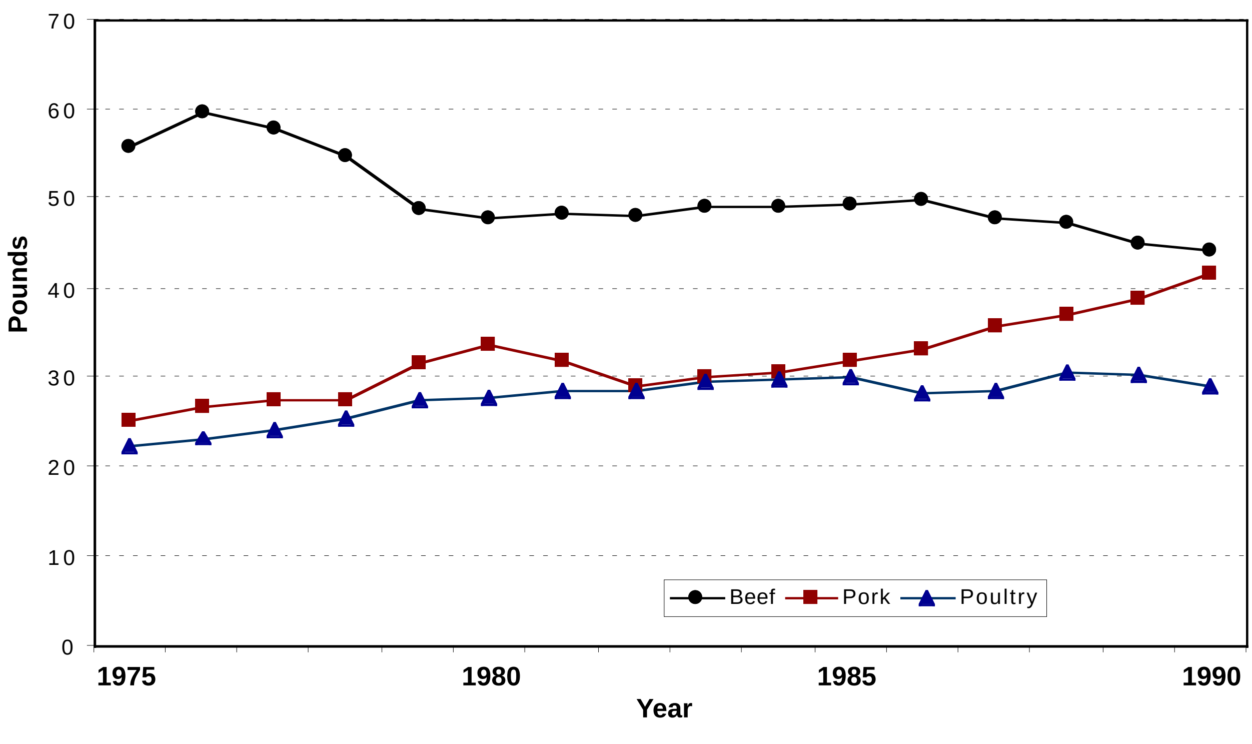
Background

The U.S. beef industry has spent the past 20 years realizing a constant and substantial loss of market share to other animal protein sources, especially poultry (see **Figure 1**). A lack of coordination has led to a roiling loss of direction in the industry. Information does not flow freely up and down the production chain. Change has been limited and has not been responsive to consumer markets. Price actions within the production chain are predatory, resulting in consolidation at all levels. Until recently, new product development was not a priority, and those products that emerged were niche products and not significant enough to affect market share trends.

Figure 1. Beef, Pork, and Poultry Per Capita Consumption



Source: U.S. Department of Agriculture 1997.

In the beef industry, three companies control 80 percent of the packing capacity. To date, these companies have been commodity/volume driven, merchandising meat and non-edible byproducts throughout the world. Branded labels have been a very rare product in this environment. Volatility of price and margins at all levels has led to consolidation and distrust along the production chain. Other competing industries, such as poultry, have integrated functions to enhance information flow and responsiveness to consumer markets. They have used the information to improve system efficiency at all levels, allowing cost to drop and volume to increase while maintaining margin.

The beef industry is harder to integrate because of its huge land and capital needs and because of the types of individuals that dominate it. Nearly one million beef producers breed 80 different kinds of cattle and send them to several hundred feedlots. The only thing ranchers and feeders have in common is a distrust for the packers, who often pay the same price for superior cattle as they do for the lower-quality kind (Conlin 1999, 76).

Many producers have reached a level of frustration, however, that makes them amenable to change. The industry is vast, and the products are popular. Even with the erosion of market share, beef and kindred products remain dominant in overall value for all agriculture. The industry has proven tough, emerging from two decades of health and safety scares and massive sophisticated competition to remain the largest protein industry segment.

How Cattle Are Sold

Throughout the first 60 years of the century, live cattle were delivered to terminal markets such as Chicago. Large commission firms at these locations handled the selling of the cattle to a packing company. This trade was on a price per hundredweight negotiated on the day of sale.

In 1960, a start-up company called Iowa Beef Processors (IBP) revolutionized the process by moving beef packing to the areas where the cattle were finished and breaking the carcasses into smaller cuts that fit into boxes. This approach cut freight costs, reduced the overhead of stockyard space, and improved some quality factors. IBP also put buyers in cars with two-way radios, eliminating the commission person from the selling process. The industry as a whole quickly followed suit and the central stockyards eventually disappeared.

In 1999, the majority of live cattle are sold on the cash market directly to a packing company. There is no middle person in this transaction, and the ownership of the cattle moves completely from the feeding entity to the packing entity. The majority of these transactions are based on only two factors: (1) the live weight of the animal minus a calculated shrink, usually four percent (the buyer takes quality into the bid consideration to a certain degree); and (2) the negotiated price per hundredweight—for example, a 1,250 pound steer minus 4 percent shrink times the live market price per hundredweight equals the amount paid to the feeder. This is known as selling live.

The second most common method of selling is to use a negotiated price for the hot carcass weight of the animal. This selling method places with the feeder the risk of the percent of the animal that actually ends up in a usable carcass (yield) at the packing plant. That risk can usually garner an extra return to the feeder unless the animals or his or her methods fall below average expectations. This method is known as selling “in the meat.”

Another method used with a significant percentage of the total cattle marketed is the grid or formula pricing method. This method uses a grid matrix of several value factors that represents premiums and discounts depending on how the animal dresses out in the packing plant. These factors include dressing percentage, lean meat cutability score, quality grade, fitting within the ideal weight range for the carcass, and other factors that might make the carcass fall outside desirable specifications for the packer. The grid matrix is built around a base price that is usually the “in the meat” price previously described. The actual cost of the animal is reconstructed or formulated on an individual basis according to how it performed in each of the categories.

Grid or formula pricing places the risk on the feeder. Animals will be discounted for realizing poor carcass specifications; however, the upside to this is if the cattle do perform above the average or norm. This method is an intermediate step toward value-based marketing. The ultimate extension into value-based pricing would be to take the various cuts of meat from the animals to their final sale and add those values backward to reconstruct the live value of the animal.

In a fully integrated system, the owners would have little interest in the live value of the animal because the margins to that business would be derived throughout the system and not through transactions at segmented points of sale. The beef industry has not achieved such integration, nor is it likely to happen very soon; however, the need for better system efficiency is driving change.

The lack of coordination or integration has meant information does not flow up or down the production/processing/marketing chain. Thus, market signals relative to quality factors or even supply are very poor. Furthermore, although the free market has worked efficiently over a long-term cyclical pattern, it has created the undue volatility and dislocation in the short run that arguably has led to consolidation. Remarkably, consolidation has not automatically led to better coordination of supply or quality. The lack of information or coordination has meant the supply chain is not responsive to end markets; therefore, a long-term loss of market share has occurred.

Significant numbers of cattle producers are trying to improve the long-term outlook for their industry. They almost universally understand that certain changes to marketing resulting in greater profitability will also result in a positive change to the industry’s competitiveness. It was in this context that U.S. Premium Beef was born.

Beginnings

U.S. Premium Beef (USPB) is deeply rooted in the cow-calf segment of the beef industry. USPB founders believed that working together and sharing information in a coordinated system could help them compete against others in the meat industry. “We could see that our industry needed to change in order to survive,” said Steve Hunt, one of the four Kansas cattlemen who started USPB and who is now the company’s chief executive officer. “We had focused so much energy on competing with each other, we had taken our eye off of the ball” (Gilmore 1999, 22).

Teaming with Hunt, a fourth-generation cattleman from Arkansas City with work experience in commercial banking and finance, were Terry Nelson, a commercial cow-calf producer, backgrounder, and cattle feeder from Long Island; Doug Laue, a custom backgrounder and cattle feeder from Council Grove; and Terry Ryan, a commercial cattle feeder from Scott City.

The group had collectively and individually tried to determine how to get more value from their animals. They first met in November 1995 to discuss the concept of forming a business. The group studied business structures and several successful agricultural co-ops, including Sunkist Oranges and Blue Diamond Almonds.

As the group continued its study, they decided if producers were to be committed to consumer-oriented beef, they also had to be committed to ownership in the structure. Thus, they proposed a marketing co-op in which members would be required to capitalize the co-op up-front rather than through earnings (Smith 1998, 9).

Thus, USPB was established on July 1, 1996. The producer-owned business elected a six-member board of directors, representing all the beef industry segments. The board membership was later increased to seven members.

The Mission

> *To increase the quality of beef and long-term profitability of cattle producers by creating a fully integrated producer-owned beef processing system that is a global supplier of high quality value-added beef products responsive to consumer desires.*

In early September 1996, the board members held meetings with livestock associations and media organizations to explain their concept of the information-based organization, which would provide feedback to the producers so that they could make changes desired by consumers in the marketplace. Five meetings were held with producers in Kansas. The road show was also taken to California, Colorado, Iowa, Missouri, Nebraska, Oklahoma, and South Dakota.

According to Hunt (Suther 1996, 68),

> As producers, we have watched ourselves selling on a commodity basis, all receiving a similar price, no matter the quality of our product. Yet we hear consumers say they are not totally satisfied with the product. It seems like the signal hasn't been transferred through the market, from consumer, to retailer, to purveyor, to processor, back to the producer, who could really make the difference.

Hunt indicated that through the co-op, members would obtain the 15-20 percent profit the processors currently get, and producers could impact quality sooner by culling cows to dispose of the outliers and sorting their better calves into the USPB program (Suther 1996, 68).

In its start-up phase, USPB faced several challenges. There was a lack of incentive to produce higher quality beef cattle. Mark Gardiner, an early participant, explained, "The economic signals have been blurred. It has been best to take a mismanaged animal that you buy cheap and upgrade him to average" (Merlo 1998, 19).

Another difficulty faced by the co-op was the problem of a "mature" market. With beef demand seemingly at its peak, fewer and fewer ranchers have entered the business. The average age of a U.S. rancher is 57 years old. According to Kelly Giles, a third generation Kansas rancher and investor in USPB,

> When you cannot bring in young people, that spells the end of an industry. In Clark County, Kansas where I live, I know of only 10 producers younger than age 40. When you're just ten years away from retirement, you're not willing to risk your neck on a new kind of investment (Merlo 1998, 21).

Despite the initial difficulties, however, within months, producers, representing more than 80,000 head of cattle, committed to financing a business plan. The business plan offered producers an opportunity by adding value through increased premiums for quality carcass characteristics. Total start-up costs were more than $1 million, which included funding for research, legal services, and administrative and system set-up costs.

The newly formed company embarked on a membership drive. Members could join with a lifetime membership fee of $500 plus a registration fee of $.50 per head of cattle that would be delivered to USPB. (The registration fee later was raised to $2 per head.)

Purchasing a Beef Plant

At the same time, USPB began to explore ways to enter the beef-processing segment. The board decided that control of a harvesting facility was necessary to complete this objective. The group analyzed a number of options, including building a new facility and custom-slaughtering cattle. In the end, they voted to partner with a successful existing company, Farmland National Beef (FNB), a subsidiary of Farmland Industries.

On July 31, 1997, USPB signed a letter of intent to purchase up to 50 percent of FNB. To make its purchase, USPB launched a stock offering at $55 per share and $38 million was raised. That offering closed in late November. On December 1, 1997, USPB became a part owner of FNB. The co-op initially bought about 25 percent of the stock. USPB matched the amount of stock raised with a loan from the Bank for Cooperatives (CoBank), located in Wichita, Kansas. In December 1997, USPB launched another stock offering, which closed a month later. With the new stock, USPB bought more shares of FNB, but will not disclose its total percentage of ownership.

FNB operates two plants in Dodge City and Liberal, Kansas. It is the fourth largest beef packer in the U.S. and processes 9 percent of all fed cattle in the country. The company markets boxed beef, Prime, and Certified Angus Beef domestically and internationally. In addition, FNB markets further-processed and value-added products, primarily portion-controlled steaks, to restaurants, mail order catalogs, and foodservice and retail customers through the Kansas City Steak Company, which it acquired in late 1997. FNB markets products under four branded labels: (1) Certified Angus Beef, (2) Farmland Black Angus Beef, (3) Farmland Certified Premium Beef, and (4) Kansas City Steak Company.

The key to USPB was the purchase of a processing facility, with associated branded products. Without a brand recognizable to consumers, the beef business doesn't have much going for it. In a good year, IBP, the biggest meatpacker, ekes out a 1.7 percent pretax margin. FNB's results last year were $43 million pretax net on sales of $2.2 billion; however, its sales of branded beef, at $100 million and growing 30 percent a year, exceed those of the three largest packers combined. The profit margins on Black Angus Beef are 20 percent higher than on no-name beef, FNB's CEO, John Miller said in a recent *Forbes* article (Conlin 1999, 76).

Like the poultry giant Tyson Foods, with its merchandising army, FNB tracks the beef all the way to grocery store shelves. Distribution is helped by the fact that FNB already has a national branded presence in pork. The FNB beef brands are displayed in their own refrigerated display cases to distinguish them from commodity meat. The branded beef products are now in 800 plus stores, including chains such as Jewel in Chicago, Lucky in California, and Acme Markets on the East Coast (Conlin 1999, 76). In addition to the domestic market, FNB has an aggressive sales force in Japan and Korea and had restructured its Mexico operations in 1998 to take advantage of expected market growth there.

USPB CEO Hunt (1999) indicated that "through Farmland National Beef (FNB), our system for the first time on a large scale, gave producers an opportunity to realize profit from the value gained through further processing beef all the way to consumers." According to Hunt in an interview for the *Angus Journal*, "By partnering with Farmland Industries in the ownership of FNB, USPB producers gained market access to the consumer through Farmland's name recognition and already successful labels. As a result, highly desirable products could be sold through branded beef labels" (Gilmore 1999, 23).

John Miller took over as FNB's CEO in 1992, after buying slaughterhouses and retrofitting them with state-of-the-art equipment. To capitalize the business, he used the cash from a family business (a meat packing business sold to ConAgra for $33 million in cash and stock), $25 million from Farmland Industries, and borrowed $74 million from banks (Conlin 1999, 76). According to Steve Kay, editor of *Cattle Buyers Weekly,* "John Miller's put together one of the most functionally integrated beef systems in the U.S. If the big three packers aren't looking over their shoulders, they should be" (76).

Types and Conditions of Membership

USPB has two types of membership: (1) lifetime and (2) associate. In addition, producers can lease shares from stockholders within the membership.

The lifetime associate membership fee for a stockholder is $500. A one-year associate membership fee costs $100. Individuals do not become voting members until they have purchased at least 100 shares of common stock in the co-op. Although membership common stock and delivery rights are transferable under certain conditions, membership in the co-op is not transferable. The co-op is not obligated to the member other than in its requirement to issue a membership certificate.

In addition to signing a membership application, the farmer/rancher seeking to be a stockholder signs a Uniform Delivery and Marketing Agreement and commits to deliver one head of cattle annually for each share of stock purchased. There is no refund of the membership fee, but the stock is transferable.

Two forms of delivery agreements are available:

1. An agreement for “even slots,” that is an even monthly delivery of the delivery commitment.
2. An agreement for “odd slots,” that is delivery of the delivery commitment during one or more specific monthly periods each year. For odd slots, the specific monthly delivery period(s) are to be selected by the designation and if overfilled, by an alternative selection procedure.

If a person cannot meet the delivery schedule due to weather or other factors, USPB works with the producer to deliver cattle when they will be ready for market. Although there is potential for seasonality of delivery because of the large geographic region USPB pulls from, they have been able to balance cattle deliveries to keep a consistent supply of cattle for their markets.

Associate members are not allowed to acquire shares of the common stock in the co-op or to become voting members in the co-op until they acquire at least 100 shares of membership common stock. The lifetime associate membership fee is $500. The one-year associate membership is $100. The lifetime associate membership fee is nonrefundable.

The co-op has the right to terminate membership if the member (1) fails to deliver cattle; (2) dies; (3) takes actions that will impede the co-op from accomplishing its purposes; or (4) takes or threatens actions that adversely affect the interests of the Co-op or its members (By-Laws 1997).

Although USPB’s stock offering was legally closed on January 23, 1998, there are several other ways in which interested producers can still participate in the company. Persons occasionally have shares they are willing to lease to other producers. Likewise, normal business attrition usually generates a limited amount of stock for sale from individual members. The company will help potential customers locate members with shares for lease or purchase.

Getting Started

On December 1, 1997, USPB started processing cattle. Its more than 690 members from 24 states delivered approximately 8,100 finished cattle each week through the end of 1998 to packing plants in Dodge City and Liberal, Kansas. Through April 1999, more than 600,000 cattle have been marketed through the USPB system. Since December 1997, premiums of more than $9 million have been paid compared with selling on the cash market.

Features of U.S. Premium Beef

USPB membership in has the following features:

- Lease or ownership of shares for members
- An opportunity to partner with feed yards or other members in retaining ownership of cattle
- No geographic restrictions on where members can do business (Members decide where the cattle will be fed. USPB cattle have been fed in more than 300 yards in 11 states.)

- Non-breed specific (except that cattle can not have a high percentage of Brahma, dairy, heiferettes, or bulls)
- Value-based grid pricing system that is very competitive
- Delivery dates determined by the owner at his or her perception of optimum endpoint
- Sharing of profits through stock dividends
- Transportation credit of up to $.55 per hundredweight
- Forward contracting available
- Individual carcass information free of charge for producers
- Advice and consultation from USPB field staff with assistance in management, genetics, economics, and animal health
- Access to market animals through value-added programs such as Certified Angus Beef, Farmland Black Angus Beef, and Farmland Premium Beef

Producers who lease shares can sell cattle on the grid, receive individual carcass data at no charge, obtain up to a $.55 per hundredweight transportation credit, and earn any patronage dividend paid out to USPB members based on FNB's earnings.

How Producers are Paid by USPB

The program is non-breed specific; however, cattle types with heavy Mexican influence do not support the product philosophy, regardless of grading characteristics, and are not encouraged to be marketed through the program. USBP does not accept heiferettes, Holsteins, cutting bulls, or cattle with a high percentage of Brahman influence.

The base live price for the grid is the weighted average in Kansas reported by the USDA for the week previous to the week the cattle are delivered plus $.25 per hundredweight. The base live price is converted to a hot carcass price using the previous week's plant average hot yield for non-grid cattle purchased in Kansas by FNB.

Actual performance of the cattle marketed under USPB's grid are compared to a base 52 percent for Choice or better and the rolling average performance of Kansas non-grid cattle at FNB during the preceding four weeks for Yield Grade premium/discount calculations. Prime, Certified Angus, Hardbone, Ungraded (Standard, Dark Cutter), and carcass weight premiums/ discounts are calculated with no comparison to plant averages. The Choice premium/discount is calculated based on a four-week rolling average of USDA Heavyweights Choice/Select cutout spread. Yield Grade 1 and 2 receive a premium for being above plant average but are not discounted if below the plant average. Yield Grade 4 and 5 receive a premium for being below plant average and are discounted for greater than plant average (see **Appendices A** and **B**).

Unit Retain Fee

A unit retain fee is used in a closed marketing cooperative (such as USPB) to build a reserve fund, and $12 per head is deducted from the cattle proceeds to fund the reserve account. USPB had the choice of either deducting a unit retain fee, or increasing the purchase price of its stock to create a capital reserve fund. This unit retain fee is repaid one year from the date the cattle are processed. The repayment of this fee is contingent on FNB's future success. The $12 is repaid on the one-year anniversary of the processing date calculated at $12 plus one percent over the January 1 Prime Interest Rate.

The First Year

Financial

"This first year of operation has been a year filled with challenges and opportunities for our members, as well as U.S. Premium Beef and our processing company, Farmland National Beef," said CEO Hunt (1998). The organization delivered about 8,100 head per week during the first year of operations; however, Hunt notes, the organization incurred additional expense, which was mostly due to start-up. Also, the organization had a 14-month year because it changed the year-end to coincide with FNB's fiscal year. USPB's fiscal year was changed from June 30 to August 29. The bottom line is that FNB showed a net income of $31 million. USPB's share was $7.5 million. Expenses and operations for USPB were about $3.8 million. Thus, USPB had a net income of $4.1 million and a taxable income close to $3.3 million. Taxable income for fiscal year 1998 was $10.14 per head. The cash patronage return per head was $4.06, with a balance of $6.08 being withheld in the member's name in USPB.

Table 1. USPB Return on Investment

	Average	*Top 25 Percent of USPB Producers*
USPB Investment	$55.00	$55.00
USPB Income/Head	$10.14	$10.14
Average Return/Head Over Grid	$7.47	$26.03
Average Return on Investment	32.02 percent	65.76 percent

Source: Hunt 1998.

Farmland National Beef

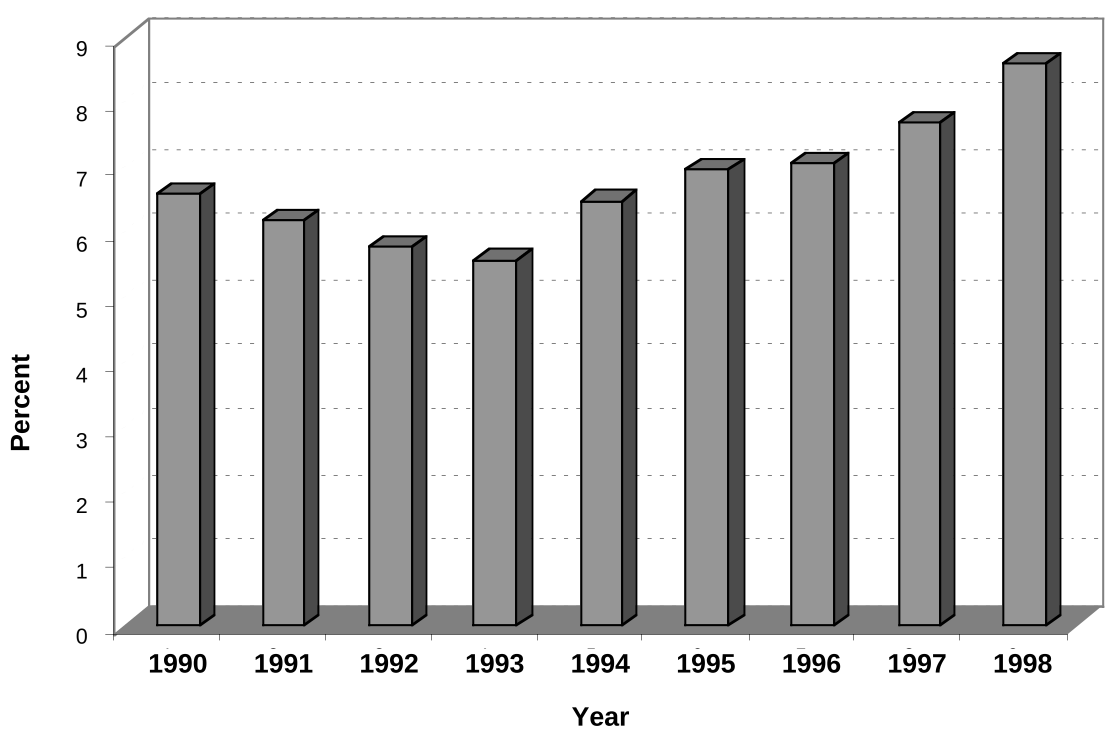
Although this case study features USPB, the analysis would not be completed without discussion of Farmland National Beef (FNB). Fiscal year 1998 may well be remembered as a year of contrasts for FNB. "There were 1.6 percent fewer cattle, but beef tonnage was up 2.2 percent," according to FNB's Executive Vice-President, Tim Klein (Miller 1998, 2). "Yet, we [the industry] had about the same amount of processing capacity to buy those fewer cattle and we had more pounds in the marketplace, which put pressure on our cutout values. That combination tends to put a lot of pressure on operating profits, which it did last year." Industry packer margins were about $18 per head lower in 1998 than in 1995. That coupled with the collapse in the drop credit area, caused specifically by the Korean financial crisis, made hides drop about $30 per hide in two weeks.

According to FNB CEO John Miller (1998, 2)

> We came into this year knowing we were going to have fewer cattle to choose from and margins would drop from the previous year, but we had a good plan. We knew we could offset some of that by lowering operating costs and by increasing gross margins by harvesting more cattle. The bottom line is that we didn't have a good year in 1998, but we had a better year than much of our competition and we made more than $31 million ($43 million pretax).

As Miller (1998) noted, although FNB did not have a stellar year, it excelled relative to the rest of the industry. The company experienced its largest one-year increase in market share in 1998 from 7.7 percent to 8.6 percent (see **Figure 2**). "What is significant is that from 1997 to 1998, the industry processed 1.6 percent fewer cattle and our market share actually went up," Klein explained.

Figure 2. FNB Slaughter Market Share



Source: Hunt 1998.

In fact, during the past five years, the industry harvested 5.8 percent more cattle than in 1993, but during the same time, FNB grew 59 percent. Klein noted, " . . . so we grew our slaughter volume at ten times the rate of the industry's growth. During the last year, we took about 37 percent of the increase in cattle supply that was available to kill and that's significant for the number four player with 8.6 percent of the market" (Miller 1998, 3).

One reason for FNB's success in terms of processing cost per head and increased market share is the significant investment the company has made in plant improvements. "Since 1992, we've spent millions of dollars to improve our plants," explained Miller (1998, 3).

In addition to increased plant efficiencies, FNB's growth in international sales, especially the Japanese market, played a large role in the company's financial success in 1998. "We export to more than 60 nations across the world," Miller (1998, 4) pointed out. "We have an office in Seoul, South Korea and this year we opened an office in Japan. We have had tremendous success in that market since doing that."

"We had about 7 percent of the chilled market in Japan in 1997, but that has climbed significantly since we opened our Tokyo office in January—to more than 12 percent in August" (Miller 1998, 4). Klein added, "Our objective in Japan is to at least double what our domestic share is so if we're at 9 percent in the U.S. market share, which is our objective for fiscal 1999, then our objective in Japan is to have at least 18 percent of that country's chilled beef market. Our Japanese customers really like U.S. Premium Beef's farm-to-table approach to producing beef," Miller (1998) pointed out. "We've taken a number of our Japanese customers on tours of USPB member operations and they really love the story. It's been a great marketing tool for us."

FNB has several line items that fit into the consumer home meal replacement market (HMR). "The idea of HMRs is just starting to catch on in the marketplace. We have precooked top rounds, roasts, and flavored ground beef items," reports Tracy Thomas (1999), director of marketing for USPB.

Producer Satisfaction

One of the concerns that many producers had initially was that if they sold cattle to USPB, other packers would not purchase cattle from their feedlots. "Our feedlots were initially concerned about discrimination, but none have indicated that has been a problem," said Thomas (1999).

Thomas (1999) noted, however, that selling cattle in a quality-based meat program versus selling live on the cash market was an initially difficult area for producers. Initially producers were selling cattle at a discount. Thomas asserts, "Producers had to make changes in management practices. Once they saw that they would be compensated for doing the right things, they changed. As genetic changes play out in the coming years, I anticipate we will continue to see improvements in the premiums paid. So far, the changes have been primarily because of management."

"There has been more than one USPB member who did not believe the carcass data sent to them was from their cattle," said Thomas (1999). The next time producers marketed cattle, however, they were invited to the packinghouse to see what was under the hide. Many producers were surprised that the meat was not the quality they thought they were producing and have started to make the necessary changes.

Using Technology

To assist in more efficiently and accurately providing individual carcass data and making genetic decisions, USPB is encouraging its producers to purchase and use electronic identification (EID) tags. To help foster their use, USPB is rebating 50 percent of the tag cost to producers who use them in 1999. EID allows a producer to keep track of the animal and record animal health history, including injections and site information that can easily be recorded and transferred to the cattle owner from the feedlot. The feedlot can use this system to track average daily weight gain and then use the ultrasound data to project when animals should be marketed. The EID system is then used at the FNB packing companies to provide feeders with individual carcass data.

Marketing to Producers

USPB must find producers willing to meet the quality standards and make the necessary changes to ensure that this happens. The co-op attends trade shows of the state cattlemen's associations, attends national trade shows, and runs advertisements in popular industry magazines. In addition, USPB staff members frequently speak at annual meetings of beef organizations, banquets, and fairs.

Staff in Place

In its first 12-18 months of operation, the staff has grown to meet the needs of the organization. Currently, there are two offices for the organization: one located in Kansas City, Missouri, and the other in Dodge City, Kansas.

Lessons Learned

In addition to sending carcass data to members within a week after slaughter, the company assists producers in analyzing results. A field representative works with members to identify problem areas. USPB has held regional meetings, and producer-education manuals have been distributed. "With information on more than 800,000 head of cattle, we now have a database that is second to none," Hunt says. "We are in a position to really help our members find out what is working and what is not" (Gilmore 1999).

One early discovery: Pens of cattle that have not suffered from heavy or lightweight carcasses or from Yield Grade (YG) 4s have consistently received premiums over the cash market. Also, a promising growth area with larger returns is the export market. In the last year, FNB opened offices in Tokyo, Japan, and Seoul, Korea, focusing on direct meat sales. Since last summer, sales in Japan have increased 50 percent. "We have had tremendous success in Japan with the U.S. Premium Beef concept," Hunt says. "The Japanese like dealing face-to-face. They like being able to trace back cattle to producers who are accountable for the meat" (Gilmore 1999).

Future Plans

USPB will continually manage its expansion as market share increases. USPB started as a Kansas-based company and has expanded into 24 states. As USPB expands the marketplace from which it buys cattle, it may also be involved in increasing its processing capacity. “We will expand in whatever way makes the most economic sense,” asserts Thomas (1999).

Another goal of USPB is to return producers’ investments within 5-10 years through premiums and patronage dividends. “Cooperatives can take years and years to be fully capitalized. From the start, USPB was more than 50 percent capitalized. With our current structure, we should be fully capitalized within 12 years. At that point, earnings will go directly to members,” said Thomas (1999).

USPB also intends to expand member communication with its members. According to Thomas (1999), “We recently completed the development of our internal home page for use with our members. In the future we anticipate that our members will have a secure password and will have access to their confidential member information on line. Additionally they will be able to compare their individual data to that of other members to see how they are doing.”

In addition, USPB plans to continue its quest to develop quality products. In that definition of quality, source verification and on-farm hazard analysis critical control points (HACCP) provide consumer assurance of quality and safety. USPB intends to implement usable, effective systems as they are developed. It also intends to work closely in developing quantifiable and predictable standards for the cattle it markets. Asserts Thomas, “If you can’t measure it, you can’t manage it. Our initial goal was not to be the savior of the beef industry, but to make our producers as much money as we could.”

For more information about the co-op, contact

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Conclusion

It seems the USPB’s success in moving relatively quickly from concept to reality was tied to the following five issues:

1. Through a process of rumination, the principal leadership of the USPB movement was ready for change. Many of the key players and early signatories have had industry involvement on a state or national level that exposed them to the decade-long

discussions about reasons for loss of market share. They seem to have substantial seasoning in the business but also have many years ahead of them.

2. There is a mix of feeders and cow/calf or stocker operators. Other similar concepts have failed to develop due to a lack of such comprehensive backing.

3. Emphasis was placed on information with application toward quality improvement. The group seems to have a powerful dual goal of improving individual profitability by doing the things that are good for the industry as a whole.

4. The group was willing to think no small thoughts. They went for an ownership position, understanding the control that would come with it. Since the stock gives a member both the right and the obligation to deliver cattle to FNB, the commitment is solid with all parties.

5. They chose a company with premier management in Farmland National Beef. The company had already committed huge amounts of money to process and product improvement since 1992, so it was well-positioned to grow. Furthermore, FNB had good brand name presence in the domestic market, with a strong international reach in place as well. The leadership of USPB was astute in recognizing the value of the brands and the well-developed merchandizing structure of FNB.

The fact that USPB could reach a deal with Farmland was probably a matter of timing and philosophy. Farmland itself could see a benefit from freeing capital it had invested in FNB. USPB was forming under a co-op structure that offered a good fit for the companies at the outset. Farmland had long recognized its connection to beef production, particularly at the cow/calf level. Through the 1990s, it had reached out to vertically coordinate segments of the industry served by the co-op. USPB would certainly fit the Farmland philosophy for improving returns for its members. The combination of meeting Farmland's capital needs and fitting philosophically was powerful in bringing the deal to fruition.

As the fourth largest packer, FNB has certainly had to feel competitive pressures from the big three packers (Monfort, IBP, and Excel). The company has been a strong "spot market" purchaser over the years and not a big contract procurer of supply. By being tied to such a narrow region, there have certainly been times when the big three packers could make life difficult for FNB. In the interest of survival and profitability, it became apparent the company would need to reach ahead and control some supply. It must have seemed fortuitous to FNB to have a quality oriented group step forward with a willingness to supply in volume under specifications. Once again, the timing helped open a door for negotiations.

Another timing factor is the growth of grid marketing and its acceptance. With a push for information, a producer has become more likely to sell on grid to get the data needed. Commercial feedlots want to offer service value to their clients, so special systems or markets would fit well. They are also struggling to help clients achieve profits. More cow operators are seeking to retain ownership through slaughter. All these factors have converged to create critical mass and ignite the fire that became USPB.

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Appendix A

U.S. Premium Beef Cattle Settlement Grid

Cattle Type

The program is non-breed specific; however, National Beef's reputation in the marketplace was built on providing high quality beef products. Cattle types with heavy Mexican influence do not support our product philosophy, regardless of grading characteristics. USPB does not accept heiferettes, Holsteins, cutting bulls or high percentage Brahman influence cattle.

Base Price

The base live price for the grid will be the weighted average price in Kansas reported by the USDA for the week previous to the week the cattle are delivered plus $.25 per cwt. The base live price is converted to a hot price using the actual weekly plant average hot yield for non-formula cattle purchased in Kansas by Farmland National Beef.

Premiums & Discounts

Actual performance of cattle marketed under USPB's grid will be compared to a base of 52% for Choice or better and the rolling average performance of Kansas non-formula cattle at Farmland National Beef during the preceding four weeks for Yield Grade premium/discount calculations. Prime, Certified Angus, Hardbone, Ungraded (Standard, Dark Cutter) and carcass weight premiums/discounts will be calculated with no comparison to plant averages. The Choice premium/discount will be calculated based on a four week rolling average of USDA Heavyweight Choice/Select cutout spread. Yield Grade 1 and 2 will receive a premium for being above plant average, but will not be discounted if below plant average. Yield Grade 4 and 5 will receive a premium for being below plant average and discounted for greater than plant average.

Category	Premium/Discount
Prime	+ $9.00/cwt
Certified Angus	+ $4.50/cwt
Choice or higher	USDA Cutout spread × weight difference above 52% (premium)
Select	USDA Cutout spread × weight difference below 52% (discount)
Hardbone	- $15.00/cwt
Ungraded	- $2.00/cwt
YG 1	+ $3.00/cwt (Premiums only, no discounts)
YG 2	+ $1.50/cwt (Premiums only, no discounts)
YG 3	Par
YG 4	- $12.00/cwt
YG 5	- $20.00/cwt
550/Down*	- $15.00/cwt
975/Up*	- $15.00/cwt
Unbranded native, heavy steer hides**	+$3/hide

* Out weight carcasses are included in determining the averages for Quality and Yield grades.

USPB pays a $3 per head premium on **native, heavy steer hides on a pen-by-pen qualifying basis. **Seventy-five percent** of the cattle in a pen must to be **unbranded steers** in order for a pen to qualify. On qualifying pens, **100%** of the animals receive the $3 per head premium.

It is understood that the premium/discount structure will be modified as new programs are developed that warrant inclusion.

Settlement

All cattle sold on the USPB grid will be issued a cash advance on the day of delivery equal to 85% of the weighted average live price for the week prior to delivery. A final check will be issued when final grade and plant averages are determined, typically Monday or Tuesday of the week after delivery.

Freight

National Beef is responsible for lining up transportation and for all costs associated with transporting live cattle from the feedyard to the plants. However, freight charges in excess of $.55/cwt will be deducted from cattle proceeds.

Carcass Data

Individual and group carcass data will be provided at no charge.

Forward Contracting

U. S. Premium Beef will offer to members selling cattle under the grid the option to forward contract cattle up to 6 months in advance. Each week a basis will be offered for future delivery periods. All forward contracting intentions must be communicated to the central procurement office with order execution during market hours.

Revised 11/16/98

Appendix B

USPB SETTLEMENT SHEET

SAMPLE

USDA Weekly Weighted Average	
USDA W Kansas Wgtd Avg.	64.93
Formula Allowance	0.25
Base Live Price	**65.18**
Combined Plant Avg. Hot Yield	62.86
Base Hot Price	**103.69**

USDA 4 Week Weighted Average	
USDA Choice 700/850 Cutout	106.03
USDA Select 700/850 Cutout	98.28
Choice Premium	7.75

Program:	USPB	# Head:	100	steers	
Plant:	Liberal or Dodge City				
Kill Date:		Live Wt:	120,000	Avg Wt:	1200
Feedyard:	XYZ Feeders	Hot Wt:	76,140	Avg Wt:	761
Lot#:	105				
Pen#:	63	Hot Yield:	63.45%		
USPB Lot#:	1900				

	Actual	Plant Average	Weight Difference	Premium/ Discount	Hot Price	Total Value
Actual Hot Weight	76,140				$103.69	**$78,949.57**
Premiums/Discounts						
Choice or Higher	63.33%	52.00%	8627	7.75		$668.59
Prime	2.69%		2048	9.00		$184.32
CAB	22.60%		17208	4.50		$774.36
Hardbone	1.00%		761	-15.00		-$114.15
Ungraded	0.80%		609	-2.00		-$12.18
Total Quality Grade						**$1,500.94**
YG1	5.01%	11.67%	-5071	3.00		$0.00
YG2	52.00%	49.24%	2101	1.50		$31.52
YG3	39.52%	36.99%	1926	0.00		$0.00
YG4	3.47%	2.10%	1043	-12.00		-$125.16
YG5	0.00%	0.00%	0	-20.00		$0.00
Total Yield Grade	100.00%	100.00%				**-$93.64**
550/Down	2.02%		1538	-15.00		-$230.70
975/Up	1.28%		977	-15.00		-$146.55
Total Out Weights						**-$377.25**
Native Hide Premium (steers only)				0.00		**$0.00**
Total Premiums & Discounts						**$1,030.05**

Gross Carcass Value	**$79,979.62**
Less Excess Freight	$0.00
Net Carcass Value	**$79,979.62**
Equivalent Live Price	**66.65**
Equivalent Hot Price	105.04
Net Premium/Discount per head *vs wgtd avg live price*	**20.64**