Here's *the* Premium!

Packers pay $25 million/year for CAB cattle

Story by
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It took 20 years of building demand for the *Certified Angus Beef*® (CAB®) brand before the pull-through effect created significant producer rewards for finished cattle. In the late 1990s, demand for CAB stormed onto the emerging value-based beef markets in the form of brand-based premiums.

In 1998, the amount paid to producers of CAB product through grid markets by the four largest beef packers totaled little more than $4 million. By 2000, it eclipsed $25 million and is estimated at more than $23 million for 2001. IBP, Excel, ConAgra and Farmland National, all licensed by Certified Angus Beef LLC (CAB), reported figures on condition that individual company numbers would not be divulged.

Value-based marketing arrangements accounted for nearly half of the CAB premiums, packers say. However, they reported at least that much more was paid in higher cash payments for pens of Angus-type cattle considered likely to achieve above average CAB acceptance. That would put the overall effect at about $50 million/year paid to producers.

Perspective

"What the market is not saying is that marbling is all you have to worry about," says one packer. "Premiums for yield grade and the innate premium for a high dressing percentage are just as important in developing higher-value carcasses — they just don't show up under a brand name."

Similarly, nobody suggests that producers can afford to ignore the production traits that keep them in business on the ranch. What the market does seem to be saying is that, in an information-driven industry where you can have both productivity and carcass value, it pays to have both.

"Producers who think beyond the scale are being rewarded for giving consumers what they want," says CAB President Jim Riemann. "That's the way our economy is supposed to work."

Gary Smith, Monfort Endowed Chair professor at Colorado State University (CSU), says he attributes the rise of CAB premiums to those basic economic principles. "This is what happens when consumers speak with up-front dollars," Smith says.

"Retailers seek more of the premium product — in this case, *Certified Angus Beef* product — and a cascade follows with trickle-down effects," he explains. "Retailers demand and pay more for it, and packers pass some of that premium back to those who produce it."

That this premium product is "branded" helps everyone who wants the CAB brand to be familiar with it, to recognize its logo and call it by name. "Thus," Smith says, "those who want it can find it, again and again. The growing market premium for producers is what happens when you produce for consumer demand."

All CAB cattle carry premiums

Most CAB-licensed packers purchase cattle through value-based pricing methods in addition to other means.

"The direct CAB premiums paid are significant and growing, but that's not really doing the brand justice," says ConAgra's Tim Schiefelbein, "because the value-added premium is always figured into a cash price, too." Premiums for a growing share of CAB-accepted cattle are paid on a formula or grid, he says. "But a similar premium is figured in on 100% of the cattle."

Packers shared grid and formula CAB premiums paid in calendar years 1998 through 2001, estimating figures for the last quarter (see Table 1). The large increase from 1999 to 2000 shows the major expansion in this buying method across all packers in the last two years, as they transfer more cash-market risk to the grid of premiums and discounts in the value-based market.

"We are delighted to see this information become public, for the good of Angus producers, and are grateful for the cooperation of our licensed packers," Riemann says. "The Certified Angus Beef program has worked 23 years to create higher value for Angus and Angus-type cattle that produce high-quality end products and will continue to do so."

Leading Angus producers have long known that high quality was the key to a successful future for their breed and industry, Riemann says. "It is good to be able to quantify that benefit. Our licensed packers have been good partners in encouraging producers to focus on improving end-product quality. That shows in the premiums they have awarded producers who are meeting the challenge," he adds.

In addition to the direct and cash producer premiums, licensed CAB packers have been the sole source of funding for this producer brand, Riemann points out. Since CAB's inception in 1978, paying pennies on the pound, packers have funded CAB operations on sales of 3.6 billion pounds (lb.) of branded product. "The effect has been additive over time," Riemann says.

Oklahoma State University (OSU) economist Clem Ward says the upward surge in CAB premiums paid to producers since the 1990s indicates the effect of competition in the market. Owned by a nonprofit subsidiary of the American Angus Association, the CAB brand is licensed across the spectrum of packers, who must compete to procure the type of cattle needed to meet demand.

"This speaks volumes about packers paying to meet customer needs," Ward says. "But there's another side as well: When producers understand the 'target' and know the 'payoff,' they can and will respond."

Overall demand for higher-quality beef has led the comeback in consumer demand,

Table 1: Grid and formula CAB premiums paid, by calendar year

1998	1999	2000	2001
$4,168,236	$7,093,628	$25,916,459	$23,204,000*

**Projected*

Note: *Share of black-hided finished cattle moved from 40% in 1998 to nearly 50% today.*

and the CAB brand played a key role. Ward says, “CAB has been a very important leader in the move toward responding to consumer demands, increasing product quality and rewarding producers for quality.

“CAB was perhaps the first, and remains the largest, ‘marketing program’ in the beef industry,” Ward says. “Many others looked to CAB as the leader and modeled parts of their programs after it. Clearly, CAB is the only such program that has its own premium identified in many grids.”

Ward says the brand’s pioneering efforts have contributed significantly to the beef industry’s progress in recent years. The net effect, he says, is that “a sort of synergy developed that has collectively contributed to improvements in the beef industry.”

Who gets the reward?

Do CAB premiums fall to producers who deserve them? Not always, or at least, not directly. Ward says some commercial feeders are rewarded for doing very little, especially if they have purchased Angus calves from unsophisticated sellers. However, several industry surveys over the past 10 years show cow-calf producers are rewarded for the average level of CAB premiums in finished black-hided cattle when buyers know they carry Angus genetics.

Increasingly, Angus producers are retaining ownership of calves on feed or entering into partnership arrangements with licensed CAB feedlots. Those agreements may permit them a share in the premiums, or help them discover individual carcass merit in preparation for more progressive value-based marketing in the future.

Schiefelbein says, cash or grid, producers are paid roughly equal CAB premiums in the long run. “But if you want an accurate accounting for your cattle any given week, you should sell on a grid,” he adds.