Contract Operations Seen Increasing Slowly

Contract production and vertical integration, sometimes touted as the wave of the future in U S. farming, aren't increasing as fast as has been supposed, according to USDA production and marketing specialists.

The Economic Research Service estimates the proportion under various forms of contracting and vertical integration increased from 19 to 22 percent between 1960 and 1970—a gain of only 3 percentage points.

The extent of contract production increased from 15 to 17 percent and vertical integration from about 4 to 5 percent.

The growth was limited because many commodities were not much affected and because increases in some commodities were partly offset by decreases in others For example, increases in contracting in cotton and vegetables were counterbalanced by decreases in citrus and in dry beans and peas group

Contracting

Contract production in farming is a fairly inclusive term that includes the various buy-sell agreements that farmers enter into with dealers or processors or other businessmen before undertaking the production of a commodity

These agreements can be either loose arrangements spelling out only minimum prices and production levels . or they can be highly specific contracts setting down tight quality and cost controls.

A couple of examples·

—Grain production contracts, while not extensive in either the food or feed grain sectors, tend to emphasize improved practices and quality controls. They rarely provide supplies or financing but they often guarantee premium prices to farmers who can produce consistently high-quality products. Breakfast food companies, for instance, sometimes contract for certain qualities of grain for cereals.

Also, producers of special strains of grain, high lysine corn, and malting barley often enter into "forward contracts" with processors. This way, the farmers of such specialized commodities are guaranteed a market before they commit their valuable production resources.

—In broiler production, where contracting is extensive, the contracting firm often is a processor or a feed mill that supplies production inputs such as chicks, feed, and medicine along with some financing. The farmer contributes his labor, buildings, and managerial expertise.

The contracting firm generally exercises a good deal of control over broiler production costs and quality over broiler production costs and quality so that it can be assured of a steady supply of birds at a consistently low price. The farmer, meanwhile, can count on a minimum payment for his resources—plus he usually gets a bonus for efficient feed conversion rates or other savings for the contractor

Production contracts figure far more prominently in livestock enterprises than in crop farming. Reason· Livestock products tend to be more perishable and are subject to quality variations which may require closer coordination.

Most commodities with important elements of contracting have had these elements for quite some time.

For instance, fluid milk production has long been organized under contract arrangements either through cooperatives or directly with indendent milk producers.

The dramatic expansion of contracting in the broiler industry was essentially complete by 1960—though there was a spillover effect on egg and turkey production in the 1960's. Contracting for the latter two items grew during the decade—the result of combining technological developments in breeding, feeding, and disease control with the economic strategies proven successful by broilermen.

Contracting gains in the fed cattle industry during 1960-1970 centered around the rapid increase in large commerical feedlots and the associated gain in custom feeding.

In crop farming contracting has long been extensive in both the production of sugarbeets and vegetables for processing. For both commodities processors need an assured supply to operate their expensive equipment efficiently. At the same time producers of both crops need guaranteed markets—in the case of sugarbeets because there are no alternative outlets, in the case of vegetables because the crop is highly perishable.

A notable drop in contracting occurred during the 1960's in production of dry beans and peas. Back in 1960 production contracts were very much in vogue for these two commodities—especially when the crops were newly introduced in an area. The contracts generally contained quality provisions and called for improved practices.

However, as growers learned the culture these features were no longer necessary and by 1970 contract production of dry beans and peas was no longer common.

In contrast, contracting in cotton production was markedly higher in 1970 than a decade earlier—the result of a short supply situation.

Cotton contracts in 1970 were usually initiated by merchants, shippers, ginners, sometimes even mills themselves in an attempt to make sure of meeting business commitments. (Actually the 11-percent share of the crop contracted for in 1970 had swelled to 32 percent by August 1, 1972 as the tight supply situation persists.)

Vertical integration

Vertical integration means tying two or more production and marketing steps together within a single firm for the purpose of lowering costs and boosting operation efficiency. At present the extent of vertical integration is about the same for both crop and livestock production—limited.

Thus far the sugarcane industry has experienced the greatest move toward vertical integration—with about 60 percent of the crop in Hawaii grown under an intricate system of plantation farming and milling, with cooperative refining and marketing, including unionized labor.

On the Mainland about a third

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