KANSAS LIVESTOCK ASSOCIATION

Since 1894

To: Special Committee on Economic Recovery
Sen. Julia Lynn, Chair
Rep. Sean Tarwater, Vice Chair

From: Aaron M. Popelka, V.P. of Legal and Governmental Affairs, Kansas Livestock Association

Re: **COVID-19 Economic Impact on the Kansas Livestock Sector.**

Date: August 13, 2020

The Kansas Livestock Association (KLA), formed in 1894, is a trade association representing over 5,700 members on legislative and regulatory issues. KLA members are involved in many aspects of the livestock industry, including seed stock, cow-calf, and stocker cattle production; cattle feeding; dairy production; swine production; grazing land management; and diversified farming operations.

Thank you, Chairwoman Lynn, Vice Chairman Tarwater, and members of the Special Committee for the opportunity to present a summary of the impacts the COVID-19 pandemic has had on the Kansas livestock sector. I will highlight impacts on the meat processing sector; the cattle, dairy, and hog sectors; and review some opportunities and challenges presented by state and local governments.

<u>Impact on the Beef Sector</u>

COVID-19 created significant stress on the not just livestock producers, but also the entire beef supply chain. In the U.S., we have an efficient and sophisticated beef supply chain, but the pandemic highlighted one of the potential vulnerabilities in the system, which is the concentration of large meat processing plants in a few select locations across the country, one of which is in southwest Kansas. Kansas produced approximately 5.4 billion pounds of beef in 2019, with most of the production coming from three cities, Dodge City, Holcomb, and Liberal, Kansas. As COVID-19 began spreading across the country, packing plants were not immune to the disease. Although packing plants were deemed essential, line speed slowed as personal protective equipment was installed and workers were quarantined for exposure to, or sickness from, COVID-19. The climax of the beef production slowdown occurred in April. The U.S. Department of Agriculture (USDA) estimated that "weekly slaughter decreased from over 684,000 head at the end of March to under 439,000 at the end of April, a decrease of 36 percent."[1]

[1] USDA, Agricultural Marketing Service, BOXED BEEF AND FED CATTLE PRICE SPREAD INVESTIGATION REPORT at 9, *available at* https://www.ams.usda.gov/sites/default/files/media/CattleandBeefPriceMarginReport.pdf (July 22, 2020).

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This reduction in slaughter capacity resulted in a short-term shortage of beef at retail, as less beef was being produced, while at the same time consumers increased their grocery store purchases by as much as 44 percent over the prior year during the last week of April.[2] This resulted in grocery stores stopping promotions, and in some cases, rationing beef sales. It should be noted, however, that some of the retail increase can be attributed to closure of or restrictions placed on use of food service establishments. According to USDA, "[t]he weekly average Choice boxed beef cutout value rose from approximately $255/cwt. at the beginning of April to over $459/cwt. by the second week of May, an increase of approximately 80 percent".[3]

At the same time, however, fed cattle began to back up in feedyards, due to the 36 percent reduction in cattle harvest rates. Not only did this create a backlog of supply in terms of number of animals, but it also increased carcass weights by approximately 50 pounds per head in May as market ready cattle could not be processed and continued to grow.[4] At its height, market analysts estimated the backlog of market-ready cattle to be nearly 1 million head of cattle.[5] This led to severe price declines for fed cattle producers.

On January 21, 2020, the day before the first case in the U.S. was made public, the CME August Live Cattle Contract traded at $116.450/cwt. On April 26, 2020 the CME August 2020 Live Cattle Contract closed at a record low of $84.275/cwt. Since that day, prices have slowly rebounded and the CME August 2020 Live Cattle Contract closed yesterday at $104.740, which is still $3.30/cwt below the CME August 2019 Live Cattle Contract close on August 9, 2019. In addition to asking congress for disaster assistance for livestock producers in the Coronavirus Aid, Relief, and Economic Security (CARES) Act, KLA also requested that USDA investigate to determine if any anticompetitive behaviors occurred during this period that would amount to violations of the Packers and Stockyards Act of 1921.[6]

The pandemic's impact on fed cattle prices resulted in additional pressure on the feeder cattle and calf markets as well. Feedyards are a margin business that rely on their ability to constantly turn inventory. Feedyards buy feeder cattle, fatten the feeder cattle into market-ready fed cattle, and sell the fed cattle to packing plants. When fed cattle harvest slowed during the height of the pandemic, it limited the amount of space available at feedyards for placing feeder cattle from ranches. This led the CME August Feeder Cattle Contract, which closed at $155.000/cwt on January 21, 2020, to drop to a low of $114.425/cwt on April 5, 2020. Since April 5, 2020, feeder cattle prices have slowly rebounded, and the CME August 2020 Feeder Cattle Contract closed yesterday at $144.750.

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[2] USDA, Agricultural Marketing Service, BOXED BEEF AND FED CATTLE PRICE SPREAD INVESTIGATION REPORT at 9, *available at* https://www.ams.usda.gov/sites/default/files/media/CattleandBeefPriceMarginReport.pdf (July 22, 2020).

[3] USDA, Agricultural Marketing Service, BOXED BEEF AND FED CATTLE PRICE SPREAD INVESTIGATION REPORT at 9, *available at* https://www.ams.usda.gov/sites/default/files/media/CattleandBeefPriceMarginReport.pdf (July 22, 2020).

[4] CattleFax Update, Issue 22, Vol. LII (May 29, 2020).

[5] CattleFax Update, Issue 22, Vol. LII (May 29, 2020).

[6] KLA Letter to USDA Undersecretary for Marketing and Regulatory Programs Greg Ibach re COVID-19 Cattle Market Impacts, available at https://www.kla.org/Media/KLA/Docs/ibach-re-covid-19-cattle-market-impacts.pdf (April 2, 2020).

During the spring and early summer, cow/calf and stocker operations had to adapt to adverse markets. Some operations with feeder cattle and calves for sale had to sell those animals at a loss because the operations could no longer accommodate feeding the cattle. Other operations were able to move those calves and feeder cattle to a higher forage, lower energy ration with lower rates of gain, or move the livestock onto summer grazing programs, to delay placement in feedyards. While these decisions often mitigated steep losses due to adverse prices during the spring, these decisions also added extra costs that will negatively impact annual profitability.

In the lead up to passage of the CARES Act, KLA's national affiliate, the National Cattlemen's Beef Association (NCBA), commissioned a study to determine the extent of losses in the cattle industry attributable to the COVID-19 pandemic. That study, led by Dr. Derrell Peel of Oklahoma State University, assisted by Glynn Tonsor of Kansas State University and other leading agricultural economists, estimated total cattle industry losses at more than $13.6 billion for 2020.[7] These included losses of approximately $205 per head of fed cattle, $160 per head for feeder cattle, and $112 per head for cow/calf operations.

This study was submitted to USDA to help guide its release of CARES Act agricultural disaster assistance. On May 26, 2020, USDA opened enrollment in the Coronavirus Food Assistance Program (CFAP).[8] While this was needed disaster relief for a number of agricultural producers, some flaws in how the program was designed resulted in disparate assistance among cattle producers. On June 4, 2020, KLA CEO Matt Teagarden sent a letter to USDA Secretary Sony Purdue highlighting these issues with the CFAP program and suggesting changes to the program to better assist livestock producers experiencing COVID-19 related losses.[9]

Currently, beef processing plants are approaching 2019 harvest levels, with last week's slaughter at 633,000 head, which is about 14,000 head less than the same time last year.[10] While this improvement in harvest rates is good news, the industry must maintain or even increase these harvest levels to work through the remaining backlog of market ready cattle.

Impact on the Dairy Sector

KLA also represents many dairy operations in Kansas. KLA member dairies produce roughly 1/3 of all the liquid milk in Kansas. As of 2019, Kansas was home to 163,000 milk cows, on a mixture of more than 270 large and small dairy farms, and these dairies produced 3.8 billion pounds of milk. These operations were dramatically impacted by COVID-19.

Early in the pandemic, the National Milk Producers Federation estimated dairy farm losses could top $2.8 billion in the U.S. While dairy products initially saw significant retail price increases in grocery stores, overall demand declined because restaurant sales stopped. Fluid

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[7] Oklahoma State University and National Cattlemen's Beef Association, Economic Damages to the U.S. Beef Cattle Industry Due to COVID-19, available at https://www.kla.org/Media/KLA/Docs/osu-ncba-beef_covid_impacts_full.pdf (April 14, 2020).

[8] *See* USDA, Livestock and the Coronavirus Food Assistance Program, available at https://www.farmers.gov/cfap/livestock (last visited August 11, 2020).

[9] KLA Letter to USDA Secretary Sonny Perdue re CFAP Deficiencies, available at https://www.kla.org/Media/KLA/Docs/kla-letter-to-sec-perdue-re-cfap-deficiencies-6-4-2020.pdf

[10] USDA, National Weekly Cattle and Beef Summary for the Week Ending August 7, 2020, available at https://www.ams.usda.gov/mnreports/lswwcbs.pdf (lasted visited August 11, 2020).

milk sales to schools also stopped. Milk products in the supply chain then had to be rerouted to retail stores. Some cooperative dairies were required to reduce production by as much as ten percent during the pandemic. This resulted in dairies either culling cows or dumping milk in accordance with waste management permits.

As these supply chain disruptions occurred, milk prices severely declined. On January 21, 2020, CME August 2020 Class III Milk Contract closed at $17.95/cwt, but by April 22, 2020, it closed at a contract low of 14.22/cwt.

The dairy export market, however, remained strong throughout the pandemic. U.S. suppliers shipped 28% more dairy products by volume than during June 2019. This pickup in exports helped prices rebound after the initial coronavirus slump, and as of August 11, 2020, CME August 2020 Class III Milk Contract closed at $19.39/cwt, $1.44/cwt above its pre-pandemic price levels.

Impact on the Pork Sector

Hog farmers in Kansas and across the U.S. also faced severe market disruptions as a result of COVID-19 related challenges. According to Dr. Steve Meyer, an economist with Kerns & Associates, U.S. hog farmers face massive losses due COVID-19 pandemic-related factors. According to his analysis, potential 2020 revenue from hog sales will be reduced by roughly $5 billion.[11] Like the beef sector, pork processing plants had to reduce harvest rates due to COVID-19 worker infections and slower line speeds to accommodate for installation of personal protective equipment. This led some hog producers in the U.S. to euthanize or donate pigs, although it seems Kansas producers were able to avoid any widespread euthanizations.

Kansas hog farmers were already in a weakened financial position due to two years of trade retaliation and COVID-19 losses have only increased the financial strain. Dr. Meyer estimates that hog farmers are now looking at approximately $37 per hog losses relative to what they expected for 2020 before the COVID-19 crisis began. Kansas expects to market approximately 3.5 million hogs in 2020, which would equate to roughly $130 million in losses to Kansas hog farmers using Dr. Meyer's estimate.

Other Government-Related Opportunities and Challenges

Small Meat Processors

One area in the beef sector that has received significant attention during the COVID-19 pandemic was small meat processing plants across the state. The COVID-19 pandemic and economic shutdown in the spring led many consumers to turn to local meat processors and butchers to fill the void when grocery stores began rationing meat. The increased interest overwhelmed small processors and resulted in bookings being backed up in excess of six months. Beef producers with market-ready cattle who wanted to engage in local sales could not get a harvest slot.

It is unclear whether this backlog at local small processors will persist into 2021, but there may be an opportunity to help small Kansas meat processors increase capacity to accommodate the

[11] National Pork Producers Council, Hog Farmers Face COVID-19 Financial Crisis, available at https://nppc.org/hog-farmers-face-covid-19-financial-crisis/ (last visited August 12, 2020).

new interest in local meat sales. Short of expanding the slaughter and fabrication areas, one easy way to expand capacity is through expansion of cold storage and equipment upgrades. Plants cannot continue slaughter and fabrication if the plant's cold storage is at capacity. By expanding cold storage, plants can continue to process animals while storing meat for future delivery. Currently, CARES Act funds are available through the Kansas Department of Agriculture (KDA) for such activities, and KLA plans to work with KDA to make small processors aware of these funds.

In addition, KLA believes there are opportunities to grow local meat sales from small state-inspected meat processors by allowing these plants to sell products across state lines. While Kansas has a robust state meat inspection program that is equivalent to federal standards, federal law prohibits these state-inspected plants, or their producer customers, from selling to out-of-state consumers without federal USDA inspections. This is not always a possibility for small meat processors due to added operational costs and availability of USDA inspectors. While this is a federal issue, KLA has expressed its interest in working with KDA to determine what changes to federal law might remedy this situation while protecting food safety.

State and Local Health-Related Restrictions

During the initial economic shutdown, KLA was pleased that Governor Laura Kelly declared both production agriculture and food processing plants essential businesses. Her uniform statewide order kept the food supply chain moving. KLA is also appreciative of the Kansas Department of Health and Environment's and KDA's assistance in finding ways to keep packing plant employees on the job and their families and communities healthy.

One challenge encountered by KLA in the early stages of the pandemic was local county health officers exceeding their authority, and in some instances, declaring agricultural employees subject to travel restrictions and general quarantines based on their county of residence. These local restrictions were in conflict with the Governor's statewide executive order and outside of the health officers' authority under K.S.A. 65-129b. KLA legal staff had to engage with numerous county officials to try and correct these invalid local orders. State officials were often reluctant to push back on these local officials because the state officials did not believe the orders were being enforced. The existence of these invalid orders, however, led to confusion, and in some instances, health officials threatened to shut down purebred cattle sales and feeder cattle markets.

To an extent, passage of HB 2016 during the 2020 Special Session helped to remedy this situation. HB 2016, however, left unclear as to whether and to what extent a county may enact more stringent COVID-19 pandemic-related restrictions. HB 2016 clearly gave counties the ability to "review, amend, and revoke" executive orders issued by the governor. The ability to amend an executive order, however, is not limitless and amendments are constrained by the statutory authorities of the county health board. These powers are typically limited to quarantine powers under K.S.A. 65-129b or authority emanating from local emergency disaster authority under K.S.A. 48-932. If the authority is exercised under the local disaster statutes, K.S.A. 48-932 requires that the actions be "pursuant to applicable local and interjurisdictional disaster emergency plans." KLA staff have observed county health officers and boards exceeding these authorities.

For instance, following passage of HB 2016, a patchwork of policies has arisen in regard to use of face masks. This issue began when Governor Kelly issued Executive Order 20-52 mandating use of face masks in public spaces. KLA disagreed with the executive order for a number of reasons, including: 1.) the executive order unconstitutionally delegated the enforcement of a law to private business rather than public officer, 2.) the order did not fit all locations and all types of employers, and 3.) the order created civil liability issues for businesses attempting to comply with its terms. On July 9, 2020, KLA, and a number of other associations, outlined these concerns in a letter to Governor Kelly, copying legislative leaders, asking the governor to withdraw Executive Order 20-52 and work with the business community on a public information campaign to put in place a best practices approach to wearing face masks for places of employment and business.

Unfortunately, the nature in which Executive Order 20-52 was issued resulted in a majority of Kansas counties opting out of the face mask mandate, while a few counties chose to retain the Governor Kelly's mandate. This alone creates logistical and legal challenges for companies doing business across county lines. More troubling, however, is that some counties devised their own mask mandates outside the purview of Kansas public health and disaster-related statutes, as described above. While a county can clearly opt out of Executive Order 20-52, it does not appear that Kansas law gives county health officers or boards the ability to mandate use of masks at private places of business.

As the legislature looks to next session, the legislature should look to refine public health and disaster laws in a way that balances the need for local control, with the need to appropriately restrain executive power, and with the need to make sure businesses have a consistent set of rules from county-to-county in a pandemic or other emergency disaster situation. Under the current system, businesses that operate across county lines can find it difficult to identify which local restriction is in place in which county. This is especially the case as many smaller counties do not have official websites, and often resort to unofficial Facebook pages that may or may not be readily identifiable by out-of-county businesses. Enhancing county and city websites and other public information tools may be an appropriate use of some of the state COVID-19 relief funds under the CARES Act.

Tax Policy

As a general matter, KLA policy supports the use value appraisal of agricultural land; opposes increased reliance on property tax revenues to fund state and local government; and supports continued sales tax exemptions for livestock and crop sales, agricultural inputs, and agricultural machinery and equipment. In regard to existing agricultural sales tax exemptions, KLA believes that the agricultural exemptions are consistent with the policy of exempting business inputs from sales tax, which was recently recognized as appropriate tax policy in the 2019 Kansas Tax Modernization report by the Tax Foundation.

In regard to property tax, while valuations have hit historic highs since reappraisal in the 1980s, KLA supports the use value appraisal system. This system looks at the actual income earning potential of land and is built on an eight-year average of an eight-year average of commodity prices net of farm expenses to determine a valuation. Despite having record high valuations, according to the use value formula, valuations should start to decline in the next one to two years as higher commodity prices from earlier in the last decade are replaced with lower prices in more recent years.

It is important to note that valuation is only one side of the tax liability equation. Mill levies, set by local units of government, are responsible for the other side of the equation. For that reason, KLA continues to support the property tax lid. It was only after imposition of the property tax lid that mill levies in rural counties started to decline. Prior to enactment of the property tax lid, data showed that while agricultural valuations were climbing, rural mill levies were also increasing leading to tax increases in excess of inflation. A move to remove the lid could once again lead to unchecked property tax increases. Property taxes are one of the most difficult taxes for agricultural operations because the tax is payable regardless of profitability, unlike the income tax, and agriculture, by nature, is invested heavily in land and buildings.

Thank you for the invitation to present information on livestock-related COVID-19 challenges. KLA and its members stand ready to assist the legislature as it looks at any necessary changes to state law.