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Grassley urges detailed review of $4.7 billion pork deal

By: Jeff Patch – May 31. 2013

Iowa lawmakers are concerned about pork. This time, the issue is Chinese influence over U.S. agriculture rather than earmarks.

A proposed merger between Smithfield Foods, the world's largest pork processor, and Chinese-based Shuanghui International Holdings could have a lasting impact on Iowa agriculture. Under antitrust law, the federal government will investigate the politically sensitive $4.72 billion deal, although it's "unlikely to face serious opposition," according to a Wall Street Journal report.

Shuanghui, China's largest meat processor, aims to acquire Virginia-based Smithfield, which has significant operations in Iowa, to increase pork exports to China, the world's largest hog market.

The deal, four years in the making, is worth $7.1 billion, including assumed debt. The $34 per share price is a 31 percent premium over the previous value of Smithfield stock. The company has facilities in 26 states, 46,000 employees and annual revenue of $13 billion.

Sen. Chuck Grassley, R-Iowa, urged a cautious approach as federal agencies examine the deal to determine whether it would materially reduce competition in the meat market.

"I share the concerns of many family farmers and independent producers that the agriculture industry has consolidated to the point where many smaller market participants do not have equal access to fair and competitive markets," Grassley said in a statement Wednesday.

National security concerns over 'the other white meat'?

Grassley said scrutiny by the Department of Justice and the U.S. Committee on Foreign Investment(CFIUS), an inter-agency body that reviews deals that might impact national security, is "vitally important."

"No one can deny the unsafe tactics used by some Chinese food companies," Grassley said. "To have a Chinese food company controlling a major U.S. meat supplier, without shareholder accountability, is a bit concerning. I've always said that we are nine meals away from a revolution, so a safe and sustainable food supply is critical to national security."

An analysis by the Rhodium Group, a consultancy, indicates that CFIUS will likely approve the deal after a customary review of about 75 days. In recent months, the committee has approved deals in the biosciences, oil and battery production industries, despite strong domestic opposition. Daniel Ikenson, the director of the libertarian Cato Institute's Center for Trade Policy Studies, dismissed concerns regarding Smithfield.

"Ham is not a national security issue," he said.

Grassley said that he hasn't yet seen information yet that would put the Smithfield deal on par with other foreign deals that have blown up over national security concerns, although he stressed that CFIUS should determine whether the Chinese government has a role in the company.

"I'm going to take a wait and see approach unless I get some evidence that they're different than other mergers," he said in an interview with TheIowaRepublican.com Thursday.

Deal poses antitrust issues

Grassley's main concern is the ability of independent pork producers to get a fair market rate when so few companies control the pork market. The top four companies control 74 percent of the market, he said.

Nonetheless, based on the information available, the Smithfield deal wouldn't seem to alter that balance as Smithfield is being acquired by a foreign company rather than consolidating with an existing market player. Indeed, Grassley said the deal could provide a win for Iowans by increasing exports of pork to foreign markets.

A Smithfield spokesman told TheIowaRepublican.com that the deal would not negatively impact the company's operations in Iowa or elsewhere: facilities will not close, collective bargaining agreements and existing wages will be honored and layoffs will not occur. Smithfield has eight operations in Iowa, ranging from pork processing to packaging, that employ about 3,500 people in Denison, Carroll, Mason City, Sioux Center and elsewhere.

On its face, the deal seems to create value in both the China and the United States. China's population has a soaring demand for pork, the deal will provide increased food safety for Chinese consumers and it would help diversify Chinese investment by directing more resources toward assets rather than American debt. Smithfield shareholders will certainly benefit: the deal represents a 31 percent premium on the company's share price.

Grassley expressed concern about the company's stated interest in vertical integration, which allows Smithfield to control every state of pig production—from birth to bacon. Companies contend that such operations allow greater quality control and consistency, but critics contend that the practice, especially in agriculture, allows meat processors to demand cut-rate prices from local farmers.

Deal represents uptick in Chinese foreign investment in U.S.

Ikenson said the United States should welcome such deals to increase foreign direct investment (FDI). The U.S. share of FDI has dropped from 41 percent in 1999 to 17 percent in 2011, signaling that foreign investors are increasingly looking to other markets although the U.S. still remains first.

“We need investment. If the Shuanghui wants to buy this company for $4.7 billion, that’s $4.7 billion in the economy that wouldn’t otherwise be there,” he said, noting that the deal shouldn’t be scuttled by anti-China sentiment.

Chinese investors are flush with cash, but limited in their U.S. investment opportunities other than American debt. Despite a recent increase, Chinese share of U.S. FDI is puny, amounting to just $5.9 billion in 2010 (0.25 percent of $2.34 trillion in total U.S. FDI).

China is already investing in the U.S. by “subsidizing Congress’ profligacy,” Ikenson said, noting that money would be invested more efficiently if the Chinese could purchase hard assets and companies rather than simply financing U.S. debt.

Left-leaning environmental groups, though, criticized the proposed deal’s potential impact on American farmers.

“Smithfield … has a growing stranglehold over U.S. farmers, who have fewer options for selling their hogs at the market and are prey to abusive contractors from processors like Smithfield,” Wenonah Hauter, the executive director of liberal advocacy group Food & Water Watch, said in a statement. “We may export the pork, but we keep millions of gallons of manure right here in U.S. hog raising communities in North Carolina and Iowa.”

Smithfield has dealt with competition issues in Iowa before

Smithfield has tangled with the Department of Justice and the State of Iowa before on merger matters. The company controls about one quarter of the U.S. pork market.

In 2004, the U.S. government fined the company $2 million for not complying with premerger notification requirements before purchasing the stock of its then-competitor Iowa Beef Processors, which is now a subsidiary of Tyson Foods, in the late 1990s.

Iowa law prohibits meat processors from owning livestock, but Iowa Attorney General Tom Miller has negotiated agreements with several companies promising to not enforce the law as long as the companies guarantee certain rights to local farmers.

Smithfield sued Iowa after the law passed in 1987, and federal judge Robert Pratt struck down the law as an unconstitutional state restriction on interstate commerce. Iowa lawmakers amended the law in response to Pratt’s ruling and an appeals court later vacated the ruling so Pratt could reconsider the new law. In the meantime, Miller reached a settlement with Smithfield (the corporate agreements expire next year).

In March 2010, U.S. Attorney General Eric Holder and U.S. Agriculture Secretary Tom Vilsack traveled to Ankeny to kick off a series of unprecedented workshops examining antitrust issues in agriculture. Advocates of a robust antitrust enforcement regime have criticized the government for not stopping more deals since then.

Assuming the government approves the deal, Iowans might want to learn the word zhūròu, the Chinese term for pork.