Inside Business 8–1

Competition in the Poultry Market

The years 1983–1991 showed continuous but falling profits in the poultry industry. Because of positive profits in the industry, the market capacity for producing broilers grew over that eight-year span. The expansion came from existing farms adding capacity and from new farms entering the industry.

Figure 8–10 shows representative market supply and demand curves and a potential cost structure for an individual farm. S^1 in Figure 8–10(a) is the market supply as it was in 1983 before expansion. With market supply of S^1, the equilibrium price is P_1 in panel a. In panel b, an individual firm chooses to produce q_1 units of output, resulting in profits of the area ABCD for each firm. The profits in the industry induce entry. The increased entry shifts the market supply curve to the right, as shown by the shift from S^1 to S^2 in Figure 8–10(a). This increase in supply reduces the equilibrium price to P_2. The new market equilibrium is at point Z in Figure 8–10(a) and results in more chicken being purchased at a lower price. When the price declines to P_2, each individual farm decreases its output to q_2 in Figure 8–10(b), where the new price equals marginal cost. The new price also results in lower profits, which are now area EFGH in panel b. However, enough farms enter the market that total market output actually increases, even though individual farm output declines.

The preceding description of the broiler industry using the perfectly competitive model reflects what happened in the broiler industry from 1990–1992. Prices in the broiler industry declined from \$.55 per pound in 1990 to \$.51 in 1991 to \$.47 in 1992. At the same time prices were declining, so were profits. Profits per pound declined from \$.08 in 1990 to \$.03 in 1992. In fact, the profits per pound in 1992 were approximately a 7 percent return on investment. This was very close to zero economic profits, since the opportunity cost of investing elsewhere in 1992 was about 7 percent. Further entry is unlikely unless cost or demand conditions change.

Source: Jon F. Scheid, "Poultry Markets Slow from Competition," *Feedstuffs*, December 16, 1991, p. 6.