

Leaflet 3. Dairy and the World Trade Organization

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Trade Situation and Outlook

Even though the U.S. is the leading country in world cow milk production, it is a relatively minor player in international trade. About 2-4 percent of domestic milk production is exported. Imports amount to a similar percentage in milk equivalent, but considerably more in terms of value. Yet trade prospects have been a hot topic of discussion among U.S. industry participants in recent years. The reasons include:

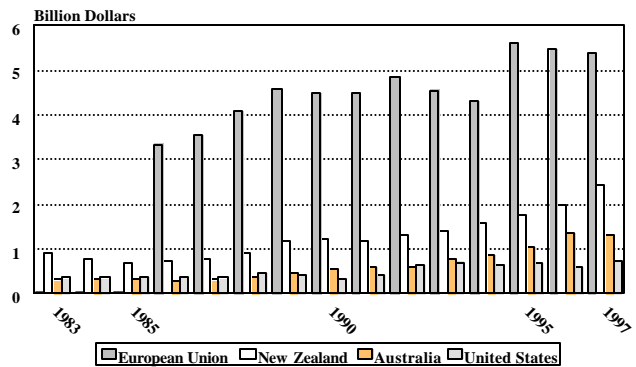
- 1) Lower levels of support prices, and recurring periods like the present, where dairy product prices hover around support.
- 2) Slowing rate of increase in domestic per capita dairy product consumption.
- 3) Brief periods when world Non-Fat Dry Milk (NFDM) prices rose to U.S. levels, with resulting surges in exports and U.S. milk prices.
- 4) Incidents of success by U.S. firms in selling differentiated products in Asia, Mexico and other countries.
- 5) Major customers (McDonalds, Pizza Hut) have taken suppliers, including dairy processors, abroad with them, whether they wanted to go or not.

There is general consensus within the industry and among researchers that the U.S. is unlikely to become a major exporter unless major changes are made through the World Trade Organization (WTO) and/or through changes in European Union (EU) domestic dairy policy.

Major Customers and Competitors.

U.S. imports are dominated by cheese and casein. About half of U.S. exports are divided fairly evenly among ice cream and yogurt,

Dairy Product Exports from Selected Countries, 1983 - 97

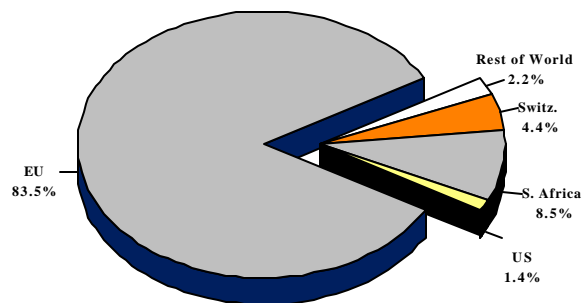


Source: FAO

cheese, NFDM, and whey.

The EU is by far the dominant player in world dairy export markets with annual sales exceeding \$5 billion. It is important to note that the EU out-produces domestic needs by a considerable margin because of its dairy program, and in turn subsidizes heavily its excess production. New Zealand and Australia are the other two major exporters. There is almost no subsidization in New Zealand and relatively little in Australia. Exports account for a major share of production in both countries. The U.S. ranks fourth in dairy exports. Our Dairy Export

Export Subsidies by Country, 1996
\$8.5 Billion Total



ERS, USDA, WRS-98-4, 12/98.

Incentive Program subsidy program is currently limited under the WTO agreement to about 79,000 mt of dry milk, 25,000 mt of butterfat, and 3,000 mt of cheese per year. Major importers include Japan, East Asian countries and Mexico.

Major Dairy Trade Issues

Export Subsidies. At a recent national workshop sponsored by Cornell's Program on Dairy Markets and Policy, industry participants voted overwhelmingly that reduction in export subsidies should be the number one focus of upcoming negotiations. The U.S. can be expected to align itself closely with the Cairns Group in attacking EU subsidy levels. Even after complete phase-in of the last WTO agreement, the EU is allowed to continue heavy subsidization.

Domestic Support. The major dairy nations (including the U.S.) continue to support production heavily except for New Zealand and Australia. Producer Subsidy Equivalent's (PSE) in 1996-98 ranged from virtually nil in New Zealand, 28 percent in Australia, slightly less than 50 percent in the U.S., slightly greater than 50 percent in the EU and Canada, to almost 80 percent in Japan. The focus in this area may emphasize means rather than absolute level. Reducing export subsidies would force the EU to change its domestic program or sharply lower production quotas.

Tariffs. Many in-quota and over-quota tariffs remain prohibitive even after complete WTO phase-in. Lowering tariffs may thus have more impact on trade flows than increasing quota limits. Considerable support exists in the U.S. industry to move slowly on removing our own tariffs and/or raising TRQ limits.

State Trading Enterprise's. The New Zealand Dairy Board, along with the Canadian Wheat Board, will continue to be attacked by U.S. trade interests for lack of transparency and possible price discrimination. Proposed changes altering the Board's complete monopoly status may defuse this issue somewhat.

NAFTA. U.S. exports to Mexico continue to grow. Canada's level of domestic support compared to ours and its consequent lack of market access remains a sore point. Changes are likely to be slow in coming because of political realities - Quebec has half of the nation's milk quota.

Standards of Identity. The FDA is currently considering a request from the National Cheese Institute and two other national food processing groups to allow the use of dried milk proteins from ultra-filtration to be used in cheese production. This would be consistent with international standards of identity. Producers oppose the change because it would allow subsidized exports of milk proteins to displace domestic milk in cheese production. Unspecified food safety concerns have also been raised with respect to ultra filtration derived proteins. Ultra filtration removes water and some sugars from milk, which reduces transportation costs and facilitates the use of milk in cheese processing.

In summary the road dairy trade negotiations will travel will be long and bumpy. More troubling, nobody is quite sure where the road to further liberalization will lead, except that Japan, the EU and Canada will be sure losers, and Ocean, the sure winner.