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Feedlots are becoming more common in Japan, but the average cattle raising enterprise is still only 8-10 animals.



John Dyck

# IT WILL BENEFIT AMERICAN AGRICULTURE

by William T. Coyle  
and John Dyck

Japan's liberalization of beef imports will probably benefit U.S. beef exports, not hurt them as Alston and his associates suggest. Therefore, past U.S. pressures on Japan to effect these changes make sense not only in the context of more general trade negotiations, but also in terms of U.S. producer interests. This expectation is consistent with U.S. experience when Japan has liberalized trade of other U.S.-targeted products.

## Look at the Record

The immediate effects of Japan's lifting quota and other trade restrictions on farm products usually have been either a modest rise or decline in the U.S. share (except in the case of pork) but a rise in U.S. exports of the products to Japan (table 1). We have no reason to believe that the U.S. experience with beef will be any different.

The elimination of the Livestock Industry Promotion Corporation's (LIPC) trade restricting role and the use of tariffs rather than quotas will mean that, in contrast to the past,

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market forces will have substantial effects on the amount of beef imported and whether it is U.S. beef. The number of Japanese making decisions about imports will increase as marketing channels become freer and more diverse. The opportunities that develop in Japan will not go automatically to one country or another. The United States and Australia are both well positioned to supply different types of beef to Japan; success will go to those suppliers who seize the opportunities, who develop and market products demanded by Japanese consumers.

## The Challenge to Market

What kind of beef will the Japanese consumer want as trade restrictions are relaxed and prices fall? Some argue that they will continue to prefer a well-marbled product such as Japan produces; this would favor grain-fed beef, the specialty of the United States. Others say that as beef consumption increases, health-conscious Japanese consumers will prefer a leaner beef; this would favor grass-fed beef, the specialty of Australia and New Zealand. We expect imports of both types of beef to grow.

Future shares of Japanese beef imports will depend on how the U.S. and foreign beef industries tailor and market their products. The competition should intensify. For example, Australia could become more of a competitor in grain-fed beef by putting more cattle on feed. The United States could compete better by increasing its supply of chilled beef to Japan. The U.S. Meat Export Federation plans to spend \$7-8 million in Japan this year, while the Australian Meat and Livestock Corporation will spend

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### Japanese Liberalizing of Imports Helps U.S. Trade

Commodity	Year of quota removal or other policy changes	U.S. import share		U.S. import volume	
		5 yr. avg. before	5 yr. avg. after	5 yr. avg. before	5 yr. avg. after
		Percent		1,000 mt	
Soybeans	1963	92	82	1009.4	1666.2
Lemons	1964	100	100	3.3	29.7
Grapefruit	1971	100	94	1.5	121.7
Pork	1971	67	30	9.2	33.4
Grapefruit juice	1986	92	91*	6.81	24.1*
Cigarettes	1987	91	95**	98.5	596.2**

\* Average for 2 years.

\*\* Average for 2 years.

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\$8 million to differentiate and promote "Aussie Country Beef."

Prospects also will be affected by Japan's investments in other countries. Since the signing of the agreement, Japanese investors have invested \$50-100 million in the U.S. beef industry, including some feedlots. They have also reportedly purchased one-third of Australia's feedlot capacity and about 15 percent of its processing capacity. There have been similar Japanese investments in Canada and New Zealand. These investments reflect, at least in part, the intent of Japanese companies to position themselves for the emerging opportunities that they foresee in the Japanese beef market. In the end Japanese know-how and capital will help tailor U.S., Australian, and other beef for the Japanese consumer.

### Important Questions

In spite of their criticism of the U.S.-Japan liberalization agreement, Alston and his associates recognize that U.S. beef producers will gain in the short and long runs if for no other reason than that world prices will rise. These higher prices would adversely affect U.S. consumers; whether this outweighs producer gains is an empirical issue that needs more work. We do not believe, however, that it would be good trade policy to avoid changing a highly distorting system because it provides a degree, probably slight, of subsidy to U.S. consumers. In removing trade-distorting policies in the developed market economies, consumer prices will rise in some instances and decline in others.

Alston and his associates emphasize the following four points, in questioning whether the 1988 U.S.-Japan agreement serves U.S. interests:

- Japan's beef quotas would have grown briskly with a continuation of the quota system, so that the increase in imports due to liberalization may be small.
- Since past import quotas were managed to favor U.S. interests, in their absence U.S. performance will be adversely affected.
- This observation about favoritism to the United States is supported empirically by an Australian study.
- The Japanese approach to beef offals is a loophole designed to give the United States a competitive advantage.

We take issue with each of these points.

### Rapid Growth With Quotas?

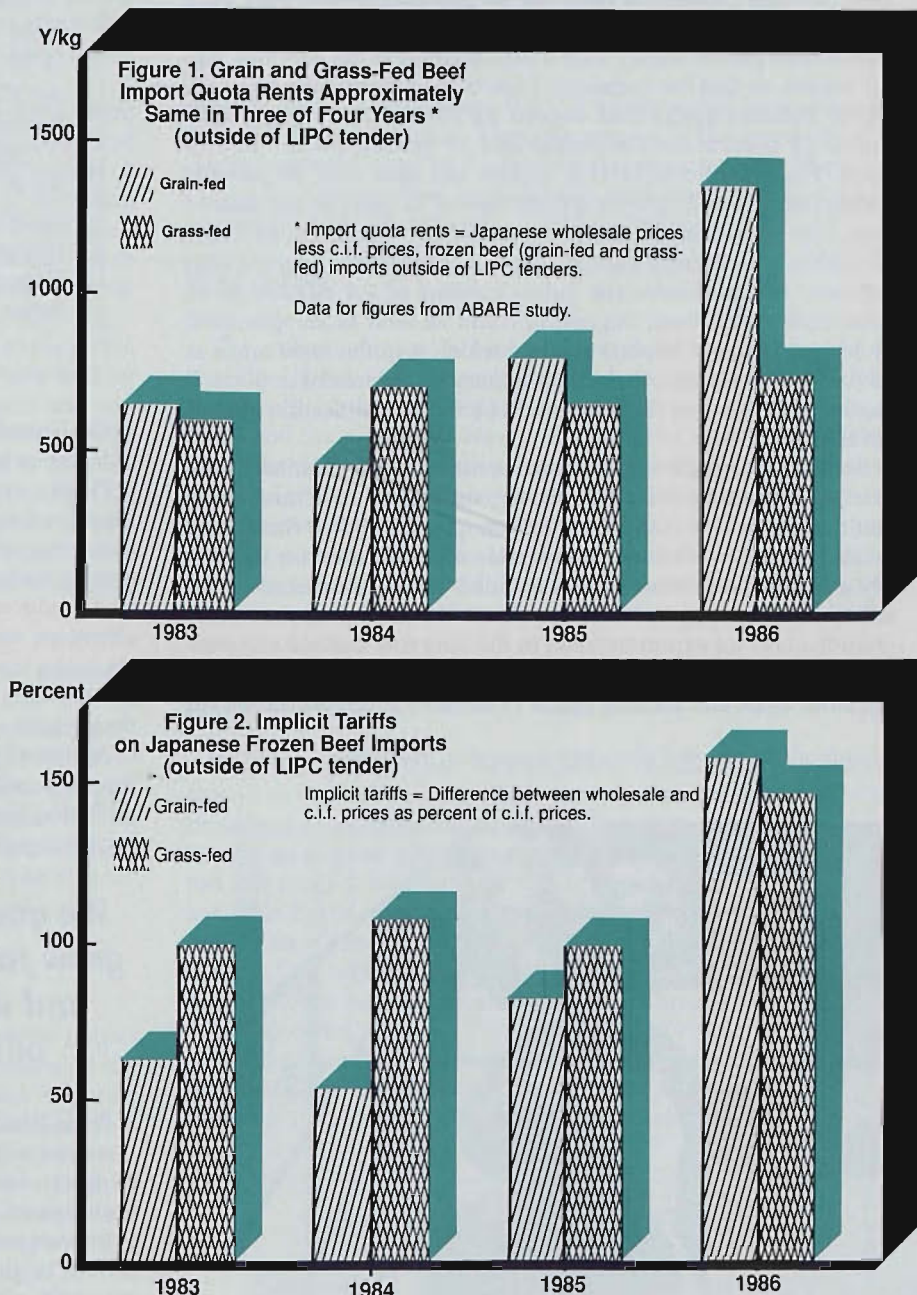
The authors are right that Japanese beef imports have grown quite rapidly over the past 20 years under a quota system. But to assume that the Japanese would continue to expand quotas rapidly into the future is questionable. The administration of quotas is susceptible to political whim and would present the market with great uncertainties about changes due to political factors. In 1974, for example, Japan cut off beef imports almost completely because of a severe cost-price squeeze in its livestock sector. This had severe adverse consequences for Australia's infant

beef feedlotting industry. There have also been periods when quotas were held virtually constant, as in 1979-82.

Quotas restrict markets in many, individually minor, rather unpredictable ways. They inhibit long-run planning and efficient trade. Without them, the Pacific Rim beef industry will be able to develop on a sounder, ultimately more stable basis, in Japan, as well as in North America and Oceania.

### Managed Import Quotas

The authors argue that the rising U.S. share of Japanese imports "does not seem to stem from U.S. comparative advantage." Rather,



imports were managed to favor the United States. But the fact that the United States is a net importer is not adequate evidence that it cannot compete in the Japanese market. Beef is a differentiated product; some countries specialize in grass-fed beef, some in grain-fed beef. Even Japan, a large net importer of beef, will likely export small quantities of its high-quality beef in the future.

Differences in the U.S. and Australian beef industries and their

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resources mean that rather than compete head-on the United States and Australia are likely to compete for different segments of Japan's beef import markets. The United States benefits from an efficient, well-developed marketing infrastructure, a widely-accepted grading system, and abundant supplies of feed. It specializes in exports of grain-fed beef. However, the U.S. industry has tended to consider overseas markets as residual to its domestic market. Therefore it has paid less attention to export marketing issues such as the apparent preference for chilled beef over frozen beef in Japan.

On the other hand, the Australian beef industry benefits from cheaper pasture and forage, greater experience in exporting chilled beef, and somewhat closer proximity to the Japanese market. It specializes in exports of grass-fed beef. But its internal marketing system is less efficient, its grading system is not well established, and its feed grain supplies are not stable. The unreliability of its feed supply could be particularly important if Australia were to shift more of its resources into feedlotting beef.

There are reasons other than favoritism that might explain U.S. past U.S. successes in the Japanese market. And they bode well for U.S. prospects under liberalized trade conditions. Import unit values for U.S. beef relative to Australian beef have declined over the years. This decline may have accounted at least partially for Australia's declining share of Japanese beef imports. The rising U.S. share and declining Australian share of the Japanese beef market began to manifest themselves in the early 1970s. This was before the first U.S.-Japan beef agreement in 1977 and at a time when U.S. trade deficits with Japan were not an issue.

The authors acknowledge, in passing, the plausibility of a higher income elasticity for grain-fed versus grass-fed beef as an economic argument to explain the rising U.S. share. They should have given it more attention rather than accept a thesis of discriminatory quota management on behalf of U.S. exporters. The authors fail to consider that Japanese interests (traders, butchers' guild, and producers) might be the principal beneficiaries and reasons for the quota system. It is far more likely that the quotas were managed with these powerful Japanese interests in mind than to placate U.S. interests.

## Favoritism

The authors' view that the Japanese use "discriminatory import quotas" to favor U.S. beef is based in part on the results of the ABARE study. (Australian Bureau of Agricultural and Resource Economics (ABARE), *Japanese Beef Policies: Implications for Trade, Prices, and Market Shares*, 1988.) It concludes that two conditions—large profits for traders and the associated lower implicit tariffs for grain-fed beef imports outside of direct LIPC control—led to private traders' preference for grain-fed beef. The study is meticulous in its examination of price data for different cuts of beef in the Japanese market. However, it is flawed because the wholesale prices for grass-fed and grain-fed beef imported outside of LIPC tender are not actual price quotes. Yet they are critical to calculating the quota rents and the implicit tariff levels. Instead, the wholesale prices were constructed by matching the import prices of non-LIPC beef with import prices of LIPC beef (of different cuts and types) and then by applying the protection level of that beef to the import prices of the non LIPC beef. There is no assurance that these proxy prices are related to the actual wholesale prices of the non-LIPC beef.

Even if the ABARE proxy wholesale prices were accepted, an unequivocal conclusion of preferential treatment for U.S. beef is not warranted. The data cover only 4 years; in one of the years, rents for grass-fed beef exceeded grain-fed beef and in another the implied tariff level for grain-fed beef was higher than for grass-fed beef. Moreover, the calculated differences in quota rents and implicit tariff levels are hardly large enough to suggest that in the

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absence of the quota system, the U.S. share would be profoundly different (figures 1 and 2). Thus, we agree with the conclusions of Harris and Wahl, cited by Alston and his associates, that liberalization of the Japanese beef market would most likely lead to modest, not radical, U.S. share changes in either direction.

## Beef Offals

The authors portray the beef offal 'loophole' as a clever effort to give the United States a competitive advantage. Admittedly, John Longworth (author of *Beef in Japan*, University of Queensland, 1983) and the Australian Meat and Livestock Corporation (AMLC) assert that U.S. grain-fed diaphragm beef substitutes for Australian grass-fed beef in Japan. However, this assertion is inconsistent with price relationships. Import unit values for U.S. beef offals are more than 50 percent higher (in 1987) than Australian beef and about the same as U.S. quota beef. U.S. beef offals might be substituting for U.S. quota beef rather than Australian quota beef. In the absence of research, we cannot say for sure.

## In Summary

From our perspective, liberalization of the Japanese market should be viewed as a significant trade policy breakthrough with important implications for the U.S. beef industry over the next decade. In contrast to the position of Alston and his associates, we feel that the U.S. beef industry should directly benefit, as it already has, from the opening of the Japanese market. As market principles replace state control, competition will increase. While we believe that the U.S. beef industry is well positioned to compete in Japan, it will have to be aggressive and pay closer attention to marketing to be successful.

In essence, we find the evidence casts a more optimistic light on the possibility, not necessarily the certainty, of successful U.S. performance in the liberalized Japanese beef market.

## Definition of Quota Rents

Quota rents are extra profits that accrue to quota holders. This rent is the "difference between the wholesale price and the price paid by the importer." In Japan, the wholesale price is artificially high because of the trade-restricting effects of the import quota system. The quota rents are an implicit tax on consumers and represent a redistribution of income from Japanese consumers to quota holders (from page 3 of ABARE study).