Beef at the Border:

Here's the Beef

The U.S. requires country-of-origin labeling for beef imports, but processors aren't required to maintain that designation through to consumers. Is that helping or hurting?

by Gary W. Brester and Vincent H. Smith

Section 304 of the 1930 Tariff Act mandates country-of-origin labeling for most products imported by the United States. However, some agricultural products, including livestock and several "natural" products such as fruits, nuts and vegetables, are exempt from existing U.S. country-of-origin labeling requirements.

Exempt products are generally those frequently combined with similar domestic products during processing and marketing. This is common in the beef industry where domestic fed beef cattle and imported fed beef cattle and carcasses are jointly processed in packing plants and other downstream processing operations.

In 1998 and 1999, concerns about low domestic cattle prices and the effects of imports on those prices stimulated renewed interest in removing livestock from the list of commodities exempt from country-of-origin labeling. Several legislative proposals requiring such labeling were introduced in Congress in 1999.

For non-exempt products, including processed livestock products, current country-of-origin labeling legislation requires listing the origin (country) of imported products throughout the marketing system until the product is acquired by an ultimate purchaser. Defining the ultimate purchaser of an imported commodity is critical for beef and beef by-products. The ultimate purchaser is not necessarily a product's final consumer. Rather, it is the last entity to receive the product in the form in which it was imported. Thus, if a domestic firm purchases a beef carcass and subsequently transforms it into a processed product such as beef entrees for frozen dinners, the frozen dinners would not need to be identified as imported. Conversely, a product whose characteristics are only moderately altered by processing, such as imported broccoli that is cut and packaged, is typically required to be identified by country-of-origin. Existing labeling rules suggest that table cuts such as steaks and roasts fabricated from imported beef carcasses could have to be identified by country-of-origin because the imported product is not being dramatically altered by processing. However, ground beef obtained from imported carcasses and/or trimmings could be viewed as a substantially altered product and not be subject to current country-of-origin labeling rules.

Country-of-Origin Labeling

Under the provisions of GATT, country-of-origin labeling is permitted as long as the same rules are applied to imported products from all WTO member nations. In addition, under the 1994 GATT (Article III - 4), imports must be treated no less favorably than domestically produced products; that is, domestic producers must also be subject to similar labeling requirements.

Country-of-origin labeling is also permitted under NAFTA. However, such labeling has to be maintained only until a commodity reaches the "ultimate purchaser" which, as noted above, is the entity that purchases the product in, or close to, the form in which it enters the country. The compatibility of any given country-of-origin labeling requirement with GATT and NAFTA is, therefore, a question of legal interpretation that is often resolved on a case-by-case basis.

Some countries currently require country-of-origin labeling for meat imports. Since July 1, 1997, Japan has insisted that all meat imports be labeled by country-of-origin. The European Community has adopted a compulsory country-of-origin labeling system for member states. The United States requires that beef imports be labeled by country-of-origin when entering the country. However, the meat processing sector is not currently required to maintain country-of-origin designations through the marketing chain to consumers.

Defining the "ultimate purchaser" of an imported commodity is critical for beef and beef by-products.

U.S. Imports of Beef

The potential scope of country-of-origin labeling requirements with respect to beef imports is quite extensive, both in terms of the countries and types of beef product imports that would be affected by such requirements. The United States imports lightweight feeder cattle from Mexico (which are subsequently finished in U.S. feedlots), trimmings and ground beef from Australia and New Zealand, and a mix of high-value table cuts, manufacturing/trimming beef, live fed cattle, live cull cows and bulls, and fed cattle carcasses from Canada. Imported beef is inspected and must meet food safety standards equivalent to those for domestically-produced beef products. Beef imported as live fed cattle or as carcasses is eligible for U.S. Department of Agriculture (USDA) quality grades.

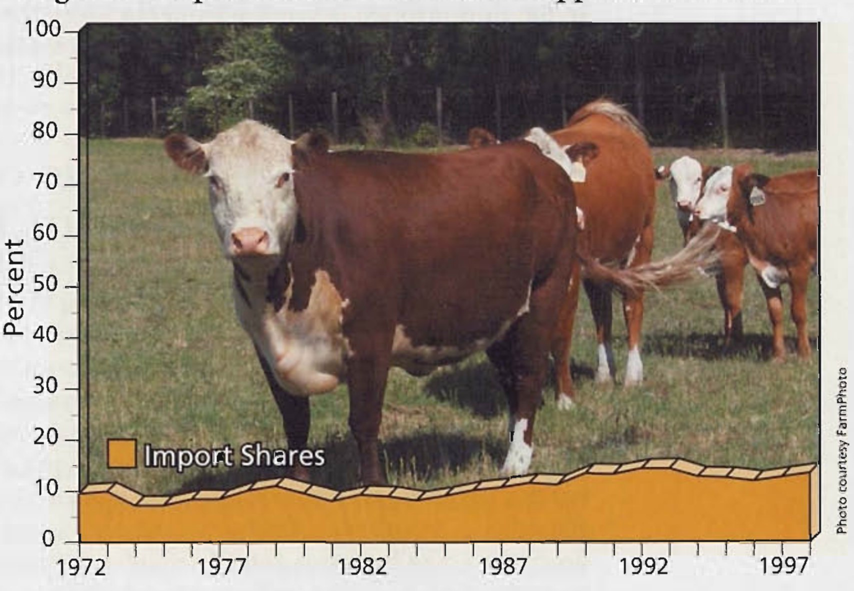
In 1998, beef imports from all sources represented 13.7 percent of total U.S. beef supplies (figure 1). The 1998 import market share is similar to the 1990 and 1991 shares, and slightly less than the 1992 and 1993 market shares (Brester and Marsh). Figure 2 illustrates the composition of U.S. beef imports from all sources. In 1998, just over 51 percent of all beef imports consisted of trimmings and manufacturing grade beef which are ground into hamburger. Live fed cattle imports, obtained almost exclusively from Canada, represent slightly more than 26 percent of U.S. beef imports. These animals are slaughtered in U.S. beef packing plants and, like domestic fed cattle, produce high-quality table cuts, ground beef, and by-products. In general, ground beef produced from these animals is consumed domestically. Table cuts may be consumed domestically or may be exported. Most by-products are exported to Pacific Rim countries. In 1998, approximately 10 percent of U.S. beef imports were table cuts imported from Canada as boxed beef or beef carcasses; almost 7 percent of beef imports were prepared and preserved beef products; and the remaining 5 percent were feeder cattle imports.

Labeling Benefits

Country-of-origin labeling would enable consumers to choose U.S.-produced beef if they have a preference for domestically-produced products, and there is some evidence that they do. A recent consumer survey conducted for the National Cattlemen's Beef Association (NCBA) indicated that 76 percent of U.S. consumers support country-or-origin labeling for meat. Furthermore, the survey results indicate that 91 percent of consumers said they would choose beef products labeled as "Product of the U.S." over similar products labeled as "Product of .... Canada, or Australia, or New Zealand." Only 6 percent indicated that they had no preference among these choices.

Empirical evidence about the effects of country-of-origin labeling with respect to other commodities on consumer attitudes towards product quality and willingness to purchase is mixed. Johnson and Nebenzahl examined the impact of country-of-origin identification in the automobile industry and reported that consumers used such information as an indicator of automobile reliability.

Figure 1: Import Shares of U.S. Beef Supplies, 1972-1998



Source: Livestock Marketing Information Center and Montana State University Trade Research Center

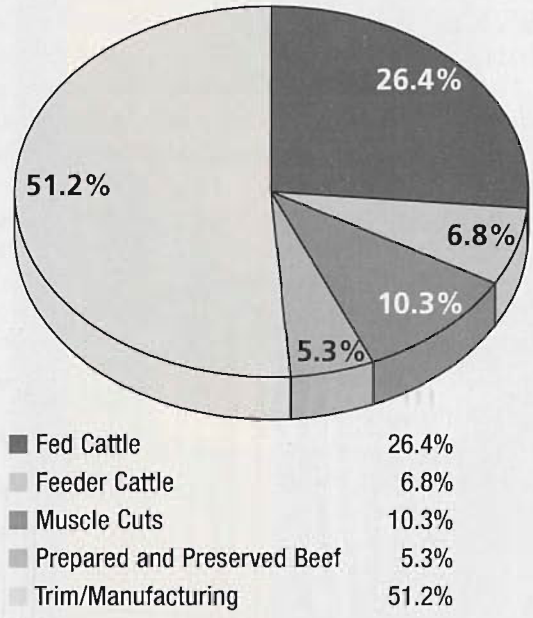
Conversely, Davis, Kern and Sternquist, examining consumer preferences for textile products, found no evidence that country-of-origin labeling had any effects on either consumer perceptions of product quality or consumer estimates of the value of otherwise identical items of apparel. The results of these studies suggests that country-of-origin labeling may affect consumer behavior only if a product has an independently documented quality difference, as Johnson and Nebenzahl reported to be the case in the 1980s with respect to automobile reliability. Thus, as with brand names, country-of-origin may be particularly important to consumers if associated reputation effects exist.

U.S. consumers might also prefer information regarding country-of-origin if or because U.S. beef products are superior to imported beef products. Recent research suggests that Korean hotel and restaurant industry officials and managers consider U.S. beef to be superior to Canadian and Australian beef (Unterschultz, et al.). If similar preferences are prevalent among domestic U.S. consumers, country-of-origin labeling could increase U.S. demand for domestic beef. In the short term, this could lead to higher U.S. beef prices, although over the longer run those price increases would be mitigated by increased domestic beef production.

It is also conceivable that country-of-origin labeling could stimulate the beef industry to develop and promote additional branded beef products. Such a move could increase beef quality by rewarding producers of higher-quality beef animals with higher prices. However, branded product distribution systems are likely to be more expensive than commodity distribution systems and may cause producers of lower-quality beef animals to exit the industry.

Figure 2.

Composition of 1998 U.S. Beef Imports (carcass weight basis)



Source: Montana State University Trade Research Center

Labeling Costs

The disadvantages of country-of-origin labeling relate to the costs involved in implementing such a system. Although the NCBA survey of consumer attitudes toward country-of-origin labeling indicated that U.S. consumers favor labeling, the study does not indicate how much consumers are willing to pay for such information. A USDA pilot study of the costs (and benefits) of country-of-origin labeling was scheduled for completion in April 2000.

Labeling costs are likely to vary by product.

Labeling costs are likely to vary by product. For example, country-of-origin labeling of feeder cattle imports might be relatively expensive given recent evidence from the Restricted Feeder Cattle Program (formerly called the Northwest Pilot Project). The program is a regulatory action which significantly lowers health restrictions and costs of exporting feeder cattle to Canada from selected States. This program, as implemented in the fall of 1998, eliminated certain sanitary requirements that had effectively prohibited U.S. feeder cattle exports to Canada from Washington and Montana (two brucellosis-free states). Prior to implementation of the Northwest Pilot Project, U.S. feeder cattle had to be segregated from Canadian cattle and were restricted to a limited number of Canadian feedlots (Young and Marsh). These restrictions apparently imposed unacceptably high costs on Canadian feedlot operators as very few feeder cattle were exported under this arrangement. However, when this restriction was lifted in the Fall of 1998, feeder cattle exports to Canada increased from 51,000 head in 1998 to 105,000 head in 1999. Country-of-origin labeling requirements for U.S. imports of Canadian feeder cattle could potentially result in similar costs for U.S. feedlot operators.

Requiring segregation of animals throughout the U.S. slaughtering process could also be relatively costly if it interferes with slaughtering or fabrication line speeds. Packing and processing plants rely on steady line speeds to minimize production costs. Interruptions caused by varying import supplies and associated inventory management problems are likely to be costly, although little evidence is available on the magnitude of such costs. Similarly, country-of-origin labeling of beef trimmings and

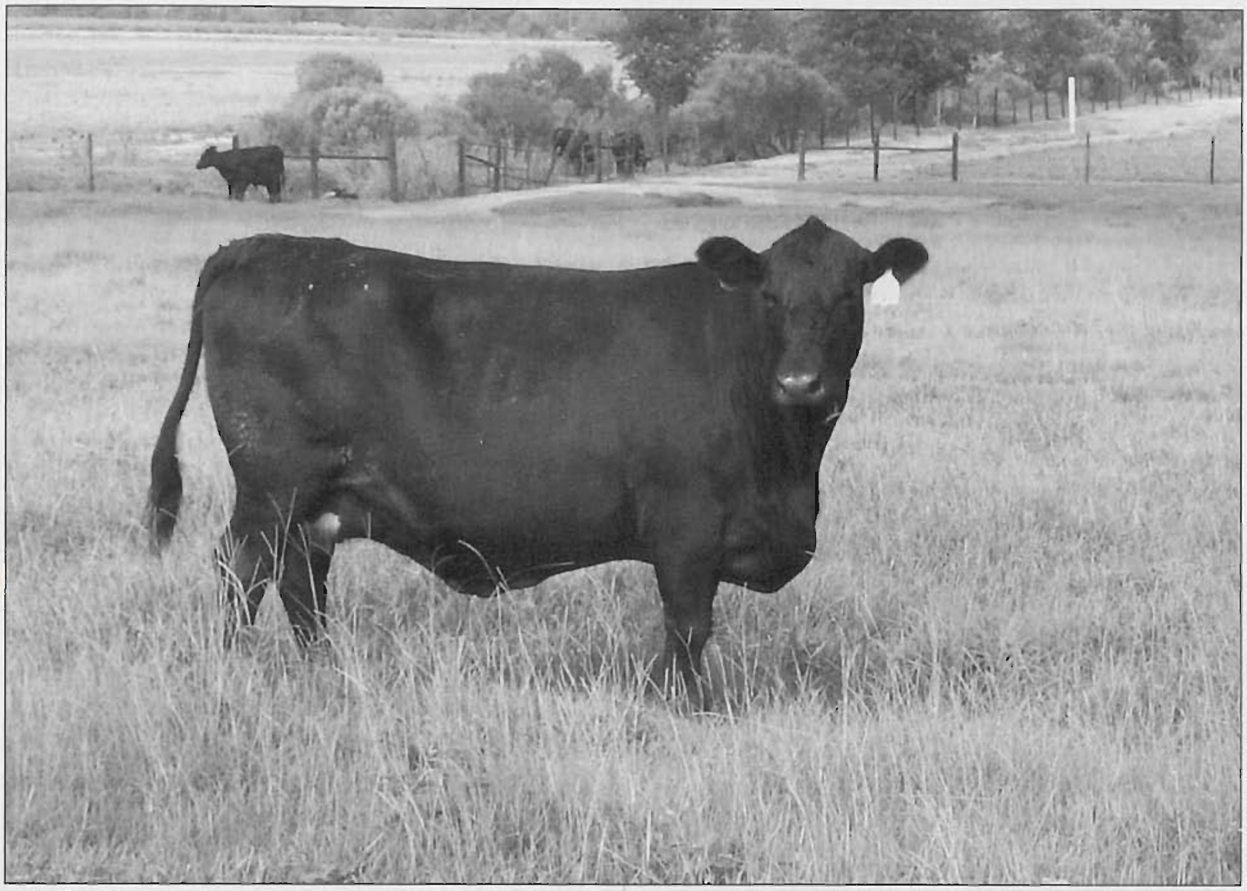


Photo courtesy FarmPhoto

manufacturing beef would be difficult given that these imports are often combined with U.S. beef in the production of ground beef for the retail and restaurant markets. However, it is possible that some plants could minimize such costs by specializing in the slaughtering and fabrication of imported beef.

The labeling of imported ground beef and processed and preserved beef products could be less costly for those products that maintain their identity through the entire marketing chain. Nonetheless, labeling costs could be significant if mandatory country-of-origin labeling were required through the hotel and restaurant sectors, which account for approximately 40 percent of domestic beef consumption in the United States.

Another potential cost relates to food safety concerns arising from pathogenic-induced problems such as *E. coli* or Lysteria contaminations. Such problems cause consumers to shun identified products, at least temporarily. Under country-of-origin labeling, food safety concerns may become associated with a specific country's products, resulting in lost market share and adverse price affects. Many beef-related food safety hazards are not country-of-origin specific as they tend to develop during the processing and meal preparation stages. Of course, some are country specific, as was demonstrated during the 1990s by the outbreak of bovine spongiform encephalopathy (BSE or Mad Cow disease) in the British beef and dairy herds. To the extent that food safety hazards do occur in the processing and meal preparation stages, the likelihood of any given country's beef products being associated with a food safety problem is approximately proportional to its market share. Given that U.S.-produced beef accounts for over 85 percent of U.S. beef supplies, U.S. beef is more likely to be associated with any given food safety or contamination incident.

Another issue concerns country-related differences in product quality and consistency. Alchian and Allen argue that countries are likely to export higher-quality products within a given commodity group in order to reduce the proportional effects of transportation costs. Therefore, regardless of the average quality of beef in the United States and other countries such as Canada, the average quality of U.S. beef imports could exceed the average quality of domestically-produced beef. Moreover, even if the quality of imported beef is similar to that of U.S. beef, the quality of Canadian beef may be more consistent than U.S. beef. The colder Canadian climate is not conducive to the production of a wide range of cattle breeds. The wide range of climates in the U.S. allows for the production of many cattle breeds which contribute to quality variations (Anderson, Mintert, and Brester). If this is indeed the case, some U.S. consumers may prefer the consistency of imported Canadian beef to U.S. beef.

Finally, beef competes with other meats and fish (for example, poultry, pork, lamb, and salmon) for consumer food expenditures. If costs associated with country-of-origin labeling are relatively high, U.S. beef producers may lose market share to other meat and fish products.

These effects could offset potential U.S. beef market share increases induced by country-of-origin labeling.

A Two-edged Sword

Country-of-origin labeling for beef appears to be a two-edged sword. It has the potential to benefit U.S. beef producers if consumers have country-of-origin preferences. In addition, if country-of-origin labeling can be accomplished at relatively low costs, consumers may also benefit from information that assists them in making more informed choices. However, if country-of-origin labeling costs are relatively high, beef products might lose market share to competing meats. Moreover, the quality of Canadian beef may be more consistent than U.S. beef, because northern climates allow the production of a narrower range of cattle breeds (Anderson, Mintert, and Brester). If so, U.S. consumers may prefer imported Canadian beef.

Finally, participants in the U.S. beef marketing system are not currently prohibited from labeling beef as being "domestically-produced" in order to capture price premiums associated with presumed consumer preferences for domestically-produced products. The current lack of such labeling on a large scale suggests that associated price premiums may not exceed the additional costs of this marketing alternative. ■

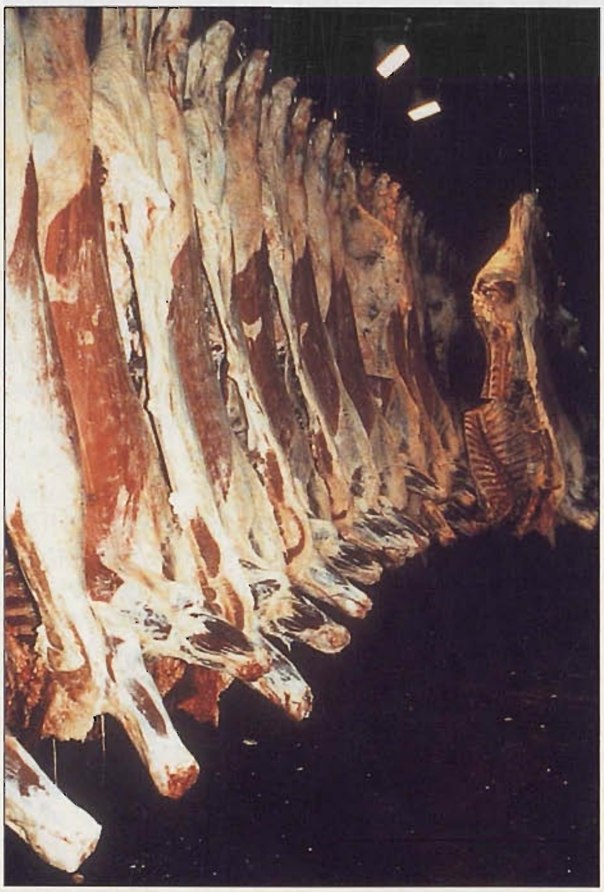


Photo: United States Department of Agriculture

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