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Agricultural
Outlook
Conference

United States
Department of
Agriculture

Dec. 3-5, 1985
Washington,
D.C.



Need For Freer Trade: Grains

By

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at the

Annual Agricultural Outlook Conference

December 5, 1985

Washington, D.C.

U.S. grain farmers can produce 50 percent more grains and oilseeds than the United States can consume. With production capacity growing at least twice as fast as domestic demand, they will reach a point in this century when they can produce twice America's domestic needs.

So, U.S. grain agriculture must export to be a dynamic, growth-oriented sector of the American economy.

While our need for exports is clear, recent events have called into question whether the export market can grow to meet that need. Does the world need America's grain? Can the United States compete against newly emerging suppliers? Can that competition be put on an economic footing, largely free of import barriers or export aids?

Those are the three questions I would like to address in discussing U.S. grain agriculture's need for freer trade.

Is the Market There?

The first question is: Does the world need America's grain? Is there still a market out there?

ANNUAL AGRICULTURAL OUTLOOK CONFERENCE
USDA • DECEMBER 3-5, 1985 • WASHINGTON, D.C.

There is a market, but it is neither the market that ran away from our capabilities in the early 1970s nor the shrinking market of the early 1980s. Rather, it is a market that requires flexibility and foresight to achieve its potential.

The U.S. grain economy has learned since 1980 that it is not recession-proof. World grain use has fallen below trend since then. This is not a pattern likely to be sustained forever, but it has dealt a real blow to farmers' and exporters' expectations.

Exports have felt the brunt of this slackening in the growth curve for a variety of reasons. At the top of that list must be customers' fears of uncertain supplies or skyrocketing prices. These fears came out of concerns about a "food crisis" in the early 1970s. They motivated many importers to shift towards greater self-sufficiency, even at relatively high cost.

Moreover, a general collapse in commodity prices and shrinking export opportunities have sharply reduced the buying power of many developing countries. Their burdensome debt loads added further pressure to curb imports.

As a result, total world grain trade has declined modestly since 1980 after doubling in volume during the 1970s. This stagnation is reversible, however.

Sustained economic growth, more stable foreign exchange rates, ample grain supplies at competitive prices, freer trade policies and reductions in the debt overhang can rekindle both demand growth and reliance on imports. In other words, export opportunities are still present, if the policy environment is adjusted.

What can result in these circumstances is not a demand explosion fueled by inflation and easy credit, as was the case in the 1970s. But, we can look forward to an environment in which population and income growth can build healthy demand expansion. World grain demand could grow at 1.5 billion bushels per year. Such expansion offers good growth opportunities for exporters prepared to serve it.

Can the U.S. Compete?

This leads to the second question: Can the United States compete economically against other potential suppliers of this demand? The answer is, yes it can.

Let's look at that competitive marketplace. During the 1970s, world grain trade grew faster than world grain

consumption. The share of world grain use met by imports grew from 9 percent to 14 percent. In other words, exportable supplies grew faster than domestic production in importing countries. We too often overlook the fact that our competition, at the margin, is really local agriculture in importing countries, not other exporters.

Local grain producers, especially in rapidly developing economies, typically face large hurdles in expanding their output as fast as local demand. Achieving self-sufficiency goals becomes increasingly unrealistic, economically and physically.

As local consumption growth outstrips local production, the impact on exports is dramatic. A multiplier effect occurs because exports are a relatively small, residual market compared to total world use. For example, U.S. exports represent only about 7-8 percent of total grain use outside of the United States. So, a one percent jump in non-U.S. demand can translate into a 12 percent growth in demand for U.S. exports. This suggests the magnitude of the opportunity, if the United States can be the preferred supplier to this residual demand.

To be that preferred supplier, the United States must beat other exporters to the business. Since 1980, we have not done well in that competition. U.S. exports of wheat, feed grains and soybeans have fallen 17.5 million tons while our competitors' exports in that period rose 16.5 million tons. Can we meet that competition--and beat it?

We have the economic edge, if our price support policies will allow it to work. Cargill recently completed a study of production and marketing costs in the United States and in other major exporting countries. Several conclusions emerged.

First, U.S. variable or incremental costs of producing wheat, corn and soybeans are generally lower than those of our major competitors. Second, our marketing costs--the costs of putting grain into export position--also are lower. Combining these two, the United States can put additional bushels into export position cheaper than any other exporter. Only Argentina could challenge this position by eliminating its export taxes, but then, it would have to find other sources of revenue to fund government services.

Current U.S. price support policies, however, are negating this advantage. They are guaranteeing prices for our competitors in excess of their total exporting costs--variable production costs plus land costs plus

marketing costs. In effect, our loan levels are guaranteeing profitable returns to our competitors' investments in new export facilities, expanded acreage or more intensive cultivation. Small wonder that they have been expanding at our expense since 1980.

The point of this analysis is not that the U.S must lower its loans to variable-cost levels. The point is that lowering loan levels below our competitors' total costs of export will discipline them much more than us. We have idle land and idle handling capacity that we can bring on stream at low cost. Our competitors are producing and exporting at capacity. They must make further capital investments, if they wish to expand. We can slow down--and in some cases stop--competitive expansion by exposing them to the threat of strong U.S. competition at levels that do not justify investments in expansion.

Again, the important point is that the United States can expect to be successful in competing for additional world grain import demand, if its own policies permit it. Market-oriented U.S. loans would force competitors to evaluate future expansion not against a guaranteed return but against the very real risk that they will bear large losses from uneconomic expansion.

In that environment, the United States could expect to be the preferred supplier to rising import demand. It would gain in two ways. It could expect to increase its market share, as it did under similar policies in the 1970s. At the same time, it could expect that market prices would actually rise to profitable levels as surpluses are worked off. The reason is that uneconomic foreign expansion would then become self-defeating rather than automatically profitable, as it is now.

Can the U.S. Achieve Freer Trade?

But, even if economics are on our side, will trade policies--here and abroad--permit a freer flow of goods? The drive for freer trade currently seems hemmed in on all sides--by unfair export competition, by barriers to imports and by a general drift toward protectionist feelings.

The problem of unfair export competition is in part reality, in part perception. The GATT rules governing agricultural export subsidies clearly are looser than for manufactured goods. GATT dispute settlement-mechanisms make enforcement even of these loose rules questionable. The European Community has exploited this situation to America's disadvantage. Particularly disturbing is the absolute protection the Community's export subsidy

provides. The EC increases it to whatever level it takes to make sales.

Beyond the Community, however, the evidence of unfair competition becomes more frail. Canada provides a rail transportation subsidy, and there may be small export aids scattered among other countries. But two of the fastest growing challengers--Argentina and Brazil--actually tax their exports at significant levels.

Import barriers to grains, on the other hand, are real, sizable and widespread. Perhaps of greater concern, these, too, tend to provide absolute margins of protection. No price level buys the business, at least in the short run. For example, the European Community has guaranteed high prices to its farmers, fully protected by variable import levies. Between 1978 and today, such agricultural protection resulted in a 40-million-metric ton swing in its net grain trade. It moved from a 20-million-ton net importer to a 20-million-ton net exporter in that period.

Unfortunately, other countries are copying this example. Japan, Korea and Taiwan are major markets for U.S grains. Between 1974 and 1984, their coarse grain imports from the United States grew from 15.3 million tons to 28.2 million tons. This is good business, which we appreciate.

Yet in the same period their degree of agricultural protection increased. Their coarse grain imports from the United States would have grown substantially more, if their degree of protection for domestic agriculture had declined rather than risen.

The overriding agricultural priority in future trade negotiations, therefore, has to be placing a limit on the degree of protection countries can provide their agricultures--both on export aids and on import restraints. By fixing a maximum degree of protection, it becomes possible to earn markets by price advantages. It also becomes possible to negotiate those margins of protection down over time.

There would be a bonus in this, as well. Doing away with absolute levels of protection will provide more stability to commodity prices. Secure supplies at stable prices would encourage more reliance on imports rather than expensive self-sufficiency policies in key markets.

The third hurdle in the way of progress toward freer trade is a growing pattern of protection and national preference in all economic sectors. The United States

has done better than most in resisting this disease, but it is gaining strength here as well.

Protectionist attitudes are easy to identify and oppose in one's neighbor, harder to deal with when one's own livelihood is affected. That is why unprecedented trade deficits and a strong dollar have proven so troublesome in sustaining America's traditional commitment to freer trade. They have made the tantalizing promise of protection attractive to more Americans than ever before.

U.S. grain agriculture is rightly concerned about this situation. It understands that trade must be a two-way street. We cannot sell more, especially to developing-country markets, while throwing up barriers to their exports to us.

As one example, U.S. agricultural exports to textile exporting countries affected by the so-called "Jenkins" bill were valued at \$13.5 billion last year. Whether that market continues to grow depends importantly on their access to U.S. markets for their exports. If that access is unduly restricted, their grain-import growth will slow. And, some of those countries could turn to other suppliers in an effort to make their point more clearly.

So, U.S. grain agriculture has much to gain from negotiating trade barriers down. It has much to lose by building barriers up to the goods our customers have to sell us.

Moreover, the solution for the workers, industries and communities hurt by imports does not lie in propping up failing causes. It lies in correcting the macro-economic policies that drive economies out of alignment. More cooperation along these lines can help contain the pressures that are currently straining the trading system while preserving the foundation for vigorous growth in the private sector. A U.S. economy that is growing and holding its own in world competition would provide ample room to accommodate the necessary shifts in economic activity caused by trade.

There is much the United States itself can--and must--do to bring this about. At the top of that list must be curbing federal budget deficits.

But, we no longer are either an overwhelming economic power or an island lying outside the major lanes of trade. Joint action is needed among the major trading nations to keep currencies in proper alignment, to

provide the demand stimulus for economic growth, to lighten the debt-servicing burdens of key developing countries and to open another round of negotiations aimed at trade liberalization and expansion.

No doubt, each of these tasks alone is challenging, and together they can seem at times overwhelming. It is tempting to accept the arguments offered for doubting the success of such cooperative efforts. It is tempting to harken to pleas that we take care of our own first.

But, such pessimism is neither justified nor wise. Compared to one or two years ago, we have made progress on currency issues, economic policy cooperation, LDC debt problems and launching another trade round. We may even be getting ready to address runaway budget deficits. Progress may be maddeningly slow, but it is occurring.

Conclusion

U.S. grain agriculture has a vital stake in sustaining this cooperative, liberalizing policy thrust. Its market growth lies abroad. That potential is large. Achieving that potential is blocked largely by ill-conceived protectionist policies--both in agriculture and industry, both here and abroad.

The grain sector of American agriculture has long been a strong voice for outward-looking, freer trade policies, for good reason. Those reasons are as compelling as ever. The voice needs to be as strong as ever.

Thank you.