

THE JAPAN CUSTOMS OIL TARIFF:  
IMPLICATIONS FOR TRADE IN CANOLA PRODUCTS

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INTRODUCTION

The purpose of this presentation is to outline the major evaluations and conclusions of a study entitled: The Impact of the Reduction or Elimination of the Japan Customs Oil Tariff on the Western Canadian Canola Industry. This study was commissioned by a research consortium composed of both industry and government participants. The study was undertaken by Landell Mills Commodities Study Limited with input from an industry appointed advisory group.

In the following presentation, the competitive impact and distortion of the tariff is examined based on the findings of Landell Mills. Although the study covers numerous topic areas, time requirements necessitate coverage of only the major and most pertinent conclusions. The authors would like to acknowledge the work of Landell Mills and the supporters of the study.

The Japan customs oil tariff is levied on all edible oils imported into Japan. At the time of the study, the tariff was 17 Yen/kg, equivalent to approximately U.S. 5112/tonne. At the time of this presentation the tariff is equivalent to 5122/tonne.

The impact of the oil tariff has created and continues to create controversy within the canola industry in Canada. Domestic crushers argue that the existence of the tariff means that vegetable oil prices in Japan are higher than world market levels and this permits Japanese buyers to bid up the price of canola seed, particularly during times of supply shortages. As a result, Canadian crushers, who are faced with selling their product at or near world market price levels have difficulty competing with the Japanese for seed. Consequently, Canadian crushing capacity is under utilized resulting in high processing costs and poor crushing margins. The frequent and significant losses experienced by domestic crushers estimated at \$150 million during the past approximate 15 years, serve as witness to the problem. On the other hand, Canadian canola seed growers are content as they believe that the existence of the tariff provides an assured market for their seed. They are concerned that if the tariff was removed unilaterally, canola seed sales to Japan could suffer and prices would be lower. Controversy in the industry stems from the capability of the Canadian crushing industry to replace lost seed sales with movements of oil and meal to Japan.

Canola Industry

Before discussing the Landell study, the following is a brief summation of major developments regarding the Canadian canola industry during the past decade:

- Production levels have ranged from a low of 1.8 million tonnes in 1981/82 to a record of 4.3 million tonnes in 1988/89.
- Crush volumes have vacillated between levels as low as 900,000 tonnes in 1982/83 to 1.6 million tonnes in 1987/88.
- Export levels have ranged from 1.3 million tonnes in 1982/83 to slightly over 2 million tonnes in 1989/90.
- Japan is the most important market for Canadian sales as the ratio of exports to Japan compared to total exports has been approximately 80%.
- Based on preliminary data for 1991, Canada's production and ratio to world output was as follows: Seed= 3.3 million tonnes (14%), Oil= 0.5 million tonnes (6%), Meal= 0.7 million tonnes (5%)
- In terms of processing, canola can be considered one of the most important grains particularly when considered within the context that approximately 35% of the product is crushed or refined in Canada. As a comparison, the ratio for wheat, barley, oats is under 7%.

#### Methodology

Methodology was based on the construction of a model to measure the likely or probable consequences of changes to the tariff structure and other market factors. The major features of the model involve the measurement of relationships or correlations amongst the factors of: oilseed prices, supply, demand and crushing margins in Japan and Canada, all within the context of the tariff and a hypothetical deletion of the tariff.

#### Benefit

The study concluded that the Japanese crushers enjoy a variable benefit from the import tariff. When oil prices in Japan are high, the crushers have available to them extra buying power not available to crushers operating at North American product price levels. For rapeseed (Table I), this has ranged from a low of US \$15 to a high of US \$54 per tonne of seed. Between 1986 and 1989, the tariff value ranged from a low of \$136 per tonne of oil to \$133 per tonne of oil for rapeseed oil.

#### Crushing Economics

Canadian crushing costs are dependant on capacity utilization (Table II). For the 1988/89, the difference between 50% use and 90% use was estimated at US \$26 to \$27 per tonne of seed processed.

Although Canadian crushing plants are smaller than that of the Japanese, at almost similar capacity utilization rates, total costs per tonne of crush were calculated to be less in Canada than Japan. In 1988/89 Canadian crushing costs were 30% less than in Japan (Table III).

For the period 1986 to 1989, the study calculated a base case for net crushing margins at a level of minus \$18.98 US per tonne (Table IV). Applying changes in the market, the study arrived at the following impact upon the net crushing margins of the industry.

- Increasing the capacity utilization rate to 100% reduces the net crush margin to minus \$4.09 or approximately \$15 less.

- A reduction of 20% in the seed price creates a positive net crushing margin of \$19.30 or an improvement of over 538.00 per tonne.
- An increase in oil price of 15% creates a positive net crushing margin of \$3.58.
- An increase in meal prices of 15% reduces the net crushing margin loss to \$7.61 per tonne.

#### Impact of Full Tariff Reduction

Based on the assumption of static growth for both oils and meals, the study arrived at the following long term projections in terms of Canadian exports to Japan (Table V).

- Canadian exports to Japan are estimated as follows:
  - \* Seed exports increase from 11.65 million tonnes to 1.69 million tonnes.
  - \* Oil export to Japan increase from 30,000 tonnes to 34,000 tonnes.
  - \* Meal exports to Japan decline from 125,000 tonnes to 112,000 tonnes.

#### Income Distribution Implications

The major conclusion of the study as indicated at the beginning of this presentation arrived at the following conclusions (Table VI):

- Under no tariff change with no consumption growth, producers are receiving benefits of 660 million dollars in the short term and 694 million dollars in the long term. For the crushers, the losses are \$30 million and \$7 million respectively. To the industry the benefits are \$630 million and \$687 million.
- Under full tariff elimination, producers acquire benefits of \$596 million in the short term and \$620 million in the long term. Crushers on the other hand sustain losses of \$7 million in the short term but achieve benefits of \$29 million in the long term. The impacts on the industry are \$589 million in the short term and \$649 in the long term.
- Gains and losses from full tariff elimination result in producers losing \$64 million in the short term and \$74 million in the long term. At the same time, crushers gain \$23 million and \$36 million. The impact on the total industry is losses of \$41 million and \$38 million.

#### Trade Theory/Analysis

Reviewing other studies regarding market impacts as a result of trade liberalization one begins to see some of the reasons why conventional trade theory appears to run counter to the recent research and projections. Reviewing one of the most comprehensive and widely used studies, regarding changes to agricultural policies in industrial market economies, one begins to see a possible explanation to the rational behind the Landell Mills calculations.

Entitled "How Level is the Playing Field", Ronnigen and Dixit of the USDA have developed an 11 region, 22 commodity world trade model which calculates the impacts associated with the elimination of protectionist agricultural policies. Some of the major conclusions of this study as related to world agricultural developments are projected as follows based on 1986/87 calculations:

- Agricultural trade for most commodities would expand if industrial market economies simultaneously liberalized their trade.
- Producer income losses for major developing countries could reach \$66 billion dollars with multi-lateral elimination in agricultural support.
- World price increases arising from free trade would not be sufficient to offset the loss of trade distorting government support.
- Liberalizing agricultural policies in all industrial economies would on average increase world agricultural prices by 22%. By contrast, world prices for oilseeds and products would increase by only 6%. World trade in oilseeds and oilseed products would increase by 14%.
- World oilseed and product trade balances change as follows: USA= \$400 million, Canada= \$200 million, EEC= -\$700 million, and Japan is unchanged.

#### Study issues and Questions

The results of the conclusions from the study by Landell Mills leaves the Canadian canola industry with a rather perplexing dilemma. There are two major aspects facing the industry. In the first instance, the study appears to turn trade theory particularly the benefits of market liberalization on its head. The basis of macro trade theory is that there are greater overall efficiencies and benefits to be obtained under conditions of free and open trade rather than under systems of protected industries, tariffs, and other trade barriers. The very basis of GATT and its subsequent successes or failures has been attempts to reduce trade barriers and encourage world trade flows. According to the study, the Canadian canola industry would obtain the greatest benefit by ensuring that the current Japan oil tariff remains in place.

Secondly, the conclusions of the study counter conclusions and actions regarding the major economic issue effecting economic development in Western Canada. Since the settlement of the Canadian West, the problems associated with economic growth have been identified within the context of a hinterland relying upon the export of raw materials with the accompanying need to develop processing and value added activities. Calculations within the study appear to counter activities which are at the core of western provincial diversification strategies. Thus, while maintaining the tariff would seem to have benefits for farmers, the canola processing industry is faced with negative consequences. On the surface it appears that canola farmers and processors can only profit at each others' expense. Difficult or impossible to identify is the balance wherein both farmers and processors are able to operate profitably.

In essence, the study reinforces the maintenance of the status quo which is not a viable option. Advancement of trade liberalization under GATT has to become the only viable alternative and is reinforced by the following obvious questions:

- If Canadian canola prices are higher as a result of the tariff, would increasing the tariff bring even higher prices to Canadian farmers?
- Applying the conclusions of the study to one of the Canadian largest wheat market, one would have to question the wisdom of Canada asking the USSR to place tariffs on flour milling in order to increase wheat prices.

Overall, the solution facing all of the players within the Canadian canola industry is a successful completion of the GATT which would involve improved market accessibility for both seed, oil, and meal. While the gains would not be automatic, Canada should at least have the opportunity to compete on an even playing field. An opportunity which is afforded to the Japanese while Canada faces a negative current account balance (1990) with Japan of almost CAN \$5 billion.

In suamation the study conclusions are indicative of the current GATT malaise. The decades of non-compliance to GATT have lead many countries developing agricultural policies which have actually altered competitive structures within the world agrifood sectors and obscured market developments. A settlement at GATT holds the only promise of dealing with the current problems and trade contradictions.

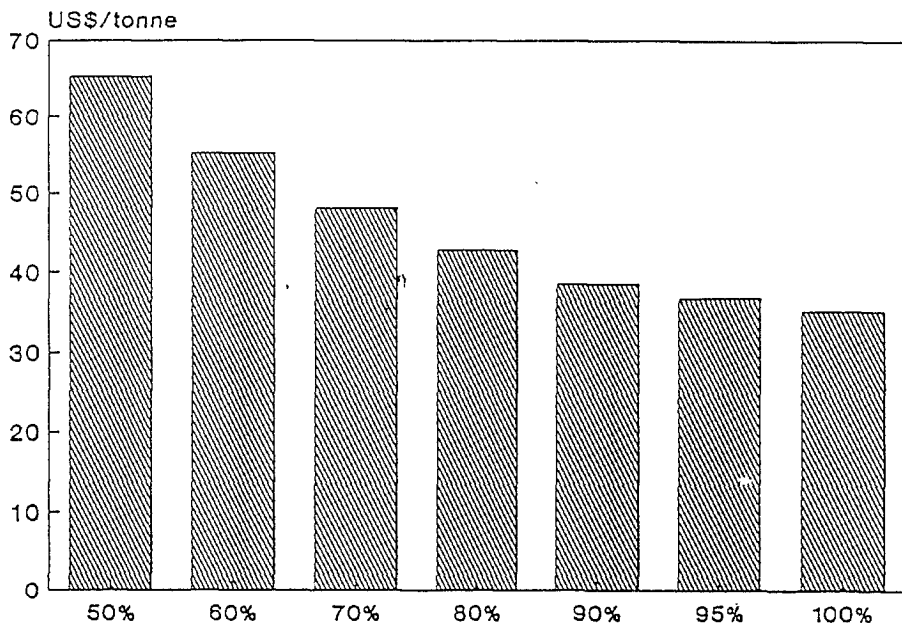
TABLE I: VALUE OF JAPAN OIL TARIFF  
RAPEOIL AND RAPESEED

YEAR	OIL PRODUCTION (000'S MT)	GROSS TARIFF VALUE (000 \$)	TARIFF VALUE (\$/MT OIL)	TARIFF VALUE (\$/MT SEED)
1986	591	21,174	36	15
1987	669	49,669	74	30
1988	683	90,688	133	54
1989	723	89,437	124	51

SOURCE: LANDELL MILLS COMMODITIES STUDIES

TABLE II

Capacity Utilisation and Total Crushing Costs, 1988/89



SOURCE: Landell Mills Commodities Studies

TABLE III: TOTAL COST OF CRUSHING RAPESEED  
IN CANADA AND JAPAN (70% CAPACITY)

YEAR	CANADA	JAPAN	ADVANTAGE TO CANADA	
	-----U.S.\$-----		\$	%
1984/85	44.43	50.79	6.36	12.3
1985/86	44.88	51.54	6.67	12.9
1986/87	44.24	58.51	14.27	24.4
1987/88	45.75	62.28	16.53	26.6
1988/89	48.10	67.45	19.35	28.7

SOURCE: LANDELL MILLS COMMODITIES STUDIES

TABLE IV

CHANGING PRICES AND THE NET CRUSHING MARGIN

		Net Crushing Margin US\$/tonne
Base Case		-18.98
Higher Capacity Use	80%	-15.05
	100%	-4.09
Lower Seed Price	-5%	-9.39
	-20%	19.37
Higher Oil Prices	+5%	-11.79
	+15%	3.58
Higher Meal Prices	+5%	-15.19
	+15%	-7.61

SOURCE: Landell Mills Commodities Studies

TABLE V

IMPACT OF FULL TARIFF REDUCTION				
Units			Short Term Impact	Long Term Impact
JAPAN				
Oil Price	(US\$/tonne)	Rapeseed	591	616
Meal Price	(US\$/tonne)	Rapeseed	204	192
Net Crush Margin	(US\$/tonne) <sup>1</sup>	Rapeseed	35	39
Oil Imports	('000 tonne/year)	Soy & Rape	80	80
Meal Imports	('000 tonne/year)	Soy & Rape	756	746
Oil Exports-Japan	('000 tonne/year)	Rapeseed	30	34
Meal Exports-Japan	('000 tonne/year)	Rapeseed	125	112

SOURCE: Landell Mills Commodities Studies

TABLE VI

Income Distribution under Varying Scenarios (US\$ million)				
	1986-89 mean outcome	Short- term outcome	Long- term outcome	
No Tariff Change with No Consumption Growth				
Producer	639	660	694	
Crusher	(27)	(30)	(7)	
TOTAL	612	630	687	
Full Tariff Elimination				
Producer	-	596	620	
Crusher	-	(7)	29	
TOTAL	-	589	649	
Gain/(Loss) from Full Tariff Elimination				
Producer	-	(64)	(74)	
Crusher	-	23	36	
TOTAL	-	(41)	(38)	

SOURCE: Landell Mills Commodities Studies