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Effect of the Trans-Pacific Partnership on U.S. Dairy Trade

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The Trans-Pacific Partnership (TPP) is a plurilateral free trade agreement presently being negotiated among 12 countries: Australia, Brunei Darussalam, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, Vietnam, and the United States. The TPP is expected to address many important trade issues; among them is increasing market access to goods and services by reducing tariffs and other trade barriers. The agreement may have an impact on the U.S. dairy industry, which is transitioning from being domestically-focused to filling an important role in global trade. In general, the TPP may:

- Create new opportunities for U.S. dairy trade in growing markets, especially Malaysia and Vietnam, where dairy consumption has expanded rapidly due to increasing incomes.
- Facilitate trade with existing partners, including Canada and Japan, by removing barriers that limit imports.
- Increase access to the U.S. dairy market for TPP partners by reducing tariffs and/or establishing dairy tariff-rate quotas (TRQs), as has been done under past U.S. free trade agreements (FTAs).

What is TPP?

TPP negotiations began in March 2010 with the goal of promoting trade and investment between nine original nations. The partnership has expanded since to 12 countries, with Japan the most recent addition. The 19th round of negotiations was completed in August 2013 in Brunei with the target of concluding discussions by the end of 2013. Details have been kept largely private, but the agreement is expected to focus on lowering existing trade barriers and integrating legal and regulatory procedures, including differences in government procurement, intellectual property rights, and Sanitary and Phytosanitary standards (SPS) (USTR 2011). The TPP aims to echo or expand on previous FTAs by increasing integration among TPP economies while streamlining diverse regulatory structures that inhibit trade.

New Opportunities for U.S. Dairy Exporters

The TPP is expected to lead to greater export opportunities for the U.S. dairy industry in both existing and developing markets. The U.S. dairy industry has become increasingly export-focused over the last decade. The United States exported \$945.5 million of dairy products in 2002. Since then, exports have increased at an average annual rate of 44 percent to total \$5.1 billion in 2012. Trade with TPP countries accounted for 46 percent of U.S. dairy exports in 2012 (table 1). Growth can be attributed to several factors, including higher global dairy product prices and a weaker U.S. dollar that made U.S. products more competitive abroad. International demand has also risen dramatically, particularly in Asia where consumption of dairy products has risen along with incomes.

Table 1: U.S. exports of selected dairy products to TPP countries, calendar year 2012

Partner Country	Nonfat dried milk	Whey	Butter	Cheese	Other ¹	Total
	Total (Million \$)					
World	1,346.09	801.15	172.51	1,111.04	1,693.06	5,123.85
TPP12	819.71	378.80	23.82	567.39	888.83	2,678.55
% U.S. Exports	61%	47%	14%	51%	52%	52%
Australia	1.04	10.57	0.50	53.92	38.89	104.92
Canada	7.28	74.07	5.79	69.02	313.52	469.68
Chile	29.88	4.49	0.88	16.84	10.18	62.27
Japan	20.04	51.46	4.55	123.26	85.09	284.39
Malaysia	51.78	24.83	0.20	8.19	48.10	133.10
Mexico	590.51	135.24	10.50	276.23	215.32	1,227.80
New Zealand	0.05	19.68	0.02	6.11	86.29	112.15
Peru	33.88	8.09	0.12	8.12	6.87	57.08
Singapore	10.64	22.36	1.26	5.12	48.08	87.47
Vietnam	74.61	28.01	0.00	0.58	36.48	139.68

1/ Other dairy products; primarily lactose, milk albumin, buttermilk, yogurt, and milk protein concentrates.

Source: U.S. Department of Commerce, Bureau of the Census.

The TPP is expected to increase trade with Malaysia and Vietnam, both growing economies with significant dairy imports. Demand is likely to grow in years to come as more affluent consumers have higher disposable incomes and demand more dairy products. Per capita GDP growth has been strong for both Malaysia and Vietnam, respectively, averaging 3.1 and 5.7 percent annually from 2003 to 2012 (USDA/ERS). In 2012, U.S. dairy exports to Vietnam totaled \$139.7 million, mostly in the form of nonfat dry milk (NDM) used in food manufacturing. Vietnam also imports significant quantities of butter and whey, but not from the United States, whose tariff rates stand at 15 percent for butter and 10 percent for cheese (table 2). U.S. dairy exports to Malaysia totaled \$133.1 million in 2012, composed primarily of NDM, whey, and buttermilk. Although Malaysia currently maintains low or zero tariff rates for most U.S. dairy product imports, the TPP could remove any remaining tariffs on U.S. dairy products and mitigate any regulatory practices that impact trade such as SPS barriers. It would also assure a level playing field for the U.S. dairy industry that competes directly with dairy industries in Oceania. Malaysia and Vietnam currently participate in an FTA with Australia and New Zealand through the Association of Southeast Asian Nations.

Table 2: Tariff rates for selected dairy products for Australia, Chile, Malaysia, New Zealand, Peru, Singapore and Vietnam

Country	Nonfat dry milk	Whey	Butter	Cheese	Duty Nature ¹	Duty Type ²
	Tariff Rate					
Australia	0.00%	0.00%	0.00%	\$0.096/kg [IQ] ³ \$1.22/kg	A S	IQ OQ
Chile	6.0%	6.0%	6.0%	6.0%	A	NQ
Malaysia	0.0%	0.0%	0.0%	0.0%	A	NQ
New Zealand	5.0%	5.0%	0.0%	0.0%	A	NQ
Peru	0.0%	0-9%	0.0%	0-9%	A	NQ
Singapore	0.0%	0.0%	0.0%	0.0%	A	NQ
Vietnam	3.0%	0.0%	15.0%	10.0%	A	NQ

1/ A signifies Ad-Valorem Duties; S signifies Specific Duties.

2/ NQ signifies non quota rate; IQ signifies in quota rate; OQ signifies over quota rate.

3/ Except blue and goat cheeses (\$0.0/kg, non quota).

Sources: Country customs tariff schedules.

Reducing Trade Barriers in Canada and Japan

Beyond U.S. trade with emerging markets, the TPP has potential to expand dairy trade with Canada and Japan, to whom the United States had exports of \$469.7 million and \$284.4 million respectively in 2012. In Canada, technological advances during the mid-20th century led to higher milk production. Meanwhile the loss of key export markets in Europe after World War II lowered dairy trade, and the introduction of dairy alternatives like margarine lowered consumption (Conference Board, 2012). The result was milk surpluses and falling prices. The present supply management system was introduced in the 1950s to remedy the problem, establishing milk quotas and setting domestic prices that are well above international prices (Conference Board, 2012). Partial reform was accomplished after the Uruguay Round, which led to a switch from binding import quotas to a system of TRQs. TRQs allow for limited imports with generally low duty rates, but once quotas are met, rates can increase dramatically (table 3). For example, the in-quota rate for cheese is 3.32 cents per kilogram but rises to 245.5 percent (and not less than \$4.25 per kilogram) for imports over quota. Imports from the United States substantially increased after the North American Free Trade Agreement, although price supports and production quotas kept trade below potential (Conference Board, 2012). Similar gains may be possible with TPP.

Table 3: Canadian tariff rates for selected dairy products

Commodity	Tariff	Duty Nature ¹	Duty Type ²
Nonfat dried milk	3.32¢/kg	S	IQ
	201.5% (but not less than \$2.01/kg)	M	OQ
Whey protein concentrate	4.94¢/kg	S	NQ
Powdered whey	3.32¢/kg	S	IQ
	208% (but not less than \$2.07/kg)	M	OQ
Butter	11.38¢/kg	S	IQ
	298.5% (but not less than \$4.00/kg)	M	OQ
Cheese	3.32¢/kg	S	IQ
	245.5% (but not less than \$4.52/kg)	M	OQ

1/ S signifies Specific Duties; M signifies Mixed Duties.

2/ NQ signifies non quota rate; IQ signifies in quota rate; OQ signifies over quota rate.

Source: Customs Tariff of Canada.

Japan's dairy industry has suffered from many of the same issues as Canada's. Surpluses and falling prices led to the creation of the Japan Dairy Council in 1962 to manage drinking-milk production. A complex system of tariffs, supply quotas, and Government support pricing currently protects farmers from international competition. As a result, Japanese consumers pay higher prices for milk and other dairy products than consumers in other developed countries. The wholesale market price for domestic butter was 1,186 yen per kilogram in 2012, equivalent to over \$12 per kilogram (USDA/FAS, 2013). This is more than double the average international market price for butter, which was \$4.81 per kilogram (USDA/ERS, 2013). Even with restrictions in place, Japan is the third largest market for U.S. dairy exports among TPP countries after Mexico and Canada. Most imports were of cheese, followed by other dairy products and whey. Tariff rates vary significantly between products (table 4). The within-quota rate for cheese is zero percent, while the rate for butter is 35 percent. Once exports rise above quota, the rates increase to 29.8 percent for cheese and 29.8 percent plus 985, or 1,159 yen per kilogram, for butter. Opening the Canadian and Japanese markets would facilitate increased trade between TPP countries while lowering prices for both Canadian and Japanese consumers.

Table 4: Japanese tariff rates for selected dairy products

Commodity	Tariff	Duty Nature ¹	Duty Type ²
Nonfat dried milk	0-25%	A	IQ
	0 or 21.3% (plus 396 ¥/kg)	M	OQ
Whey	0-35%	A	IQ
	29.8% (plus 400 - 1,023 ¥/kg)	M	OQ
Butter	35%	A	IQ
	29.8% (plus 985 or 1,159 ¥/kg)	M	OQ
Cheese	22.4-40%	A	NQ
	0.0%	A	IQ
	29.8%	A	OQ

1/ A signifies Ad-Valorem Duties; M signifies Mixed Duties.

2/ NQ signifies non quota rate; IQ signifies in quota rate; OQ signifies over quota rate.

Sources: Dairy Policies in Japan, LDP-M-134-01 (Aug. 2005) and Customs Tariff Schedule of Japan.

Increasing Access to U.S. Dairy Markets

The TPP offers the potential for increasing access to the U.S. dairy market for TPP partners beyond the current access provided by the United States' dairy TRQs established under the World Trade Organization. The United States is a net exporter of dairy products, in part due to a large domestic industry and the presence of import tariffs (table 5). In 2012, dairy imports totaled \$3.1 billion, 46 percent of which came from TPP countries (table 6). Most imports from TPP countries came from New Zealand, followed by Canada and Mexico. The highest volumes of imports are of products with zero or low tariff rates, including milk protein concentrates, casein, and whey. Therefore, it is unlikely that the TPP would have much of an effect on imports of these products. The agreement would have a greater effect on products for which tariff rates are relatively large, such as butter and cheese.

Table 5: U.S. tariff rates for selected dairy products

Commodity	Tariff	Duty Nature ¹	Duty Type ²
Nonfat dried milk	3.3¢/kg	S	IQ
	86.5¢/kg	S	OQ
Modified whey	8.5% ³	A	IQ
	13% ⁴	A	IQ
	8.5% (plus \$1.035/kg)	M	OQ
Dried whey	3.3¢/kg	S	IQ
	87.6¢/kg	S	OQ
Butter	12.3¢/kg	S	IQ
	\$1.541/kg	S	OQ
Cheese	varies	A	IQ
	varies	S	OQ

1/ S signifies Specific Duties; A signifies Ad-Valorem Duties; M signifies Mixed Duties.

2/ NQ signifies non quota rate; IQ signifies in quota rate; OQ signifies over quota rate.

3/ In-quota duty rate for milk protein concentrate (MPC).

4/ In-quota duty rate for modified whey, excluding MPC.

Source: Harmonized Tariff Schedule of the United States.

Table 6: U.S. imports of selected dairy products from TPP countries, calendar year 2012

Partner Country	Butter	Cheese	Milk protein			Other ¹	Total
			concentrate	Casein	Total (Million \$)		
World	71.16	1,094.01	351.79	609.73	957.48	3,084.16	
TPP12	47.70	89.06	333.61	272.25	678.17	1,420.78	
% U.S. Imports	67%	8%	95%	45%	71%	46%	
Australia	7.71	7.37	37.27	4.94	19.48	76.76	
Canada	1.42	24.40	4.93	0.79	389.45	420.99	
Chile	0.16	0.01	0.00	0.00	13.63	13.79	
Japan	0.00	0.00	0.00	1.21	1.18	2.39	
Malaysia	0.09	0.00	0.00	0.00	2.79	2.88	
Mexico	3.80	15.26	0.20	0.70	142.59	162.56	
New Zealand	34.46	42.02	291.21	264.59	98.95	731.23	
Peru	0.00	0.00	0.00	0.02	6.83	6.85	
Singapore	0.06	0.00	0.00	0.00	3.16	3.22	
Vietnam	0.00	0.00	0.00	0.00	0.11	0.11	

1/ Other dairy products; primarily whey, miscellaneous food preparations, and ice cream.

Source: U.S. Department of Commerce, Bureau of the Census.

If the TPP leads to preferential dairy access for TPP partners, U.S. imports of dairy products may increase. New Zealand is the most likely source of raising U.S. imports due to its large export-oriented dairy industry (USDA/FAS, 2013). Because of its strong market position, New Zealand may have the ability to affect international dairy prices. However, in recent years, New Zealand has been unable to fill its allowance of U.S. TRQs due to lower prices for

U.S. dairy products coupled with rising New Zealand exports to China and other parts of Asia. Therefore, the U.S. net trade position is likely to improve from TPP even if New Zealand exports should increase.

Conclusions

The TPP has the potential to increase economic cooperation and trade between the United States and some of its most important partners. The TPP expands U.S. relations with six countries that have existing FTAs while adding agreements with five new partners. The partnership could have a significant effect on U.S. dairy, an industry undergoing rapid change to become more integrated with the international market. At present, further market evolution is restricted by trade barriers, which remain strong in the United States and other TPP countries. The TPP seeks to remove barriers to trade, thus helping to expand markets for U.S. products while expanding access for TPP partners to U.S. dairy markets.

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