

Trade Issues in Citrus

Thomas H. Spreen

Professor and Chair

Food and Resource Economics

UF/IFAS

Graduate Programs in Food and Resource Economics

- Master of Agribusiness (MAB)
- Executive MBA specializing in Entrepreneurship – begins 5/04
- Master of Science with thesis

Economic Effect of a Tariff

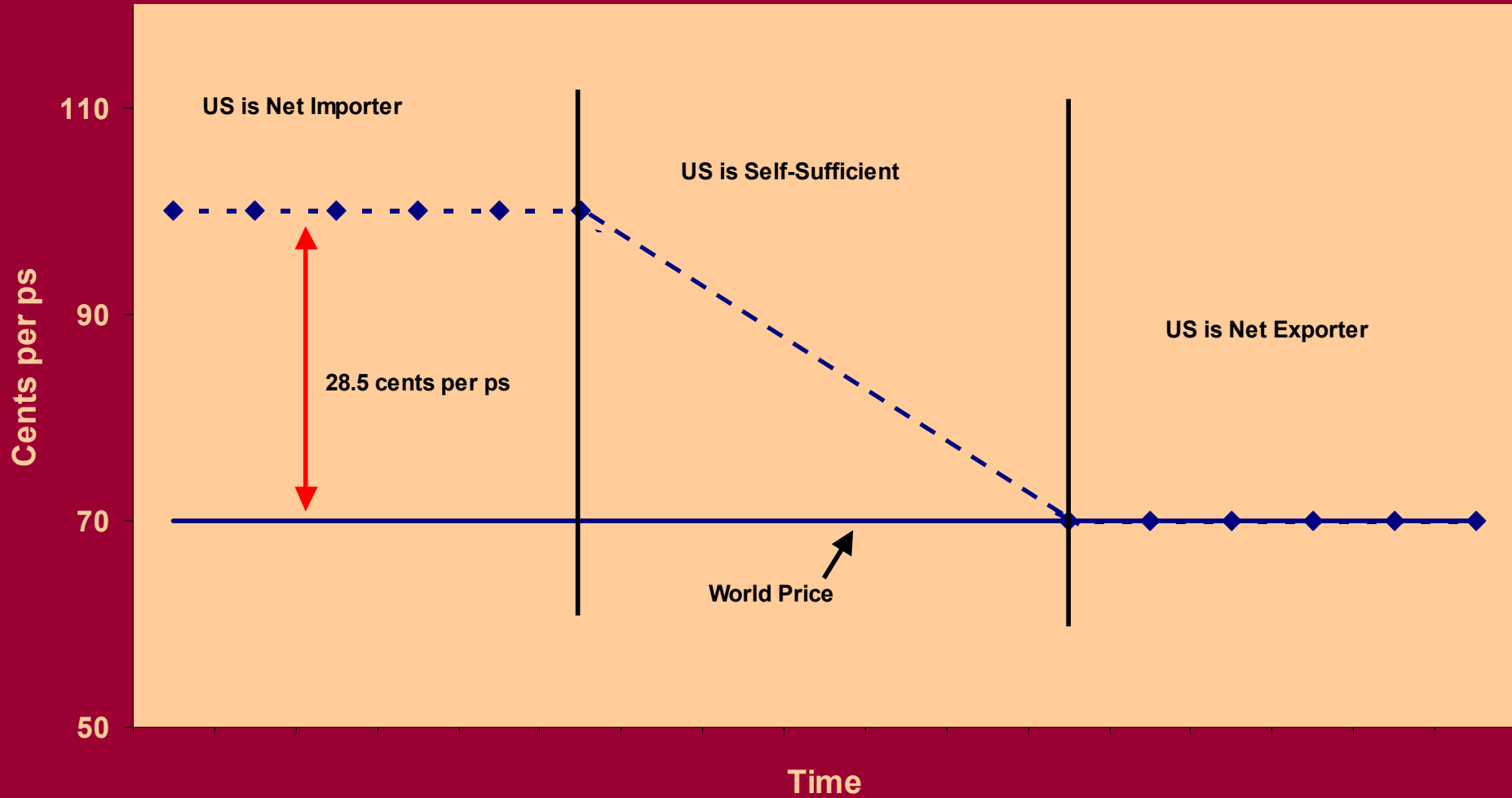
- Increases domestic prices via a tax levied on imports.
- Domestic producers are the primary beneficiaries of a tariff.
- Domestic consumers pay higher prices.
- The government receives tax revenue in the form of the proceeds from the tariff.

- What is the importance of the U.S. orange juice tariff?
- At present, it increases the cost of imports from Brazil, thereby reducing the volume of those imports.
- Lower import volume increases the price received by Florida growers.

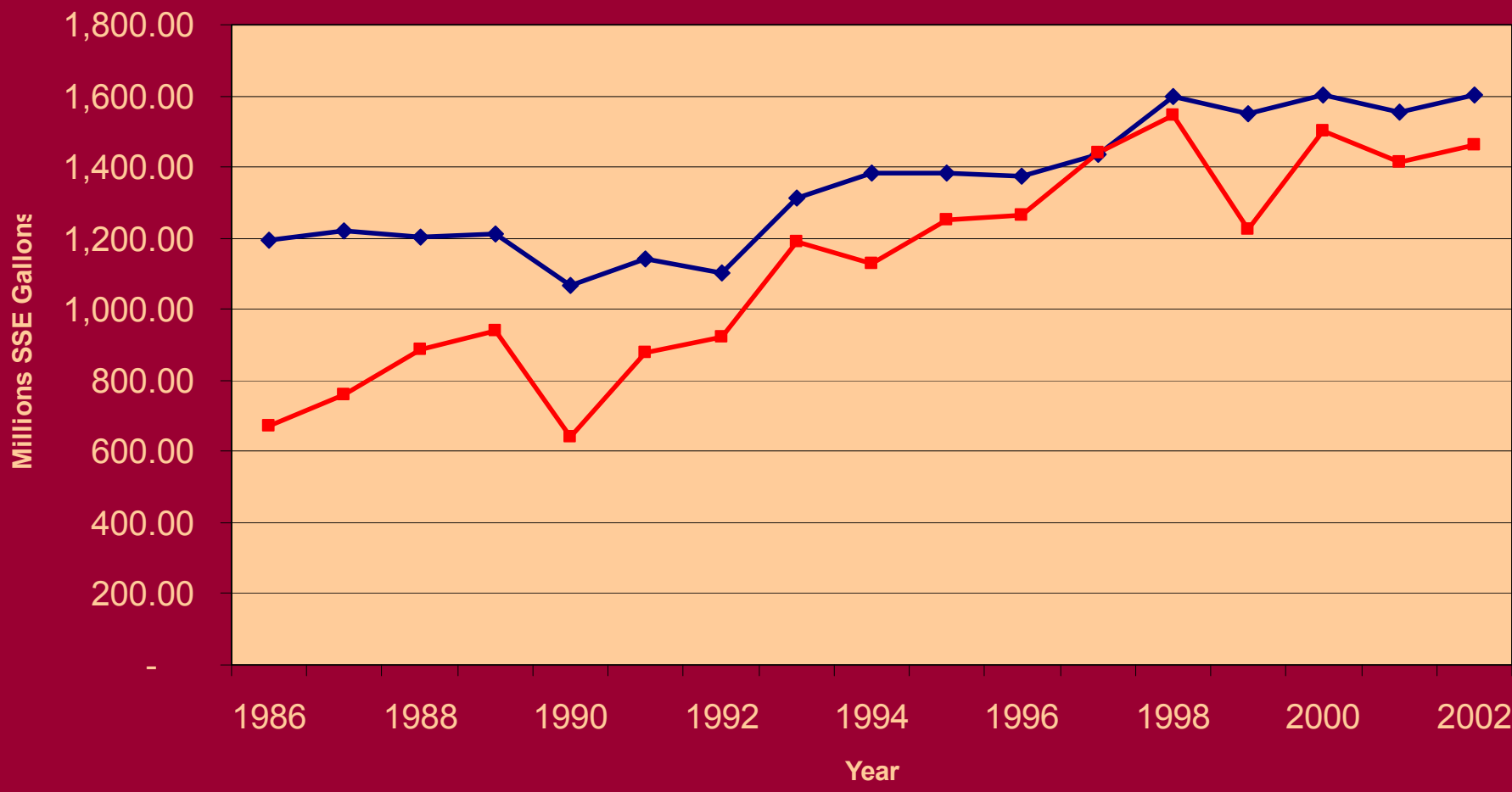
- What are the mechanics of the tariff?
- Imports from Belize, Costa Rica, and Honduras are duty free.
- Imports from Mexico are subject to the NAFTA tariff schedule.
- All imports from Brazil are subject to the most favored nation (MFN) duty which currently is 28.9 cents per pound solid for FCOJ and 17.0 cents per SSE gallon for single-strength OJ.

- There is a provision called “duty drawback” which allows an importer to claim a 99 percent refund on imports that are re-exported within two years.
- Duty drawback is important to those companies that have foreign markets in that it represents a subsidy that lowers the cost of exported product.
- For the tariff to be effective, the country must be a net importer.
- In the case of orange juice, the U.S. must import from Brazil.

The Theoretical Relationship Between U.S. and World OJ Prices



U.S. OJ Production and Consumption

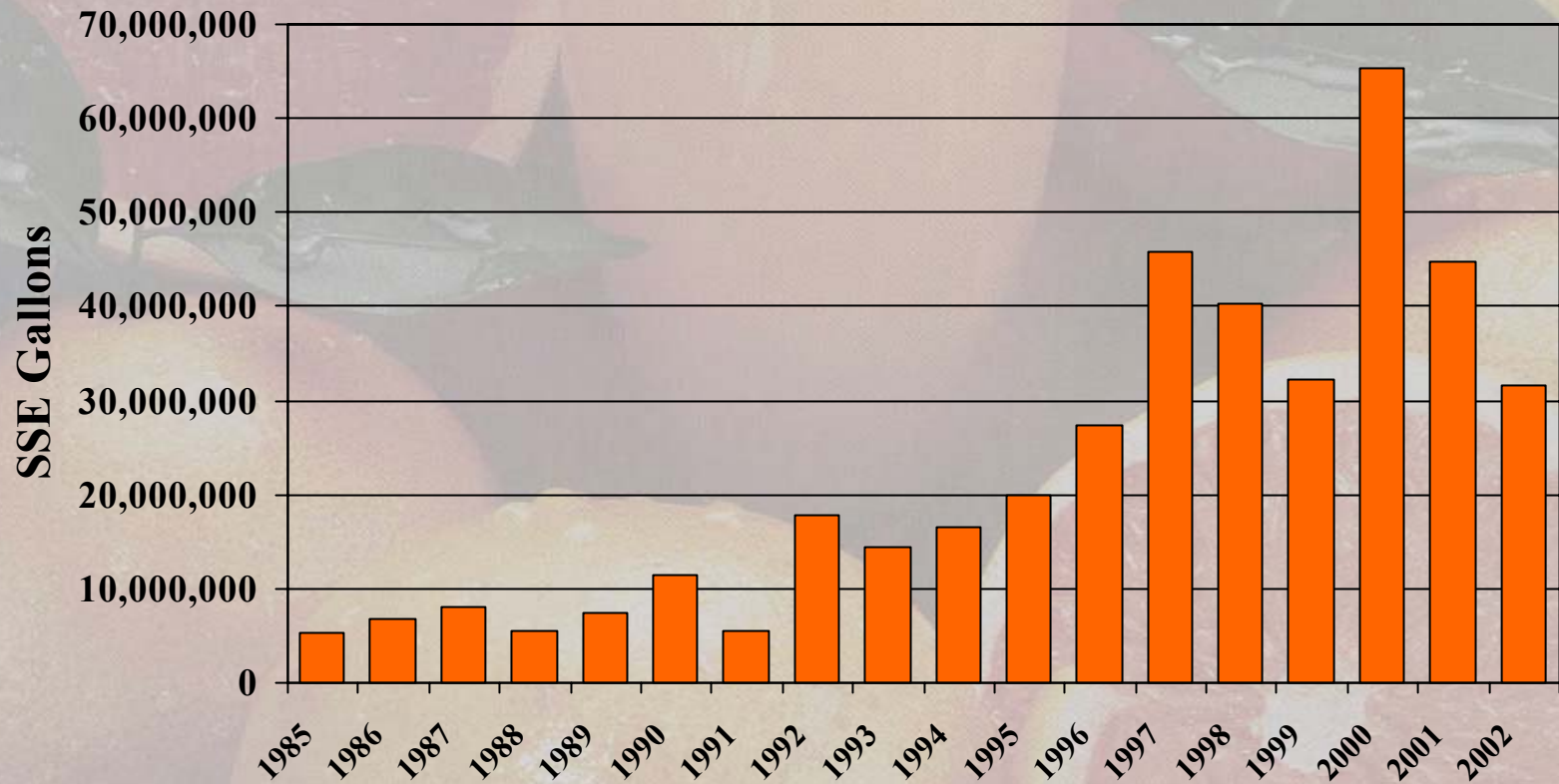


Source: FDOC

—◆— US Consumption —■— US Production

- In recent years, U.S. orange juice import requirements have declined substantially.
- While many might view this as a good thing, higher Florida OJ production means lower grower prices.
- When imports from the CBI countries and Mexico are included, the U.S. supply-demand situation has changed.

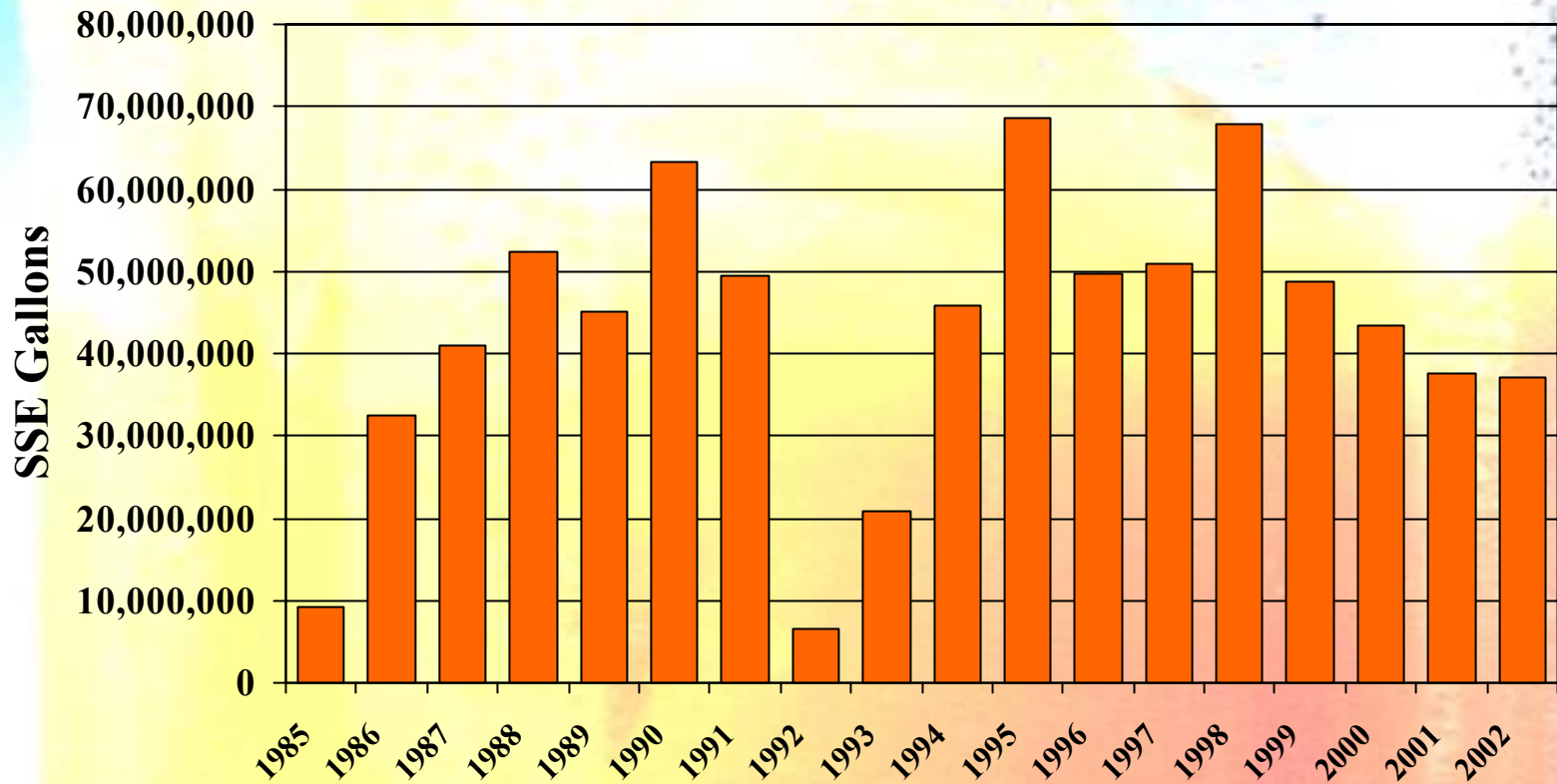
US Imports of Orange Juice from CBERA Countries, 1985-2002



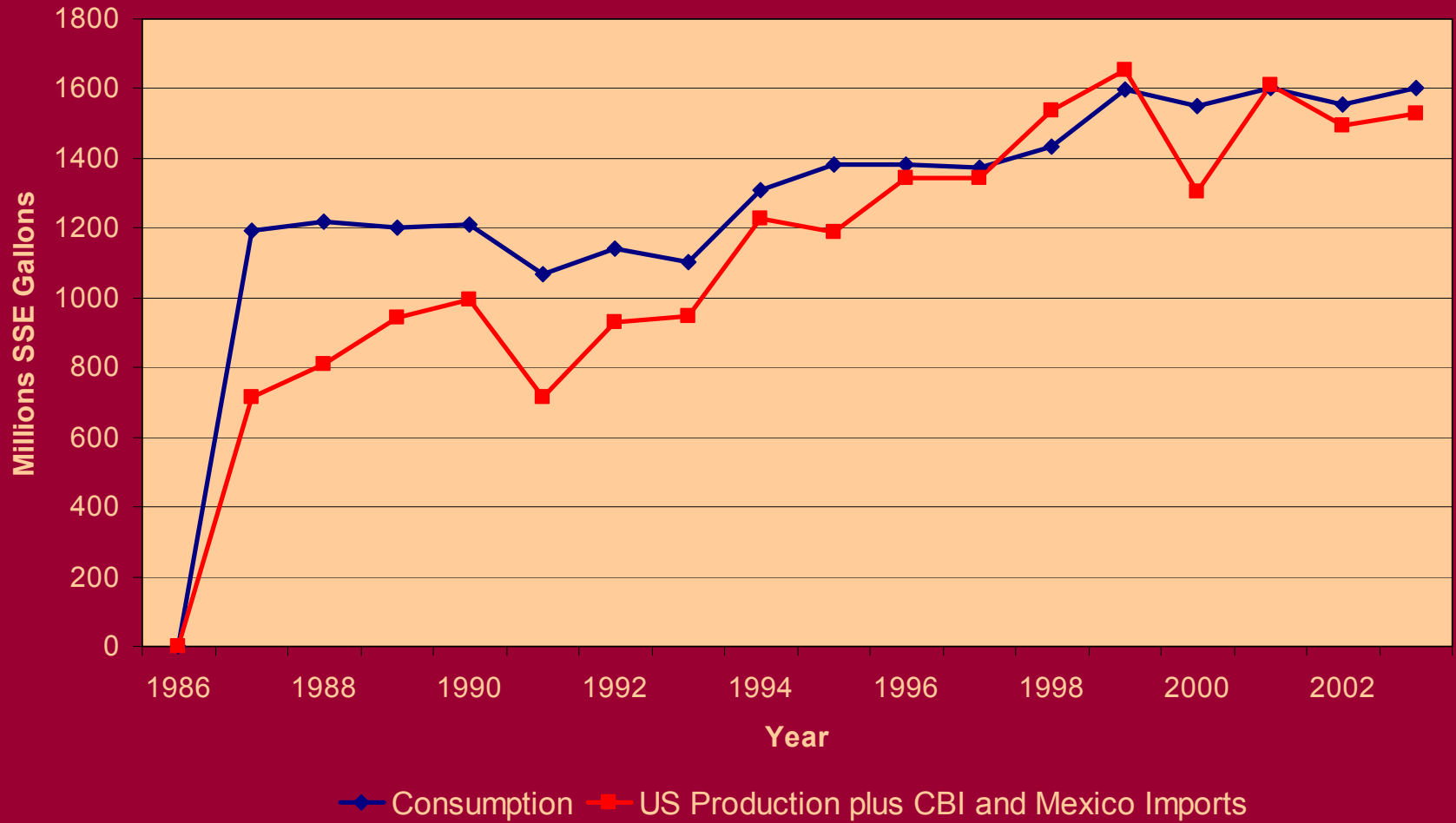
North American Free Trade Agreement (NAFTA)

- NAFTA was passed by the U.S. Congress in December 1993 and implemented January 1, 1994.
- The negotiations over orange juice were particularly contentious.
- A complicated phase-out of both U.S. and Mexican orange juice import tariffs was ultimately negotiated.

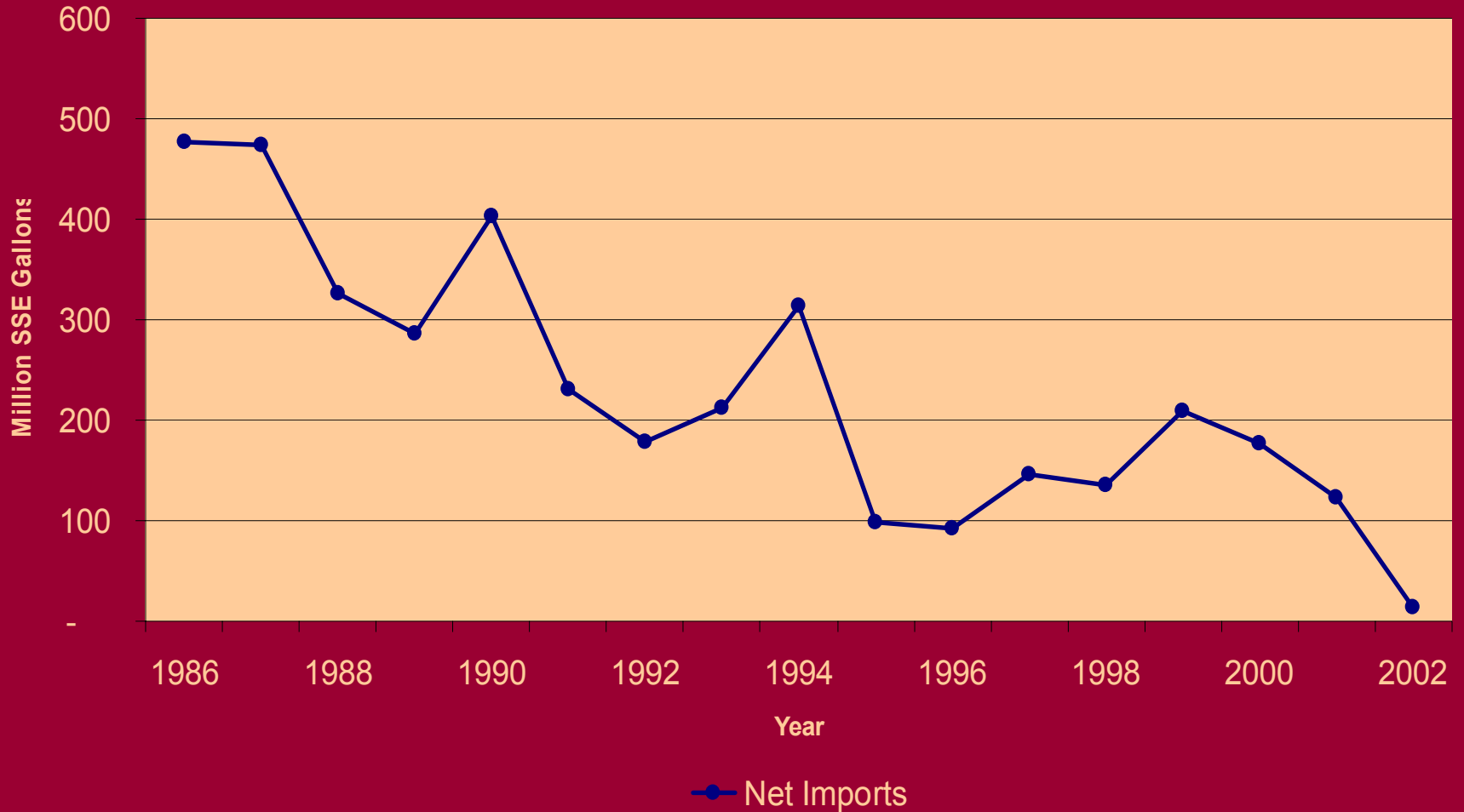
US Imports of Orange Juice from Mexico, 1985-2002



U.S. OJ Consumption and U.S. Production plus Imports from CBI and Mexico

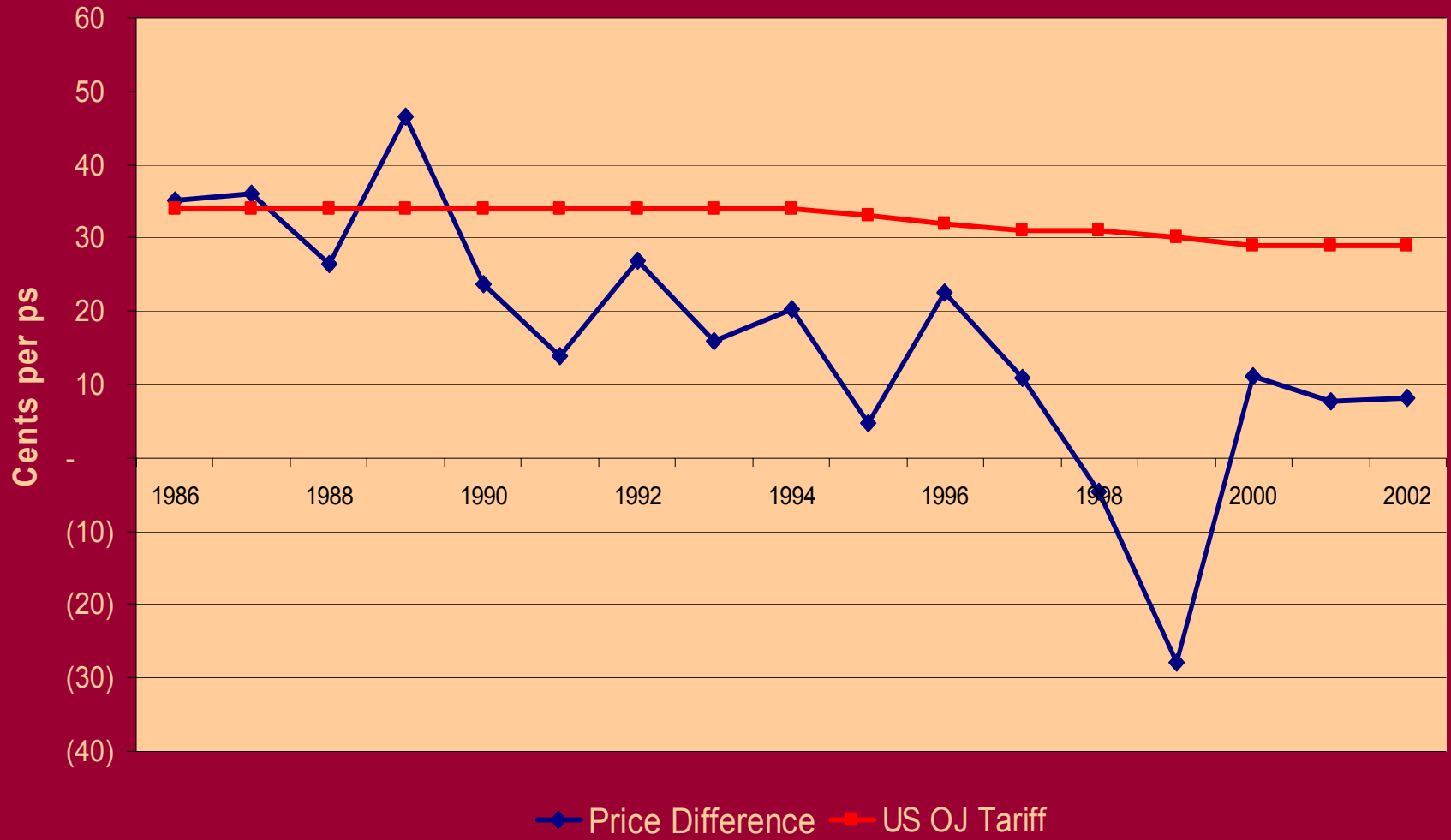


U.S. Net Imports of OJ



Source: Commerce Dept.

U.S. World Price Differential Futures – Europe FOT Price Spread



Source: FDOC, Commerce Dept.

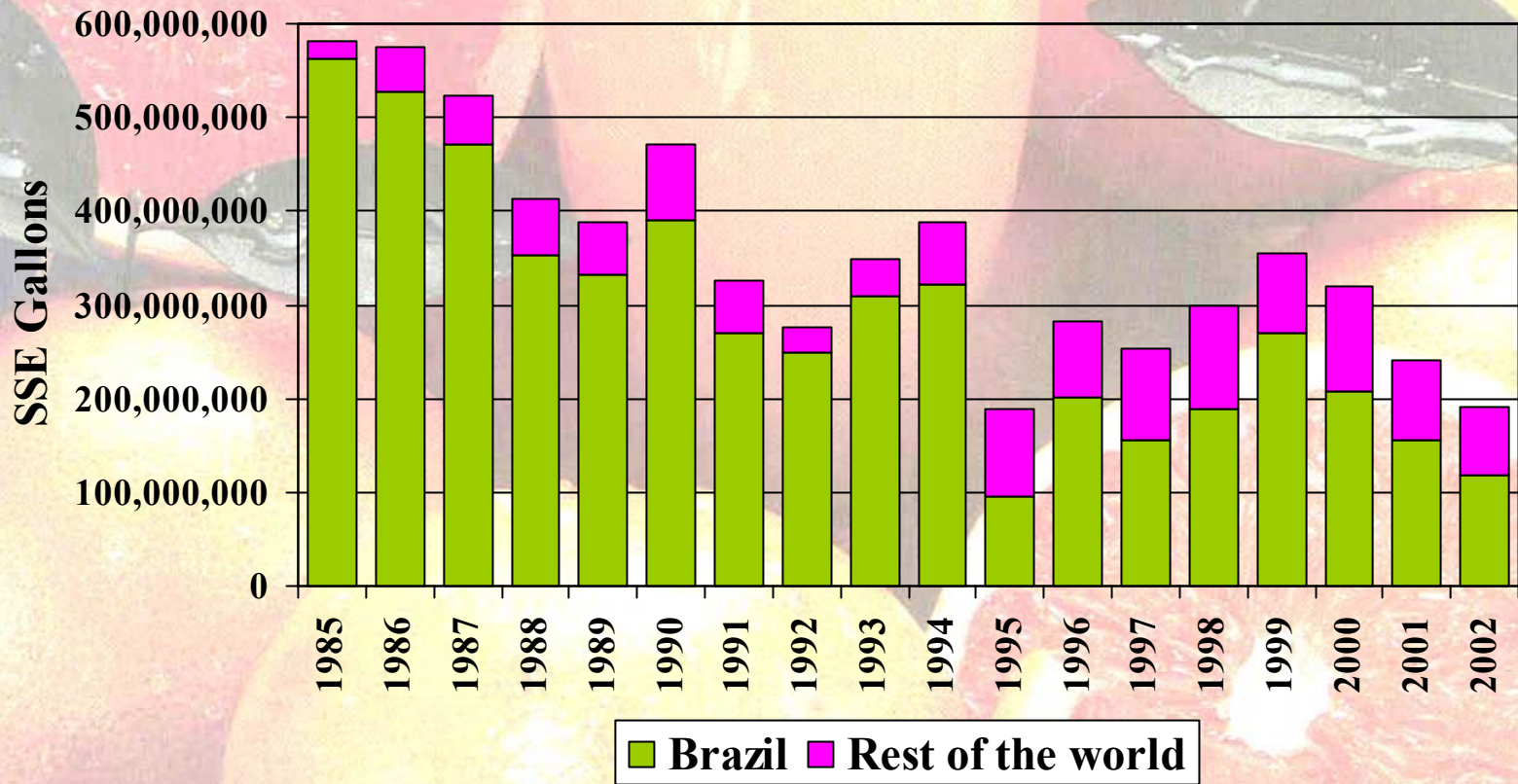
The Uruguay Round of GATT

- GATT is an acronym for the General Agreement on Trade and Tariffs. It is the rule-making entity that governs world trade.
- The World Trade Organization (WTO) now administers these rules.
- The Uruguay Round was completed in late 1994.
- The Uruguay Round was the first time that agricultural products were included in the agreement.

FCOJ Tariff Schedule for Major Orange Juice Importing Countries Under GATT

Year	U.S. cents/SSE gal	Europe ----- ad valorem -----	Japan
1994	35.01	19	30
1995	34.13	18.37	29.25
1996	33.24	17.74	28.5
1997	32.36	17.1	27.75
1998	31.48	16.47	27
1999	30.59	15.84	26.25
2000 and beyond	29.71	15.2	25.5

US Imports of Orange Juice from Brazil and the Rest of the World, 1985-02



FTAA and U.S. Agriculture

- Countries in the Western Hemisphere protect their agricultural sectors in different ways.
- For most crops, the United States uses a price support approach to support farm income. In the current environment, this has resulted in government payments to farmers.

- Other countries use a combination of import tariffs and quotas to support higher prices for commodities.
- U.S. agricultural interests seek lower tariffs and elimination of import quotas in hope of increasing exports to Western Hemisphere countries.
- The tariff on U.S. orange juice is somewhat at odds with other U.S. agricultural commodities.
- Orange juice consumption in other FTAA countries outside of Canada is quite small.

- Thus, the interests of the U.S. processed citrus industry do not coincide with those of the majority of U.S. agriculture.
- This makes the negotiating position of that industry tenuous.
- Even if FTAA is not enacted, U.S. trade negotiators may still push for tariff reductions in the Doha Round of WTO.

The Implications of Elimination of the U.S. Orange Juice Tariff

- Immediate elimination of the tariff would lower processor prices of FCOJ in the United States by 21 cents per pound solid.
- Phased elimination of the tariff over a 15-year period has a less dramatic effect on prices. In year 15, Florida orange juice prices decline 6 cents per pound solid.

- Immediate tariff elimination would, in turn, lower delivered-in prices by 21 cents per pound solid.
- Depending on juice yield, on-tree prices would decline by \$1.20 to \$1.40 per box.
- Because juice from Brazil is mainly Valencia, Valencia prices in Florida would decline more than prices for early-mid varieties.
- Nearly all increased imports would be in the form of FCOJ. Florida would still have an advantage in the production of NFC.

The Swiss25 Formula

The Swiss25 tariff reduction formula is given by

$$T_n = \frac{25 * T_0}{(25 + T_0)}$$

- The current U.S. orange juice tariff is a per unit tariff, so it must be converted to a percentage or ad valorem tariff.
- If domestic FCOJ prices are \$1.05 per pound solid, then the U.S. border price is $1.05 - .2886 = .7614$.
- At this price level, the U.S. FCOJ tariff is equivalent to a 37.9% ad valorem tariff.
- If this Swiss25 formula were adopted, the U.S. tariff would become 15.06% or 11.47 cents per pound solid

- The U.S. the NFC tariff would be reduced to 11.41 cents per pound solid.
- If the Swiss 25 proposal were implemented, U.S. FCOJ prices would be reduced by seven cents per pound solid at the processor level.

Concluding Remarks

- The trend to globalization has affected the orange juice industry.
- The United States has already committed to two agreements that affect orange juice: CBI and NAFTA.
- The U.S. orange juice declined 15 percent from 1994 to 2000 from the Uruguay Round of GATT.

- The proposed FTAA would likely result in elimination of the tariff applied by the United States on imports of OJ from Brazil.
- Immediate elimination of the U.S tariff would decrease domestic FCOJ prices by 21 cents per pound solid.
- Elimination of all OJ tariffs worldwide would cause the U.S. to decline by seven cents.
- Enactment of the Swiss25 formula would cause the U.S. price to decrease by 11.5 cents.

- If the United States is a net exporter of orange juice, the tariff is not effective in supporting domestic prices.
- Substantial erosion in the domestic demand for orange juice would have a price effect similar to elimination of the tariff.
- Enhancement of domestic prices entails both maintenance of the tariff and domestic demand.

Thomas H. Spreen

Professor and Chair

Food and Resource Economics

UF/IFAS

Gainesville

352-392-1826, ext 209

E-mail: THSpreen@ifas.ufl.edu