IMPORT TARIFFS ON WHEAT

3 February 2009

The import duty or tariff structure for agricultural commodities, and in particular that of wheat, has attracted much media attention over the past weeks. Parties representing opposing interests across the spectrum of the value chain are polarized and have simultaneously argued for increased import protection for farmers on the one hand and more openness to international trade to inject price competition and enhanced product quality into the markets on the other. Both camps have cited food security as an important objective.

A sideline observer of this debate is prompted to raise the topical questions of: Who or what body mediates here or does the necessary investigation to determine the structure and level of protective import duties (if any) for different commodities and under changing circumstances, taking into consideration the continued viability or interests of primary producers, value added producers, and consumers? How does such a body navigate this maze of different and opposing interests and what methods are used in setting tariffs?

This article aims to answer these questions particularly as they relate to the complex variable tariff formula applicable to wheat.

The International Trade Administration Commission of South Africa (ITAC) successor to the previous Board on Tariffs and Trade (BTT) at a juncture in our recent history where more openness and increased trade facilitation was required, is the body advising the Minister of Trade and Industry on matters pertaining to the setting of import tariffs.

The Commission has set comprehensive criteria for adjudicating tariff applications. Its processes are rigorous, thorough, evidence-based, and are carried out on a case by case basis. These criteria are applied consistently to all applications and includes an analysis of the following factors: whether a product is produced domestically or not, or whether there is tangible potential to produce a particular product domestically; import and export data; domestic demand and supply; comparison of domestic prices with import prices; productivity; productive capacity; market share; profitability; effective rate of protection; employment and investment.

Tariffs on agricultural goods are not homogenous; it depends on the specific economic conditions of particular sub-sectors, industries or products, hence the critical and strategic approach that ITAC takes on tariffs. The table below is an aggregated tariff structure for agricultural goods:

Primary and Processed Agriculture Tariff Structure

	WTO Bound Rates	**Applied Rates as at 2008**
Number of Lines	870	870
Average %	39.7	9
Number of Lines at zero	0	370
Non Advalorem Lines	0	179

Upon deregulation, the abolition of the Agricultural Marketing Boards and concomitant price and import controls, and after earlier tentative import duty support measures, the existing variable tariff formulae were introduced in 1999 at the recommendation of the BTT and were designed as a long-term protective regime and price support mechanism for the heavily internationally traded and, in some countries, subsidized agricultural commodities of wheat, maize, and sugar. Grain farming is also much susceptible to the quirks and ravages of nature. This particular dispensation is deemed to better suit the circumstances surrounding the production and trade of these commodities than the normal *ad valorem* import duties that are in place for other products. The reason for this is that rapid reaction is required due to the high frequency of the sudden and sharp peaks and troughs evident in the price cycles of these commodities. The formulae also accommodate exchange rate fluctuations.

The variable tariff dispensation operates on the premise that South African domestic prices should be equal to a notional long-term world reference price after adjustments, where applicable, for the effects of interventionist policies followed by some other major agricultural commodities producing countries.

To achieve this, and as South African domestic grain prices are import parity prices determined on the South African Futures Exchange (SAFEX), the specific customs duty for wheat is calculated as the difference between the domestic reference price for wheat and the world reference price, where the domestic reference price is the long-term average US No.2 HRW (ord) Gulf price, calculated as $157 per ton, and the world reference price is the 3-week moving average US No.2 HRW (ord) Gulf price for wheat as published in the IWC Grain Market Report.

To calculate adjustments to the level of protection, the difference between the world reference price on which the previous adjustment was based, and the 3-week moving average of the same price is calculated on a weekly basis. When this deviation amounts to more than US$10 for 3 consecutive weeks, a new tariff is triggered. Adjustments to the tariff are calculated in US$ and converted to Rand against the exchange rate applicable on the day when the adjustment is triggered.

Logically, when the world reference price is higher than the long term domestic reference price (as now), the formula will not yield any duty. Domestic producers would not require protection under such circumstances due to the high prevailing import prices. It will only trigger again when the world reference price dips to below the domestic reference price.

Before an explanation of the request to increase tariffs on wheat and the recommendation of the Commission, it's important that the value chain in this industry is understood. The basic wheat value chain (excluding input suppliers, silos and animal feed industry) is shown below:

Producers → Millers →Bakers → Retailers → Consumers

In tariff setting this value chain has to be kept in mind. What happens down this value chain in terms of competition issues will be left to the relevant government authority.

Over the past years since 2005, the Commission considered requests by the industry for possible changes to the variable tariff formula. In 2005 and again in 2007, a request by the industry for an increase in tariffs on wheat by deflating, through a downward adjustment, the world reference price through the inclusion of (non-subsidised) Argentinean wheat, could not be supported by the Commission. By increasing the price differential between the higher domestic reference price and (with the inclusion of competitively priced Argentinean wheat) the much lower world reference price, such a move would have led to tariff levels in excess of an *ad valorem* equivalent duty of 35% for wheat and wheat flour.

These requests could not be justified especially as the South African wheat and flour producers did not experience price disadvantages against foreign competitors, also in the light of the natural geographic protection enjoyed by domestic producers. The duty would have provided the leverage to increase prices for downstream industries and consumers appreciably, bearing in mind that grain prices are import-parity prices. South Africa has also been a net importer of wheat over the last two decades. The Commission recommended the introduction of a low 2% *ad valorem* duty on wheat in 2005. However, in 2008, the Commission recommended that the duty of 2% *ad valorem* be replaced by the original variable tariff formula (which now returns a duty of zero per cent) as the former rendered unnecessary protection for wheat producers in the current era of relatively high international wheat prices. Moreover, the much-publicised recent ban on wheat exports by Argentina would, if sustained, lead to higher domestic prices, favouring the wheat farmer by removing a source of competitively priced wheat. It should be noted that whilst the primary producers wanted increased protection, one of the major interest groups in the value chain requested that the domestic reference price be reduced from $157 per ton to

$154 per ton, the effect of which would have been a reduced protection for wheat farmers. This was rejected by the Commission.

The request to increase tariffs on wheat was also accompanied by a request to withdraw rebates on wheat to Botswana, Lesotho, Namibia and Swaziland (BLNS countries). These rebates allow for the duty free importation of wheat by the BLNS countries, which are not producers of wheat except Namibia, to access wheat at world prices for use in the production of goods for domestic consumption. The Commission could not accede to this request for the withdrawal of the rebate provisions.

From the foregoing, it is clear that the question has never been whether government should provide tariff protection for the wheat industry but rather at what level should the protection be, taking into account the need to have viable wheat farming on the one hand and the value chain implications on the other. This entails a delicate balancing act.

The trends in the wheat industry over a ten-year period between 1997 and 2007 have seen a decrease in production, reduction in total area planted, falling exports, rise in imports, falling employment, and rise in prices. This has been accompanied by increased efficiency, productivity and quality. These trends beg the question: what is constraining increased production?

Often, when ITAC is approached by the agriculture sector to increase tariffs on specific products as was the case with wheat it is evident that the problems faced by the sector are multi-dimensional. These problems range from input costs (e.g. cost of fertilizers and the cyclical fuel prices), infrastructural issues (e.g. transport costs) and management of land reform, to climatic conditions. The idea that increasing import tariffs is the only solution to all these problems is at best misguided. These problems require well coordinated policy responses by the relevant government departments and agencies as well as collaboration with organized agriculture, with import tariffs only having a part to play. Such an approach would also increase prospects for creating more jobs in this industry, especially unskilled labour which is relatively abundant in the South African context.

In the quest for food security, a distinction needs to be made between food security and food self-sufficiency as the two mean different things. In particular for ITAC they have different tariff policy implications. Food security considers access to food at affordable prices whether it is produced domestically and/or imported. Food self-sufficiency considers producing food domestically and such an approach tends to be less sensitive to price considerations.

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