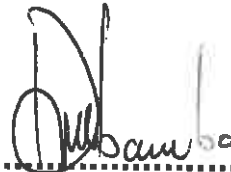


REPORT NO. 608

INCREASE IN THE GENERAL RATE OF CUSTOMS DUTY ON FROZEN MEAT OF FOWLS OF THE SPECIES *GALLUS DOMESTICUS*; BONE-IN PORTIONS CLASSIFIABLE UNDER TARIFF SUBHEADING 0207.14.9 AND BONELESS CUTS CLASSIFIABLE UNDER TARIFF SUBHEADING 0207.14.1

The International Trade Administration Commission of South Africa herewith presents its **Report No. 608: Increase in the general rate of customs duty on frozen meat of fowls of the species *Gallus domesticus*; bone-in portions classifiable under tariff subheading 0207.14.9 and boneless cuts classifiable under tariff subheading 0207.14.1**



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Dumisani Mbambo

DEPUTY CHIEF COMMISSIONER

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REPUBLIC OF SOUTH AFRICA

INTERNATIONAL TRADE ADMINISTRATION COMMISSION OF SOUTH AFRICA

REPORT NO. 608

INCREASE IN THE GENERAL RATE OF CUSTOMS DUTY ON FROZEN MEAT OF FOWLS OF THE SPECIES *GALLUS DOMESTICUS*; BONE-IN PORTIONS CLASSIFIABLE UNDER TARIFF SUBHEADING 0207.14.9 AND BONELESS CUTS CLASSIFIABLE UNDER TARIFF SUBHEADING 0207.14.1

Synopsis

The Commission considered an application by Webber Wentzel, which submitted it on behalf of the South African Poultry Association ("SAPA" or "the Applicant"). The application is for an increase in the general rate of customs duty on bone-in portions ("BIP") classifiable under tariff subheading 0207.14.9 and boneless cuts ("BLC") classifiable under tariff subheading 0207.14.1 from 37 per cent *ad valorem* and 12 per cent *ad valorem*, respectively, to the World Trade Organisation ("WTO") bound rate level of 82 per cent *ad valorem*.

During its deliberations and in arriving at its recommendation, the Commission considered the information at its disposal, including comments received during the investigation and with due regard to food security and the effect on downstream consumers, especially the poor who consume poultry as one of their main sources of protein. In particular the Commission took the following factors into account:

- South Africa remains the major broiler producer in Southern Africa accounting for 80 per cent of total broiler production in the region. Broiler production dominates the agricultural sector and it remains the cheapest source of protein when compared to all other animal proteins followed by beef.
- The poultry sector has spill over effects in the grain and chick industries, which is evidenced by the fact that it is the second biggest user of maize in the region and a significant user of soybeans.
- For the period under investigation (2015 to 2018), there was an average decline in domestic demand for the products concerned, as well as a decline in the

Participating Producers' production volume, capacity utilisation, sales and market share.

- The importers' market share for BIP and BLC has been on an upward trend from 2015 to 2018.
- For the period under investigation (2015-2018), the origin of imports shifted from non-dutiable imports from the European Union ("EU") to dutiable imports from the rest of the world, mainly Brazil and the United States of America ("USA").
- According to information at the Commission's disposal, on average, the Participating Producers' production costs increased between 2015 and 2018. The major cost drivers were input materials (i.e. live bird, feed, labour and utilities). However, as a result of declining feed costs, the Participating Producers experienced a marginal decline in their cost of production in 2018.
- On average, the Participating Producers' net profits have been positive over the period of the investigation. However, profit margins initially declined, before increasing marginally in 2018, which can be ascribed to a decline in feed costs.
- On average, the Participating Producers' investment levels increased for the period under investigation.
- The Commission found that the domestic poultry industry producing BIP and BLC experienced price disadvantages *vis-à-vis* foreign producers.
- The Commission found that, on balance, taking into account the adjudication criteria of a tariff amendment application as well as the potential impact of the duty on consumers, there is adequate justification for an increase in the rate of duty on BIP and BLC.
- In terms of following a balanced approach, the Commission determined that the level of duty for BIP, which will minimise the price disadvantage and soften the impact on consumer welfare, amounts to 62 per cent *ad valorem*. At this level of duty, although the price disadvantage would not be removed entirely, it would decline and enable the domestic industry to increase domestic demand for its products, increase its production capacity utilisation and achieve economies of scale.
- It was found that the level of duty for BLC, which would remove the price disadvantage and soften the impact on consumer welfare, amounts to 42 per cent *ad valorem*, which would place domestic producers of BLC on an equal footing with similar imported products. At this level of duty, the price disadvantage would be removed and enable the domestic industry to increase the domestic demand for its products; increase its production capacity utilisation; and achieve economies of scale.

- It should be noted that the proposed levels of customs duty will provide relief with regard to current industry pressures. However, broader structural reforms, which include, amongst others, investment in industry technology, research developments as well as a meaningful transformation program to accommodate new entrants in the industry, should still be considered.
- Reciprocal commitments made by the Participating Producers were provided, particularly with respect to levels of production, investment and employment creation, as articulated in the New Growth Path (“NGP”). The Applicant submitted that should tariff support be granted, production volumes, employment and investment by the Participating Producers are expected to increase between 2019 and 2021.

In light of the foregoing, the Commission decided that the duties on the products in question be amended as shown below and that the duties be reviewed after a period of 3 years, or such other period as decided by the Commission, to determine the impact on employment, production and investment. It is also envisaged that annual monitoring of the sector’s performance will be undertaken to monitor compliance with the Participating Producers’ reciprocal commitments.

Tariff subheading	Product	Existing duty	Recommended duty
0207.14.1	Boneless cuts	12% <i>ad valorem</i>	42% <i>ad valorem</i>
0207.14.9	Bone-in portions	37% <i>ad valorem</i>	62% <i>ad valorem</i>

1. APPLICATION AND TARIFF POSITION

1.1. The International Trade Administration Commission of South Africa (“ITAC” or “the Commission”) received an application from Webber Wentzel, who submitted it on behalf of the South African Poultry Association (“SAPA” or “the Applicant”). The application is for an increase in the general rate of customs duty on bone-in portions (“BIP”) classifiable under tariff subheading 0207.14.9 and boneless cuts (“BLC”) classifiable under tariff subheading 0207.14.1 from 37 per cent *ad valorem* and 12 per cent *ad valorem*, respectively, to the World Trade Organisation (“WTO”) bound rate level of 82 per cent *ad valorem*.

1.2. As reasons for the application, the Applicant submitted, *inter alia*, that:

- “The SACU poultry industry (meat and eggs) supplies more than 60% of the animal protein consumed in SACU and makes up almost 20% of South Africa’s

agricultural gross domestic product. It is the single largest part of agriculture in SACU and is core to SACU food security.

- *The poultry industry is the second biggest user of maize in the region and by far the biggest user of soybeans. The South African Government's soybean development strategy is dependent on the success of the local poultry industry.*
- *The SACU domestic broiler industry directly employs at least 47,025 people with a further 58,383 people indirectly employed in support industries that are dependent on the broiler industry. The crops which are used as feed in the poultry industry account for approximately 17,738 workers in the crop farming sector.*
- *SACU is a globally efficient producer of chicken. Despite this, the SACU poultry industry has faced, and continues to face, enormous profitability challenges. These have resulted in downsizing in late 2016 and early 2017, resulting in job losses and deterioration in SACU's food security position.*
- *The profitability challenges experienced by the SACU industry are directly linked to increasing volumes of opportunistic imports of frozen chicken which significantly undercut the SACU industry.*
- *Dutiable imports of frozen chicken have increased drastically over the period 2015 to 2017. This has caused and threatens to cause serious injury.*
- *These low priced imports limit the SACU industry's ability to increase prices in line with the increases in costs (price suppression) and also reduces sales volumes and market share (as there is a preference for the lower priced imports). The SACU industry has limited storage capacity and export opportunities. This means that when these opportunistic imports enter the SACU market, the SACU industry is forced to lower its prices in order to sell stock and create storage capacity."*

1.3. The application was published in the Government Gazette on 30 November 2018, for interested parties to comment.

1.4. The tariff structure pertaining to the subject products is as shown in Table 1 below.

Table 1: Tariff position for the subject products

Tariff heading	Tariff subheading	Description	Statistical unit	Rate of Duty				
				General	EU	EFTA	SADC	MERCOSUR
02.07		Meat and edible offal, of the poultry of heading 01.05, fresh, chilled or frozen:						
	0207.1	Of fowls of the species Gallus domesticus:						
	0207.14	Cuts and offal, frozen						
	0207.14.1	Boneless cuts						
	0207.14.11	Breasts	kg	12%	free	12%	free	12%
	0207.14.13	Thighs	kg	12%	free	12%	free	12%
	0207.14.15	Other	kg	12%	free	12%	free	12%
	0207.14.9	Other						
	0207.14.91	Whole bird cut in half	kg	37%	free	37%	free	37%
	0207.14.93	Leg quarters	kg	37%	free	37%	free	37%
	0207.14.95	Wings	kg	37%	free	37%	free	37%
	0207.14.96	Breasts	kg	37%	free	37%	free	37%
	0207.14.97	Thighs	kg	37%	free	37%	free	37%
	0207.14.98	Drumsticks	kg	37%	free	37%	free	37%
	0207.14.99	Other	kg	37%	free	37%	free	37%

Source: SARS

1.5. The applicable WTO bound rate for both BLC and BIP of chicken is 82 per cent *ad valorem*.

1.6. The Applicant's requested tariff position is provided in Table 2 below.

Table 2: Requested tariff position

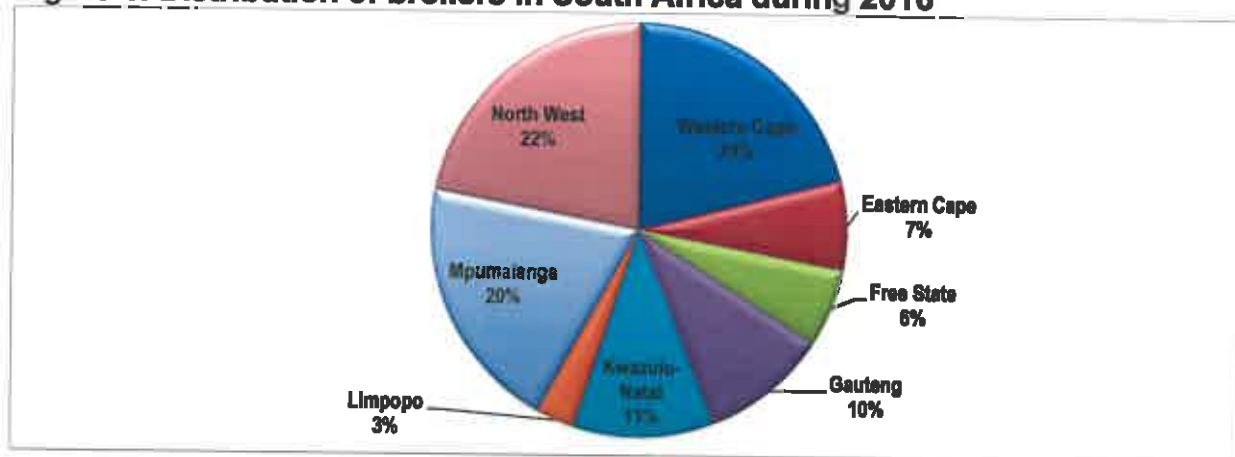
Tariff heading	Tariff subheading	Description	Statistical unit	Rate of Duty				
				General	EU	EFTA	SADC	MERCOSUR
02.07		Meat and edible offal, of the poultry of heading 01.05, fresh, chilled or frozen:						
	0207.1	Of fowls of the species Gallus domesticus:						
	0207.14	Cuts and offal, frozen						
	0207.14.1	Boneless cuts						
	0207.14.11	Breasts	kg	82%	free	82%	free	82%
	0207.14.13	Thighs	kg	82%	free	82%	free	82%
	0207.14.15	Other	kg	82%	free	82%	free	82%
	0207.14.9	Other						
	0207.14.91	Whole bird cut in half	kg	82%	free	82%	free	82%
	0207.14.93	Leg quarters	kg	82%	free	82%	free	82%
	0207.14.95	Wings	kg	82%	free	82%	free	82%
	0207.14.96	Breasts	kg	82%	free	82%	free	82%
	0207.14.97	Thighs	kg	82%	free	82%	free	82%
	0207.14.98	Drumsticks	kg	82%	free	82%	free	82%
	0207.14.99	Other	kg	82%	free	82%	free	82%

Source: SARS

2. DISCUSSION

- 2.1. SAPA is an association that represents and serves the interests of the domestic poultry industry. SAPA represents small scale, emerging and larger commercial poultry farmers in the following sectors: the broiler and egg industries, the breeding / day-old chick supply industry and smallholder and developing farmers ("SAPA, 2016").
- 2.2. According to information at the Commission's disposal, all Southern African Customs Union ("SACU") countries have poultry producing industries. According to the Department of Agriculture, Forestry and Fisheries ("DAFF"), although broiler farming has a national footprint, production is concentrated in the North West, Western and Northern Cape, Mpumalanga and KwaZulu-Natal provinces, which together, accounts for approximately 74 per cent of total production ("DAFF, 2017").
- 2.3. Figure 1 below shows the distribution of broiler production during 2016:

Figure 1: Distribution of broilers in South Africa during 2016



Source: DAFF

- 2.4. According to a DAFF document titled: "A profile of the South African broiler market value chain, 2017", the broiler sector is deemed the biggest sector within the agricultural sector of South Africa in terms of production value. In 2015/16, the sector generated R38.6 billion of gross value, which constituted approximately 15.6 per cent of total gross value of agricultural products. In comparison to other livestock products, the broiler sector accounts for 33 per cent of all animal products in South Africa in Rand terms. South Africa remains the major broiler producer in Southern Africa accounting for 80 per cent of total broiler production in the region. Broiler

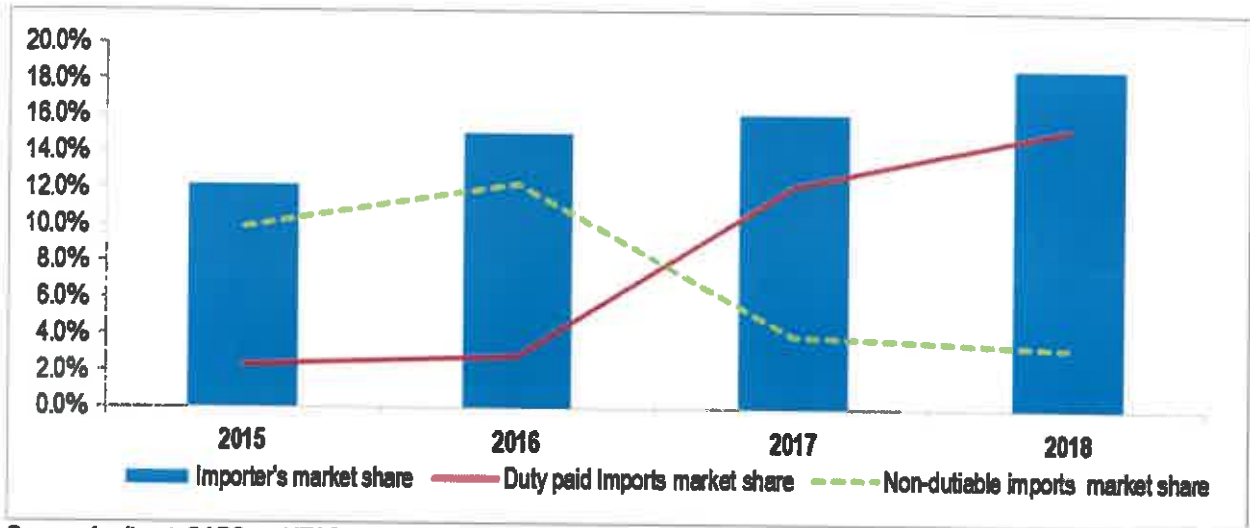
production dominates the agricultural sector and it remains the cheapest supplier of protein when compared to all other animal proteins, followed by beef.

- 2.5. According to DAFF (2017), the poultry sector has spill over effects in the grain and chick industries, which is evidenced by the fact that it is the second biggest user of maize in the region and a significant user of soybeans. Broiler meat accounts for approximately 93.6 per cent of total poultry-meat production, with the rest made up of mature chicken slaughter (culls), small-scale and backyard broiler meat production and other specialized broiler meat products (geese, turkey, ducks and guinea fowl).
- 2.6. For the purpose of this report, the economic analysis is split into two parts, with the first part focusing on BIP and the second part focusing on BLC. The information is provided by SAPA on behalf of its members. This information, namely the individual and consolidated data submitted, is for Astral Operations Ltd, Afgri Poultry (Pty) Ltd, Grain Field Chickens (Pty) Ltd, RCL Foods Consumer (Pty) Limited, Sovereign Food Investments Ltd and Supreme Poultry (Pty) Ltd, collectively defined as "Participating Producers". The analysis of the SACU market is based on general information (i.e. information for "non-participating producers") and company specific information (i.e. information for "Participation Producers").

BONE-IN PORTIONS

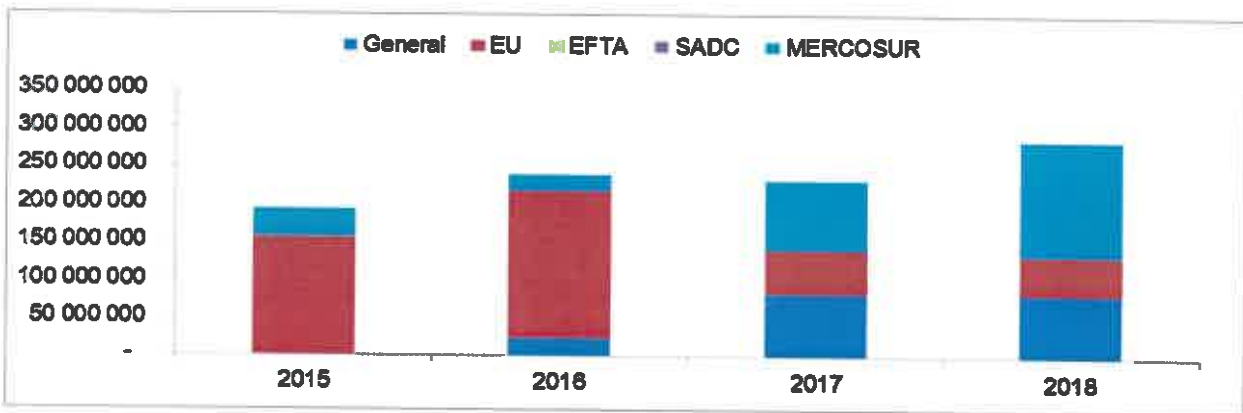
- 2.7. In terms of BIP, it was found that for the period under investigation (2015 to 2018), there was an average decline in domestic demand as well as a decline in the Participating Producers' production volume, capacity utilisation, sales and market share.
- 2.8. The SACU industry's market share (including non-Participating Producers), declined from 88 per cent in 2015 to approximately 81 per cent in 2018. On average, the industry's market share declined by approximately 2.1 percentage points per annum for the period 2015 to 2018, while importers increased their share of the market by 2.2 percentage points per annum during the same period.
- 2.9. Figures 2 and 3 below depict the importers' market share in the SACU and the share of imports into SACU by regions.

Figure 2: Importers market share in the SACU



Source: Applicant, SARS and ITAC calculation

Figure 3: SACU Import share by region



Source: SARS, ITAC Calculations

2.10. As shown in Figure 2 above, importers' market share for BIP has been on an upward trend, increasing from 12.2 per cent in 2015 to approximately 18.7 per cent in 2018. For the period under investigation (2015-2018), the origin of imports shifted from non-dutiable imports from the European Union ("EU") to dutiable imports from the rest of the world, mainly Brazil and the United States of America ("USA"). Duty paid imports' market share increased significantly from just 2.3 per cent in 2015 to approximately 15.4 per cent in 2018. At the same time, non-dutiable imports' market share, mainly from the EU, declined significantly from 9.9 per cent in 2015 to approximately 3.3 per cent in 2018.

2.11. According to information at the Commission's disposal, this shift in imports could be attributed to an outbreak of Avian Influenza in the majority of EU countries around

November 2016 and the imposition of a safeguard duty on imports of BIP from the EU in December 2016.

- 2.12. According to information at the Commission's disposal, the Participating Producers' production costs for BIP increased, on average, between 2015 and 2018. The major cost drivers were input materials (i.e. live bird, feed, labour and utilities). However, as a result of declining feed costs, the Participating Producers experienced a marginal decline in their cost of production in 2018.
- 2.13. According to information at the Commission's disposal, the Participating Producers recorded a positive profit level in 2015, before recording losses in 2016. However, profit levels subsequently increased in 2017 and 2018. On average, over the period of the investigation, the Participating Producers realised a positive profit level, attributed to a decline in feed costs, which is one of the major input costs.
- 2.14. According to the Applicant, the Participating Producers experienced price suppression for BIP in 2016, when they sold the product at a significant loss. Although this situation improved in 2018, the Applicant submitted that profit margins are still well below the level required to achieve a whole business Earnings Before Interest and Tax ("EBIT") of 12 per cent.
- 2.15. On average, the Participating Producers' investment levels for BIP increased for the period 2015 to 2018.
- 2.16. The Association of Meat Importer and Exporters ("AMIE") and Merlog contended that post-importation adjustments should be made to the landed cost of imported BIP, when compared to the ex-factory selling prices of the domestic producers. The contention is that imported BIP arrives in bulk form and is therefore not at the same level of trade as the BIP of the Participating Producers. The Commission declined to make this adjustment because of a lack of verifiable data demonstrating that all imports arrive in this form.
- 2.17. Amongst other critical factors in adjudicating tariff applications is the determination whether a domestic producer is suffering price disadvantages *vis-à-vis* foreign producers.

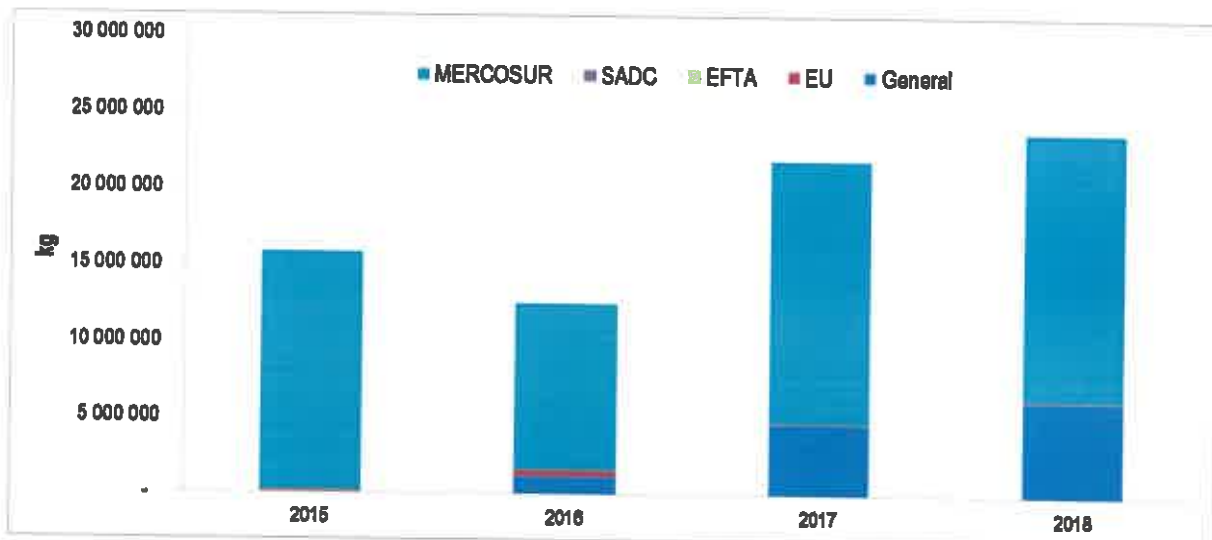
- 2.18. To determine the competitive position of domestic producers *vis-à-vis* imports, a comparison between the two price structures was done by the Commission at the appropriate point of comparison.
- 2.19. The Commission found that the domestic poultry industry producing BIP experiences price disadvantages *vis-à-vis* foreign producers.
- 2.20. According to the foregoing and other information at the Commission's disposal, on balance, and taking into account the adjudication criteria pertaining to tariff amendment applications, the Commission determined that there is adequate justification for an increase in the rate of duty on BIP. However, in order to assess the price impact on end-consumers, the Commission requested the National Agricultural Marketing Council ("NAMC"), a statutory body reporting to the Minister of Agriculture, Forestry and Fisheries, to conduct an impact analysis of the effects that various levels of increases in the duty on BIP (and BLC) would have on domestic production levels and consumer prices.
- 2.21. In terms of following a balanced approach, the Commission found that the level of duty, which will best minimise the price disadvantage and the impact on consumer welfare amounts to 62 per cent *ad valorem*. At this level of duty, although the price disadvantage would not be removed entirely, it would enable the domestic industry to increase the domestic demand for its products; to increase its production capacity utilisation; and achieve economies of scale.
- 2.22. The Commission considered that there are potential price impacts associated with the 62 per cent *ad valorem* rate of duty. The NAMC impact analysis found that the immediate price impact on consumers would be significantly lower than the potential price impact should duties be increased to 82 per cent *ad valorem*. At 82 per cent *ad valorem*, the immediate price impact on consumers would have an adverse effect on downstream consumers, especially the poor who consume poultry as one of their main sources of protein.
- 2.23. The Commission noted that the proposed level of customs duty of 62 per cent *ad valorem* may only provide partial relief with regard to current industry pressures and therefore broader structural reforms, which include, amongst others, investment in

industry technology, research developments as well as a meaningful transformation program to accommodate new entrants in the industry should be considered.

BONELESS CUTS

- 2.24. In terms of BLC, it was found that for the period under investigation (2015 to 2018), there was an average decline in domestic demand as well as a decline in the Participating Producers' production volume, capacity utilisation, sales and market share.
- 2.25. The decline in the Applicant's sales volumes for BLC were accompanied by an increase in import volumes for the period 2015 to 2018.
- 2.26. The SACU industry's market share for BLC (including non-Participating Producers), declined from 82.9 per cent in 2015 to approximately 72.7 per cent in 2018. The importers' market share for BLC has been on an upward trend, increasing from 17.1 per cent in 2015 to approximately 27.3 per cent in 2018. On average, the industry's market share declined by approximately 3.4 percentage points per annum for the period 2015 to 2018, while importers increased their share of the market by approximately 3.4 percentage points per annum during the same period.
- 2.27. The majority of imports of BLC into the SACU consisted of duty paid imports, mainly from Brazil, Argentina and the USA. Figure 4 below depicts the share of imports into SACU by region.

Figure 4: SACU import share by region



Source: SARS

- 2.28. As can be seen in Figure 4 above, for the period under consideration, the majority of imports of BLC originated from the Mercosur region, mainly Brazil and Argentina. For the period 2015 to 2018, the share of BLC imports from Mercosur compared with total imports, was, on average, 84 per cent per annum. In 2018, non-dutiable imports from the EU constituted less than 1 per cent of total imports.
- 2.29. The Participating Producers were faced with increased input costs between 2015 and 2016, mainly driven by the cost of live birds, feed, labour and utilities. However, between 2016 and 2018, costs declined marginally. The decline in production cost for the period 2016 to 2018 has mainly been as a result of declining feed cost.
- 2.30. The Participating Producers' net profit for BLC have been positive over the period of the investigation, however, profit margins declined between 2015 and 2017, before increasing marginally in 2018, which can be ascribed to a decline in feed cost. It should be noted that BLC only represents a smaller percentage of the Participating Producers' combined sales of BIP and BLC.
- 2.31. Similar to BIP, amongst other critical factors in adjudicating tariff applications is the determination whether a domestic producer is suffering price disadvantages *vis-à-vis* foreign producers.
- 2.32. To determine the competitive position of domestic producers *vis-à-vis* imports, a comparison between the two price structures was done by the Commission at the appropriate point of comparison.
- 2.33. The Commission found that the domestic poultry industry producing BLC experiences price disadvantages *vis-à-vis* foreign producers.
- 2.34. According to information at the Commission's disposal, on balance, taking into account the adjudication criteria of a tariff amendment application as well as the potential impact of the duty on consumers, it was found that there is adequate justification for an increase in the rate of duty on BLC.
- 2.35. In terms of following a balanced approach, the level of duty, which will remove the price disadvantage and soften the impact on consumer welfare amounts to 42 per cent *ad valorem*, which would place domestic producers of BLC on an equal footing

with similar imported products. At this level of duty, the price disadvantage would be removed and enable the domestic industry to increase the domestic demand for its products; increase its production capacity utilisation; and achieve economies of scale.

- 2.36. It should be borne in mind that there are potential price impacts associated with the 42 per cent *ad valorem* rate of duty. However, this is significantly lower than the potential price impact should duties be increased to 82 per cent *ad valorem*.
- 2.37. It should be noted that the proposed level of customs duty of 42 per cent *ad valorem* will provide relief with regard to current industry pressures, however, broader structural reforms, which include, amongst others, investment in industry technology, research developments as well as a meaningful transformation program to accommodate new entrants in the industry should still be considered.
- 2.38. Reciprocal commitments made by the Participating Producers were provided, particularly with respect to levels of production, investment and employment creation, as articulated in the New Growth Path (“NGP”). The Applicant submitted that should tariff support be granted, production volumes, employment and investment by the Participating Producers are expected to increase between 2019 and 2021.
- 2.39. As was the case in its 2013 chicken investigation, studies were commissioned by and submitted to ITAC, analysing the impact of potential duty increases. In this investigation, ITAC requested NAMC to conduct an impact analysis of the effect that the proposed tariff increase by SAPA will have on domestic production levels and consumer prices. ITAC also received a study from Genesis Analytics (Pty) Ltd (“Genesis”), commissioned and submitted by SAPA, a report from the Bureau for Food and Agricultural Policy (“BFAP”)¹ and a report from FTI Consulting submitted by AMIE². The NAMC study³ is the most comprehensive of these analyses,

¹ The BFAP Report is entitled *Key fundamentals underlying the crisis in the South African poultry sector*

² The FTI Report is entitled *comments on SAPA’s application for an increase in the customs duty on bone-in pieces and boneless cuts of broiler meat (01 April 2019)*.

³ *Impact analysis on the application for an increase in the rate of customs duty on frozen meat and edible offal of fowls of the species Gallus Domesticus, boneless cuts classifiable under tariff subheading 0207.14.1 and bone-in portions classifiable under tariff subheading 0207.14.9 (08 January 2019) (“NAMC Report”)*.

simulating the effects of tariff increases at both a macro (economy-wide) and a sectoral (domestic chicken industry) level.

- 2.40. In general, the NAMC Report suggests that an increase in the general rate of customs duties on BIP and BLC will lead to increases in the domestic production of poultry, but also to a reduction in consumer welfare in the form of a reduction in household consumption and savings.

3. COMMENTS RECEIVED ON THE APPLICATION

- 3.1. To ensure that the Commission had relevant information at its disposal, comments from interested parties were solicited through the publication of the application in the Government Gazette. Subsequently, ITAC received a substantial number of comments and statements.
- 3.2. **Grain SA** supported the application, citing, *inter alia*, that:
- The poultry industry remains under pressure due to the surge in imports and insufficient safeguard mechanisms in place thereby placing the grain industry in an unfavourable position. The poultry industry is viewed as a very important market within the grain and oilseed value chain;
 - A decline in local poultry production will also have an effect on demand for grain and oilseeds;
 - Grain SA emphasised that the poultry industry is one of the largest consumers of feed and thus it is important to increase local production of chicken; and
 - Considering the link between the poultry, maize and oilseed industries, poultry production in South Africa can form a vital role in creating employment through upward and downward value adding within the value chain.
- 3.3. **Fairplay Movement**, a not-for-profit trade movement whose mandate is focussed on ending predatory trade practices between countries, indicated their support for the application. The main aspects of their comment are as follows:
- The poultry industry accounts for more than 120 000 direct and indirect jobs in the SACU economy and as a largely rural industry, chicken farming impacts most powerfully on rural jobs, small towns and their economies and dependent small businesses. Therefore, job losses due to opportunistic predatory chicken imports directly endanger the viability and sustainability of small towns and the rural economy;

- The Fairplay Movement believes that South Africa is a highly efficient producer of chicken. However, the industry's competitiveness is compromised due to high foreign government subsidies granted in Brazil and the EU; and
- The local poultry industry is viewed as South Africa's most popular source of meat protein and largest staple protein for low-income households. In this regard, the Fairplay Movement stated that any disruption of the local poultry industry will directly affect the food security of lower-income households throughout the SACU region.

In addition to the Fairplay Movement's official comment, the movement also submitted an *op-ed* to the Commission with regards to the impact of escalating Brazilian chicken imports on the local chicken and grain industries.

3.4. The South African Liquor Brand owners' Association ("SALBA") and Vinpro, the wine industry's representative bodies jointly submitted its objection to the application, citing, *inter alia*, that:

- This application may have an impact on general and agricultural South African exports to the USA;
- The increase in tariff might lead to a retaliation by the USA Government and result in increased tariffs on South African products entering the USA; and
- The increase in tariffs on poultry will have a far greater negative impact on jobs in other agricultural sub-sectors should the application be approved and should the USA decide to retaliate with counter measures.

3.5. Merlog Foods (Pty) Ltd submitted its objection to the application, citing, *inter alia*, that:

- There is already high protection for SACU producers on imported chicken. No additional protection should be required. If the industry cannot be competitive and sustainable with the current protections in place the production and marketing model should be revisited;
- Duties will not assist new entrants and development of smallholders to enter the market. We have included some research on the matter, and other interventions will be required to develop the sector; and
- Most importantly the level of trade at which the measure of price suppression or disadvantage has been calculated by applicants must be revisited and

equivalent level of trade determined. Merlog Foods has put forward some proposals to take into account post landed costs to level the playing fields.

3.6. Shoprite Checkers (Pty) Ltd (“Shoprite”) objected to the application based on the effect the tariff increase will have on chicken prices and affordability for the South African consumer. Furthermore, Shoprite also submitted that the tariff increase will not just affect the import price but also result in an increase in the local price due to the lack of competition and shortages of certain cuts.

3.7. The Association of Meat Importers and Exporters (“AMIE”) represented by XA International Trade Advisors submitted its initial comments in objection of the application citing, *inter alia*, that:

- The outcomes of the tariff increase application will have substantial price-rising effects on chicken thereby impacting significantly on poor households. AMIE submitted that for every 10 per cent increase in duties, there may be a 4.7 per cent increase on the price of chicken on the shelf;
- AMIE accepts that some level of tariff protection is necessary and is of the view that the existing levels are adequate;
- The local poultry industry is not under performing or in distress based on the profits attained by certain poultry producers including Astral Foods and RCL Foods in 2018;
- In terms of the duty calculation, SAPA based its request on the required EBIT for the whole business to allow for reasonable return on capital employed (“ROCE”). AMIE contended with the correctness of the benchmark and further stated that if the industry is performing above the benchmark, the duty should be accordingly adjusted downwards;
- There is a severe shortage of wings in the local market and thus the current duties on wings are misplaced;
- The level of trade comparison should be taken into account when ITAC determines the price disadvantage relating to the products concerned. AMIE therefore suggested that the price comparison be selling price to selling price and not selling price of local producers to cost of price of imported chicken;
- The actions by SAPA have been an attempt to reverse the agreement reached between South Africa and the USA in 2015 relating to the rebate of anti-dumping duties. AMIE suggests that the increase in tariffs may negatively impact on South Africa’s position under the AGOA agreement; and

- The local poultry industry is already a highly protected industry and thus if the current protection is insufficient for the local industry, the problems are being misdiagnosed and further increasing the tariffs will not solve these problems.

3.8. **The Organisation of Black Importers and Exporters of South Africa ("EBIESA")** geared towards providing support to emerging black importers and exporters, objected to the application citing, *inter alia*, that:

- EBIESA is in contention with the industry's admission that there is efficiency in the local poultry industry and that there are low priced imports of poultry of inferior quality; and
- EBIESA also expressed that the tariff increase will undermine the consumer and protect the South African industry against world producers which is deemed unfair.

3.9. Comments objecting to the application were received after the close of comment period from Romans Pizza, Frey's Food Brands (Pty) Ltd and National Federation of Meat Traders. However, in making its recommendation, the Commission also considered these comments.

a) **Romans Pizza** indicated, *inter alia*, that –

- Boneless chicken breasts, breast pieces or inner fillets are their single biggest acquired raw material procured for use in their manufacturing plant. In this regard, Romans indicated that should the tariff change, their input cost will surge and as a result the selling price of chicken pizza products will be adjusted accordingly;
- Should the tariff increase and locally produced chicken becomes better priced, they would certainly procure product locally;
- Demand for poultry products increase coupled with challenging economic circumstances and higher cost pressures, local producers will then increase their price throughout the value chain;
- They will be unable to replace or substitute chicken-based products with any other form of protein or value offering as chicken is a staple food source and the foundation of the company's protein offering;
- In terms of quality, it was explained that local un-injected chicken offers a suitable quality aspect but not at a beneficial price-point. In addition, Romans

Pizza has taken the decision in 2018 to steer away from the use of any injected boneless chicken to improve the quality and yield of the product;

- Actual manufacturing yield information provided shows that Romans Pizza makes use of a higher proportion of imported chicken when compared to the use of locally procured chicken; and
- Romans Pizza indicated that should the tariff increase be implemented, it will impact on their business model and therefore on employment levels at national store levels.

b) Frey's Food Brands (Pty) Ltd ("Frey's") objected to the application, stating the following:

- Frey's submitted that the increase in tariffs will have a significant impact on the pricing of boneless chicken, used in their manufacturing processes;
- The company stated that the local poultry industry is unable to fully meet its production requirements and they will still be required to import boneless chicken to meet production demand; and
- The quality of imported boneless chicken is more consistent than locally produced boneless chicken.

c) National Federation of Meat Traders ("NFMT") submitted that it is representative of all role players in the distributive meat industry and is recognised by producers through to consumer bodies. It further submitted that it represents retail outlets, which employ approximately 60 000 employees. NFMT objected to the application and elaborated on the following:

- SA already has a protective tariff of 37% on bone-in chicken imports and 12% on boneless chicken imports;
- These tariffs give enough (excessive) protection to the local chicken producing industry; and
- The consumer is already heavily burdened by the ever-increasing prices of regulated products including transport and energy.

4. STATEMENTS TO THE COMMISSION BY FOREIGN GOVERNMENTS AND ENTITIES

4.1. The Brazilian Association of Animal Protein (“ABPA”), which represents the Brazilian poultry exporters, submitted its objection to the application citing, *inter alia*, that:

- Prices practiced by Brazilian producers are historically higher than the world’s average and its main competitors in the South African market;
- ABPA argued that one of the main reasons as to why SACU is facing difficulties, is due to the fact that South African poultry production was highly affected by the Pathogenic Avian Influenza (H5N8) in recent years;
- The increase in customs duty will also affect the domestic prices and that local chicken production cannot satisfy growing domestic consumption needs; and
- ABPA stated that although the rate increase to 82 per cent is as per the WTO bound rate, this measure would be more restrictive than necessary and engender trade diversion.

4.2. USA Poultry and Egg Council (“USAPEEC”), a national trade association in the USA representing the interests of America’s poultry and eggs export industry, submitted its statement objecting to the application. The main aspects of the statement are highlighted below:

- USAPEEC’s objection is based on the view that the increase in tariffs constitutes the repeal of the agreement between industries of the USA and South Africa, in which the Governments of both countries were involved;
- According to USAPEEC, during the negotiation between Governments in Paris in 2015, there was an agreement that USA would have meaningful access to the South African market under an annual quota arrangement. The commitment purportedly included both the rebate of anti-dumping duty and the application of ordinary customs duty at a rate no greater than the most-favoured nation tariff, which is currently set at 37 per cent; and
- Lastly, USAPEEC believes and attempts to show that the arguments advanced by SAPA in connection with its application are unsupported and untrue.

4.3. The Embassy of the United States of America submitted a statement objecting to the application and alerted the Commission to the following concerns relating to an increase in custom duties:

- A sharp increase of duties will pose a significant obstacle for USA chicken imports into South Africa,
- The USA Embassy also raised the concern about the signals such an increase would send regarding South Africa – USA bilateral trade relationship and additionally highlighted how South Africa has benefitted from its trade relationship with the USA under the AGOA Act;
- According to the USA Embassy's internal analysis, it was found that the increase in duties would effectively halt USA chicken imports into South Africa;
- The USA Embassy also pointed out that the increase in duties will inhibit imports in an anticompetitive manner and make the TRQ for USA chicken imports under rebate of the antidumping duty, unviable;
- The USA Embassy cautioned that food security of South Africa may be affected by the increase application due to the local poultry industry being susceptible to diseases, droughts and extreme weather; and
- It was also highlighted that the tariff increase will not decrease overall imports from all sources but rather result in increased prices for South African consumers.

4.4. The Embassy of Brazil, submitted its statement objecting to application and requested the Commission to consider the following:

- The Brazilian Embassy emphasised that the measure under analysis would have a direct effect on Brazil's exports, since the country is the main international source of the product to South Africa;
- The Embassy also explained their view relating to the impact that the outcome of the SAPA application would have on the economic relations between South Africa and Brazil. The Embassy's main contention in this regard is that the unilateral imposition of an 82 per cent duty would cause trade diversion to the extent that the South African market will be closed to Brazilian producers;
- The Brazilian Embassy proposed alternative cooperative policies that may be pursued to assist with the production deficit in the SACU for poultry inputs, as expressed by SAPA in their application;
- In its supplementary statement to the Commission, the Brazilian Embassy contends that due to avian influenza affecting European exports of poultry, Brazilian poultry became an alternative supply channel thereby causing the increase in "dutiable imports";

- Brazil also gave a brief overview on the impact of the tariff increase on, *inter alia*, consumption, inflation and productivity; and
- Reiterated that a substantive increase in the tariff would displace much of Brazilian poultry imports due to a manipulation of terms of trade and would close the market for the two types of products under investigation.

5. SAPA'S COUNTER COMMENTS

5.1. In response to comments raised by interested parties, SAPA responded, *inter alia*, as follows:

5.1.1. Recurrence of Avian Influenza

- SAPA submitted that it is speculative to suggest that the recurrence of avian influenza maybe a recurring problem in South Africa. Further, the effect on broiler production was minimal and Avian Influenza cannot be seen as a cause of any of the harm suffered by the Participating Producers, particularly before June 2017.

5.1.2. Complementary role of imports

- SAPA submitted that the SACU producers are able to produce sufficient volumes of the subject products to meet demand in the SACU and the primary reason for a decrease in profitability and production volume is the influx of significant volumes of low-priced imports, which prevent SACU producers from increasing their production. There is therefore no need for imports to meet demand.

5.1.3. Negative effect on consumers

- SAPA submitted that the possible effect of the Most Favoured Nations ("MFN") tariff increase on end retail prices is addressed in a report by Genesis Analytics. According to the Genesis Report, an increase in the MFN tariffs does not necessarily translate into a significant increase in retail prices, but the increase, if any, may be immaterial, as there are various other factors that influence retail prices, including competition amongst the Participating Producers and other local producers, the countervailing power of the retailers and competition amongst them; and
- SAPA further submitted that without a tariff increase the SACU poultry industry will be forced to continue to reduce production and employment levels, which will increase unemployment levels and increase malnutrition as less families will be

able to afford basic foodstuffs. As more SACU producers go out of business, SACU will become increasingly reliant on other countries for its food security.

5.1.4. SA Strategic partners (e.g. Brazil)

- SAPA submitted that SACU has the right to exercise its policy discretion to increase import tariffs, so long as the applied tariff does not exceed the bound rate.

5.1.5. Threat of US Retaliation

- SAPA submitted that it would be inappropriate for ITAC to take into account possible reprisals from the United States in making its determination.

5.1.6. Shortage of supply

- SAPA submitted that there is more than sufficient capacity in SACU to meet demand for all products concerned, provided that customers are willing to make firm long term commitments to justify the additional expenditure;
- Inability to supply wings is denied and is not supported by any proof by the importers; and
- The imposition of additional duties of each of the subject products at the requested levels will allow the Participating Producers to regain lost market share and increase production volumes of all cuts, thus allowing for improved economies of scale.

5.1.7. Profitability of major producers

- SAPA submitted that the financial results referred to by the importers are for large groups of companies, which are involved in many different businesses and products that are not part of this application. Furthermore, some of the major producers such as Astral Foods have recently indicated that their headline earning for the most recent period have declined and this is mainly in the sugar and chicken units. RCL Foods on the other hand indicated that its outlook for the financial year is that raw material prices were on an upward trend and consumer's disposal income was under pressure. Higher feed input costs and depressed poultry selling prices will result in significant pressure on profit margins.

5.1.8. Industry inefficient

- SACU industry is a globally efficient producer of chicken but has experienced profitability challenges due to constantly being undercut by low priced and opportunistic dutiable imports.

5.1.9. Level of trade calculation

- The correct level of trade comparison is the landed cost of imports and the ex-factory prices of the domestic industry and is settled practice by ITAC in both tariff investigations and anti-dumping investigations.

5.1.10. Brining

- Brining is lawful in South Africa subject to a limit of 15% and brining is also used in many jurisdictions in the world. It was also submitted that the sale of mixed portions into the SACU market and the age at which chickens are slaughtered is determined by SACU market preferences including a preference for a higher number of smaller portions.

5.1.11. Previous chicken related application

- SAPA submitted that the current application is separate and distinct from any previous applications.

5.1.12. Distinguishing different cuts

- SAPA submitted that the reason for consolidating the data is mainly that the separation of data for the different cuts would not result in an accurate comparison with imports due to the fact that the majority of SACU sales are mixed portions, which contain a variable combination of cuts and as such cannot be accurately compared with any individual 8-digit tariff sub-headings.
- SAPA further submitted that if different tariffs are applied to the different 8-digit tariff subheadings under tariff subheading 0207.14.1, this would allow importers to easily circumvent the payment of the duty by declaring the product under a different tariff subheading as it is impossible to distinguish between these products when they are frozen.

6. FINDINGS

- 6.1.** During its deliberations and in arriving at its recommendation, the Commission considered the information at its disposal, with due regard to food security and effects on downstream consumers, especially the poor, who consumes poultry as one of their main sources of protein.
- 6.2.** South Africa remains the major broiler producer in Southern Africa accounting for 80 per cent of total broiler production in the region. Broiler production dominates the agricultural sector and it remains the cheapest source of protein when compared to all other animal proteins followed by beef.
- 6.3.** The poultry sector has spill over effects in the grain and chick industries, which is evidenced by the fact that it is the second biggest user of maize in the region and a significant user of soybeans.
- 6.4.** For the period under investigation (2015 to 2018), there was an average decline in domestic demand for the products concerned, as well as a decline in the Participating Producers' production volume, capacity utilisation, sales and market share.
- 6.5.** The importers' market share for BIP and BLC has been on an upward trend from 2015 to 2018.
- 6.6.** For the period under investigation (2015-2018), the origin of imports shifted from non-dutiable imports from the European Union ("EU") to dutiable imports from the rest of the world, mainly Brazil and the United States of America ("USA").
- 6.7.** According to information at the Commission's disposal, on average, the Participating Producers' production costs increased between 2015 and 2018. The major cost drivers were input materials (i.e. live bird, feed, labour and utilities). However, as a result of declining feed costs, the Participating Producers experienced a marginal decline in their cost of production in 2018.
- 6.8.** On average, the Participating Producers' net profits have been positive over the period of the investigation. However, profit margins initially declined, before increasing marginally in 2018, which can be ascribed to a decline in feed costs.

- 6.9. On average, the Participating Producers' investment levels increased for the period under investigation.
- 6.10. The Commission found that the domestic poultry industry producing BIP and BLC experienced price disadvantages *vis-à-vis* foreign producers.
- 6.11. The Commission found that, on balance, taking into account the adjudication criteria of a tariff amendment application as well as the potential impact of the duty on consumers, there is adequate justification for an increase in the rate of duty on BIP and BLC.
- 6.12. In terms of following a balanced approach, the Commission determined that the level of duty for BIP, which will minimise the price disadvantage and soften the impact on consumer welfare, amounts to 62 per cent *ad valorem*. At this level of duty, although the price disadvantage would not be removed entirely, it would decline and enable the domestic industry to increase domestic demand for its products, increase its production capacity utilisation and achieve economies of scale.
- 6.13. It was found that the level of duty for BLC, which would remove the price disadvantage and soften the impact on consumer welfare, amounts to 42 per cent *ad valorem*, which would place domestic producers of BLC on an equal footing with similar imported products. At this level of duty, the price disadvantage would be removed and enable the domestic industry to increase the domestic demand for its products; increase its production capacity utilisation; and achieve economies of scale.
- 6.14. It should be noted that the proposed levels of customs duty will provide relief with regard to current industry pressures. However, broader structural reforms, which include, amongst others, investment in industry technology, research developments as well as a meaningful transformation program to accommodate new entrants in the industry, should still be considered.
- 6.15. Reciprocal commitments made by the Participating Producers were provided, particularly with respect to levels of production, investment and employment creation, as articulated in the New Growth Path ("NGP"). The Applicant submitted that should tariff support be granted, production volumes, employment and investment by the Participating Producers are expected to increase between 2019 and 2021.

7. RECOMMENDATION

- 7.1. In the light of the foregoing, the Commission decided that the duties on the products in question be amended as shown below and that the duties be reviewed after a period of 3 years, or such other period as decided by the Commission, to determine the impact on employment, production and investment. It is also envisaged that annual monitoring of the sector's performance will be undertaken to monitor compliance with the Participating Producers' reciprocal commitments:

Tariff subheading	Product	Existing duty	Recommended duty
0207.14.1	Boneless cuts	12% <i>ad valorem</i>	42% <i>ad valorem</i>
0207.14.9	Bone-in portions	37% <i>ad valorem</i>	62% <i>ad valorem</i>