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Re-emergence of South American Beef Exporters: New Competition for U.S. Producers?

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Under new rules defined by the World Trade Organization in the Uruguay Round, sanitary barriers cannot be used for commercial purposes. This rule, combined with the recent eradication of foot and mouth disease (FMD) in Argentina and Uruguay, is allowing these countries to gain access to beef markets that were previously closed to them. This access is expected to lead to a significant increase in South American beef exports to Pacific Rim countries such as the U.S., Canada, Mexico, Japan, South Korea and Taiwan.

FMD is a highly contagious disease capable of inflicting significant mortality and large production losses in herds that have not been previously exposed. As a result of this threat, most countries in the Pacific Rim basis, including the U.S., long followed a policy of zero tolerance to FMD, meaning that they imported only cooked beef from countries with endemic FMD. Because fresh and frozen beef from FMD-endemic countries could not be exported to most FMD-free markets, the price of beef from FMD-endemic countries sold in international markets at a substantial discount, about 50%, of the price of beef from FMD-free countries.

Under the new WTO regulations that resulted from the Uruguay Round, sanitary barriers can be imposed only when they are backed by scientific evidence. Consistent with the fact that FMD is carried in the bones, blood and ganglia of the animal, but not in the muscle, the U.S. negotiated import quotas of 20 thousand tons of boneless fresh beef, each with Uruguay and Argentina. Meanwhile, these countries successfully embarked on a national campaign to eradicate FMD. Uruguay was declared free of FMD without vaccination in 1995, and Argentina in 2000.

Argentina and Uruguay have already shown that they can easily fulfill their U.S. quotas (Table 1).

Beef Exports —continued on page 2

In this issue...

Kyoto Greenhouse Gas Emissions Reduction Targets: Economic Issues and Prospects
Y. Hossein Farzin.............5

Beef Market Update
Steven C. Blank...............9

ARE Faculty Profile
Desmond Jolly...............11

Table 1. Exports of Fresh Beef from Argentina and Uruguay into the U.S. 1998-2000

Fresh Beef Annual Exports
Metric Tons of Product Weight

	1998	1999	2000 – Partial
Argentina	6,704	23,576	14,227 (*)
Uruguay	14,391	21,606	11,185 (**)

Sources: INAC (Instituto Nacional de Carnes, Uruguay) and SAGPYA (Secretaría de Agricultura, Ganadería, Pesca y Alimentación, Argentina).
(*): January-July (**): January-May.

They have been rapidly increasing their exports to other NAFTA members as well. Total NAFTA exports grew from 23 to 85 thousand tons of fresh beef between 1998 and 1999, and are expected to grow more this year since neither Canada nor Mexico imposes a beef import quota.

The quota that the U.S. negotiated with Argentina and Uruguay does not represent a serious threat for U.S. producers, as it constitutes a very small proportion of the U.S. market. For example, Australia and New Zealand currently hold U.S. beef quotas permitting them to export much larger amounts to the U.S., 378,000 tons and 213,000 tons, respectively. However, Argentina and Uruguay have both expressed interest in obtaining larger U.S. quotas. They argue that since Australia and New Zealand have not filled their respective quotas in recent years, the U.S. should reallocate parts of those quotas to them. This proposition has encountered stiff opposition from Australia and New Zealand, but if it succeeds, the supply of imported beef in the U.S. will increase somewhat. Argentina and Uruguay might also sell beef to the U.S. outside the quota, despite the 26.4 percent tariff that applies, because of their low production costs (Table 2).

Beef production in Argentina and Uruguay has been relatively stagnant for decades due the poor export opportunities previously available. The adoption of new technologies has been slow and productivity is still low by international comparison. Only recently have beef producers realized the need for incorporating new techniques in breeding ("early weaning") and fattening (use of silage, and to some degree, grain supplements). Beef prices in Argentina and Uruguay are expected to be higher as a result of gaining access to new markets and higher prices should result in more investment and higher output.

Beef produced in Argentina and Uruguay is leaner than U.S. beef, contains little marbling and, since it is mostly grass-fed, has a different taste. Uruguay and, especially, Argentina have begun to finish some cattle on grain supplements, but rarely for more than 90 days. Most of these animals thus have carcass weights that are too light for the U.S. market and are sold in the domestic market. Argentina's domestic market (85 percent of total production), and in some degree Uruguay's market, are demanding relatively light animals, because consumers associate tenderness with young age and they are willing to pay a premium for small cuts, even though beef from heavier animals could be as tender after a short period of aging. In Argentina, 47 percent of animals slaughtered are calves, young steers and heifers weighing an average of 384 pounds carcass weight. Steers with carcasses heavier than 600 pounds account for 37 percent of total slaughter numbers. Thus, to become a major exporter of cuts to the U.S. market, one possible strategy for Argentina and Uruguay would be to significantly alter their production practices, developing a competitive feedlot industry. But, since the resulting carcasses could be sold domestically (if a part or all could not be profitably sold abroad) only at a

Table 2. Domestic Prices of Cattle (steers). U.S. $/kg liveweight, annual average

	1994	1995	1996	1997	1998	1999
Argentina	0.76	0.79	0.81	0.91	1.06	0.79
Uruguay	0.70	0.82	0.76	0.79	0.87	0.75
Australia	1.01	0.96	0.74	0.86	0.83	0.78
U.S.A.	1.57	1.47	1.43	1.46	1.36	1.45

Sources: Argentina: SAGPYA (pesos/kg; exchange rate is about 1:1 with the dollar); Uruguay: OPYPA; Australia: ABARE, (estimated 60% yield); USA: Agricultural Agricultural Outlook, ERS/USDA, average of Kansas and Texas slaughter choice steers.

Table 3. Argentina and Uruguay Exports to Pacific Rim Countries other than the U.S.; Full 1999, Partial 2000. (Thousand $ FOB)

	Argentina		Uruguay (*)	
	1999	2000	1999	2000
Exports to	(12 mo.)	(Jan-July)	(12 mo.)	(Jan-Aug)
Japan	210	n/a	12,710	20,735
South Korea	—	n/a	110	10,375
Taiwan	5,969	5,438	—	—
Mexico	—	—	14,186	25,784
Canada	26,804	39,389	26,865	26,654

Sources: Uruguay: INAC; Argentina: SAGPYA. *(*) Includes byproducts*

significant discount, this strategy is risky. It seems unlikely that it will be widely adopted in the near future. A different strategy that both countries are already exploring is to compete in some high quality niche markets, e.g., natural (grass-fed, hormone free) beef. Such sales will occur primarily in large urban areas where consuming grass-fed South American beef has a caché with the sophisticated consumer. It does not appear that they will capture a large market share unless some incident creates widespread consumer concern with beef quality that shifts demand to the more natural product.

In fact, Argentina and Uruguay are exporting more manufacturing beef and less high quality beef to NAFTA markets, which is consistent with the export mix of Australia and New Zealand to the U.S. Thus, it seems likely that Argentina and Uruguay will compete more directly with Australia and New Zealand in a number of Pacific Rim markets rather than with the U.S., which tends to export higher quality cuts. Argentina and Uruguay face higher freight costs to Asian markets and to the U.S. west coast than do Australia and New Zealand, but both South American countries have been able to compete better than was expected. They are expanding into several markets, e.g., Mexico (Uruguay), Taiwan (Argentina) and Canada at a surprisingly rapid rate. It seems certain that this expansion will continue as both countries gain access to new markets and gain experience and exposure in the markets in which they are currently operating (Table 3).

Argentina and Uruguay long expected that they would enjoy sharply higher prices if they could eliminate FMD and gain access to markets that were previously closed to them, with fresh boneless cuts. Somewhat surprisingly, a more important benefit that was not initially foreseen in these countries was the ability to sell manufacturing beef, specialty cuts (tongue, liver, lips, tail, kidney) and other byproducts at higher prices. Part of the recent increase in exports is composed of beef cuts and byproducts that previously had less value in domestic markets, e.g., trimmings and other manufacturing beef and specialty cuts like tongue and offal. These sales seem capable eventually of adding as much as 20% to the overall value of the animal. A further increase might occur as a result of selling higher value cuts in higher priced markets.

Ultimately, the higher value achieved in export markets should be reflected in a higher producer price. A number of studies have suggested that the long-run supply elasticity of beef supply in Argentina and Uruguay is about 1, implying that a 20% price increase should lead to a 20% output increase. If so, the higher prices that the two countries are beginning to receive should substantially increase exports in the longer run. Argentina produces about 2.8 million tons, of which 15% is exported, while Uruguay produces about 450,000 tons, of which 55% is exported.

The processing industry in each of the two countries is dispersed, undercapitalized, inefficient in its use of byproducts, and it fails to achieve economies of scale. Exporters are just beginning to learn new ways of marketing beef internationally. As a result, beef from the two countries is more expensive and/or producers in the two countries receive prices that are lower than would be the case if processing efficiency were increased. Efficiency is relatively low because slaughter plants are small and because poor use is made of

many byproducts. Neither country has a significant promotional strategy for its beef. In Argentina, many of the sanitary regulations that are enforced in plants that export are not required in the plants that sell beef only in the domestic market. Since exporting firms must sell a significant part of each animal slaughtered on the domestic market, these firms operate at a considerable disadvantage. The transformation of the National Meats Institute (Instituto Nacional de Carnes, a semi-public organization that basically enforces regulations in the Uruguayan industry) toward a more promotion-oriented institution, and the creation of a similar organism in Argentina, are currently under debate by the respective governments.

Argentina and Uruguay each has significant opportunities to expand beef production and beef exports. The principal limitation on expanding production is that Uruguay has limited land area of sufficiently high quality soils. This makes it difficult to fatten animals on pasture and grain is also more expensive than in Argentina. In contrast, Argentina has an abundance of excellent land, but rapid technological change in cropping during the last decade has made crop production more profitable than livestock. If the two countries linked their production area, they could produce more efficiently. Uruguay has land that is excellent for cow-calf operations, but not fattening, while Argentina has excellent land for fattening and cheap grain. Traditionally, there has been little trade in live animals. Such trade is now legal, but it is impeded by high transport costs, high marketing costs and taxes. If these institutional details can be resolved, the two countries could produce and export more beef to international markets.

The two South American exporters will expand exports to FMD-free countries on the Pacific Rim, including the U.S., at a relatively fast pace in the short run. The amount of beef they can supply is small relative to the total market in this segment and their increased supply will not greatly depress prices. To significantly affect U.S. beef consumers, Argentina and Uruguay will have to obtain a much larger share of the U.S. quota. They are not expected to achieve this goal unless agreement is reached in the future to achieve economic integration between NAFTA and MERCOSUR, the customs union formed by the Southern Cone countries, Argentina, Brazil, Uruguay and Paraguay. In that case, Argentina and Uruguay would export more beef (especially grass fed beef) to the U.S. at the cost of less beef from Australia and New Zealand. Argentina and Uruguay might also substantially increase production of grain fed beef in the longer run.

To significantly affect U.S. beef producers, Argentina and Uruguay must be able to greatly increase their total exports. They will increase exports only as they transform their production and processing sectors. That process will proceed relatively slowly.

Beef cattle grazing in a pasture in Argentinia. New WTO rules and the eradication of foot and mouth disease have opened up new beef markets for Argentina and Uruguay.

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