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Rice Tariffication in Japan: What Does It Mean for Trade?

Rice has long been the staple food of Japan, a country of just over 125 million people with a land area slightly smaller than California. Because of the high costs of producing rice in Japan, rice prices there are among the highest in the world. The wholesale price of domestically grown Japanese rice averages about 306 yen/kg, compared with about 60 yen/kg for California rice arriving at a Japanese warehouse (excluding government markup or tariff) . Rice-exporting countries see marketing potential in Japan, and have sought to persuade it to change the policies that insulate and isolate it from world rice markets. But Japan has effectively kept most imported rice out of the domestic market, arguing that food security requires protecting domestic production.

On April 1, 1999, Japan changes its rice import system to allow imports outside the existing minimum access quota. But subsequent annual increases in the quota will be less than without the April 1 change. The tariff to be applied to imports outside the quota is equivalent to $3,080 per ton at current exchange rates, representing a tariff rate of about 450 percent on last year's U.S. rice exports to Japan. The new tariff is about 20 percent higher than the maximum government "markup" currently allowed for rice imports within the quota.

Total world trade in rice has recently grown to more than 20 million tons per year. Japan imports over 600,000 tons of rice, mostly the high-priced varieties, and therefore accounts for a disproportionate share of the value of world rice trade. However, if Japan were to ease its import policy, the level of rice imports could be higher than under the current managed-trade regime.

Japan's Minimum Access

Until 1995, Japan had maintained an effective ban on rice imports, which rested on the exclusive right of part of its agriculture ministry, the Food Agency, to conduct trade in rice. Under this state trading regime, Japan imported rice only if domestic production failed to satisfy consumption needs. When it joined the General Agreement on Tariffs and Trade (GATT) in 1955, Japan claimed the right to regulate trade in rice and some other commodities under GATT's "Balance of Payments" (BOP) clause that granted concessions to countries with trade deficits. But in 1963, Japan "disinvoked" the BOP rationale for trade barriers as the trade balance went from deficit to surplus in the wake of Japan's successful export of manufactured goods. However, Japan maintained some "residual" trade barriers, such as those for rice and beef, which were to be lifted at an unspecified future time.

In the 1980's, the U.S. rice industry twice petitioned the U.S. government to persuade Japan to relax its barriers against rice imports, and U.S. officials frequently raised the issue with Japan. However, Japan refused to alter its stance, and in most years imported no rice other than a relatively small quota that was opened in 1972, principally for the use of Okinawa's sake brewers, when the Okinawa island group passed from U.S. to Japanese control.

The Uruguay Round (UR) of GATT negotiations focused particularly on barriers to agricultural trade, and in general were able to "tariffy" nontariff barriers—i.e., to substitute tariffs on imports for fixed quantitative limits to trade. However, negotiating countries agreed to exceptions under conditions spelled out in Annex 5 to the UR Agreement on Agriculture (URAA). Annex 5 provides that a developed country (such as Japan) will allow "minimum access" for imports in the first year of URAA commitment equal to 4 percent of average annual consumption in the UR base period, 1986-88. This rises in annual increments of 0.8 percent of the base period consumption until it reaches 8 percent in the final year.

Japan's first year of URAA commitment was Japanese fiscal year (JFY) 1995 (April 1, 1995-March 31, 1996), and the final year is 2000, with quantities of required imports rising from 379,000 tons of milled rice to 758,000 tons in 2000. Japan imported rice according to this commitment through JFY 1998, with imports reaching 606,000 tons (milled basis), or 6.4 percent of the base period consumption. However, Annex 5 of the URAA also allows a developed country to "tariffy" its import barriers (convert an import ban or quota to an import duty) at the beginning of any year. In accordance

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with Annex 5, Japan announced that it would lower annual market access increases in 1999 and 2000 from 0.8 percent of base period consumption to 0.4 percent on April 1, 1999. While Annex 5 requires that Japan continue to meet its existing minimum access amount (606,000 tons in 1998), the smaller increases in minimum access will put the import quota in 1999 at 644,000 tons instead of 682,000, and in 2000, the quota will be 682,000 tons instead of 758,000. Until another agreement is made, Japan's annual minimum access after 2000 will remain at 682,000 tons.

The tariff for imports within the minimum access quota is zero, but the URAA allows Japan to add a markup to within-quota imported rice of up to 292 yen/kg when it enters Japan. The markup remains a part of Japan's new import rules. For imports above the minimum access amount, Japan has specified a tariff of 351.17 yen/kg in 1999 and 341 yen/kg in 2000.

In addition to the tariff on over-quota imports, the Japanese government reportedly also wants to implement a special safeguard mechanism. One version of this proposal, which has not yet been officially announced, states that if over-quota imports exceed 30,000 tons, or if imported rice prices fall below 90 percent of the average for 1986-88, an additional tariff of 117.6 yen could be imposed, bringing the total tariff in 1999 to 468.77 yen/kg. Presumably, the special safeguard would be removed at the end of the fiscal year in which it was imposed.

Tariff Puts Foreign Rice Out of Reach

Japan's tariffication measures will slow the rate of increase in minimum access in 1999 and thereafter, reducing the previously expected level of imports in 2000 by 76,000 tons. Since the U.S. has accounted for a large share of Japan's imports to date (nearly 50 percent), U.S. rice exports will likely be lower than they would have been without tariffication. Hardest hit will be California, since the overwhelming majority of U.S. rice exports to Japan under the minimum access arrangement has originated in California. Other major suppliers to Japan have been China, Australia, and Thailand.

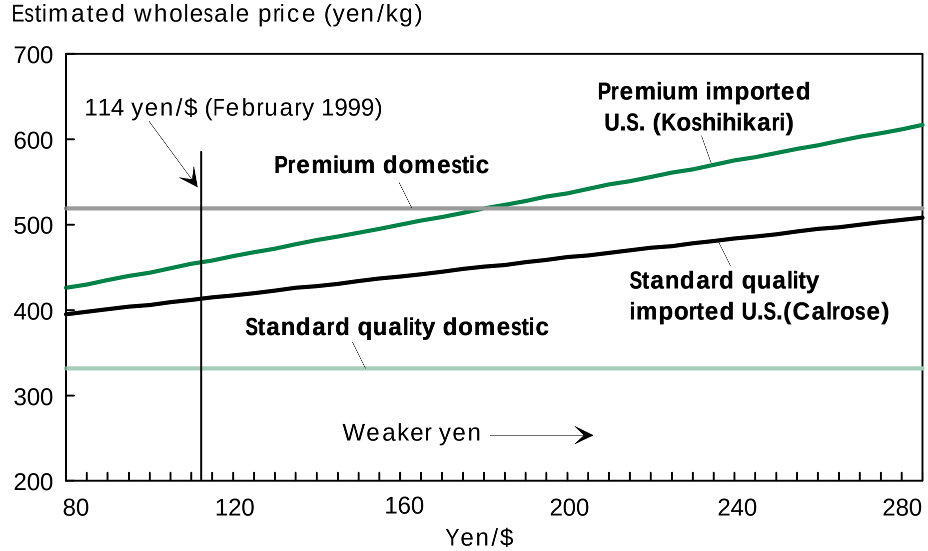
Could relatively high-quality rice conceivably be imported over the quota and still compete with Japanese production? The effect of the tariff (equivalent to about $3,080 per ton at an exchange rate of 114 yen/$) depends on the price of imported rice relative to domestic. Using January to November 1998 prices (c.i.f., milled rice—includes cost, insurance, and freight) for Regular Minimum Access imports, the tariff of 351.17 yen/kg will raise the per-kg price of Chinese rice to 425 yen/kg (up 474 percent), Australian rice to 435 yen/kg (up 420 percent), and U.S. rice to 429 yen/kg (up 449 percent). In contrast, Japan's highest-priced rice type, Uonuma Koshihikari, sells at wholesale for 519 yen/kg, and standard quality rice sells at 332 yen/kg.

Sales results from a special part of the quota reserved for the "simultaneous buy-sell system" (SBS) indicate that there is virtually no chance that any rice paying the over-quota tariff could compete. The SBS has been used with some success in other commodity markets, such as the Japanese and Korean markets for beef. In an SBS, private-sector buyers and sellers

Rice Preferences Vary

Because rice consumption is so differentiated in Japan, it presents a potential market for several different kinds of rice imports. While there is some demand for long grain indica rice in ethnic restaurants, the main table rice is shorter grain japonica rice. The table-rice market is further differentiated by preferences for certain varieties of short grain rice, and these varieties are sometimes promoted as products from a certain area, such as a prefecture or town. Smaller markets exist for glutinous (very sticky) japonica rice and for rice for industrial uses, such as sake (rice wine) brewing and rice crackers, etc. Organically produced rice is popular and commands a price premium. Japanese rice is sold as a single variety or marketed as a blend. Most imported rice is blended with other rice and Japanese consumers do not know its origin.

Weaker Yen Makes U.S. Rice Less Competitive in Japan



Imports are outside quota (no markup), and include a 351-yen/kg tariff. In 1998/99, Calrose (medium-grain japonica) accounted for about 88 percent of U.S. rice exports to Japan. Koshihikari (premium short-grain japonica) accounted for a large share of the remainder.
Source: *Rice Market News* (USDA), industry sources, and U.S. Embassy, Tokyo.
Economic Research Service, USDA

can negotiate directly to determine the quantity, quality, timing, etc. of a sale. In the Japanese rice SBS, buyers and sellers propose a quantity and price of rice to be exchanged. The Food Agency then examines all bids, choosing those that have the widest margin between the proposed selling and buying prices. The Agency keeps the margin.

The margin is the markup, which under the URAA cannot exceed 292 yen/kg. The closer the margin gets to 292 yen/kg, the more likely the Food Agency will accept the bid, so buyers' and sellers' bids reflect pressure to maximize the difference. However, at some price buyers will lose money if they cannot dispose of the imported rice within Japan and recover at least the SBS purchase price. Results of recent SBS sales give some idea of the maximum price at which imported rice types can be sold in the Japanese market.

The outcome of the last SBS sale—a total of 30,000 tons on December 9, 1998—indicates that a tariff of 351 yen/kg is likely to preclude any over-quota purchases. The markup for whole-grain rice sales (milled and brown) ranged from 167 to 179 yen/kg, and for broken rice was about 50 yen/kg. Sale results indicate that the highest marketable addition to imported rice prices—whether markup or other additions such as a tariff—is currently around 179 yen/kg, and current market conditions would clearly not support over-quota sales with an added 351-yen/kg tariff. Nor would a reduction to 341 yen in 2000 be enough to stimulate over-quota trade.

Import Prices Remain High

Behind the Japanese government's decision to impose a high tariff on rice is the high price of domestically produced rice in Japan, upwards of 400 yen/kg at retail. Japanese producers' prices are about two-thirds of retail rice prices, with the remainder going to wholesale and retail marketing costs. During the 1990's, the Japanese government has taken steps to allow more competition in retailing and wholesaling of rice. However, producer prices, although somewhat lower than in the past, remain extremely high because of the government's trade and agricultural policies.

Pressure to keep prices high reflects fears that lower prices would put small-scale, high-cost farmers out of business, and that larger scale, low-cost farmers would lose the extra income that comes from high prices. Despite the URAA, the Japanese have effectively kept most imported rice out of the domestic market in order to prevent greater supply from depressing prices. In addition, the government has bought large stocks of Japanese rice and expanded a program to pay producers to divert riceland to other uses, in order to keep producer prices strong.

Since Japan sets its tariff in yen, the effect of the tariff on import demand varies with the exchange rate. The rise of the yen from 360 per dollar—the fixed rate prevailing in the 1970's—to rates as low as 80 yen per dollar in 1995 made Japanese rice much more expensive compared with imported rice. In 1998, the yen ranged from 147 per dollar to 108 per dollar.

Given a tariff level at 351 yen/kg, Japanese buyers are unlikely to import any rice other than premium outside the minimum access amount. With a very strong yen, premium U.S. rice may be competitive with top-quality Japanese varieties. But regardless of the exchange rate, prices for standard quality U.S. imports—including the 351-yen/kg tariff—would not be competitive with domestic rice in Japan. Japan will, however, meet its commitments for minimum access quantities. The minimum access quota is divided into two components: the SBS share and the general quota. A minimum SBS share is mandated by the URAA, and the remainder, the general quota, is purchased by the Food Agency, which puts most of it into stocks.

The government currently aims to replace rice stocks each year. Very little Food Agency imported rice is consumed as table rice in Japan; industrial use, feed use, and food aid exports have been the primary uses of imported rice. Since the Food Agency paid an average of 68,000 yen per ton for the imports ($599/ton at 114 yen/$—the average exchange rate for the first 2 weeks of February 1999) and sold most of the rice at a lower price or donated it, the government lost money on this rice. In addition, the cost of storing rice for a year is substantial, especially for brown rice, which is stored in refrigerated warehouses.

The amounts of rice imported under the SBS, which allows rice exporters greater contact with Japanese buyers, far exceed the minimum share mandated in the URAA, increasing from 3 percent of total Japanese rice imports in JFY 1995 to 19

Japan: California Rice Growers' Best Customer

Japan produces and consumes primarily japonica rice, a variety usually purchased by higher income countries. Japonica accounts for about 15 percent of world production and 11-12 percent of world trade in most years, while indica rice accounts for more than three-fourths of world production and trade. Japonica rice is slightly more rounded (or plump) and stickier than indica, and typically sells at a premium to indica in international markets.

Japan is the world's largest importer of japonica rice, which accounts for the bulk of Japan's rice imports. Without Japan's purchases, world japonica trading prices would be much lower than today, as was the situation during most of the 1980's after South Korea—the largest importer at that time—withdrew from the market. The bulk of world japonica exports are from Australia, the U.S., and China, with smaller quantities supplied by Egypt, the European Union, and Taiwan (food aid only). Besides Japan, other major japonica importers are Turkey, Jordan, and South Korea.

California produces mostly japonica, and Japan is now the largest export market for California rice. In U.S. market year 1997/98 (August-July), Japan accounted for about half of California's rice exports and almost one-fifth of the state's crop. Without the Japanese market, California would have severe excess supply, lower prices, and would likely decrease production.

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Japanese Tariff Significantly Raises Prices for Imported California Rice

Representative wholesale price for:	Yen/kg[1]	$/ton[1]
Calrose (standard quality)		
California price (fob, mill)	49	430
Marketing costs	11	94
Warehouse price in Japan	**60**	**524**
Within-quota imports		
Markup (RMA)[2]	163	1,427
Estimated wholesale price	**222**	**1,951**
Outside-quota imports		
Tariff[3]	351	3,080
Estimated wholesale price	**411**	**3,604**
Koshihikari (premium quality)		
California price (fob, mill)	80	700
Marketing costs	26	231
Warehouse price in Japan	**106**	**931**
Within-quota imports		
Markup (SBS)[4]	179	1,570
Estimated wholesale price	**285**	**2,501**
Outside-quota imports		
Tariff	351	3,080
Estimated wholesale price	**457**	**4,012**

1. Exchange rate 114 yen/$ (average of first 2 weeks in February 1999). 2. Average markup for 1998 Regular Minimum Access imports. 3. Tariff scheduled to be implemented April 1, 1999. 4. Highest reported markup for October simultaneous buy-sell tenders.
Source: *Rice Market News*, Agricultural Marketing Service, USDA; Japanese and U.S. industry sources.

Economic Research Service, USDA

percent in JFY 1998. Since the Food Agency keeps the price margin or markup, it makes money on the SBS rice, instead of losing it in general quota purchases, and further expansion of the SBS might be expected. However, as the quantity of imports actually competing with Japanese domestic rice increases and greater rice supply acts to depress prices within Japan, the Food Agency may be pressured to limit expansion of the SBS.

Rice varieties imported through the SBS have been very diverse, reflecting strong differentiation of rice markets within Japan and worldwide. For example, in the December 1998 SBS sale, c.i.f. (selling) rice prices in successful bids ranged from 45 yen/kg to 180 yen/kg. Some imports appear destined for table use, such as the Chinese short grain milled rice which dominated in 1998, while other imports were industrial use or glutinous rice (a market which California has dominated). Little of the rice recently imported under the SBS has been medium grain, the predominant rice produced in California and Australia, which makes up the largest share, by type, of purchases made by the Food Agency in the general quota.

Japan's government continues to argue that stringent protection at the border is required to ensure that rice production area does not fall drastically, for both food security and environmental reasons. In Japan, rice paddies are considered a defense against flooding as well as a water filtration system. In addition, rice cultivation has cultural and aesthetic dimensions.

Japan's trade partners counter that food security is better achieved through free trade and that environmental and other possible benefits of rice farming should be realized through other means than high rice prices and barriers to trade. The coming multilateral negotiations for a new World Trade Organization agreement are likely to address these arguments as well as the size of Japan's proposed tariff on rice. **AO**

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