Oral Testimony by
Shawna Morris on behalf of
The National Milk Producers Federation
To the United States International Trade Commission
Regarding
"North American Free Trade Agreement: Advice on the Probable Economic Effect
Of Providing Duty-Free Treatment for Currently Dutiable Imports"

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Thank you Madam Chairman and members of the Commission for the opportunity to present testimony before you today on the dairy industry's interests and concerns regarding negotiations to modernize the North American Free Trade Agreement (NAFTA). I am Shawna Morris, Vice President for Trade Policy of the National Milk Producers Federation.

NMPF represents America's dairy farmers and the dairy cooperative marketing associations they own and operate throughout the United States.

Our written submission provides extensive detail on the growing importance of trade in general and of NAFTA in particular to the U.S. dairy industry. I will only briefly summarize these and focus most of my testimony on the specific issues that will be of most interest to us as we embark on negotiations with Canada and Mexico to modernize NAFTA.

Over the last two decades the U.S. has shifted from being a consistent net importer of dairy products to a significant net exporter and over the past five years our cumulative exports were more than double our import total. We've gone from exporting less than $1 billion in 2000 to exporting a high of $7.1 billion in 2014, before a dip in foreign demand dropped us to about $5 billion in 2016.

Our NAFTA member partners, Mexico and Canada, are our top two foreign markets, accounting for over a third of our global exports. In 2016, we exported $1.2 billion worth of product to Mexico and more than $600 million to Canada.

But the significance of the export figure to Canada must be tempered by the fact that a sizable portion of our shipments to that market ends up being for further processing and ultimate re-export outside of Canada, including back to the United States.

As I will discuss further in a moment, our exports to Canada remain greatly restricted by measures that were left untouched by NAFTA and by measures introduced more recently.

The importance of the Mexican market to our industry needs no qualifier, however.

The $1.2 billion in product we shipped to Mexico last year is 10 times higher than what we shipped in 1995. NAFTA has been the driving force behind this remarkable growth.

Without NAFTA, the duty-free access we enjoy into Mexico could evaporate and be replaced by WTO most-favored nation tariff levels. This would dramatically undermine a core advantage of U.S. suppliers as the only major dairy supplier to Mexico currently benefiting from free trade.

If our competitor countries, such as the EU which is actively negotiating an FTA extension with Mexico, were to negotiate zero duty treatment in Mexico for their dairy products, our 73% share of the Mexican import market could wither away. That is what makes NAFTA absolutely essential for our industry.

Because of NAFTA and because of Mexico's commitment to a mutually beneficial trading relationship, we currently have very few trade problems with Mexico in dairy. It is our goal to keep it that way.

In the NAFTA negotiations involving Mexico, our focus will mainly be on improving rules-based matters, such as adopting new commitments on geographical indications and strengthening obligations on sanitary and phytosanitary measures.

Our goal with respect to Canada, on the other hand, is quite different.

Canada's continuing efforts to use policy tools to undermine access to its market and impair the value of concessions for products containing dairy are a very deep concern, which absolutely require a solution through the NAFTA modernization discussions. This opportunity cannot be squandered.

Canada's market for imported dairy products is tightly restricted in virtually all product areas. Canada's over-quota tariffs for the vast majority of dairy products are roughly between 200 and 300% and U.S. dairy exports are still subject to them.

We estimate that full bilateral tariff removal between the United States and Canada could increase U.S. milk prices by an average of about 40 cents a hundredweight during an assumed phase-in period of 2017-2022, during which time U.S. dairy farmers would earn additional income from milk sales of about a billion dollars. That presumes, however, that the U.S. is actually able to capitalize in practice on the access Canada would grant.

For years, Canada has used one policy or regulatory tool after another to chip away at the access it has granted under other agreements. Given this, an environment of uncertainty about ongoing access to the Canadian market has always existed.

There must be absolute clarity moving forward that current dairy sales to Canada – and, of course, new access established under the NAFTA modernization negotiations – will take place without Canada introducing measures intended to inhibit or block them. We need meaningful disciplines to ensure that access on paper equates to access in reality.

We have included in our written submission descriptions of a number of actions by Canada to close off the valves of imports whenever trade has started to cause domestic political problems.

However, I must spend a few moments to highlight Canada's recent use of milk class pricing schemes to actively restrict U.S. exports. They do this in two distinct ways.

First, they undermine U.S. exports to Canada, particularly ultra-filtered milk, which enjoyed duty-free access under NAFTA and had seen growing sales in recent years.

Second, they allow Canadian milk powder prices to undercut U.S. and other commercial dairy suppliers on the global market.

In the spring of 2016, the province of Ontario approved a special Class 6 milk class for ingredient usage that was intentionally designed to force out competition from U.S. imports and provide an incentive for Canadian processors to use domestic product instead.

Subsequently, Canada moved to expand this program through the National Ingredients Strategy and implement a Class 7 milk arrangement across the country. Class 7 began to be implemented across Canada in February 2017.

Class 7 establishes a new ingredient milk class to be priced at the lowest of the US, EU and Oceania price for solids-not-fat for 7 years and then adds onto that a very generous so-called processor "make-allowance" adjustment that in practice leads to the offering of Canadian product at prices that can be far below even the lowest of prevailing world commodity prices.

Reports to date from various markets around the world indicate that product is being offered even below the lowest world market price. This below-cost pricing avenue applies to the manufacture of skim milk powder, whole milk powder, milk protein concentrate, ultra-filtered milk and similar dairy protein products.

This recently introduced provision of below market price milk for the production of the listed dairy products provides an incentive to substitute those products for their imported counterparts in Canada while enabling the export of Canada's structural surplus of skim milk powder at below the cost of production.

It flies in the face of common sense that a country with one of the world's highest milk prices would be offering a commodity dairy product at levels far below those offered by all other major dairy suppliers.

This type of mismatched result can only be achieved through government policies designed to put a thumb on the scale of global milk powder commerce to favor Canada. As a result, these pricing schemes have already harmed U.S. exports to Canada of ultra-filtered milk and have begun facilitating the dumping of Canadian milk powder onto the commercial global markets – markets on which the U.S. so much relies.

This is the latest in a series of narrowly targeted milk classes that have been created over the past few years specifically aimed at displacing imports. This new one adds the harm of also displacing U.S. exports to other markets.

Given the damage to our export interests that we're already experiencing, we are urging the U.S. to secure an immediate halt of Canada's Class 6 and 7 pricing schemes and to use the NAFTA negotiations to permanently end this new form of trade distortion.

I must also mention several over-arching issues of enormous importance to us.

The first is the treatment of geographical indications, or GIs. There are unique issues with both Mexico and Canada involving GIs that will need to be dealt with appropriately on a bilateral basis. In addition to those efforts, however, it is essential that the NAFTA negotiations incorporate specific text on the issue of GIs and common names.

This would be in keeping both with the Trade Promotion Authority directive to address this issue and the Administration's intention to modernize the agreement as it relates to more recently emerging trade issues.

In order to build upon the progress made to date with our trading partners on this issue, we encourage the Administration to use the TPP text on GIs as a starting point and further improve upon that to preserve U.S. market access opportunities for common name products despite foreign governments' efforts to misuse GIs to erect barriers to those products.

The second over-arching objective is to include what we call a "WTO-Plus" Chapter on sanitary and phytosanitary measures.

Our industry helped spearhead an effort to include such a chapter in the Trans Pacific Partnership (TPP) negotiations. The goal was to strengthen the existing WTO SPS commitments in order to address the escalating threat that unwarranted and sudden SPS measures were posing for U.S. agricultural exports.

We believe that it is critical that the NAFTA modernization effort incorporate the work done in this area within TPP and work to build further upon that base of "WTO SPS-Plus" commitments.

I thank you for the opportunity to present these views on behalf of the U.S. dairy industry.