Not So Cool? Economic Implications of Mandatory Country-of-Origin Labeling

by

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The 2002 Farm Bill mandated country-of-origin-labeling for fresh and frozen food commodities. This regulation provides uncertain benefits unlikely to exceed its costs. As a form of protectionism, it may be especially costly for export-dependent California agriculture.

Japan has mandatory country-of-origin retail labeling requirements for agricultural products that principally affect fruits, vegetables and animal products–a scheme that is generally regarded by the rest of the world as protectionist. In the U.S., some states such as Florida also require country-of-origin labeling of fresh fruits and vegetables. Now the entire United States is getting in on the act. The 2002 U.S. Farm Bill mandated country-of-origin-labeling (COOL) for fresh and frozen food commodities such as beef, pork, lamb, fish, fruits and vegetables, and peanuts. The new law will take effect in September 2004. Is this a good idea for California agriculture? We do not think so and the purpose of this article is to explain why.

The Simple Economics of Country-of-Origin Labeling

The direct costs of COOL will include the costs of segregating and tracking product origins throughout the marketing chain, enforcement costs, and distorted producer and consumer prices. Some foreign products will even be taken off the retail shelves.

The U.S. government itself forecasts that domestic producers, food-handlers and retailers will spend $2 billion on COOL in the first year. The Food Marketing Institute estimates that compliance by fruit and vegetable suppliers alone will cost $1.3 billion annually. The U.S. General Accounting Office (GAO) reports that the cost of monitoring COOL for produce will be about $56 million annually. From a policy perspective, whether these costs outweigh the benefits to society of the program, and the extent to which retailers, producers and consumers will share these costs, are of equal importance.

COOL imposes a "deadweight" cost because it creates a wedge between producer and consumer prices, much as a per-unit tax does. It will raise the consumer price and lower the producer price for most products. Imported products will be scarcer at the retail level. Putting aside any potential benefits of the information contained in COOL, higher prices for consumers means that demand for labeled products will fall and profits for suppliers will decline accordingly. How much demand falls depends on consumers' willingness to substitute away from labeled products to unlabeled goods (e.g., from beef to chicken, which is not subject to the regulation).

Supporters of COOL often point to consumer surveys that show they have a stated preference for country-of-origin food labeling, but economic logic and empirical evidence both suggest that the benefits of COOL are unlikely to outweigh the costs of compliance. It is true that consumer surveys indicate that American consumers say they would prefer to buy U.S. food products if all other factors were equal, and that consumers believe American food products are safer than imports. These surveys also suggest that labeling information about freshness, nutrition, storage and preparation tips is more important to consumers than country-of-origin. More tellingly, the fact that producers have not found it profitable to voluntarily provide COOL to customers is strong evidence that willingness to pay for this information does not outweigh the cost of providing it. This view is consistent with the conclusion of the U.S. Food Safety and Inspection Service that there is no evidence that "a price premium engendered by country-of-origin labeling will occur, and, if it does, [that it] will be large or persist over the long term."

Some foods are now voluntarily labeled for a variety of reasons. Producers of organic products have voluntarily labeled their products to try to capture a price premium, as have producers of "dolphin-safe" tuna. If demand for information exists,

the agricultural and food industry has generally been quick to seize this opportunity. This is the reason that lamb imports from Australia and New Zealand bear country-of-origin labels going beyond legal requirements: consumers prefer this product to domestic lamb. The USDA previously created a voluntary COOL program. It has not been widely adopted.

There are other non-economic arguments that are used to support mandatory COOL that relate to food safety. It is possible that COOL would make tracing disease outbreaks easier, thus reducing the health costs of food-related diseases. This is less likely than might initially seem to be the case, because of the long delay between disease outbreaks and the shipment of contaminated products. If domestic products are systematically safer than foreign products, substitution towards domestic goods could also increase the average safety level of food consumed. However, there is no scientific evidence that demonstrates foreign food products are less safe than domestic products. Existing inspection rules ensure that foreign and domestic meats adhere to the same standards. Foreign fruits and vegetables do not carry more pesticide residue than domestic produce does.

Explaining Political Support for COOL–It is Simple Protectionism

Not surprisingly, many retailers have argued that the cost of COOL implementation will be excessive. These costs will be borne by the private sector, as the Farm Bill provides no funds to alleviate industry costs for developing and maintaining the necessary record-keeping systems. While retailers' organizations, like the Food Marketing Institute, are against mandatory COOL, the strongest criticism has come from the meatpacking and processing industry. In particular, the costs of tracking and labeling the origin of ground meat products will be high.

The American Meat Institute has pointed out that COOL regulation will result in companies sourcing their meat domestically in order to simplify compliance with labeling requirements. As a result, consumers will not have access to a variety of imported meat that may be either of higher quality or a better price. The National Pork Producer's Council estimates that the cost of COOL implementation will translate into a $0.08 per pound increase in the average retail cost of pork.

Agricultural producers are a more easily identifiable constituency for members of Congress than consumers, retailers and even meat packers. Growers and ranchers have largely supported COOL. The California Farm Bureau, among other such organizations, has endorsed the COOL regulation. These organizations generally argue that consumers have a "right to know" the country-of-origin, and that COOL is a valuable "marketing tool." However, some grower organizations have openly characterized COOL as relief from foreign competition. We believe this support from California farm groups is shortsighted because it sends a message to trading partners that U.S. agriculture is protectionist. Foreign markets are extremely important to California agriculture, and so the state's industry has a huge stake in increased trade liberalization, not more protectionism. See, for example, the article by David Roland-Holst in this issue of the *ARE Update*.

Table 1 provides a comparison of origin labeling regulations in other countries compared to the provisions in the U.S. Farm Bill. In 2002, the EU required member states to label all beef at the retail level, including ground beef, with information on the country of birth, place of fattening and slaughter. Canada, Mexico and Japan all have some version of COOL regulation though only Japan has rules as strict as those in the 2002 Farm Bill.

One of the main arguments in favor of COOL, discussed above, has also been used to justify mandatory labeling of genetically modified (GM) food in Europe. That is, the consumer has a "right to know" what they are eating. The U.S. government has strongly opposed mandatory GM labeling, and for good reason. In practice, GM labeling has not given EU consumers greater choice, because food processors in Europe have recombined ingredients away from GM food to avoid labeling. The same phenomenon has taken place in Japan. This pattern may well develop with COOL and therefore U.S. consumers will not be given a choice because imported labeled food will not be made readily available. Instead, the imported commodity will be processed, re-exported or sold into the restaurant or food service industry, to avoid COOL.

As a non-tariff barrier to trade, COOL may be challenged at the WTO, or at least become subject to negotiation. COOL compliance may be most costly for developing country suppliers to the U.S. market who lack record-keeping infrastructure to maintain

Table 1. Comparison of Country-of-Origin Food Labeling Requirements

	U.S. Farm Bill	Japan	Australia & New Zealand	Canada	Mexico	EU
Retail COOL for fresh produce?	YES	YES	NO	Varies- Ontario and Quebec only	NO	YES
Comments	Florida has had mandatory COOL since 1980	About 10 popular products covered	Proposal under consideration	Provincial decision	Grapes, avocados and mangos have specific rules	
Retail COOL for fresh meats?	YES	YES	NO	YES- Pre-packaged meat, NO- imported meat processed in Canada	YES- Pre-packaged meat NO- imported meat processed in Mexico	YES
Comments	Exception for processed products	Full traceability within domestic beef industry	Proposal under consideration	"Processed" determined by a rule of 51% value added (including labor)		Label must indicate country of birth, fattening and slaughter

Source: Compiled from various USDA Foreign Agricultural Service attaché reports available at www.fas.usda.gov/scriptsw/attacherep/default.asp.

audit trails. To this extent, COOL directly conflicts with the spirit of trade liberalization in the current WTO round, which aims to give preference to the trade agendas of developing countries.

The U.S. Export Enhancement Program (EEP) offers export subsidies which purportedly offset export subsidies and trade distortions used by export competitors, such as the EU. To continue to justify EEP spending, U.S. Congress expanded its list of unfair trade practices to include "unjustified trade restrictions or commercial requirements, such as labeling, that affect new technologies, including biotechnology." The irony of this new requirement in the same piece of legislation mandating country-of-origin labeling will not be lost on U.S. trading partners.

California growers have a great deal to gain from breaking down foreign trade barriers for fruits and vegetables. This is less true for Florida growers, who are not as dependent on foreign markets as California is. Thus, COOL may be cool for Florida growers but not so cool for California farmers.

For additional information, the authors suggest:

Americans for Labeling (2002), "The top ten reasons why U.S. consumers deserve swift implementation of country-of-origin labeling," http://www.americansforlabeling.org/resources/topten.htm.

Golan, E., F. Kuchler, L. Mitchell, C. Greene, and A. Jessup (2001), "The Economics of Food Labeling," ERS/USDA Agricultural Economic Report No. AER 793, January.

Hayes, D. J. and S. R. Meyer (2003), "Impact of mandatory country-of-origin labeling on U.S. pork exports," Iowa State University mimeo.

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