

Committee on Safeguards

Original: English

NOTIFICATION PURSUANT TO ARTICLE 12.1(C)
OF THE AGREEMENT ON SAFEGUARDS

Supplement

The following communication, dated 24 March 1997, has been received from the Permanent Mission of Korea.

Further to my letter of 21 January 1997, I wish to inform you that the Korean Government has taken a final decision on the application of a safeguard measure on certain dairy products. This decision was taken, and went into effect on 7 March 1997.

You will recall that in my aforementioned letter, I reserved the right of the Korean Government to provide further relevant information as necessary. In this line, attached herewith is a further notification regarding this matter, which I request be circulated as an addendum to our previous notification under Article 12.1(c) of the Agreement on Safeguards (G/SG/N/10/KOR/1 of 27 January 1997).

**ADDENDUM TO NOTIFICATION UNDER ARTICLE 12.1(C) OF
THE AGREEMENT ON SAFEGUARDS**

(G/SG/N/10/KOR/1 of 27 January 1997)

With respect to the safeguard measure on certain dairy products as notified to the Safeguard Committee through G/SG/N/10/KOR/1 on 27 January 1997, the Government of the Republic of Korea hereby notifies the contents of the safeguard measure upon the taking of a final decision on 7 March 1997. The final decision was taken after having comprehensively reviewed the opinions of countries which participated in the bilateral consultations (the EU, Australia and New Zealand on 4 and 5 February 1997) and the special meeting of the Committee on Safeguards held on 21 February 1997. This is an addendum to notification G/SG/N/10/KOR/1 of 27 January 1997, which shall continue to apply unless otherwise modified by this Addendum.

1. Items subject to the safeguard measure

The products subject to the safeguard measure fall under four categories¹ of the Harmonized System of Korea (HSK) : 0404.10.2190, 0404.10.2900, 0404.90.0000 and 1901.90.2000.

Among the above products, milk mineral (calcium) concentrated product (limited to use as an additive for the production of mineral fortified food), whey protein concentrated product, milk protein concentrated product (limited to use as an additive for the production of protein fortified food), Chilean special products and raw material for production of Cerelac of Nestlé which are not "mixtures of milk powder" shall be exempted from the safeguard measure.

2. Date of implementation, duration and quota

The safeguard measure will go into effect as of 7 March 1997. Quotas during the period subject to the measure are as follows:

	Mar. 7'97-Feb. 98	Mar. '98-Feb. '99	Mar. '99-Feb. 2000	Mar. 2000-Feb. 2001
Quota (tons)	20,521	21,691	22,927	24,234

¹Subheading numbers 0404.10.2190, 0404.10.2900 and 0404.90.0000 were classified into one item (0404.90.0000) when the KTC carried out the investigation.

1. 0404.10.2190 (Modified whey/whey from which all or part of the lactose, protein or minerals have been removed/other than Lactose removed, demineralized and whey protein concentrates.)
2. 0404.10.2900 (Modified whey/other than whey from which all or part of the lactose, protein or minerals have been removed.)
3. 0404.90.0000 (Other than whey and modified whey.)
4. 1901.90.2000 (Food preparations for goods of headings 0401 to 0404 except goods containing more than 10% cocoa powder.)

3. Method of quota allocation

Quotas shall be commonly allocated irrespective of country of origin and product. This content was announced pursuant to legal procedures set forth in the Foreign Trade Control Regulation.

End users of imitation milk powder such as milk processing companies, confectionery, bakery companies, and food manufacturing companies are entitled to import imitation milk powder. The quota for the first year shall be allocated on a *pro rata* basis to end users based on the quantity they imported in the past while those for the following years shall be distributed prior to the beginning of each term, based on the ratio of imports recorded in the previous year. However, a quantity not exceeding 10% of whole quota shall be reserved for new participants. The final subquota of each end user shall be fixed after the quota for new participants is adjusted to the extent that it shall not exceed the minimum quantity to be allocated to existing end users.

4. Consideration for developing countries

Pursuant to Article 9.1 of the Agreement on Safeguards, this safeguard measure shall not be applied against any product originating in a developing country Member as long as its share of imports of the product concerned in the Republic of Korea does not exceed 3% , provided that developing country Members with less than 3% import share collectively account for less than 9% of total imports of the product concerned.

5. Others

With a view to helping Member countries understand Korea's notification (G/SG/N/10/KOR/1) of 27 January 1997 in connection with this safeguard measure, the following Attachment is provided.

ATTACHMENT

Based on the injury review of the relevant domestic industry, the Korea Trade Commission (the "KTC") recommended that a safeguard measure be taken against imported imitation milk powder to grant relief to the domestic industry suffering serious injury. The KTC made the recommendation to impose a safeguard measure for four years, to allow relief from serious injury to the domestic raw milk and milk powder industry triggered by drastically increased imports of imitation milk powder.

The Ministry of Agriculture & Forestry (the "MAF") reviewed the recommendation of the KTC in accordance with relevant domestic laws and recognized the need to introduce the safeguard measure. Consultations were held between the Governments of the Republic of Korea, EU, Australia and New Zealand on 4-5 February 1997, in Geneva, and a special meeting of the Committee on Safeguards was held on 21 February 1997, after a notification (G/SG/N/10/KOR/1 of 27 January 1997) had been made for prior consultation with countries involved pursuant to the Agreement on Safeguards.

The MAF has made a final decision on the safeguard measure after having reviewed KTC's findings and recommendations and various issues raised by Members concerned during the bilateral consultations and special meeting of the Committee on Safeguards. To enable a better understanding by Member countries concerned, more detailed information is provided herein.

I. Procedure

1. Application of investigation

The National Livestock Cooperatives Federation (the "NLCF") submitted to the KTC on 2 May 1996 a petition for the investigation of injury to the domestic industry in accordance with Article 32.1 of the Foreign Trade Act and the Provisions of Article 65 of its Enforcement Decree. The petition stated that increased imports of dairy products (HSK 0404.90.0000, 1901.90.2000) from the Netherlands, Belgium, and Sweden caused serious injury to the domestic dairy and milk powder industries, or a threat thereof, following the import liberalization of the said products in January 1993. The NLCF requested relief measures, including an HS code reclassification of the products involved, an increase in the tariff rate for a period of four years, and the imposition of quantitative restrictions amounting to less than 10,000 tons.

2. Decision of initiation of investigation

Pursuant to relevant law and enforcement decree¹, the KTC decided to initiate an investigation on dairy products on 17 May 1996² after reviewing the applicant's petition. The NLCF is a producers' organization established under the Livestock Cooperatives Act. It has standing to request an injury determination pursuant to provisions of Article 64 of the Enforcement Decree of the Foreign Trade Act since its members, livestock cooperatives and farms, account for 43.7% of domestic raw milk production and 23.8% of domestic milk powder production. In addition, the petition claimed that imports of the products subject to the investigation were found to have increased absolutely from 1993 to February 1996, and the information provided by NLCF pointed to a domestic industry suffering serious injury from increased imports.

¹Articles 32, 33 and 40 of the Foreign Trade Act, Articles 64, 65, 66 and 76 of the Enforcement Decree of the Foreign Trade Act.

²Determination of the KTC, 96-6 (17 May 1996).

KTC initiated the investigation (KTC/Investigation Reference No.: Foreign Trade 32-1-96-1) and duly published its decision to initiate the investigation in the Official Gazette on 28 May 1996 (KTC/Announcement No. 1996-2). Notification of the initiation of investigation was circulated to the WTO Members (G/SG/6/KOR/2).

3. Investigation of injury to domestic industry

The KTC organized an investigation team which circulated questionnaires to domestic producers, importers and users on 13 June 1996, analyzed the results of the questionnaires which were collected by 15 July 1996, and conducted investigative visits to domestic producers, importers and users. In addition, the KTC investigated the relative condition of the dairy product industries of major dairy product exporting countries, such as the Netherlands, Belgium and Sweden, through Korea Trade Investment Promotion Agency (KOTRA). The KTC also consulted with the Ministry of Health & Welfare (MOHW) and the MAF, which are the agencies responsible for the products involved, to ascertain the relationship between policies of dairy and dairy products industries and related industries.

4. Public hearing

The KTC's investigation team made its investigation report (draft) based on information collected through the procedure described above and made the report public to all parties concerned on 12 August 1996. Based on the draft of the investigation report, a public hearing attended by the applicant, importers, users, governments of exporting countries, and representatives of related associations, was held on 20 August 1996.

Most dairy farmers, including those who sell their raw milk to milk processing companies, are members of livestock cooperatives. Thus, the position of dairy farmers is identical to that of the livestock cooperatives. KTC also provided non-NLCF milk powder producers the opportunity to voice their own opinions. At the public hearing, the Korea Dairy Industries Association ("KDIA"), an organization of milk powder producers not affiliated with NLCF, submitted the opinion that it was necessary to restrict imports of imitation milk powder.

On 23 September 1996, the KTC decided to extend the investigation period for 30 days from 24 September to 24 October 1996 in accordance with applicable regulations³ to review the issues raised at the public hearing.

5. Decision of injury to industry

Based on information submitted by the Office of Administration and Investigation of the KTC and pursuant to the provisions of Articles 33 and 34 of the Foreign Trade Act and Article 76 of the Enforcement Decree of the Foreign Trade Act, the KTC determined⁴ that increased imports of products subject to the investigation caused serious injury to the domestic industry producing directly competitive products. This determination was circulated to the WTO Members through notification G/SG/N/8/KOR/1.

³Provision 3 of Article 33 of the Foreign Trade Act and Provision 1 of Article 76 of the Enforcement Decree of the Foreign Trade Act.

⁴KTC determination (determination 96-20, 23 October 1996).

6. Recommendation for relief measure

The KTC recommended to the MAF, which is the government authority in charge of the products involved, that a safeguard measure be imposed pursuant to Article 34.1 of the Foreign Trade Act and Articles 71, 72 and 74 of the Enforcement Decree of the Foreign Trade Act.

7. Prior consultation

The MAF reviewed the KTC's recommendation in accordance with relevant domestic laws and regulations and judged that a safeguard measure was needed to grant relief to the domestic industry. In order to make its final decision on safeguard measures, the government of the Republic of Korea ("ROK") circulated a notification (G/SG/N/10/KOR/1 of 27 January 1997) to provide an opportunity for consultations with Member countries concerned in accordance with the Agreement on Safeguards. ROK then held bilateral consultations with the EU, Australia and New Zealand on 4 and 5 February 1997 in Geneva, and also attended a special meeting of the Safeguards Committee on 21 February 1997.

8. Implementation of relief measure

During the week beginning 24 February 1997, the ROK made a final decision on relief measures to be effective as of 7 March 1997, after reviewing various issues raised during the consultations with countries concerned and the recommendation of the KTC. This final decision was announced to the public through notification in the revision of "Separated Notice of Export-Import" and in "Detailed Principle of Import License on Imitation Milk Powder."

II. Products Subject to Investigation

1. Definition

The imported products subject to investigation come under HSK⁵ (products consisting of natural milk constituents, except whey) and HSK 1901.90.2000 (food preparations for goods of headings of 0401 to 0404). They are skimmed milk powder (or whole milk powder) mixed with whey powder or malt concentrate (hereinafter referred to as "imported products").

The standard name of the imported product is "milk preparation" (or "skimmed milk preparation"), though it is also variously called "imitation milk powder," and "milk powder blend."

2. Tariff rate

Korea's tariff rates on the imported products for each year shall be as follows:

	1997	1998	1999	2000	2001
0404.90.0000 (other than whey)	40%	40	40	40	39.4
1901.90.2000 (food preparation)	38.8	38.4	38.0	37.6	37.2

⁵0404.90.0000. This product was separated into 0404.10.2190, 0404.10.2900 and 0404.90.0000 due to revision of HSK on 1 January 1997.

III. Definition of Directly Competitive Products and Domestic Industry

1. Directly competitive products

In order to determine whether increase in imported products caused serious injury, or a threat thereof, to the domestic industry, the imported products concerned must be found to be "like or directly competitive products" with the products of domestic industry.

In comparing physical characteristics and quality, the imported products subject to investigation were found not to be "like products" with domestic raw milk and milk powder due to differences in ingredients (physical characteristics).

However, a comparisons of function and commercial usage showed that the imported products were "directly competitive products" with domestic raw milk and milk powder because they can be, and are used as raw materials to manufacture processed milk, fermented milk, ice cream, and other dairy products as evidenced by the fact that domestic producers of these final dairy products increased their purchase of the imported goods while decreasing their purchase of domestic raw milk and milk powder.

2. Definition of domestic industry

Pursuant to the relevant laws⁶, "domestic industry" is defined as "entire domestic producers producing the like or directly competitive products with specific imported products subject to safeguard investigation" or "a group of domestic producers producing a major proportion of total domestic production".

However, the applicable laws also stipulate that in the case of a domestic producer which also imports, only its domestic production shall be treated as part of the domestic industry, and in the case of a domestic producer which produces more than one item, only the production of the product concerned shall be treated as part of the domestic industry.

In this investigation, the "domestic industry" is the industry that produces raw milk and milk powder. These products are directly competitive with the imported products under investigation. Raw milk producers consist of dairy farming households and milk processing companies which directly operate their own dairy farms; milk powder producers are livestock cooperatives and milk processing companies, including producers, who commission processing to third parties because of the absence of facilities for manufacturing milk powder.

Given that Korean milk powder producers also produce dairy products other than milk powder, and import the products under investigation as well, the portion of the production of other dairy products and the import of the products concerned were excluded from the investigation, and only milk powder production was considered as a part of the domestic industry. In other words, in cases where a single producer produced both milk powder and dairy products, only the milk powder portion of production was treated as part of the domestic industry, while the portion of milk processing other than milk powder processing was not treated as part of the domestic industry.

⁶Article 2-1 of the Regulation for the Relief of Injury to the Domestic Industry caused by Imports.

IV. Serious Injury

1. Method of use of data

As raw milk is highly perishable and its collection cannot be adjusted to meet temporary changes in demand, all remaining raw milk after the production of market milk, fermented milk and other food preparations is processed into milk powder. Some of this milk powder is consumed, while the rest is stored as inventory.

Raw milk, milk powder and imported products can be used for the production of processed market milk, fermented milk and ice cream. The increased import of the products subject to investigation had a direct influence on domestic inventories and the price of milk powder. Increase in imported products caused a reduction in the consumption of domestic raw milk and milk powder, and this then required the conversion of surplus raw milk into milk powder.

In the statistics related to domestic industry during the investigation, the production quantity of raw milk included production of domestic milk powder. Likewise, the consumption quantity of raw milk included consumption of domestic milk powder since raw milk and domestic milk powder are closely related.

The most recent data available was utilized in this investigation.

2. Increase in the quantity of imports

The increase of imported quantity is defined as occurring when imports have increased absolutely or relatively in comparison with domestic production during a certain period⁷. An analysis was conducted to determine whether imported products was increased and whether it was an absolute increase and/or a relative increase compared with production of domestic products.

Imports of products subject to investigation increased 384% from 3,217 tons in 1993 to 15,561 tons in 1994, 80.0% to 28,007 tons in 1995, and 16.9% during the first 8 months over the same period of the previous year. Accordingly, imports of the products concerned increased absolutely from 1993 to August of 1996.

Production of domestic raw milk increased by 3.2% in 1994 over 1993 and by 4.2% in 1995 over 1994, while imports increased by 384% and by 80.0% respectively. For the first half of 1996, domestic raw milk production rose by 4.4% while the imports grew by 16.9% over the corresponding period of the previous year. Thus, imports of the products concerned also increased relatively.

Although imports of subheading 1901.90.2000 products declined during the period under investigation, the difference between subheadings 0404.90.0000 and 1901.90.2000 is simply the starch content. Items imported under the two subheadings are regarded as identical since they show almost no difference in terms of usage. Therefore, the total import of subheadings 0404.90.0000 and 1901.90.2000 combined increased both absolutely and relatively.

⁷Article 2-3 of the Regulation for the Relief of Injury to the Domestic Industry caused by Imports.

3. Condition of domestic industry

3.1 Production of domestic raw milk and milk powder

The production amount of domestic raw milk and milk powder was 1,857,873 tons in 1993, 1,917,398 tons in 1994, 1,998,445 tons in 1995, and 1,069,224 tons during the first half of 1996. These figures represent annual increase rates of 3.2% in 1994 and 4.2% in 1995, and 4.4% during the first half of 1996 over the same period of the previous year.

The above-mentioned increase in domestic raw milk production was taken into consideration in determining serious injury. Such an increase, however, was found not to be the result of favourable market conditions, but rather of characteristics of the industry which require all raw milk produced to be collected by livestock cooperatives. Raw milk which are not sold by dairy farmers and livestock cooperatives become inventory in the form of milk powder because freshness of raw milk cannot be maintained. Increase in the production amount of raw milk cannot, in the present case, be regarded as an indicator of positive market conditions.

The production of raw milk cannot be temporarily reduced without resorting to the slaughter of dairy cows. Rather than reducing the size of their herds - the average size of which is quite small - Korean dairy farmers continue normal levels of raw milk production even during periods of weak demand, since excess raw milk is supplied to the livestock cooperatives for conversion into milk powder.

Milk processing companies decreased their purchases of raw milk from dairy farmers, while increasing their purchase of cheaper imported products. As milk processing companies curtailed their purchases of domestic raw milk, Korean dairy farmers were forced to turn to the livestock cooperatives, which were obliged to collect the unsold raw milk produced by their member dairy farmers. In short, the absolute increase of the imported products led to a drastic increase in the surplus of raw milk, all of which was then converted into milk powder.

3.2 Productivity and rate of capacity utilization

The review of production level included productivity and capacity utilization. Capacity utilization was always 100% in the raw milk industry since raw milk is produced by dairy cows, which cannot be left idle like some other form of production.

Because the production of milk powder is greatly affected by the supply and demand of raw milk, and as production facilities cannot accommodate drastic changes in the short term, a review productivity can be replaced by a review of the production level.

It is difficult to calculate the exact level of raw milk productivity. However, the investigation revealed that domestic raw milk production increased slightly despite a reduction in the number of dairy farming households and dairy cows. This indirect indication of increased productivity is found to be the result of advances in technology, not of changes in the market condition. The fact that the domestic industry stagnated in spite of increased productivity, indicates that the injury to the domestic industry was caused not by its internal factors but by external factors, i.e., increased imports.

3.3 Consumption of domestic raw milk (including milk powder)

The consumption of domestic raw milk (including milk powder) was 1,844,463 tons in 1993, 1,947,128 tons in 1994, 1,947,965 tons in 1995, and 984,934 tons during the first half of 1996, reflecting a distinct decreasing trend from 5.6% in 1994 to 0.0% in 1995 and -2.0% during the first half of 1996.

3.4 Share of domestic products

Of the total market share, defined as including domestic raw milk and milk powder, imported milk powder and imported products subject to investigation, portion occupied by domestic raw milk and milk powder declined from 91.1% in 1993 to 87.8% in 1994, 84.6% 1995 and then increased slightly to 85.4% during the first half of 1996.

The slight increase in the share of domestic raw milk during the first half of 1996, following continued decreases since 1993, was found to be a temporary phenomenon triggered by sales of milk powder below manufacturing cost in order to reduce inventories which was incurring storage costs and expenses.

3.5 Inventories of domestic milk powder

Inventories of domestic milk powder totalled 4,509 tons at the end of 1993, 1,517 tons in 1994, 6,565 tons in 1995 and 14,994 tons at the end of June of 1996, reflecting inventory ratios of 2.4% in 1993, 0.8% in 1994, 3.3% in 1995, and 13.0% during the first half of 1996 vis-a-vis the total demand. The total value of inventories of milk powder at the end of June 1996 was estimated at 92,633 million Won (about US\$122 million).

3.6 Employment

The number of dairy farmers in Korea has seen a steady decrease from 28,219 in 1993 to 25,617 in 1994, 23,519 in 1995, and 22,725 at the end of June of 1996.

The employment level in the milk powder industry was reviewed. However, no exact figure could be quantified because those workers producing processed milk products would perform the function of manufacturing milk powder as well. Depending on the need, producers of processed milk products would also work in the capacity of milk powder producers.

3.7 Price

The price of milk powder is subject to change according to the market forces of supply and demand, although that of raw milk is maintained at a stable level fixed by the government. The government increased the raw milk price twice during the period under investigation. The sales price of milk powder by the livestock cooperatives (periodic average price) fell from 5,354 Won/kg in 1993 to 5,294 Won/kg in 1994, increased slightly to 5,388 Won/kg in 1995, and decreased sharply to 4,994 Won/kg during the first four months of 1996. There was no correlation between such change and seasonal factors.

Although the sales price of imported products rose by 381 Won/kg during the period under investigation, the sales price of domestic milk powder dropped by 360 Won/kg.

Price comparison between imported and domestic products

(Unit : Won/kg, Won)

		1993	1994	1995	Jan - Apr. 1996
Imported Products	Import price (CIF)	1,750	1,689	1,709	2,008
	Sale price in Korea (A)	2,590	2,500	2,530	2,971
Domestic Products	Sale price (B)	5,354	5,296	5,388	4,994
	Manufacturing cost ©	5,158	5,426	5,860	6,178
	Difference (B - C)	196	-130	-472	-1,184
Price Difference	B - A	2,714	2,796	2,858	2,023

3.8 Manufacturing cost

The Increased manufacturing cost of milk powder was inevitable given the increased production cost of raw milk (increase of feed cost, etc.). Manufacturing cost per unit increased from 5,158 Won/kg in 1993 to 5,426 Won/kg in 1994, 5,860 Won/kg in 1995, and 6,178 Won/kg during the first four months of 1996.

3.9 Loss per unit

The difference between sales price and production cost per unit (periodic average price) was 196 Won in 1993, -130 Won in 1994, -472 Won in 1995, and -1,184 Won during the first four months of 1996. Selling below manufacturing cost, which has continued since 1994, had an overall adverse effect on gross profit, operating income and ordinary income (LEBEIT: Loss/Earning Before Extra Items & Income Taxes, hereinafter referred to as "ordinary income") of the livestock cooperatives.

3.10 Financial analysis

3.10.a Profit (loss) of livestock cooperatives

It is impossible to ascertain estimate the operating income of Korean dairy farmers as their total number exceeds 23,000 households and their operations are, for the most part, small and unsystematic.

However, profitability of livestock cooperatives can be used to measure the financial condition of raw milk producers since these cooperatives are owned by individual dairy farmers and the profits are distributed to them.

The financial balance sheets of milk processing operations of the following 14 livestock cooperatives were reviewed: Seoul Dairy Cooperative, Kangwon Dairy Cooperative, Chuncheon Dairy Cooperative, Taebak Dairy Cooperative, Chungju Dairy Cooperative, Daejeon-Chungnam Dairy Cooperative, Seohae Dairy Cooperative, Chunju Dairy Cooperative, Imsil Dairy Cooperative, Kwangju-Cheonnam Dairy Cooperative, Taegu-Kyungbuk Dairy Cooperative, Pusan-Kyungnam Dairy Cooperative, Kyungnam Dairy Cooperative and Cheju Dairy Cooperative.

Gross profit, operating income and ordinary income were reviewed as indicators for calculating the profit or loss of the livestock cooperatives. However, gross profit could not be considered as an

adequate indicator of profit or loss since it was calculated by simply deducting the cost of goods sold from sales revenue.

Operating income was not an adequate indicator of profit or loss since losses other than operating loss (in particular, losses from accumulated inventories) was not reflected. Therefore, ordinary income, which reflected such factors, was regarded as the appropriate indicator in determining profit or loss.

Furthermore, ordinary income was the profit indicator for livestock cooperatives which showed changes of value of assets invested by member dairy farmers.

Ordinary income (loss) of livestock cooperatives

The aggregate ordinary profit of all 14 livestock cooperative was 6,720 million Won in 1993, 4,721 million Won in 1994, 209 million Won in 1995 and -17,546 million Won during the first half of 1996, while the ratio of ordinary income (loss) to sales (expenditure) was 1.4%, 0.8%, 0.0% and -5.3%, respectively.

Debt-to-capital ratio of livestock cooperatives

At the end of the first half of 1996, seven of the 14 livestock cooperatives had debt-to-capital ratios (ordinary liabilities over capital) exceeding 1,000%. They were: Chuncheon Livestock Cooperative, Chunju Livestock Cooperative, Imsil Dairy Cooperative, Kwangju-Cheonnam Dairy Cooperative, Taegu-Kyungbuk Dairy Cooperative, Kyungnam Dairy Cooperative and Cheju Dairy Cooperative.

Capital loss of livestock cooperatives

According to preliminary accounts settlement data on livestock cooperatives during the first half of 1996, those cooperatives suffering a net loss totalled 11, while those having depleted their paid-in-capital numbered six.

3.10.b Loss of major producers of milk powder

The Seoul Dairy Cooperative and the Pusan-Kyungnam Dairy Cooperative produced a combined total of 97.9% of milk powder produced by all of the livestock cooperatives in 1995. Maeil Dairy Co., Haitai Dairy Co., Vilac Co., and Lotte Ham & Milk Co. are milk processing companies, which produced 52.4% of total milk powder produced by milk processing companies in 1995. Seoul Dairy Cooperative, Pusan-Kyungnam Dairy Cooperative, Maeil Dairy Co., Haitai Dairy Co., Vilac Co. and Lotte Ham & Milk Co. combined accounted for 63.7% of total domestic production of milk powder in 1995. The operating income of Seoul Dairy cooperative, Pusan-Kyungnam Dairy Cooperative, Haitai Dairy Co., Vilac Co., and Lotte Ham & Milk Co. were reviewed⁸.

3.10.b.i Turnover

Net turnover from milk powder operations of Seoul Dairy Cooperative and Pusan-Kyungnam Dairy Cooperative revealed a decreasing trend from 11,937 million Won in 1993, 9,533 million Won in 1994, 11,589 million Won in 1995, and to 2,310 million Won during the first four months of 1996.

Turnover from milk powder operations of the milk processing companies (Haitai Dairy Co., Maeil Dairy Co., Vilac Co., Lotte Ham & Milk Co.) decreased from 21,010 million Won in 1994 to 19,750 million Won in 1995.

3.10.b.ii Operating loss

Operating losses from milk powder operations of the livestock cooperatives (Seoul Dairy Cooperative and Pusan-Kyungnam Dairy Cooperative) increased from -755 million Won in 1993, -622 million Won in 1994, -1,244 million Won in 1995, and -681 million Won during the first four months of 1996.

The corresponding operating losses sustained by milk processing companies (Haitai Dairy Co., Maeil Dairy Co., Vilac Co., Lotte Ham & Milk Co.) rose from -680 million Won in 1994 to -1,330 Won in 1995.

4. Determination of serious injury

It was determined that the domestic industry was suffering serious injury based on, inter alia, the following facts: the market share of domestic raw milk decreased between 1993 and June 1996; inventory of domestic milk powders grew from 4,509 tons in 1993 to 14,994 tons in June 1996; sales price witnessed a drop while manufacturing costs increased; livestock cooperatives' ordinary income steadily decreased and registered a huge loss in the first half of 1996; seven livestock cooperatives had a debt to equity ratio exceeding 1,000% while six cooperatives depleted their paid-in-capital; and employment decreased.

V. Causal Link

In order to determine the causal relationship between increased quantities of the imported products and serious injury to the domestic industry, the KTC conducted extensive investigation into the market share of the imported products, price comparisons between imported and domestic milk powder, the effect of the imported products on sales of domestic raw milk and milk powder, and the influence of factors other than increased imports on the domestic industry.

1. Influence by increased imports

1.1 Increase of share of imported products and displacement of domestic production

The market share of the imported products subject to investigation out of total domestic consumption (domestic raw milk (including milk powder), imported milk powder, and imported products concerned) continued to rise from 1.6% in 1993 to 7% in 1994, 12.2% in 1995, and 14.1% during the first half of 1996. In particular, their share in the consumption of milk powder and the like (domestic milk powder, imported milk powder, and the imported products concerned) increased rapidly from 10.7% in 1993, 38.4% in 1994, 60.6% in 1995, to 69.4% for the first half of 1996.

1.2 Increased imports triggered a decline in the sale price of domestic milk powder

The average import price per unit in Korea was 1,750 Won/kg in 1993, 1,689 Won/kg in 1994, 1,709 Won/kg in 1995, and 2,008 Won/kg for the first four months of 1996. The average sales price of the imported products in Korea was 2,590 Won in 1993, 2,500 Won in 1994, 2,530 Won in 1995, and 2,971 Won for the first four months of 1996. The average sales price of domestic milk powder dropped from 5,354 Won/kg in 1993 to 5,296 Won/kg in 1994, 5,388 Won/kg in 1995, and 4,994 Won/kg for the first four months of 1996.

The price difference (periodic average) between the imported products and domestic milk powder fluctuated from 2,764 Won in 1993 to 2,796 won in 1994, 2,858 Won in 1995, and 2,023 Won for

the first four months of 1996. This wide price gap has forced Korean producers to lower the price of domestic milk powder, eventually making sales below manufacturing cost inevitable.

Analysis showed that as the share of imported products in total consumption increased, the sales price of domestic milk powder dropped from 5,354 Won/kg in 1993 to 4,994 Won/kg for the four months of 1996. Thus, increased imports of the products subject to investigation caused the price of domestic milk powder to drop.

As imports of the products under investigation increased, the gap between the sales prices and manufacturing costs of domestic milk powder widened from 196 Won in 1993 to -130 Won in 1994, -472 Won in 1995, and -1,184 Won for the first four months of 1996.

1.3 Increased share of livestock cooperatives in collecting raw milk and shrinkage of white market milk sector

The share of livestock cooperatives' raw milk collection in Korea increased from 40.56% in 1990 to 41.14% in 1991, 40.19% in 1992, 41.36% in 1993, 42.80% in 1994, 44.30% in 1995, and 45.30% for the first four months of 1996 because milk processing companies either stopped purchasing or reduced the purchase amount of domestic raw milk. Instead, the milk processing companies would purchase the cheaper imported products in manufacturing processed milk and other dairy products to maximize profit. The effect was the share of white market milk, which can only use domestic raw milk, decreased from 92.9% in 1990 to 92.4% in 1991, 92.4% in 1992, 91.3% in 1993, 88.6% in 1994, 83.8% in 1995, and 82.1% for the first half of 1996. In conclusion, increased imports of the products subject to investigation had an adverse effect on the white market milk sector.

1.4 Increased imports caused injury to domestic industry

Given the above, it is apparent that imported products increasingly replaced domestic products in terms of over-all market share, and market share in the milk powder and white milk market during the period under investigation. The price difference between the imported and domestic products forced domestic producers to decrease their price to the point of sales below cost, and to stockpile excess inventory of unsold milk powder. Faced with increasing competition from imported products, the number of dairy farmers decreased as well. Therefore, increased imports of the products under investigation were found to be the cause of serious injury to the domestic industry.

2. Other factors

2.1 The influence of controversy over milk quality

The Korea Food Industries Association (the "KFIA") and milk products-exporting countries presented their opinion that the controversy over milk quality was a major cause of serious injury to the domestic industry. After examining the facts related to the controversy which occurred from October to November 1995, it was acknowledged that this incident did reduce the demand for market milk, though only temporarily. It was determined that the controversy ceased to be a cause of reduced market milk demand in January 1996. The quality dispute affected only three months of consumption out of an investigation period totalling 42 months. No evidence was submitted by any of the parties concerned which demonstrated that the injury caused by the quality dispute was as serious or persistent as that caused by increased imports.

2.1.a Reason why KTC rejected analysis presented by the KFIA

KFIA claimed that, of the increased inventories of domestic milk powder, 81.17% was attributable to reduced consumption of market milk caused by the milk quality controversy, 8.03% to increased production of raw milk, and 4.80% to increased imports of milk powder.

The analysis and conclusion presented by the KFIA was rejected for several reasons. First, the methodology employed by the KFIA was flawed. To derive at the findings, the KFIA took the increase of production rate of market milk and raw milk from November 1994 to June 1995 and simply multiplied the rate by the actual production for the same period to forecast the November 1995 to June 1996 production amount of market milk and raw milk. KFIA assumes these projections are appropriate production levels for the period covering November 1995 to June 1996. The actual amount of production of market milk and raw milk for the period covering November 1995 to June 1996 was less than the forecasted amount. KFIA attributed the differential between the forecasted amount and the actual production amount to quality dispute. KTC determined that it was inappropriate take one year from November 1994 to June 1995 as being representative to determine the production level for November 1995 to June 1996. Second, in calculating the increased inventories of milk powder and increased imports of products under investigation, the KFIA used different periods for comparison. Third, there was insufficient evidence to estimate the volume of inventory reduction in the non-livestock cooperative sector.

2.1.b Review on material submitted by other Parties concerned

Parties concerned other than the KFIA could not provide evidence that the controversy over milk quality was a substantial cause of injury to the industry.

2.2 Influence of reduced imports of milk powder

It has been noted that the increase in imports of the products under investigation contributed to a reduction in imports of milk powder from 14,843 tons in 1993, 11,581 tons in 1994, 7,576 tons in 1995, to 583 tons in the first half of 1996. However, it has also been noted that there is an important difference between the imports of the products under investigation and those of milk powder. The milk powder imported by ROK in 1993-1994 was to supplement the shortage of domestic raw milk and milk powder, and was allocated to users at reasonable prices.

During the period of 1993-1995 the imports of products under investigation grew by 24,790 tons, while those of milk powder fell by 7,267 tons. Therefore, the decreased imports of milk powder had a very slight, albeit positive, impact on the injury to the domestic industry compared with the increased imports of the products under investigation.

2.3 Review of demand

2.3.1. Review of the Overall Consumption

The total consumption of raw milk (including milk powder) was 2,025,063 tons in 1993, 2,218,738 tons in 1994, 2,303,795 tons in 1995 and 1,153,964 tons in the first half of 1996. Given this overall increase in consumption, the injury to the domestic industry is not attributable to a decrease in consumption.

2.3.2 Explanation of decrease of white market milk and increase of processed milk sales and consideration of changes in consumer preference

The sales ratio of processed milk to white market milk remained stable during the period of 1990-1992 but processed milk occupied a larger proportions as of 1993. This shift was found to be attributable to milk processors seeking to change the production structure in order to maximize their profits through the use of cheaper imported products, as opposed to changes in consumer preference.

2.3.3 Consumption of final dairy products

The consumption quantity of market milk and fermented milk (for which statistics are not available) was measured by production quantity of the same products because their shelf-life is short and the producers could quickly adjust their production in accordance with the market situation. Dairy products consumption is measured in this way - which could affect the raw material usage of imported products subject to investigation as well as domestic raw milk, domestic milk powder and imported milk powder - increased during the period of 1993; June 1996. Therefore, it was not regarded as a cause of injury to the domestic industry.

2.3.4 Review of price trend of milk products

Increases in market milk prices in early 1993 and in April-May 1996 was followed by a temporary decline in consumption. However, the price increases came only at the beginning and the end of investigation period, and thus could not have been a substantial cause of injury to the domestic industry.

2.3.5 Review of seasonal influence

Seasonal factors can also have an effect on the supply and demand of dairy products. While production is rarely influenced greatly by seasonal factors, consumption often is. The KTC reviewed the effect of seasonal changes using monthly data and forecasts, but found no evidence that factor was related to the injury to the domestic industry.

2.3.6 Review of the effect of other dairy products on injury

The ROK analyzed the potential effect of the situation in other dairy products sectors, including the white market milk, milk powder preparation, evaporated milk, butter and cheese which does not use imported imitation milk powder. The production and consumption of these dairy products increased during the period of the survey. Accordingly, the consumption of raw milk and domestic milk powder, which are the raw materials of these dairy products, increased. Nevertheless, the raw milk and milk powder industry suffered serious injury. Therefore, no connection could be established between the effect on these dairy products and injury to domestic industry. Imports and consumption of cheese rose continuously. However, given the dynamics of Korean cheese industry⁹, this consumption increase had little or no effect on the consumption of domestic raw milk or milk powder.

2.4 Review of price decision by the government

The price of raw milk is determined by the government by taking into account production costs, influence on domestic commodity prices, domestic supply and demand, etc. The price set by the government is not an obligatory price but rather a base price for contracts between dairy farmers and milk processing firms. Therefore, this did not affect the domestic industry adversely. If the government had not set a base price and the livestock cooperatives had refused to collect raw milk, dairy farmers would have been directly injured.

3. Conclusion on causal link

In light of the above causation analysis, it is the conclusion of the KTC that the serious injury to the domestic industry was caused by the sharp increase of imported products.