

Chinese Agricultural Exports Provide Growing Competition

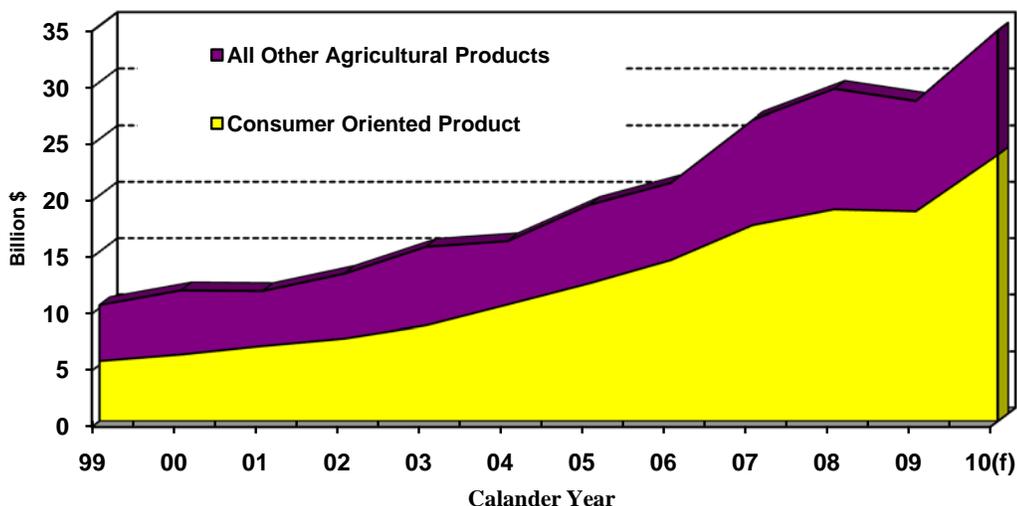
Summary

With China becoming the second largest U.S. market in fiscal year 2010, China's emergence as a major agricultural importer is well-known. While China is a large net food importer, it is also becoming a formidable competitor in the export market with shipments nearly tripling over the past 10 years and market share increasing. While some of China's exports are bound for the United States, others directly compete with U.S. products in foreign markets. Exports of consumer-oriented high-value products (HVPs) have shown particular growth, especially to nearby markets in Japan and Southeast Asia. Although China faces production constraints and booming domestic consumption, future exports, particularly of high value products, have room for expansion.

Exports Rise Along with Market Share

Chinese agricultural exports began to surge after 1999, with shipments increasing in value from \$10.3 billion in 1999 to an estimated \$28 billion in 2010. This \$18 billion increase is impressive, but as global agricultural trade was also on the rise over this period, perhaps more important was the increase in market share. Chinese exports accounted for 4.5 percent of global agricultural trade in 1999, but climbed to 5 percent in 2009. Meanwhile, over the same period, U.S. export share fell from 22 percent to 18 percent. Although other exporters, particularly Brazil and Argentina, played a larger role in the fall of U.S. share, the growth of Chinese exports likely contributed to the drop, particularly in certain markets for consumer-oriented HVPs.

Consumer-Oriented Products Push Exports

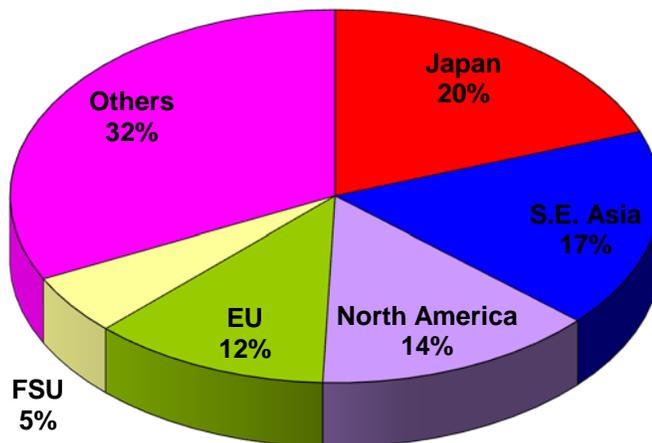


Consumer-Oriented HVP Exports on the Rise

As seen in the chart above, much of the growth in Chinese exports over the past decade was due to greater shipments of consumer-oriented products, which increased by more than \$18 billion compared to under \$6 billion for all other products. While the category consists of over 300 items,

top products include garlic, tomato paste, fresh apples and juice and processed poultry. Compared to other major agricultural exporters, consumer-oriented products make up a large part of the overall Chinese export basket, accounting for two-thirds of exports in 2009. Meanwhile, the category accounts for about one-third of U.S. exports, 39 percent for Canada, and 30 percent of Brazilian exports.

**Chinese Consumer Oriented Export Markets
(2009)**



Chinese Exports Heat Up In Battleground Markets

As seen in the chart above, Japan and Southeast Asia¹ have been the largest markets for Chinese consumer-oriented products, in part due to a freight cost advantage and shorter delivery times compared to U.S. and European suppliers. The Japanese market has been particularly important for Chinese exports, some of which compete with U.S. products, including meats and processed fruits and vegetables. Chinese exports of consumer-oriented products to Japan in 2009 were \$3.5 billion compared with U.S. exports of \$4.4 billion. However, Chinese exports have grown over the past decade (1999 vs. 2009) by \$1.3 billion while U.S. consumer-oriented exports fell by \$244 million. Chinese consumer-oriented exports also compete directly with U.S. products in several other markets including Southeast Asia, Europe, South Korea and Canada. China's trade with Southeast Asia was boosted by the "early harvest" provision in its new free trade agreement with the Association of Southeast Asian Nations (ASEAN) that reduced tariffs on agricultural products. Although Chinese exports to Canada were only \$321 million last year, shipments of low-priced apple juice concentrate, pasta and fruits provide competition for U.S. products. Chinese exports to the European Union, another top market for U.S. consumer-oriented products, have also performed well and doubled over the past five years from \$1.1 billion in 2004 to \$2.2 billion in 2009.

Apple Market Demonstrates Emergence Of Growing Competition

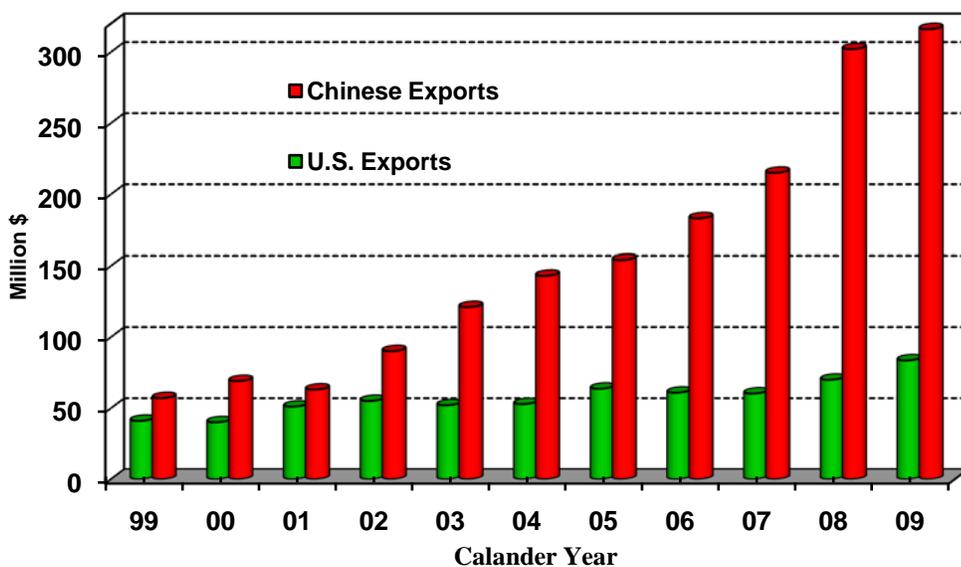
Perhaps no commodity better illustrates the emergence of China as an export competitor than

¹ For this paper, Southeast Asia includes Malaysia, Thailand, Vietnam, Singapore, and Indonesia.

apples. China's share of global apple exports in 1999 and 2000 (July/June) was just 10 percent, but reached 23 percent in 2009 and 2010. Meanwhile, over the same time frame, the U.S. share of global apple exports fell from 21 percent to 16 percent. While Chinese apples appear to be a growing competition to U.S. apples around the world, nowhere is this more pronounced than in Southeast Asia. Though U.S. apple exports to the region have grown over the past decade, they have grown at a slower rate than Chinese exports. As seen in the chart below, Chinese exports to the region have increased dramatically from only \$57 million in 1999 to \$315 million in 2009. Chinese apples are generally lower-priced and compete in a separate quality category from U.S. apples. However, whether creating new demand based on price or competing directly with U.S. apples, China has clearly captured the growth in Southeast Asian demand for apples. Nevertheless, U.S. apples continue to perform well in many markets, including Mexico, due to higher U.S. quality and safety standards.

As with many of China's consumer-oriented products, the future looks bright for increasing apple production and exports. With abundant cheap labor, China has a natural advantage in labor-intensive crops. Though land area available for expansion is limited, yield gains for high value crops could provide future production growth as has been the case with apples. Area dedicated to apples in traditional growing regions of Eastern China has stagnated, but new orchards are being planted in western provinces. Moreover, yields have improved. Government programs are encouraging dissemination of new apple varieties, providing subsidies to bag apples in the field after harvest, thus improving quality, assisting producers in adopting "green food," good agricultural practices and other quality management systems, setting up centers to test for toxic pesticide residues, and sponsoring trade fairs. Quality has also improved due to better orchard management. As with many of China's consumer-oriented products, however, price should continue to be the principal driver behind increased exports.

Chinese Apple Exports to S.E. Asia Soar Past Competition



Date Source: GTA

Future Export Growth Faces Challenges

Rising costs and concerns about commodity price inflation may constrain China's export growth. Farm labor costs are rising as much as 10 percent annually as rural laborers migrate to cities while the competition for scarce land is raising rents. Rapid urbanization is consuming suburban vegetable plots and Chinese food manufacturers are pushing farther into China's interior to search for supplies of fruits, vegetables and aquaculture products as raw materials for domestic and exported products. Rapidly-rising prices of garlic and other vegetables during 2010 raised concerns about domestic vegetable supplies. Meanwhile, China's State Council directed municipal authorities to set up vegetable farms and establish vegetable reserve systems.

Continued growth in both overall exports and global market share will depend on several factors including 1) production growth given rising domestic consumption and land constraints; 2) overall food safety conditions in agricultural production; and 3) labor and other production costs. Though China enjoys a freight advantage to East and Southeast Asian markets, relatively high internal transportation costs can mitigate some of the price competition of Chinese products. Despite the rising cost structure on Chinese farms, robust investment in new processing facilities (encouraged by subsidized loans and tax breaks) tends to push down prices of final products. Relatively low production costs and the push of exporters into western regions may enable China to maintain its status as a low-cost supplier for many products.

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