

Strategic Analysis Paper

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The Politicisation of Australian Agricultural Trade with China Suggests that New Export Markets Need to be Cultivated

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Key Points

- More than one-third of Australian agricultural exports are sold to China – a level of trade dependence that has not existed since the 1950s, when a similar share was exported to the United Kingdom.
- Beijing has shown that it is not afraid to use the trade relationship for political ends. According to Australian trade data, the trading relationship remained steady despite increased friction in the first six months of 2020. The latest Chinese customs data, however, indicates that the relationship is deteriorating.
- While China is the largest single market for Australian agricultural exports, global demand for high-quality farm goods remains high. There are many other markets that most of those exports could be diverted to if the relationship were to continue to sour.
- A reinvigoration of Australia's trade diplomacy is required to secure the opportunities offered by those markets.

Summary

The Australia-China trade relationship has become increasingly politicised. Australia is becoming increasingly exposed to Chinese coercion as a result of a high proportion of its exports being sold to China. While Australian agricultural exports remained steady year-on-year in the first six months of 2020, the latest trade data from China suggests that tariffs and other trade barriers are starting to take a toll on the trade relationship. It is becoming increasingly clear that Australia will need to develop other export markets to reduce its reliance on China. As high quality, premium agricultural products remain in high demand

globally, there is no shortage of countries that Australian agricultural commodities could be exported to.

Analysis

Beijing has demonstrated on many occasions throughout 2020 that it will not shy away from using the agricultural trade relationship to send Australia a political message. It has imposed [two tariffs on Australian barley](#), one of which is due to Beijing's insistence that barley growers are subsidised by the Australian Government. Beijing argues that Canberra paid farmers to upgrade water infrastructure in the Murray-Darling Basin, which it claims is a form of subsidy. The argument is baseless, however, as the vast majority of barley exported to China is grown in Western Australia, thousands of kilometres from the Murray-Darling Basin. China [banned barley shipments from the Co-operative Bulk Handling Group](#) (CBH) in early September, after it allegedly found excessive levels of weed seeds in some shipments. As CBH is the largest grain exporter in Australia, the ban will have a significant effect on the amount of grain that is shipped to China. CBH has [retested its cargo vessels and grain shipments](#) and found that weed contaminants are well within the tolerances accepted by Beijing and Canberra. Some of the barley that was originally destined for China has been redirected to Thailand, Japan and Saudi Arabia.

China also banned exports from four Australian beef processors, under the pretext of incorrect labelling. About 20 per cent of Australian beef exports are prepared by those processors but, due to Covid-19-related shortages, most of those exports were [diverted to the US and South Korea](#). Beijing has [not lifted the ban](#), even after those processors addressed the labelling concerns. The ban was recently extended to a [fifth processor](#), after a drug used to treat eye infections in dogs and cats was allegedly identified in beef shipments by the Chinese customs office. The ban is possibly in retaliation to the Australian Government announcing that it will pursue [new foreign relations legislation](#) and prevent Victoria from making any further progress on its Belt and Road Initiative agreement with Beijing. In the same week, China also launched an [anti-dumping investigation into the Australian wine export industry](#), followed by an investigation into the [possible subsidisation of that industry](#).

Despite the rising hostility in the Australia-China relationship, trade with China remained steady in the first six months of 2020, according to Australian trade data. On a year-to-year basis, the value of Australian exports to China increased by [four per cent in the year to June 2020](#). While that is mainly due to the higher iron ore price (iron ore accounts for [56 per cent](#) of all Australian goods exported to China), an increase in the volume of agricultural goods has also played a part. Between May and June, iron ore exports rose by 14 per cent, while agricultural exports increased by four per cent. Grains and wool increased by 33 and 24 per cent, respectively. The Department of Agriculture estimates that the volume of beef exported to China will reach [324,000 tonnes in 2019-20](#), up from 228,000 tonnes last year. That estimate was made before China imposed restrictions on a fifth meat processing plant, however, and it is possible that it will choose to import a larger amount of beef from the US instead of Australia. The loss of hundreds of millions of pigs in China as a result of the African Swine Fever outbreak is expected to drive increased demand for alternative sources of protein

for several years. Regardless of any potential increase in US shipments, Australian beef will still be in high demand in China for the foreseeable future.

In July, the monthly value of Australian agricultural exports to China fell below \$1 billion for the first time since at least 2018. A single month of trade statistics does not create a particularly clear picture of what is occurring in the trade relationship. On an annual basis, however, the decline appears more sharp. By July 2019, Australia had exported about \$9.7 billion worth of agricultural goods to China. In the first seven months of 2020, however, the value of those exports had reached only about \$8.5 billion. That decline in value could, however, be attributed to the trade disruption caused by Covid-19 and its associated lockdowns. Trade with China was notably lower in February 2020, at the height of its Covid-19 lockdown. Agricultural exports increased in March and April, but have declined sharply in the months since.

Monthly Value of Australian Agricultural Exports to China July 2018 to July 2020 (\$)

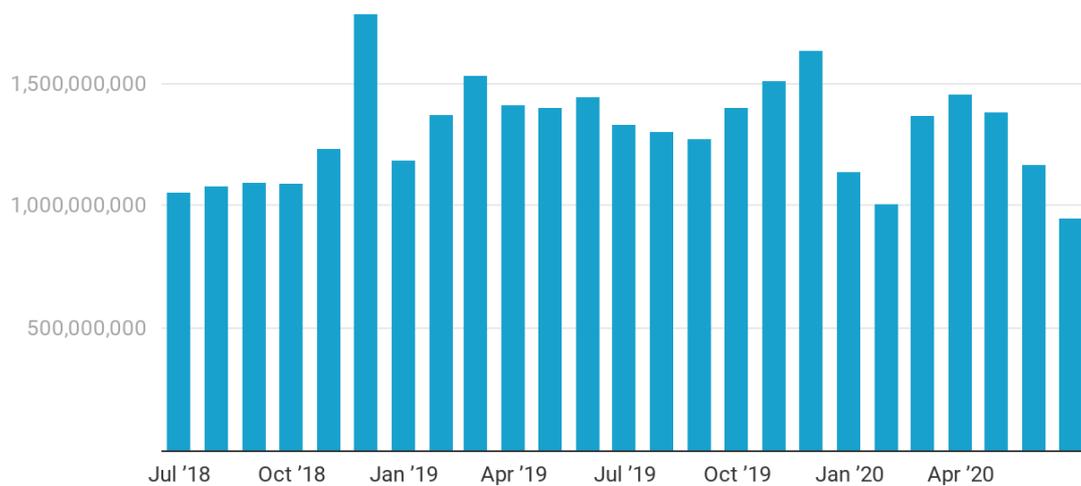


Chart: Future Directions International • Source: Australian Department of Foreign Affairs and Trade • Created with Datawrapper

Annual Value of Australian Agricultural Exports to China 2006 to July 2020 (\$)

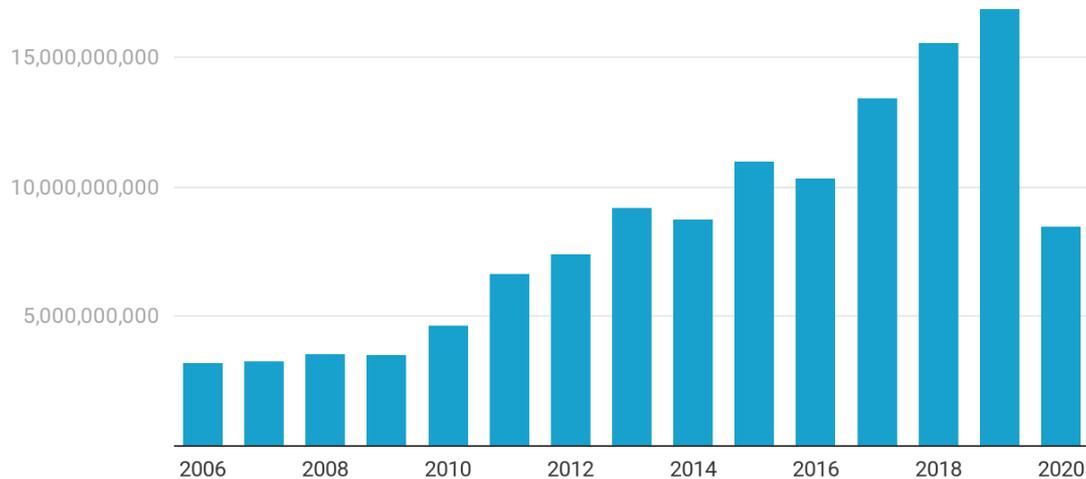


Chart: Future Directions International • Source: Australian Department of Foreign Affairs and Trade • Created with Datawrapper

The value of Australian barley exports to China has declined since 2017, but that could be due to the lower barley production in Australia in 2019 and a reduction in Chinese demand for feedstock. The value of barley exports in 2020 could surpass that of 2019, even with the application of tariffs and the recent ban on CBH shipments. It is unlikely that they will get anywhere near the levels reached between 2014 and 2018, however, as the trade barriers are too steep.

Value of Australian Barley Exports to China 2006 to July 2020 (\$)

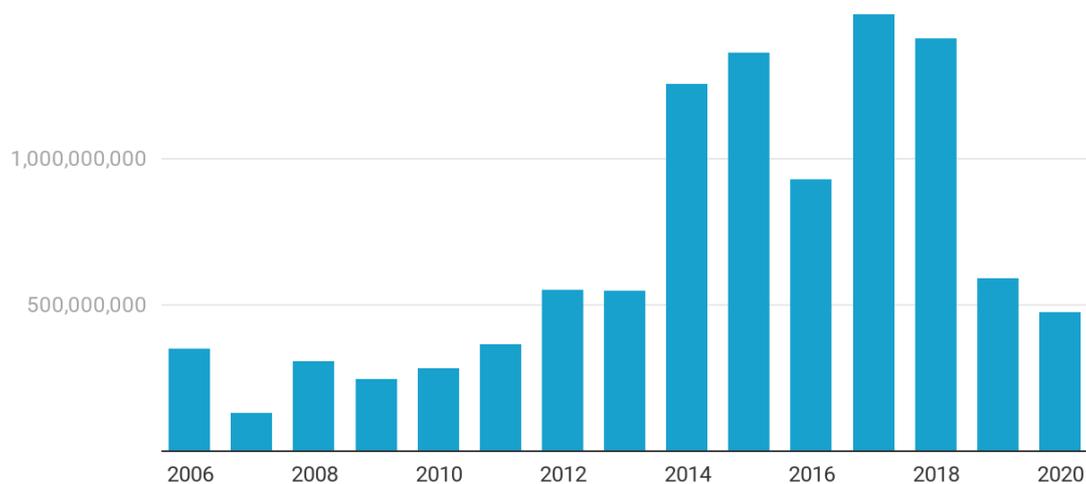


Chart: Future Directions International • Source: Australian Department of Foreign Affairs and Trade • Created with Datawrapper

There was no decline in the value of Australian beef exported to China in the first half of 2020. Beef sales have already surpassed the annual value reached in every year except for 2019, when annual beef sales reached a record high of more than \$2.6 billion. In the first seven months of 2019, about \$1.25 billion worth of beef had been exported to China. Over the same time period in 2020, about \$1.3 billion worth of beef had been exported. Sales of beef have been so strong that they triggered the tariff-rate quota established in the China-Australia Free Trade Agreement. As a result, Australian beef exports to China are now subject to a 12 per cent tariff (instead of a tariff rate below five per cent). Chinese demand for beef is likely to remain elevated, however, due to the large reduction in the Chinese swine herd, caused by African Swine Fever.

Value of Australian Beef Exports to China 2006-July 2020 (\$)

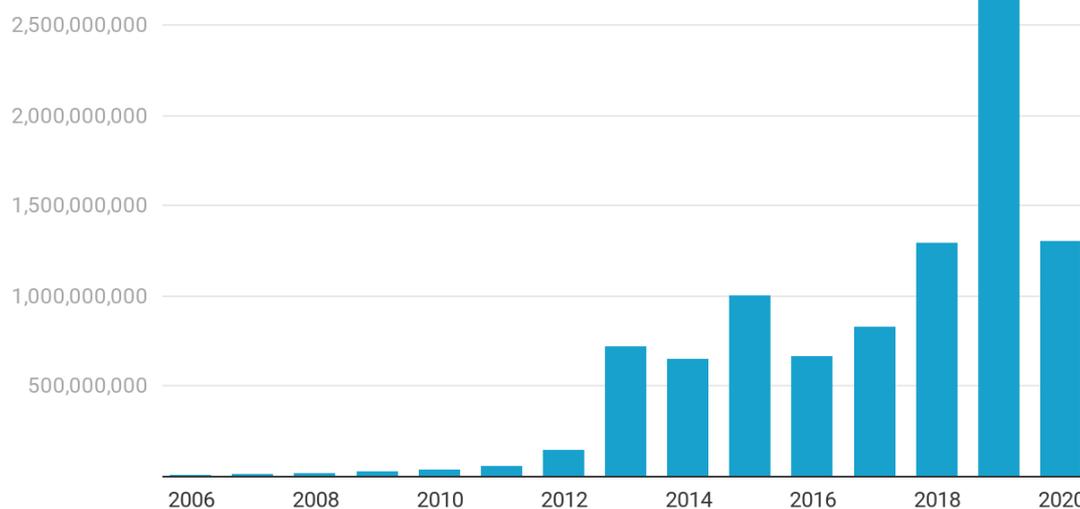


Chart: Future Directions International • Source: Australian Department of Foreign Affairs and Trade • Created with Datawrapper

The latest trade data from the Chinese Customs General Administration suggests that the Australia-China trade relationship is deteriorating. In August, the value of Australian goods exported to China declined by [26.2%](#) – the steepest monthly decline experienced by any country. Chinese customs data does not break down trade statistics by industry, making it impossible to determine how well agricultural exports have performed. It is possible that they led the decline, however, especially as they have been targeted with trade restrictions while other industries remain unaffected.

The Australian agricultural export sector is heavily exposed to the Chinese market. More than one-third of Australian agricultural exports are sold to China – a level of trade dependence that the sector has [not experienced since the 1950s](#), when a similar share of agricultural goods were exported to the United Kingdom. Australia has allowed itself to focus too heavily on China, to the detriment of many other export opportunities. While Australia has undoubtedly benefited from its trade relationship with China over the last 30 years, the relationship has deteriorated, perhaps irreparably.

It has been [suggested](#) that as Australia is:

Already selling all it can to Japan and Korea, Australia would not find any new markets for iron ore and coal to replace even a part of what it now sells to China. Nor could it easily replace exports of wine, meat, dairy products, and manufactures to China ... Australia cannot and will not decouple from China's economy any more than Japan, Korea, Taiwan, or Southeast Asia can, wish to, or will.

That could very well be the case, but if China continues to ban or impose tariffs on a large portion of Australian agricultural exports, Australia is left with little option but to identify and cultivate new markets. Continuing to rely on China to buy more than one-third of the agricultural goods that Australia exports is extremely foolhardy.

It is also lazily argued that Australia should not bother establishing trading relations with other countries because there are no other "giant markets" outside China. James Laurenceson, the Director of the Australia-China Relations Institute, suggests that it will be difficult for Australia to replace the Chinese market by [stating](#) that 'Engaging with giant markets other than China would be wonderful - if only they existed'. While China is by far the largest single market for Australian agricultural exports, there are numerous other countries that, taken together, could easily replace at least some of the trade lost to China as a result of rising tensions.

Agricultural market analysts frequently indicate that there are [short-term opportunities](#) in Australia's "own backyard" – countries such as India, Bangladesh, Indonesia and virtually every other country in South-East Asia. India presents a [growth market for Australian barley](#) and Vietnam has been purchasing increasing amounts in recent years. Australia recently became the only country to have [tariff-free access to the Indonesian grain market](#), after the ratification of the Indonesia-Australia Comprehensive Economic Partnership Agreement. Indonesia will allow up to 500,000 tonnes of barley, wheat and sorghum into the country duty free. That quota will increase by four per cent every year for the next six years.

In the longer term, there are [emerging opportunities in Africa](#), which Australia is doing relatively little to cultivate. Washington has begun to [negotiate a free trade agreement with Kenya](#), which could help the US to market its exports across the continent if an African continental free trade area is finalised. The US would have a first mover advantage in a market that already has a population equal to that of China and is predicted to be [twice as large by mid-century](#). While Africa continues to confront significant challenges, it is undeniably a market that will be of increased importance over the course of this century.

Furthermore, there are growing indications that many of Australia's major export markets are seeking to decouple from China, at least to some extent. While it is unlikely to decouple from the Chinese economy entirely, Japan has expressed an interest in reducing its reliance on Chinese manufacturing. It is in discussions with India and Australia to form a [Supply Chain Resilience Initiative](#), which could launch as early as November. In August, 57 Japanese companies were offered US\$536 million (\$737 million) in subsidies to [shift production out of China](#) into Japan. Another 30 companies with a presence in China were offered subsidies to invest in South-East Asia. Those funds are part of a 243.5 billion yen (\$3.15 billion) initiative

to reduce the Japanese reliance on Chinese supply chains. The Covid-19 pandemic exposed the risks associated with relying on a single market for vital medical supplies and other goods. Many countries are likely to reconsider their supply chains in the wake of the pandemic. South-East Asian countries are also likely to welcome increased foreign investment, especially after the [severe economic downturn](#) experienced across the region in 2020.

Australia will not cease trading with China, to do so would not be in the interests of either country. The current situation, where more than one-third of Australian exports are destined for China, however, is clearly unsustainable. Beijing has demonstrated that it will use the trade relationship to apply pressure on Canberra. As high-quality, premium agricultural goods are in high demand globally, there is no shortage of alternative markets for Australian agricultural commodities.

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