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Chinese Tariffs on Australian Wine in 2020: The Domestic Drivers of International Coercion

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Key Points

- Twelve industries were targeted in China's economic coercion programme on Australia in 2020. While all cases are designed to pressure the Australian Government to change policy, particular industries were targeted for particular reasons.
- Australian wine has a high coercion value because exports to China have exploded in recent years to become a AUS$1 billion market. Trade heavily exposed the industry to the Chinese market, especially for premium reds.
- Analysis in this paper also shows that this growth is seen as a threat to the development of the Chinese domestic wine industry that was thwarted through a protectionist and spurious anti-dumping case. The barriers will have a substantial effect on the Australian wine industry.
- The broader lesson is that Chinese economic coercion is often driven by domestic factors as much as it is by bilateral relations. Cases such as this could be expected to increase under China's economic self-reliance programme.

Summary

In 2020 China applied barriers to the export of 12 Australian industries and began 2021 with ominous signs for the higher education sector. An article published by Future Directions International outlined the logic of China's economic coercion based on an asymmetry of costs, where China seeks to impose costs on Australia to change its behaviour, but also selects industries where there will be low costs for China, or even strategic benefits.

Thus China's tariffs on barley targeted a high value export trade, but also aimed to diversify supply of this important grain away from Australia. This article argues that comparable forces are at play in the case of wine. Australian wine exports were rapidly gaining market share in the lucrative Chinese wine market, which China argued damaged its domestic industry, so the trade stopped through a spurious anti-dumping case. As China is a major market for premium wines, there will be significant effects on the industry – likely to be higher than for other affected commodities – that the industry will adapt to.

Analysis

Chinese barriers to Australian wine

On 18 August 2020, the China Alcohol and Drinks Association (CADA) applied for an initial investigation into dumping and subsidies of Australian wine. On 28 November 2020, the Ministry of Commerce (MOFCOM) ruled on the investigation and applied provisional tariffs on Australian wine in containers of two litres or less. The tariffs are effective for four months (28 November to the end of March 2021), but could be extended for an additional five months to complete a full investigation.

The initial investigation claimed an anti-dumping tariff of 202.7%, but provisional tariffs were applied to individual Australian wine exporters at a rate of 107.1% to 212.1%. On 10 December 2020, additional countervailing duties of 6.3% were imposed on alleged subsidisation of Australian wine. The anti-dumping and anti-subsidy tariff rulings were interspersed in November by informal barriers and holdups at customs. This also follows similar holdups in 2018.

Several factors make Australian wine a target of high coercion value. Substantive barriers on wine impose high costs on the industry. China is a major export market for Australian wine (valued at $US792 million in 2019) and accounts for a large proportion of total Australian exports (39 per cent), with a large premium market that is not readily substituted. In addition, parts of the Australian wine industry have been outspoken about government policy, so may have been expected to apply political pressure. As is the case in beef and cotton, the significant Chinese investment in the Australian wine industry has not deterred the coercion.

In addition to imposing costs on Australia, the barriers are also driven by domestic forces from within China. The anti-dumping case states that China has applied the tariffs on the basis that high Australian imports damaged the Chinese domestic wine industry. While there are fundamental flaws in the case, this paper documents China's policies to develop its domestic wine industry, which it regards as more achievable without competition from Australian imports. Protectionism appears to be an important driver of the trade barriers on Australian wine.

Chinese industry policy

China has for many years sought to develop the domestic wine industry through policy measures from central down to local levels, including those listed in Table 1. Policy-makers are particularly interested in developing the industry to promote higher farmer incomes including in rural and undeveloped areas (including Ningxia, Xianjiang and Gansu), as a pillar industry with high value-adding opportunities and for improved "ecological" land use.

Date	Agency / policy	Content
Central policies		
December 2011	National Development and Reform Commission (NDRC) and MIIT issued the "12th Five Year Development Plan for the Food Industry"	Construction of "raw material bases", diversify wine varieties, promote high-end and mid-range wines.
May 2012	MIIT issues "Access Conditions for the Wine Industry"	New projects or enterprises must be large (>75,000l and produce 50-70% of own grapes. Designed to regulate and standardise the industry, increase quality and safety.
August 2020	MIIT abolishes "Access Conditions for the Wine Industry"	The standards were abolished in 2020 because they constrained domestic production, including of boutique wineries.
July 2012	MIIT issues 12th Five Year Development Plan for the Wine Industry	Raw material bases, especially in central and western regions, then eastern areas. Upgrade industrial chains and enterprises.
April 2016	CADA "Guiding Opinions on the Development of China's Wine Industry during the 13th Five-Year Plan"	Plans to increase wine output to 1.6 million kl per year, sales revenue to Rmb65bn.
May 2017	NDRC and MIIT issues 13th Five Year Development Plan for the Food Industry	Continuation of 12th FYP
July 2020	"Green Factory Evaluation Requirements for the Wine Industry" (Industry Standards) drafted	
Various 2019	Tax policy	As an industrial (not agricultural product), China levies a 10% consumption tax. VAT was reduced from 16% to 13% in 2019 Liberalisation of import duties
2013-14 2020	Consumption policies	Sangong（三公）"3 public" Consumption Policy (restrictions on official banquets, car use, overseas travel) Guangpan (Clean Plate，光盘) Policy (to reduce waste in Catering (out-of-home) consumption
2020	CADA "14th Five Year Development Plan for China Alcoholic Drinks (Draft)". More detail here.	Plans to 2025 to increase wine output to 700 million litres and sales revenue to Rmb20bn. Recommends abolishment of domestic wine consumption tax and promote the integration of wine varieties. Increase financial credit support for the wine industry.
Provincial policies		
 2013 2016	**Ningxia** Regulations on the Protection of Ningxia Helan Mountain Wine Production Areas Support Policies Implementation Measures on Innovating Financial Support to Accelerate the Development of the Grape Industry	
 2017 2017	**Shandong** Support policies for the development of wine enterprises Detailed Rules for the Implementation of Policies to Support the Development of Wine Enterprises	
 2019	**Xinjiang** Xinjiang Uygur Autonomous Region Wine Industry Development Plan (2019-2025)	
 2020	**Jilin** Development Plan for Wine Industry in the Yalu River Valley of Jilin Province	
 2010 2015 2016	**Gansu** Gansu Wine Industry Development Plan Opinions on Promoting the Accelerated Development of the Province's Wine Industry Opinions on Further Promoting the Development of the Province's Wine Industry in the Hexi Corridor	
 2019	**Hebei** Implementation Opinions on Strengthening and Optimizing the Wine Industry	

Table 1 Chinese wine industry plans and policies, 2010-20

China's proactive industry policy includes government financial support, credit and land policy. As widely debated in the Chinese industry, however, several industry development policies have constrained industry development including restrictions on SMEs, tax treatment and consumption policies.

Domestic industry and trade structures

Despite or perhaps because of the industry policies, Chinese domestic wine production has shown a long-term decline especially since 2011. This coincides with an increase in imports over the period to reach 6 million hl. This means that imports are a similar volume to domestic production, to account for nearly half of total supply.

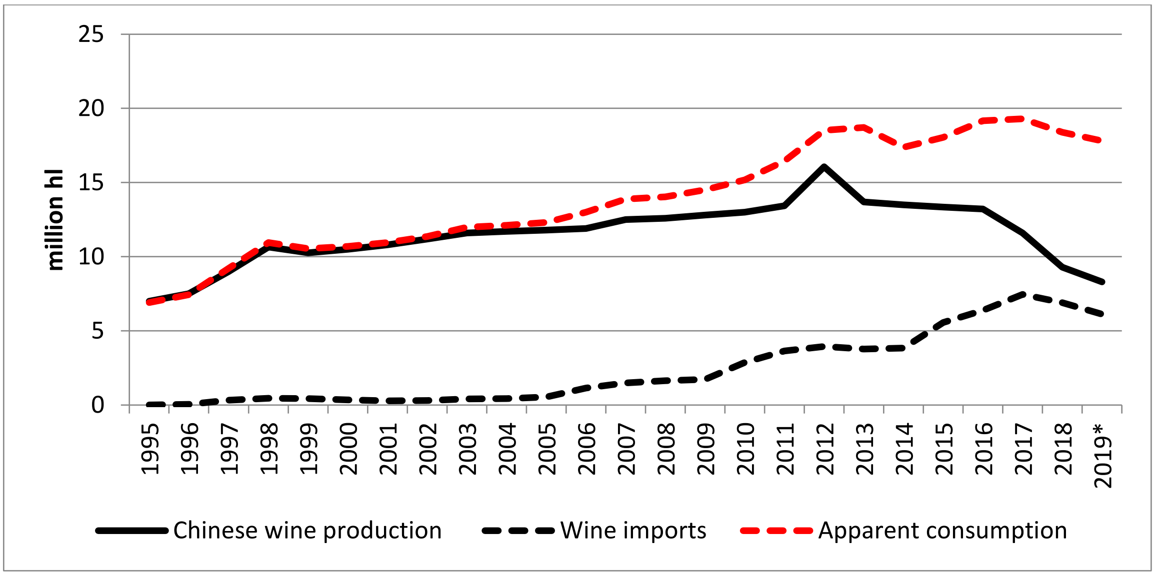

Figure 1 Chinese wine production, imports and total supply, 1995-2019. Source: OIV-International Organisation of Vine and Wine.

While the trends are clear, the reliability of the statistics should be interpreted with caution.

- Partly because of measures to increase "scale" and "standardisation" in the industry, statistics on domestic wine production are only regularly collected from wine companies classed as "large", the number of which declined to 128 in 2020. This is likely to under-state domestic production, given that there are at least 800 wineries in China.

- However, several factors may over-state domestic production (Anderson and Harada, 2018). There is double-counting where wine produced in one region is blended with wine from another, and counted as production for both.

- Similarly, imported bulk wine (that made up 30 per cent of all wine imports in 2019) can be blended or labelled as a "Product of China" and counted as domestic production.

- The incidence of wine smuggling (through Hong Kong) understates imports, but has subsided in recent years. The tariffs to the mainland may reboot this grey trade.

- "Apparent consumption" is estimated through net trade and domestic production – as discussed above, the latter is likely to be inaccurate.

A more adverse picture for domestic wine would emerge if measured by value rather than volume (Figure 2). While (cheaper) bulk wine accounted for 92 per cent of Chinese imports by value in 2000, this reduced to 23 per cent in 2019. Conversely, wine in containers of two litres or less (bottles) grew to 74 per cent in 2019. The average unit value of imported wine increased from US$0.8 to US$4 over the period.

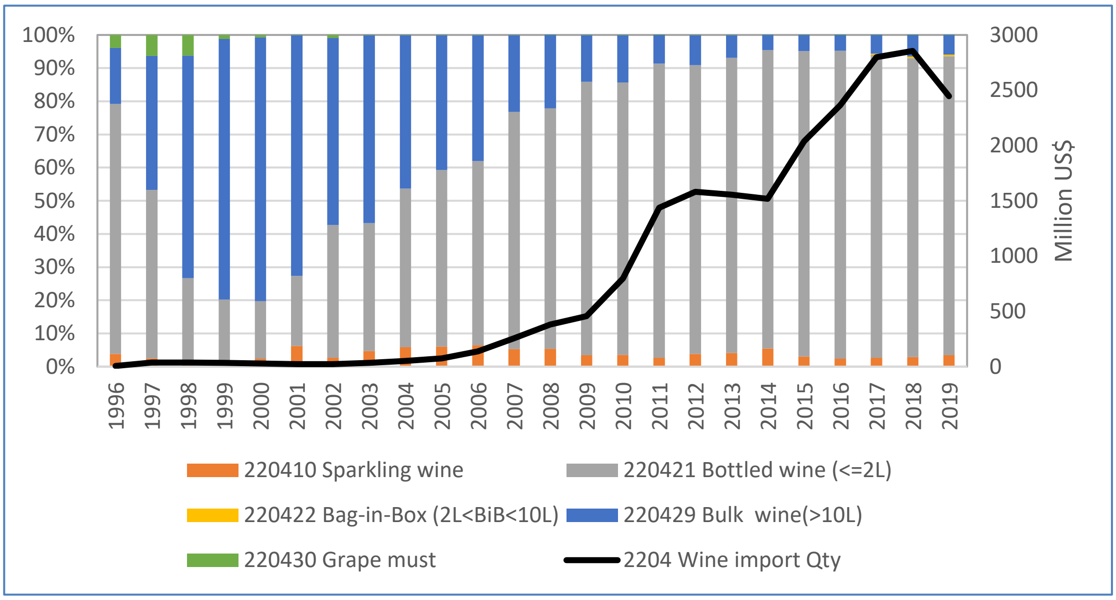

Figure 2 Structure of imported wine products to China by value. Source: UNComtrade

China is disappointed in this alignment of domestic production and imports. As stated by the Vice-Chairman of CADA Wine Sub-Association '[Chinese wine] … consumption is increasing but foreign wineries have robbed domestic wine market share and robbed potential customers.' CADA is the applicant in the anti-dumping investigation on Australian wine.

China is particularly concerned about imports of Australian wine. The value of imports of wine in containers <2 litres from Australia increased by 13 per cent per year between 2015 and 2019 to account for 37 per cent of all imports and displace France as the biggest source (Figure 3). The tariff investigation and ruling did not affect annual trade figures for 2020, which remained high (US$712 million), but there was a large spike in imports in October before the ruling in November and a large decline in December (to US$30 million).

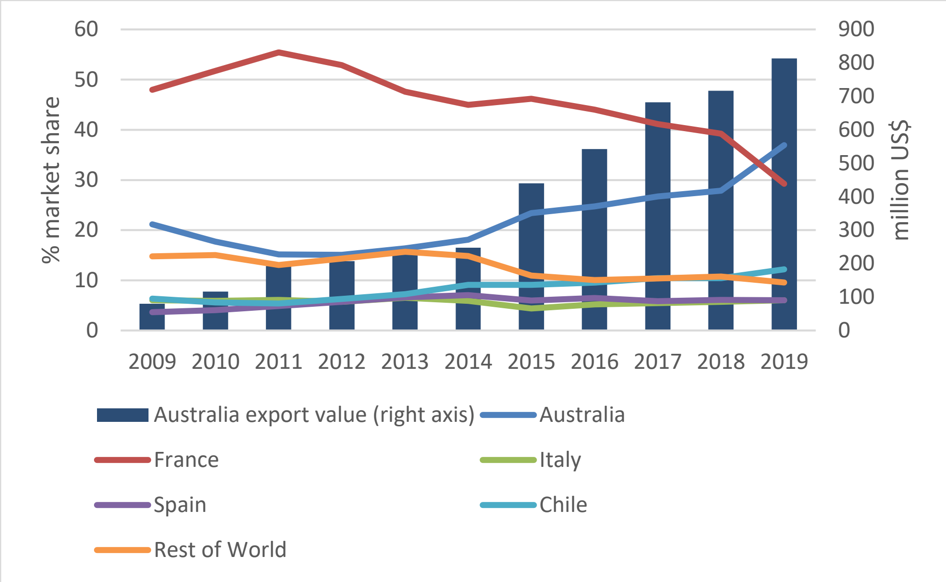

Figure 3 China imports of bottled wine <2 litres by value, 1996-2019 (% market share by major sources and value from Australia). Source: UNComtrade

The large increase in imports is partly a result of more liberal trade policy. Tariffs on Australian wine were reduced under ChAFTA from 14-20 per cent in 2014 to zero in January 2019. In 2019 tariffs for Chile and New Zealand were also zero, while tariffs for the European Union, South Africa and Argentina were 14 per cent. High tariffs on US wine (54 per cent) increased in the trade war (to total 79 per cent). The US has, however, never been a significant wine exporter to China.

China also argues that the gain in market share of Australian wine has been due to declining prices of Australian wine, although this is not supported by aggregate trade data (Figure 4). Australian wine prices (in containers <2l) are higher than Chinese domestic wine prices and those of other major exporters. There appear to be anomalies in the large divergence in Chinese CIF import prices from Australia and Australian FOB export prices to China. CIF prices have increased over the last five years and Chinese FOB prices increased in 2019, the period of investigation.

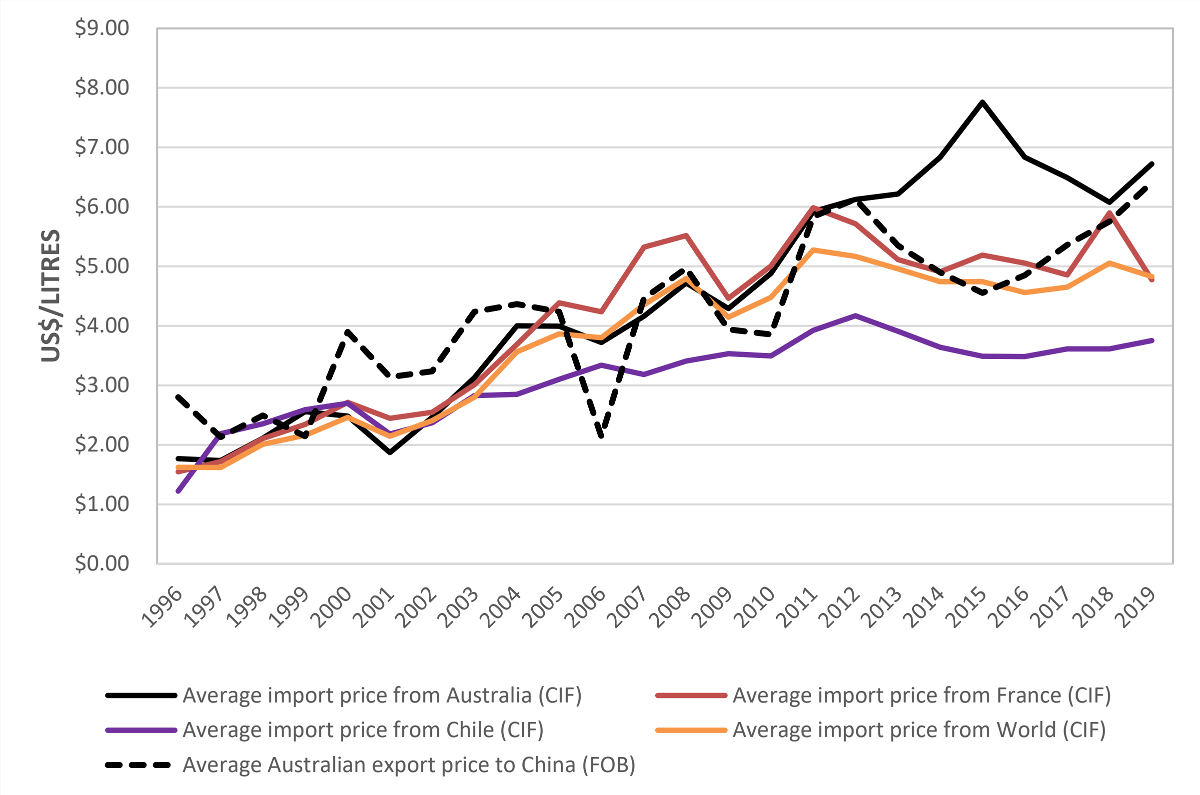

Figure 4 Average wine price (bottle <2l) imported into China from major sources. Source: UNComtrade.

China's anti-dumping case

To address burgeoning wine imports from Australia, China imposed prohibitive tariffs on Australian wine in 2020 that will all but halt the trade. Australia has responded through a large number of government and industry submissions, including those from Australian Grape and Wine (AGW).

- AGW disputes the MOFCOM assumption that Australian and Chinese wine are "similar products" that compete in a bulk wine market, which is not an accurate depiction of the highly differentiated Chinese wine market. MOFCOM has therefore failed to establish a "proper comparison".

- MOFCOM calculated the "normal value" of Australian wine based on the value of the insignificant counter-flow of Chinese wine exported to Australia. The difference between this value ($US20/l) and Australian wine exported to China (US$6.4/l) was used to set the average anti-dumping rate (202.7%).

- AGW argued it is unrealistic that, at an anti-dumping margin of 107-212 per cent, the Australian wine industry would forgo revenue of AU$1.3-$2.6 billion per year, which would mean large parts of the industry were trading insolvent.

- MOFCOM rejected as "incomplete" the detailed questionnaires and financial information submitted by Australian wine exporters to counter anti-dumping claims. AGW argues MOFCOM has not therefore used the "best available information".

- MOFCOM has not established causation between Australian wine exports and material injury to the Chinese domestic industry. It failed to consider "other economic factors" (including domestic policies and low or zero import duties).

- Claims of Australian subsidies through industry schemes and government policies are rejected (and ironic given industry policy in China).

Based on these and other points, AGW finds there is no evidence of dumping and that the MOFCOM Preliminary Determination cannot be considered to be consistent with the requirements and standards set out in Article 3.1 of the World Trade Organization Anti-Dumping Agreement.

There are several possible outcomes of the trade dispute. The first is that Australian wine will be subject to prohibitive tariffs and legal dispute for the medium term. Under this scenario, China may extend the current provisional tariffs until July 2021, and the current full investigation will impose permanent tariffs for five years. In that case, Australia is likely to appeal the case at the WTO, as it did for barley, but resolution may also take years.

A second scenario is that China will terminate the investigation. Australia would appear to have a good chance of winning an appeal in the WTO and China may choose to terminate or reduce the tariff rate before then. In this case, Australian exporters would be eligible for a rebate on the anti-dumping deposits (although trade volumes would be low). Even then, the Australian industry is likely to incorporate the risks of over-exposure to China into future investments and decisions.

Effects and mitigation

The certainty of major disruptions raises questions about alternative markets – domestic, traditional or new. While in 2008 China accounted for less than two per cent of Australian exports for all wine by value, this had increased to 39 per cent in 2019. An inverse pattern applies to the UK (35 per cent to nine per cent), while the market share to the US reduced from 32 per cent to 24 per cent over the period. The share of the "rest of the world" has remained around 25 per cent of Australian exports.

The opportunities for substitution are limited by the highly segmented international wine market. While the average price of wine exported to China has traditionally been similar to other major markets and indeed the world, a large premium had emerged in the Chinese market by 2019 (Figure 5). These premium markets are not replaceable in the near future without substantial cost.

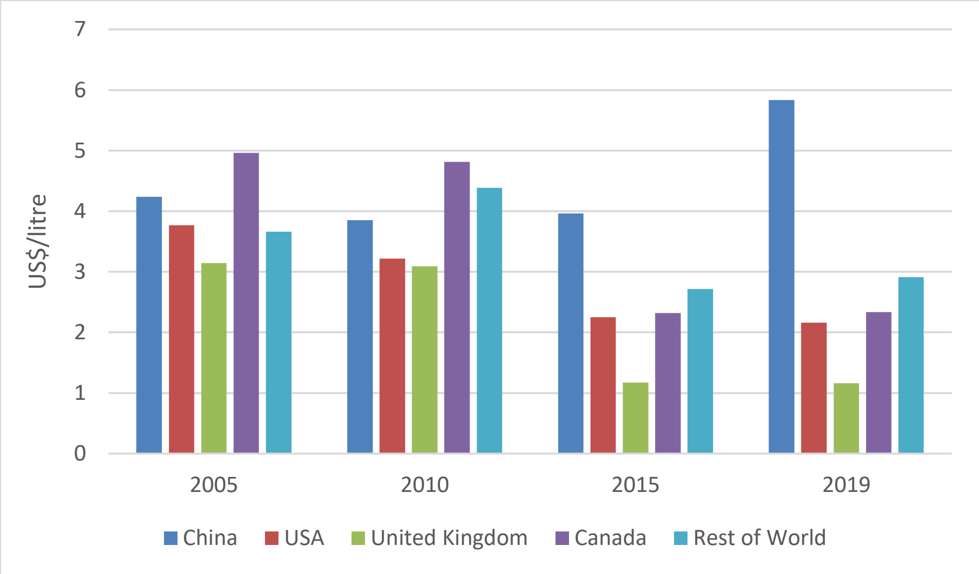

Figure 5 Average annual prices of Australian wine (all wine) exports, 2005-2019. Source: UNComtrade

Recent modelling by Wittwer and Anderson simulated the effects of a 170 per cent tariff on Australian wine. The tariff wipes out the trade to China, but is partly offset by increased exports to other markets and a net loss of US$225 million (although this in the context of windfall gains in recent years). This is estimated to decrease winegrape prices by 11 per cent, which compares with 13 per cent in the AUD appreciation 2007-11 and 8 per cent due to COVID.

Conclusions

In some ways the Australian wine industry has been too successful in China. The growth in market share was seen as a threat to the Chinese domestic wine industry and to long-standing Chinese industry policy. It has also made the Australian industry vulnerable to Chinese economic coercion and a range of risks emanating from China, including Chinese domestic drivers. The protectionism against Australian wine may reflect the growing momentum of China's economic self-reliance programme in 2020 that includes measures to 'reshape new industry chains and comprehensively increase technological innovation and import substitution'. Other industries should take note.

The case of wine also illustrates differences between commodities. High volume, globally traded commodities like barley and beef have been able to mitigate the costs of the Chinese barriers, while specialist products like wine and lobster are more exposed. As it has for other shocks, the resilient, innovative and competitive wine industry will have to adapt.

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