

2011



The AMERICAN CHAMBER of COMMERCE in SHANGHAI

# VIEWPOINT

AGRICULTURE

Agriculture in China  
*Boosting American Opportunities  
in the World's Largest Market*

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Insight*



# Executive Summary

As the world's largest agricultural market, China should be the focus of U.S. efforts to grow tens of billions of dollars worth of agricultural and food exports. China's rapidly developing agriculture industry is also an opportunity for U.S.-China cooperation as China strives to address challenges in improving the safety of its domestically produced food for consumption at home and for export.

Agricultural exports to China can be a driving force for achieving the objectives of the National Export Initiative (NEI), which calls for doubling U.S. exports by 2015 in support of two million American jobs. Already, the \$17.8 billion that China buys in U.S. agricultural and food products is more than any other country. Agricultural exports to China create and support American jobs – an estimated 150,000 in 2010.

Going forward, China's demand for U.S. goods to feed a population of 1.3 billion people will only increase. It is no easy feat for China's farmers to satisfy the government's policy objective to grow 95 percent of the country's own staple crops. China has 20 percent of the world's population yet only seven percent of the world's arable land and seven percent of freshwater resources. Natural resource challenges likely will intensify going forward as rural plots of farmland are replaced with industrial zones, while cities swell to include new housing developments and roads needed to support millions of new urban households.

Another reason is China's growing consumer market for foreign products. China's increasingly wealthy – and consumer savvy – middle class is demanding more brand name foreign-produced food, whether in supermarkets or at popular eateries like Yum! Brand's KFC. Though foreign products account for a rather meager percentage of total food products sold, a willingness to pay a premium for foreign products not only helps fulfill changing dietary choices among many Chinese but also addresses worries of contracting food-borne illness from contaminated domestically-produced products.

In addition to exports, China's drive to improve food safety provides an opportunity for relevant U.S. government agencies and U.S. companies to assist China. As the Chinese government clamps down on food safety violations, the U.S. can lend valuable expertise,

technical assistance and know-how to help China build capacity to enforce its developing food safety standards. This not only paves the way for U.S. food exports to China and the adoption of U.S. standards in China, but U.S. consumers have a direct interest in the safety of Chinese food as China exports more and more food products to the U.S. each year.

U.S. agricultural companies are competing at a high level thanks in part to U.S. Department of Agriculture (USDA) support programs. But they are confronted with numerous challenges in China, including limitations on accessing the Chinese market through exports, concerns over intellectual property rights (IPR) and contending with Chinese government interventions in the market.

**The U.S. is in a strong position, given its capacity in agricultural production and technology adaption, to take advantage of China's growing market for agricultural and food products. AmCham Shanghai has developed the following recommendations for the U.S. government:**

- Secure greater market access for U.S. companies in China and follow up on commitments made by China to open up the China market
- Engage China to improve IPR enforcement to protect U.S. intellectual property and encourage innovative approaches to address China's food production and food safety challenges
- Boost funding for U.S. Food and Drug Administration (FDA) operations in China to advance food safety in China, protect U.S. consumers and promote U.S. standards in China's food industry
- Support existing USDA cooperative programs that promote U.S. agricultural products in China 

# Powering America's No. 1 Agricultural Export Market

China presents an enormous opportunity for U.S. agricultural and food companies to boost exports given China's increasingly diverse food demands and the immense food needs of a 1.3 billion person strong population.

Demand for U.S. agricultural and food exports is exploding in China thanks to such drivers as rising Chinese spending power, a widening middle class consumer base and growing demand for high quality, higher value and a greater variety of foods. Improved living standards have led to changes in urban diets, such as an increase in demand for meat-based protein, thereby forcing China to import more soybeans, corn and fishmeal for animal feed.

In the background is China's food security policy, which strives for 95 percent self-sufficiency in production of staple crops – i.e., grains like wheat, corn and rice deemed important for national security. But maintaining a food self-sufficiency goal is not without major challenges, including a shrinking supply of farmland and water scarcity. It is no easy feat for China's farmers to satisfy the government's policy objective given that China has 20 percent of the world's population yet only seven percent of the

world's arable land and seven percent of freshwater resources.

These trends, coupled with the sheer enormity of China's food market – the world's largest – quietly have shifted China into a net food importer on a scale only second to the U.S. The U.S. has capitalized by nearly tripling agricultural exports to China since 2005, reaching a value of \$17.8 billion in 2010. Export growth has increased to such an extent that in 2010 China moved past Canada to become the No. 1 export destination for U.S. agricultural products.

Agricultural exports help support and create new U.S. jobs and generate economic activity in the U.S. The U.S. Department of Agriculture (USDA) estimates that every \$1 billion in agricultural exports supports 8,000–9,000 American jobs, which translates into about 150,000 jobs supported by agricultural exports to China in 2010. The USDA's Economic Research Service



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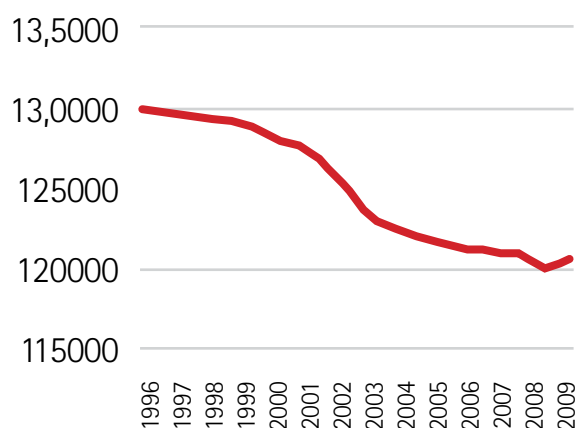
– U.S. Department of Agriculture

estimates that each \$1 in agricultural exports generates \$1.48 in supporting business activity thanks to a complex supply chain needed to get products to their final destination.

The U.S. also controls the largest share of China's import market for agricultural products. Over the period 2005 through 2010, U.S. companies supplied 26 percent of China's imported agricultural products, 11 percent more than second-place Brazil. U.S. soybeans, cotton, processed animal feed and animal hides and skin are some of the goods most in demand in China, though China imports only a few U.S. agricultural goods on a large scale.

Going forward, although growing 95 percent of its own essential crops, China could look to the U.S. to close supply gaps for some of these crops (e.g., corn) to bring down food prices. Meanwhile, there are growing opportunities for U.S. companies to supply China with greater amounts of more value-added crops that China imports to free acreage for essential crops. Thanks to excess agricultural capacity in the U.S., U.S. companies are in a strong competitive position versus other nations exporting to China and can play a leading role in fulfilling stronger demand for such goods as higher quality consumer-oriented products, meats, nuts, dairy, dried fruits, baking ingredients, animal products and processed foods.

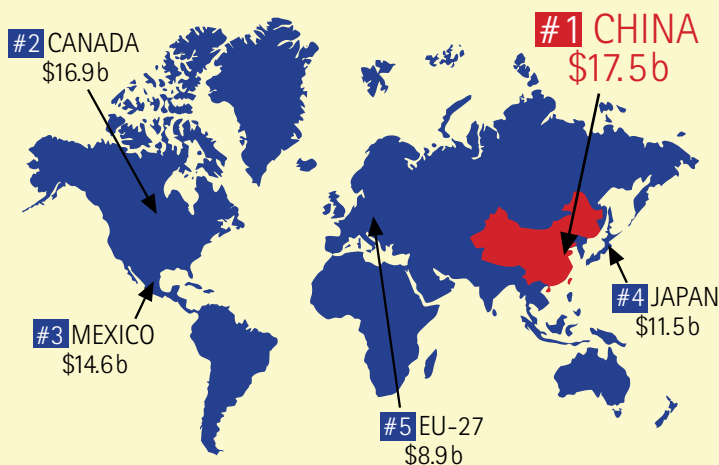
## China's Arable Land (in thousand hectares)



Source: Ministry of Land Resources (MLR), China Development Gateway/APCO Worldwide

## China: Top Market for U.S. Agricultural Exports

Top five destinations for U.S. agricultural products in 2010 (billion US\$)



**World Total: \$115.8 billion**

Source: U.S. Department of Agriculture

## U.S. Goods in Demand in China

Value of top U.S. agricultural exports to China in 2010 (million US\$)

1. Soybeans	11,319
2. Cotton	2,000
3. Hides and skins	822
4. Processed animal feed	821
5. Corn	328
6. Soybean oil	255
7. Dairy	243
8. Fruits, fresh	236
9. Poultry	168
10. Processed foods	158
11. Tobacco and products	155
12. Nuts	151
13. Vegetables, processed	103
14. Fruit, processed	86
15. Alcoholic beverages	45

**Total: \$17.8 billion**

Source: U.S. International Trade Commission



# Helping China Improve Food Safety

Food-safety crises continue to occur with regularity in China. Such incidents are a major concern for Chinese consumers, as well as Americans who increasingly eat food made in China. As China's fourth-largest agricultural export market, the U.S. imported \$3.2 billion worth of food products from China in 2010.

The U.S. government is helping to strengthen the already substantial amount of work China has invested to improve food safety and develop new food safety standards, thereby working to ensure the quality of food that Americans consume from China.

For example, the U.S. Food and Drug Administration (FDA), which set up offices in Shanghai, Beijing and Guangzhou in November 2008, is helping to strengthen China's regulatory efforts by carrying out hundreds of inspections and audits in China, working to build China's supervision capacity and conducting technical exchanges and training on food safety best practices. The FDA works in cooperation with China's State Food and Drug Administration and the General Administration of Quality Supervision, Inspection and Quarantine (AQSIQ).

U.S. companies are an important player in the effort to promote food safety standards in China. Many larger and more experienced U.S. food suppliers, processors and retailers in China, mindful of the importance of food safety and the challenges, already have integrated high standard food safety procedures in their factories.

For example, Austin, MN-based Hormel Foods employs metal detection, microbiological swabbing programs and pest control programs in its Shanghai and Beijing plants. AmCham Shanghai members meet regularly with U.S. FDA officials and, in cooperation with the agency, established a web platform for Chamber members to post concerns and questions on food safety directly to China-based FDA staff.

Nearly 70% of the Chinese population remains very concerned about food safety.

- Tsinghua Media Survey Lab



IMAGINECHINA

## China's 12th Five-Year Plan: Driving China's Agricultural Market

China's 12th Five-Year Plan for National Economic and Social Development (FYP), which the National People's Congress (NPC), or legislature, approved in March 2011, will offer opportunities and have a profound impact on foreign companies in the food and consumer products sector in China. An understanding of the areas of emphasis in the 12th FYP is critical for foreign agricultural companies' China strategy.

Covering the years 2011–2015, the 12th FYP emphasizes the quality, rather than the quantity, of economic growth and strives to shift the national economy to a consumption-driven path of development rather than one driven by exports. A shift to consumption-led growth creates growth opportunities to serve China's widening middle class consumer base, whose spending power China aims to boost by increasing household disposable income by an annual rate of seven percent.

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Specifically, the FYP identifies bio-agriculture as one of seven "Strategic Emerging Industries" that are essential for China's long-term growth. A modern agricultural sector in China is viewed as critical to helping China increase production yields to provide enough food to feed its massive population and address food safety concerns. China plans to implement on a large scale new modern farming technologies to achieve these goals and will advance agricultural land consolidation to better manage objectives.

U.S. companies, which lead the world in commercializing agricultural technology, should have an opportunity to support these efforts with investment in research projects and pilot initiatives to accelerate development of scientific innovation and infrastructure development in agriculture. More will be known as plans and incentives within this portion of the FYP are developed.

Although the Chinese government will be looking to partner with foreign players, companies planning to take advantage of emerging opportunities in the bio-agriculture sector face the reality that the ultimate, likely policy objective is the "assimilation and absorption" of foreign technology. Hence, intellectual property (IP) protection will be a key consideration.

# Challenges Facing U.S. Companies

U.S. companies operating in China's agricultural sector face numerous challenges, including market access barriers, ongoing intellectual property rights (IPR) concerns and intervention by the Chinese government into food markets.

## Market Access

A 2011 U.S. International Trade Commission (ITC) report finds that the U.S. lost an estimated \$5.2 billion in agricultural exports to China in 2009 because of Chinese tariffs and non-tariff measures. Non-tariff measures hurt U.S. competitiveness by making it more difficult for exports to enter China, increasing risks and therefore costs to traders. According to the ITC, China's non-tariff measures "effectively prohibit imports of U.S. beef, pears, fresh potatoes, pet food, and strawberries, and significantly restrict imports of U.S. apples and pork."

U.S. and other foreign agricultural companies remain largely frozen out from supplying China with staple crops – i.e., grains like wheat, corn and rice – that China deems important for national security and reinforces with import quotas. These government-determined quotas, called tariff-rate quotas (TRQs), set a specified quantity

of key commodity imports to be levied a lower tariff rate; imports that exceed the acceptable limit are subject to a much higher tariff. When China has needed to import commodities, only large state-owned traders have been allowed to use the preferential quotas.

## IPR Challenges

U.S. agricultural companies face numerous IPR challenges in China that impact their competitiveness. Specific concerns include counterfeiting of branded U.S. agricultural products or labels, trademark violations and technology theft of new varieties of plants and seeds.

The Chinese government has made legal improvements to enhance deterrence efforts provided by administrative, civil and criminal penalties, and successful public outreach programs have increased. However, lack of coordination among the main enforcement bureaus, poor training for



## Food Safety: A Trouble Spot in China

Food safety is a top concern among the Chinese public. According to a recent survey by Tsinghua Media Survey Lab and Insight China, nearly 70 percent of the Chinese population remains very concerned about food safety, and more than half of survey respondents view government failure as the key reason behind unsafe food. A number of widely reported food scandals in 2011 – tainted buns, steroid-laced pork, vinegar contaminated with antifreeze and "exploding" oversized watermelons – have reinforced the public's uneasiness. Structural factors such as

enforcement personnel, low public awareness and local corruption remain major hurdles.

### Market Intervention

Government interventions to tame a surge in food inflation and policies on food safety and security have created heightened uncertainty for foreign companies in China.

Inflation has heightened sensitivity to food price increases and exposed companies that wish to raise prices to a strong risk of backlash from both government and consumers. Since late 2010, China has stepped up pressure on foreign companies to keep prices on key essentials level. The government is closely supervising price increases and issuing fines for even public discussion of potential price hikes. Although foreign companies are facing cost pressures on labor, commodity prices, environmental and regulatory compliance, they now are increasingly reluctant or even unable to pass on these cost increases to consumers.

The Chinese government also is tightening control over foreign companies per the Ministry of Commerce's 2007 Foreign Investment Catalogue, restricting investments to most aspects of the value chain – from seed development to primary processing and especially on essential food products. The government's goal is to ensure greater levels of "food security" by consolidating the producing, processing and increasingly the importing and trading of essential agricultural commodities in the hands of Chinese entities.

industry fragmentation, use of banned chemicals to gain a competitive edge and prohibitively stringent testing and safety requirements, which discourage compliance, all have led to elevated safety risks. Enforcement is a challenge as well because of a decentralized and overlapping regulatory authority, insufficient government supervisory resources and the sheer enormity of China's agricultural market that regulators police.

In response, China's government is continuing a focus on consolidating the food and agricultural sectors to facilitate oversight, as well as redrafting and streamlining standards, particularly on food additives and ingredients and on new under-regulated areas such as food packaging. The government has

## Despite Progress, Obstacles to U.S. Agricultural Exports Remain



An open market in China – America's No. 1 export destination for agricultural products – is increasingly important for U.S. agricultural companies given the immense scale of China's food market opportunity and growing need for food imports. Yet, China's market remains restricted or outright closed to certain key U.S. crops despite progress made through U.S. government efforts to secure improved market access.

These include:

- **Beef:** U.S. beef exports to China have been banned since 2003 but could result in more than \$200 million in sales for the U.S. beef cattle industry, according to the National Cattlemen's Beef Association
- **Poultry:** Anti-dumping and countervailing duties on U.S. poultry result in up to \$363 million in lost U.S. exports, according to a 2011 U.S. International Trade Commission (ITC) estimate
- **Pork:** U.S. pork exports to China have recovered to a healthy level since China's partial import ban was lifted in 2009, but shipments are limited because ractopamine, an approved growth additive used by around half of U.S. pork producers, is prohibited in China

committed to continue closely monitoring safety in the dairy sector and extend its oversight to the meat, edible oil and alcohol sectors. Penalties for food safety crimes have been increased and crackdowns on violators have intensified.

The impact for foreign companies is although compliance costs are rising, a tighter regulatory environment has made progress towards leveling the playing field for foreign companies, which tend to have a better track record at ensuring food safety. Opportunities have opened for foreign retailers because of a preference among Chinese consumers for brand name foreign products perceived to be of a higher quality and therefore safer to eat.

# Recommendations

AmCham Shanghai encourages the U.S. government to help U.S. agricultural companies take advantage of China's growing market for agricultural and food products.

We recommend that the U.S. government should:

**1. Secure greater market access and improved regulatory transparency for U.S. companies in China and follow up on commitments made by China**

The U.S. government should help U.S. agricultural and food companies capitalize on China's growing need for food by engaging the Chinese government to open additional food markets to U.S. exports. The U.S. has achieved some success in this area, such as securing China's commitment at last December's U.S.-China Joint Commission on Commerce and Trade (JCCT) session to find a solution to reopen its market to U.S. beef. Although a welcome step, vigorous U.S. government-led engagement with China at recurring secretarial, high-level meetings and at follow-up discussions – at both the national and provincial levels – is critical for expanding export opportunities for U.S. food and agricultural companies.

The U.S. also should encourage China to improve transparency of import policy regula-

tions to help U.S. food and agricultural exporters better guard against costly holdups when goods enter China Customs.

**2. Engage China to improve IPR enforcement to protect U.S. intellectual property and encourage innovative approaches to address China's food production and food safety challenges**

The U.S. government should continue its multifaceted pursuit of improved IPR enforcement through the U.S.-China Strategic and Economic Dialogue (S&ED), JCCT, the World Trade Organization (WTO) and U.S. Trade Representative (USTR) reviews. Recurring high-level meetings provide forums for resolving disputes and for ensuring that U.S. enterprises operate on a level playing field in China.

Improved IPR enforcement not only means increased revenue for U.S. agricultural companies through the introduction of products, services and technology to China. It also helps China address food safety issues by improving the quality of products in China and ultimately



China's food demand continues to outpace its domestic production, creating a market opportunity for exporting countries such as the United States.

– USDA Foreign Agricultural Service

increasing local agricultural yields through use of bio-technology and other technological advances being used in the U.S.

### 3. Boost funding for U.S. FDA operations in China to advance food safety in China, protect U.S. consumers and promote U.S. standards in China's food industry

While China has developed new food safety standards, implementation and enforcement are major challenges. The U.S. government should continue funding U.S. FDA operations in China with a focus on capacity building of Chinese food safety agencies like AQSIQ.


For Chinese food products destined for the U.S., the U.S. government should support FDA cooperation programs on improving China's food safety labs and testing equipment, as well as training programs that provide valuable guidance on how to implement U.S. food safety standards throughout the vast Chinese food industry. The FDA could also develop a training program for China's farmers and agriculture companies who are interested in exporting to the U.S. with a focus on sharing the latest U.S. food safety techniques.

Such positive engagement with China will not only improve food safety. It has the

potential to improve the quality of China's food exports to the U.S. and paves the way for U.S. food companies to access China.

### 4. Support existing USDA cooperative programs that promote U.S. agricultural products in China

The U.S. government should support successful USDA programs that grow exports, advance U.S. food standards and support engagement with Chinese officials. One key program is the Market Access Program (MAP), which helps promote U.S. agricultural commodities and products overseas. This public-private partnership provides matching funds to U.S. food associations, non-profits and enterprises with a clear focus on growing exports from small U.S. agricultural companies with less than 500 employees, which oftentimes do not have the resources to reach remote overseas markets.

The California Walnut Commission, Alaska Seafood Marketing Institute, Washington Apple Commission, Ginseng Board of Wisconsin, American Soybean Association and U.S. Dairy Export Council were several of the more than 60 state or national participant groups or companies awarded MAP grants in 2010. 

## USDA in China: Elevating U.S. Agricultural Commodities and Products

Agencies of the U.S. Department of Agriculture's (USDA) Foreign Agricultural Service, including the Office of Agricultural Affairs (OAA) and Animal and Plant Health Inspection Service (APHIS) in Beijing and five Agricultural Trade Offices (ATO) around China, provide a critical support function. USDA staffs its offices with foreign and local experts to promote U.S. food and agricultural products, gather market intelligence, improve market access for U.S. products, connect potential Chinese

buyers to U.S. producers, address agricultural and food safety concerns and ultimately help to increase exports that support American jobs.

The USDA Foreign Agricultural Service has been instrumental in the success of U.S. agricultural exports to China. For example:

- Every \$1 invested in USDA foreign market development programs returns \$35 in food and agricultural exports, according to Global Insight, Inc.
- Alfalfa exports jumped 221 percent in 2010 to \$61 million in part because of efforts by officers in ATO's Shanghai, Beijing and Guangzhou offices to address potential market access barriers and promote alfalfa as high quality

fodder in Chinese dairy production.

- In 2010, USDA signed a memorandum of understanding (MOU) with China's AQSIQ to establish a formalized inspection and quarantine structure for U.S. soybean exports, protecting access for America's No. 1 crop export to China.
- USDA endorsed trade shows in China attract hundreds of Chinese buyers for a wide variety of U.S. food and beverage products, helping to generate at least \$40 million in sales in 2010 alone.
- ATO-facilitated reverse trade missions bring hundreds of potential Chinese customers to the U.S., resulting in more than \$82 million in tree nut sales from 2008 to 2010 and more than \$5 million in hides & skins sales in 2009.



The AMERICAN CHAMBER of COMMERCE in SHANGHAI

## VIEWPOINT

### Viewpoint

An analysis of issues impacting today's business environment in China

### About The American Chamber of Commerce in Shanghai

The American Chamber of Commerce in Shanghai (AmCham Shanghai), known as the "Voice of American Business in China," is the largest and fastest growing American Chamber in the Asia Pacific region. Founded in 1915, AmCham Shanghai was the third American Chamber established outside the United States. As a non-profit, non-partisan business organization, AmCham Shanghai is committed to the principles of free trade, open markets, private enterprise and the unrestricted flow of information.

For more information, please visit: [www.amcham-shanghai.org](http://www.amcham-shanghai.org).

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The American Chamber of Commerce in Shanghai  
Shanghai Centre, Suite 568  
1376 Nanjing Road West  
Shanghai 200040 China

上海美国商会中国上海市南京西路  
1376号上海商城东峰办公楼568室

Phone: (+86 21) 6279-7119  
Fax: (+86 21) 6279-7643