

China

Type: Dynamic Growth Market; High Volume, Large Market Share

China is a large and important market for U.S. exporters of agricultural equipment, one that presents both significant opportunities and formidable challenges. U.S. exports in 2014 totaled \$376.1 million.⁵⁵ Although growth has been substantial and sustained for more than a decade, exports in several major product categories fell sharply last year. Exports in the livestock and produce sectors increased, but they were unable to compensate for declines elsewhere. The Chinese Government's role in the agricultural economy—unique among major agricultural equipment markets—and its aggressive efforts to favor and promote domestic manufacturers will continue to present challenges for U.S. exporters. U.S. companies, especially SMEs, should consider carefully whether or not China is a suitable market for their business.



*Note: Ranking based on a comparison of U.S. exports to five large dynamic growth markets: Brazil, China, Russia, South Africa, and Ukraine.

Total U.S. agricultural equipment exports to China will likely fall again in 2015, although not as sharply as last year, due to continued weakness in global grain prices. Stabilizing commodity prices will improve prospects for U.S. exporters in 2016. Exports of equipment for the livestock sector will remain a growth area for U.S. exporters. Fresh produce and other high-value food products represent an area of opportunity, especially as Chinese producers position themselves to comply with the U.S. Food Safety Modernization Act (FSMA). Significant risk will continue to characterize the Chinese market for U.S. exporters – even as the world's largest agricultural economy mechanizes itself at a rapid pace.

Overview

China is a large market for U.S. agricultural equipment exporters with significant potential for future growth. U.S. exports to China grew at an annual rate of 21.7 percent from 2004 to 2013. Although shipments to China declined in 2014, there are strong reasons to believe the Chinese market will return to robust growth in the future.

The country is in the midst of an historic transformation from traditional, labor-intensive farming practices to mechanized, high-technology agriculture. A variety of forces drive this transformation. The Chinese Government, which effectively owns and operates the country's farm

sector, has made mechanizing agriculture and moving rural inhabitants to urban areas a top policy objective. Behind this policy lie China's changing demographics, limited agricultural land and water resources, the Chinese population's increasingly varied dietary preferences, and the high priority the government continues to attach to food security.

The opportunities presented by the rapid mechanization of the world's largest agricultural economy have to be balanced against the challenges faced by U.S. exporters doing business in China.

China: Major Crops

- Fresh Produce and other high-value products: tomatoes, apples, garlic, mushrooms and truffles, cucumbers and gherkins, watermelons, chilis and green peppers (28.7 percent).
- Red Meat (25.8).
- Grains oilseeds, and other row crops: rice, wheat, potatoes, corn, peanuts (23.8).
- Poultry (14.0).
- Dairy: fresh milk (3.2).

(Percentage share of the top 20 commodities produced in 2012, by value; Source: U.N. Food and Agriculture Organization.)

These challenges include an array of Chinese Government policies, local business practices, and the cost—and attendant business risk—of simply establishing business operations in China before significant sales can be realized.

The Chinese Government’s “Strategic Emerging Industries” industrial policy identifies agricultural equipment as a priority industry.⁵⁶ As a result, a variety of policies favor local manufacturers and products over imports. Although China does offer patent protection to foreign products, theft of intellectual property is widespread within China’s borders and beyond. A robust, effective business presence in China can mitigate some of these risks. Nevertheless, the cost—informally estimated at \$500,000 over at least a three-year period—can be prohibitive for many SME exporters.

U.S. manufacturers hold a 43.5 percent share of China’s import market for agricultural equipment.⁵⁷ Taking into account domestic production, however, ITA estimates that imports from the United States represent less than two percent of a total Chinese market that may be worth as much as \$8.8 billion. Despite their substantial position in the import market, strong and growing competition from domestic manufacturers and well-established third-country competitors challenge U.S. suppliers across all major categories of agricultural equipment sold in China.⁵⁸

In 2014, China was United States’ sixth-largest export market for agricultural equipment, worth \$376.1 million. Machinery and equipment for producing grains, oilseeds, and other commodity row crops represented 38.1 percent of total U.S. exports, valued at \$143.2 million. Exports related to livestock and fresh produce represented 18.8 and 9.0 percent of total exports respectively, amounting to \$70.8 million and \$33.7 million. Exports of parts, at 34.2 percent of the total and with a value of \$128.8 million, are proportional to global U.S. exports in this category. Exports of agricultural sprayers and tractors in the 40-100hp and less-than-40hp ranges together accounted for less than one percent of U.S. exports.

Exports to China fell sharply in 2014, declining by 23.3 percent from the previous year. This followed the steep decline in global grain prices that began in 2011-2012. It is consistent with falling exports in other markets where machinery and equipment for producing grains and oilseeds and other row crops are a large portion of U.S. exports.

U.S. shipments of agricultural equipment parts fell at almost the same rate in 2014—22.4 percent—as total agricultural equipment exports to China. Export performance in the broad parts segment varied widely in 2014, with strong growth in parts for highly specialised equipment such as milking machinery, seeders and planters, and certain tractor components. Weak 2014 results notwithstanding, exports of parts have grown strongly in recent years, at annual rate of more than 27 percent from 2009 to 2014.

Parts exports reflect not only the demand for after-market parts and components, but also the rapidly evolving character of China’s agricultural equipment manufacturing sector.⁵⁹ A downturn in domestic demand certainly contributed to this. However, the global decline in agricultural equipment trade—and Chinese exports— is also likely to have reduced Chinese demand for imported parts.

Equipment exports to China’s livestock sector continued to show strong growth, up 23.8 percent in 2014. This is consistent with 27 percent annual growth from 2009 through 2014. Performance was flat in the produce sector, with U.S. exports down 0.6 percent for the year. The on-going decline in exports of agricultural sprayers accelerated in 2014, with shipments from the United States worth only \$1.5 million. Exports of 40-100hp and less-than-40hp tractors were negligible.

China’s domestic agricultural equipment industry is characterized by a large number of largely unspecialized manufacturers producing low-technology machinery. The domestic industry is described by an authoritative Chinese source as having “the technology level of their counterparts in the developed countries in the 1970s.” The industry has a “loose and chaotic” structure, with “large enterprises not...strong and small enterprises not specialized.”⁶⁰

Competition is intense, especially among domestic manufacturers of lower-technology products.⁶¹ The presence of leading international manufacturers only adds to the competitive character of the market.⁶² As recently as 2011, the China Agricultural Machinery Distribution Association (CAMDA) estimated that the top five domestic manufacturers accounted for less than 25 percent of the market.⁶³ Major Chinese agricultural equipment companies include First Tractor, the YTO Group, Foton Lovol, and Changzhou Dongfeng Agricultural Equipment.⁶⁴

Leading U.S. and international manufacturers with investments in China include the AGCO Corporation, Deere & Company, the Claas Group (Germany), CNH Industrial (Italy), and the Kubota Corporation (Japan). AGCO manufactures agricultural tractors, harvesting machinery, diesel engines, and systems for grain-storage, poultry, and swine production at plants in Shanghai, Changzhou, Yangzhou, and Daqing. Deere manufactures agricultural tractors, corn harvesters, and engines at factories in Harbin, Jiamusi, Ningbo, and Tianjin. Claas Jinyee Agricultural Machinery manufactures agricultural tractors and combine harvesters in Gaomi and Daqing. CNH Industrial manufactures agricultural tractors, combine harvesters, cotton and sugar cane harvesters, and other equipment at facilities in Harbin, Guangzhou, Shanghai, Foshan, and Urumqi. Kubota manufactures agricultural equipment in Suzhou and engines in Shanghai and Wuxi.⁶⁵

The Chinese Government is taking aggressive measures to support and modernize the domestic agricultural equipment sector. Industrial policy goals include consolidating the structure of the industry around “five globally competitive large enterprise groups” with annual sales of RMB15 billion each; developing more technologically advanced, higher-capacity products, such as high horse-power (100hp and up) tractors; developing core industrial technologies, such as more sophisticated transmissions, engines, and electronic controls; improving product quality, and locating joint research and development facilities with foreign companies in China.⁶⁶

The most direct competitive impact of China’s industrial policy for U.S. agricultural equipment exporters is the extensive system of subsidies provided to farmers for the purchase of domestically-manufactured products. Since the subsidies were introduced in 2004, their scope has expanded to more than 175 types of machinery. In 2012, government-designated subsidies for purchasing agricultural machinery were worth \$3.5 billion. Equipment eligible for subsidies includes tractors, harvesting machinery, planters, agricultural implements, and farm dairy machinery. Decisions on what equipment to subsidize are made at the provincial and local level. Imported products are not eligible for subsidies.⁶⁷

Despite the sharp downturn in 2014, China will remain an important market for U.S. exporters of agricultural equipment. China has the world’s largest agricultural economy, producing a highly diverse array of food and

fibre, staple commodities and high-value agricultural products. The country is the world’s leading producer of rice, cotton, pork, and a variety of other agricultural products such as fresh eggs, tomatoes, garlic, and watermelons. China ranks among the top three producers of a many other products including wheat, corn, chicken meat, beef, fresh milk, oranges, and sugar cane.

Significant scope remains for mechanization of this vast agricultural economy. For example, some 35 percent of China’s labor force is employed in agriculture. In comparison, two percent is typical of capital-intensive, high-technology agricultural economies—in North America, the European Union and the OECD—that take most U.S. exports of agricultural equipment.⁶⁸

Because subsidies are only available for domestic products, U.S. exporters necessarily will find their opportunities at the high-technology end of the agricultural equipment market and for higher-value food products. Because of Chinese population’s growing taste and ability to afford meat and dairy products, the livestock sector (pork, poultry, dairy, beef) is likely to remain an attractive segment for some time to come.

The produce sector is also a likely growth area for a variety of reasons. As with meat and dairy, China’s urban consumers can afford to eat more fresh produce and processed fruits, vegetables, juices, etc. Demand for will continue to grow as the population shifts from rural areas to the cities.

Chinese consumers are also increasingly conscious of food safety. Significant investment will be required by China’s food processors to meet their growing expectations. In addition, the U.S. Food Safety Modernization Act (FSMA) is also likely to influence Chinese investment in the fresh produce and other high-value sectors.

FSMA will require Chinese exporters of fresh produce, seafood, spices, ingredients and other FDA-regulated food products to the United States to meet—and document that they meet—the same requirements as U.S. domestic producers [See Box on Page 7]. To meet these requirements, growers and processors will have to invest in water treatment for agriculture and food processing, irrigation and packing-house equipment, specialized information technology, and related goods and services.

Land and Water

A major influence driving mechanization of Chinese agricultural is the need to make the most of scarce agricultural land and water. Although China has roughly 20 percent of the world's population, it possesses only nine percent of the world's farmland and six percent of its freshwater. Freshwater per capita in 2009 was one-third the global average at the time.⁶⁹

Land and water are also located disproportionately in different parts of the country. Sixty-five percent of China's agricultural land is in northern China, which produces half the country's grain and nearly all of its wheat and corn, along with numerous other commodities. Yet, only 20 percent of China's freshwater resources are located in the north.⁷⁰

Market Access/Trade Barriers⁷¹

Despite China's accession to the World Trade Organization (WTO) in 2001, extensive barriers remain to U.S. exports in the Chinese market. The U.S. Government works to address these barriers through bilateral dialogue and engagement, active export promotion, and enforcement of U.S. and international trade laws and obligations.

As a member of the WTO, imports from the United States are assessed at China's Most-Favored-Nation (MFN) rate. The five Special Economic Zones, open cities, and foreign trade zones within cities offer preferential duty reductions or exemptions. Companies doing business in these areas should consult the relevant regulations. China may apply tariff rates significantly lower than the published MFN rate in the case of goods that the government has identified as necessary for the development of a key industry.

For customs purposes, the value of an imported product is its Cost, Insurance, and Freight (CIF) price. Customs officers use a database that lists valuations for various imports, based on foreign and domestic market prices. Normally, China Customs will accept the

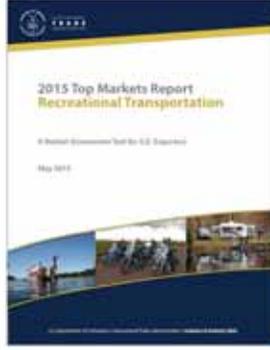
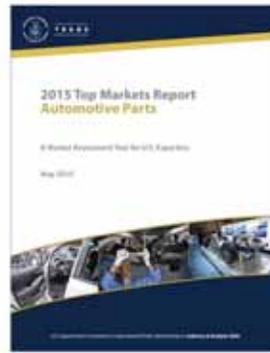
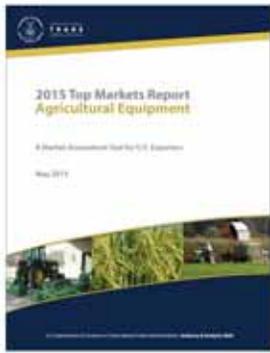
importer's price. If the reported value deviates significantly from the database however, the value of the goods may be estimated based on methods listed in the relevant Administrative Regulations.

Both foreign and domestic enterprises are required to pay value-added and business taxes. The value-added tax (VAT) is assessed on sales and imports of goods, as well as processing, repairs, and replacement services. Business taxes are levied on providers of services, transfers of intangible assets, and/or the sale of immovable property within China. VAT incorporates the value of the tariff, and is collected on imports at the border.

Inadequacies in China's protection and enforcement of intellectual property rights (IPR) continue to present serious barriers to U.S. exports. China was again placed on the Priority Watch List in the 2015 Special 301 report, and several online and physical markets were named in USTR's 2013 Out-of-Cycle Review of Notorious Markets, which identifies Internet and physical markets that exemplify key challenges in the global struggle against piracy and counterfeiting.⁷²

The protection and enforcement of trade secrets in China is also a serious problem. Thefts of trade secrets that benefit Chinese companies occur both within China and beyond its borders. The Chinese Government frequently has failed to recognize serious infringements of IPR that violate Chinese law. Entities affiliated with the Chinese Government and the Chinese military have infiltrated the computer systems of U.S. companies, stealing huge amounts of data, including intellectual property.⁷³

For more information on these and other concerns, see the "2014 National Trade Estimate Report on Foreign Trade Barriers," published by the United States Trade Representative, at <https://ustr.gov/sites/default/files/2014%20NTE%20Report%20on%20FTB.pdf>.



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