Is China Playing By the Rules? Free Trade, Fair Trade, and WTO Compliance
Wednesday, September 24, 2003
10:30 AM - 12:30 PM

Statement of
President and CEO
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Thank you for the honor and opportunity to address the Executive Commission.

The North American Export Grain Association (NAEGA), established in 1912, is comprised of private and publicly owned companies and farmer-owned cooperatives involved in and providing services to the bulk grain and oilseed exporting industry. NAEGA member companies ship practically all of the bulk grains and oilseeds exported each year from the United States. The Association's mission is to promote and sustain the development of commercial export of grain and oilseed trade from the United States. NAEGA acts to accomplish this mission from its office in Washington D.C., and in markets throughout the world. NAEGA has a joint operating and service agreement with the National Grain and Feed Association (NGFA), whose 1,000 member companies consist of all sectors of the U.S. grain, feed processing and exporting business. NGFA member companies operate approximately 5,000 facilities that handle more than two-thirds of all U.S. grains and oilseeds. NGFA and NAEGA coordinate policy and government representation on trade related issues that affect economic prospects of the industry. This enables the organizations to speak in a unified voice to government and to the industry's domestic and international customers.

Our trade relationship with the Peoples Republic of China is of great importance to the economic success of US Agriculture. Compliance with the World Trade Organization (WTO) rules is a foundation of successful economies around the world as well as critical element in a successful trade relationship with China. The North American Export Grain Association has a long history of facilitating the export of US wheat, corn and soybeans to China. We are very much engaged in resolution of concerns related to several questions to be addressed in today's hearing. In particular, I would like to focus on three questions: Which Chinese government policies have made Chinese exports competitive? Which remaining non-tariff barriers hinder market access for U.S. imports into China? and, what type of U.S. government policy changes could help in changing conditions in China?

By most measures, China's efforts to meet it's WTO commitments to reduce both tariff and non-tariff barriers in the agricultural sector have been met with mixed results. There has been welcome progress in some key areas such as tariff reductions. Unfortunately, many issues that amount to non-tariff barriers continue to limit progress under China's WTO commitments and exports to the Chinese marketplace. However, from the perspective of US agriculture and the grain trade, the impact of China trade is difficult to overstate. Likewise the implementation of China's WTO commitments continues to have a profound impact.

To put some perspective on the questions under consideration by the Committee, we should acknowledge the recent growth in agricultural exports to China. On a July through June basis, we have seen total value of US agricultural exports to China rise from less than 500 million dollars in 1999 to almost 2.25 billion in 2003. Since China was accepted into the WTO (December 2002), it is safe to say that US agriculture exports to China are on a pace to double in value.

When China imports the impact can be quite dramatic. Our soybean sales to China this year may exceed $ 2 billion. US Soybean exports to China represent not only a very large percentage of overall US soybean exports but also big piece of our overall agricultural export value and very large, market dominating share of world trade in soybeans.

When China stops imports or fails to meet expectations, the result is a large negative impact on our agricultural markets. A short 20-30 day interruption in soybean trading (due to uncertainty over biotechnology policy) last year may have resulted in up to $100 million in lost US sales. Expectations of large export markets for US corn and wheat simply have not been met. While import demand for these crops is largely dependent on domestic supply, we think it is clear that WTO non-compliant policies of the Chinese government have stimulated production, reduced access and, in the case of corn, subsidized exports. For wheat, calendar year to date exports total over one million tons - up 104 percent from 2002. Chinese wheat imports have fallen this year by 60 percent to about 200,000 tons. Chinese corn exports have recently overtaken several long term US corn export markets. This year China has exported 50 percent more corn than it did in the same period last year – a calendar year to date total of over 9 million tons. Our expectations were for Chinese membership in the WTO to result in significant imports from the United States of both corn and wheat.

As China continues to transition its economy and agricultural policies, we expect China will continue progress toward a policy more accommodating to international trade. I believe China recognizes the need to further open agricultural markets to provide for enhanced food security and economic well being. The difficulty is in the transition from a centrally planned and managed economy to an economy that benefits from allowing market forces to prevail. For agriculture, as we too have experienced, this transition can be especially difficult.

In response to these three questions: Which Chinese government policies have made Chinese exports competitive? Which remaining non-tariff barriers hinder market access for U.S. imports into China? and what type of U.S. government policy changes could help in changing conditions in China? – There are several key issues related to trade in agricultural products that need to be addressed:

- Uncertainty regarding biotech regulations and the issuance of permanent safety certificates for biotech products. Much progress has been made in this regard. Our industry is especially appreciative of the effective and timely response of President Bush and his Administration in moving this complex and difficult issue very close to resolution.
- Labeling and information requirements on meat and poultry products that increase export costs without enhancing food safety.
- Chinese adherence to the Agreement on the Application of Sanitary and Phytosanitary Measures (the SPS Agreement). Particular concerns regarding the failure to utilize the International Plant Protection Convention and “zero tolerance” pathogen standards that are neither science-based or practical, as well as undue quantitative restrictions on meat and poultry imports.
- Administrative interference with import trade by China’s quarantine authorities and Ministry of Commerce, including requiring import permits before signing purchase contracts and making shipment. Most administrative measures lack transparency and appear to be used to institute short term quotas established to address political concerns.
- Significant export subsidies for agricultural products, particularly corn.
- A range of problems with the implementation of China’s promised tariff-rate quota (TRQ) system, including a lack of transparency, delay in the announcement of quotas, granting of insignificant and uneconomic quotas, imposition of restrictions that are not required of domestic producers or merchants, and inclusion of quotas for mandatory re-export.

While China has eliminated or reduced some tariff barriers, the benefits from these actions can be quickly offset by continued non-tariff barriers that restrict trade into China, create significant marketplace uncertainty and discourage further foreign investment. The agricultural TRQ issue has the potential to be the first case against China under the WTO dispute resolution system. US industry has consistently called for science-based, permanent rules for genetically modified organism (GMO) imports, a transparent TRQ system, and an end to agricultural export subsidies.

The progress made by the governments of China and the United States through collaborative work to reduce these unjustified barriers to agricultural imports has been significant and is certainly in the best interest of both countries and the modernization of Chinese food production.

We need to aggressively focus the attention and improve China's compliance with the WTO in three areas: 1) the regulatory practices of Chinese State Administration of Quality Supervision and Inspection and Quarantine (AQSIQ); 2) the complete and final elimination of agricultural export subsidies; and 3) the implementation of agricultural TRQ systems.

AQSIQ Regulatory Practices

U.S. soybean, cotton and meat traders continue to experience significant restrictions on exports of products to China stemming from AQSIQ's posture on the issuance of Import of Animal and Plant Quarantine permits and its inspection procedures. Chinese quarantine regulations require importers to obtain import permits before entering into purchase contracts and effecting shipments. With import permits valid for only 90 days or less, buyers are locked into a very narrow period to purchase, transport and discharge their cargoes before expiration of the permit.

While the technical requirement imposed on importers is to obtain an import permit in advance of contracting for commodity shipments, the current AQSIQ requirement is essentially unworkable, as importers buy products when prices are low - sometimes months ahead of actual shipment. Contracting parties cannot wait to obtain an import permit first, before making a contract for shipment of commodities.

Although China removed soybean import quota control in 1999, the Chinese government now appears to control import volume through WTO-inconsistent methods such as the use of quarantine import permits.

In the recent past, AQSIQ has slowed the issuance of permits, which has resulted in significant commercial uncertainty and, in some cases, has placed U.S. foreign investment in the Chinese agricultural sector at risk. Because of the commercial necessity to contract for commodity shipments when prices are low, combined with the inherent delays in having import permits issued, many cargoes of soybeans end up arriving in Chinese ports without import permits. This has created delays in vessel discharge and resulted in demurrage bills for Chinese buyers.

AQSIQ has committed to notify importers about the result of their permit application within 30 days of receipt. However, some importers are waiting well beyond 30 days without obtaining any feedback from AQSIQ, as provincial CIQ offices that act as intake centers for import permit applications appear to be asked to delay submitting these applications to AQSIQ in Beijing. This effectively extends the 30-day notice period AQSIQ has to respond to the party requesting an import permit.

Most recently, AQSIQ has suggested to foreign diplomats that it will take action to restrict specific firms from exporting or importing soybeans based on allegations that the firms have failed to meet certain quarantine regulation and mandatory quality requirements. The quality requirements and quarantine regulations are undocumented, non-transparent and do not comply with the requirement of the WTO SPS Agreement or the International Plant Protection Convention.

Recommendations:

- AQSIQ should restrict its activities to science-based, WTO and international convention compliant import quarantine procedures and should not impose delays, uncertainties, commercially discriminatory or commercially unrealistic requirements that inhibit free trade.
- AQSIQ should approach the approval of import permit requests in a timely and commercially realistic manner.
- AQSIQ should ensure that all formalities are transparent, with clear timelines openly promulgated.

Agricultural Export Subsidies

U.S. feed grain producers and exporters have serious concerns about China's failure to live up to the commitment to eliminate export subsidies for corn.

We are convinced China is using export subsidies to ship major volumes of corn into markets such as South Korea, Malaysia, Indonesia and most recently Japan. After a record-setting year in 2002, exporting more than 11.6 million tons of corn, China is currently 100% above that year's pace in exporting 6.7 million metric tons in the first six months of 2003 (1.8 million metric tons in June alone). Those exports have come mostly at the expense of the U.S. corn industry. If China's use of export subsidies for corn is not addressed now, we will continue to see significant erosion of U.S. markets throughout Asia.

Prior to its WTO entry, China subsidized corn exports at $40-$45 per ton. However, throughout much of 2002 and 2003, the price for Chinese corn exports has remained at pre-accession levels. Given China's ocean freight and internal corn costs, it is inexplicable how corn could be exported at those prices without further government subsidization, even after accounting for measures outlined by the Chinese government to reduce corn export prices. By calculating the size of the gap between domestic and export prices, the findings refute explanations given by Chinese officials as to how China was able to reduce corn export prices after WTO accession by means allowable under WTO rules, i.e. VAT rebate and transportation tax waivers.

Recently, world prices have increased while China's domestic corn prices have decreased, reducing the need for export subsidies. However, we still question how China is exporting at levels of $15 to $25 per ton below domestic prices. We are also concerned that the VAT is not being collected on domestic corn, or is being assessed at a much lower rate than the officially declared 13 percent. Furthermore, with China's grain stocks currently at a very high level, there will be additional pressure for China to continue to aggressively subsidize corn exports throughout next year if allowed to do so. China has exported more than 18 million metric tons of corn at price levels significantly below domestic prices during the past year. Although China has announced measures to lower the corn price for export within WTO disciplines, it is clear that corn exports continue to be subsidized by the government.

Although the subsidy gap between China's domestic and export prices for corn has narrowed in 2003, it still accounts for a substantial competitive advantage for China as its exports remain at record high levels. Based on data provided by the U.S. Grains Council, Chinese exports to South Korea in June were priced at $106 FOB China (Dalian). Mid-June domestic corn prices at Dalian were 1060 RMB/mt or $128/mt. On a direct comparison basis, the gap between domestic and export prices would then stand at $22/mt for June. Using a six month lag from the time contracts were signed and shipments exported - so that the June export price is compared to December 2002 domestic price (1030 RMB, or $124.50) - the gap amounts to about $18.50 (about 15% of the domestic FOB Dalian price).

While export prices for the July-September period may be slightly higher than June's $106/mt, they most likely will not be more than $110/mt (current domestic Dalian prices are unchanged at $128/mt). That implies a significant gap continuing in the foreseeable future. If China continues to apply these levels of subsidies to corn exports the remainder of this year, U.S. exports will be significantly impaired in this current marketing year.

Recommendations:

- China should formally and fully account for the discrepancy in domestic and export corn prices.
- China should immediately meet its WTO commitment and proceed to eliminate the officially supported mechanisms that permit exports at lower than domestic prices.

Agricultural Tariff Rate Quotas

China has not made sufficient progress[1] in implementing tariff rate quotas (TRQs) for bulk agricultural commodities such as wheat, corn, cotton and vegetable oil in a manner that opens the market to trade as anticipated under China's WTO accession agreement. Regulations designed to establish TRQ systems were late in being released, lack sufficient transparency and introduce unreasonable licensing procedures for importers. In some cases, China has contravened its accession agreement by allowing TRQs reserved for "non-state trading companies" to be issued to state-owned enterprises.

The TRQs for corn and wheat in many cases were distributed in such small quantities as to render them uneconomic to fulfill. When TRQs were issued, it has been very difficult, if not impossible, to ascertain which companies were granted quotas. This is in violation of the WTO agreement.

Of greatest concern is that the State Development and Reform Commission (SDRC) requires a significant portion of each TRQ be used only for processing and mandatory re-export of finished products. This restriction is most important for cotton, where well over one half of the TRQ is restricted to re-exports and represents a violation of China's accession agreement.

Recommendations:

- China should honor its TRQ obligations and not engage in such practices as: delaying announcements; granting insignificant, uneconomic quotas; applying restrictions that are not required of domestic producers or merchants; or designing non-tariff trade barriers that circumvent TRQ obligations.
- China should ensure that there is greater transparency in the TRQ process, including the requirement to publish a list of importers that have been granted TRQ allocations.
- China should eliminate the quota for mandatory re-export provisions.

In summary, much has been accomplished with regard to Chinese accession to the WTO and the commitments related to agricultural trade. However Chinese commitments and U.S. expectations are for additional and more timely progress. The US and Chinese government have demonstrated an ability to resolve some outstanding issues. Given the importance of several unresolved concerns to both China, the U.S. and global markets, renewed commitment and additional effort by the U.S., China and the WTO are warranted.

Thank You

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[1] It should be noted that China's Ministry of Commerce and National Development and Reform Commission has recently published a draft regulation amending management of TRQs for imported agricultural products. The impact of the new regulation needs further review.