A discussion paper on vegetable import data and the implications for the Australian vegetable industry

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Background

Imports of vegetables grew strongly in 2011/12. However, this is not a new phenomena and it is important to dissect the economic data to get to the core of why this is occurring. This paper seeks to inform readers by drawing on the relevant economic data, challenge some widely held views and give consideration to the economic impact of the growing level of imports on the Australian vegetable industry.

Vegetables at a trade disadvantage

Four things are critical in the import debate:

- Supply.
- Price and product differentiation.
- Economic conditions.
- Trade barriers.

Supply: Global supply of vegetables is generally not a problem. Vegetable growing is land intensive requiring small hectarage. Most countries have sufficient land to support a domestic industry and in respect of fresh product distance gives the local producer an advantage. Where land is restricted or climatic conditions poor, undercover growing can be undertaken. Vegetable growing also responds quickly to natural disasters as the crop turnaround times are much shorter than the typical annual cycle for most other agricultural products. The ability of supply to rebound quickly usually ensures that any spike in price is short-term and in the long-term there is downward pressure on prices.

Price and product differentiation: Price remains the key element in selling vegetables. Premiums can be extracted for quality and other attributes but they are vulnerable to changes in economic conditions and income levels. Anything that can assist the ability of Australian growers to extract a premium should be undertaken. Promotion of fresh 'green' environmentally-friendly vegetables and the need for stricter country of origin labelling are important issues for the vegetable industry. They can provide a marketing advantage but they will not be accepted by Australia's policy makers to preclude imports.

Economic conditions: Extracting premiums is more difficult in straightened economic times. Frozen French fries from Australia, New Zealand, the USA or Belgium to most consumers look and taste the same, but more so when consumers perceive their incomes are under threat. Consumers may be willing to pay a small premium for Australian frozen vegetables or for quality and freshness variations in vegetables, but when things get tough price will be the overriding consideration.

Trade barriers: There are no tariffs on fresh vegetable imports into Australia and only very small tariffs on some processed vegetables of 5% for developed countries and 4% for developing countries except where free trade agreements exist. There are some biosecurity restraints on imports of certain vegetables where it is considered that the import poses a high risk of transmission of pests and diseases into the local industry. Under World Trade Organisation rules to which Australia is a signatory, biosecurity cannot be used as a trade barrier and arguments against market access must be based on scientific evidence showing that there is a reasonable risk that the pest or disease will be transmitted to Australian producers. AUSVEG's campaign against the import of fresh potatoes from New Zealand is soundly based because it questions the science employed by Biosecurity Australia. Australia has a poor reputation in world forums and is often accused of using biosecurity as a trade barrier, with the most notable example being the banning of New Zealand apples because of fire blight. On the other hand many Australian producers believe that Australia has been naive in trade and biosecurity negotiations, pointing to Australia's relative open borders and difficulty in accessing many foreign markets.

The Australian vegetable industry is vulnerable to all four of these factors. Supply is plentiful, low prices are the driver of demand, there is limited scope for product differentiation and trade barriers are unfavourable. All of these factors increase the pressure from imports and impact on the rates of return for growers.

Be careful of scapegoats

At times of crisis people seek simple explanations for the crisis. With the present concern about the level of imports there are two plausible scapegoats.

1. **The currency**

This is an easy scapegoat to blame for the level of imports. The high value of the Australian dollar improves the price competitiveness of imports against local produce. Industries across the economy are complaining that the dollar is the reason for them being uncompetitive.

The expectation is that the dollar will fall from its lofty highs but there are few pundits expecting it to fall back to the levels of three years ago. The Australian dollar has always been seen as aligned to commodity prices. Commodity prices have fallen but so far with little impact on the value of the currency. The failure of the currency to fall has now led to the argument that the Australian dollar remains high because of the attractiveness of Australia as an investment destination because of superior economic performance and the higher interest rates on offer here. A reduction in interest rates will see a fall in the dollar.

Three points need to be made about the impact of the high dollar.

1. The currency factor is difficult to assess due to lags in response to currency changes.
2. There is a danger that fundamental structural shifts are occurring in the economy unrelated to the currency which if ignored can seriously damage industry. Currency is one factor in influencing trade decisions but only one. In looking at the issue of vegetable imports it is necessary to consider the whole gamut of possible causes for the rise in vegetable imports.

3. While the Australian dollar has appreciated against the US dollar, the Chinese yuan, the US dollar and the Euro, the currency has barely moved against countries such as New Zealand and Canada.

The currency and vegetable trade

It takes a while to build sound trade relationships. Imports can be opportunistic, especially if there is a shortfall in domestic supply due to say adverse climatic conditions. In the case of fresh vegetables the window of opportunity is narrow due to the short growing cycle of most vegetables. For processed vegetables the timeframe is longer. The decision to import is influenced by a number of considerations.

Firstly, currency considerations. Is the movement in the currency of a short or long-term nature? If short-term and the currency is expected to pull back, the importer may have burnt domestic bridges with an impact on profitability.

Secondly, there are the supply issues associated with imports. Can the overseas supplier guarantee timely delivery on a consistent basis? Is the agreement to supply based on short-term considerations in their own markets e.g. oversupply?

Thirdly, price competitiveness independent of currency movements remains critical. Much of the justification for moving vegetable processing offshore or sourcing vegetables from overseas is that production in Australia costs too much and is non-competitive.

Fourthly, consideration must be given to the ability to supply the required volumes that will ensure consistency of supply to retailers and food service clients is important. This can be impacted strongly by climatic conditions.

Lastly, relationships between Australian-based businesses and overseas vegetable exporters are also in the mix, as is the fact that the vegetable food processing sector in Australia is mostly foreign-owned, with factories located in several countries.

In an earlier research paper released in February 2012 on the impact of currency movements on imports of vegetables into Australia (see AUSVEG website) the conclusion was reached that 'changes in the value of the Australian dollar have some impact after a time lag on the level of vegetable imports. However, drilling down to individual vegetable products suggests that while currency movements can impact on decisions to source vegetables from overseas, they appear to be one of the factors in a business pot pourri. The importance of the currency movement relative to other factors varies enormously depending on the vegetable in question and the source country of the import.'

Economics suggests that the decision to import rather than source product locally will be influenced by currency fluctuations due to the price impacts in the domestic currency. However, the vegetable industry would do itself a disservice if it sought to attribute the rising tide of vegetable imports to the appreciation of the Australian dollar alone.

2. China

The argument can be made that Chinese products are so cheap that Australia will never be able to compete.

Australians are confronted everyday with a range of goods with the ‘made in China’ label. The Chinese have achieved high rates of economic growth with a policy of exporting cheap products around the world. This strategy was based on the availability of plentiful and cheap labour in China. Excess labour in rural areas was fed into the cities. The government allocated investment sources to build industrial plants. As economic development progressed, China expanded its production into more sophisticated goods.

But the days of cheap and plentiful labour are over. Some commentators believe that sometime last year, due to some extent to the success of the one child policy, China moved to a position of labour shortages. Wages are rising. Chinese parents place a huge emphasis on education as an avenue for social advancement and many young Chinese are looking for white collar rather than factory jobs. In addition, the Chinese leadership is concerned about the widening gap between the standard of living in rural and urban China and have set out to raise wages and living standards in rural China. Preventing political unrest in rural China is a key plank of economic policy. And remember, unlike Russia, China’s communist revolution came out of rural areas. These policies have implications for vegetable trade.

To-date there appears to be no reason to single out China as the scapegoat for rising levels of vegetable imports. China is Australia’s second major source of vegetable imports but this has been the case for all of this century. It is a player but so are developed countries such as New Zealand, the USA, Italy, the Netherlands and Belgium. A host of other new competitors are lining up to make a splash in the rather limited market in tradeable vegetable products. Fears of a deluge of cheap Chinese product may be misplaced. As wages and living standards rise in rural China, China’s competitive advantage in the availability of cheap and competitive labour will be undermined.

Import penetration – the evidence from the data

The value of vegetable imports has been on a rising trend since data became available to the industry in 1995. The Australian dollar was floated on December 12, 1993, so throughout this period the currency has freely floated i.e. the Australian dollar’s value has been determined by the market. Rising imports over this period would not be considered abnormal. World trade has expanded, freight and technology have developed and globalisation of production has become an increasing feature of the world economy. The table below shows the total value of vegetable imports from 1995/96.

Key points to note about the table are:

- The fall in imports in 2009/10.
- The strong rise in imports both absolute and in percentage growth for the years 2006/07, 2007/08 and 2008/09, a rise in absolute terms of $263 million.

- Resumption of strong growth in absolute terms in the last two years up $141 million.
- The Australian dollar has been strong against most major vegetable importing countries over the period 2006/07 to 2011/12. The exception was 2008/09 when at the height of the global financial crisis the currency sank below $0.60 against the US dollar.

Year	Total Imports AUD $M	Yearly % Growth
1995/96	227	
1996/97	208	-8.4
1997/98	226	8.7
1998/99	250	10.6
1999/20	258	3.2
2000/01	281	8.9
2001/02	281	0
2002/03	320	13.9
2003/04	339	5.9
2004/05	351	3.5
2005/06	374	6.6
2006/07	430	15.0
2007/08	550	28.0
2008/09	637	15.8
2009/10	556	-12.7
2010/11	609	9.5
2011/12	688	11.5

Apart from 2009/10 the aggregate figures show an alarming increase in imports in recent years. There are two points to note in this regard. Firstly, the value of imports expressed in Australian dollars will be impacted by the value of the currency. The Australian dollar has traditionally been a volatile currency with the currency in most years swinging in a wide range to the US dollar The Australian dollar against the US dollar has traded on a monthly basis between $0.96 and $1.09 over the last two years. Secondly, the value of Australian imports is set at custom valuation. For all intents and purposes this is the cost of goods free on board (FOB) so it excludes costs such as insurance and freight (CIF) involved in getting the goods from the source country to Australia. When looking at unit values an allowance has to be made for this fact.

Aggregate numbers can indicate a problem but in order to provide some meaningful comment we need to breakdown the data. The vegetable industry divides the import data between fresh, frozen, processed and other (vegetable seeds, tuber vegetables, dried and provisionally preserved vegetables). This paper will examine the import data on fresh, frozen and processed vegetables.

The evidence to-date on fresh imports

The tables in the attached sheet show the level of fresh imports both by value and quantity over the last three years where values exceeded $1 million last financial year. The value of fresh imports at its peak in 2010/11 only represented 2.3% of the total value of Australian vegetable production.

Last financial year there were ten countries whose value of fresh imports was over AUD $1 million. In order, they were ***China, New Zealand, the USA, Mexico, Peru, South Korea, Spain, Argentina, Thailand and the Netherlands.*** Fresh vegetables imported with values over AUD $1 million were (in order) ***garlic, asparagus, onions, capsicums, tomatoes, peas and mushrooms***.

The major import is ***garlic,*** sourced from a number of countries, with China accounting for 75% of supply by volume and 53% by value in 2011/12. The value of garlic imports fell substantially last financial year due to substantial falls in the price of garlic from most source countries. The imported price of garlic from China more than halved from an average of $2.63 per kg to $1.18 per kg. Volumes of garlic imports continue to increase.

Asparagus imports are mainly from Peru, Mexico and the USA. Australian asparagus is principally grown at Koo Wee Rup in Victoria and harvested in the December quarter. Peru, a southern hemisphere competitor, can supply asparagus all year round. Imports are minimal in the Australian season. The growth in asparagus imports appears more a reflection of counter seasonal buying to satisfy consumers (who can afford it) with constant product.

Onion imports have increased over the last three years as they have become cheaper. They are principally sourced from the USA although Chinese imports are increasing. This may reflect the increasing competitiveness of imports from China. Imports from the USA are generally cheaper but in 2011/12 the price of onion imports from China averaged $0.66 per kg compared to USA at $0.79 per kg. Onion imports are also largely counter seasonal trade.

Capsicums and tomato imports are mainly from New Zealand. Imports rose in 2010/11 due to the floods in Queensland and Victoria but fell back down last year. ***Pea*** imports are from China and prices have remained around the $3.00 per kg range for the last three years.

Mushrooms are from South Korea. South Korea gained biosecurity clearance for greenhouse capsicum imports into Australia last year. Imports have increased this year, albeit off a small base.

In short, the data suggests that except for the case of garlic, where it appears that Australian production is non-competitive (imports of around 11,000 tonnes versus estimated domestic production of 800 tonnes), much of the trade in fresh vegetables is counter seasonal or niche marketing. As such, the impact of imports on Australian vegetable growers supplying the fresh market has not been significant, though the same may not be said for processed vegetables. Whether they have an impact on growers' margins is a different question as the threat of imports may have suppressed the prices received.

The future threat of fresh imports on growers

Vegetable growers in Australia enjoy some degree of natural protection from fresh imports. While fresh vegetable imports are free of import licensing, quota and tariff restrictions, some vegetables face biosecurity barriers in gaining access to Australian markets. It is important that the vegetable industry fights tooth and nail to retain existing biosecurity measures.

In the future, improvements in chilling processes and transport logistics could improve the competitiveness of fresh vegetable imports. Imports are more likely to pose a threat for root crops rather than aboveground crops.

Innovation and reducing costs of production per unit produced is imperative. Costs of domestic production can be higher than for the imported product given the costs of getting the import from the source country to Australian markets. But if the gap becomes too wide then imports are likely to enter if they have biosecurity clearance.

Larger farms, increased mechanisation of harvesting, improvement in labour force skills, increased on-farm efficiencies in the use of inputs including precision agriculture, lowering the percentage of wasted product and gaining some economic return from it, and improvement in transport logistics, are all factors which can assist in improving the competitiveness of Australian product against the import threat.

Frozen and processed vegetables

The evidence to-date

This is where the deluge of imports is most apparent and this is not surprising. Issues of freshness are not an issue. To the consumer a pack of frozen peas from New Zealand looks little different from the Australian product. Canned vegetables from Italy or pickled cucumbers from India look little different to the Australian product, particularly if the packaging looks 'familiar.' In short, most of these vegetable products are seen as commodities with very little market differentiation. In these markets price is the critical factor. Unless the product can differentiate itself then the consumer will be attracted to the cheapest price. This is why the issue of clarification of country of origin labelling laws and the prominent display of country of origin labels as occurs in supermarkets for fresh produce is such an important issue for the Australian vegetable industry. It doesn't guarantee that Australians will buy the local product but it does create a point of differentiation.

Frozen imports

The vegetable industry groups all frozen products together so this category includes processed frozen vegetables. Frozen vegetable imports surged strongly in 2011/12 (up $78.5 million to $275 million) representing a staggering increase of 40% on 2010/11. Frozen vegetable imports exceeded processed vegetable imports for the first time ever in 2011/12. The attached tables provide details of countries and product by value and quantity for the last three years where imports exceeded $1 million in 2011/12.

New Zealand has traditionally been the major supplier of frozen product with a market share of around 50% and China the second major supplier. Imports from ***New Zealand*** rose $30 million and volumes were up 23,000 tonnes in 2011/12. The increases were even more staggering from the ***USA, the Netherlands and Belgium. China*** was the only major supplier of frozen products where imports fell, pushing China down to fourth place as a supplier nation.

South Africa has emerged as a new and threatening supplier. Two years ago it supplied only $4,000 worth of frozen imports. In 2011/12 it supplied over $4 million, up 252% on 2010/11. Quantity increases were even greater. Outside the major suppliers, ***Vietnam, France and Egypt*** were emergent new players with imports of over $650,000.

All categories of frozen imports rose in both value and quantity in 2011/12.

The major frozen import is ***prepared potatoes*** (fries, wedges and the like) which surged strongly in 2011/12. Frozen prepared potatoes accounted for $51.5 million of the total rise of $78.5 million. Almost all imports of frozen prepared potatoes were from New Zealand, the USA, Netherlands, Belgium, Canada and the new player on the block, South Africa. Imports surged from all these countries except Canada, with imports from USA more than doubling to over $30 million. Canadian imports came in at a higher price averaged out over 2011/12 at $1.42 per kg. The Benelux countries were cheapest with Netherlands at $0.79 per kg and Belgium at $0.86 per kg. New Zealand potatoes were $0.92 per kg and USA $0.93 per kg. New Zealand potatoes would have an advantage over other competitors because of lower cost, insurance and freight costs.

Imports of levy paying vegetables also surged strongly in 2011/12.

Vegetable mixtures, the largest import category, rose 15.5% to $41.5 million with strong increases from New Zealand, Belgium and the UK. Imports from the traditional source of China fell.

Peas rose 23% to $30 million with all the increase coming from New Zealand and the USA. The latter landed $3.5 million worth of pea imports compared to zero the previous year. Imports of peas from China fell.

Corn rose 24% to $15 million with most of the increase coming out of USA, although imports from New Zealand and China also increased.

Bean imports rose a staggering 70% to $14 million with imports from New Zealand almost doubling to over $10 million. USA re-entered the market after a two year absence and imports from Belgium were up sharply, while imports from China fell.

Imports of ***spinach*** rose 28% to $6.5 million with imports from Netherlands and Belgium up sharply with a more moderate increase from China.

Other vegetable imports rose 15% to $23 million with increases from China, the major supplier, as well as New Zealand, the Netherlands, Turkey, India, Belgium and Egypt.

Processed Imports

This is the category where imports have historically been the highest. Last financial year processed imports, which exclude frozen prepared vegetables totalled $244 million, less than the dollar level of frozen product. Canned vegetables are included in this category. The attached table records countries and product by value and quantity where imports totalled more than $1 million in 2011/12.

Italy was by far the largest supplier, with just over a third of the market, mostly related to tomato products. Four other countries, ***China, the USA, Thailand and Turkey,*** supplied over $10 million worth of imports. These five countries supplied 69% of the total value. Another 19 countries supplied imports totalling over $1 million.

The notable feature of processed imports as opposed to fresh and frozen imports is a much larger number of supplier countries. In 2011/12 processed vegetables were sourced from 78 countries. Some of these, such as Syria, Iran, Jordan, Mongolia and El Salvador, may surprise. While the supplies out of El Salvador are miniscule, imports from Iran and Mongolia exceeded $500,000.

The value of imports in 2011/12 was up 10% on the previous year. Import growth of this proportion or greater came from most of the top supplier countries. Particularly strong growth came out of the ***USA, Portugal and France***. In many cases the volume increases were even more spectacular.

Tomato based products dominate processed imports. Canned tomatoes, tomato paste and tomato sauce totalled $115 million or 47% of the total. ***Prepared potato*** products have grown strongly over the last three years, particularly from the USA. Most ***canned*** imports such as ***beans, peas, corn, mushrooms, asparagus and cucumbers*** have shown little growth. This may reflect shifting consumer tastes away from canned vegetables rather than an easing of import pressure.

Vegetables other than those mentioned above and packaged ***vegetable mixes,*** however, were up over 12% in 2011/12 and totalled $43 million. Quantity was up even sharper by 19%, with the gap reflecting lower landed Australian dollar prices.

The economic ramifications of the import data on frozen and processed vegetables

The processing side of the Australian vegetable industry is in trouble. As evidenced by the surge in imports in 2011/12, at present exchange rates it appears that much of the industry is struggling to compete with imported product. Frozen vegetable imports are of particular concern, as are canning operations.

Vegetable processing is now a global business and processed and frozen vegetable products can easily be shipped around the world from cheap producer countries with the freight cost the only constraint. Vegetable processing is being rationalised worldwide with large multinational firms building large factory capacities in selected countries.

Large sections of the Australian processing vegetable industry have closed down. If the recent surge in imports continues then the limited capacity left in Australia is under threat. Many of the existing processing plants lack the scale and technology to compete with overseas factories. Closures have and will continue to occur when capital is fully drawn down and new investment is required to upgrade existing facilities.

There are some advantages in retaining local factories even for the multinational countries that operate in the processing side of the vegetable industry. But if costs get too out of wack with the imported product they are not likely to remain. For vegetable growers this means a continuing squeeze on margins as processors try to reduce the cost of producing local product.

In short, vegetable growers face the prospect of loss of markets for processed product or a continual downward squeeze on profits unless they are able to substantially reduce unit costs.

Conclusion

The alarming surge in imports of vegetable products in recent years should be sending alarm bells ringing across the industry. While the high exchange rate and cheap Chinese product are part of the problem, the data suggests that other factors are contributing to a growing non-competitiveness of the industry. There is little that the industry can do about the exchange rate and in respect to cheap Chinese product the only weapon is to maintain existing biosecurity restrictions and marketing campaigns around fresh, green, healthier Australian products.

The data suggests that providing costs are kept in check, the industry can hold the fort against most fresh vegetable imports. The position is much more problematic in frozen and processed vegetables. Vegetable growers require a commitment by vegetable processors for investment in large-scale plants using updated technology and low costs of production that enables them to compete with similar plants being established overseas. On present indications this is unlikely to be forthcoming. Retailers may be able to exert some influence to maintain what is left of the vegetable processing industry. They require consistency of supply to consumers and may seek to achieve a marketing advantage by promoting Australian products. But apart from this a radical rethink about production techniques and industry structure is necessary if Australia is to have an economically viable vegetable processing sector.