



WHY WE SHOULD BE OPTIMISTIC ABOUT THE FUTURE OF AUSTRALIAN AGRICULTURE EXPORTS TO ASIA

“Asia will more than double its total spend on food over the next decade”¹

INTRODUCTION

Asia is Australia’s most important agricultural export partner, representing approximately 76% of total exports.² The recent uptick in geopolitical tensions between China and Australia has raised concerns that Australia’s current level of agricultural exports to Asia may not be sustainable. While China is an important market for Australian agriculture, we expect there is more than a reasonable chance that Asian exports ex-China outpace China growth over the next decade.

Asia ex-China now accounts for 17% of world GDP, a regional economy larger than the economies of the China and the Euro zone.³ Key non-Chinese Asian economies have risen rapidly in recent years, particularly India, Indonesia, Vietnam and the Philippines.⁴ Not surprisingly, merchandise trade in the Asian region has grown faster than the US and Europe over the last 20 years.⁵ As Australia reflects on its relationship with its largest trading partner, what does the future look like in Asia ex-China?

The objective of this paper is to briefly document the history of Australian agriculture exports and offer insights into the potential opportunities in Asia excluding China.

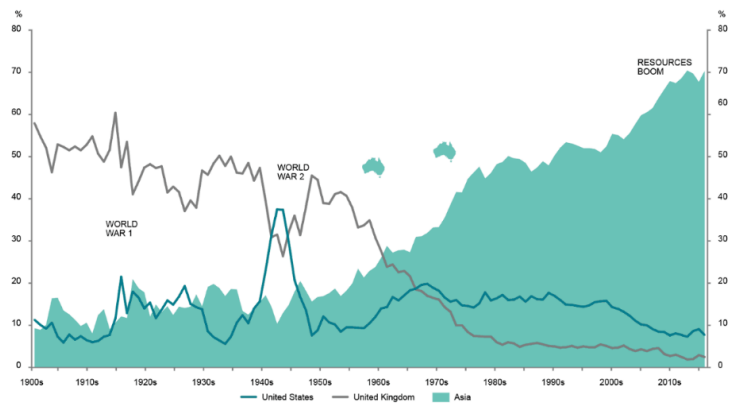
AUSTRALIA’S AGRICULTURAL TRADE

In the 230 years that has followed European settlement agriculture has played an important role in the development of Australia. The sector has relied on export markets since the first recorded wool exports to the United Kingdom in 1807.⁶ The United Kingdom (as a trade partner) and agricultural goods (particularly wool and to a lesser extent wheat) dominated Australian merchandise trade from 1900-1970’s. Its only over the last 40 - 50 years that Asia has become an increasingly important trading partner,⁷ and the last 10 years that China has become the leading agricultural export market for Australia.⁸

Australia is now considered amongst the 15 largest agricultural exporters in the world, exporting approximately 70% of all agricultural goods produced to 192 countries. 12 out of Australia’s 15 largest export markets are located in Asia.⁹

The growth in agricultural trade to Asia has been supported by multiple factors; Free Trade Agreements reached with key Asian countries including Indonesia, Japan, China, Korea, Malaysia, Singapore, Thailand, Hong Kong; population and income growth; higher urbanization and fundamental constraints on both land and water.

CHART 1: Australia's two-way goods trade to Asia, the UK and the US per cent share of total¹⁰

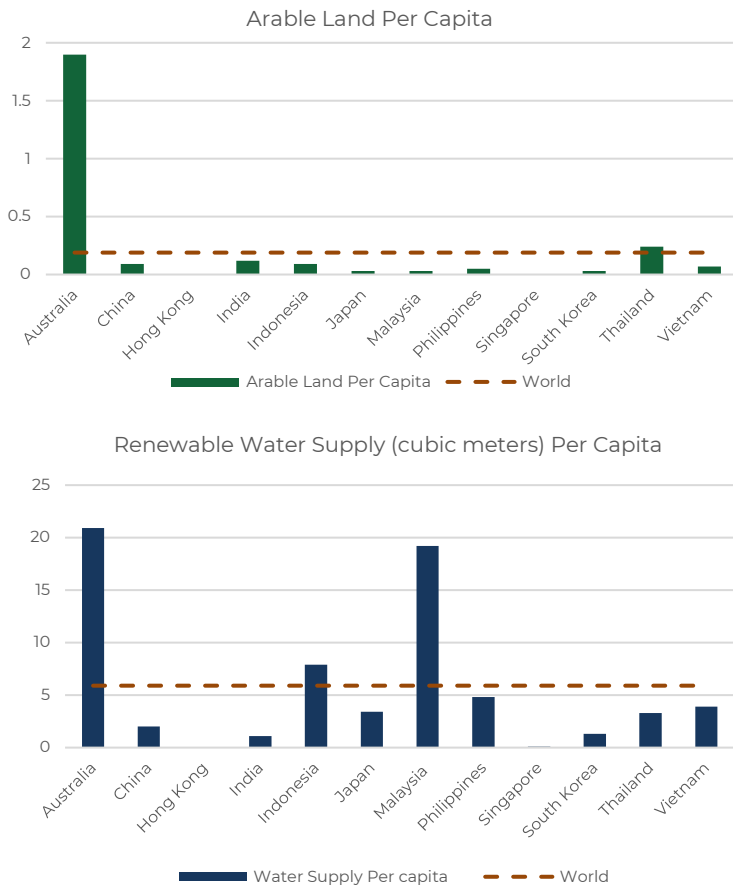


RESOURCE CONSTRAINTS INCREASINGLY FAVOR AUSTRALIA

Asia’s ability to lift agricultural production is limited by both land and water constraints. Population growth and increased wealth per capita have stretched critical resources. Australia’s key Asian agricultural export partners have either arable land per capita or renewable water supply per capita levels below the world average.¹¹ Climate change is expected to exacerbate production challenges for Asian countries. Admittedly, these statistics mask in-country geographical variations but regardless they clearly illustrate Australian agriculture’s comparative advantage and the trade opportunity in the Asian region. In our view, if population and GDP growth is maintained, resource constraints will increasingly shape the future of agriculture trade across Asia and favour Australia.

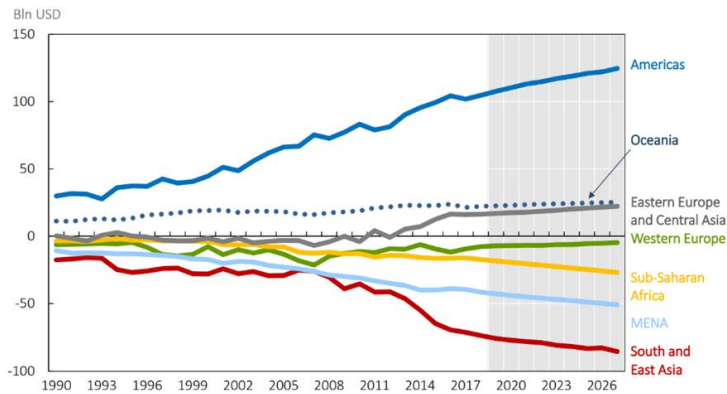


CHARTS 2 and 3: Arable Land¹² and Renewable Water¹³ Supply Per Capita



In a 2015 report, the Grains Research and Development Corporation noted that Asia's potential to lift agriculture production is limited by land and water constraints.¹⁴ The OECD projects regions with abundant resources (including Oceania) will export more agricultural goods to regions with scarce land and water resources and high population pressure, particularly south and east Asia.¹⁵ The Deputy Director General of the WTO, expressed a similar view to the OECD; "international trade in food is trade in land, trade in water and trade in energy" and "using current data on population, food and water consumption in each nation, the Potsdam Institute concludes that countries will find themselves obligated to increase their dependence on each other to feed their people".¹⁶

CHART 4: Agricultural trade balances by region, in constant value, 1990-2027¹⁷



STRUCTURAL TAILWINDS POINT TO HIGHER FOOD CONSUMPTION IN ASIA

The 2020 Agricultural Outlook noted "population is the key determinant of total food use. Income, relative prices, other demographic factors, consumer preferences and lifestyles, meanwhile, determine a person's desired food basket".¹⁸ A 2015 European Commission report into world food consumption patterns reached a similar conclusion, implying the combined forces of population growth and income growth determine total food consumption.¹⁹

Asia's population and economic prospects will have a significant influence on global demand for food. Asia's upward trajectory is apparent in multiple indicators; its GDP is expected to overtake the GDP of the rest of the world in 2020,²⁰ it is expected to contribute 60% of global growth by 2030,²¹ Asia's population is expected to be 250 million larger and represent almost half of the global population by 2030,²² and Asia's share of the global middle class is expected to reach 54% in 2040 up from 23% in 2000.²³ COVID-19 has done little to change Asia's trajectory, the IMF expects emerging and developing Asia to outperform world GDP growth in 2020 and for the foreseeable future.²⁴

GROWTH FROM ASIAN COUNTRIES (EX-CHINA) IS PROJECTED TO ACCELERATE

China is undoubtedly a critical component of the Asian economy. It has also played a major role in growing Australia's Asian exports, particularly since its accession to the WTO in 2001. While the outlook is somewhat complicated by the impact of COVID-19, data suggests that the Asian region, excluding consideration for China, is home to some of the fastest growing populations and economies in the world. Countries such as India, Indonesia, Thailand, Malaysia and the Philippines are expected to lead a group of developing nations that together are projected to account for 35% of global consumption by 2030.²⁵ By 2050 Indonesia alone is projected to have per capita consumption of select agricultural commodities above that of China.²⁶ As importantly, while these countries are existing trade partners of Australia and the majority are signatories to the Regional Comprehensive Economic Partnership, analysis suggests the majority have per capita consumption of Australian agriculture goods well below what may be considered saturated levels.

CHART 5: Population and GDP growth of select Asian markets²⁷



The Potential Impact of China Trade Tensions on Australian Agriculture

China is the world's leading producer and consumer of a range of agricultural commodities.²⁸ China joined the World Trade Organization in 2001 and has since increased agricultural imports from not only Australia but also prominent agricultural exporters including the US, Brazil, Canada and New Zealand.²⁹ In 2011 China became Australia's largest agricultural trading partner accounting for 18% of Australia's agriculture, forestry and fisheries exports. By 2019 China's share of exports had increased to 32% of the total.³⁰

Australia's relationship with China has been well documented and is undoubtedly, for agriculture sector participants, important to monitor. However, Australia is not alone. Over the last 24 months China's relationship with a number of western countries (United States, Canada, European Union and United Kingdom) has deteriorated. Unsurprisingly, China's favorability rating in the US, Canada, UK and Australia dropped meaningfully in the 2 years to 2019.³¹

China faces significant natural resource constraints in expanding agriculture production to meet demand. Absent imports, China faces the challenge of supplying food for its people (which represent ~20% of the world's population) with only 7% of the world's cropland and 6% available fresh water.³² It should be no surprise that China is a net importer of select agricultural goods, and is forecast to remain such for some time yet.³³

Arguably the question is not if China imports food but rather where they import it from. We should expect, based on historical precedence, that the origins of Chinese imports will change over time. The Wall Street Journal stated in mid 2020 that "during its trade war with the US, China raised tariffs on lobster from Maine, while simultaneously cutting tariffs on lobster from Canada".³⁴ In August 2020, the ABC reported "China began importing huge imports of Argentine barley, for beer and livestock feed, after recently slapping an 80 percent tariff on Australia".³⁵ A similar trend is apparent in Australian almond exports to China and India (Australia's two largest export markets in 2020) following the commencement of the US China trade war in July 2018. Between 2017 and 2020 exports to China increased from 0.5% of total Australian exports (tonnes) to 52% and Indian exports fell from 25% to 11% of total exports.³⁶

The opposite is true for US almond exports (although the percentage change was smaller in both owing to higher production – the US accounts for 80%+ of all almond exports).³⁷ It is important to point out that the interchangeability (between exporting countries) is not necessarily as straightforward as reports suggest but regardless the point is unchanged, there are nations other than Australia that China can source agricultural goods from and other export markets that Australia can sell goods too.

The potential impact of a sustained trade dispute between China and Australia varies by commodity. For example, ~75% of total Australian wool exports were sent to China in 2018/19 whereas approximately only 13-14% of total orange/mandarin production was exported to China in the same year.³⁸ The breadth of alternative markets also varies between wool and citrus – Australia exported mandarins to 35 different markets in 2018 and oranges to 40 markets, this is hardly the case for wool.³⁹ Anecdotal evidence suggests that some Australian exporters are actively building alternative export markets, stepping back from a sustained strategy over the last decade to expand exports to China.

China is undoubtedly an important market for Australian agriculture but not the only market. Likewise, Australia has been a reliable supplier, but not the only supplier, of essential agricultural goods to China. As importantly, Australia is a critical supplier of natural resources (particularly iron ore) that is crucial to powering the Chinese economy and that would be challenging for China to replace.⁴⁰ From our perspective, the current situation seems to be an uneasy balancing act for both countries but one in which China holds an advantage.

Engaging in comprehensive dialogue between government representatives of Australia and China seems a reasonably logical next step. That said, the dispute may not resolve quickly. The challenge for commercial enterprises in Australia is maintaining private trade relationships while further developing alternative Asian export markets.

CONCLUSION

Despite trade tensions increasing globally, longer term the prospects for Australian food and fibre demand remain strong, particularly in the Asian region underpinned by population and economic growth that is expected to result in a doubling of food expenditure through 2030.⁴¹ Agriculture trade in the future will not only be shaped by demographics, geopolitics and trade policy but increasingly land and water resource distribution. There is no guarantee that Australia will successfully capitalise on the opportunities Asia presents. That said, the sector is well positioned as a strongly competitive producer of agricultural goods located within close proximity to evolving Asian markets and with access to a meaningful resource base.⁴²

Riparian invests across the agricultural value chain in real asset backed investments critical to producing essential goods including water entitlements, farmland, agricultural infrastructure and agribusinesses. Given our appreciation of history and the precedents over the medium term, the development of recent trade tensions with China is not surprising. We recognize that Australian agriculture participates in a competitive global marketplace, that it takes time to develop export markets and that a sustained trade dispute with a major trading partner, should it eventuate, will have a variable impact across Australian agricultural commodities. It follows, that participants who hold well designed diversified portfolios of agricultural or water assets are more likely than not to be well placed over the longer-term.

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Riparian Capital Partners, a specialist water, agriculture and food investment firm, focuses solely on identifying, acquiring and managing investments across the agricultural sector. Through its investment strategies, Riparian provides investors with exposure to a diverse range of Australian agriculture sector assets. Riparian's investment strategies have been designed to provide investors uncorrelated returns to traditional markets, a mix of yield and capital growth and deliver liquidity options seldom offered on private market real asset investment products.

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