

10: On the Promise and Reality of New Zealand-China Trade

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Over the past half century New Zealand's trade policy has focused on evolving away from a traditional reliance on Britain and Europe as the main markets for its primary export activities. The goal has been to secure more wealthy markets to sell high value goods to, and establish a competitive place in the global market. In recent decades the focus to that end has particularly been on the fast developing Asian markets, so the establishment of the New Zealand-China Free Trade Agreement in 2008 was seen as an important step in achieving diversification and development goals. It must be asked, however, how much this relationship has contributed to trading progress and real economic development spinoffs for New Zealand, and the current review of the free trade agreement has raised important questions in that respect. This paper presents an overview of key elements of New Zealand's export trade to China since 2008 as a context for the review of this trade agreement.

New Zealand exports to China

Statistics show that the New Zealand-China FTA provided the catalyst for substantial growth in bilateral trade between those two countries since 2008. China has certainly become an increasingly important market for New Zealand products, growing from being New Zealand's fourth largest export market in 2007 to its largest by 2013. In 2016, exports to China were worth \$9.4 billion, comprising 19 per cent of New Zealand's total outgoing commodity trade. The increase in value of exports to China from 2008 to 2016 of \$7 billion was more than the total growth of New Zealand's exports worldwide, of \$5 billion.⁸¹

The substantial growth in export trade to China has clearly been driven by primary industry. In 2016, 70 per cent of New Zealand's export products to China were from the top five commodity areas of dairy, forestry, meat, fish and wool. The increase in value of these export areas and their importance to New Zealand's overall exports to China is illustrated in the table below.

⁸¹ Unless otherwise stated, statistics are sourced and calculated from Statistics New Zealand (n.d.). *Infoshare*. Retrieved from <http://www.stats.govt.nz/infoshare/TradeVariables.aspx?DataType=TEX>

Table 2: New Zealand exports to China (2007-2016)

| Total all exports | | Main exports to China by value (NZD\$) 2007-2016 | | | | | Total 5 main areas |
|-------------------|---------------|--|----------------|---------------|----------------------|---------------|--------------------|
| | | Wool | Fish & seafood | Meat | Wood & wood products | Dairy | |
| 2007 | 1,934,301,424 | 174,038,971 | 92,612,750 | 70,390,511 | 234,635,603 | 390,962,964 | 962,640,799 |
| 2008 | 2,516,154,892 | 190,117,187 | 127,392,398 | 95,996,170 | 347,010,689 | 521,298,473 | 1,281,814,917 |
| 2009 | 3,613,047,492 | 239,619,350 | 136,393,949 | 140,522,200 | 703,059,602 | 977,760,678 | 2,197,355,779 |
| 2010 | 4,809,399,673 | 292,256,090 | 160,251,508 | 135,567,575 | 991,697,311 | 1,825,969,087 | 3,405,741,571 |
| 2011 | 5,863,790,222 | 396,268,660 | 279,710,636 | 215,264,235 | 1,178,940,111 | 2,172,186,149 | 4,242,369,791 |
| 2012 | 6,840,528,216 | 388,354,066 | 335,227,952 | 411,719,261 | 1,240,107,927 | 2,567,565,707 | 4,942,974,913 |
| 2013 | 9,943,827,105 | 395,142,481 | 394,035,962 | 880,939,042 | 1,898,909,440 | 4,590,792,367 | 8,159,819,292 |
| 2014 | 9,934,550,729 | 412,239,572 | 423,489,062 | 1,057,920,368 | 1,729,710,220 | 4,325,575,950 | 7,948,935,172 |
| 2015 | 8,572,576,323 | 459,252,629 | 484,928,269 | 1,210,992,095 | 1,550,521,068 | 2,466,613,283 | 6,172,307,344 |
| 2016 | 9,407,147,443 | 316,861,628 | 560,146,814 | 1,011,401,793 | 1,969,262,411 | 2,733,096,313 | 6,590,768,959 |

Source: Compiled from Statistics New Zealand, Infoshare: <http://www.stats.govt.nz/infoshare/>

These five main commodity areas contributed approximately \$5.6 billion, or 75 per cent, of overall growth in exports to China from 2007 to 2016. Dairy experienced the greatest increase and is the obvious mainstay of the trade relationship. Dairy comprises a substantial proportion of exports to China (29% in 2016), followed by forestry products (20.93%), meat exports (10.75%), fish and seafood exports (5.95%) and wool products (3.37%).

Of even more significance is the reliance of these main commodity exports on China. In dairy, for example, China has clearly become more important as a market for New Zealand's exports since 2008, and accounts for almost all of the \$2.2 billion of New Zealand's total dairy export growth in that period. Exports of dairy products to China grew swiftly from 2008, peaking at \$4.6 billion in 2013 when they comprised one third of total dairy exports. Since then despite some decline in both total export values and the proportion going to China, that market remains very important, buying 24 per cent of New Zealand's total dairy product exports in 2016. China is also by far the largest single market for dairy, in 2016 taking more than four times the value of the next largest market Algeria, and more than five times that of the next two largest markets USA and Australia.⁸²

New Zealand dairy export activity has accordingly become intrinsically linked with China. Overall increases and declines in New Zealand's dairy exporting from year to year have tended to reflect what has happened with the Chinese market. A similar story can be told of wood products, of which the growth to China contributed 83 per cent of total increases in those exports from 2008 to 2016. Growth in exports to China,

⁸² International Trade Centre. (n.d.). Trade map - List of importing markets for a product exported by New Zealand. Retrieved from http://www.trademap.org/Country_SelProductCountry_TS.aspx?nvpm=1|554|||04|||2|1|1|2|2|1|2|1|1

in fact, comprised more than New Zealand's total worldwide export growth in wool, fish and seafood and meat products in that period as well.

While China is obviously an important source for increasing New Zealand's export revenue, the reality is that the greatest proportion of the products sold there tend to have lower 'value added'; the extent of manufacturing to increase the value of a raw product in the production process, thereby increasing returns on capital.⁸³ Within dairy exports, remaining limits on trade have caused products to be of lower value. Whole milk powder, for example, faces the lowest limits on trade, and comprised just over half of New Zealand's exports to China. In 2016, the return for this product equated to an average of \$3.55/kg, in contrast with higher value-added milk powder products such as baby formula powder at \$13.13/kg. This latter category sold only 492 tonnes to China, however, compared with 386,039 tonnes of whole milk powder.⁸⁴ Similarly, a higher volume of unsalted butter (47,545 tonnes returning \$4.81/kg) than salted butter (618 tonnes returning \$9.33/kg) was sold to China.⁸⁵ The same is clear for cheese; in 2016 the greatest amount of cheese product exported was fresh cheese (24,872 tonnes) returning \$5.70/kg, whereas only 4 tonnes of higher returning Gouda cheese (\$13.50/kg) was exported.⁸⁶

Wood exports to China have also had limited processing. In 2016, 80 per cent of New Zealand's total wood exports to China were rough-sawn untreated *Pinus radiata*, returning on average \$148.74/cubic metre. This compared unfavourably with lightly processed untreated cut *Pinus radiata* exports which averaged \$334.56/cubic metre, but only comprised 4 per cent of wood exports there.⁸⁷ Similarly, sheep meat exports are only allowed in frozen form, cutting out fresh or chilled which fetch higher prices. In 2016, 91 per cent of products to China were frozen bone-in cuts, returning on average \$4.24/kg for lamb cuts and \$3.68/kg for cuts from sheep. Both of these figures are also lower than what New Zealand receives worldwide for similar products (\$6.26/kg and \$3.95/kg respectively). Such figures are particularly of concern when it is realised that exports to China have equalled or more than contributed to the growth in New Zealand's sales of these products worldwide in the past eight years.

While exports to China have been important for maintaining and growing New Zealand's primary industries since 2008, the continued reliance on low value-added products does little for related secondary industries, and makes the country vulnerable to future competition. New Zealand products' place in that market could be seen as being based on being 'first in', rather than any specific preference for

⁸³ Fonterra, for example, cites return on capital for lower value-added 'ingredients' products such as whole milk powder at 13.4 per cent for 2016, compared with 41.7 per cent for higher value-added 'consumer' and 'food service' products. Fonterra. (2016). *Fonterra Annual Review 2016* (p. 12). Auckland, New Zealand: Fonterra Cooperative Group Limited. Retrieved from <https://view.publitas.com/fonterra/fonterra-annual-review-2016/page/1>

⁸⁴ Returns calculated by dividing 2016 FOB total with quantity exported for HS codes 0402210019 and 0402210001; Statistics New Zealand. (n.d.). *Infoshare*. Retrieved from <http://www.stats.govt.nz/infoshare/>

⁸⁵ Returns calculated for HS codes 040510001 and 040510009; Statistics New Zealand, Infoshare.

⁸⁶ Returns calculated for HS codes 0406100001 and 0406900031; Statistics New Zealand, Infoshare.

⁸⁷ Comparisons are made between 2016 exports in 2016 for HS codes 4403200031 and 4407109913; Statistics New Zealand, Infoshare.

niche products. The vast Chinese market is seen as an opportunity for many primary producing countries, and as it extends its trade relationships, similar low-value commodities from other sources may easily replace New Zealand products. Australia is noted as being particularly well placed to compete with New Zealand in the Chinese market, with a review of its 2015 free trade agreement already underway. That country is China's main alternative source for sheep meat imports, and is also the second largest source of dairy product imports. In frozen sheep meat cuts it appears that holding market share is based on a tenuous 'race to the bottom' in prices, with average costs per quantity of frozen cuts decreasing progressively over the past three years from all the main sources.⁸⁸ Chile, which also has a free trade agreement with China, has in the last decade developed specific initiatives to grow its sheep meat industry and worldwide exports,⁸⁹ and could also present real competition for New Zealand in future. Some success in the Chilean policies is indicated from small increases in Chilean sheep meat product sales to China in recent years.

Possibilities for future development?

There are signs that some higher valued exports from New Zealand have enjoyed increases in sales to China. Mechanical machinery exports to China have grown, despite some fluctuations from year to year. An average of \$53.8 million in mechanical machinery was exported from 2012 to 2016, compared with an average of \$31 million over the previous five years.⁹⁰ Therapeutic respiration equipment exports have also increased from \$3.2 million in 2008 to \$17 million in 2016.⁹¹ Higher value primary products have also enjoyed some increases in exports, such as honey which reached \$48 million in exports to China in 2016. These products have high average returns per kg, with the main two honey product categories averaging \$35.37/kg and \$43.53/kg respectively in China,⁹² a slightly higher than the average return than received worldwide. Still wine exports to China have also increased, reaching \$26 million in 2015 and 2016. Some heart may be taken by these examples of value-added export growth, but they must be recognised as very small export earners compared with the main five product areas; even added together these exports represented only two per cent of the total to China in 2016.

The review of the New Zealand-China FTA may hold hope for New Zealand to develop more sophisticated exporting activity. The FTA 'upgrade' has been heralded as an opportunity to 'modernise' and enhance areas of the agreement.⁹³ Political leaders have argued that there is high consumer demand for New Zealand's goods

⁸⁸ Costs calculated from imported value vs. quantities of Chinese imports of HS codes 020442 and 020443. International Trade Centre. (n.d.). *Trade map*. Retrieved from <http://www.trademap.org/>

⁸⁹ Muller, N. (2009, July 15). Chilean sheep farming industry targets double lamb exports by 2010. *Santiago Times-MercoPress*. Retrieved from: <http://en.mercopress.com/2009/07/15/chilean-sheep-farming-industry-targets-double-lamb-exports-by-2010>

⁹⁰ HS code 84, nuclear reactors, boilers, machinery and mechanical appliances; parts thereof.

⁹¹ HS code 9019101900.

⁹² Returns calculated for HS codes 0409000001 and 0409000018; Statistics New Zealand, Infoshare.

⁹³ Ministry of Foreign Affairs and Trade. (n.d.). *NZ-China FTA upgrade*. Retrieved from: <https://mfat.govt.nz/en/trade/free-trade-agreements/free-trade-agreements-in-force/nz-china-free-trade-agreement/>

in the Chinese market, but have equally recognised the predominance of low value products in New Zealand's exports there so far,⁹⁴ and commentators have argued for the review to develop opportunities for higher-value trading.⁹⁵ Of particular pertinence is the call to pave the way for more small and medium New Zealand businesses to be able to engage in export trade with the Chinese market, because they may be able to supply more distinctive, higher value products.⁹⁶ This may be the key means by which New Zealand's export products can come to competitively hold their own in the expansive and increasingly wealthy Chinese marketplace.

Conclusion

The call to modernise the New Zealand-China FTA is apt, because the evidence indicates that New Zealand's trade activity may be regressing rather than evolving under the current arrangements. China has undoubtedly been very important for increasing New Zealand's export revenue, but the nature of this activity so far has done little to enhance this country's status in the global marketplace. The substantial shift in focus to the Chinese market leads one to question whether New Zealand primary industries have simply redirected reliance, rather than truly diversifying or creating a sustainable developmental platform for the future. The limited amount of processing that many of the exports to China require has done little for progressing New Zealand's secondary industries or optimising returns that might be gained from further and more diverse processing of dairy, meat and forestry products.

The current review of the free trade agreement, therefore, presents a necessary opportunity for New Zealand to break out of the status of being a provider of low value primary products in the global marketplace. The Chinese market has been recognised as exhibiting demand for New Zealand's high-value consumer goods, but the potential remains untapped under the current trading context, and may well need greater support from government to push the more lucrative relationships into being. While there are clearly a number of services in place to facilitate trade in the Chinese market, the question remains whether the different areas of business, investment source and diplomatic need are sufficiently 'joined up' to genuinely progress new opportunities for New Zealand in the Chinese market. The recent Ministry of Foreign Affairs and Trade strategy to engage with the public and exporters could be an important step in establishing where the areas of need most lie. It is clear, however, that the learnings, and actions from them, need to be timely in order for New Zealand to properly capitalise on its early trade relationship with China.

⁹⁴ Leslie, D. (2017, May 8). *Insight: Upgrading the China free trade agreement* [Radio broadcast]. Auckland, New Zealand: Radio New Zealand. Retrieved from: <http://www.radionz.co.nz/national/programmes/insight/audio/201799415/insight-upgrading-the-china-free-trade-agreement>

⁹⁵ For example, O'Riley, B. (2017, March 28). FTA upgrade can open new doors (p.D22). *New Zealand Herald*; Zhao, W. (2017, March 28). China's changing - and NZ needs to change too (p.D11). *New Zealand Herald*.

⁹⁶ Barnett, M. (2017, March 28). Smaller companies need to come into play with China (p.D12). *New Zealand Herald*.

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