THE UNIVERSITY of ADELAIDE

# Wine Economics Research Centre

# Wine Policy Brief No. 28

## How will markets adjust to China's new tariff on imports of Australian wine?

**Glyn Wittwer and Kym Anderson**

**February 2021**

**University of Adelaide**

**SA 5005 AUSTRALIA**

https://economics.adelaide.edu.au/wine-economics/

# WINE ECONOMICS RESEARCH CENTRE

The Wine Economics Research Centre was established in 2010 by the School of Economics and the Wine 2030 Research Network of the University of Adelaide, having been previously a program in the University's Centre for International Economic Studies.

The Centre's purpose is to promote and foster its growing research strength in the area of wine economics research, and to complement the University's long-established strength in viticulture and oenology.

The key objectives for the Wine Economics Research Centre are to:

- publish wine economics research outputs and disseminate them to academia, industry and government
- contribute to economics journals, wine industry journals and related publications
- promote collaboration and sharing of information, statistics and analyses between industry, government agencies and research institutions
- sponsor wine economics seminars, workshops and conferences and contribute to other grape and wine events

Contact details:

Wine Economics Research Centre
School of Economics
University of Adelaide
SA 5005 AUSTRALIA

Email: kym.anderson@adelaide.edu.au

Centre publications are at: https://economics.adelaide.edu.au/wine-economics/

# How will markets adjust to China's new tariff on imports of Australian wine?

**Glyn Wittwer**
*Centre of Policy Studies, Victoria University, Melbourne, Australia*
glyn.wittwer@vu.edu.au

and

**Kym Anderson**
*Wine Economics Research Centre, University of Adelaide, Adelaide and*
*Arndt-Cordon Department of Economics, Australian National University, Canberra*
kym.anderson@adelaide.edu.au

February 2021

*Corresponding author:*
Professor Kym Anderson, Executive Director,
Wine Economics Research Centre
School of Economics,
University of Adelaide
Adelaide SA 5005, Australia
Phone +61 8 8313 4712
kym.anderson@adelaide.edu.au

*Acknowledgement:*
The authors are grateful for financial support from Wine Australia, under Research Project UA1803-3-1, and from the University of Adelaide's Faculty of the Professions and School of Agriculture, Food and Wine. Wine Economics Research Centre Wine Brief 28, University of Adelaide, February 2021. Forthcoming in *Wine and Viticulture Journal* 36(2), Autumn 2021.

# How will markets adjust to China's new tariff on imports of Australian wine?

In late 2020 China imposed 'temporary' tariffs on its imports of Australian bottled wine, pending its investigation into alleged producer subsidies to and dumping by Australian producers. The tariffs vary by firm, ranging from 113% to 218% and averaging more than 170%; and they are expected to remain at a high level once those investigations are completed in August 2021. They came at the end of a difficult year for the Australian grape and wine sector. Following our analyses of the impacts of bushfires and COVID-19 (Wittwer 2020; Wittwer and Anderson 2020b, 2020c), this article provides comparable estimates of the likely consequences of those tariffs. It reviews the recent growth of Australian and other countries' wine exports to China before employing our new model of global beverage markets to estimate the likely diversions and overall reduction in global wine trade and the impacts on Australia's wine markets at home and abroad. To put those impacts in perspective, they are compared with the impacts in 2020-21 of COVID-19.

## Background

China progressively imposed a series of trade sanctions on Australian products in 2020, in response to Australian government initiatives it disliked. In addition to restrictions or virtual bans on imports of lobster, coal, copper, cotton and some beef and timber from Australia, tariffs have been imposed on China's imports of Australian barley (at a rate close to 80%) and bottled wine (rates ranging from 113% to 218% depending on the firm, including a 6% add-on to the anti-dumping rates to countervail alleged subsidies).

The Australian Government has taken the barley case to the WTO's Dispute Settlement Body, and is considering further responses to these various developments. If the temporary wine tariffs were to remain after China's investigations are completed in August 2021, the Australian Government could take the matter to the WTO – but several years would elapse before the case is resolved there. That reality is forcing Australian producers to look to alternative markets, and simultaneously is encouraging other wine-exporting countries to sell more to China.

The net effect of a near-prohibitive ban on imports from one country is less than the gross effect, because shipments can be directed to alternative markets that will become more accessible as other exporters divert some of their trade to China. But this is harder for products that are more differentiated by country of origin, and also when the market in the destination involved (China) is different from those of other destinations.

Quality differences across countries are much less for barley and coal than for wine. As well, the shares of Australia's exports going to China prior to the new trade restrictions were almost the same in volume as in value terms for barley (around three-quarters) and for coal (a little over one-fifth), so quality differences between China and Australia's various other export markets are not great. For wine, by contrast, the differences are huge: almost two-fifths of the value of Australia's wine exports have been going to China recently compared with just one-sixth of the volume; and the average price of Australian wine sales to China in the 12 months to September 2020 was one-tenth above the average to other Asian markets (5% of total sales in 2020), one-third above the domestic market average (38% of sales), and three times the average to the rest of the world (41% of sales).

Thus diverting wine sales to alternative export markets following China's tariff imposition will not be easy.

Nor will it be easy to displace imports in the domestic wine market. In recent years a little under 40% of the volume of Australian wine sales have been domestic, although on average they are higher quality than sales abroad and have accounted for around 55% of the value of total sales of Australian wine (Wine Australia 2020). Currently imports (around two-thirds are from New Zealand) account for about 15% of sales by volume and almost twice that share by value in Australia. Moreover, selling domestically more of our higher-priced wines previously destined for China, by crowding out imports, will be more difficult than those volume vs value shares imply, because premium exports to China are mostly red wines whereas New Zealand imports are mostly whites.

## Recent growth in Australia's wine exports to China

Exports of wine from Australia to China had been growing rapidly since 2005, from a very low base, but they accelerated after 2014. The share of our total wine exports going to China has grown much faster than that for our other agricultural exports. By 2019 it equalled the share for all exported goods and hence was close to the Australian mining sector's exposure to Chinese markets (Figure 1). For the twelve months to October 2020, China's share of

Australian wine exports was even higher at 42% (and Australia's total wine exports reached a new 12-month record of just over AUD3 billion). But then the tariffs were imposed, and Australia's wine exports to China were close to zero for the remaining two months of 2020.

[insert Figure 1 about here]

Another way to capture the extent of exposure of Australia's grape and wine sector to China's policies is to estimate the index of intensity of that bilateral trade, defined as the share of a country's wine exports to China divided by China's share of global wine imports. Figure 2 reveals that Australia's wine exports to China were twice as intense as that of France during the first decade of this century, but by 2019 it was six times as intense (and more than twice as intense as the next most-exposed country, namely Chile).

[insert Figure 2 about here]

**Estimating the impact of China's wine tariffs on trade and Australia's wine markets**

To estimate the market impact of these new tariffs, we use our new model of the world's beverage markets (Wittwer and Anderson 2020a). It is a global economic model of national wine, beer and spirits markets connected through international trade, in which the interactions between each nation's producers and consumers of these three beverages are explicitly recognized. This GLOBAL Bev Model is calibrated to 2019, and includes zero tariffs on China's imports of Australian wine (as implemented from 1 January 2019 under the China-Australia Free Trade Agreement that entered into force on 20 December 2015). Results are reported relative to a no-new-tariffs business-as-usual baseline simulation that excludes any effects of COVID-19. But since these impacts are being felt after the COVID epidemic, it is helpful to compare them with the impacts of COVID as estimated with the same GLOBAL Bev model. To get a sense also of their likely combined impact on Australia's wine regions, we employ our new TERM-Wine economywide model of the Australian economy used by Wittwer and Anderson (2020b) to examine COVID, and superimpose the China tariff shock on top of the COVID shock to demand.

The trade shock we impose on the model is the imposition of a 170% tariff on bottled wine imports from Australia by China. That is the rate applied since November 2020 on wines from Australia's major wineries, and may be conservative because only a few Australian wineries are subject to tariffs as low as 113% and the majority of smaller firms are subject to the maximum tariff of 218%.

## Results

A tariff of 170% is estimated to virtually wipe out Australia's bottled wine exports to China. This hits fine wine exports especially, since 52% of the value of sales to China recently have been above A$15/litre (compared with just 5% of Australia's sales to the US and 3% to the UK). That loss in exports to China amounts to US$785 million per year (close to the AUD1.1 billion in exports in the 12 months prior to the new Chinese tariff). The total loss of exports is much smaller than that of course, as some shipments from Australia are diverted to other countries. According to the GLOBAL Bev Model, Australia will raise its annual exports to the US by US$120 million, to Canada by $49m, to the UK by $45m, to other Asia by $42m, etc. (Figure 3). The net reduction in Australian wine exports is estimated at US$225m. Recall, though, that this is compared with business as usual: Australian wine exports grew by 30% in the four years to 2019 in US$ terms (and nearly doubled in AUD terms between 2014 and 2019, see Wine Australia 2021), so this just erodes some of that recent growth.

[insert Figure 3 about here]

This shock is estimated to reduce the average producer price of wine in Australia by 11%, of winegrape prices by 12%, of the volume of exports by 13%, and of total wine sales value by 14% (a drop of 22% for exports and 2% for the now-lower-priced albeit 3% larger volume of domestic sales). In the wake of more local (especially premium) wine crowding retail shelves domestically, Australia's imports of wine fall, in volume terms by an estimated 5% and in value terms by 10%.

The breakdown of these results into sparkling wine and three different categories of still wines is reported in Table 1. Even though most of Australia's wine exports to China have been in the super-premium category in recent years, the impact of the tariff cascades down to commercial premium grapes and wine: their price drop encourages local consumers to buy more from that category as well as from the fine wine category.

[insert Table 1 about here]

To put the estimated fall in winegrape prices in perspective, in a previous modelling exercise we estimated that the strengthening of the AUD in 2007-11 depressed Australian winegrape prices by 13% (see Anderson and Wittwer 2013, Table 1a). In a more-recent exercise using the GLOBAL Bev model we estimated that COVID would depress the average winegrape price and wine price in Australia by 8% in 2021 (Anderson and Wittwer 2020b). The country's estimated export losses from COVID are less than half as large as from the Chinese new tariff. But there are considerable losses in domestic sales as well in the case of

COVID, thanks to greater purchases off-premise instead of on-premise and reductions in in-bound tourists and students, compared with little change in the case of the Chinese tariff (compare Tables 1 and 2).

[insert Table 2 about here]

Figure 4 reveals how the origins of China's wine imports may change as a consequence of its new tariff. France, Chile, Spain, Italy and the United States are expected to be the main beneficiaries (in that order, see Figure 4). But their increase in imports only partly offset the fall in imports from Australia, with China's total wine imports being lower by US$215m per year because of this new protectionist barrier.

[insert Figure 4 about here]

To assess the tariff's impacts on wine regions within Australia, our new TERM-Wine model can be used, as it has also for examining COVID's effects (Wittwer and Anderson 2020b). The grape and wine price drops that producers are feeling due to China's tariff are on top of the price drops due to COVID, so their impacts are cumulative. To see the combined impacts of this double whammy for Australian wineries, we superimposed the tariff shock on top of the COVID shock in the TERM-Wine model. In this model the projected drop in Australia's winegrape and wine prices for the 2021 vintage due to COVID in the absence of China's tariff is worsened by four percentage points when China's tariff also is imposed. Sales volumes also fall, and together these changes lower winery gross earnings. The combined impacts of price and quantity drops in Australia are greater due to tariffs than due to COVID. Moreover, while the COVID impacts do not vary greatly across wine regions, the additional impacts of China's tariff do: the premium regions of South Australia and Victoria are the worst hit (because premium red wines dominate exports to China), but the warm irrigated areas also suffer thanks to the cascading effects of a hit to super premium wines on the prices of lesser-quality wines and hence grapes (Figure 5).

[insert Figure 5 about here]

## Conclusion

These results are merely illustrative, based on assumptions and model parameters that may deviate from reality. For example, the US market may not be able to absorb such a large increase in Australian wine imports in the near term, which would initially put even more pressure on other markets including the domestic one. Also, the largest (multinational) wineries may buy fewer Australian winegrapes and instead expand their wine production in other countries, such as France for exporting from there to China. To the extent that happens more than we have modelled, it suggests Australian winegrape prices may fall by more than indicated above. The degree of producer substitutability between the three quality categories may be underspecified in the TERM-Wine model too. That would limit the projected cascading of impacts from super premium to lower-quality wines and thus grapes.

Clearly growers, and their industry associations, will need to expand their initiatives aimed at penetrating non-Chinese markets in the years ahead if they are to offset the consequences of China's tariff. One means toward that end is to take advantage of the Federal Government's AUD72.7 million *Agri-Business Expansion Initiative*, announced at the close of 2020 to fund, among other things, market access efforts abroad (Ministers for Agriculture and Trade 2020). With the UK now out of the EU, and the US imposing trade-retaliating tariffs on EU wines, those two traditional markets plus Canada and New Zealand are the easiest to re-assess because of a common language and customs. Bilateral FTA trade negotiations are currently under way with both the UK and EU27, offering further prospects there. More promotional efforts in the lucrative markets of other northeast and southeast Asian countries, if not regulation-ridden India, are likely to have a high payoff too (Anderson 2020). And while South Africa starts putting more effort into penetrating China, now would be a good time to begin to compete with it on the African continent, where wine market growth prospects look bright for the decade ahead (Anderson and Wittwer 2018).

The other obvious initiative is to boost promotion efforts in the domestic market, where imports currently account for about 15% of sales by volume and around twice that share by value. Selling domestically more of our higher-priced wines previously destined for China, by crowding out imports, may not be easy in the current COVID environment, however. This is especially so given that exports to China are mostly red wines whereas wines from New Zealand (our dominant importer) are mostly whites.

## References

Anderson, K. (2020), "Asia's Emergence in Global Beverage Markets: The Rise of Wine", *Singapore Economic Review* 65(4): 755-79, June.

Anderson, K. and G. Wittwer (2013), "Modeling Global Wine Markets to 2018: Exchange Rates, Taste Changes, and China's Import Growth", *Journal of Wine Economics* 8(2): 131-58.

Anderson, K. and G. Wittwer (2018), "Projecting Global Wine Markets to 2025", Ch. 18 in *Wine Globalization: A New Comparative History***, e**dited by K. Anderson and V. Pinilla, Cambridge and New York: Cambridge University Press.

Ministers for Agriculture and Trade (2020), *Agri-Business Expansion Initiative*, Canberra, 23 December. https://www.agriculture.gov.au/market-access-trade/agri-business-expansion

Wine Australia (2020), *Australian Wine Production, Sales and Inventory 2018-19,* Adelaide: Wine Australia, February.

Wine Australia (2021), *Export Report, 12 Months to 31 December 2020,* Adelaide: Wine Australia, February.

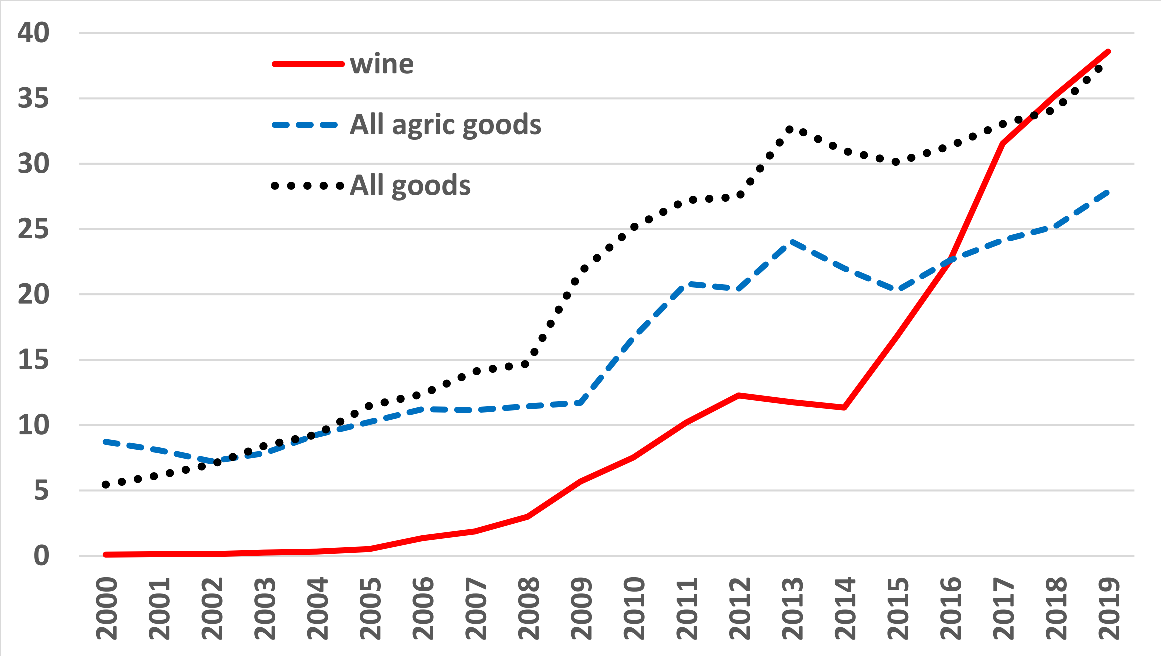
Wittwer, G. (2020), "The 2019-20 Australian Economic Crisis Induced by Bushfires and COVID-19 from the Perspective of Grape and Wine Sectors", CoPS Working Paper No. G-299, Victoria University, Melbourne, March. http://www.copsmodels.com/ftp/workpapr/g-299.pdf.

Wittwer, G. and K. Anderson (2020a), "A Model of Global Beverage Markets", *Journal of Wine Economics* 15(3): 330-54, August.

Wittwer, G. and K. Anderson (2020b), "COVID-19's Impact on Australian Wine Markets and Regions", Wine Economics Research Centre Working Paper 2020-03, University of Adelaide, December. Presented at the Annual AARES Conference, University of Sydney, 9-12 February 2021.

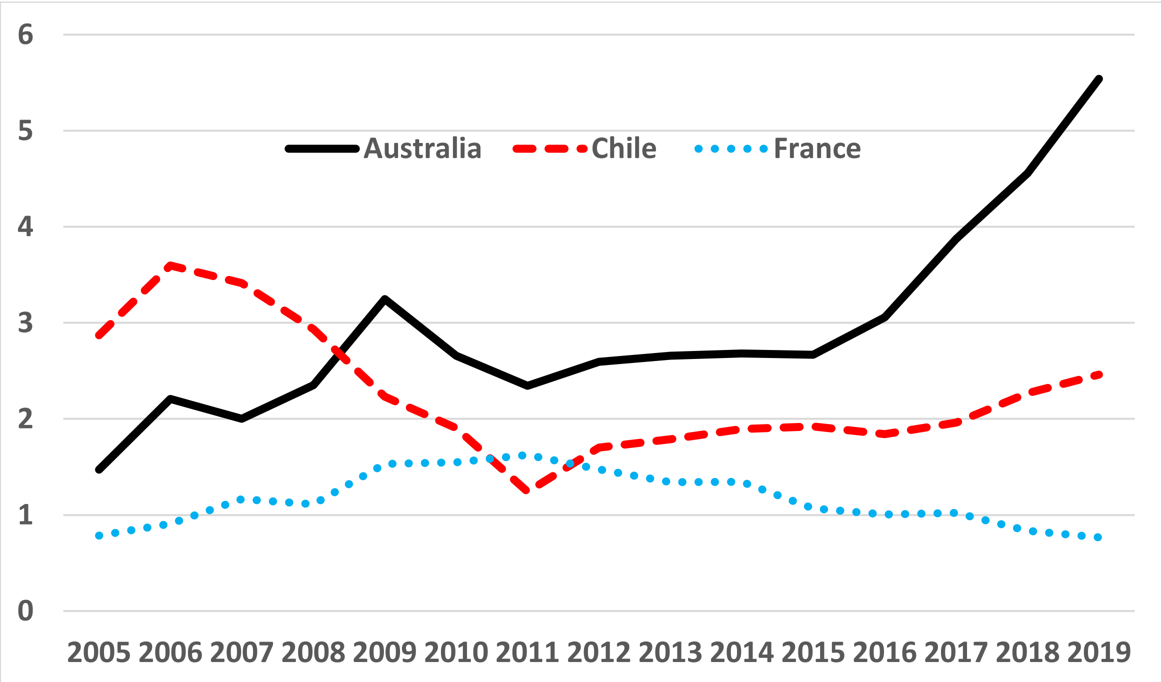
Wittwer, G. and K. Anderson (2020c), "How is COVID Influencing Global Wine Trade and Australia's Wine Regions?" Wine Economics Research Centre Wine Brief 27, University of Adelaide, December.

Figure 1: Shares of the value of exports of Australian goods going to China, 2000 to 2019 (%)



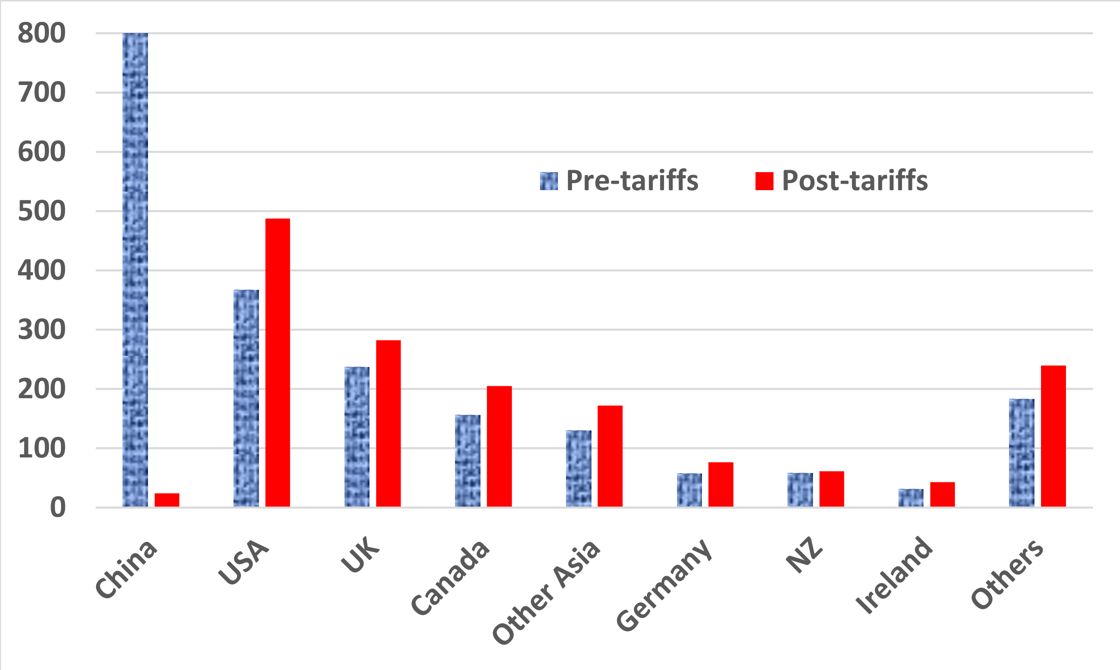

Source: ABS online data.

Figure 2: Index of intensity of wine exports to China from Australia, Chile and France, 2005 to 2019 (defined as the share of country i's wine exports to China divided by China's share of global wine imports)



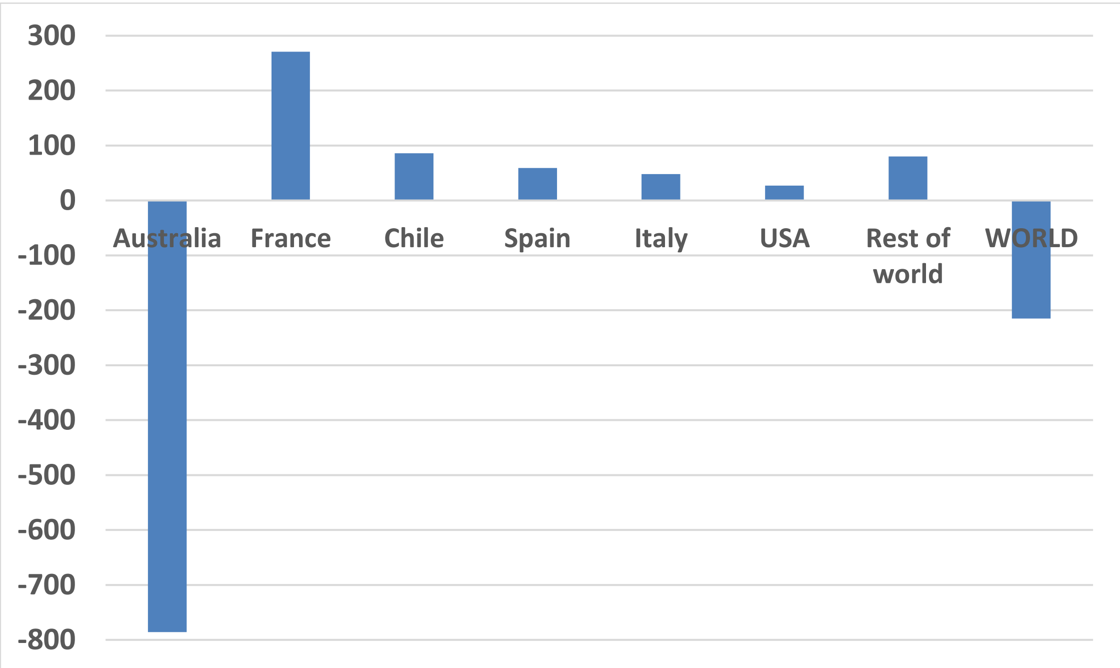

Source: United Nation's COMTRADE online data.

Figure 3: Value of Australian wine exports by destination, pre- and post-tariff imposition of a 170% tariff on bottled wine imports by China from Australia (US$ million per year)



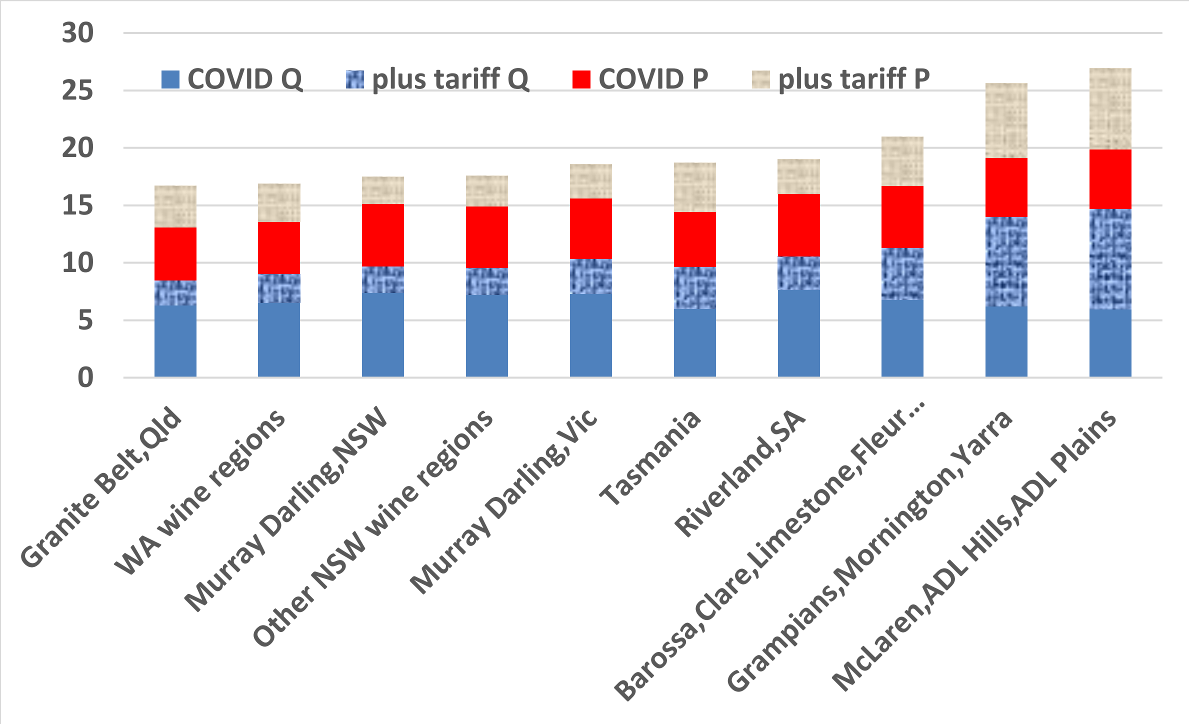

Source: Authors' GLOBAL Bev model results.

Figure 4: Change in value of China's wine imports by source, pre- and post-tariff imposition of a 170% tariff on bottled wine imports by China from Australia (US$ million per year)




Source: Authors' GLOBAL Bev model results.

Figure 5: Decline in gross winery earnings (sales volume Q plus price falls P) due to COVID, without and with China's tariffs, by wine region, Australia, 2020-21




Source: Authors' TERM-Wine model results.

Table 1: Wine market impacts of imposition by China of a 170% tariff on imports of Australian bottled wine, Australia (% change)

| | Producer price | Domestic consumption | | Exports | | Imports | |
|---|---|---|---|---|---|---|---|
| | | Volume | Value | Volume | Value | Volume | Value |
| **ALL WINE** | **-11** | **3** | **-2** | **-13** | **-22** | **-5** | **-10** |
| Non-premium wine | 0 | 0 | -0 | 1 | 1 | -0 | -0 |
| Commercial premium | -14 | 4 | -4 | -10 | -22 | -16 | -18 |
| Super-premium wine | -12 | 4 | -1 | -46 | -52 | -13 | -14 |
| Sparkling wine | -3 | 1 | -0 | -13 | -16 | -2 | -2 |
| **Winegrapes** | **-12** | | | | | | |

Source: Authors' GLOBAL Bev model results.

Table 2: Wine market impacts of COVID-19 on Australia's wine markets, average for 2020 and 2021 (% change, relative to no-COVID and no new Chinese tariffs baseline)

| | Producer price | Domestic consumption | | Exports | | Imports | |
|---|---|---|---|---|---|---|---|
| | | Volume | Value | Volume | Value | Volume | Value |
| **ALL WINE** | **-7** | **-4** | **-9** | **-3** | **-9** | **-5** | **-15** |
| Non-premium wine | -5 | -3 | -5 | -3 | -8 | -2 | -7 |
| Commercial premium | -7 | -3 | -8 | -2 | -9 | -0 | -8 |
| Super-premium wine | -6 | -2 | -6 | -3 | -9 | -1 | -7 |
| Sparkling wine | -17 | -17 | -26 | -15 | -28 | -16 | -30 |
| **Winegrapes** | **-8** | | | | | | |

Source: Authors' GLOBAL Bev model results, as reported in more detail by Wittwer and Anderson (2020b).