Experts disagree about degree of risk facing U.S. ag

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Associated Press

A cargo ship loaded with containers calls on the Port of Qingdao in China. About $20 billion in U.S. agricultural goods were sold to China last year.

down domestic crop prices, experts say.

This scenario would be particularly dangerous if a crumbling Chinese economy were to coincide with a politically motivated trade dispute between the Chinese and U.S. governments.

Ag bears brunt

"Ag does end up bearing the brunt, particularly the initial blows, of any of these kinds of trade disruptions," said Bob Young, chief economist for the American Farm Bureau Federation.

Given the Chinese economic system's lack of transparency and the unpredictability of the Trump administration's trade stance toward the country, experts disagree about the degree of risk facing U.S. agriculture.

Jim Budzynski is a pessimist.

As managing principal of Macrogain Partners, a company that advises on agricultural investment, Budzynski is troubled by the trillions of dollars in debt that China's government and corporations have taken out to keep the economy growing.

"It's going to be very difficult to unwind," he said. "They're in a very precarious situation."

The current state of affairs in China is similar to the U.S. before the housing-induced financial crisis nearly a decade ago, Budzynski said.

Chinese banks are disguising loans as investments in "wealth management" entities, circumventing government limits on debt, he said.

The Chinese government tolerates this deception because it needs to pump money into the economy to keep it growing, Budzynski said.

As with the U.S. financial crisis, the danger is that eventually these entities will become insolvent and fail to repay debts, sending ripples through the entire Chinese financial system, he said.

Such unraveling could result in a worse global financial catastrophe than seen in 2008, since off-balance sheet debt has mounted since then, Budzynski said.

"At some point, you have to stop digging" deeper into debt, he said. "We keep digging."

Exactly how quickly such pressures could reach a breaking point is tough to forecast, said Desmond O'Rourke, a retired Washington State University agriculture economist and world apple market analyst.

"Certainly the system could collapse. However, like our housing bubble, bubbles can continue for a long time and it is difficult to predict when they might burst," said O'Rourke.

China is borrowing 250 percent of its annual gross domestic product compared to 100 percent for the U.S., he said. Anything over 50 to 60 percent is considered unsafe.

Flight of capital

Experts are also worried by wealthy Chinese companies and individuals who are trying to get their money out of the country — both because it signals internal economic anxiety and because it can lead to further weakening of the financial system.

"There is the potential for a huge looming crisis to occur," said Piegza of Stifel Financial Corp.

Such flight of capital has another impact. When investors take their money out of China, they must convert the Chinese yuan into U.S. dollars or another foreign currency, said Fred Gale, a USDA economist who studies China.

Quickly selling a large amount of currency has the same effect as unloading large quantities of any other commodity. The sudden surplus drives its value down, he said.

In effect, the Chinese yuan is devalued by capital flight, which is bad for U.S. farmers because their crops become more expensive in that country as the dollar strengthens, Gale said.

The dynamic also undermines the resiliency of Chinese banks.

"If you have lots of people doing the same thing, the currency reserves of the Chinese banks go down," he said. "That means they have less cash on hand to back their liabilities. It puts them in a perilous state."

However, the Chinese government can counteract the devaluing of the yuan by selling its reserves of foreign currency, said Piegza. By trading foreign currency for yuan, China buys its own currency to boost its value.

Ultimately, China must reassure investors about the stability of its economic system to avoid volatility in financial markets, which could cause the flow of credit to freeze, Piegza said. That would curtail global spending on commodities, hurting crop prices.

"How do you invest in something if you don't know what's happening there?" she said of the Chinese financial market.

Reassurances

For some analysts, recent history provides some reassurances.

Dan Kowalski, research director at the agricultural lender CoBank, said China is in for "a bumpy ride," but the previous financial crisis showed it's equipped to deal with volatility.

The Chinese government then injected roughly $600 billion in capital into the economy, but the situation is less severe now — roughly $200 billion to $300 billion would suffice, he said.

"They're going to do whatever is necessary to shore the system up," Kowalski said. "I don't think a major crisis is coming."

Some experts say that friction between the Trump administration and Chinese leaders is perhaps a greater concern for agriculture than its slowed economic growth.

"It's to be expected that China is not going to go back to growing at 10 percent (a year). Are they still going to grow? Probably. Are they still going to buy stuff? Yeah," said Daniel Sumner, director of the Agricultural Issues Center at the University of California-Davis.

President Donald Trump made getting tough on China a key point in his campaign, but former President Barack Obama's administration also took several steps that could complicate relations, Sumner said.

The U.S. recently filed a World Trade Organization complaint against China over its aluminum subsidies, while outgoing USDA Secretary Tom Vilsack criticized the pace at which China has approved genetically modified crops.

Capital Press reporters Tim Hearden, Matthew Weaver and Dan Wheat contributed to this story.

U.S. commodities have mixed experiences in China

By DAN WHEAT and TIM HEARDEN
Capital Press

O'Rourke

Two years ago, when the U.S. apple industry gained full varietal access to China, economist Desmond O'Rourke warned that the Asian nation might not be the panacea it appeared for apples, citrus, nuts and other commodities.

O'Rourke called China "extremely unreliable" for its ability to cut off trade, as it had for all U.S apples for two years on phytosanitary grounds.

In time, Washington apple exporters hoped China would grow from a 3 million-box, $60 million annual market to a 10 million-box market worth $200 million.

After the ban was lifted, Washington sold 2.9 million boxes of apples to China and Hong Kong from the 2014 crop. But sales dropped to 1.9 million boxes from the 2015 crop and, as of Jan. 3, were 1.2 million boxes this season.

The drop in 2015 was caused by China's economic troubles, more high-quality Chinese Fuji apples competing against Washington apples and Washington's supply being lower and prices higher, said Lindsey Huber, international marketing specialist at the Washington Apple Commission.

California farmers shipped more than $2 billion in agricultural goods to China and Hong Kong in 2014, according to the California Department of Food and Agriculture.

Almonds were the leading commodity at $402.2 million, followed by pistachios at $362.8 million, dairy products at $239.1 million and walnuts at $181.9 million, according to the CDFA.

While overall exports to China have been trending downward since 2013, California commodity groups aren't very concerned — at least yet.

"It still remains strong for us," said Michelle McNeil Connelly, the California Walnut Commission's chief executive officer. "Year to date, we're down just slightly ... but demand has been strong. ... The Chinese New Year is just around the corner, and that's a peak consumption season for us."

In the 2016-17 fiscal year, almond shipments to China are up 49 percent from this point last year, making China the largest export market for California almonds, followed by India and Spain, said Julie Adams, the Almond Board of California's vice president of global, technical and regulatory affairs.

"The China government has expressed the priority of maintaining stability for 2017, which would be important for continued demand for imports such as almonds," Adams said in an email.

For pistachios, China is the No. 1 export market. In the current fiscal year that started in September, China is buying as much as what the U.S. is shipping to the rest of the world and consuming domestically combined, said Richard Matoian, executive director of the Fresno-based American Pistachio Growers.

"It's pretty incredible," Matoian said. "China just seems to be going like gangbusters for us."

Fruit producers are also optimistic that China will remain a key market. For citrus fruit, China and Hong Kong combined were the No. 3 destination behind South Korea and Japan in 2015 with about $130 million in purchases, said Bob Blakely, vice president of California Citrus Mutual.

"Citrus is something that they really like and actually, their buying power has increased," Blakely said. "We haven't seen an indication that that's being affected."

Even without TPP, wheat industry has traded with other countries

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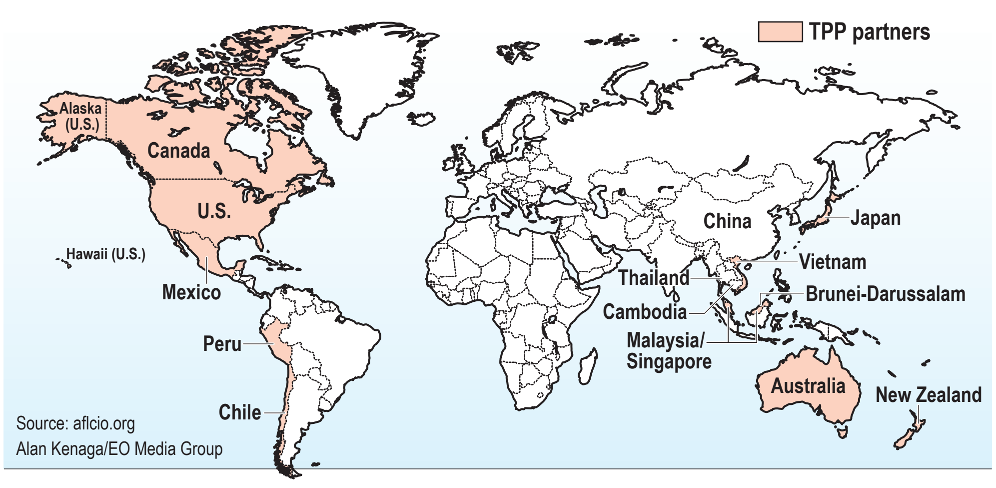
Trans-Pacific Partnership Free Trade Agreement partners



ensuring we do not lose the ground gained — whether in the Asia-Pacific, North America, Europe or other parts of the world."

Any renegotiation of NAFTA must assure that U.S. agriculture trade with Canada and Mexico remains strong, Duvall said.

The U.S. wheat industry also supported the TPP, saying it would have provided a level playing field and reduced tariffs imposed on U.S. wheat.

The National Association of Wheat Growers and U.S. Wheat Associates issued a joint statement calling Trump's decision "inevitable."

"It is disappointing, however, that until an alternative trade policy is established, export opportunities in the promising Pacific Rim markets that could help U.S. wheat farmers at a time when they need it most are very much at risk," the statement says.

Wheat prices have been low the past year.

"Without TPP or alternative agreements, U.S. farmers will be forced to the sidelines of trade while losing market share to competitors, including Australia, Canada, Russia and the European Union, which have current agreements or are negotiating new ones with countries outside the network of existing U.S. trade agreements," said NAWG president Gordon Stoner, an Outlook, Mont., wheat farmer.

"Obviously, we're supportive of trade," said Glen Squires, CEO of the Washington Grain Commission. Roughly 85 to 90 percent of wheat produced in Washington is exported. "Moving forward, we're still going to be supportive of trade."

Even without TPP, the wheat industry has traded with other countries, Squires said.

"If it's not there, we still have to try to compete the best we can in all markets," he said.

Others in agriculture welcomed the news.

National Farmers Union president Roger Johnson said in a statement that he was pleased by Trump's decision.

"For too long, our nation's trade negotiators have prioritized a free trade over fair trade agenda, leading to a massive $531 billion trade deficit, lost jobs and lowered wages in rural communities across America," Johnson said. "It's time our country refocuses the trade agenda to prioritize balanced trade, U.S. sovereignty and U.S. family farmers, ranchers and rural communities."

Shawna Morris, vice president of trade policy for the National Milk Producers Federation and U.S. Dairy Export Council, said the TPP had valuable gains, but wasn't a perfect agreement for dairy producers, particularly for market access.

Dairy producers see Trump's decision as an opportunity to directly engage key Asian markets and establish export advances in Japan, Vietnam and Southeast Asia, Morris said.

"Certainly what we can't see is a situation where the U.S. effectively sits back now and lets our competitors run the board in Asia by sewing up all of their own trade agreements without us being at that table," Morris said.

Tracy Brunner, president of the National Cattlemen's Beef Association, criticized the withdrawal.

"Fact is, American cattle producers are already losing out on $400,000 in sales every day because we don't have TPP, and since NAFTA was implemented, exports of American-produced beef to Mexico have grown by more than 750 percent," Brunner said in a prepared statement. "Sparking a trade war with Canada, Mexico, and Asia will only lead to higher prices for American-produced beef in those markets and put our American producers at a much steeper competitive disadvantage."

R-CALF USA, an independent ranchers' group, applauded Trump's order, saying TPP would have put U.S. livestock producers at a disadvantage.

"It's really a huge relief that now the president of the United States is saying exactly what we've been saying for 20 years," said Bill Bullard, CEO of the organization.

Agreements require Scotts to provide technical assistance to affected farmers

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lays out the company's continued responsibilities for helping control the bentgrass.

As part of the agreement, the company has agreed not to commercialize the plant, which was being developed for use on golf courses.

Jim King, senior vice president of corporate affairs for Scotts, said the golf course industry has changed dramatically since the company started developing the plant and the marketplace for that product is no longer viable and shrinking.

"Economically, it makes no sense to commercialize it," he said.

The company opted to continue to pursue deregulation because it felt it needed an answer from USDA on whether a product Scotts invested tens of millions of dollars in should be approved, King said.

USDA has a regulatory road map that allow companies such as Scotts that are in the business of innovation to know if a certain product should be approved, he said.

"We had a legitimate petition in front of USDA, we wanted an answer and they finally provided the answer," he said.

Lori Ann Burd, director of the Center for Biological Diversity's environmental health program, said the decision to deregulate the bentgrass means the agreements covering the control of the escaped crop are no longer valid.

She pointed out that the word "regulated" appears before "glyphosate tolerant creeping bentgrass" each time Scotts responsibilities are laid out in the agreements.

The responsibilities "apply exclusively to regulated (bentgrass)," she said.

But even if that's not the case, she said, the agreements only require Scotts to take minimal action.

Burd said USDA's decision leaves her group no choice but to explore legal options to challenge it. The agreements require the company in 2017 and 2018 to provide technical assistance to affected farmers and irrigation districts and provide incentives for the adoption of best management practices to control the grass.

Scotts will pull back a little after that but still continue to analyze the situation, educate growers and provide technical assistance.

Coker said the agreements "remain in effect regardless of the deregulated status of (the grass) because the compliance incidents predated the deregulation."

King said Scotts will honor the agreements "and, if we have to, we'll do more. We consider those to be documents that were negotiated in good faith ... and we have every intention of living up to everything we said we were going to do."