

THE IMPACT OF CHINA'S ECONOMIC SANCTIONS ON AUSTRALIAN EXPORTS

POLICY BRIEF TO THE AUSTRALIAN BUSINESS SUMMIT
B173504

WORD COUNT: 1489
ECONOMIC POLICY – SCOTTISH GRADUATE PROGRAMME IN ECONOMICS

Background

A decade ago, Australia thought it was on the verge of an intimate bilateral relationship with China. The [Asian Century White Paper](#), released by the Australian government in 2012, was a forward-looking roadmap designed to create constructive engagement in Asia, particularly China. The Australian-China relationship appeared to flourish, culminating in The [China Australia Free Trade Agreement \(ChAFTA\)](#) in 2015. However, the political relationship slowly declined from here, with disagreements on [various issues](#), including the South China Sea, Australia's foreign interference laws, Hong Kong and Uyghurs in Xinjiang province.

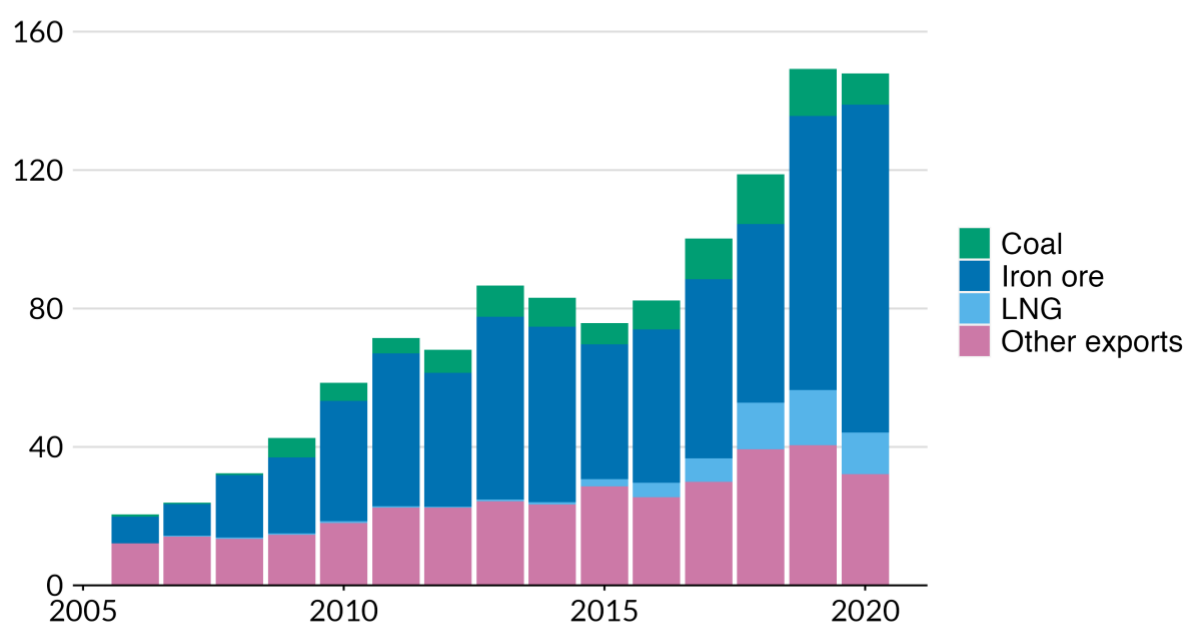
The China-Australia diplomatic relationship nosedived further in April 2020, when Australia [led the call](#) for an independent investigation into the origins of COVID-19. Starting in May 2020, China hit many Australian products with trade sanctions, which [commentators](#) described as a “fairly overt attempt at economic coercion”. Although these sanctions were not framed as political retaliation at the time, Chinese officials have since [publicly declared](#) that Beijing singled out Australia for economic punishment. What has been the economic impact of these trade sanctions on Australian exports?

The Trading Relationship

China's economy today is more than [five times bigger](#) than it was at the turn of the century. Urbanisation [underpinned](#) this rapid growth, along with a shift from agriculture to industry, and increasing openness to global trade. To build new infrastructure, skyscrapers and apartments, China needed steel – and lots of it. Australia has the largest [reserves](#) in the world of the most important component in steelmaking – iron ore. The [resource-intensive](#) nature of China's development led Australian exports to China to expand rapidly over this period. China's growing middle class also became the largest destination for a range of other Australian exports, including wine, barley, timber, cotton and food items such as milk products and lobster.

Australian exports to China have increased substantially, largely because of resource exports

Annual Australian merchandise exports (A\$bn)



Note: Merchandise exports exclude service exports. LNG = Liquefied Natural Gas.
Source: DFAT

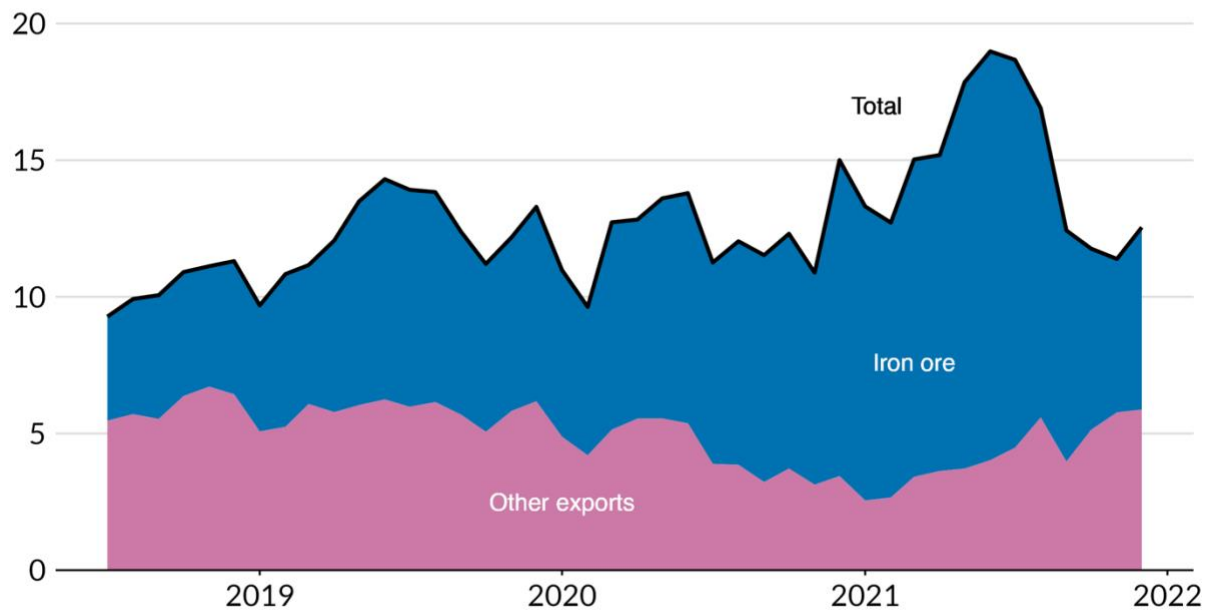
Previously, Australian export data by country and commodity was only available annually. However, the Australian Department of Foreign Affairs and Trade (DFAT) has recently released new [monthly trade data](#) by commodity and country. This new data provides insight into the impact of China's economic sanctions on Australian exports at a more granular level.

At a headline level, there appears to have been little impact from the sanctions, with Australia setting a [record trade surplus](#) of \$13.3 billion in the month of July 2021, and exports to China hitting a record high. This increase was entirely due to iron ore exports, with both quantity and price increases driven by [strong demand](#) from China. From July 2021 to the end of 2021, the value of Australian exports to China declined significantly, but this was again due to [falling prices](#) of iron ore. Excluding iron ore, merchandise exports (goods exports, which exclude service exports such as tourism and education) to

China declined from \$5.2 billion in June 2020, to a low of \$2.5 billion in January 2021, but have since recovered to as \$5.9 billion as of December 2021.

Australian exports to China rose and then fell largely due to price fluctuations of iron ore

Monthly Australian exports (A\$mn) of iron ore and 'other exports' to China



Note: Other exports includes all merchandise exports excluding iron ore.
Source: DFAT

What products were targeted by Chinese sanctions?

During 2020 and early 2021, China imposed tariff and non-tariff barriers on several Australian goods exports.

Table 1: Timeline of Chinese trade restrictions on Australian exports

Date trade restrictions first reported	Australian export	Proportion of Australian exports that went to China in 2019*
May-2020	Barley	57%
May-2020	Beef	25%
October-2020	Cotton	71%
October-2020	Timber	94%
October-2020	Coal	21%
November-2020	Wine	36%
November-2020	Lobsters	80%
November-2020	Copper ores and concentrates	36%
November-2020	Sugar products	6%
Unconfirmed trade restrictions		
November-2020	Live fish	26%
February-2020	Education	32%*
March-2021	Hay	11%
April-2021	Table grapes	40%

*2018-19

Note: For specific Standard International Trade Classifications (SITC) used, see Table 2 in the Data Appendix.

Sources: Table adapted from Benjamin Herscovitch's article in the Australian Industry Group's [2022 Exporters Guide](#), with data from DFAT and news reports in [The Conversation](#), [Australian Broadcasting Commission](#), [South China Morning Post](#) and the [Australia-China Relations Institute](#).

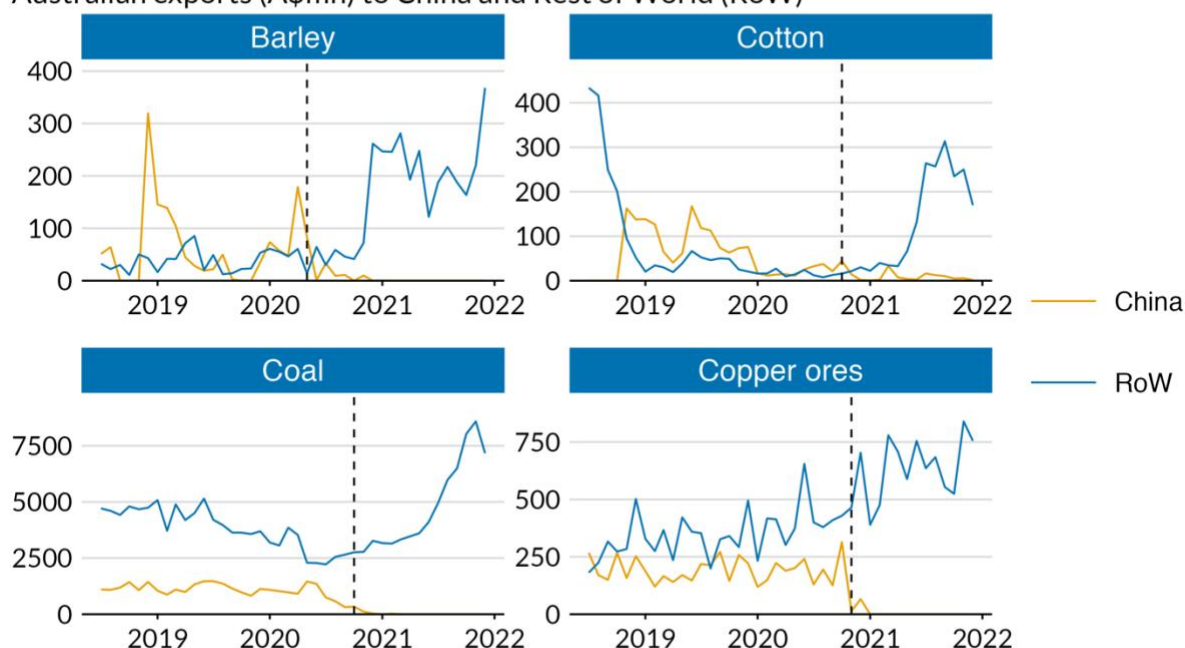
What was the impact on these exports?

Some exports have been more successful in finding other markets than others. For globally traded commodities, increased demand for non-Australian imports from China created opportunities for Australian exporters in other markets, as other countries [diverted exports](#) to China. Notably, exporters of barley, cotton, copper ore and coal have been relatively successful in finding other markets, albeit sometimes at lower prices.

- Exports of barley (for feed) increased to the Middle East (namely Saudi Arabia) and South-East Asian countries such as the Philippines and Vietnam. Further, a [trial](#) is underway selling premium malting barley to Mexico, with exports valued at \$21.5 million in August 2021.
- Cotton export earnings picked up significantly to India, Indonesia, Thailand and Vietnam.
- Copper concentrate grew to India and South Korea. Much of the increase in the value of exports was price driven due to strong [demand](#) for green technology (which is copper intensive) pushing up prices.
- Australian coal found new customers in Japan, South Korea, India, Pakistan and the Middle East.

Australian barley, cotton, coal and copper ore exports have largely found other markets

Australian exports (A\$m) to China and Rest of World (RoW)



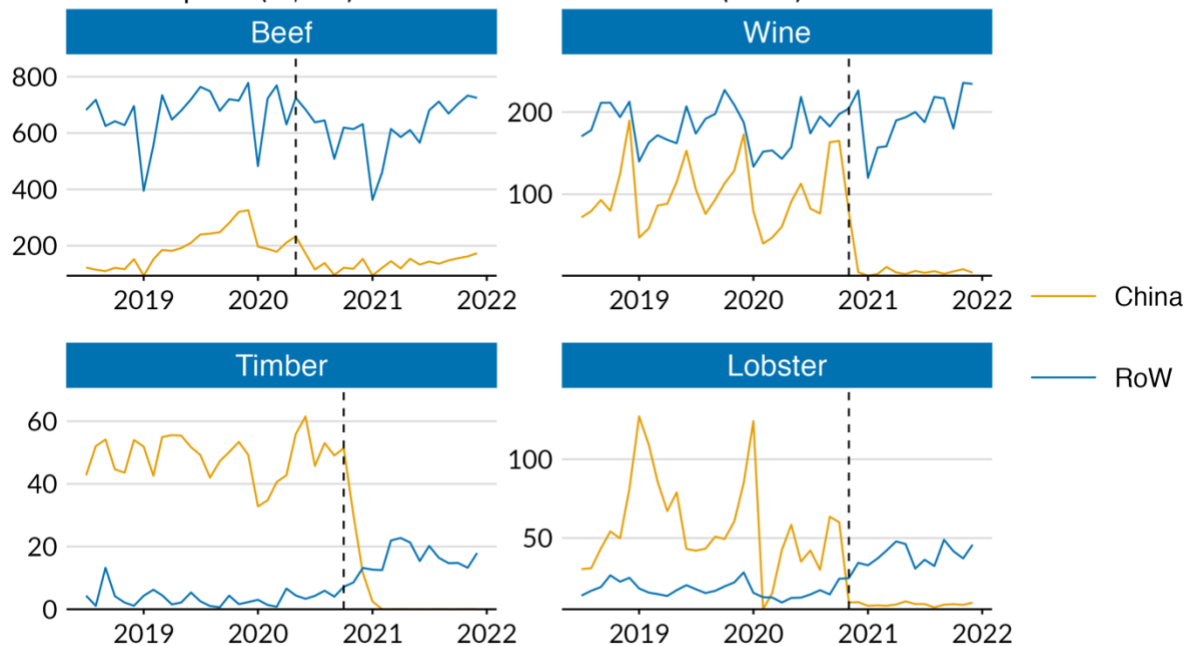
Note: Dashed line indicates month trade restrictions were first reported.
Source: DFAT

In contrast, lobster and timber export earnings have suffered because of Chinese sanctions, and to a lesser extent, so have wine and beef exports. Exports of these goods have found other markets, but not enough to compensate for the Chinese market.

- Between October 2020 and April 2021, log timber exports were down by half, although exports to some markets increased during the period. Monthly exports to India, for example, went from around \$0.2 million to nearly \$20 million over this period.
- Lobster exports to the Chinese market fell from \$843 million in 2019 to \$94 million in 2021, but have increased to Hong Kong, Taiwan, Thailand and Vietnam.
- Alcoholic beverage exports (mostly wine) exports fell from \$3.4 billion in 2019 to \$2.3 billion in 2019. This decline was almost entirely due to Chinese sanctions, with exports declining from \$1.2 billion in 2019 to just \$63 million in 2021. This large decline was partially offset by rising exports to the United Kingdom (UK), Hong Kong, Singapore, South Korea, Denmark, Thailand and Taiwan.
- Beef exports to China have gradually recovered in 2021, but remain well below the recent peak at the end of 2019.

Australian beef, wine, timber and lobster exports have had more difficulty finding other markets

Australian exports (A\$m) to China and Rest of World (RoW)



Note: Dashed line indicates month trade restrictions were first reported.
Source: DFAT

It is important to point out that this data can fluctuate because of other factors, such as weather events, the timing of shipments, and commodity prices. But it is clear China has targeted products for which there are other suppliers. However, this also means there are alternate buyers. Finally, exporters can also adapt to export demand shocks by expanding domestic sales in Australia, as was the case for Australian lobster over [Christmas](#) in 2020.

Who is winning?

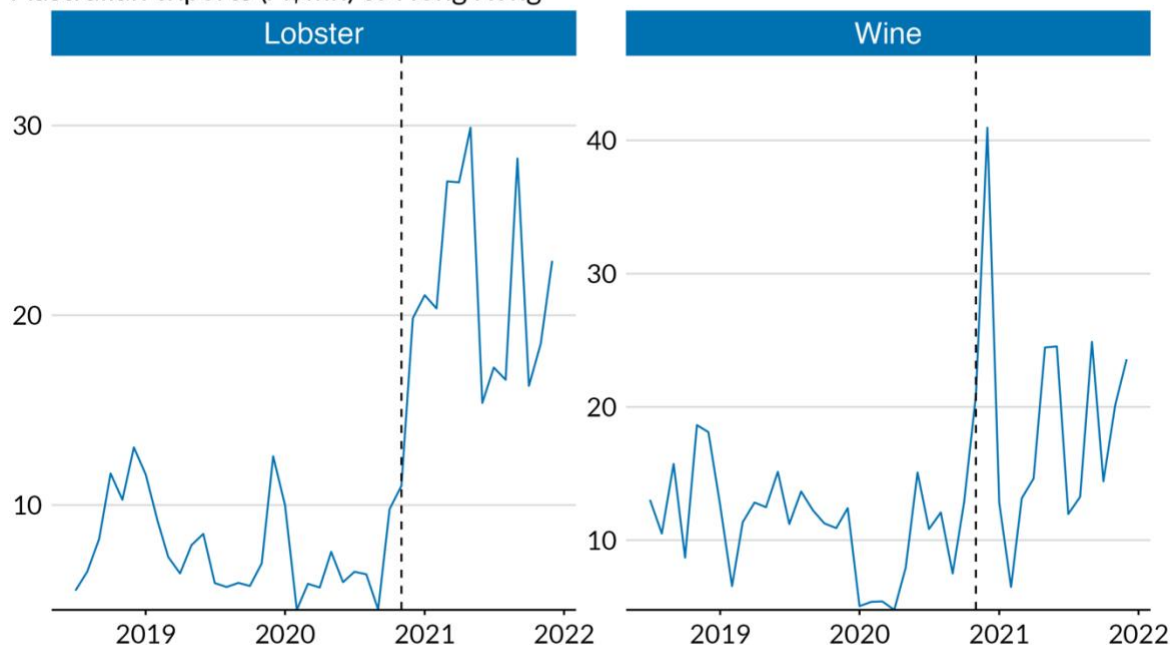
On an aggregate level, the impact on the Australian economy has been negligible. Estimates of the overall cost to the Australian economy are difficult given counterfactuals, the impact of COVID-19, and global supply chain pricing pressures. The Australian Treasury [estimates](#) that goods affected by Chinese trade restrictions lost \$5.4 billion in exports in the year to June 2021, but at the same time exports of these goods to the rest of the world increased by \$4.4 billion. A net loss of \$1 billion in an economy worth \$2 trillion is barely a drop in the ocean. Still, some Australian exporters have lost significant income, time and investment, while many exporters that found new markets had to bear the costs of rerouting exports.

But, these sanctions also hurt China.

Firstly, Chinese consumers miss out on Australian products. For example, premium Australian wine and lobsters are highly sought after for [celebrations](#). This has led to [reports](#) of banned Australian lobsters and wine being smuggled through Hong Kong. The data seems to support these reports, with a 3-fold increase in lobster exports to Hong Kong since the ban was implemented. This shows how Chinese demand for Australian lobster is being satisfied by "grey channels" - or unauthorised trade routes.

Some Chinese demand for Australian wine and lobster is being met by "grey-trade channels" through Hong Kong

Australian exports (A\$m) to Hong Kong



Note: Dashed line indicates month trade restrictions were first reported.
Source: DFAT

Secondly, Australian exports, particularly to China, are often [used](#) to produce goods exported to third markets. Chinese producers that used Australian inputs in their production might have to pay more or use lower quality inputs. For example, paying more for barley in brewing beer, using copper for

electronics, or using lower quality coal for electricity generation. This could hurt China's productivity, economic growth and competitiveness against other countries using Australian inputs.

Finally, this can damage China's reputation. Trade is usually beneficial to both countries' trading, but if China is seen to weaponize its trading relationships, other countries and businesses might see China as a less reliable trade partner and find partners elsewhere, ultimately hurting China's economy.

China could hurt the Australian economy by banning imports of Australian iron ore. But this would also have significant consequences for China. It would sharply increase the price of iron ore from other countries, while forcing Australian iron ore to be diverted to other markets at a much lower price, making other countries' steel production more competitive against China. As with the current trade sanctions, the banning of Australian iron ore would result in a lose-lose scenario for both countries, but at a much larger scale than the current sanctions.

Recommendations

China should use economic sanctions sparingly. Often the threat of sanctions is more powerful than the sanctions themselves. The threatening power of China's economic sanctions is reduced, when countries like Australia are subjected to them, but remain somewhat resilient to their effects.

Meanwhile, the Australian Government and its policymakers should:

- Avoid retaliatory economic sanctions and use the proper resolution forums through the World Trade Organisation.
- Encourage its large diplomatic network around the world to not just engage in diplomacy, but also actively engage with Australian businesses to find new markets.
- Increase the number of AusTrade officials in key alternate markets, such as in the subcontinent, ASEAN, the Middle-East, and Latin and South America.
- Provide targeted financial support and export diversification advice to Australian businesses hit by China's sanctions.
- Avoid megaphone diplomacy and overreactions.

Data Appendix

1. All data are in nominal Australian dollars.
2. Code to reproduce charts can be found at my [GitHub](#).
3. All data in charts and tables are sourced from the Australian Department of Foreign Affairs and Trade.
 - a. DFAT publication 'Composition of Trade Australia'. Accessed 16 March 2022. Available at: <https://www.dfat.gov.au/about-us/publications/trade-statistical-pivot-tables>
4. Data goes down to 3-digit Standard International Trade Classification (SITC). For example, the SITC used for wine is 112 – Alcoholic beverages.

Table 2 – SITC matched up to export analysed

SITC	Product
011 Beef, f.c.f.	Beef
034 Fish, f.c.f.	Live fish
036 Crustaceans, f.c.f.	Lobster
043 Barley	Barley
057 Fruit & nuts	Table grapes
061 Sugars, molasses & honey	Sugar products
081 Animal feed	Hay
112 Alcoholic beverages	Wine
247 Wood, rough	Timber
263 Cotton	Cotton
283 Copper ores & concentrates	Copper ores and concentrates
321 Coal	Coal