

USDA Foreign Agricultural Service

# GAIN Report

Global Agricultural Information Network

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## China - Peoples Republic of

**Post:** Beijing

### China Food Price Inflation in 2010

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Agricultural Situation

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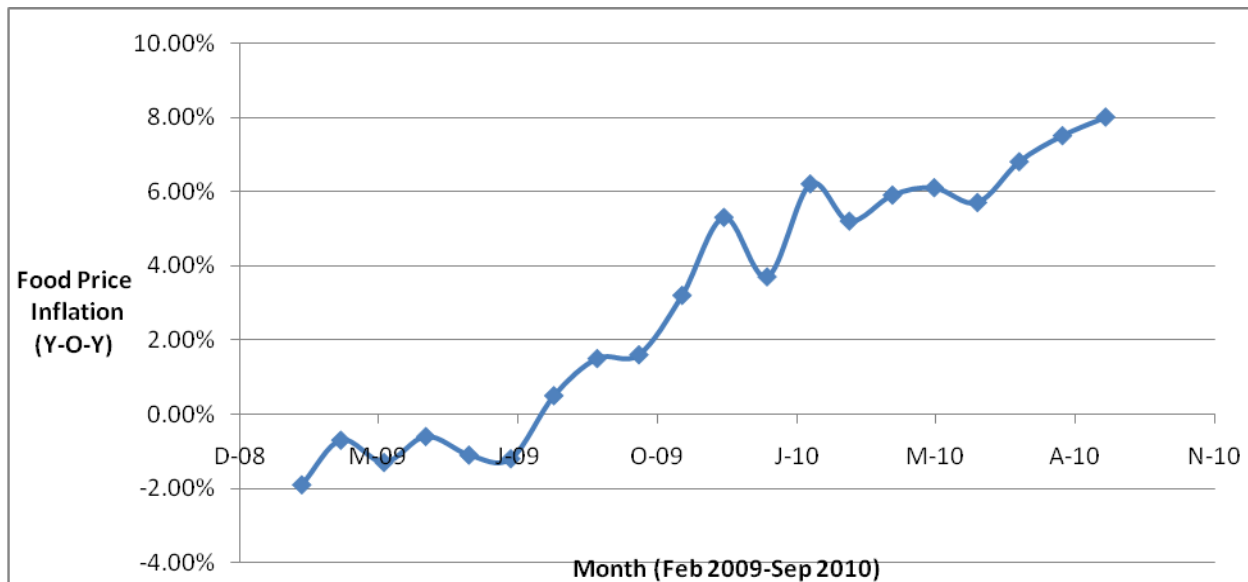
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**Report Highlights:**

China may become more reliant on the global food market as rising domestic food prices continue to push inflation beyond the yearly target and place heavy burdens on low-income and rural residents. If prices continue to escalate, the U.S. may see greater opportunities to export key commodities to China.

## Multiple Factors in China Have Caused Escalation in Domestic Food Prices



Data Source: National Bureau of Statistics (NBS)

The Government of China (GOC) is particularly concerned with rising food prices, which have pushed inflation beyond the yearly target and placed heavy burdens on low-income and rural residents. To ease rising prices, the GOC is taking immediate action by releasing central reserves in the market and aiding specific areas, while also introducing long-term policies to increase production. As domestic food prices escalate, China may become more reliant on the global food market and the U.S. will see greater opportunities to export key commodities to China.

Food prices have steadily risen in the past 20 months, with food price inflation reaching 8 percent y-o-y in September. In the same month, the GOC's targeted Consumer Price Index (CPI) rose to a 23-month high of 3.6 percent, which exceeds the yearly target of 3.0 percent and is largely due to food prices accounting for about one-third of the CPI. The combination of multiple factors that contribute to rising domestic food prices include severe weather, increasing labor wages, and rising demand for certain commodities.

This year, severe droughts and floods hindered crop production. For example, in the spring season, droughts in Southwest China caused a short water supply for millions of livestock and farming areas. In early summer months, heavy flooding affected 28 provinces by damaging about 9 million hectares of farmland.

Experts claim that the food shortages resulting from extreme weather will only have a temporary effect on overall inflation. It was also mentioned that it is normal for many food products to experience seasonal inflation, and that the government stockpiles massive reserves to properly respond to food shortages. The GOC advised local authorities to intervene in the market by decelerating rising food prices. In fact, central pork reserves were released in major cities to ease rising prices prior to the

Chinese holidays in October. The GOC is also enacting numerous policies to ensure a good autumn harvest, which accounts for 70 percent of grain production. These policies consist of increasing the use of technology for weather forecasting, sending experts to aid in grain production, assisting specific areas in recovering from flooding, and allocating 1.1 billion RMB to subsidize purchases of fertilizer and pest control.

Additional contributions to rising food prices include increased labor cost and rising demand for meat, dairy, and grain products. For instance, corn is in high demand for feed, bio-fuel production and industrial use. Domestic consumption for corn increased by 3.0 MMT in 2009 from 2008. With lower-than-expected grain production in 2010, China did not offer a VAT rebate in MY 2009/10 for many grain exports. In June, the U.S. exported its largest corn shipment of 55,000 MT to China in 15 years. It is unclear whether the increased imports will be temporary or permanent; estimates of Chinese corn imports for MY 2011 range from 2.0 to 10 MMT.

Due to China's food price inflation, imports of other commodities may rise as well. For instance, China recently lifted a ban on Argentine soy oil imports partly due to sharp price increases domestically for soybean oil. In 2008, U.S. exports of pork to China surged due to China's severe drop in supply and high demand. This indicates that there is great potential for U.S. exports of grains, meat, and other key commodities to China as domestic prices continue to rise. However, if China's domestic demand surpasses its supplies, China may be forced to become more dependent on the unpredictable international food market, which could later contribute to unstable prices.

The government is continuing to introduce policies to remain self-sufficient and to keep food prices under control in the long run. In December 2009, the Ministry of Agriculture approved the use of some genetically modified strains of corn and rice, which can significantly increase the crop yield. In addition, China has a plan to increase grain production (see 2010 GAIN report "*National Plan for Expansion of Grain Production Capacity*") which includes improving irrigation and farming techniques. Another method to ease supply constraints is using wheat-based feed instead of corn-based feed.

Surprisingly, small products, such as mung beans and garlic, have also experienced price hikes this year due to hoarding. Until the government imposed market regulations, grain hoarding raised food prices and limited the government's ability to buy grains for reserve. The National Development and Reform Commission (NDRC) is planning to implement market regulations and fines to impede non-competitive behavior.

Many Chinese economists predict that high food prices will only be temporary. The GOC's short-term measures are expected to be effective at reducing food price inflation this year. However, the macro environment suggests there are factors that may contribute to further price increases. The future of domestic food prices will be dependent on the success of the long-term policies imposed by the Government of China.